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ABBREVIATIONS

ADB  Asian Development Bank
BoM  Bank of Mongolia
CMP  Child Money Program
CPI  consumer price index
EAP  East Asia and Pacific
EMDEs  emerging market and developing economies
FDI  foreign direct investment
FX  foreign exchange
GDP  gross domestic product
GIR  gross international reserves
HRPS  Household Response Phone Survey
HSES  Household Socio-Economic Survey
H1  first half of the year
H2  second half of the year
IMF  International Monetary Fund
LFS  Labor Force Survey
LLP  loan loss provisions
MoF  Ministry of Finance
MPC  Monetary Policy Committee
NPLs  nonperforming loans
NSO  National Statistics Office
OxCGRT  Oxford COVID-19 Government Response Tracker
Q1  first quarter of the year
Q2  second quarter of the year
Q3  third quarter of the year
Q4  fourth quarter of the year
SEC  State Emergency Commission
SMEs  small and medium-sized enterprises
y/y  year-over-year
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This edition of the Mongolia Economic Update (MEU) was prepared by Jean Pascal Nganou (Senior Economist), Davaadalai Batsuuri (Economist), Undral Batmunkh (Research Analyst), Maheshwor Shrestha (Economist), and Ikuko Uochi (Economist). Sebastian Eckardt (Lead Economist), Ibrahim Saeed Chowdhury (Senior Economist), and Eka T. Vashakmadze (Senior Economist) provided constructive comments. The MEU was prepared under the direction of Martin Raiser (Country Director), Hassan Zaman (Regional Director), Deepak Mishra (Practice Manager), and Andrei Mikhnev (Country Manager). The team is grateful to Sukhchimeg Tumur (Program Assistant) and Indra Baatarkhuu (External Affairs Officer) for their support on administrative and communication affairs.

Each edition of the MEU consists of two parts. Part I discusses recent economic developments and presents the medium-term economic outlook, and Part II focuses on a specific theme. The theme for this edition is the socioeconomic impacts of COVID-19 on households, based on the recent Household Phone Survey. The MEU is intended for a wide audience, including policymakers, business leaders, financial market participants, and the community of analysts and professionals engaged in Mongolia.

The findings, interpretations, and conclusions expressed in this update are those of the World Bank staff and do not necessarily reflect the views of the Executive Board of the World Bank or the governments they represent. For information about the World Bank and its activities in Mongolia, please visit https://www.worldbank.org/en/country/mongolia. For questions and comments on the content of this publication, please contact Jean Pascal Nganou (jnganou@worldbank.org). The cutoff date for this edition of the MEU is December 31, 2020.
Recent Economic Developments

Strict implementation of social distancing, mobility restrictions, and quarantine measures have helped Mongolia contain the worst health effects of the COVID-19 pandemic, though the country remains in the midst of a significant outbreak. While the swiftness of these measures was key to containing the pandemic, their strictness is taking a significant toll on the economy. Particularly, the unavoidable strict lockdown measures from mid-November 2020 in response to the domestic transmission of the pandemic have reduced mobility and stalled economic activity. However, by bringing the pandemic under control, these measures are not only saving precious lives but are also expected to facilitate a swifter and robust recovery.

The economic impact of the COVID-19 pandemic has been severe and widespread. In the first nine months of 2020, the Mongolian economy contracted by 7.3 percent, one of the worst contractions since the 1990s. The mining sector was affected significantly by a sharp decline in demand for key commodities and border closures with China. The services sector was also hit hard due to mobility restrictions and falling incomes. In fact, firm-level surveys indicate that the impact of the COVID-19 shock was most severe for small and young firms, and for enterprises in the manufacturing, tourism, trade, transportation, construction, and education sectors. However, generous economic support provided by the government has so far prevented a wave of business closures.

The COVID-19 shock also affected the structure and conditions of the labor market. While some sectors including hospitality and entertainment experienced declining employment, employment increased in some sectors such as information technology, as demand for online services increased. Overall, the labor force participation rate shrank by 1.1 percent in September 2020 from a year ago and the unemployment rate slightly edged up in Q3 2020, reflecting weakening labor market conditions. However, sizable policy support partially mitigated the impact of COVID-19 and encouraged firms to limit layoffs and opt for reduced working hours instead. At the same time, generous income support and the lack of adequate and affordable childcare service during the closure of schools partly contributed to declining labor force participation.

The pandemic-induced economic crisis has been severe. Households from various segments of the income distribution were affected by COVID-19-related shocks, with those employed in the low-skilled informal sectors, with limited economic buffers or job protection, and those living just above the national poverty line, at greater risk of falling below the poverty line. The latest Household Response Phone Surveys (HRPS) jointly conducted by the National Statistics Office of Mongolia and World Bank reveal that household labor income was affected by the pandemic shock, as many people stopped working due to business closures or faced a reduction in working hours, particularly under the second nationwide lockdown in mid-November. The government’s generous direct transfers to households helped partially mitigate the negative income shock. A poverty micro-simulation analysis, using the Household Socio-Economic Survey from 2018 and latest GDP growth forecasts, indicates that without mitigating measures, approximately 195,000 to 260,000 more
people could have been pushed into poverty as a result of the pandemic, bringing the poverty rate up to 33.6 percent in 2020 from 28.4 percent in 2018. In fact, the analysis shows that the quintupling of benefits under the Child Money Program during May 2020–July 2021, on its own would be enough to bring poverty incidence below the pre-COVID level (see Part II for details).

The external position improved substantially faster than initially expected, mainly supported by the notable current account adjustment. After a sharp deterioration in the early months of 2020, pressures notably eased in the second half of the year, and the current account even recorded a surplus amid a quick recovery of exports and persistent imports compression (due to lower demand for capital and intermediate goods and declining service fees). Meanwhile, despite a fall in foreign direct investment and sizable private sector external repayments, the balance of payments improved, with the authorities taking advantage of improved financing conditions to refinance external debt. The Mongolian tugrug depreciated moderately and the level of foreign exchange reserves reached a historical high of US$4.5 billion, supported also by higher gold purchases by the authorities.

The cost of fiscal relief measures is estimated to be over 9 percent of GDP. Fiscal imbalances had started to emerge in early 2020 prior to the introduction of COVID-19-related measures, with the government’s decision to increase wages and pensions and to write off pension loans. Fiscal imbalances widened significantly further between April and December 2020, as the effects of the pandemic intensified. The budget deficit reached 9.5 percent of GDP in 2020, its highest level since 2016, amid a large revenue shortfall and sizable fiscal relief (spending) measures. Overall, the authorities’ fiscal response has provided adequate support to firms and households, but the size of the deficit has raised questions over its sustainability.

Monetary policy was loosened to fight the economic impact of the pandemic through policy rate cuts, increased banking sector liquidity, and the introduction of regulatory forbearance. Moreover, the monetary authorities engaged in quasi-fiscal activities, thus violating the Law on Central Bank, which prohibits the Bank of Mongolia from engaging in these activities. The looser policy stance followed a period of tightening starting in late 2018, which helped slow credit growth and stabilize inflation, giving the central bank some room to relax when the pandemic hit. Nonetheless, monetary policy space continues to be limited by the country’s relatively weak external position.

With respect to the financial sector, despite the relaxation of macroprudential regulations and buffers, banks remain cautious in issuing loans. In 2020, domestic credit contracted by about 5 percent (year-over-year) compared to growth of 5.1 percent in 2019. While a sizable portion of this contraction is explained by the authorities’ decision to write off the pension loans in January 2020, issuance of new loans remained subdued due to heightened perceptions of risk, deteriorating asset quality, and significant currency mismatches (including deposit dollarization). Moreover, regulatory forbearance may be hiding more serious problems in the financial sector and thus complicates a full assessment of financial sector stability.

Outlook and Risks

Recovery in the post-pandemic period is likely to be slow and erratic. Following an estimated contraction of 5.2 percent in 2020, the Mongolian economy is expected to grow by 4.3 percent in 2021, as the authorities take control of the pandemic, stimulus measures prop up domestic demand, the adverse impact of the global economy recedes, businesses and consumers adjust to the new norm of living with the pandemic, and a vaccine is introduced. However, the recovery is subject to risks of (i) a sharp rise in domestic COVID-19 cases that could trigger stricter and prolonged lockdowns; (ii) the potential for further global waves of the virus that would worsen the domestic and external environment; (iii) possible financial instability as regulatory forbearance is withdrawn and the underlying fragile condition of bank balance sheets is revealed; (iv) weather-related shocks (for example, a harsh winter, which could hit the agriculture sector); and (v) the likelihood of new spending and overstretched public finances in the run-up to the presidential election.

1 It includes the extension of some measures which are expected to be implemented until July 2021. But it does not include the government’s recent decision on exempting utilities fees for households and enterprises.
Mongolia, like other countries, will need to transition from policies focused on short-term economic relief to accelerating recovery and building resilience. The challenge Mongolia faces in this regard is that the fiscal space to continue the generous support policies enacted during 2020 is quite limited, while their rapid withdrawal as long as the economy remains weakened by public-health-related mobility restrictions could create significant difficulties for households and firms. The government’s fiscal consolidation plan takes this into account by committing to medium-term adjustment but keeping current support measures in place until the summer of 2021. This plan will need to be implemented, as further fiscal expansion beyond what has been agreed in the 2021 budget could erode confidence, lead to currency pressures and capital outflows, and require harsher austerity measures to reestablish macroeconomic control. Mongolia has so far managed to avoid a repeat of the traditional macro boom-and-bust cycles. It should cherish this achievement. Further exchange rate flexibility could help cushion additional external shocks and thereby preserve the limited domestic policy room.

Another priority is to prevent the COVID-19 shock from undermining financial stability. While a swift policy response was welcome and necessary, the extension of regulatory forbearance would further reduce transparency around the underlying quality of banking sector balance sheets, while delaying the necessary adjustments in the real sector. The COVID-19 shock has left scars among companies and some may not be able to survive. They should be allowed to close and their resources reallocated to other, more profitable ventures. Banks play a key role in facilitating this reallocation of resources, but excessive forbearance may lock funds in poor investment decisions made in the past, increasing the long-run costs of the shock to the economy. Relatedly, Mongolia’s efforts to implement structural reforms in the banking sector should gain traction. Key elements of these reforms include the strengthening of capital buffers and improved corporate governance of banks (including ongoing reforms in ownership structure of banks), both of which would be facilitated by the gradual exit from COVID-19 related regulatory forbearance.

Finally, Mongolia should adopt an integrated and fiscally sustainable approach to boosting medium-term economic prospects and job creation. Such an integrated approach would place the highest emphasis on leveraging private sector investment in the mining and non-mining sectors to create higher-productivity jobs and sustainable income opportunities for Mongolians. These efforts would be complemented by better-prioritized and targeted government investments in infrastructure and a more efficient and fiscally affordable social safety net. They would also require continued attention to the generation of skills required for successful employment, and addressing the possible losses of human capital, particularly among the poor, as a result of repeated school closures. While over the coming year government policy will need to remain attentive to national and global developments in the management of the pandemic and react flexibly to any downside risks, the rollout of vaccines raises the prospect that policy efforts can gradually return to this critical medium-term agenda.
Strict containment measures have helped Mongolia check the spread in most of 2020

However, relative to some of its regional peers, the number of confirmed infections has surged since November 2020

Exports were significantly affected in H1, but have recovered quickly...

...while the hard-hit nontradeable services sector has been slow to recover

Government provided sizable fiscal relief package...

...which supported household consumption

Sources: NSO; World Bank staff estimates.

Sources: NSO; World Bank staff estimates.
With subdued inflation, the monetary policy rate reached a historic low

However, banks with excess liquidity have been reluctant to lend...

Sources: BoM; World Bank staff estimates.
Note: RHS = right-hand side; LHS = left-hand side.

...mainly explained by a deterioration in the loan quality and rising NPLs

Sources: BoM; World Bank staff estimates.
Note: RHS = right-hand side; LHS = left-hand side.

Current account surplus in recent months has contributed to reserves accumulation...

Sources: BoM; World Bank staff estimates.
Note: FX = foreign exchange; RHS = right-hand side; LHS = left-hand side.
### Key Macroeconomic Indicators

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<th>2016</th>
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<th>2020e</th>
<th>2021f</th>
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<td><strong>Real GDP growth, at constant market prices</strong></td>
<td>1.4</td>
<td>5.4</td>
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<td>4.3</td>
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<td>Government Consumption</td>
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<td>11.5</td>
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<td>Gross Fixed Capital Formation</td>
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<td>9.1</td>
<td>-5.0</td>
<td>13.4</td>
<td>7.4</td>
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<td>24.8</td>
<td>30.9</td>
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<td>-9.0</td>
<td>14.1</td>
<td>8.4</td>
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<tr>
<td><strong>Real GDP growth, at constant factor prices</strong></td>
<td>1.2</td>
<td>5.3</td>
<td>7.2</td>
<td>5.2</td>
<td>-5.2</td>
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<td>6.0</td>
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<td>Industry (incl mining)</td>
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<td>7.9</td>
<td>3.1</td>
<td>-11.0</td>
<td>6.3</td>
<td>5.4</td>
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<td>Services</td>
<td>1.1</td>
<td>7.7</td>
<td>4.7</td>
<td>5.8</td>
<td>-5.7</td>
<td>2.5</td>
<td>5.2</td>
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<td>Inflation (CPI, end-period)</td>
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<td>6.4</td>
<td>8.1</td>
<td>5.2</td>
<td>2.3</td>
<td>5.0</td>
<td>7.0</td>
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<td>Current account balance (% of GDP)</td>
<td>-6.3</td>
<td>-10.2</td>
<td>-16.8</td>
<td>-15.4</td>
<td>-3.3</td>
<td>-7.7</td>
<td>-8.3</td>
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<td>Financial and Capital account (% of GDP)</td>
<td>7.6</td>
<td>24.5</td>
<td>17.4</td>
<td>21.1</td>
<td>9.2</td>
<td>11.8</td>
<td>13.2</td>
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<td>Net Foreign Direct Investment (% of GDP)*</td>
<td>1.1</td>
<td>12.7</td>
<td>16.3</td>
<td>16.5</td>
<td>12.5</td>
<td>14.0</td>
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<td>Fiscal Balance (% of GDP)**</td>
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<td>2.6</td>
<td>1.4</td>
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<td>Primary Balance (% of GDP)</td>
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<td>5.8</td>
<td>3.7</td>
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<td>-0.3</td>
<td>0.1</td>
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<td>Debt (% of GDP)**</td>
<td>87.6</td>
<td>84.7</td>
<td>72.6</td>
<td>69.0</td>
<td>79.4</td>
<td>77.7</td>
<td>73.0</td>
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*In 2016, net FDI number excluded the transactions of Oyu Tolgoi-2 project financing in May–June 2016.

**Development Bank of Mongolia (DBM) spending is excluded from fiscal balance and monitored separately.

***General government debt data exclude SOE debt and central bank liability from People’s Bank of China swap line.
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I. ECONOMIC PERFORMANCE AND PROSPECTS

A1. Output contracted sharply during the first nine months of 2020

The COVID-19 crisis has triggered a global economic shock of unprecedented magnitude, causing synchronized collapses in economic activity across the world. In particular, economic conditions in the East Asia and Pacific (EAP) region deteriorated sharply due to the pandemic-related lockdowns. Although the Chinese economy is recovering at a brisk pace, recovery in the rest of the region is expected to be subdued and fragile as disruptions to economic activity were more acute than expected. The pandemic has caused a heavy toll of deaths and illness, plunged millions into poverty, and may depress economic activity and incomes for a prolonged period. Furthermore, the pandemic has exacerbated the risks associated with debt accumulation as debt levels have reached historic highs and financial market stress builds.

The COVID-19 health crisis quickly escalated into deep economic turmoil in Mongolia, affecting businesses, households, and government revenue. This manifested itself through four key channels: (i) the government’s containment measures have had a direct and immediate adverse impact on small businesses and household income, weighing on already weakening domestic economic activity (see box I.1); (ii) the mining sector has been hard hit by weaker Chinese demand, compounded by self-imposed border closures, a drop in commodity prices, and greater risk aversion of investors; (iii) the services sector (including tourism and transportation), which accounts for about 40 percent of the Mongolian economy, was affected by the containment measures; and (iv) unforeseen revenue shortfalls and increased spending on health care and social protection further exacerbated fiscal pressures.
Box I.1. The government’s measures to contain the COVID-19 pandemic

The Government of Mongolia, through the State Emergency Commission (SEC), which is tasked with handling emergencies at the national level, introduced throughout 2020 a series of restrictions to contain the risk of COVID-19. These include:

- **Border closures**: All travel (air, road, and railway) from or through China was banned since February 1, 2020. Cross-border passenger transportation of all forms ceased starting March 10. Mongolia’s borders have remained closed for passengers, with the exception of Mongolian nationals arriving through special chartered flights organized by the government. Upon arrival, passengers are subject to a 21-day mandatory strict quarantine to limit the risks of domestic contagion. Hygiene protocols were elevated on the trucks transporting consumer items imported from Russia.

- **Suspension of exports**: Exports of coal and crude oil were suspended during February 10–March 2, in an attempt to minimize the risk of infection of truck drivers over the Mongolia-China border. Although the official suspension was lifted as scheduled, export did not return to its regular pace until August, when the government introduced the Green Gate program, which aimed to accelerate truck transportation through improved customs clearance and proper implementation of hygiene protocols.

- **Suspension of educational activities**: All activities of schools, kindergartens, universities, vocational centers, production centers, and training centers were suspended from January 27 to September 1. Online/TV schooling was provided for students until September 21, when in-class education resumed.

- **Restriction of services and community activities**: Bars, cafés, and restaurants were instructed during mid-February to July 2020 to close at 10:00 p.m. rather than the usual 4:00 a.m. In early May, nightclubs and karaoke bars were banned from operating, and in early March, the government suspended community activities including meetings, trainings, sport competitions, travel, arts, cultural activities, cinema, driving courses, and game center activities. These restrictions have been gradually loosened since then.

- **Introduction of a strict lockdown when the first domestic contagion was recorded on November 11, 2020**: Ulaanbaatar and several other regions remained in strict lockdown between November 11 and December 14. During this period, the sale of alcohol was prohibited, pedestrian and automobile movement in the city was restricted to grocery, health care, and other essential services only, public transportation service was limited, travel between regions was prohibited, and charter flights were suspended. During the lockdown, the authorities traced the domestic infections and conducted PCR (polymerase chain reaction) tests of a sample of households. On December 14, when the strict lockdown ended, a number of economic activities that could enforce social distancing were allowed to reopen. Passenger travel between towns remains conditional on PCR testing. In-class educational activities have been suspended since November 11, and TV schooling resumed.

- **After a temporary loosening, a strict lockdown was reintroduced in the city of Ulaanbaatar starting December 14**: An accelerating number of COVID-19 cases in the city triggered the authorities to introduce a strict lockdown until January 11, 2021. Unlike in the preceding lockdown, delivery services were restricted within the city. Due to consequences on economic activities, starting January 11, the strict lockdown has been loosened step by step.

Source: Compiled from various government websites.
Mongolia’s economy is facing one of its most severe contractions triggered by the outbreak and associated precautionary measures. The COVID-19 shock came at a time when Mongolia’s economy was already facing a slowdown - particularly in the second half (H2) of 2019 - mostly driven by weaker commodity prices and the deteriorating quality of locally produced copper, a key mineral export. Hit by the COVID-19 shock through both domestic and external channels, Mongolia’s real GDP contracted by 7.3 percent (year-over-year [y/y]) in the first nine months of 2020 (figure I.1), its worst contraction since the economic transition period in early 1990s. Although the contraction was broad-based, it was significantly felt in the mining sector (-20.7 percent, y/y). Output in non-mining industry fell by 3.7 percent (y/y), while services contracted by 7 percent in the same period. Meanwhile, the agriculture sector was the key driver of growth, as it expanded by 11.3 percent (y/y), supported by favorable weather conditions. The adverse impact of a weaker global economy was exacerbated by a sharp fall in domestic economic activities due to the authorities’ containment measures, including the exports ban.

On the demand side, although final consumption growth moderated during January–September 2020, it remained a key driver of growth (figure I.2). Final consumption grew by 7.1 percent (y/y) in the first three quarters of 2020 from 9.9 percent in the same period in 2019. Household consumption growth slowed to 6.1 percent (y/y) during this period from 9.5 percent one year ago, as COVID-19-related restriction measures affected private spending on retail trade, travel, leisure, and recreational activities. The Household Response Phone Survey indicates that the pandemic has led to significant deceleration in labor income, particularly among the self-employed and household business owners (see part II for details). However, household consumption and income were supported by, among others, the wage/pension increase, the write off of pension loans, and COVID-19-related income support measures. Meanwhile, government consumption expanded by 11.7 percent, mainly reflecting COVID-19-related spending.

Investment, especially in the private sector, plummeted, pulling down growth on the demand side. The contribution of gross capital formation to GDP growth turned significantly negative (-14.3 percentage points) during January–September 2020, from +10 percentage points a year ago. This is mainly explained by a combination of factors including declining commodity prices, weakening domestic demand, and deteriorating investor confidence. In fact, foreign direct investment (FDI) flows, which account for about 70 percent of the gross capital formation, fell by over 20 percent (y/y)

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**Figure I.1.** Output contraction was mostly driven by the mining and services sectors

Supply contribution to GDP growth, percentage points

- Mining
- Services
- Non-mining industry
- GDP growth
- Agriculture

**Figure I.2.** Steady growth of private consumption was not enough to compensate sharp drop in investment

Demand contribution to GDP growth, percentage points

- Household consumption
- Public consumption
- Gross capital formation
- Net exports

**Sources:** NSO; World Bank staff estimates.
to US$1.2 billion during January–September. Moreover, total outstanding loans in the banking sector, a key source of financing of domestic investment, contracted by over 5 percent (y/y) amid the ongoing deterioration of loan quality. Meanwhile, the accelerated execution of public investment projects was not sufficient to offset the slump in private investment.

Exports were hit hard in the first half but recovered quickly (figure I.3). In the first nine months of 2020, exports of goods and services contracted by 8 percent in real terms, the largest decline since the 2009 global financial crisis. In fact, in the same period of 2019, real exports expanded by 15.1 percent. The contraction was most significant in coal and crude oil (which accounted for 45 percent of the total export in 2019) following the COVID-19 shock suppressing global demand. However, exports recovered quickly, particularly in the third quarter (Q3), mainly driven by increasing commodity prices, the gradual easing of COVID-19 preventive measures, and the government’s initiative to boost exports through the Green Gate program. In addition, in Q3 2020, gold exports reached their highest peak since 2008, as the central bank provided soft loans to gold miners (0.3 percent of GDP during January-October).

Imports also contracted significantly amid weaker domestic demand and lower oil prices. As a net importer of energy, Mongolia benefited from declining global oil prices. Real imports of goods and services fell by 8 percent (y/y) during January-September 2020 compared to an expansion of 23.2 percent a year ago (figure I.4). The import compression is supported by, among others, subdued purchase of capital goods (mostly reflecting lower private investment), lower oil prices, and reduction in imported consumer goods triggered by COVID-19-related precautionary measures (for example, cancellation of the official celebration of the 2020 lunar new year and reduced economic activity in retail trade and other services). Meanwhile, imports of services also declined sharply, partly due to weaker demand for transportation services (mainly triggered by travel restrictions and limited truck activities), and reduction in overseas tourism and international consultancy services (particularly in the mining sector).

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2 The Green Gate initiative introduced by the government has helped the gradual recovery of coal and copper exports.
Mining sector output contracted sharply, especially in H1 2020, but recovered quickly. In H1 2020, production of coal contracted by 49 percent (y/y), while its volume of exports contracted by 52.1 percent (y/y). Weak demand from China and the COVID-19-related precautionary measures of the authorities largely explain the weak performance. Meanwhile, crude oil production was down by about 70 percent (y/y) during the same period. Copper production contracted by 8 percent in H1 2020, reflecting the declining quality of copper from the Oyu Tolgoi mines and lower international prices. However, the output contraction of the mining sector decelerated to 5.2 percent (y/y) in Q3 (figure I.5). This was mainly driven by strong gold production following higher prices, and the Bank of Mongolia (BoM)’s program to support gold production and exports. Moreover, coal production also recovered in the same period supported by the government’s efforts to boost coal exports, including through the Green Gate initiative with China.

Non-mining output also contracted notably, as the services sector was significantly hit by COVID-19-related precautionary measures. After recording growth of 6.7 percent (y/y) in 2019, non-mining GDP contracted by 3.7 percent (y/y) in the first nine months of 2020 (figure I.6). The services sector, mainly trade and transportation, declined significantly (by 13 to 25 percent), reflecting its strong link with the mining sector. Mainly explained by reduced production of textiles, manufacturing output contracted by 6.6 percent (y/y) in the same period from 9.2 percent growth a year ago. Despite the accelerated execution of public investment projects and the resumption of a subsidized housing program by the BoM since April 2019, the construction sector also contracted by 6.3 percent (y/y) in the same period from expansion (8 percent) in 2019, with a fall in both residential and industrial building activity (the latter mainly due to the slowdown in the development of the Oyu Tolgoi mine’s underground project). In contrast, expansion in the

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1 Coal exports accounted for 45 percent of total mineral exports in 2019.
2 As a part of the precautionary measures, the export ban during February–March contributed to a sharp fall in mineral output.
3 In 2019, coal production and export grew by 1.9 percent and 2 percent, respectively, to reach historically high levels (that is, 50.8 million tons and 36.5 million tons, respectively).
4 The copper export unit price fell by about 14.3 percent during the H1 2020 following the collapse in global prices amid the impact of the COVID-19 shock on the commodity market.
5 Gold production grew by 35 percent (y/y) in the first nine months of 2020.
6 The Bank of Mongolia has also provided soft loans to gold mining companies, which may have also contributed to boosting gold production.
7 The contraction in the textile industry, which represents nearly 14 percent of manufacturing production, is mainly attributed to weakened business activity, especially in the cashmere industry.
agriculture sector accelerated to 11.3 percent during January–September 2020, up from 8.4 percent in 2019, reflecting relatively favorable weather conditions and higher survival rates of livestock. Finally, net taxes contracted by 8.4 percent (y/y) amid subdued domestic demand and import compression (mainly a sharp fall in imports of passenger cars and mining-sector-related capital goods).

A2. Inflation moderated notably, reflecting subdued domestic demand and lower oil prices

Weakening domestic demand largely contributed to moderate inflation in 2020. Inflation moderated to 2.3 percent in December 2020, down from 5.2 percent in 2019 on the back of muted domestic demand pressures following plummeting private investment and decelerating private consumption growth (figure I.7). Supply side factors, such as lower global oil prices, have also contributed to low inflation as Mongolia is a net oil importer. Moreover, the government decision to reduce the price of coal briquettes also significantly contributed to moderate inflation through end-2020. However, food price inflation remained high at 8.5 percent at end-2020 (8.3 percent at end-2019) amid the lockdowns and panic buying.

With subdued inflation, the monetary policy rate was reduced to a historic low to mitigate the economic impact of the COVID-19 shock. Reflecting weaker domestic demand, core inflation moderated to 0.2 percent at end-2020 from 4.2 percent (y/y) at end-2019 (figure I.8). Moreover, domestic credit contracted in March as banks’ risk aversion toward new loans increased amid heightened market uncertainty triggered by the COVID-19 shock. This also contributed to the falling core inflation trend. The authorities consequently cut the policy rate by a total of 500 basis points in 2020 to 6 percent, a historic low.

Sources: NSO Bulletin; World Bank staff estimates.

Note: Domestic demand is defined as the sum of final consumption and investment from national accounts data. RHS = right-hand side; LHS = left-hand side.
A3. The COVID-19 shock affected the structure and conditions of the labor market

The COVID-19 pandemic has led to job losses in several sectors and labor force participation rate (LFPR) marked the lowest level in a decade. According to official NSO data, at end-September 2020, total employment increased by 20,400 (1.7 percent, y/y) relative to a year ago. While sizable COVID-19-related relief measures to firms overall might have contributed to this outcome, the difference in level of skills required for different sectors may explain the ups and downs in employment across sectors. In fact, the mining, construction, manufacturing, agriculture, and entertainment sectors all posted a year-on-year decline in their employment as of September 2020 (figure I.9) amid the lockdowns and precautionary measures by the authorities. Moreover, this could also be explained by the fact that the industrial sectors require relatively lower skilled labor compared to sectors such as information technology (IT), finance, education, and health, and therefore workers in these fields had lower job security and limited opportunity to work from home. In contrast, during the pandemic, the health sector saw a substantial rise in employment. Furthermore, employment in the trade and IT sectors increased during this period, partly explained by the digital transformation of economic activities, including trade. In the meantime, the labor force (employment + unemployment) decreased by 1 percent in the same period, and the number of those out of the labor force increased by 4 percent. This indicates that finding a job has become more difficult and that some of the unemployed moved out of the labor force.

Unemployment rates moderately increased in Q3 2020. Despite the sharp output contraction, unemployment rates were relatively stable in H1 2020, partly supported by the sizable income support measures.

Figure I.9. The COVID-19 pandemic has put some jobs at risk...

![Change in employment (Q3 2020–Q3 2019, y/y percent change)](image)

Sources: NSO Bulletin; World Bank staff estimates.

Figure I.10. ...thereby reversing declining trends of the unemployment rate

![Unemployment rate by gender](image)

Sources: NSO Bulletin; World Bank staff estimates.

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10 Measures include exemptions on tax, social security contributions, and use of the unemployment insurance fund to support firms that did not lay off workers.

11 However, according to the latest Household Response Phone Survey by NSO and World Bank, the strict lockdown since mid-November 2020 may have caused significant disruptions of employment in the private sectors (see Part II for details).

12 Measures include exemptions on tax, social security contributions, and use of the unemployment insurance fund to support firms that did not lay off workers.
However, unemployment moderately increased to 7.3 percent in Q3, up from 6.6 in H1 (figure I.10). The rise in unemployment was faster for men than for women, as more women dropped out of the labor force, thus reducing the number of women actively seeking jobs.

Generous income support is likely to have contributed to the moderate impact of the pandemic on labor market conditions (see Part II for details). A moderate rise in unemployment and shrinking labor force participation during times of severe economic crisis often reflect the fact that people believe it would be harder to find employment and they stop looking for jobs. With COVID-19 spreading so easily, people may have stopped looking for a job to reduce the risk of contracting the virus. Closing kindergartens and schools may have also discouraged unemployed parents from looking for a job due to increased household and childcare responsibilities. This is more relevant to women, who traditionally bear the responsibility of caregiver. Also, the generous increase of social welfare benefits coupled with other relief measures increased the financial means of eligible households and hence may have reduced the need to look for employment (figure I.11). Still, family support remains the main source of income assistance for people currently out of work. In 2019, about 85 percent of the unemployed indicated that financial support from family members was their main source of income. This share declined in Q2 2020 to 80 percent, while about 14 percent of the unemployed reported that they mainly rely on cash transfers and social welfare benefits (figure I.12).

*Figure I.11. Relevance of cash transfers for people currently out of work in Q1-2020*

<table>
<thead>
<tr>
<th>Share of people reporting cash benefits/social welfare as main source of income support</th>
</tr>
</thead>
<tbody>
<tr>
<td>Q1-19</td>
</tr>
<tr>
<td>Unemployed</td>
</tr>
<tr>
<td>9%</td>
</tr>
</tbody>
</table>

Sources: NSO (LFS 2019, 2020); World Bank staff estimates.

*Figure I.12. For unemployed, main source of income support shifted in Q2 2020*

<table>
<thead>
<tr>
<th>Y/y change in main source of income support for unemployed people</th>
</tr>
</thead>
<tbody>
<tr>
<td>Q1</td>
</tr>
<tr>
<td>Family support</td>
</tr>
<tr>
<td>-6</td>
</tr>
<tr>
<td>-2</td>
</tr>
<tr>
<td>2</td>
</tr>
<tr>
<td>6</td>
</tr>
</tbody>
</table>

Sources: NSO (LFS 2019, 2020); World Bank staff estimates.

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13 There were 92,600 unemployed people in September, up from 83,700 people in H1 2020.
A4. The budget deficit widened sharply in 2020 but is expected to narrow in 2021

The decline in economic activity and forgone revenue linked to selected COVID-19 relief measures led to a large overall revenue shortfall in 2020. Total revenue declined by 13 percent (y/y) in 2020, reflecting weaker mineral revenue, subdued consumption, income losses, and tax relief measures (figure I.13).\(^\text{14}\) Tax revenue fell by 12.8 percent (y/y), while non-tax revenue contracted by 12.6 percent (y/y). Notably, the corporate income tax, social security contributions, and the value-added tax, which together accounted for 61 percent of overall tax revenue, contracted by 15.8 percent (y/y), 19.6 percent, and 11.2 percent, respectively, amid the COVID-19-related relief measures and the fall in mineral sector revenue. The personal income tax fell by 7.2 percent (y/y), reflecting tax relief and income losses amid the COVID-19-related precautionary measures and moderate labor market pressures. Excise and customs duties also declined. In fact, as the revenue shortfall had already reached 3.9 percent of projected 2020 GDP by July 2020, a series of revenue-enhancing measures (for example, collection of tax arrears, and tax prepayment from major state-owned enterprises) were sanctioned under the 2020 supplementary budget.

Meanwhile, measures to minimize the economic and social impact of the COVID-19 crisis drove a surge in spending. Total budget spending rose by 22.1 percent (y/y) in 2020 following 24 percent growth in 2019 (figure I.14). Social protection and welfare spending increased by 128.7 percent (y/y) in 2020 due to crisis response measures (mainly the sharp increase in benefits of the Child Money Program) (see box I.2). Health spending increased by 27 percent (y/y) in the same period. Meantime, capital spending execution was stronger than in the previous years (8.3 percent), reflecting the government’s efforts to support the economy by boosting domestic demand.\(^\text{15}\)

\(^{14}\) In fact, the revenue shortfall had already reached 3.9 percent of projected 2020 GDP by July 2020 when the authorities were considering the 2020 supplementary budget.

\(^{15}\) In fact, the increased social transfers and higher health spending were partly compensated by government capital expenditure cuts worth 0.6 percentage points of GDP in the 2020 supplementary budget.
The fiscal deficit increased significantly owing to revenue losses and spending needs to fight the pandemic. The budget deficit reached 9.5 percent of GDP in 2020, its highest level since 2016 (figures I.15 and I.16). The three years of fiscal consolidation that helped to rebuild sizable buffers also contributed to the government’s efforts to cope with the COVID-19 shock in the early months of 2020. In contrast to what was observed during the 2015-16 economic slowdown, the government had no pressing need to borrow from either domestic or international markets in the first five months of 2020. However, since June 2020, government requests for donor financing have intensified, including additional budget support totaling US$550 million from the International Monetary Fund (IMF), Asian Development Bank (ADB), Asian Infrastructure Investment Bank, and Japan, disbursed in H2 2020.

After a surging deficit in 2020, the 2021 budget plans to return to fiscal consolidation. The 2020 supplementary budget exhibited a widening of the overall fiscal deficit from an initial target of 2.4 percent of GDP to 9.9 percent of GDP. However, the 2021 budget plans to bring back the fiscal deficit within 2 percent of GDP (figure I.20). A projected rebound in revenues (3.4 percentage points of GDP) and substantial spending cuts (4.6 percentage points of GDP) are estimated to support the sharp improvement in the fiscal stance in 2021. The underlying assumptions of the 2021 budget include, among others, strong economic recovery (7.2 percent in 2021), modernization/renovation of customs and border points, digitalization of tax administration, improved governance of state-owned enterprises, and introduction of a new tax on livestock headcount (see box I.3). It also considers a reduction of total spending mainly reflecting the expiry of major COVID-19-related relief/stimulus measures (except the Child Money Program) and a moderate reduction of the capital budget relative to the 2020 supplementary budget. In addition, a substantial increase of accumulation in the fiscal stabilization and future heritage funds, similar to their levels in 2019, is also estimated under the 2021 budget. Finally, after an increase in 2020, the government expects that the debt-to-GDP ratio will resume its downward trajectory in 2021-22 based on these fiscal policy assumptions.

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**Figure I.15. The revenue shortfall was exacerbated by huge spending...**

**Figure I.16. ...reversing the fiscal surplus trajectory of the past three years**

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16 In fact, the 2020 budget amendment (August 2020) exhibits a widening of the overall fiscal deficit from an initial target of 2.4 percent of GDP to 9.9 percent of GDP.

17 The prudent fiscal policy followed by the authorities during 2017–19 created some fiscal space and led to the accumulation of sizable cash reserves of about MNT 2.7 trillion (over 7 percent of GDP) at end-2019.
The government’s COVID-19 relief package, totaling about MNT 3.6 trillion (over 9 percent of GDP), was rolled out in three phases.\(^1\) The government response is primarily focused on supporting households and firms particularly affected by the economic downturn, and on small and medium-sized enterprises (SMEs) to cushion loss of income and avoid mass unemployment and bankruptcies. This includes over 3 percent of GDP in tax relief measures and 6 percent of GDP in increased social transfers and higher health spending (figure I.17).

**Box I.2. Government fiscal relief measures to alleviate the economic impact of the COVID-19 pandemic**

**Figure I.17. COVID-19 fiscal relief measures**

<table>
<thead>
<tr>
<th>Tax relief measures (over 3% of GDP)</th>
<th>Spending measures (over 6% of GDP)</th>
</tr>
</thead>
<tbody>
<tr>
<td>SSC exemptions</td>
<td>Increase in CMP</td>
</tr>
<tr>
<td>PIT exemptions</td>
<td>3.4</td>
</tr>
<tr>
<td>CIT exemptions (turnover &lt; MNT1.5 bn)</td>
<td>0.5</td>
</tr>
<tr>
<td>PIT/CIT exemption if rent has been lowered</td>
<td>0.16</td>
</tr>
<tr>
<td>Waiving late payment penalties for PIT/SSC</td>
<td>0.07</td>
</tr>
<tr>
<td>VAT exemption (Medical &amp; Food)</td>
<td>0.03</td>
</tr>
<tr>
<td></td>
<td>Increase in health spending</td>
</tr>
<tr>
<td></td>
<td>0.7</td>
</tr>
<tr>
<td></td>
<td>Cash transfer to herders</td>
</tr>
<tr>
<td></td>
<td>0.5</td>
</tr>
<tr>
<td></td>
<td>Increase in social welfare pension</td>
</tr>
<tr>
<td></td>
<td>Wage subsidies for employers</td>
</tr>
<tr>
<td></td>
<td>0.13</td>
</tr>
<tr>
<td></td>
<td>Increase in govt’s emergency fund</td>
</tr>
<tr>
<td></td>
<td>0.1</td>
</tr>
<tr>
<td></td>
<td>Interest subsidies for cashmere producers</td>
</tr>
<tr>
<td></td>
<td>Doubling food stamp allowance</td>
</tr>
<tr>
<td></td>
<td>0.04</td>
</tr>
</tbody>
</table>

**Figure I.18. Mongolia’s fiscal relief package is one of the highest among EAP countries**

**Figure I.19. Income support and tax exemptions dominated fiscal relief measures**

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\(^1\) It includes the extension of some measures which are expected to be implemented until July 2021. But it does not include the government’s recent decision on exempting utilities fees for households and enterprises.
Mongolia has limited headroom to provide further fiscal relief (and to boost economic recovery). In terms of government debt sustainability, Mongolia compares unfavorably to other countries. Government debt as a share of GDP accounts for about 70 percent at end-2019, compared to the 40 percent average for emerging markets and developing economies (EMDEs). Moreover, banks’ excess liquidity was estimated MNT 7.7 trillion in November 2020, of which central bank bill holdings by banks was around MNT 5.4 trillion, indicating sizable room for domestic debt issuance. Given large external debt (over 60 percent of GDP compared to the 40 percent EMDE average), borrowing in foreign currency is still not a favorable option. Finally, tapping into the Fiscal Stability Fund could not provide enough fiscal space to mitigate the impact of the pandemic, considering declining coal prices. In fact, the Fiscal Stability Fund’s liquid part is estimated at MNT 150 billion (0.4 percent of GDP) as of end-November.

The revenue projections in the 2021 budget are moderately optimistic. At 7 percent, the growth assumption in the 2021 budget appears ambitious given the ongoing strict lockdown at the start of 2021. It is, however, achievable, assuming a strong recovery of mining exports and successful domestic containment of COVID-19. While commodity price assumptions are broadly in line with the projections of international institutions, export projections may be optimistic. In particular, the 2021 budget assumes that coal export volumes will increase to 42 million tons next year, a 15 percent rise from the historically high level (36.6 million tons) achieved in 2019. To achieve this target, the government plans to improve the capacity at the border posts and accelerate digitalization to reduce red tape. However, this is likely to be optimistic amid the preventive public health measures still in place and continued worries about the rise in infection rates in major markets. Moreover, the budget assumes that tax administration reforms (simplification, digitalization, international taxation issues) will bring an additional MNT 1.1 trillion in revenue (1.5 percent of GDP), contributing to 44 percent of the total expected revenue increase (figure I.21). However, the successful and timely implementation of these measures may be challenging in a context dominated by the pandemic.

**Figure I.20. The deficit widened sharply in 2020 but is expected to narrow notably in 2021**

**Figure I.21. The revenue projections in the 2021 budget are moderately optimistic...**

**Sources:** MoF; World Bank 2020b; World Bank staff estimates.
Box I.3. Summary of the 2021 budget

The 2021 budget is based on optimistic macroeconomic assumptions. It assumes (i) real economic growth of -1 percent in 2020 and 7.2 percent in 2021; (ii) strong demand for coal and relatively higher production of copper concentrate; (iii) continuation of tax reforms in 2021; and (iv) inflation of 7 percent in 2021, in line with the monetary policy guidelines. The revenue projections and corresponding expenditure plans are shown in Table I.1.

Table I.1. Mongolia: Improvements in the overall fiscal balance in 2021 (% of GDP)

<table>
<thead>
<tr>
<th></th>
<th>2020 Supplementary</th>
<th>2021 Plan</th>
<th>Diff</th>
</tr>
</thead>
<tbody>
<tr>
<td>Revenues</td>
<td>27.7</td>
<td>31.1</td>
<td>3.4</td>
</tr>
<tr>
<td>Stabilization &amp; Heritage Funds</td>
<td>2.6</td>
<td>3.2</td>
<td>0.6</td>
</tr>
<tr>
<td>Tax Revenues</td>
<td>22.9</td>
<td>25.5</td>
<td>2.6</td>
</tr>
<tr>
<td>Non-Tax Revenues</td>
<td>2.3</td>
<td>2.5</td>
<td>0.2</td>
</tr>
<tr>
<td>Expenditures</td>
<td>37.7</td>
<td>33.0</td>
<td>-4.6</td>
</tr>
<tr>
<td>Recurrent spending</td>
<td>26.3</td>
<td>23.3</td>
<td>-3.0</td>
</tr>
<tr>
<td>o.w. Wages and Salaries</td>
<td>6.9</td>
<td>5.7</td>
<td>-1.2</td>
</tr>
<tr>
<td>Goods &amp; Services</td>
<td>5.9</td>
<td>4.8</td>
<td>-1.2</td>
</tr>
<tr>
<td>Others (incl. Social Spending)</td>
<td>13.5</td>
<td>12.8</td>
<td>-0.7</td>
</tr>
<tr>
<td>Capital spending</td>
<td>8.8</td>
<td>8.4</td>
<td>-0.4</td>
</tr>
<tr>
<td>Interest Payments</td>
<td>2.5</td>
<td>2.7</td>
<td>0.2</td>
</tr>
<tr>
<td>Overall balance</td>
<td>-9.9</td>
<td>-1.9</td>
<td>8.0</td>
</tr>
<tr>
<td>Primary balance</td>
<td>-7.4</td>
<td>0.8</td>
<td>8.2</td>
</tr>
</tbody>
</table>

Source: MoF.

Key highlights of the 2021 budget:

- Return to a fiscal sustainability path after a substantial hike in the fiscal deficit in 2020 driven by a sharp revenue shortfall and a rise in public spending to mitigate the impact of COVID-19 crisis.
- Fiscal improvements mainly supported by:
  - Higher mineral revenue, reflecting the positive prospect in commodity prices and ambitious export targets.
  - Stronger economic recovery leading to higher tax revenue under existing and new policies.
  - Rolling back (expiry) of COVID-19-related spending measures and other recurrent spending, and rationalization of capital expenditures to compensate for the substantial increase in social spending (mainly the Child Money Program) planned in H1 2021.
  - Improvement in the overall balance of over US$1 billion (8 percentage points of GDP) and a primary deficit of over US$1.1 billion (8.2 percentage points) compared with the 2020 supplementary budget.
- Ambitious but achievable growth assumptions depending on recovery in mining exports.
- Revenue projections are predicated on successive implementation of tax administration reforms (simplification, digitalization, international taxation issues including introduction of transfer pricing and renovation of customs capacity).
- Assuming successful containment of the pandemic, recurrent spending related to COVID-19 measures are planned to be scaled down.
- No growth assumed in the size of the civil service, the wage bill, or pensions.
- Partial extension of top-up on benefits of the Child Money Program entails sizable fiscal burden (about 2.2 percent of GDP).
• Capital expenditure allocation (8.4 percent of GDP) slightly declined from 2020 supplementary budget - largely to complete ongoing projects. It remains higher than in the pre-COVID years (which were significantly expansionary).
• Interestingly, many projects that were included in the 2020 budget for reconstruction have been scaled down for renovation, with substantial cost savings (these include the state drama theater, state opera house, and national library). However, there is room for further rationalization and reprioritization of the current public investment program. The capital expenditure execution rate has generally averaged about 80 percent over the past three years.
• Commitment to budget credibility as overall budget envelope is consistent with the 2020 Medium-Term Fiscal Framework.

Sources: MoF, 2020 budget document; World Bank staff illustrations.

A5. External pressures considerably eased following notable current account adjustment

Despite lower capital inflows and large private sector debt repayments, external pressures eased considerably amid exports recovery and imports compression. In 2020, Mongolia’s balance of payments recorded a surplus of US$787 million (figure I.22). Despite a narrower surplus of the financial account, external pressures were reduced thanks to a remarkable current account adjustment. Lower FDI (which contracted by about 30 percent [y/y] in 2020) and the private sector external debt payment (US$500 million in May 2020) accounted for the narrower financial account surplus despite official sector support from development partners including ADB, IMF, AIIB, the World Bank and Japan. In contrast, weak domestic demand and the quick recovery of exports have resulted in a remarkable current account adjustment.

![Figure I.22. Current account adjustment was enough to ease external pressures](image)

**Figure I.22. Current account adjustment was enough to ease external pressures**

![Figure I.23. Current account surplus in recent months is unprecedented in Mongolia’s recent history](image)

**Figure I.23. Current account surplus in recent months is unprecedented in Mongolia’s recent history**

![Sources: BoM; World Bank staff estimates.
Note: CA = current account; KA = capital account; FA = financial account; and BOP = Balance of payments.](image)

![Notes: 3 mma = three-month moving average.](image)

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17 The recent sovereign bond issuance (US$600 million in late September) by the government did not have a sizable direct impact on the country’s external position as the proceeds were used mainly to pay off existing public debts. In contrast, it had significant implications on market expectations regarding immediate pressure of external liquidity and exchange rate depreciation.
Improvement in the trade balance drove the current account adjustment. The current account deficit narrowed to US$433 million in 2020 from US$2.1 billion in 2019. In fact, the current account posted a surplus of US$530 million during May–December, which is unprecedented in the past decade (figure I.23). Import compression supported by weaker domestic demand and lower oil prices contributed to the current account adjustment, coupled with the relatively quick recovery of exports (figures I.24 and I.25).20,21,22 Moreover, lower profits repatriation and declining service payments (for example, travel restrictions and limited truck activities) also played an important role in the improved current account balance. Furthermore, the BoM’s gold purchase, which reached a historically high level of 23 metric ton in 2020, significantly supported the export recovery (figure I.24).23

Current account adjustment, specifically a surge in gold purchases by the BoM, led to a strong recovery in reserves after a significant drop during January–May. Due to the sharp drop in exports, the current account deficit widened in H1 2020 compounded by declining capital inflows (mainly FDI) and large private sector external debt repayments, resulting in a drain on foreign exchange reserves (figure I.26). However, reserves recovered significantly in H2 2020 amid the current account adjustment, disbursement from some donors, and extensive gold purchases by the BoM. In fact, gross international reserves reached a historically high level of US$4.5 billion (equivalent to over eight months of imports) at end-2020, up from US$4.3 billion in 2019.

Figure I.24. Exports were hit hard in H1, but have recovered quickly

<table>
<thead>
<tr>
<th>Contribution to growth (y/y, percentage points)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Gold</strong></td>
</tr>
<tr>
<td><strong>Copper</strong></td>
</tr>
<tr>
<td><strong>Coal</strong></td>
</tr>
<tr>
<td><strong>Crude oil</strong></td>
</tr>
<tr>
<td><strong>Others</strong></td>
</tr>
<tr>
<td><strong>Total exports growth</strong></td>
</tr>
</tbody>
</table>

Sources: NSO; BoM; World Bank staff estimates.

Note: Coal, copper and gold accounted for 75 percent of total export proceeds in 2020.

Figure I.25. Import compression has largely been driven by lower fuel and capital goods imports

<table>
<thead>
<tr>
<th>Contribution to growth (y/y, percentage points)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Consumption</strong></td>
</tr>
<tr>
<td><strong>Capital goods</strong></td>
</tr>
<tr>
<td><strong>Industrial &amp; Intermediate Fuels</strong></td>
</tr>
<tr>
<td><strong>Others</strong></td>
</tr>
<tr>
<td><strong>Total imports growth</strong></td>
</tr>
</tbody>
</table>

Sources: BoM; World Bank staff estimates.

20 Imports were also severely affected by friction at main border ports with Russia and China. Since the first domestic contagion of the virus, all transportation through the main borders were ceased, and there has been an increasing congestion of merchandise and traffic on the other side of the border. Without customs clearance, these items are not recorded as imports, despite having already been paid for. Since the friction is not expected to be resolved soon, the imports are likely to be recorded in late January or February 2021.

21 The government’s efforts to boost exports by accelerating coal transportation at the key border posts with China have also supported the recovery of exports.

22 Exports declined by 45.3 percent (y/y) in the first four months of 2020, but contraction eased significantly to 0.6 percent by December 2020 amid easing/expiry of some precautionary measures, recovery in Chinese demand and commodity prices (mainly copper prices), and a surge in gold exports.

23 To support gold mining, the BoM provided soft loans of MNT 110 billion (US$42 million) to gold miners under the “Gold-2” program.
The tugrug depreciated moderately against the US dollar in 2020 supported by foreign exchange (FX) interventions. In nominal terms, the tugrug depreciated by 4.2 percent against the U.S. dollar and by 11.2 percent against the Chinese RMB in 2020 (figure I.27). The depreciation of the tugrug was smaller in 2020 relative to the exchange rates of Russia and Kazakhstan (figure I.28). Such moderate depreciation was supported by the intervention of the BoM, which continued to sell foreign exchange on the domestic market. In fact, BoM’s gross foreign exchange interventions (excluding direct FX purchases from large mining companies) reached US$2.63 billion in 2020, close to the US$2.87 billion in 2019 (figure I.29). Nonetheless, with moderate inflation, the real effective exchange rate depreciated by over 3 percent (y/y) by November 2020.

Figure I.26. FX reserves recovered strongly after a sharp fall in H1, supported by eased current account adjustment and gold purchases...

Gross international reserves (GIR) (billion US$)

Source: BoM.
Note: FX = foreign exchange.

Figure I.27. …and the exchange rate stabilized in H2 after a moderate depreciation in the first half

Exchange rate: Tugrug (Spot rate, Index, Dec 31, 2015=100)

Source: BoM.

Figure I.28. The tugrug depreciation was moderate compared to Mongolia's structural peers...

Nominal exchange rate per US$ (y/y change, end-2020)

Sources: https://www.x-rates.com/; BoM; World Bank staff estimates.

Figure I.29. …supported by FX interventions by the BoM, particularly in the first half of 2020

The BoM's net FX sales and MNT/US$:

Sources: BoM; World Bank staff estimates.
Note: The BoM's gross FX sales exclude its direct FX purchases from large mining companies, which started in June 2018. eop = end-of-period; RHS = right-hand side; LHS = left-hand side.
A6. Monetary conditions have eased, but risks in the banking sector are building as asset quality deteriorates

Prior to the onset of the COVID-19 pandemic, monetary policy focused on addressing unsustainable credit growth through macroprudential measures. As inflation was well within the BoM’s target of 8 percent in 2018–19, the BoM focused on addressing unsustainable credit growth (particularly household loans) and external imbalances with a mix of contractionary monetary and macroprudential policy measures. In fact, the rapid credit expansion in 2017–18 was channeled mainly to households, and consequently, the household debt-to-income ratio was estimated to have reached as high as about 70 percent at end-2018, up from an average of 39 percent in 2012. As a result of macroprudential measures, broad money growth and domestic credit growth fell from 23 percent and 26.5 percent, respectively, in December 2018, to 7 percent and 5.1 percent in December 2019 (figure I.30).

In 2020, the monetary policy stance shifted toward mitigating the economic impact of the pandemic. Since March 2020, the BoM lowered its policy rate four times by a cumulative 500 basis points to 6 percent, a historical low (figure I.30). The goal was to reduce market interest rates and boost domestic demand in the medium term. The BoM has also been trying to nudge banks to use their excess liquidity to support economic activities by making it relatively unattractive for banks in the short run to passively deposit funds with the central bank in the form of central bank bills. Moreover, the central bank reduced the reserve requirement ratio, and introduced a longer-term liquidity instrument to further encourage banks to lend their excess liquidity.

In addition, the BoM reengaged with the government’s subsidized mortgage program, introduced a freeze on mortgage loan repayments, engaged in several asset purchasing programs, and provided soft loans to banks to support non-mineral export industries and SMEs. In total, these measures are estimated to cost around 3 percent of GDP, while the effective cost of other regulatory measures could not be estimated (see box I.4).

The impact of the monetary policy easing was mitigated by a credit contraction amid the pandemic. Broad money growth accelerated to 16 percent (y/y) in December, from its recent low of 1.6 percent in April 2020. However, domestic credit growth remained in negative territory while banking sector excess reserves continued to increase gradually (figure I.31). The overall economic contraction, rising nonperforming loans, and risk aversion due to heightened uncertainty made banks reluctant to lend and companies reluctant

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**Figure I.30. The monetary policy rate was lowered to a historical low to revive credit growth**

![Graph showing the monetary policy rate, money supply, domestic credit, and policy rate](image)

**Sources:** BoM; World Bank staff estimates.

**Note:** RHS = right-hand side; LHS = left-hand side.

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**Figure I.31. However, banks have been reluctant to lend despite having sizable excess reserves**

![Graph showing domestic credit and banks excess reserves](image)

**Sources:** BoM; World Bank staff estimates.

**Note:** RHS = right-hand side; LHS = left-hand side.

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24 These include macroprudential measures aimed at limiting the debt-to-income ratio of individual borrowers from as high as 100 percent to 60 percent, reducing the maturity on non-mortgage household loans, and raising the risk weight on unhedged foreign currency borrowing.
The Monetary Policy Committee (MPC) of the Bank of Mongolia (BoM) met six times since the start of the COVID-19 pandemic in February 2020. Several decisions were taken by the MPC aimed at boosting credit growth, relieving the debt burden, and supporting liquidity of the banking system. These include:

- **Reducing the policy rate sequentially from 11 percent to 6 percent**, over meetings held in March, April, September, and November 2020. As the inflation outlook remained within the central bank’s target, reduction of the policy rate was intended to relieve the financing costs of banks, support financial intermediation, and stimulate domestic demand.

- **Relaxing the condition of repo financing instruments** to support liquidity of the banks. The MPC narrowed the interest rate corridor by 200 basis points, which effectively reduced the interest rate on the short-term repo instrument. In September, the maturity of the longer-term repo instrument was temporarily extended from 90 days to 180 days and its interest rate reduced from 16 percent to 11 percent. Consequently, banks could borrow from the BoM at a lower rate and for a longer term.

- **Releasing more liquidity to the banking system by reducing the required reserve ratio** on domestic currency liabilities by 4.5 percentage points to 6 percent in March. As a result, an estimated MNT 730 billion was released to the market.

- **Promoting incentives to reduce interest rates on FX deposits and discourage deposit dollarization** by reducing remuneration provided to banks by the amount equivalent to their FX deposits and interest-bearing FX current accounts. In addition to applying higher reserve requirements on FX liabilities, this measure was intended to support the stability of the financial system by addressing the growing currency mismatch.

- **Allowing the restructuring and extension of the maturity of consumer loans** of troubled borrowers for up to 12 months and later extending the deadline to the end of the year. These measures are intended to reduce monthly payments of troubled borrowers and support private consumption.

- **Purchasing assets and providing concessional loans.** The BoM purchased municipal bonds to support its mortgage program (MNT 100 billion) targeting civil servants at the COVID-19 frontline; provided repo loans to banks to indirectly support loans for non-mineral exports and SMEs (MNT 230 billion), and directly provided concessional funding for gold companies under the “Gold-2” program (MNT 110 billion).

Under its supervisory function, the BoM made temporary changes to its regulations, effective until the end of 2020. These include:

- **Loosening the asset classification regulation** starting in March so that borrowers’ credit history is not affected. Consumer and mortgage loans that are in arrears for less than 90 days will be considered normal (the regular cutoff is 15 days), those in arrears for 91 to 120 days will be considered past due (the regular cutoff is 90 days), and those that missed payments for over 121 days would be considered nonperforming.

- **Reducing the liquidity ratio** for banks from 25 percent to 20 percent, so that banks could reduce their liquid assets and create room for issuing loans.

- **Encouraging banks to reduce their transaction fees and removing FX deposits** from the insurance coverage to discourage deposit dollarization.
Under the framework of a Parliamentary resolution to support the economy amid COVID-19, passed on April 29, the BoM took the following measures:

- **Allowing the freezing of payments of the subsidized mortgage program** and extending its maturity for up to six months (later extended by eight more months). The subsidized mortgage borrowers were given a one-time option to restructure their loans without any interest accrual on their balance starting May 1. As of June 19, 38,270 borrowers had restructured their loans and delayed payments of MNT 121 billion MNT. In November, the freeze period was extended by eight more months and is expected to delay payments of MNT 310 billion.

- **Continuing to finance the subsidized mortgage program.** As agreed under the IMF Extended Fund Facility program and the World Bank’s Economic Management Support Operation series, BoM financing of the subsidized mortgage program ended on January 1, 2020. However, the Law on Pandemic Preparedness and Response of April 2020 reauthorized BoM’s financing of the program, which currently amounts to about MNT 245 billion.

Source: BoM.

Note: a. The BoM provides some remuneration to banks for their assets held at the central bank in accordance with the reserve requirement. b. The option to restructure is usually not restricted by the BoM. However, loans issued before January 1, 2019, were not capped by the ceiling of 60 percent set on the debt-service-to-income ratio and a 30-month term limit. Restructuring these loans would have violated either one of these restrictions. The BoM therefore provided a one-time pardon on the term limit of 30 months to reduce the debt burden of households.

to invest – explaining the limited impact of monetary policy easing on credit growth. A thorough clean-up of bank balance sheets post crisis may be needed to encourage fresh lending activity and thus support the recovery.

The credit contraction was prolonged as consumers and small businesses were severely hit by the COVID-19 shock. Domestic credit contracted by about 5 percent in 2020, marking a contraction of 10 consecutive months. While banks have tightened their loan issuance to corporates and households as loan quality deteriorated rapidly, weakening income of households and lower profitability of the corporates have curtailed their potential to borrow, as well. According to the NSO’s survey, 64.2 percent of firms reported an income loss over 50 percent due to the COVID-19 shock. Corporate loan issuance has been declining in all sectors and seems most severe in key sectors such as construction, trade, transportation, manufacturing, and mining (figure I.32). In addition to tighter conditions and weakening income, the decelerating preference of households for durable goods such as cars may have contributed to declining loan issuance (figure I.33).

**Figure I.32. Corporate loans issuance has been declining across sectors**

<table>
<thead>
<tr>
<th>Corporate loans issuance (a 12-month rolling sum, y/y)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agriculture</td>
</tr>
<tr>
<td>60%</td>
</tr>
<tr>
<td>-10%</td>
</tr>
</tbody>
</table>

**Sources:** BoM; World Bank staff estimates.

**Figure I.33. Banks have also tightened new loan issuance to individuals, entrepreneurs, and SMEs**

<table>
<thead>
<tr>
<th>Individual loans issuance (a 12-month rolling sum, y/y)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Salary and pension backed</td>
</tr>
<tr>
<td>Dec-18</td>
</tr>
<tr>
<td>50%</td>
</tr>
<tr>
<td>-10%</td>
</tr>
</tbody>
</table>

**Sources:** BoM; World Bank staff estimates.
Asset quality of the banking system has deteriorated notably, reflecting the impact of the pandemic. The nonperforming loans (NPLs) of commercial banks reached MNT 2 trillion by December, a 10 percent increase relative to end-2019. The NPL ratio (nonperforming loans to total outstanding loans) increased to 11.7 percent in December from 10.1 percent in December 2019 (figure I.34). Past-due loans have been increasing more rapidly. The amount of past-due loans reached about MNT 1.3 trillion from MNT 816 billion in December 2019. The ratio of past-due loans to total loans jumped to 7.4 percent in December from 4.5 percent at end-2019. Problematic loans (NPLs and past-due loans) are likely to rise further once forbearance on identification of these loans expires as planned by July 2021. According to the BoM, as of September 2020, over 20 percent of total loans in the banking sector were affected by the pandemic, and additional loans may become problematic once regulatory forbearance is scaled back. Across sectors, the mining sector claimed the highest proportion of loans affected by the COVID-19 shock (46 percent), followed by construction (38 percent), trade (35 percent), and real estate (26 percent) (figure I.35).

The adequacy of loan loss provisions (LLP) for both corporate and individual loans is uncertain. As of December 2020, LLP for corporate loans stood at MNT 1.2 billion. This covers over 80 percent of NPLs and around half of the value of problematic loans (NPLs + past due loans), (figure I.36). The LLP coverage of problematic loans for the mining, construction, manufacturing, and trade sectors ranged between 33 and 77 percent, while these sectors combined account for about 70 percent of total problematic loans. Meanwhile, 51 percent of the value of problematic loans issued to individuals is currently covered by provisions (figure I.37). The weakest provisioned loans are car loans.

The banking system remains liquid. The liquidity ratio (liquid assets to total assets) has been trending up since June 2020 and reached 40.6 percent in December 2020, its highest in the past two years (figure I.38). Bank reserves stood at 15.9 percent of total deposits in December 2020, above the reserve requirement ratios (15 percent for FX deposits and 6.5 percent for MNT deposits). However, this is a reduction from 25.6 percent in April 2020 mainly due to a steady increase in FX deposits (denominator) until September 2020.

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25 The provision coverage ratio is used to determine how banks are protected from possible losses on nonperforming credits.

26 The consistent increase in the FX deposits since March 2020 was reversed in October 2020. From a peak of 31 percent in September 2020, the FX deposit - total deposit ratio reached 25.7 percent in December 2020, its level in March–April 2020.
However, the risk of currency mismatch remains high in the banking system. The share of foreign liabilities in the banking system is almost triple the size of foreign assets, which exposes banks to high risks of currency mismatch. In fact, FX deposits reached 31 percent of total deposits in September 2020, the highest rate in two years, while FX loans were 9 percent of total loans (figure I.39). Credit risk associated with exchange rate fluctuation is now relatively moderate as banks have significantly tightened their condition for FX loans over the past few years. In contrast, households and corporates have ramped up their FX deposits following mounting external pressures, particularly in the first half of the year. Deposit dollarization has declined somewhat in recent months amid an improving current account balance and sequential policy measures by the BoM, including setting higher reserve requirements on FX deposits and removing its insurance coverage in case of bank failures (see box I.4). Nevertheless, the large gap between deposit dollarization and credit dollarization in times of an uncertain external environment exposes banking system balance sheets to significant fluctuations in the exchange rate.

Sources: BoM; World Bank staff estimates.
Note: FX deposits of firms and households are considered liabilities for banks, while FX loans are assets of banks.
RHS = right-hand side; LHS = left-hand side.
B. Outlook and Risks

The Mongolian economy is expected to recover moderately from the pandemic, as the latest outbreak has added considerable uncertainty. Mongolia is expected to have experienced its first recession in a decade in 2020 as real GDP is estimated to contract by 5.2 percent (table I.2).\textsuperscript{27} Mongolia trails the Philippines, Thailand, and Malaysia, which are the other economies projected to be most impacted in the EAP region (box I.6). The mining and services sectors, particularly, are expected to be severely hit by weak external demand and COVID-19 containment measures. However, real GDP growth is projected to accelerate to about 5 percent in 2021–22, supported by a renewed drive of investment in the mining sector (compounded by higher-grade ore and increased production of gold) despite delay in the production schedule of Oyu Tolgoi’s underground development.\textsuperscript{28} Private investment backed by FDI and domestic credit (mainly corporate loans) will remain a key contributor to growth in 2021-22, especially in mining, manufacturing, and transport services. Private consumption will also support growth in the medium term.

Monetary policy is expected to be tightened in the medium term as inflation and external sector pressures re-emerge. Inflation moderated in 2020 driven by weak domestic demand, lower imports, and negative credit growth. However, it will pick up gradually in 2021–22, while exceeding the BoM’s medium-term target as economic activity recovers.\textsuperscript{29} Moreover, relatively higher fiscal spending in 2020 compared to the previous two years and the expected recovery of domestic credit could generate inflationary pressures in 2021.\textsuperscript{30} Our base case is built on the continued commitment of the monetary authorities to price stability keeping inflation within the central bank’s target, which would eventually help lower inflation expectations. Interventions in the foreign exchange market are expected to be limited to smoothing excessive volatility, allowing more flexibility in exchange rate movements, and rebuilding international reserves. Further policy rate cuts are unlikely as the external environment remains uncertain and the central bank’s policy rate is already at a historical low (6 percent). In addition, the reserve requirement ratio stands at 6.5 percent, its lowest level since the 2008–09 global financial crisis, leaving little room for decreasing it further to induce liquidity into the financial system. Recently introduced monetary policy tools such as long-term repo transactions (which has availed MNT 230 billion to banks in Q4 2020 and up to MNT 250 billion

\textsuperscript{27} Our estimate of real GDP growth for 2020 contrasts squarely with overoptimistic growth assumptions of the 2021 budget, which considered a 1 percent contraction in 2020 and 7.2 percent growth in 2021 (see box I.3).

\textsuperscript{28} This increase in the gold production outlook is the result of initiatives implemented by Oyu Tolgoi that have brought the higher-grade gold-bearing ore from the South West pit forward into 2020 and 2021. The plan also allows for copper production growth of 315 percent from 2022 to 2028 as well as gold production growth of 140 percent in the same time frame.

\textsuperscript{29} Through the approval of 2021 monetary policy guidelines, the BoM reduced its inflation target rate for 2021–23 to 6 percent, with a +/-2-percentage-point band.

\textsuperscript{30} IMF 2012.
is expected in Q1 2021) could put further pressure on the domestic FX market amid weak FX inflows.31 32

Further loan forbearance by the BoM could lead to unintended effects including on economic growth in the medium term. As indicated earlier, the asset quality of several banks has been threatened amid diminishing corporate earnings over the past few months. In addition, the forbearance measures could be masking a significant amount of problematic loans as discussed above. By September 2020, over 20 percent of the banking sector loan book had been reportedly impacted by COVID-19. Therefore, advancing bank reforms would be critical to support growth in the medium term as several banks, especially those exposed to sector-distressed loans, lower earnings, and insufficient capital, may be vulnerable.

The 2021 budget and the medium-term fiscal framework for 2021 - 23 are broadly consistent with fiscal consolidation and the debt reduction objective. The government’s Medium-Term Fiscal Framework projects an overall budget deficit of 1.5 percent of GDP, on average, in 2021-23. However, under less optimistic revenue projections, we project that the overall fiscal deficit would average about 1.9 percent of GDP during 2021-23. Financial support from multilateral and bilateral donors would be necessary to ensure sustainable financing of the deficit. Interest payments, reflecting projected concessional financing, are projected to decline to 2 percent of GDP during 2021-23 from 2.6 percent of GDP in 2020 and 2.3 percent in 2019.33

After a rise in 2020, the government debt-to-GDP ratio is expected to decline again in the outer years with favorable debt dynamics in part driven by a cyclical recovery. Before the COVID-19 outbreak, broadly prudent fiscal management in 2017–19 led to a sharp reduction in government debt, giving the government some room to craft a fiscal response. The combination of increased spending and an expected decline in revenue collection is estimated to widen the fiscal deficit considerably and lead to an increase in government debt. The three phases of stimulus packages combined amount to approximately over 9 percent of GDP, which was financed mainly by external concessional lending and a drawdown of the government’s deposits in the sovereign wealth fund. With a sizable revenue shortfall and fiscal relief measures, government debt is estimated to have risen in 2020 before declining gradually starting from 2021. However, Mongolia’s debt ratio remains high among comparators (figure I.40).

Figure I.40. The government debt-to-GDP ratio is estimated to have risen in 2020 in many selected peers

<table>
<thead>
<tr>
<th>Country</th>
<th>2020</th>
<th>2021f</th>
<th>2022f</th>
</tr>
</thead>
<tbody>
<tr>
<td>China</td>
<td>38.5</td>
<td>36.0</td>
<td>33.5</td>
</tr>
<tr>
<td>Chile</td>
<td>37.5</td>
<td>35.0</td>
<td>32.5</td>
</tr>
<tr>
<td>Kazakhstan</td>
<td>36.0</td>
<td>33.5</td>
<td>31.0</td>
</tr>
<tr>
<td>Malaysia</td>
<td>35.0</td>
<td>32.5</td>
<td>30.0</td>
</tr>
<tr>
<td>Mongolia</td>
<td>40.0</td>
<td>39.0</td>
<td>38.5</td>
</tr>
<tr>
<td>Peru</td>
<td>45.0</td>
<td>43.5</td>
<td>42.0</td>
</tr>
<tr>
<td>Philippines</td>
<td>48.0</td>
<td>47.0</td>
<td>46.5</td>
</tr>
<tr>
<td>Russia</td>
<td>52.0</td>
<td>51.5</td>
<td>51.0</td>
</tr>
</tbody>
</table>

Sources: IMF 2020; World Bank staff estimates.

Risks

There is a large band of uncertainty around the baseline forecast, with both upside and downside risks. In the near term, the biggest risk is the inability to contain the latest outbreak, resulting in a prolonged lockdown. This would take a significant toll on public health and the economy in the coming months. Other risks to the growth outlook include the impact of further waves of the COVID-19 global pandemic on commodity prices (especially coal and copper), a relaxation of the government’s commitment to reforms after the COVID-19 pandemic, weather-related shocks (drought/floods, a harsh winter), and limited progress on banking sector reforms (box 1.5). A downside scenario of the outlook could materialize if the impact of COVID-19 persists in advanced economies exacerbated by trade

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31 The recent renewal of the border bottleneck with China following the domestic contagion of the COVID-19 in Mongolia is an additional external sector pressure. In fact, coking coal prices in China recently soared to a four-year high after Mongolia’s first local transmission of the COVID-19 by mid-November 2020 resulted in emergency measures. These measures have slowed operations at the border crossings. Some traders have recently continued to lift Mongolian coal prices after noting firm coking coal demand from Chinese end-users.
32 The Monetary Policy Committee decided on December 18th that up to MNT 250 billion in funding would be provided to non-mining exporters and SMEs in Q1 2021.
33 One key feature of the government’s debt management strategy is to substitute expensive domestic debt with concessional borrowing and foreign debt obtained through refinancing on preferential terms, resulting in a considerable decline in interest payments in 2017-18.
### Table I.2. Key macroeconomic indicators

<table>
<thead>
<tr>
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<th></th>
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</tr>
</thead>
<tbody>
<tr>
<td><strong>Real GDP growth, at constant market prices</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Private Consumption</td>
<td>-2.2</td>
<td>5.4</td>
<td>12.4</td>
<td>9.9</td>
<td>2.0</td>
<td>3.6</td>
<td>4.5</td>
</tr>
<tr>
<td>Government Consumption</td>
<td>10.6</td>
<td>-1.8</td>
<td>-0.8</td>
<td>11.5</td>
<td>17.5</td>
<td>-5.1</td>
<td>1.6</td>
</tr>
<tr>
<td>Gross Fixed Capital Formation</td>
<td>0.5</td>
<td>35.6</td>
<td>21.3</td>
<td>23.5</td>
<td>-16.3</td>
<td>9.0</td>
<td>10.0</td>
</tr>
<tr>
<td>Exports, Goods and Services</td>
<td>15.8</td>
<td>14.8</td>
<td>24.0</td>
<td>9.1</td>
<td>-5.0</td>
<td>13.4</td>
<td>7.4</td>
</tr>
<tr>
<td>Imports, Goods and Services</td>
<td>12.7</td>
<td>24.8</td>
<td>30.9</td>
<td>22.3</td>
<td>-9.0</td>
<td>14.1</td>
<td>8.4</td>
</tr>
<tr>
<td><strong>Real GDP growth, at constant factor prices</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Agriculture</td>
<td>6.2</td>
<td>1.8</td>
<td>4.5</td>
<td>8.4</td>
<td>10.8</td>
<td>5.0</td>
<td>6.0</td>
</tr>
<tr>
<td>Industry (incl mining)</td>
<td>-0.4</td>
<td>0.7</td>
<td>7.9</td>
<td>3.1</td>
<td>-11.0</td>
<td>6.3</td>
<td>5.4</td>
</tr>
<tr>
<td>Services</td>
<td>1.1</td>
<td>7.7</td>
<td>4.7</td>
<td>5.8</td>
<td>-5.7</td>
<td>2.5</td>
<td>5.2</td>
</tr>
<tr>
<td><strong>Inflation (CPI, end-period)</strong></td>
<td>0.9</td>
<td>6.4</td>
<td>8.1</td>
<td>5.2</td>
<td>2.3</td>
<td>5.0</td>
<td>7.0</td>
</tr>
<tr>
<td><strong>Current account balance (% of GDP)</strong></td>
<td>-6.3</td>
<td>-10.2</td>
<td>-16.8</td>
<td>-15.4</td>
<td>-3.3</td>
<td>-7.7</td>
<td>-8.3</td>
</tr>
<tr>
<td><strong>Financial and Capital account (% of GDP)</strong></td>
<td>7.6</td>
<td>24.5</td>
<td>17.4</td>
<td>21.1</td>
<td>9.2</td>
<td>11.8</td>
<td>13.2</td>
</tr>
<tr>
<td>Net Foreign Direct Investment (% of GDP)</td>
<td>1.1</td>
<td>12.7</td>
<td>16.3</td>
<td>16.5</td>
<td>12.5</td>
<td>14.0</td>
<td>15.0</td>
</tr>
<tr>
<td>Fiscal Balance (% of GDP)**</td>
<td>-15.3</td>
<td>-3.8</td>
<td>2.6</td>
<td>1.4</td>
<td>-9.5</td>
<td>-2.7</td>
<td>-1.9</td>
</tr>
<tr>
<td>Primary Balance (% of GDP)</td>
<td>-10.1</td>
<td>0.4</td>
<td>5.8</td>
<td>3.7</td>
<td>-6.9</td>
<td>-0.3</td>
<td>0.1</td>
</tr>
<tr>
<td><strong>Public Debt (% of GDP)</strong>***</td>
<td>87.6</td>
<td>84.7</td>
<td>72.6</td>
<td>69.0</td>
<td>79.4</td>
<td>77.7</td>
<td>73.0</td>
</tr>
</tbody>
</table>

*In 2016, the net FDI number excluded the transactions of Oyu Tolgoi-2 project financing in May–June 2016.
** Development Bank of Mongolia (DBM) spending is excluded from fiscal balance and monitored separately.
***General government debt data exclude SOE debt and the central bank liability from the People’s Bank of China swap line.

Uncertainty between the United States and China. These events could severely cripple global demand, the price of key export commodities (particularly copper), and financial markets. Additionally, weather-related shocks (including potential risk of the dzud[^1]) could affect non-mining exports (for example, meat and cashmere) and thus adversely impact the income of poor and vulnerable herders. Finally, the failure to gradually return to fiscal discipline, as foreseen in the 2021 budget, could precipitate a deterioration in investor and consumer confidence and derail the incipient recovery. Inadequate recapitalization of the banking sector could exacerbate these risks and furthermore affect planned official sector support. On a positive note, the Financial Action Task Force removed Mongolia from the list of countries with inadequate protection against money laundering and terrorist financing, commonly referred to as the “grey list.” This would positively affect FDI inflows and boost the credibility of the financial sector.

A shrinking fiscal and monetary space could pose challenges to the Mongolian economy if the COVID-19 pandemic continues through 2021. Mongolia has used its available monetary and fiscal space to offset the negative economic impacts of the COVID-19 pandemic. However, with the Bank of Mongolia’s policy rate now at a historically low level, monetary policy space is limited to stimulate the economy if the pandemic persists. In addition, other monetary policy tools such as quantitative easing measures (including the recent introduction of a long-term repo instrument) could decrease the BoM’s space for further liquidity support. After a sharp rise in 2020 largely driven by the COVID-19 response package, government debt is expected to remain elevated and thus erode the existing fiscal space. Therefore, rebuilding fiscal buffers is a key priority in the medium term.

**External financing pressures could reemerge in the medium term.** Although exports are expected to recover notably in 2021–22, an expected renewed drive in imports of investment-related merchandise and services will likely keep the current account in the red in the coming years. Unless further external financing is timely and successfully mobilized, a higher current account deficit could easily translate into a deficit in

[^1]: Dzud “is a Mongolian term for a severe winter in which large number of livestock die, primarily due to starvation due to being unable to graze, in other cases directly from the cold” (https://en.wikipedia.org/wiki/Zud_(Mongolia).
Box I.5. Medium-term Banking Sector Strengthening Program for 2020–2023

On January 29, 2020, the Economic Standing Committee of the Parliament passed a resolution that authorized the Bank of Mongolia to implement the Medium-Term Banking Sector Strengthening Program for 2020–23. The program has five main objectives with detailed actions and expected outcomes:

1. **To reduce ownership concentration of the banking sector and improve its governance**, the BoM shall, among others, require banks to change their form from limited liability companies (LLCs) to joint stock companies (JSCs), limit the sum of shares with voting rights and offer some shares to the public, and make necessary changes in the legal framework to ensure the rights of the minority stakeholders. As a result, banks’ shareholding structure would be more diversified, and bank funding sources could be improved with public participation and oversight.

2. **To continue enhancing the banking supervision and regulatory instruments to international standards**, the BoM shall introduce prudential ratios conforming with the Basel standards, establish a legal framework for risk-based supervision, and collaborate with relevant authorities for effective enforcement. An expected outcome is a flexible risk-based banking supervision regulatory environment.

3. **To successfully complete the International Monetary Fund (IMF) Extended Fund Facility Program**, the BoM shall ensure that banks raise their additional capital in full from legitimate sources, take necessary actions on banks that failed to meet the capital requirement, and make an effort to reach an agreement with the IMF to complete the sixth review. As a result, the resilience and soundness of the banking system will be improved, and long-term economic growth will be sustained.

4. **To enhance the effectiveness of Anti-Money Laundering/Combating the Financing of Terrorism (AML/CFT)**, the BoM shall enhance the AML/CFT regulatory framework for banks and the effectiveness of its supervision with relevant authorities, support correspondent banking relationships of banks, and improve requirements and supervision of bank shareholders and their paid-in capital.

5. **To provide specialized banking licenses with requirements tailored to their operations and business models**, the BoM shall build an effective legal framework to issue specialized banking licenses, support introduction of FinTech to the banking sector, and modify the supervisory methodology accordingly.

Sources: BoM; minutes of the Economic Standing Committee meeting on January 29, 2020.

—the balance of payments. Despite, the extension of swap lines with the People’s Bank of China and successful refinancing of immediate payments of US$570 million, a total of US$2.1 billion in sovereign external debt is still due during 2021–24 (figure I.41). In addition, delayed implementation of ongoing reforms (including fiscal consolidation and the banking sector) and a less effective response to the pandemic could affect Mongolia’s sovereign ratings and reduce the odds of refinancing under favorable conditions. Although gross reserves reached a historically high level of US$4.5 billion (over eight months of imports) at end-2020, and it is expected to remain at that level in the medium term, it is still below 100 percent of the IMF’s Assessing Reserve Adequacy metric (a ratio between 100 and 150 percent is considered adequate).  

Figure I.41. The size of external bonds maturing during 2022–24 is significant

Payment schedule of key sovereign bonds (million US$)

<table>
<thead>
<tr>
<th>Year</th>
<th>O/W refinanced through the “Nomad” bond (US$600 mn)</th>
<th>Government international bonds</th>
</tr>
</thead>
<tbody>
<tr>
<td>2021</td>
<td>370</td>
<td>130</td>
</tr>
<tr>
<td>2022</td>
<td>600</td>
<td></td>
</tr>
<tr>
<td>2023</td>
<td>800</td>
<td></td>
</tr>
<tr>
<td>2024</td>
<td>600</td>
<td></td>
</tr>
</tbody>
</table>

Sources: MoF, BoM, World Bank staff estimates.

—The People’s Bank of China swap line with the BoM was renewed for another three years. Also, no large repayments of the public debt are due until 2022, partly thanks to a successful issuance of a US$600 million international bond in September 2020 (with a maturity of 5.5 years with a 5.1 percent coupon). This issuance (i) helped reassess market sentiment toward Mongolia; (ii) helped repurchase three-fourths of a US$500 million bond due in 2021, and one-fifth of a US$1.0 billion bond due in 2022; and (iii) contributed to interest savings of approximately US$27 million per year, according to the government.

The assessing reserve adequacy metric reflects potential balance-of-payments FX liquidity needs in adverse circumstances and is used to assess the adequacy of FX reserves against potential FX liquidity drains (see IMF 2016).
The massive shock triggered by the COVID-19 pandemic and shutdown measures to contain it have plunged the global economy into a severe contraction (figure I.42). In advanced economies, precautionary social distancing and stringent lockdowns in response to surging COVID-19 cases triggered an unprecedented collapse in the demand and supply of services in mid-2020, and the ensuing recovery has been dampened by a substantial resurgence of COVID-19 cases. The health and economic crisis triggered by COVID-19 caused emerging markets and developing economies (EMDE) output to shrink by an estimated 2.6 percent in 2020 - the worst rate since at least 1960. Excluding the recovery in China, the contraction in EMDE output in 2020 is estimated to have been 5 percent, reflecting recessions in over 80 percent of EMDEs—a higher share than during the global financial crisis, when activity shrank in about a third of EMDEs. The severity of the shock to EMDEs was uneven, depending on the intensity of pandemic-related domestic disruptions and the spillovers from the global recession. The worst-hit economies were those with extended periods of lockdowns combined with large domestic outbreaks or domestic policy uncertainty, and those that rely heavily on tourism and travel.

**Global economic output is expected to expand by 4 percent in 2021 but remain below pre-pandemic projections by more than 5 percent.** This outlook is predicated on proper pandemic management and effective vaccination limiting the community spread of COVID-19 in many countries, and on continued monetary policy accommodation accompanied by diminishing fiscal support. Global growth is projected to moderate to 3.8 percent in 2022, weighed down by the pandemic’s lasting damage to potential growth. Although aggregate EMDE growth is envisioned to firm to 5 percent in 2021 and to moderate to 4.2 percent in 2022, the improvement largely reflects China’s expected rebound. Absent China, the recovery across EMDEs is anticipated to be far more muted, averaging 3.5 percent in 2021–22, as the pandemic’s lingering effects continue to weigh on consumption and investment. Despite the recovery, aggregate EMDE output in 2022 is expected to remain 6 percent below its pre-pandemic projection. The pandemic is expected to leave lasting scars on productivity, including through its effect on the accumulation of physical and human capital, which will exacerbate the downward trend in potential growth.

Investment in EMDEs collapsed in 2020, following a decade of persistent weakness. Some recovery of investment growth is expected to expand in 2021 but will not be sufficient to offset the 2020 loss. Based on the experience of past epidemics, investment is likely to remain weak for several years following the COVID-19 pandemic. A supportive policy environment will be key to laying the groundwork for an investment rebound in EMDEs. The COVID-19 shock has triggered a surge in debt levels and has exacerbated debt-related risks in EMDEs, where even before the pandemic, a rapid debt buildup had raised concerns about debt sustainability and the possibility of financial crisis.
Most commodity prices rebounded in the second half of 2020; however, the pickup in oil prices lagged the broader recovery in commodity prices due to the prolonged impact of the pandemic on global oil demand. Oil prices are forecast to remain close to current levels and average US$44 per barrel in 2021 before rising to US$50 per barrel in 2022. The main risk to this forecast relates to the evolution of the pandemic, with oil demand particularly susceptible to lockdown measures and reduced mobility; however, positive vaccine news has reduced this risk somewhat. Base metal prices were, on net, broadly flat in 2020, as sharp falls in the first half of the year were followed by a strong recovery in the second half due to rising demand from China. Prices are expected to increase 5 percent in 2021 alongside the expected rebound in global demand (figure I.43). Agricultural prices rose 4 percent in 2020, largely driven by supply shortfalls and stronger-than-expected demand in edible oils and meals. Some regions experienced localized food price spikes, and a decline in household incomes, particularly among the poorest populations, has increased the risk of food insecurity. Agricultural prices are forecast to see a further modest increase in 2021.

After a sharp slowdown to 0.9 percent in 2020, output in East Asia and Pacific (EAP) is projected to expand 7.4 percent in 2021, to a level still around 3 percent below pre-pandemic projections (figure I.44). Growth in China is projected to accelerate to 7.9 percent this year, reflecting the release of pent-up demand and a quicker-than-expected resumption of production and exports. Growth is expected to slow to 5.2 percent in 2022, well below its pre-pandemic potential rate, leaving output about 2 percent below pre-pandemic projections. In the rest of the region, the recovery is expected to be more protracted. Following last year’s contraction, output in the region excluding China is expected to expand by 4.9 percent in 2021 and 5.2 percent in 2022, to a level around 7.5 percent below pre-pandemic projections, with significant cross-country variations.

While global growth is projected to recover in 2021, it will be weaker if a protracted pandemic requires an extension of control measures, the COVID-19 vaccine procurement and distribution are delayed, and a prolonged disruption to economic activity exacerbates financial stress resulting in a widespread financial and debt crises. For instance, fiscal measures have replaced a proportion of lost incomes and mitigated default risk, loan guarantees have helped keep businesses afloat, and liquidity provision by central banks has kept the financial system functional. However, if the impact of the pandemic continues to grow, financial crises may follow, resulting in a collapse in lending, a longer global recession, and a slower recovery. Even if the global financial system avoids a crisis, the debt accumulated in response to the pandemic may weigh on growth in the longer run.
II. COVID-19 IMPACTS ON HOUSEHOLDS IN MONGOLIA

A. Channels of COVID-19 Shocks to Households
B. Impacts on Employment and Labor Income
C. Impacts on Non-labor Income
D. Potential Impacts on Poverty
E. Potential Mitigation Impacts of Policy Responses
II. COVID-19 IMPACTS ON HOUSEHOLDS IN MONGOLIA

A. Channels of COVID-19 Shocks to Households

Mongolia went into nationwide lockdown for the second time on November 12, 2020. At the beginning of the COVID-19 outbreak, the Government of Mongolia took early and decisive measures to prevent the inflow of COVID-19, including closures of its borders and all schools (figure II.1). As confirmed cases grew globally, greater travel restriction measures have been imposed: the Trans-Siberian Railway and all inbound international flights were suspended and the border with Russia was closed. The government also canceled Mongolia’s national Lunar New Year celebrations and restricted travels in Ulaanbaatar and all 21 aimags (provinces). As these prompt containment and mobility restriction measures appeared to have been effective in preventing the local spread of COVID-19 in Mongolia, the government gradually lifted strict measures from May 31 and schools reopened on September 1, 2020. However, in mid-November, after the first locally transmitted cases were verified, the government imposed a strict nationwide lockdown, and while strict containment measures were lifted, some businesses remain closed and other containment measures continue as of end-January 2021.\footnote{This chapter was prepared by Ikuko Uochi (Economist) and Lydia Kim (Consultant) of the Poverty and Equity Global Practice at the World Bank.}

Despite fewer confirmed cases in Mongolia than in neighboring countries, the household-level shocks caused by COVID-19 may be long-lasting and disproportionately affect the poor and vulnerable. The poor and vulnerable generally have limited resources to protect themselves and are therefore likely to be most exposed to the negative impacts of many shocks. COVID-19-related shocks are no exception, and given their breadth and persistence, they have the potential to threaten the sustainability of poverty reduction efforts. While the poverty rate in Mongolia declined during 2016–18, the speed of poverty reduction has slowed, and much of the population is still clustered just above the national poverty line. When a shock hits, these vulnerable households can easily fall back into poverty while the poor can sink into deeper poverty.

COVID-19-related shocks may lead to adverse effects on various dimensions of household well-being through various transmission channels. Figure II.2 illustrates how the effects of COVID-19 are transmitted at the household and individual level. The impact of

\footnote{As of January 31, 2021, 1,779 cases were confirmed (https://coronavirus.jhu.edu/region/mongolia).}
COVID-19 can be divided into economic and social impacts. The economic impact is further divided into labor income, non-labor income, and price shocks on consumption. Given the relatively limited number of COVID-19 infections in Mongolia, households are more likely to be impacted by indirect economic shocks. The social impacts of the pandemic are mainly related to service delivery disruptions in health, education, and social protection. This section of the report will primarily focus on the economic aspects of COVID-19 shocks at the household level and explore how the impacts of COVID-19 are translated from aggregate shocks to households and individuals and estimate the potential effects of COVID-19 on the poverty rate.

### Figure II.1. Authorities tightened containment measures as the number of COVID-19 cases increased

![Stringency index graph](chart)

**Source:** Oxford University (OxCGRT).

**Note:** The stringency index measures the stringency of government containment measures, including school and workplace closings and restrictions on gatherings in response to COVID-19. Higher values indicate more stringent measures.

### Figure II.2. Transmission channels of COVID-19 impacts to households

![Transmission channels diagram](chart)

**Household Coping Strategies:**
- Reduced total food/education/health consumption
- Household labor/entering work force
- Use saving, borrowing
- Selling assets
- Risk pooling
- Government assistance and other aids, etc.

**Sources:** Modified based on World Bank (2020a).
B. Impacts on Employment and Labor Income

The COVID-19 Household Phone Response Survey (HRPS) shows that the pandemic caused significant disruptions in employment (box II.1). Almost 19 percent of workers who had been working pre-crisis had stopped working by the end of May 2020, with two-thirds out of work due to COVID-19-related issues such as mandated business closures, quarantine, or other reasons caused by mobility restrictions. Between June and September, some recovery in employment was visible, as nearly half of those who had been out of work by late May had returned to work by early September. However, with the rise in COVID-19 cases in early November and stricter containment measures, the share of individuals working pre-crisis who were no longer working rose to 51 percent by early December 2020 (figure II.3).

Box II.1. Mongolia COVID-19 Household Response Phone Survey

To explore transmission channels of COVID-19 shocks to households, the analysis in this report uses data from three rounds of the Mongolia COVID-19 Household Response Phone Survey (HRPS). The HRPS was jointly implemented by the National Statistics Office of Mongolia (NSO) and the World Bank with the aim of monitoring the economic and social impacts of the pandemic at the household level. The HRPS drew a subsample of 2,000 households from the nationally representative 2018 Household Socio-Economic Survey (HSES) and aimed to monitor and collect information from the same households across multiple rounds. The first round took place from May 22 to 29, 2020; the second from August 31 to September 7, 2020; and the third from December 3 to 15, 2020. The second lockdown occurred in mid-November to December 2020, which overlaps with the reference period for the third round of the HRPS. Comparison of the third-round results to other rounds in the HRPS or to any other surveys would be sensitive considering the timing and intensity of the containment measures. As the HRPS was phone-based, the sample is representative of households that have access to a telephone. Out of 16,454 households sampled in the 2018 HSES, 95.1 percent had a valid working phone number. Sampling weights were constructed to ensure unbiased estimates from the sample, and the sample distribution of the HRPS is similar to that of the 2018 HSES on key household characteristics such as location, education level of household head, and poverty status. The HRPS questionnaire covers a range of topics, including knowledge and behavior associated with COVID-19, employment, family business, herders’ livelihood, income, access to food and basic services, methods of coping with the crisis, and safety nets.

Table II.1. Overview of HRPS Rounds 1–3

<table>
<thead>
<tr>
<th></th>
<th>Round 1</th>
<th>Round 2</th>
<th>Round 3</th>
</tr>
</thead>
<tbody>
<tr>
<td>Data collection period</td>
<td>May 22 to 29, 2020</td>
<td>August 31 to September 7, 2020</td>
<td>December 3 to 15, 2020</td>
</tr>
<tr>
<td>Implementation method</td>
<td>Computer-assisted telephone interviewing (CATI)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Number of respondents</td>
<td>1,333 households</td>
<td>1,212 households</td>
<td>1,147 households</td>
</tr>
<tr>
<td>Response rate</td>
<td>66.7 percent (out of 2,000 households sub-sampled from 2018 HSES)</td>
<td>90.9 percent (out of 1,333 households interviewed in Round 1)</td>
<td>94.6 percent (out of 1,212 households interviewed in Round 2)</td>
</tr>
</tbody>
</table>


Respondents who “stopped working” in the HRPS refers to those who did not work for permanent or temporary reasons during the week preceding the survey, while they had worked in previous rounds or pre-pandemic. Please note that the definition of “stopped working” in the HRPS is different from the definition of unemployment in the Labor Force Survey, which refers to a person who is actively looking for a job during the last 30 days preceding the survey and is ready to start to work but is unable to find work.

In the HRPS, pre-crisis and pre-pandemic are defined as before January 27, 2020.
While the majority of these shocks to employment appear to have been temporary, poorer workers were more likely to face long-term job losses. About 6 out of 10 respondents to the HRPS who stopped working between June and December 2020 indicated that they had a job to return to once stringent containment measures have been lifted. Although this likelihood is similar across the welfare distribution, poorer workers have been significantly more likely to face long-term unemployment: Among those who were working pre-pandemic, 21 percent of workers in the bottom 40 of the welfare distribution had stopped working by June and continued to be unemployed by December, while just 11 percent of those in the top 60 had them.

Although the employment impacts of the crisis have extended across most economic sectors, industry, tourism, hospitality, transportation, and trade have been particularly affected. Shares of those who stopped working by December 2020 among the industry sectors - namely, manufacturing, utilities, construction, and mining - reached 70 percent (figure II.4). In particular, the construction and manufacturing sectors were heavily affected by the lockdown that occurred in mid-November to December 2020, which overlaps with the reference frame for the third round of the HRPS. As many construction sites and factories reopened once mobility restrictions eased, disruptions in employment in the industry sector are likely to be temporary: nearly two out of three of those who stopped working in the industry sector reported they have a job to return to. Private service sectors such as accommodation, restaurants, and transportation, as well as retail trade and other services (for example, personal services and recreation/entertainment), have also faced sizable employment shocks. While a

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41 These sectors are referred to as "affected sectors," and workers engaged in these sectors are referred to as "affected workers" in this report.
large share of those working in these service sectors had stopped working between January and December 2020, these employment disruptions likely happened during the strict second lockdown, and more than half of those out of work have a job to return to.\(^{42}\) In contrast, workers employed in the agriculture, public administration, health, and education sectors are by far less affected. Even under the second lockdown, only about one-third of those were out of work. However, once farmers and herders lose a job, they are less likely to be able to return to the same job even after the lockdown is lifted.

**Two out of three workers who stopped working between January and December 2020 were employed in the aforementioned affected sectors.** In 2019, about half of workers in Mongolia (48 percent of the employed population or 557,000 people) were engaged in the affected sectors (figure II.5). However, among workers who experienced job losses between the onset of the crisis and December 2020, almost 1.4 times this share was from the affected sectors. Overall, nearly 3 in 10 workers who faced disruptions were employed in industries, and 6 in 10 in services.

**Tourism-related service sectors were severely hit due to early and prolonged travel restrictions.** As shown in figure II.6, the first lockdown, during which the Government of Mongolia suspended all international flights, road and rail travel, and closed nonessential businesses last February resulted in a significant decline of carried passengers, and another nationwide lockdown from November 2020 halted the steady recovery of passenger railway use that began over the summer. Travel restrictions critically impacted tourism-related sectors (such as accommodations and restaurants), retail businesses, transportation, and other services (such as personal services and recreation). The number of tourists entering Mongolia more than halved in the first quarter of 2020 compared to the same period of 2019. It further declined to less than 10,000 people during the peak tourist season in the second and third quarters (figure II.7). As 70 percent of tourists came to the country during the second and third quarters in recent years, a prolonged decline in tourism flows worsened the impact on the tourism sector.

**COVID-19-related mobility restrictions and disruptions also decreased domestic private consumption in transportation, retail, hospitality, and other services, including personal services and recreation.** Figure II.8 exhibits Google mobility data, which indicate how busy certain types of locations are compared to a five-week period from early January to February 2020. The data show a significant decline in the number of trips to retail and recreation places, grocery stores, and transportation stations during February to April and again during November to December 2020. In particular, a sharp drop in visits to these places is visible in the last week of February and in mid-November, when the government restricted nonessential travel

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\(^{42}\) While more than 60 percent of those working in services sectors including accommodation and restaurants, retail trade, transportation, professional or technical activities, real estate, finance, insurance, information, and communication had stopped working by December 2020, previous rounds of the HRPS show that job losses were relatively small in these sectors until September 2020, before lockdown measures were put in place.
and ordered business and school closures. Despite an increase in mobility between April and November, COVID-19-related disruptions have continued having a detrimental effect on livelihoods - particularly during the second lockdown in November 2020 - in the retail, hospitality, personal services, and recreation sectors, which are concentrated in urban areas.

The affected service sectors are characterized by relatively high informality and low skill levels, rendering workers in these sectors more vulnerable to negative employment shocks. Over half of workers in retail trade and transportation are self-employed (figure II.9, panel a). In the trade sector and in the accommodation and restaurant sector, where, respectively, 44 percent and 70 percent of workers are paid employees, more than three-quarters are working for small firms with fewer than 50 employees (figure II.9, panel b). Without appropriate policy responses and aid, these small firms are likely to face significant operating constraints as their access to finance is relatively limited, and their employers might have to lay off employees or reduce working hours. Wage workers in the trade and hospitality sectors are also less likely to be given employee benefits such as social insurance and paid leave (figure II.9, panel c). Moreover, workers in the affected sectors generally have lower levels of education compared to others working in sectors characterized by greater formality, such as public administration, education, real estate, and finance. Workplace closures and business disruptions endanger their business continuity, and without job security, low-skilled and informal workers face a higher risk of losing their job and labor income sources.

Sources: NSO; World Bank staff estimates.
Note: Number of passengers includes both domestic and international travel.
Despite considerable negative impacts on employment in particular sectors, the pandemic has led to even more widespread reductions in labor income. Nearly 6 out of 10 households in Mongolia engaged in labor experienced a decrease in income from this source compared to the same period of previous year (figure II.10). Households with non-farm businesses were most likely to be affected, with almost 9 out of 10 participating households suffering reductions in income from this source. According to the Household Response Phone Survey (HRPS), by June 2020, more than 40 percent of households operating non-farm businesses pre-pandemic had temporarily or permanently closed their business, and closures continued into December 2020. Among businesses that were still operating over this period, income losses were significant, particularly during the second lockdown, in which more than half of non-farm businesses experienced a 60 percent loss or more in income compared to the same time in the previous year.

Although nonagricultural sectors have been more likely to experience employment shocks, disruptions in supply chains and contractions in external demand for livestock products have led to significant earnings losses among rural herders. Most herders and farmers continued to work in the initial months of the pandemic, with very few reporting that they stopped working from January to June. However, employment disruptions in agriculture have increased since then: By December 2020, a third of individuals who had been working in agriculture before the pandemic were no longer working. In addition, two out of three households engaged in agricultural activities experienced a significant decline in agricultural income in 2020 (figure II.10). Many herders depend on the harvest of cashmere, which is the most lucrative livestock product. However, contractions in the global demand for cashmere that have coincided with the peak season for harvesting cashmere has resulted in significant negative impacts on herders’ cash income. Negative income shocks to rural herders are particularly detrimental because income growth among this group was the biggest driver of the recent poverty reduction (between 2016 and 2018).
While poor workers were more likely to experience employment losses during the first half of 2020, both employment and income losses were felt similarly across the welfare distribution during the second lockdown. Although poor households are more likely to work in agriculture - which was less affected by the pandemic in terms of employment losses compared to other sectors - engagement in low-skilled jobs in the above-mentioned affected sectors, particularly manufacturing, utilities, mining, and personal services, is also high among poorer workers. Generally, about two in three workers in the bottom 20 percent of the welfare distribution are employed in low-skilled jobs. Workers at the top of the welfare distribution are more likely to have formal job protection or skilled jobs in services that may be more amenable to working from home such as professions in public administration, finance, and other professional jobs. Indeed, workers at the bottom of the welfare distribution, namely the bottom 20 percent, were significantly more likely to face job losses between January and June 2020, when mobility restrictions were still low and business closures were not mandated by the government (figure II.11, panel A). However, disruptions in employment were more widespread across the distribution between June and December 2020, particularly during the second lockdown, when most businesses were ordered to close.

Given high participation among the wealthy in retail trade and non-farm businesses, mandated closures had a significant impact on employment among the top quintiles in the latter half of 2020. While the wealthy may have been less vulnerable to job losses during the first half of 2020, income losses were generally felt across the welfare distribution throughout the year, and more than half of households in all welfare quintiles faced income losses in 2020 (figure II.11, panel B). Lower external and internal demand, business closures, and reduced work hours have resulted in lower wages and/or business profits throughout the distribution. The HRPS data indicate that, generally, the wealthy suffered greater percentage and absolute losses than poorer households, although the marginal effect per tugrug on well-being is likely to be higher for poorer households. This implies that the economic contraction in 2020 has so far had a widespread impact across the welfare distribution.

**Figure II.11. Employment and income losses across welfare distribution**

<table>
<thead>
<tr>
<th>Panel A. Stopped working due to COVID-19</th>
<th>Panel B. Income loss between Dec 2019 and Dec 2020</th>
</tr>
</thead>
<tbody>
<tr>
<td>Percent of workers</td>
<td>Percent of households with labor income</td>
</tr>
<tr>
<td>Q1 (poorest)</td>
<td>Q2</td>
</tr>
<tr>
<td>Jan - Jun 2020</td>
<td>Jun - Dec 2020</td>
</tr>
</tbody>
</table>

**Sources:** NSO; HRPS 2020 Rounds 1 and 3; World Bank staff estimates.

**Note:** The sample in panel A is restricted to respondents who were the same across rounds 1 and 3. Panel A uses those who stopped working due to COVID-19-related reasons such as workplace and school closures, quarantine, and stay-at-home orders under the government’s containment measures.

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63 Employment losses include temporary work disruptions under nationwide lockdowns due to COVID-19.

64 NSO and the World Bank 2020; World Bank 2018.
Geographically, urban households have been more likely to face the economic repercussions of COVID-19. Employment in the highly affected sectors is concentrated in urban areas: 82 percent of those working in these sectors live in urban areas, mainly Ulaanbaatar, which is significantly higher than the overall share (62 percent) among all workers. Those living in Ulaanbaatar or Aimag centers were at least 1.9 and 3.9 times more likely to stop working between January and December 2020 than those living in Soum centers and the countryside, respectively (figure II.12). In particular, poor workers residing in urban areas are more likely to be engaged in informal, part-time, and small businesses in the affected sectors and are thus exposed to a higher risk of job losses than their wealthier counterparts.

Also, under the COVID-19 pandemic, unemployed and inactive individuals face further difficulties in searching for a job, leading to a greater likelihood of sinking into deeper poverty. Even without the COVID-19 pandemic, poverty headcount rates for unemployed and economically inactive individuals were significantly higher compared to the employed or retiree population. The poor and near-poor, who have low levels of human capital, are less likely to be able to meet labor market needs and often face difficulties in finding a job. Being unemployed or economically inactive means no labor income, translating into lower consumption and a higher chance of staying in poverty. The COVID-19 pandemic can exacerbate the already devastating situation and high poverty rates for this segment of the population.

C. Impacts on Non-labor Income

Remittances are a critical income source for recipient households, but their inflows are expected to fall during the COVID-19 pandemic. According to the 2018 HSES, 18 percent of households received some sort of private remittance in the last 12 months prior to the survey. In Mongolia, most remittances are domestic transfers: only 2 percent of households received private transfers from abroad. By consumption levels, wealthier households are more likely to receive remittances, with 24 percent of households in the wealthiest quintile receiving remittances, while only about 14 percent of the bottom 40 percent of households receiving them (figure II.13). However, as shown in figure II.14, regardless of household welfare level, remittances are a critical income source for all remittance-receiving households, accounting for one-quarter to one-third of their total household income. The COVID-19 disruptions can significantly affect the employment status of migrant workers, and, thus, inflow of remittances. The impact might be long-lasting if businesses where migrant workers are engaged do not improve quickly. For the poor and vulnerable recipient households that heavily rely on remittances and have little savings or assets to buffer themselves, the remittance impacts will compound their existing vulnerabilities.
Other non-labor income, notably public transfers, represents an important share of household income for the poor. Although labor income accounts for more than 60 percent of household income for the poor, one-third of their income comes from social transfers such as child money, other social protection programs, and pensions. According to the HRPS (Round 3), only 3 percent of social assistance recipients have faced disruptions in receiving government assistance under the pandemic.

**D. Potential Impacts on Poverty**

This section assesses the potential impacts of the COVID-19 pandemic on the national poverty headcount rate by adapting a macro-micro simulation model. The ADePT macro-micro simulation combines macroeconomic projections and household welfare and profile from the latest household survey and then incorporates microsimulation assumptions related to the labor market, non-labor income, and price changes to project distributional and poverty effects of these assumptions. Table II.2 summarizes GDP and price projections for three scenarios: (i) pre-COVID case (business as usual), (ii) baseline case, and (iii) lower case. The baseline and lower-case scenarios also incorporate adverse remittance flow in the simulation, with assuming a 50 percent decline for two quarters in 2020 for the baseline scenario and a 50 percent decline for all quarters in 2020 for the lower-case scenario. The employment-output elasticities used as inputs into the simulation are calculated based on information of sectoral GDP growth and employment changes between 2010 and 2018, and the population growth forecasts are based on the latest UN World Population Prospects (2019).

The simulation results suggest that without mitigation measures there would be an increase of 5.9 to 7.9 percentage points in the national poverty rate in 2020, compared to the pre-COVID forecast. This is equivalent to adding approximately 195,000 to 260,000 people into poverty (figures II.15 and II.16). Even without the COVID-19 pandemic, the recent increasing food prices placed great stress on poorer households, slowing the speed of poverty reduction between 2019 and 2020 under the pre-COVID case. With deteriorating economic forecasts under the COVID-19 pandemic, the poverty rate would go up to 31.7 and 33.6 percent in the baseline and lower case, respectively, meaning that over 1 million people in Mongolia would be under the poverty line. The impacts of COVID-19 would last beyond the current pandemic and will not be easily recovered. With the projected slower-paced recovery, the baseline case simulation results suggest that poverty rate of 2022 would not go back to the level

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45 NSO and World Bank 2020.
46 The microsimulation model used in this report is outlined in Olivieri et al. (2014).
47 HSES 2018.
48 The poverty line in the simulation was adjusted by the difference in food and non-food inflation rates. Since the ratio of food consumption to total consumption in the poverty line is 51 percent, which is significantly higher than the ratio of food items in the CPI basket (26 percent), higher food price inflation relative to non-food inflation would shift the poverty line upward, pushing more people under the poverty line.
Table II.2. GDP growth and inflation assumptions\(^a\)

<table>
<thead>
<tr>
<th></th>
<th>2018</th>
<th>2019 F</th>
<th>2020 E</th>
<th>2021 E</th>
<th>2022 E</th>
</tr>
</thead>
<tbody>
<tr>
<td>(1) Pre-COVID Case (business as usual)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Agriculture</td>
<td>4.5%</td>
<td>4.5%</td>
<td>4.4%</td>
<td>4.4%</td>
<td>5.0%</td>
</tr>
<tr>
<td>Industry including mining</td>
<td>7.9%</td>
<td>3.4%</td>
<td>3.1%</td>
<td>5.6%</td>
<td>5.7%</td>
</tr>
<tr>
<td>Services</td>
<td>4.7%</td>
<td>6.8%</td>
<td>6.2%</td>
<td>6.2%</td>
<td>6.7%</td>
</tr>
<tr>
<td>Total</td>
<td>7.2%</td>
<td>5.8%</td>
<td>5.3%</td>
<td>5.6%</td>
<td>5.8%</td>
</tr>
<tr>
<td>(2) Baseline Case</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Agriculture</td>
<td>4.5%</td>
<td>8.4%</td>
<td>10.8%</td>
<td>5.0%</td>
<td>6.0%</td>
</tr>
<tr>
<td>Industry including mining</td>
<td>7.9%</td>
<td>3.1%</td>
<td>-11.0%</td>
<td>6.3%</td>
<td>5.4%</td>
</tr>
<tr>
<td>Services</td>
<td>4.7%</td>
<td>5.8%</td>
<td>-5.1%</td>
<td>2.9%</td>
<td>5.2%</td>
</tr>
<tr>
<td>Total</td>
<td>7.2%</td>
<td>5.2%</td>
<td>-5.2%</td>
<td>4.3%</td>
<td>5.4%</td>
</tr>
<tr>
<td>(3) Lower Case</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Agriculture</td>
<td>4.5%</td>
<td>8.4%</td>
<td>9.4%</td>
<td>4.0%</td>
<td>5.0%</td>
</tr>
<tr>
<td>Industry including mining</td>
<td>7.9%</td>
<td>3.1%</td>
<td>-12.2%</td>
<td>2.9%</td>
<td>3.9%</td>
</tr>
<tr>
<td>Services</td>
<td>4.7%</td>
<td>5.8%</td>
<td>-7.9%</td>
<td>1.6%</td>
<td>3.0%</td>
</tr>
<tr>
<td>Total</td>
<td>7.2%</td>
<td>5.2%</td>
<td>-7.1%</td>
<td>2.4%</td>
<td>3.5%</td>
</tr>
</tbody>
</table>

Inflation (YoY) for pre-COVID case

<table>
<thead>
<tr>
<th></th>
<th>2018</th>
<th>2019</th>
<th>2020 E</th>
<th>2021 E</th>
<th>2022 E</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total CPI</td>
<td>8.1%</td>
<td>5.2%</td>
<td>7.0%</td>
<td>8.0%</td>
<td>8.5%</td>
</tr>
<tr>
<td>Food CPI</td>
<td>9.1%</td>
<td>8.3%</td>
<td>11.0%</td>
<td>9.0%</td>
<td>8.6%</td>
</tr>
<tr>
<td>Non-Food CPI</td>
<td>7.8%</td>
<td>4.2%</td>
<td>5.6%</td>
<td>7.6%</td>
<td>8.5%</td>
</tr>
</tbody>
</table>

Inflation (YoY) for Baseline and lower cases

<table>
<thead>
<tr>
<th></th>
<th>2018</th>
<th>2019</th>
<th>2020 E</th>
<th>2021 E</th>
<th>2022 E</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total CPI</td>
<td>8.1%</td>
<td>5.2%</td>
<td>2.3%</td>
<td>5.0%</td>
<td>7.0%</td>
</tr>
<tr>
<td>Food CPI</td>
<td>9.1%</td>
<td>8.3%</td>
<td>8.5%</td>
<td>8.0%</td>
<td>8.2%</td>
</tr>
<tr>
<td>Non-Food CPI</td>
<td>7.8%</td>
<td>4.2%</td>
<td>0.1%</td>
<td>4.0%</td>
<td>6.6%</td>
</tr>
</tbody>
</table>

Note: a. The pre-COVID case was based on forecasts from the Mongolia Economic Update (as of January 2020), whose 2019 GDP was a forecast since the final 2019 GDP figure was not published at that time. Baseline and lower cases are the latest World Bank forecasts provided as of January 18, 2021.
of 2018, and nearly 1 million people would remain in poverty. Given the limited share of remittance-receiving households, the overall impacts of remittances are relatively limited. Without adverse impacts in remittances, the poverty rates are projected to increase by 5.5 to 6.4 percentage points in the baseline and lower-case scenarios, respectively.

The welfare impact on the poor, particularly among the “new poor,” would be significantly higher than that observed in the rest of the population. The COVID-19 economic impacts would affect households across all income classes, but the relative welfare impact, with the absence of effective mitigation policies, is highest among the poorest population group that would expect a consumption decline by 18 percent between 2018 and 2020 under the lower-case scenario (figure II.17). As a result, the depth and severity of poverty would worsen, with an increase of 3.4 percentage points in the poverty gap, and 1.9 percentage points in the poverty severity index. Among the poor population, notably the “new poor,” who became poor in 2020 due to the COVID-19 economic shocks, would be severely affected. Their welfare would decline significantly because they would be forced to decrease their per capita consumption by 27 to 31 percent from 2018 to 2020 in real terms (figure II.18).

Source: World Bank staff estimates (ADEPT simulation).
Note: Impacts of COVID-19-related mitigation responses by the government were not included in the poverty projection.

Source: World Bank staff estimates (ADEPT simulation).
Note: Impacts of COVID-19-related mitigation responses by the government were not included in the poverty projection.

Source: World Bank staff estimates (ADEPT simulation).
Note: Impacts of COVID-19-related mitigation responses by the government were not included in the poverty projection.
Urban households are more likely to be adversely affected than those in rural areas. While the simulated poverty rate for 2020 in the countryside remains at the same level from the pre-COVID to the lower-case scenario, it would significantly increase in other locations of the nation (figure II.19). In particular, poverty incidence in the Aimag centers would reach the highest levels, rising from 28 percent in the pre-COVID case to 38 percent in the lower-case scenario. Indeed, nearly three-quarters of the "new poor," who fell under the poverty line due to the COVID-19 shocks, are from either the capital city or Aimag centers (figure II.20). As a result, under the lower-case scenario, more than 200,000 people in urban areas would be newly added to the existing poor, while 74,000 people fell into poverty in rural areas.

Nearly two-thirds of “new poor” attributable to the COVID-19 shocks are from the services sectors. While the COVID-19 shocks have affected a wide range of economic activities, the intensity of the impacts was not the same across the sectors. Figure II.21 shows the distribution of the “new poor” and “already poor” who already live under the poverty line in the pre-COVID scenario by employment sectors. Before the COVID-19 outbreak, the share of the poor was relatively uniform across all sectors, but the projected economic contraction clearly pushes more service workers into poverty. In turn, as the limited aggregate impacts are projected in the agriculture sector under the COVID-19 scenarios, only 6 percent of the new poor in the baseline and lower-case scenario are linked to agriculture.

**Figure II.19. Poverty headcount by location**

<table>
<thead>
<tr>
<th>Year</th>
<th>Ulaanbaatar</th>
<th>Aimag center</th>
<th>Soum center</th>
<th>Countryside</th>
<th>National</th>
</tr>
</thead>
<tbody>
<tr>
<td>2018 Poverty headcount rate (%)</td>
<td>26</td>
<td>30</td>
<td>29</td>
<td>33</td>
<td></td>
</tr>
<tr>
<td>2020 pre covid</td>
<td>28</td>
<td>28</td>
<td>26</td>
<td>30</td>
<td></td>
</tr>
<tr>
<td>2020 base</td>
<td>30</td>
<td>33</td>
<td>29</td>
<td>32</td>
<td></td>
</tr>
<tr>
<td>2020 lower</td>
<td>30</td>
<td>35</td>
<td>38</td>
<td>30</td>
<td></td>
</tr>
</tbody>
</table>

Source: World Bank staff estimates (ADePT simulation).
Note: Impacts of COVID-19-related mitigation responses by the government were not included in the poverty projections.

**Figure II.20. Distribution of the poor by location**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Ulaanbaatar</td>
<td>41</td>
<td>22</td>
<td>19</td>
</tr>
<tr>
<td>Aimag center</td>
<td>49</td>
<td>25</td>
<td>19</td>
</tr>
<tr>
<td>Soum center</td>
<td>49</td>
<td>24</td>
<td>19</td>
</tr>
<tr>
<td>Countryside</td>
<td>18</td>
<td>7</td>
<td>7</td>
</tr>
</tbody>
</table>

Source: World Bank staff estimates (ADePT simulation).
Note: Impacts of COVID-19-related mitigation responses by the government were not included in the poverty projections.

**Figure II.21. Distribution of the poor by economic sector**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Agriculture</td>
<td>34</td>
<td>6</td>
<td>6</td>
</tr>
<tr>
<td>Industry</td>
<td>28</td>
<td>30</td>
<td>28</td>
</tr>
<tr>
<td>Services</td>
<td>38</td>
<td>64</td>
<td>66</td>
</tr>
</tbody>
</table>
E. Potential Mitigation Impacts of Policy Responses

There is an immediate need to increase the resilience of the poor (including “new poor”) and vulnerable households that are severely affected under the ongoing and prolonged shocks. The Government of Mongolia responded quickly and implemented a series of measures to mitigate negative welfare impacts under the COVID-19 pandemic, which include allowance increases in the Child Money Program, food stamps, and other employment and social welfare benefits (table II.3). In this section, using the microsimulation results, the potential mitigation impacts of these policy responses on household welfare will be examined.\(^{50}\)

The Child Money Program (CMP) is the largest social protection program and covers more than 90 percent of the poor in Mongolia.\(^{51}\) The CMP provides 20,000 tugrug per child (under age 18) per month and covers 80 percent of all children. As of 2018, about 92 percent of the poor population lives in households with CMP benefits (figure II.22). As less wealthy households tend to have more children, the poor are more likely to receive higher levels of CMP benefits compared to better-off households. The CMP accounts for 10 percent of household income for the bottom 20 percent of households (figure II.23).

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\(^{50}\) As of November 23, 2020. The monthly increased benefit amount for children in the Food Stamp Program decreased from MNT 16,000 to the original benefit amount of MNT 8,000 from November 1, 2020. While the extension of additional benefits for the adult Food Stamp Program was not announced, the program continued at least until the end of 2020. In addition to these social protection measures, the Government of Mongolia has implemented other COVID-19-related responses, including exemptions of social security contributions, utility payment, and personal income tax.

\(^{51}\) Due to the difficulties identifying “children (under age 18) in need for permanent care” in HSES, the response impact of “children for permanent care” is not examined in this analysis.

\(^{52}\) Based on household-level data (population weighted) from HSES 2018.
Table II.3. Government responses to COVID-19 (Social protection-related measures)

<table>
<thead>
<tr>
<th>Program</th>
<th>Eligibility criteria</th>
<th>Original benefit size (monthly, MNT)</th>
<th>Increased amount (MNT)</th>
<th>Time frame to apply</th>
<th>Number of beneficiaries</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 Child Money Program (CMP)</td>
<td>Children age 0–18</td>
<td>20,000</td>
<td>100,000</td>
<td>Apr 1, 2020–July 1, 2021</td>
<td>1,144,630</td>
</tr>
<tr>
<td>2 Social Welfare Pension (goes for the following groups):</td>
<td>(1) Seniors (not eligible for SI pension), F55+/M60+</td>
<td>188,000</td>
<td>288,000</td>
<td>May 1–Dec 31, 2020</td>
<td>3,140</td>
</tr>
<tr>
<td></td>
<td>(2) Dwarf individual age 16+</td>
<td>188,000</td>
<td>288,000</td>
<td>May 1–Dec 31, 2020</td>
<td>106</td>
</tr>
<tr>
<td></td>
<td>(3) Disabled persons age 16+</td>
<td>188,000</td>
<td>288,000</td>
<td>May 1–Dec 31, 2020</td>
<td>36,486</td>
</tr>
<tr>
<td></td>
<td>(4) Orphan children, under age 18</td>
<td>188,000</td>
<td>288,000</td>
<td>May 1–Dec 31, 2020</td>
<td>14,219</td>
</tr>
<tr>
<td></td>
<td>(5) Single parent w/4+ children under age 18</td>
<td>188,000</td>
<td>288,000</td>
<td>May 1–Dec 31, 2020</td>
<td>12</td>
</tr>
<tr>
<td>3 Children under age 16 in need for permanent care</td>
<td>Children under age 16 in need of permanent care</td>
<td>188,000</td>
<td>288,000</td>
<td>May 1–Dec 31, 2020</td>
<td>10,243</td>
</tr>
<tr>
<td>4 Food Stamp Program</td>
<td>(1) Poor HHs: Adults</td>
<td>16,000</td>
<td>32,000</td>
<td>May 1, 2020–Nov 1, 2020</td>
<td>118,748</td>
</tr>
<tr>
<td></td>
<td>(2) Poor HHs: Children</td>
<td>8,000</td>
<td>16,000</td>
<td>May 1–Nov 1, 2020</td>
<td>123,189</td>
</tr>
</tbody>
</table>


Additional CMP benefits provided by the government would mitigate the COVID-19 welfare loss for the poor. In response to COVID-19, the government expanded CMP’s monthly benefit level from 20,000 to 100,000 tugrug per child for 15 months from April 1, 2020 to July 1, 2021, which is equivalent to a cost of 3.0 percent of GDP. The additional CMP benefits would increase per capita consumption of the poorest population group by 30,000 tugrug on average, accounting for 36 to 38 percent of their average per capita consumption (figure II.24). The CMP compensation amount would completely mitigate welfare losses due to the COVID-19 shocks for the bottom 40 (figure II.25). In the lower-case scenario, for example, without effective mitigation measures, the poorest group's consumption would decline by nearly 20 percent from the pre-COVID consumption level, but with additional CMP benefits, their consumption is projected to expand by 11 percent. By contrast, additional CMP benefits are not sufficient to recover COVID-19 welfare losses for the top 50.

As a result, with the government’s mitigation measures, poverty is expected to fall below the pre-COVID level in both the baseline and lower-case scenarios. As shown in figure II.26, taking into account the additional CMP benefits, the 2020 simulated poverty rate for the baseline and lower-case scenarios would drop to 22.3 and 23.9 percent, respectively. While additional allowances on the social welfare pension and Food Stamp Program would have little effect on overall poverty given their limited coverage of the poor, those interventions to reach different vulnerable groups are critical. By combining these policy responses, the simulation results suggest that potential welfare loss among poor households would be eliminated and poverty rates return to below the pre-COVID level.

GDP is based on nominal 2019 figure (Source: NSO).
Figure II.24. CMP additional benefits as share of per capita consumption, 2020

![Bar chart showing % change from the uncompensated case for different poverty groups.](chart1)

**Source:** World Bank staff estimates (AdePT simulation).

**Note:** a. CMP recipients are based on information from the HSES 2018.

Figure II.25. Welfare changes with CMP additional benefits compared to pre-COVID case, 2020

![Bar chart showing % change from the 2020 pre-COVID case for different poverty groups.](chart2)

**Source:** World Bank staff estimates (AdePT simulation).

Figure II.26. Poverty headcount rates with and without policy responses, 2020

![Bar chart showing 2020 poverty rates (%) for different scenarios.](chart3)

**Source:** World Bank staff estimates (AdePT simulation);

**Note:** a. All beneficiary and pre-COVID allowance level information of each program is based on the HSES 2018.

CMP = Child Money Program; FSP = Food Stamp Program; SWP = Social Welfare Pension.
The HRPS results also suggested that COVID-19-related government assistance has generally been helpful in mitigating negative economic impacts of the pandemic for beneficiary households, particularly the poor. Among households receiving any type of government assistance, 35 percent expressed that the aid completely made up for the negative repercussions of the crisis, while another 57 percent said that it partially offset impacts (figure II.27). These numbers are largely driven by the ability of the CMP to partially or fully offset the negative income shocks that households have experienced since the crisis began. While most of both poor and non-poor CMP recipients expressed that the transfers were beneficial, poor recipients were 6 percent more likely to indicate that the aid completely or partially mitigated the effects of the crisis.

COVID-19-related disruptions have been ongoing and might have escalated since the government imposed the second lockdown measures in mid-November, and the actual impacts on household welfare need to be closely monitored. The estimated potential impacts on poverty in this report are based on the latest available macroeconomic forecasts, distributional and price assumptions. Once the macroeconomic forecasts and other model assumptions are revised, the microsimulation results need to be updated accordingly.

**Figure II.27. Perception of usefulness of government assistance**

<table>
<thead>
<tr>
<th>Any government assistance</th>
<th>35</th>
<th>57</th>
<th>6</th>
</tr>
</thead>
<tbody>
<tr>
<td>Child Money Program</td>
<td>37</td>
<td>56</td>
<td>34</td>
</tr>
<tr>
<td>Other Direct Cash Transfers</td>
<td>18</td>
<td>60</td>
<td>8</td>
</tr>
</tbody>
</table>

- Completely mitigated
- Partially mitigated
- Has not mitigated
- Not affected by COVID-19

*Source: World Bank staff estimates (HRPS Round 2).*
References


