



Report and Recommendation of the President to the Board of Directors

INTERNAL

Project Number: 56144-001
August 2022

Proposed Countercyclical Support Facility Loan Mongolia: Weathering Exogenous Shocks Program

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Asian Development Bank

CURRENCY EQUIVALENTS

(as of 5 July 2022)

Currency unit	–	togrog (MNT)
MNT1.00	=	\$0.00031875
\$1.00	=	MNT3,137.25

ABBREVIATIONS

ADB	–	Asian Development Bank
AIIB	–	Asian Infrastructure Investment Bank
BOM	–	Bank of Mongolia
CDEP	–	countercyclical development expenditure program
CMP	–	Child Money Program
COVID-19	–	coronavirus disease
CSF	–	countercyclical support facility
GDP	–	gross domestic product
IMF	–	International Monetary Fund
MOF	–	Ministry of Finance
MSMEs	–	micro, small, and medium-sized enterprises
MTA	–	Mongolian Tax Authority
OP	–	operational priority
PBL	–	policy-based loan
PRC	–	People's Republic of China
SIB	–	systemically important bank
SOE	–	state-owned enterprise
TA	–	technical assistance

NOTE

In this report, "\$" refers to United States dollars.

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PROGRAM AT A GLANCE

1. Basic Data		Project Number: 56144-001	
Project Name	Weathering Exogenous Shocks Program	Department/Division	EARD/EAPF
Country	Mongolia	Executing Agency	Ministry of Finance (formerly Ministry of Finance and Economy)
Borrower	Mongolia		
Country Economic Indicators	https://www.adb.org/Documents/LinkedDocs/?id=56144-001-CEI		
Portfolio at a Glance	https://www.adb.org/Documents/LinkedDocs/?id=56144-001-PortAtaGlance		
2. Sector		ADB Financing (\$ million)	
✓ Public sector management	Public expenditure and fiscal management		100.000
		Total	100.000
3. Operational Priorities		Climate Change Information	
✓ OP1: Addressing remaining poverty and reducing inequalities		GHG reductions (tons per annum)	0
✓ OP2: Accelerating progress in gender equality		Climate Change impact on the Project	Low
✓ OP6: Strengthening governance and institutional capacity			
		ADB Financing	
		Adaptation (\$ million)	0.000
		Mitigation (\$ million)	0.000
		Cofinancing	
		Adaptation (\$ million)	0.000
		Mitigation (\$ million)	0.000
Sustainable Development Goals		Gender Equity and Mainstreaming	
SDG 1.a		Effective gender mainstreaming (EGM)	✓
SDG 5.c			
SDG 10.4		Poverty Targeting	
SDG 17.1		General Intervention on Poverty	✓
4. Risk Categorization:	Complex		
5. Safeguard Categorization	Environment: C	Involuntary Resettlement: C	Indigenous Peoples: C
6. Financing			
Modality and Sources		Amount (\$ million)	
ADB		100.000	
Sovereign Countercyclical Support Facility Lending (Regular Loan): Ordinary capital resources		100.000	
Cofinancing		0.000	
None		0.000	
Counterpart		0.000	
None		0.000	
Total		100.000	
Currency of ADB Financing: US Dollar			

I. THE PROPOSAL

1. I submit for your approval the following report and recommendation on a proposed countercyclical support facility (CSF) loan to Mongolia for the Weathering Exogenous Shocks Program.

2. The invasion of Ukraine by the Russian Federation and the continued border restrictions with the People’s Republic of China (PRC) because of the coronavirus disease (COVID-19) pandemic are exerting significant pressure on the Mongolian economy. These issues have caused severe economic shocks and substantial fiscal stress. The Government of Mongolia has prepared a countercyclical development expenditure program (CDEP) to help poor and vulnerable groups, including women and girls; tame inflationary pressure; and support macroeconomic stabilization. The proposed CSF loan from the Asian Development Bank (ADB) will support government measures and financing needs to enable Mongolia to weather the adverse social and economic impacts, and targets poor and vulnerable groups, including women and girls.¹ The budget support provided through the CSF loan will also provide the necessary fiscal space to continue with the implementation of critical structural reforms over the medium-term.

3. The CSF is an appropriate instrument to respond to exogenous shocks with adverse implications where development financing needs have been created. The program is fully aligned with ADB’s Strategy 2030, namely operational priority (OP) 1: addressing remaining poverty and reducing inequalities, OP 2: accelerating progress in gender equality, and OP 6: strengthening governance and institutional capacity.² Mongolia satisfies the access criteria of ADB’s CSF (Table 1 and Appendix 4).

Table 1: Compliance with the Countercyclical Support Facility Access Criteria

Access Criteria		ADB Staff Assessment
1.	Adverse impact of exogenous shocks	The ongoing border restrictions with the PRC and the Russian invasion of Ukraine have resulted in severe economic shocks and fiscal stress. ADB’s economic growth forecast for 2022 has been considerably downgraded, from 6.0% in September 2021 to 0.6% in June 2022. GDP contracted over three consecutive quarters (Q3 2021–Q1 2022), exports fell by 11.0% in the first 4 months of 2022 and total revenues declined by 31.5% in April 2022 year-on-year. ADB estimates that government financing needs could rise by \$611 million in 2022, from 5.1% to 8.9% of GDP. Inflation reached 16.1% in June 2022, putting huge pressure on vulnerable groups.
2.	Countercyclical development expenditures	The government is implementing a CDEP facilitated through budget amendment to mitigate adverse economic and development impacts with a specific focus on poor and vulnerable groups, including women and girls. It features three broad areas: (i) temporary increase in cash transfers to households, (ii) targeted measures to cushion socioeconomic impacts on vulnerable groups, including women and girls and (iii) measures to counteract inflationary pressures, especially in relation to rising food prices.
3.	Pre-shock record of generally sound macroeconomic management	Annual GDP growth averaged 6.3% from 2017 to 2019, before contracting by 4.6% in 2020 and recovering to 1.4% in 2021. Mongolia reduced its debt-to-GDP ratio by more than 30 percentage points from 2016 to 2019 before it rose by 14 percentage points in 2020 due to COVID-19 and fell by more than 10 percentage points to 80.4% in 2021 before the onset of the exogenous shocks. Inflation remained below the target of 8% since 2017 but started to increase in 2021 due to COVID-19 related supply disruptions, prompting BOM to increase the policy rate by 4 percentage points to 10% in 2022. Despite this generally positive record of macroeconomic management, challenges remain including continued pressure on debt sustainability and the level of foreign exchange reserves, which have been put under pressure by the current economic situation. In addition, as

¹ The design and monitoring framework is in Appendix 1. The list of linked documents is in Appendix 2. The Development Policy Letter is in Appendix 3.

² ADB. 2018. [Strategy 2030: Achieving a Prosperous, Inclusive, Resilient, and Sustainable Asia and the Pacific](#). Manila. Accessed on 21 July 2022.

Access Criteria		ADB Staff Assessment
		highlighted by the IMF, fiscal support measures in response to COVID-19, while necessary and helped to contain poverty, were excessive and may create inflationary pressure. ^a
4.	Structural reforms	Despite the exogenous shocks induced difficulties, Mongolia is committed to maintaining reform momentum. The government is committed to strengthening debt and fiscal management, while gradually reducing its public debt in line with the Fiscal Stability Law. ^b The government is also undertaking measures to improve targeting and fiscal sustainability of social protection programs. In the finance sector, the government is implementing a comprehensive Banking Sector Medium-Term Strengthening Program and parliament amended the Banking Law in 2021 to improve the banks' capital base and promote good governance. Under a proposed ADB programmatic PBL, the government and ADB are targeting policy reforms in domestic resource mobilization, debt management, finance sector, and private sector development. ^c
5.	Debt sustainability	The government requested a \$100 million CSF loan from ADB and cofinancing of \$100 million from the Asian Infrastructure Investment Bank. Based on ADB's DSA, ^d the additional borrowing will not significantly affect debt sustainability or exacerbate any weaknesses in fiscal sustainability. The DSA builds on the IMF Article IV DSA (footnote a), which indicates that Mongolia's public debt is sustainable under the baseline scenario, but that Mongolia is at a high risk of debt distress. The government will continue the implementation, with support from development partners, of a medium-term debt management strategy to gradually reduce its debt-to-GDP ratio. In terms of foreign exchange reserve adequacy, the IMF's Article IV assessment indicates that reserves decreased, but remain at the lower end of recommended levels. Nevertheless, the IMF assessment letter indicates that external buffers have been eroded because of the recent economic challenges.
6.	IMF coordination	ADB has maintained close dialogue with the IMF in terms of economic analysis, reform support, and crisis response. The IMF provided an assessment letter to ADB for the CSF program in June 2022. ADB will continue to coordinate closely with the IMF and other development partners going forward.
7.	Monitoring and Evaluation	The government has agreed to establish a monitoring and reporting mechanism to report on the implementation of the countercyclical development expenditure program and the CSF. Quarterly reports will be prepared and will be complemented by qualitative analysis through consultations with beneficiary groups, including women and girls. These reports and analyses will form the basis of a strategic dialogue led by ADB's country director for Mongolia and the state secretary of the Ministry of Finance.

ADB = Asian Development Bank, BOM = Bank of Mongolia, COVID-19 = coronavirus disease, CSF = countercyclical support facility, DSA = debt sustainability analysis, GDP = gross domestic product, IMF = International Monetary Fund, PBL = policy-based loan, PRC = People's Republic of China, Q = quarter.

^a IMF. 2021. [Mongolia: Staff Report for the 2021 Article IV Consultation](#). Washington, DC.

^b Under the law, the structural budget deficit shall not exceed 2% of GDP.

^c The proposed programmatic PBL for Strengthening Economic, Fiscal, and Financial Resilience Programmatic Policy-Based Lending is scheduled for ADB Board of Directors consideration in November 2022.

^d Summary of Debt Sustainability Analysis (accessible from the list of linked documents in Appendix 2).

Sources: Asian Development Bank, International Monetary Fund, and the Ministry of Finance.

II. PROGRAM AND RATIONALE

A. Background and Development Constraints

4. **War in Ukraine.** The invasion of Ukraine by the Russian Federation is weighing on global economic recovery from the COVID-19 pandemic. The war, which began in late February 2022, has disrupted global economic conditions, sending shockwaves through financial and commodity markets, and exerted inflationary pressure on energy and food prices. This exogenous shock hit the Mongolian economy hard before key structural reforms had been fully implemented and at a time when the government continues to grapple with COVID-19 related challenges, including border restrictions with the PRC.

5. **Macroeconomic management.** Mongolia's record of macroeconomic management prior to the COVID-19 pandemic is generally sound. Gross domestic product (GDP) grew at annual

average rate of 6.3% from 2017 to 2019 before contracting by 4.6% in 2020 with the onset of the COVID-19 pandemic and recovering weakly to 1.4% in 2021. Mongolia reduced its debt-to-GDP ratio by more than 30 percentage points from 2016 to 2019, underlining its commitment to debt reduction. In 2020, weak growth and rising expenditure needs increased debt-to-GDP ratio by 14 percentage points before Mongolia again reduced debt-to-GDP by more than 10 percentage points in 2021 despite economic pressures. Inflation remained below target (8%) since 2017 but started to pick up in 2021 because of COVID-19 impacts, including border restrictions with the PRC, and climbed to 16.1% in June 2022. In response, the Bank of Mongolia (BOM) increased the policy rate by 4 percentage points to 10% as of June 2022. Exports hit a historic high of \$7.6 billion in 2019, foreign direct investment remained stable at \$2.1 billion, and the balance of payments recorded a surplus of \$0.5 billion, which increased gross foreign exchange reserves to \$4.4 billion (5.6 months of imports) in 2019. Therefore, despite Mongolia's dependency on commodity revenues and a tendency for procyclical policies, macroeconomic management since 2017 was largely effective in achieving economic growth and stability until the onset of the exogenous shocks: the COVID-19 pandemic and the Russian Federation's invasion of Ukraine.

6. **Exogenous shocks adversely impact economy.** GDP growth reached 6.3% in the first half of 2021 because of a strong recovery in mining and services, but Mongolia's economy contracted in the third and fourth quarters of 2021 due to trade disruptions resulting from COVID-19-related restrictions at the main trade portals with the PRC. On 14 February 2022, Mongolia lifted domestic COVID-19-related restrictions, underpinned by a successful vaccination campaign.³ Any resulting boost was short-lived, however, as the Russian Federation invaded Ukraine on 24 February 2022; this placed huge downward pressure on Mongolia's trade with the Russian Federation (which accounts for 29% of Mongolia's imports, including 97% of oil imports) as well as with Europe (13% of imports), as the Russian Federation also serves as an important transit country for Mongolia's traded goods. The border restrictions with the PRC (82.7% of Mongolia's exports and 37% of imports) continue to cause trade disruptions. The combination of these external shocks has prompted the robust 6% growth forecast for 2022 (made in September 2021)⁴ to be considerably downgraded as of June 2022 to a much more sobering 0.6%.⁵ A recent projection by the International Monetary Fund (IMF) forecasts 1% GDP growth for 2022, with risks tilted to the downside.⁶

7. **Rising fiscal deficit and declining fiscal space.** In April 2022, total revenues declined by 31.5% year-on-year, while tax revenues declined by 13.9%. Income tax revenues declined by 58.7% and corporate income tax revenues by 69.2% over the same period.⁷ In an adverse scenario under a deep GDP contraction of 0.8%, ADB estimates that budget financing needs could rise by \$611 million for 2022, from 5.1% to 8.9% of GDP.

8. **Current account, foreign exchange, and external financing stresses.** Mongolia is experiencing a widening current account deficit, increased pressure on foreign exchange reserves, and rising external financing needs. In the first 4 months of 2022, merchandise exports decreased by 11.0%, while imports increased by 23.8% year-on-year. This resulted in a significant deterioration of the merchandise trade balance and increased the current account deficit almost threefold to \$1.5 billion. As of May 2022, foreign exchange reserves have fallen by 28.4% to \$3.1 billion, or cover for 4.1 months of total imports, the lowest import cover since September 2018,

³ As of 18 May 2022, 66.9% of the total population was fully vaccinated (two shots) and 32.1% had at least one booster shot. Source: Ministry of Health.

⁴ ADB. 2021. *Asian Development Outlook Update: Transforming Agriculture in Asia*. Manila (September).

⁵ ADB. 2022. *Asian Development Outlook Supplement*. Manila (July).

⁶ International Monetary Fund. 2022. *Mongolia: Concluding Statement of 2022 IMF Staff Visit*. 12 May.

⁷ Source: Ministry of Finance.

and 1.6 months less than at the end of 2021. BOM forecasts a \$1.3 billion (8.6% of GDP) balance of payments gap as a baseline, which would put further pressure on reserves and the local currency. The latest estimates of the external financing gap under the adverse scenario are in the range of \$1.7 billion–\$1.8 billion for 2022. This external financing gap can be reduced if recent improvements in coal exports are sustained and the planned mobilization of up to \$690 million through pre-export financing is realized.⁸

9. **Increased pressure on the finance sector.** The finance sector is dominated by banks, which account for more than 90% of sector assets. The five systemically important banks (SIBs) currently meet BOM's prudential ratio and liquidity ratio requirements.⁹ Additional monetary tightening by BOM in line with global trends combined with domestic inflationary pressures could further tighten domestic financing conditions, including for micro, small, and medium-sized enterprises (MSMEs). Banks still face challenges associated with the COVID-19 pandemic, and higher interest rates and the phasing out of regulatory forbearance measures could trigger a rise in banks' nonperforming loan ratio, which was 8.9% as of May 2022 (while high, this is a decline from 11.1% in May 2021). Weakening of banks' balance sheets could undermine their capacity to extend credit to support economic recovery. The initial public offering of the SIBs by 30 June 2023 is expected to strengthen their capital adequacy and corporate governance through additional and more diversified shareholders.

10. **Inflation.** Rising food and fuel prices are eroding purchasing power and increasing poverty. Inflation spiked to 16.1% nationwide as of June 2022, and was particularly high for food and fuel. Persistent exchange rate depreciation pressure suggests a risk of further pass-through inflation affecting imported goods.¹⁰ Reduced purchasing power is particularly challenging for the 27.8% of people who live below the poverty line and spend an average of 43% of their total income on food compared with 32% spent on food by non-poor households. Estimates suggest that real incomes of the poorest 40% of households in Mongolia will fall by 5.6% in 2022, elevating concerns that in the absence of effective responses rising food prices will place the 15% of the population living just above the poverty line (totaling 500,000 people) in poverty.¹¹

11. **Impacts on the poor and vulnerable.** Exogenous shocks disproportionately affect poor and vulnerable groups, including women and girls. Women's labor force participation fell to 49.9% in 2021, 3.5 percentage points down from the pre-pandemic (2019) level of 53.4% (compared with a 3.1 percentage point decrease in men's labor force participation rate from 68.3% in 2019 to 65.2% in 2021). This decline resulted from job losses caused by the COVID-19 pandemic as well as increased unpaid care responsibilities because of school closures. Women are highly concentrated in lower wage sectors such as services, food production, and wholesale and retail trade, which are among the sectors most adversely affected by the pandemic because of mobility restrictions. In 2021, the national average wage for men was 19.5% higher than that for women.¹² Children comprise one-third of the population, and 42% of the poor in Mongolia are children under the age of 15. The government has used the Child Money Program (CMP), a universal child grant given to all people under 18 years old, as the primary mechanism to reach vulnerable families

⁸ As of June, \$200 million pre-export financing have been already mobilized through state-owned enterprises.

⁹ The five SIBs are Golomt Bank, Khan Bank, Khas Bank, State Bank, and Trade and Development Bank, which collectively hold over 93% of the country's banking assets.

¹⁰ The nominal exchange rate against United States dollar has depreciated by 9.9% from the beginning of 2022 through the end of June 2022.

¹¹ E. Artuc et al. 2022. [War-induced food price inflation imperils the poor](#). Vox.EU; National Statistics Office of Mongolia and World Bank. 2020. [Mongolia Poverty Update 2018: Main Report of the Household Socio-Economic Survey 2018](#). Ulaanbaatar and Washington, DC

¹² Mongolian Statistical Information Service. [Statistics: Labour Force Participation Rate](#) (accessed 19 May 2022).

during the COVID-19 pandemic. Mothers are the custodians of children's CMP accounts in 85.6% of households and can make spending decisions to support their families' needs. Mongolia's experience of both past crises and the COVID-19 pandemic confirms the high risk of adopting negative coping strategies—such as selling productive assets, reducing consumption levels, or reducing investments in education, health, and livelihoods—all of which can impact long-term well-being.¹³ As a result of the COVID-19 pandemic, 27% of households reported that their food consumption had declined, with households headed by women particularly affected.¹⁴

12. **Weathering exogenous shocks.** A sound approach to weathering exogenous shocks will support macroeconomic stability, protect vulnerable groups, and sustain momentum for reforms. Mongolia was on the road to recovery, bolstered by a groundbreaking agreement on what will soon be the world's fourth-largest copper mine,¹⁵ strong growth in the first half of 2021, and a positive credit rating assessment in May 2022.¹⁶ At the same time, Mongolia has continued undertaking critical structural reforms to promote economic stability. An effective policy response to exogenous shocks will help cushion adverse socioeconomic implications and create fiscal space to sustain reform momentum. This also underpins the complementarities between the proposed CSF and the proposed policy-based loan (PBL) for Mongolia.¹⁷

B. Countercyclical Expenditure Package, ADB's Value Addition, and Sustainability

13. **Countercyclical development expenditure program.** The state budget approved by the Parliament in November 2021 contained several critical measures designed to support poor and vulnerable groups and to mitigate the continued drag on economic growth caused by COVID-19-related border restrictions with the PRC. This response was enhanced to create additional fiscal space for pro-poor spending through two subsequent budget amendments in January and April 2022 reducing capital expenditure by 17.6% and operational expenses for all budgetary public institutions by 30% compared to the original budget, approved in November 2021. These also contained several targeted measures for vulnerable groups, including women and girls. The total size of the CDEP is \$860 million, equal to 6.2% of GDP. It covers three broad areas: (i) temporary increase in cash transfers to households, (ii) targeted measures to cushion socioeconomic impacts on vulnerable groups, including women and girls,¹⁸ and (iii) measures to counteract inflationary pressures and safeguard food security. Table 2 presents the expenditure items, and specific measures are detailed in section C.

¹³ ADB. 2018. *Strengthening Resilience Through Social Protection Programs: Guidance Note*. Manila.

¹⁴ United Nations Development Programme. 2020. *Rapid Socio-Economic Impact Assessment of COVID-19 Prevention Measures on Vulnerable Groups and Value Chains in Mongolia*. Ulaanbaatar.

¹⁵ The shareholders of the Oyu Tolgoi mine in the South Gobi (Rio Tinto, Turquoise Hill Resources and the Government of Mongolia) reached an agreement in January 2022 to proceed with underground operations paving the way for sustainable production in 2023. By 2030, Oyu Tolgoi is expected to be the fourth largest mine in the world. [Rio Tinto news release January 2022](#) (last accessed on 31 July 2022).

¹⁶ Fitch Ratings. 2022. *Fitch Affirms Mongolia at 'B'; Outlook Stable*. Rating Action Commentary (18 May).

¹⁷ The proposed programmatic PBL for Strengthening Economic, Fiscal, and Financial Resilience Programmatic Policy-Based Lending is currently under preparation.

¹⁸ According to clause 18.2 of the Law on Social Welfare, vulnerable groups consist of elderly people, disabled people, children at risk, victims of violence, citizens released from prison, alcohol and drug addicts, people with terminal illness, homeless people, migrants, single parents, and families with disabled children.

Table 2: Allocation of Countercyclical Development Expenditure Program

Item	Amount		
	MNT billion	\$ million	Share (%)
Countercyclical Development Expenditure Program 2022	2,685.0	860.0	100.0
A. Cash transfers to households	1,462.0	469.0	54.5
1. Extension of Child Money Program	1,462.0	469.0	54.5
B. Targeted measures for vulnerable groups	916.0	293.0	34.1
1. Increased pension payments	610.0	195.0	22.7
2. Social insurance reimbursements	172.0	55.0	6.4
3. Increased access to kindergartens	100.0	32.0	3.7
4. Increased salary for low wage earners	34.0	11.0	1.3
C. Measures to counteract inflationary pressures	307.0	98.0	11.5
1. Customs and excise duty exemptions on essential goods	137.0	44.0	5.1
2. Interest subsidy to small and medium-sized enterprises	110.0	35.0	4.1
3. Interest subsidy to agriculture sector	37.0	12.0	1.4
4. Support to supply of essential consumer goods	23.0	7.0	0.9

Sources: Budget documents of the Ministry of Finance.

14. **Support for poor and vulnerable groups.** As an additional measure, the BOM is providing lending to banks through repurchase operations for intermediate working capital loans with concessional interest rates to key sectors, including meat suppliers, flour producers, and fuel and gasoline importers. This will help mitigate inflationary pressures. In addition, BOM will issue loans and advance payments to gold producers through banks, increasing BOM reserves and easing economic pressures on gold producers. This is in addition to existing measures that BOM has already introduced to mitigate the impact of COVID-19 pandemic, including a continued deferral of consumer loan repayments until the end of 2022, and credit support programs for SMEs. Further, to curb rising inflationary pressure and protect the purchasing power of citizens, BOM raised the policy rate by 50 basis points to 6.5% in January 2022, and further to 9.0% in March 2022, and 10.0% in June 2022; this marked the first monetary tightening since November 2018. Additionally, BOM raised the reserve requirement ratio on local currency-denominated liabilities by 200 basis points to 8.0%.

15. **ADB's value addition.** ADB's value addition is manifested in four ways. First, as also demonstrated during the COVID-19 pandemic response, ADB has assisted the government with the preparation of a well-designed and targeted CDEP. Second, ADB has established strong credibility across a range of reform areas, notably including macroeconomic policy, fiscal and public financial management, banking sector reforms, and social protection.¹⁹ As a result, the emergency support provided under the CSF is well aligned with the need to maintain momentum on critical structural reforms related to domestic resource mobilization, debt management, banking sector governance and regulation, and the further rationalization of social welfare support.²⁰ Building on its sustained engagement, ADB is helping the government strengthen social protection systems through poverty targeting. Third, the government places high value on ADB's ability to mobilize resources quickly to support a countercyclical response to exogenous shocks with the availability of the CSF facility. ADB's early engagement with other donors has resulted in AIIB pursuing parallel cofinancing to the CSF. Finally, ADB will provide technical

¹⁹ ADB. 2017. [Social Welfare Support Program, Phase 2](#); ADB. 2018. [Strengthening Information and Communication Technology Systems for Efficient and Transparent Public Investment and Tax Administration Project](#); ADB. 2020. [Mongolia: Support for Effective Public Sector Management](#); ADB. 2020. [Mongolia: Strengthening Banking Sector Stability and Performance](#); ADB. [Support for Data Analytics in Mongolian \(Supported through the Domestic Resource Mobilization Trust Fund\)](#); ADB. 2021. [Regional: Supporting Capital Market Development and Reform in Developing Asia \(Phase 1\)](#); and ADB. 2021. [Mongolia: Strengthening Public Resource Management, Private Sector Development, and Finance Sector Performance](#).

²⁰ ADB. 2020. [Assessment of the Social Protection Response to COVID-19 in Mongolia](#). Consultant's report. Manila. This assessment found that CMP top-ups were pro-poor and contributed significantly to a reduction in inequality

assistance (TA) to the government to monitor the implementation of the CDEP and to undertake deeper analysis of the impact on women and girls through the analysis of sex-disaggregated data and the conduct of additional qualitative research, such as focused group discussions.²¹

16. **Lessons.** The program incorporates lessons from the COVID-19 pandemic response option in Mongolia,²² including (i) the imperative of providing timely and flexible budget support that does not undermine fiscal sustainability; (ii) using the operation as a platform to deepen the targeting of the government program for poor and vulnerable groups such as women and girls, (iii) the importance of working with the government to strengthen shock responsive social protection systems that can be efficiently expanded and utilized during a crisis, and (iv) providing TA support to strengthen institutional capacity and enhance monitoring of the CDEP, and using this to deepen the dialogue with the government on crisis response as well as medium-term reform priorities. Another important lesson is the need to continue structural reforms on fiscal, debt, finance sector, and economic diversification alongside CSF operations through PBLs and TAs to ensure reform momentum is not lost during the economic crisis.

17. **Debt sustainability.** Public debt, including the central bank's external liabilities, decreased by 10.8 percentage points to 80.4% of GDP in 2021. According to the government's draft medium-term fiscal framework, the government debt stock is expected to increase by 13.4% in 2022. Based on this estimate, public debt, including central bank's external liabilities, is expected to rise by 10.0 percentage points from 80.4% of GDP in 2021 to 90.4% in 2022, slightly lower than the 2020 level. The government is also implementing a medium-term debt management strategy to reduce its debt-to-GDP ratio and gradually shift from external to domestic borrowing. During its Article IV consultation in November 2021, the IMF considered Mongolia's public debt is sustainable under the baseline scenario, but that Mongolia is at a high risk of debt distress.²³ Mongolia's debt sustainability is most vulnerable to prolonged periods of low growth and also to significant exchange rate depreciation.

18. **Coordination with IMF and other development partners.** ADB has coordinated closely with the IMF, the World Bank, the United Nations, and other development partners. Since 2018, ADB has worked closely with the IMF on domestic resource mobilization and support for the Mongolian Tax Authority (MTA). ADB financed the MTA's Business Continuity Plan, which was developed with support from the IMF, allowing MTA staff to work from home during the COVID-19 pandemic. In addition, ADB's TA for the MTA is aligned with the IMF's assistance. ADB hosted the development partner debriefing after IMF's mission in April 2022. In addition, ADB has coordinated closely with the IMF on data and analysis, most specifically on the debt sustainability analysis. The IMF provided ADB with an assessment letter for this operation in June 2022. The government has asked ADB to seek cofinancing of \$100 million from the AIIB, which ADB facilitated and which AIIB is pursuing. In addition, the government has requested emergency financing from the World Bank and maintains a close dialogue with the IMF on possible support. While the focus of the program is to help the government respond to the current crisis rather than driving structural reforms, ADB is coordinating closely with the IMF and other development partners to ensure that progress on key structural reforms continues. Under the Shock Responsive Social Protection Project 2,²⁴ ADB will support the implementation of a new proxy means test methodology and update the Integrated Household Database. This will allow the

²¹ The TA resources will come from ADB. 2021. [Mongolia: Supporting Inclusive and Sustainable Development](#). Manila.

²² ADB. Forthcoming. Completion Report: COVID-19 Rapid Response Program in Mongolia. Manila.

²³ IMF. 2021. [Mongolia: 2021 Article IV Consultation-Press Release; Staff Report; and Statement by the Executive Director for Mongolia](#)

²⁴ ADB. 2020. [Mongolia: Shock-Responsive Social Protection Project](#) (accessed on 21 July 2022). Manila.; and ADB. 2021. [Mongolia: Second Shock-Responsive Social Protection Project](#) (accessed on 21 July 2022). Manila.

government to better identify poor and vulnerable households and make social protection more targeted and efficient in the future. Under a proposed PBL, and in close coordination with the IMF, ADB has included policy actions to (i) undertake an asset quality review of SIBs required to undergo an initial public offering, (ii) enhance the legal environment for nonperforming loan resolution, (iii) strengthen banking sector regulation and supervision, (iii) strengthen domestic resource mobilization through improved tax administration, (iv) improve Mongolia's debt management, and (v) promote private sector development. These align with the key medium-term structural reforms identified by the government and ADB.

C. Expected Outcome of the Reforms

19. The impact of the proposed CSF program will be inclusive and sustainable economic growth maintained, which aligns with Mongolia's Vision 2050.²⁵ The outcome will be resilience of the population, specifically the poor and vulnerable groups, to adverse socioeconomic shocks increased. The program will have three key outputs:

20. **Output 1: Measures for temporary increase in direct cash transfers to households implemented.** This output will provide social protection support to vulnerable households under the CDEP. The CDEP extends the increased allocation under the CMP of MNT100,000 per child per month until the end of 2022. This increase was originally planned to be phased out after 31 December 2021, but it has been extended until 31 December 2022. This measure will reach 1.2 million children (48.8% girls) in 64% of the country's households through direct transfers.²⁶

21. **Output 2: Measures to cushion adverse socioeconomic impacts on vulnerable groups, including women and girls, implemented.** The government has introduced three key measures to directly support the most vulnerable groups: (i) 300,000 employees (56% women) earning a monthly salary of less than MNT1 million will receive a 50% reimbursement of their social insurance premium contributions for 2022; (ii) 107,000 lowest earning public service employees, 75% of whom are women, will receive an average salary increase of 8.5% because of the clear benefit to women and other vulnerable groups (these targeted measures will enhance their crisis resilience); and (iii) about 16,000 new kindergarten spaces for young children in poor areas will be made available for the school year starting in September 2022. In addition to clear early childhood development benefits, increased access to kindergarten for young children will reduce women's unpaid childcare burden and time poverty, thus increasing opportunities for women to participate in the labor force.²⁷

22. **Output 3: Measures to counteract inflationary pressures and safeguard food security implemented.** The government has introduced several measures to help vulnerable groups manage the impacts of high inflation. These include funding to provide interest rate subsidies to MSMEs and concessional loans in the agriculture sector to ease financing conditions

²⁵ Government of Mongolia, State Great Khural. 2020. *Mongolia's Vision-2050*. Ulaanbaatar.

²⁶ The CMP is a universal child grant that is pro-poor and reduces inequality. In Mongolia, 42% of the total poor are children and families from the poorest quintile in the income distribution, which have 5.1 children on average, compared to 2.6 in the highest quintile (footnote 19). Hence, increasing child grants is an effective way of reaching poorer households. ADB simulations of the child money top-ups suggest that they are effective at reducing poverty, showing that the top-ups alone could reduce poverty to 24.7% compared with 36.7% in a scenario with no social protection response to the COVID-19 pandemic.

²⁷ ADB research also shows that increasing female labor force participation would also significantly increase economic growth in Mongolia. ADB. 2020. [Boosting Mongolia's Long-Term Economic Growth through More Equal Labor Force Participation between Men and Women](#). Manila.

for these enterprises.²⁸ Measures also support the domestic production of essential food products, thereby reducing reliance on imported food products that are subject to high inflationary pressure. In addition, the government will provide support in the form of exemptions from customs' duties on essential food products (i.e., rice, vegetable oil, and sugar). Along with easing inflation pressures, these measures are critical to safeguard food security and avoid worsening poverty, particularly as poor households spend a much larger share of their disposable income on food than non-poor households (para. 10).

D. Development Financing Needs and Budget Support

23. The exogenous shocks affecting Mongolia are generating deep adverse impacts on the government budget and increasing domestic financing needs (Table 3). Using an alternative baseline scenario that assumes GDP growth of 1% for 2022, the structural fiscal deficit is expected to rise by \$337 million (from 5.1% of GDP to 7.6% of GDP) compared to the baseline under the budget amendment ratified by Parliament in April 2022. Under an adverse scenario of GDP contracting by 0.8%, gross revenues are estimated to fall by 12.2% compared to the baseline scenario. The combined impacts of exogenous shocks would cause the structural fiscal deficit to rise by \$611 million, equivalent to 8.9% of GDP. To meet these financing needs, the government has reduced expenditures (para. 13). The government also plans local currency bond issuances, withdrawals from the fiscal stabilization fund, and is seeking \$300 million in financing from international financial institutions, including ADB.

Table 3: Budget Forecasts and Domestic Financing Needs^a

Item	2021		2022							
			Original (approved in November 2021)		Baseline (amended in April 2022)		Alternative Baseline ^b		Adverse Scenario ^c (based on ADB analysis)	
	\$ million	% GDP	\$ million	% GDP	\$ million	% GDP	\$ million	% GDP	\$ million	% GDP
Gross revenues	5,003	33.1	5,265	35.1	5,221	34.9	4,860	33.4	4,583	29.5
(i) Structural revenues	4,454	29.5	5,058	33.7	4,980	33.3	4,643	31.9	4,369	28.1
(ii) Total expenditure	5,474	36.3	5,824	38.8	5,745	38.4	5,745	39.5	5,745	37.0
Structural balance (i-ii)	(1,020)	(6.8)	(766)	(5.1)	(765)	(5.1)	(1,102)	(7.6)	(1,376)	(8.9)
Financing need	1,020	6.8	766	5.1	765	5.1	1,102	7.6	1,376	8.9

() = negative, ADB = Asian Development Bank, GDP = gross domestic product.

^a 2022 budget items were converted to United States dollars, using the spot exchange rate of \$1 = MNT3,118 as of 19 May 2022.

^b The alternative baseline scenario is based on GDP growth of 1% but assumes that total expenditures would remain unadjusted from the recent amendment in April 2022.

^c The adverse scenario is based on further deterioration with respect to both (i) the border restrictions with the People's Republic of China, and (ii) the Russian Federation–Ukraine war; this could increase the balance of payments and fiscal deficits and reduce GDP growth by more than 3.0 percentage points from the current baseline estimate of 2.3% in 2022, resulting in a 0.8% GDP contraction. This scenario also assumes that total expenditure would remain unchanged from the recent amendment. ADB. 2022. *Mongolia Quarterly Economic Insight #8*. Manila. Source: Asian Development Bank and Ministry of Finance estimates.

24. The government has requested a regular loan of \$100 million from ADB's ordinary capital resources to help finance the program. The loan will have a 7-year term, including a grace period of 3 years; an interest rate determined in accordance with ADB's Flexible Loan Product plus 75 basis points; a commitment charge of 0.15% per year; and such other terms and conditions set forth in the draft loan agreement. Based on the straight-line method, the average maturity is 5.25 years, and there is no maturity premium payable to ADB.

²⁸ Under these measures a total of MNT930 billion in concessional loans to MSMEs will be provided. The MSMEs will pay an interest rate of 3% with the remaining amount subsidized by the government.

E. Implementation Arrangements

25. The Ministry of Finance (MOF) will be the executing agency for the program. The proceeds of the loan will be withdrawn in accordance with ADB's *Loan Disbursement Handbook* (2017, as amended from time to time). As the CDEP is part of the government budget, it will be subject to audit by the National Audit Office. This audit will be finalized and shared with ADB in June 2023 for monitoring purposes. The loan will be withdrawn as a single tranche. The implementation period is 1 September 2022–30 June 2023.

26. **Monitoring, evaluation, and ongoing policy dialogue.** A monitoring and reporting mechanism is being established for the program to provide a platform for stakeholder consultations and to enable a strategic dialogue with the government on the implementation of the CDEP and the CSF.²⁹ MOF and ADB will establish a high-level policy dialogue group, chaired by the state secretary of MOF and the ADB country director with representation from the Ministry of Economy and Development, the Ministry of Labor and Social Protection, the Mongolian Tax Authority, the Ministry of Food, Agriculture and Light Industry, and BOM. In addition, other relevant ADB departments and offices will join and provide technical support to these dialogues. These will include staff from ADB's Public Management, Financial Sector, and Regional Cooperation Division in the East Asia Department; the Governance Thematic Group of the Sustainable Development and Climate Change Department; and/or the Economic Research and Regional Cooperation Department. The policy dialogue group will meet quarterly and discuss the delivery of CDEP measures, review the design and monitoring framework targets in the CSF, and progress on key structural reforms. ADB and the government may also invite representatives of development partners and other key stakeholders to participate in the policy dialogue. The policy dialogue group will be supported by a technical group that will gather and collate data and prepare assessments regarding the delivery of selected CDEP measures, the CSF and structural reforms. Several of the initiatives under the CDEP use existing government mechanisms, such as the CMP and the tax administration system. These mechanisms are subject to their own monitoring arrangements, which will be used to assess the effectiveness of the CDEP and the CSF. The monitoring and evaluation dialogue contributes to strengthening Mongolia's governance and institutional capacity and is therefore aligned with ADB's OP 6. MOF has also requested that ADB help strengthen monitoring of the CDEP, including sex-disaggregated data monitoring. ADB will provide additional analysis and administrative support under an existing TA.³⁰

III. DUE DILIGENCE

27. **Safeguards.** Following an assessment of the outputs, the program will not have any likely environmental or social safeguard issues, and therefore is assigned category C for environment, involuntary resettlement, and indigenous peoples.

28. **Governance.** Mongolia has strong financial management legislation (the Integrated Budget Law and the Law on Development Planning), governance structures, and operational public financial management systems in place, including a functional treasury single account, a unified and consistent chart of accounts, and an integrated government debt and financial management information system. Nevertheless, there are areas in which improvements can be made related to the efficiency, effectiveness, and transparency of the public financial management system.³¹ ADB's Anticorruption Policy (1998, as amended to date) was explained

²⁹ Overview of Monitoring and Reporting Mechanism (accessible from the list of linked documents in Appendix 2).

³⁰ ADB. 2021. Technical assistance to [Mongolia for Supporting Inclusive and Sustainable Development](#). Manila.

³¹ World Bank. 2018. [Public Expenditure Review. Growing Without Undue Borrowing](#). Washington, DC.

to and discussed with the government. Major risks and mitigating measures are summarized in Table 4 and described in detail in the risk assessment and risk management plan.³²

Table 4: Summary of Risks and Mitigating Measures

Risks	Mitigation Measures
Prolonged duration of crises	
Extension of the current crises heighten their socioeconomic impact, requiring a more significant response that exceeds the government's capacity.	Regular dialogue with authorities through the monitoring and reporting mechanism under this program will allow the Asian Development Bank (ADB) to identify emerging challenges early and respond. ^a ADB is closely coordinating with other development partners.
Public financial management	
The social protection program lacks precise targeting, reducing the efficiency of public expenditure in reducing poverty.	ADB is implementing an ongoing social protection project (footnote 24). Under this project, ADB is supporting the government to implement an updated proxy means test methodology. This methodology will be used to better identify poor households, allowing the government to improve the targeting of its social protection programs.
Vulnerability to corruption	
Vulnerability to corruption undermines accountability throughout the economic and political sphere.	ADB is supporting the strengthening of institutions that are vital for Mongolia's integrity system, such as the Mongolian National Audit Office, and citizens' participation in monitoring budget-financed activities. ADB is facilitating an active role for Mongolia in international anticorruption initiatives and Mongolia's participation in the Extractives Industries Transparency Initiative. ^b ADB also includes Mongolia in its ADB-wide anti-corruption initiatives including anticorruption and integrity seminars, knowledge capacity building, and training on ADB's anticorruption policies.

^a Overview of Monitoring and Reporting Mechanism (accessible from the list of linked documents in Appendix 2).

^b ADB. 2019. *Mongolia: Strengthening the Supreme Audit Function*. Manila; ADB. 2014. *Transparency and Efficiency in Public Financial Management (Financed by the Japan Fund for Poverty Reduction)*. Manila. Mongolia is also an active member of the Anticorruption Initiative for Asia and the Pacific, which is supported by ADB and the Organisation for Economic Co-operation and Development (OECD. [Anti-corruption Initiative for Asia Pacific](#)).

Source: Asian Development Bank.

29. Social and poverty impact. Despite favorable pre-pandemic growth and the government's efforts to contain poverty during COVID-19, 27.8% of the population lived below the poverty line in 2020. Children remain among the most vulnerable (42% of the poor are children under the age of 15). Because of the COVID-19 pandemic, as of the first quarter of 2022, labor force participation stood at 58% (66.6% for males and 50.4% for females), below the pre-pandemic (2019) level of 60.5%. One in five employed people are poor, and 39% of employees engaged in elementary occupations³³ are the working poor (footnote 10). Poverty is becoming more concentrated in urban areas, while a reduction in poverty in rural areas is attributable to increased demand for livestock and price increases. Urban poverty has been persistent and concerning as it is the only impoverishment indicator showing an overall increase since 2010. One in four people in Ulaanbaatar live below the poverty line. Urban poverty is fueled by difficult conditions in urban *ger* (traditional yurt) areas, urban migration brought on by harsh weather conditions, and the loss of livelihoods in the countryside. In addition, the 14.9% of people living just above the poverty line are highly vulnerable to shocks and risk falling below the poverty line. The program aims increase the resilience of the population, specifically the poor and vulnerable groups, to adverse socioeconomic shocks and is therefore aligned with ADB's OP 1: addressing remaining poverty and reducing inequalities.

³² Risk Assessment and Risk Management Plan (accessible from the list of linked documents in Appendix 2).

³³ Elementary occupations consist of simple and routine tasks which mainly require the use of hand-held tools and often some physical effort. [International Standard Classification of Occupations](#). International Labor Organization. Last accessed on 21 July 2022.

30. **Gender.** The program is categorized as *effective gender mainstreaming*.³⁴ Gender-based inequalities were amplified during COVID-19 because of the increased burden of women's unpaid care work and women's predominant role in the health sector and in micro and family-owned businesses, which were badly affected by the pandemic. Public kindergartens in Ulaanbaatar select students by lottery, leaving those who are not selected with the option of either paying for a private kindergarten or staying at home. Therefore, children from vulnerable households stay home with their mothers, which reduces women's opportunity for employment and increases unpaid care burdens. Women are often highly concentrated in lower-earning sectors and one in five employed women are among the working poor.³⁵ In 2021, women accounted for 62.6% of all public servants and 75.9% of public support service employees, whose average salary is 27.1% lower than the national average salary. Further, there is no accepted definition for enterprises owned by women, which results in a lack of sex-disaggregated data on businesses. The program's social protection measures will mitigate economic shocks, increase food security, and address women's needs, including through financial inclusion. This is aligned with ADB's OP 2: accelerating progress in gender equality. Direct gender benefits of the program include (i) wage increases for women in low-earning public support service roles; (ii) enhanced access to early childhood education, including for girls and children with disabilities; (iii) reduced unpaid childcare responsibilities and reduced time poverty for women, freeing up time to pursue work outside the home; and (iv) universal cash transfers for children, with mothers as custodians of children's accounts in 85.6% of households.

IV. ASSURANCES

31. The government has assured ADB that implementation of the program shall conform to all applicable ADB policies, including those concerning anticorruption measures, safeguards, gender, procurement, consulting services, and disbursement, as described in detail in the draft loan agreement.

V. RECOMMENDATION

32. I am satisfied that the proposed countercyclical support facility loan would comply with the Articles of Agreement of the Asian Development Bank (ADB) and recommend that the Board approve the loan of \$100,000,000 to Mongolia for the Weathering Exogenous Shocks Program, from ADB's ordinary capital resources, in regular terms, with interest to be determined in accordance with ADB's Flexible Loan Product plus 75 basis points; for a term of 7 years, including a grace period of 3 years; and such other terms and conditions as are substantially in accordance with those set forth in the draft loan agreement presented to the Board.

Masatsugu Asakawa
President

04 August 2022

³⁴ ADB. 2021. [Guidelines for Gender Mainstreaming Categories of ADB Projects](#). Manila.

³⁵ National Statistics Office. 2020. [Income and Consumption Inequality](#). Ulaanbaatar.

VI. DESIGN AND MONITORING FRAMEWORK

Impact the Program is aligned with Inclusive and sustainable economic growth maintained (Mongolia's Vision 2050) ^a			
Results Chain	Performance Indicators with Targets and Baselines	Data Sources and Reporting Mechanisms	Risks and Critical Assumptions
<p>Outcome</p> <p>Resilience of the population, specifically the poor and vulnerable groups, to adverse socioeconomic shocks increased</p>	<p>By 31 December 2022:</p> <p>a. 480,000 vulnerable households currently benefiting from CMP have benefits extended (2021 baseline: 480,000^b) (OP1.1)</p> <p>b. At least 423,000 vulnerable people (of whom 59% are women or girls) benefit from tailored social assistance provided under CDEP in response to adverse socioeconomic shocks (2021 baseline: No tailored social assistance) (OP 1.1)</p> <p>c. At least 1,500 MSMEs in the agriculture sector benefit from concessional loans in response to adverse socioeconomic shocks (2021 baseline: 995 MSMEs benefited under a similar scheme)</p>	<p>a. MOF and MLSP reports on total sex-disaggregated number of monthly children and payments from January to December 2022</p> <p>b. MLSP, MES, and MED reports on program recipients, including sex-disaggregated data</p> <p>3a. MOFALI reports, including the MSMEs that received agricultural loan interest subsidies from May to December 2022</p>	<p>R: Changes in budget priorities may cause budget revenue shortfalls</p> <p>R: Domestic security and international COVID-19 situation prolonged or deteriorates</p> <p>R: Crisis-induced finance sector instability</p>
<p>Outputs</p> <p>1. Measures for temporary increase in direct cash transfers to households implemented</p>	<p>1a. By 31 December 2022, government will have provided MNT100,000 per month and per child for at least 1.2 million children (of whom 49% are girls) under the government extended CMP (sex-disaggregated) (2021 baseline: 1,220,158, 49% of whom [595,937] were girls^b) (OP1.1, OP 1.1.3, OP 2.5.4)</p>	<p>1a. Monitoring of CMP, including through audit of 2022 budget</p>	

Results Chain	Performance Indicators with Targets and Baselines	Data Sources and Reporting Mechanisms	Risks and Critical Assumptions
<p>2. Measures to cushion adverse socioeconomic impacts on vulnerable groups, including women and girls, implemented</p>	<p>2a. By 31 December 2022, the government will have provided at least 300,000 employees (56% women) who have monthly salaries of less than MNT1 million, with a reimbursement of 50% of their social insurance premium contribution (2021 baseline: No reimbursements were given) (OP 1.1, OP 1.1.3, OP 2.5.4)^c</p> <p>2b. By 31 December 2022, government will have provided an average 8.5% salary increase to 107,000 public service employees, of whom at least 75% are women (2021 baseline: No salary increase) (OP 1.1, OP 1.1.3, OP 2.5.4)^d</p> <p>2c. By 31 December 2022, through subsidies, the enrolment rate in early childhood education increased to 85%, or 16,000 additional children, of whom 49% are girls (academic year 2021-2022 baseline: 76% or 190,991 children enrolled of whom 49% are girls) (OP 1.1, OP 1.1.3, OP 2.5.4)</p>	<p>2a. MLSP report including the total sex-disaggregated number of monthly exempted insured employees and total amount from May to December 2022</p> <p>2b. MLSP report including the total sex-disaggregated number of public support service employees and total amount from May to December 2022</p> <p>2c. MES report including the total number of sex-disaggregated additional monthly children that had access to kindergartens from this measure and monthly cost from May to December 2022</p>	
<p>3. Measures to counteract inflationary pressures and safeguard food security implemented</p>	<p>3a. Government's commitment to providing up to MNT930 billion in concessional loans to agriculture sector MSMEs to promote domestic production of essential goods and prevent price increases of key commodities achieved, of which 50% (or MNT465 billion) will be disbursed by 31 December 2022 (2021 baseline: Concessional loan amount of MNT266 billion)</p>	<p>3a. MOFALI reports on total amount of MSME loan subsidies from May to December 2022</p>	

Results Chain	Performance Indicators with Targets and Baselines	Data Sources and Reporting Mechanisms	Risks and Critical Assumptions
	<p>under a similar scheme) (OP 1.3.3, OP 6.1.2)^e</p> <p>3b. By 31 December 2022, custom's duty exemption on 150,000 tons of essential food products with a value of MNT300 billion in place (2021 baseline: No exemption) (OP 1.3.3, OP 6.1.2)^f</p>	<p>3b. MTA and MOF reports on monthly custom's duty exemptions on essential food products and key commodities including the number of monthly importers, name of products and commodities, with total amounts expressed in tons and United States dollars, from May to December 2022</p>	
<p>Key Activities with Milestones Not applicable</p> <p>Inputs Asian Development Bank: \$100,000,000 ordinary capital resources loan</p>			

CDEP = countercyclical development expenditure program; CMP = Child Money Program; COVID-19 = coronavirus disease; MED = Ministry of Economy Development; MES = Ministry of Education and Science; MOF = Ministry of Finance; MOFALI = Ministry of Food, Agriculture and Light Industry; MLSP = Ministry of Labor and Social Protection; MTA = Mongolian Tax Authority; MSMEs = micro, small, and medium-sized enterprises; OP = operational priority.

^a Government of Mongolia. State Great Khural. 2020. *Mongolia's Vision-2050*. Ulaanbaatar.

^b Government provided MNT100,000 per child in 2021, and intended to stop these payments on 31 December 2021. According to clause 18.2 of the Law on Social Welfare, vulnerable groups consist of the elderly, persons with disabilities, children at risk, victims of violence, citizens released from prison, alcohol and drug addicts, people with terminal illness, homeless people, migrants, single parents, and families with children with disabilities.

^c 648,429 employees have a monthly salary of less than MNT1 million and are eligible for this exemption.

^d Among public service employees, some are responsible for delivering quality, accessible, and equitable public services and facilitating normal operations of public institutions.

^e These measures correspond to government resolutions 117 (approved on 16 March 2022), 174 (approved on 27 April 2022), and 175 (approved on 27 April 2022). Eligible MSMEs include agricultural businesses involved in domestic food production (e.g., meat, flour, sugar, vegetable oil, milk, potatoes, fruit, and vegetables), cashmere, wool, and leather. MSMEs engaged in food packaging and food processing, food chain stores, and imports of essential food products are also covered. The government used a similar subsidy scheme in 2021 to support MSMEs that were suffering under the COVID-19-related downturn. In total, 995 MSMEs received a total of MNT266 billion in lending under the scheme in 2021. As the 2021 scheme was not designed to reduce inflationary pressures, these numbers have not been considered as a baseline.

^f Customs exemptions cover 49 tons of rice, 34 tons of vegetable oil, and 69 tons of sugar with a total value of MNT316 billion and a customs exemption amount of MNT7.8 billion.

Contribution to Strategy 2030 Operational Priorities

Expected values and methodological details for all OP indicators to which this operation will contribute results are detailed in Contribution to Strategy 2030 Operational Priorities (accessible from the list of linked documents in Appendix 2).

Source: Asian Development Bank.

LIST OF LINKED DOCUMENTS

<http://www.adb.org/Documents/RRPs/?id=56144-001-3>

1. Loan Agreement
2. Sector Assessment (Summary): Public Sector Management
3. Contribution to Strategy 2030 Operational Priorities
4. Development Coordination
5. International Monetary Fund Assessment Letter
6. Summary Poverty Reduction and Social Strategy
7. Program Economic Assessment
8. Risk Assessment and Risk Management Plan
9. List of Ineligible Items

Supplementary Documents

10. Gender Monitoring Matrix
11. Safeguards Assessment Matrix
12. Overview of Monitoring and Reporting Mechanism
13. Summary of Debt Sustainability Analysis
14. Country Economic Indicators

DEVELOPMENT POLICY LETTER**MINISTER OF FINANCE OF MONGOLIA**

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Masatsugu Asakawa President
Asian Development Bank Mongolia:
Countercyclical Support Facility
Development Policy Letter

Date 23 June 2022
Ref. 01/4444

Dear President Asakawa,

I would like to express my sincere gratitude to the Asian Development Bank (ADB) for the effective and prompt support to Mongolia in a time of need. The Government of Mongolia acknowledges ADB's commitment towards supporting its developing member countries to counter the economic and social impacts during difficult times.

The Government would like to reiterate its request for additional \$100 million through ADB's Countercyclical Support Facility (CSF); the Government also recognizes ADB's leadership in mobilizing an additional \$100 million from Asian Investment Infrastructure Bank. This is in addition to the planned \$100 million in policy-based lending for Mongolia in 2022.

The ADB fielded a fact-finding mission to Ulaanbaatar, Mongolia, on 12 May - 19 May, 2022 for the proposed the Countercyclical Support Facility (CSF) loan for Mongolia. The purpose of the proposed consultation mission was to meet officials from the Ministry of Finance (MoF) and other relevant institutions, such as the Bank of Mongolia, and the Ministry of Economy and Development. We discussed in detail the challenging economic situation Mongolia is facing and measures we are taking to cushion development impacts through our countercyclical development expenditure program. As will be elaborated below, Mongolia meets the seven CSF access criterias.

Adverse impact of exogenous shocks. The exogenous shocks created by the ongoing border restrictions with the People's Republic of China (PRC) due to the COVID-19 and the current situation in Ukraine, has made Mongolia one of the most severely affected economies in the world. In the Medium Term Fiscal framework of 2022, MOF's forecast for Mongolian economy's GDP growth in 2022 and 2023 is 2.8 percent and 4.5 percent, respectively. This is a severe downgrade compared with the previous projections of 4.6 percent and 6.3 percent in 2022 and 2023 in Fiscal framework of 2021 before the occurrence of the exogenous shocks. We estimate that in an adverse downside scenario, Mongolia's economic growth could fall to as low as 0.7 percent this year due to continued border restrictions and the ongoing military conflict in Europe.

International financial organizations have considerably lowered Mongolia's economic growth forecast for 2022, too. As of April 2022, ADB's Asian Development Outlook 2022 projects Mongolia's economic growth to expand by 2.3 percent in 2022 compared to the 6.0 percent forecast in its Asian Development Outlook Update 2021, published in September 2021. In the same vein, the World Bank has lowered Mongolia's economic growth forecast for 2022 to 2.5 percent from a 5.2 percent forecast in October 2021. Growth forecasts by international financial institutions were even much lower for adverse case scenarios. As of

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May 2022, the IMF also lowered the Mongolia's economic growth forecast for 2022 to 1 percent as a baseline. In approved budget of 2022, budget revenue is MNT 15.8 trillion but currently expected to decrease by 1.6 percent due to above-mentioned exogenous shocks. If the current conditions keep remaining we expect that budget revenue would decline, widening the fiscal deficit further.

The forecast reflects the impact of the challenging situation in Ukraine—chiefly manifested through higher prices of imported food, fuel and fertilizers—coupled with ongoing border restrictions caused by the COVID-19 pandemic. Due to the border restrictions by the PRC and strict national implementation of quarantine measures, Mongolia's economy shrank by 4.6 percent in 2020. For similar reasons, in 2021, Mongolia's economic growth was only 1.4 percent, which was well below our expectation of economic growth of 4.1 percent at the time when we approved our 2022 budget in November 2021. The Government of Mongolia removed COVID-19 restrictions on 14 February 2022 due to high vaccination rates, low infection and mortality rates. However, Mongolia has not been able to benefit from this and strong export demand as the Russia-Ukraine war started on 24 February 2022 and protracted impacts of the COVID-19 pandemic continued. Due to the war situation in Ukraine, global uncertainty is on the rise, with commodity prices, including oil and gas, rising sharply, threatening global inflation and slowing economic growth. In Mongolia, this situation also increases the uncertainty, intensifies inflation through the direct and indirect effects of fuel, food, and other import prices, increases production costs, and slows economic growth. In 2021, petroleum's price soared by 48.3 percent compared with 2020, and in 2022 the price also increased by another 6.7 percent. As a result of rising inflation, household real income contracted by 6.6 percent in 2021. With nearly half of Mongolia's consumption basket composed of imported goods and services, real incomes eroded rapidly as inflation accelerated sharply in 2021. Rising food price inflation could prompt poverty to climb above the pre-COVID-19 level as urban poor households spend nearly 40 percent of their consumption on food.

Rising fuel and food prices negatively affect Mongolia's current account balance, economic growth and inflation through rising costs of production and consumption. Furthermore, with 24-28 percent of its wheat supply (100 percent of wheat imports) and 88 percent of fertilizers being imported from Russia, war-driven supply constraints in Russia could add to already high food price inflation, and further weaken growth and hence the livelihood of the population, especially of vulnerable groups. Our country has been importing 91 percent of petroleum products solely from Russia for the last four years. As such, the Russia-Ukraine war situation is already causing major supply disruptions and higher inflation. The exogenous shocks are expected to yield wider negative socioeconomic implications, especially on lower income households and vulnerable groups, including women and girls. 250 thousand people, 8 percent of the total population, in lower income groups are at risk to falling into poverty, due to ballooning inflation and resulting loss in purchasing power.

Countercyclical development expenditures. The Government has developed a countercyclical expenditure program to support the needs of those most affected by the current situation. The Government amended its 2022 budget, on 31 Jan 2022 and on 29 April 2022, in response to the crisis. The approved budget already included several important measures to support vulnerable groups affected by slow economic growth; The two subsequent budget amendments contained additional measures to protect vulnerable groups and to contain inflationary pressures. Countercyclical development expenditures consist of cash transfers to households, targeted measures to cushion socioeconomic impacts on vulnerable groups and measures to counteract inflationary pressures.

Cash transfers to households will continue under the Child Money Program of MNT 100,000 per child per month until the end of 2022. In Mongolia, 42 percent of the total poor are children and families from the poorest quintile have five children on average compared to 2.6 in the highest quintile. This suggests that increasing child money transfers, whilst being a universal benefit, will provide more money to poorer households and enhance their resilience to this economic shock.

The government has also introduced several targeted measures to directly support the most vulnerable from the current situation. Specifically, there are three main measures. 648,4 thousand employees, 56.2 percent of which were women, with a monthly salary of less than MNT 1 million received reimbursement of 50 percent of employee's social insurance premium contribution for 2022. Furthermore, public support service employee, the lowest earning public employees, of which 75.9 percent (104,443) are women, will receive a permanent salary increase of 8.5 percent. In addition, the government will increase the availability of kindergarten spaces for young children in poor areas. The latter measure will increase female labor force participation and reduce women's unpaid work.

There are several measures to help vulnerable groups manage the impacts of inflation which include interest rate subsidies to micro-, small- and medium-sized enterprises in the agriculture sector to ease the pressure on these companies given the challenges facing the sector. In addition, the government will provide customs duty exemptions on essential food products and key commodities, again to ease the pressure on actors in the agriculture and commodities sectors, and to eventually cushion inflationary pressures.

The Government of Mongolia is financing the countercyclical expenditure program through pre-export payments, expenditure reprioritization, expenditure cuts and increased external borrowing. The Government has cut capital expenditures by 10.6 percent and recurrent expenses for all budgetary public institutions, including state-owned enterprises, by 30 percent.

Sound pre-shock macroeconomic management. Mongolia is strongly committed to sound macroeconomic management and our pre-COVID-19 record shows this. Annual average economic growth was 6.3 percent during 2017–2019 before contracting by 4.6 percent in 2020 during COVID-19 and recovering slightly to 1.4 percent in 2021. Government's external debt to total government debt averaged 87.0 percent during 2017-2019 before it increased to 94.0 percent in 2020 and 2021, due to increased external borrowing in response to aforementioned exogenous shocks. The fiscal expenditure was 30.7 percent of GDP before reaching to 33.3 percent of GDP in 2020 due to fiscal measures in response to the shock. The Government of Mongolia is pursuing a policy of gradually reducing the structural budget deficit in accordance with the Fiscal Stability Law. Accordingly, the structural budget balance was set in the 2022 Fiscal Framework Statement to reach -5.1 percent of GDP in 2022, -3.6 percent in 2023, and -2.8 percent in 2024.

Commitment to structural reforms. The Government of Mongolia remains strongly committed to medium-term structural reforms. Despite the recent exogenous shocks, the authorities remain on course to meet the requirements of the FSL by 2024 through a combination of better medium-term fiscal and debt management planning. On the fiscal side, the Government is deeply committed to strengthening medium-term planning in debt and fiscal management, with the ultimate aim to increase coherence with the FSL. On the finance sector side, all systemically important commercial banks are mandated to undertake an initial public offering (IPO) by 30 June 2023, to diversify their shareholder structure and strengthen the capital base. Furthermore, the Government is committed to

the implementation of the Banking Sector Medium-Term Strengthening Program and implementing changes to the Banking Law to improve the capital base of banks as well as the resolution of nonperforming loans. These policy actions will improve financial sector performance, which in turn will benefit the economy overall over medium-term.

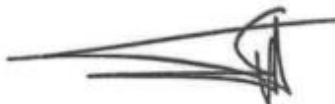
Debt sustainability. Based on Government of Mongolia's Debt sustainability analysis, the additional borrowing over the general government debt stock of \$9.5 billion in 2021, expected at the end of 2022 will not significantly affect debt sustainability or annual debt service obligations. The parliament approved a Government medium-term /2023-2025/ debt management strategy on 27 May 2022 to reduce its debt-to-GDP ratio and gradually shift from external to domestic borrowing through the domestic issuance of government securities denominated in local currency. According to the ADB, the CSF, PBL and the cofinancing loan would not worsen Mongolia's debt sustainability.

Coordination with the IMF. Under Article IV of the IMF's Articles of Agreement, the IMF held bilateral discussions with the Government of Mongolia during October 1 to October 5, 2021. As a result, the Staff Report prepared by a staff team of the IMF for the Executive Board's consideration on November 19, 2021. In the Article IV consultation document, staff team of the IMF concluded that "Risks to the outlook are on the downside risks. A worsening of the pandemic, extended border restrictions, and tighter global financing conditions pose significant risks. The government and BOM have appropriately managed Mongolia's external vulnerabilities." The IMF conducted a review mission with the Government from 28 April to 3 May 2022 in addition to their regular Article IV missions. ADB requested an IMF assessment letter to this operation on 16 May 2022, and received a reply on 13 June. The government continues to maintain a close dialogue with the IMF and their resident mission. Monitoring and evaluation. The Government has agreed to establishing a monitoring and evaluation mechanism to report transparently on the implementation of the countercyclical expenditure program supported by the CSF. Quarterly reports will be prepared, complemented by qualitative analysis through consultations with representative beneficiary groups, including women and girls. These reports and analyses will then form the basis of a strategic dialogue led by ADB's Country Director for Mongolia and the State Secretary of the Ministry of Finance.

The \$100 million CSF contributes to the Government's immediate financing needs; the loan is well suited to support Mongolia in the current situation given the severity of the economic shock, but also Mongolia's recent strong record on macroeconomic management and sound policy framework. The loan will allow us to implement the necessary steps in addressing immediate economic challenges and to finance the increased Government expenditure needs to support those suffering from the crisis and bolstering foreign exchange reserves. It will further provide us with the necessary space to allow us to continue with the implementation of critical structural reforms over the medium-term.

Finally, we would like to convey our appreciation to the ADB for being our sincere development partner and for your additional support in the current economic situation which will help us to better navigate through this challenging period.

Sincerely yours,



Javkhlan Bold

**ASSESSMENT OF COMPLIANCE WITH THE ELIGIBILITY CRITERIA FOR THE
COUNTERCYCLICAL SUPPORT FACILITY**

	Access Criteria	Asian Development Bank's Assessment
1	Adverse Impact of Exogenous Shocks	<p>The continued border restrictions with the PRC since October 2021 and the Russian invasion of Ukraine in February 2022 have resulted in severe shocks in economic activities and substantial fiscal stress. The shocks expose especially the vulnerable segment of the population to economic hardship, including women and girls.</p> <p>The exogenous shocks compromised Mongolia's otherwise favorable recovery prospects. Mongolia was on its way to recovery with growth of 6.3% in the first half of 2021 when hit by two consecutive contractions in Q3 and Q4 2021 that were caused by trade disruptions resulting from COVID-19-related restrictions with the main trade portal with the PRC in October 2021. Any boost from Mongolia's lifting of domestic COVID-19 related restrictions on 14 February 2022, due to a successful vaccination campaign, was short-lived as the Russian invasion of Ukraine started on 24 February 2022.</p> <p>The Russian invasion of Ukraine is putting huge downward pressure on trade with the Russian Federation (29% of Mongolia's imports, including 97% of oil imports) and with Europe (13% of imports), as the Russian Federation also serves as an important transit country for traded goods. The continuation of the border restrictions with the PRC (82.7% of Mongolia's exports and 37% of imports) results in major trade disruptions.</p> <p>The combination of these external shocks has resulted in severe downgrade of economic growth forecasts. It first prompted consensus growth forecasts for 2022 to go on a downward slide from 6% (Asian Development Outlook Update, September 2021) to a much more sobering 2.3% (Asian Development Outlook, April 2022) and more recently 0.6% (Asian Development Outlook Supplement, July 2022). A recent projection by the IMF forecasts 1% GDP growth for 2022, with risks tilted to the downside.</p> <p>Adverse fiscal implications due to reduced revenues have increased external and domestic financing needs. In April 2022, total revenues and tax revenues declined by 31.5% and 13.9% year-on-year respectively and are expected to continue declining amid the exogenous shocks. Income tax revenues and corporate income tax revenues decreased by 58.7% and 69.2% over the same period, respectively. In an adverse scenario under a deep GDP contraction of 0.8%, ADB estimates that</p>

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		<p>budget financing needs could rise by \$611 million for 2022, from originally planned 5.1% to 8.9% of GDP.</p> <p>Wider negative socioeconomic implications are expected, especially on the 27.8% of households already below the poverty line as well as low-income and vulnerable groups, with a further 14.9% of people at risk of falling into poverty, due to ballooning inflation and the resulting loss in purchasing power. Consumer price inflation is rising. It picked up since the second quarter of 2021 and has exceeded 10% since November 2021, reaching 15.1% nationwide as of May 2022 with both food and fuel inflation particularly high, hitting those below the poverty line the most, as poor people spend 43% of their disposable income on food. The government estimates that with each 10% increase in food prices, poverty is expected to increase by one percentage point, or about 34,100 people.</p>
2	Countercyclical development expenditures	<p>The Government has introduced a countercyclical development expenditure program (CDEP) to respond to the adverse impacts of the exogenous shocks. As a result of a parliamentary-approved budget amendment in April 2022, the CDEP aims to mitigate adverse economic and development impacts stemming from the shocks and to maintain inclusive and sustainable economic growth. The total size of the CDEP is \$860 million, equal to 6.2% of GDP and features the following three areas of support to enhance resilience of the population, specifically the poor and vulnerable groups, including women and girls.</p> <p>Cash transfers to households through top-ups to the child money program (CMP) to help reduce vulnerability. Cash transfers to households will reach 1.2 million children (48.8 % girls) in 64% of the country's households under the child money program, which is a universal child grant that is pro-poor and has proven to reduce inequality during the pandemic.^a</p> <p>This measure will provide social protection support to vulnerable households under the CDEP through extending the increased allocation under the CMP of MNT100,000 per child per month until the end of 2022. It was originally planned that this increase would be phased out after 31 December 2021. This measure will reach 1.2 million children (48.8% girls) in 64% of the country's households. In Mongolia, 42% of the total poor are children and families from the poorest quintile in the income distribution, which have five children on average compared to 2.6 in the highest quintile.^b Hence, increasing child grants reaches poorer households. ADB simulations of the child money top-ups suggest that they alone could reduce poverty to 24.7% compared with 36.7% in a scenario with no social protection response to COVID-19 pandemic. Women are also the</p>

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		<p>custodians of 90% of the child money accounts, underlining important gender impacts of this measure.</p> <p>Targeted measures to cushion adverse socioeconomic impacts on vulnerable groups, including women and girls. These measures will protect those suffering the most from the impacts of the exogenous shocks through waiving social insurance premiums for low wage earners, increasing salaries of low wage earners, and providing kindergarten subsidies for low-income households.</p> <p>The government has introduced three key measures to directly support the most vulnerable groups. First, 300,000 employees (56% women) earning a monthly salary of less than MNT1 million will receive a 50% reimbursement of their social insurance premium contributions for 2022; second, 107,000 lowest earning public service employees of whom 75% are women, will receive an average salary increase of 8.5%.^c These targeted measures will enhance the crisis resilience of vulnerable groups; third, about 16,000 new kindergarten spaces for young children in poor areas will be made available from the start of the new school year in September 2022. In addition to clear early childhood development benefits, increased access to kindergarten for young children will reduce women's unpaid childcare burden and time poverty, thus increasing opportunities for women to participate in the labor force.^d In the longer term, early childhood education is vital for human capital formation of young children.</p> <p>Measures to counteract inflationary pressures, especially in relation to rising food prices. Amid the rising inflation in Mongolia and its adverse development implications, these measures are essential to avoid worsening poverty, particularly as poor households spend a much larger share of their disposable income on food than non-poor households. Measures include concessional loans, including interest subsidies, for MSMEs in agriculture and customs exemptions on essential food products.</p> <p>Eligible MSMEs for obtaining concessional loans include agricultural businesses involved in domestic food production (e.g., meat, flour, sugar, vegetable oil, milk, potatoes, fruit, and vegetables), cashmere, wool, and leather. MSMEs engaged in food packaging and food processing, food chain stores and importers of essential food products are also covered. Cheaper interest rates for MSMEs in the agriculture sector will not only ease the financial pressure on these enterprises, but also promote the domestic production of essential food products, thereby reducing reliance on imported food products that are subject to high inflationary pressure. Additionally, food price</p>

	Access Criteria	Asian Development Bank's Assessment
		inflation will be tamed through exemptions from customs' duties on essential food products (i.e., rice, vegetable oil, and sugar).
3	Pre-shock record of generally sound macroeconomic management	<p>Macroeconomic management pre-coronavirus disease (COVID-19) pandemic was generally sound though there are areas where continued reform is needed. Annual average growth was 6.3% from 2017–2019 before contracting by 4.6% in 2020 with the onset of COVID-19 pandemic and recovering weakly to 1.4% in 2021.</p> <p>Before hit by the exogenous shocks, growth expectations were positive and on a visible path of recovery. In the first half of 2021, real GDP growth recovered from a 9.0% contraction in the first half of 2020 to a 6.3% growth. This resulted in an April 2021 forecast for 2021 of 4.8% by the ADO. In 2021, the fiscal balance improved to a deficit equal to 3.1% of GDP, narrower by 6.4 percentage points than in 2020 as revenue increased by 37.0%, outpacing 11.7% expenditure growth.</p> <p>Mongolia reduced its debt-to-GDP ratio considerably from 2016 to 2019 and increased foreign exchange reserves. Mongolia decreased its debt-to-GDP ratio by 32 percentage points from 2016 to 2019 before weak growth and rising expenditure needs resulted in an increase of 14 percentage points in 2020. Despite continued difficult economic conditions in 2021, the government reduced debt as a percentage GDP from 91.2% in 2020 to 80.4% in 2021, underlining their commitment to debt reduction. Gross foreign exchange reserves also rose from 2.8 months of imports in 2016 to 7.4 in 2020 before falling to 5.7 months in 2021.</p> <p>Although public debt is sustainable, it remains at risk of debt distress. According to the IMF Debt Sustainability Analysis (November 2021) and the IMF assessment letter (June 2022), Mongolia's public debt is sustainable under the baseline scenario, but the risk of public and external debt distress remains elevated.^f</p> <p>Despite a solid record from 2017-2019, the fiscal policy to COVID has been termed "excessive" by the IMF. The IMF estimates that budgetary measures reached 12% of GDP in Mongolia in response to COVID-19 in comparison to 5.7% for Emerging Markets. In addition, the extension of the Anti-Pandemic Law to end 2022 means that BOM continues to inject additional liquidity into the economy, which could pressure on inflation. There are important fiscal reforms outstanding, including the need to manage increasing pension liabilities and improve the targeting of social protection spending.</p>

	Access Criteria	Asian Development Bank's Assessment
		<p>Inflation remained below target (8%) between 2017 and 2020 but started to pick up in 2021 due to COVID-19 restrictions. In response, BOM, the central bank, increased the policy rate by 4 percentage points to 10% as of June 2022. After falling to 5.1% in 2020, the current account deficit rose to 13.0% of GDP in 2021 as imports rose while exports remained constrained by border restrictions.</p> <p>Despite structural weaknesses in the banking sector, bank credit expanded in 2021 and the proportion of nonperforming loans also fell in 2021, though still at an elevated level of 9.2% in April 2022. The authorities are in the process of implementing a medium-term banking sector strengthening program aimed at tackling underlying structural challenges in the financial sector.</p> <p>Overall, despite challenges in particular areas, Mongolia's precrisis macroeconomic management was generally sound. Core economic indicators such as GDP growth and inflation have largely been solid. Government's fiscal management has reflected strong attention to debt management but with a continued need to reign in fiscal tools to avoid inflationary impacts and crowding out of the private sector. Finance sector has historically been a challenging area, but the government has a medium-term plan in place and it is moving ahead with implementation.</p>
4	Structural reforms	<p>Despite the exposure to the exogenous shocks, Mongolia is committed to continue implementing critical structural reforms. Key reforms relate to fiscal sustainability, financial sector performance and stability, and social protection.</p> <p>On the fiscal side, the government is committed to strengthen medium-term debt and fiscal management. Parliament on 27 May 2022 ratified a new Medium-Term Debt Management Strategy for 2023–2025, which relates to improving fiscal and debt management, expenditure efficiency, domestic capital market development, and contingent liability management. The Government remains committed to reduce public debt in line with the Fiscal Stability Law.⁹ In addition, the government is committed to improving social protection both to ensure it is more fiscally sustainable and more effective at targeting support for vulnerable groups. This also responds Mongolia's COVID-19 measures, which were successful in responding to the pandemic even as they may have resulted in some excessive spending.</p> <p>In the finance sector, the government is implementing the Banking Sector Medium-Term Strengthening Program (2020–2023). The program includes 49 actions and focuses on</p>

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		<p>five key reform areas: (i) reduce bank ownership concentration, undertake public listing of banks, and enhance prudent governance framework for bank operations; (ii) align banking supervision and regulatory instruments with international best practices, including a plan to introduce Basel III supervision standards; (iii) successfully complete the financial sector agenda of IMF's 2017 EFF; (iv) address gaps in anti-money laundering/combating the financing of terrorism (AML-CFT) and graduate out of the Financial Action Task Force (FATF) grey list at the earliest (already achieved in October 2020); and (v) introduce a legal framework to recognize and license banks differentiated on the basis of their type, size, and functions performed.</p> <p>In line with the Banking Sector Medium-Term Strengthening Program, the Mongolian Parliament amended the Banking Law in 2021 to reduce bank ownership concentration and mandating public listing of banks. Major changes include: all five SIBs must get publicly listed on the Mongolian Stock exchange by 30 June 2022 (The deadline was recently extended till 30 June 2023); (ii) all commercial banks must diversify their shareholding structure by end-2023 so that any group of related parties owns less than 20% of any bank, and (iii) any group of related parties is not allowed to own more than 5% of more than one bank.</p> <p>The public listing of SIBs by June 2023 will not only address recapitalization concerns but will also yield broader and long-term benefits. In particular, it will expand the banks' capital base, attract foreign and domestic investments in the banking sector, diversify shareholding structure, reduce ownership concentration, and thus promote good governance practices in the banking industry.</p> <p>ADB has consistently performed an important role in facilitating and leveraging structural reforms. This has been achieved through the implementation of a series of programmatic approach PBLs, targeting policy reforms to both strengthen fiscal sustainability and safeguarding space for critical social expenditures. Additionally, ADB's Second Shock-Responsive Social Protection Project supports the government to better identify poor and vulnerable households and make social protection more targeted and efficient.</p>
5	Debt sustainability	<p>The countercyclical expenditure plan does not adversely affect the overall sustainability of Mongolia's debt. The government requested a \$100 million CSF loan from ADB and cofinancing of \$100 million from the Asian Infrastructure Investment Bank. The government will also borrow \$435 million domestically to respond to increasing financing needs. Based on</p>

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		<p>ADB's debt sustainability analysis the additional borrowing will not significantly affect debt sustainability or annual debt service obligations. The government will continue the implementation, with ADB support, of a medium-term debt management strategy to reduce its debt-GDP ratio gradually.</p> <p>In this analysis, we used two GDP growth scenarios (point (i), below) with core assumptions on other key indicators:</p> <ul style="list-style-type: none"> (i) Economic growth for 2022 is expected to reach 2.6% under the baseline scenario or 1.0% under the alternative scenario. Growth will average 6.3% in 2023–2025. (ii) Average annual inflation will peak at 14.4% in 2022 before moderating to an average of 9.9% in 2023–2025, and the nominal exchange rate is expected to depreciate in both scenarios. (iii) The structural fiscal deficit will be consistent with the ceilings set by the Fiscal Stability Law, and shall not exceed 5.1% of GDP in 2022, 3.6% in 2023, 2.8% in 2024, and 2.0% in 2025 under the baseline scenario. However, the structural deficit in 2022 will be higher at 7.6% of GDP under the alternative scenario. (iv) Mongolia would retain access to concessional budget support and project loans in line with current commitments, and Mongolia would maintain access to international bond markets over the forecast period. <p>Under the baseline scenario, the debt-to-GDP ratio in 2022 will temporarily rise by 2.2 percentage points to 82.6%, but by 10 percentage points to 90.4% under the alternative scenario (higher than the end-2018 level, but still well below the end-2017 level) before resuming a downward trajectory in subsequent years. Based on the assumption of a return of economic growth momentum from 2023, debt-to-GDP is forecast to fall to 73.4% of GDP (baseline) and 82.9% of GDP (alternative) by the end of 2025.</p> <p>The IMF assesses Mongolia's public debt as sustainable under the baseline scenario. According to the IMF Debt Sustainability Analysis (November 2021) and the IMF assessment letter (June 2022), Mongolia's public debt is sustainable under the baseline scenario, but the risk of public and external debt distress remains elevated.^f The IMF assessment underlines that Mongolia's debt dynamics are particularly vulnerable to the economic outlook, the exchange rate, and the realization of financial sector contingent liabilities.</p>

	Access Criteria	Asian Development Bank's Assessment
		<p>According to the IMF, reserve adequacy improved in 2021 but remains thin. During the first half of 2020, the combination of large BOM interventions and the sharp decline in exports led to a decline of reserves by \$1 billion. However, as conditions improved since the second half of 2020, reserves increased and reached \$4.4 billion by end-August 2021 after peaking at a record \$4.9 billion in April 2021. Reserves net of BOM's foreign exchange liabilities have also improved to \$0.76 billion by end-August 2021. Even if the People's Bank of China swap facility is fully rolled over in 2023, reserve coverage is projected to remain within the recommended range but would fall below recommended levels in the event that the swap is repaid.</p>
6	IMF coordination	<p>ADB supported the implementation of the IMF's Extended Fund Facility (EFF) from 2017-2020 in several areas. This was a \$5,650 million package—with ADB contributing \$900 million—which included financing from the IMF, the WB, ADB, the Government of Japan, the Government of the Republic of Korea, and the People's Republic of China. The program was designed to help deal with economic challenges triggered by falling commodity prices, plummeting foreign direct investment, and expansionary fiscal and monetary policies.</p> <p>The EFF set several macroeconomic and structural reform priorities. Among them were the strengthening of macroeconomic policies to stabilize the economy and avoid boom-bust cycles, and structural reform to diversify the economy and allow for sustainable medium-term growth. Improvements have been sought to the social welfare system to better protect the poor. Efforts have been made to strengthen the banking sector.</p> <p>ADB continues to maintain close dialogue with the IMF in terms of economic analysis, reform support, and crisis response. This also includes close coordination on the policy reform areas supported under a proposed PBL,⁹ including (i) support to the mandated initial public offerings of banks to support banks' capital base, shareholder diversification, and corporate governance, (ii) enhancements to Mongolia's NPL resolution framework and legal environment, and (iii) further alignment of the banking sector supervision and regulation with international standards. In addition, ADB has closely coordinated with the IMF on data and analysis, including on debt sustainability where the ADB Summary Debt Sustainability Analysis builds on IMF Debt Sustainability Analysis. Since 2018, ADB has worked closely with the IMF on domestic resource mobilization and support for the Mongolian Tax Authority (MTA). ADB financed the MTA's Business Continuity Plan, which was developed with support from the IMF, allowing MTA staff to work</p>

	Access Criteria	Asian Development Bank's Assessment
		<p>from home during the COVID-19 pandemic. In addition, ADB's TA for the MTA is aligned with the IMF's assistance.</p> <p>ADB and IMF have been coordinating at senior and technical levels. ADB senior management has discussed Mongolia with the IMF during the IMF Spring Meetings in April and again in July 2022 after the appointment of IMF's new Director for the Asia and Pacific Department. At a technical level, ADB and IMF teams are in weekly contact and ADB hosted the IMF development partner debrief after the IMF mission to Mongolia in April 2022. The IMF provided an assessment letter to ADB for the CSF program in June 2022.</p>
7	Monitoring and Evaluation	<p>The government has agreed to establish a monitoring and reporting mechanism to report on the implementation of the CDEP and the CSF. Quarterly reports will be prepared which will be complemented by qualitative analysis through consultations with beneficiary groups, including women and girls. These reports and analysis will then form the basis of a strategic dialogue led by ADB's Country Director for Mongolia and the State Secretary of the Ministry of Finance (MOF).</p> <p>The following topics will be included in the group's dialogue:</p> <ul style="list-style-type: none"> (i) The delivery of the measures included in the CDEP to the intended beneficiaries and DMF indicators; (ii) Additional efforts required to improve the effective and timely delivery of the CDEP and the CSF; and (iii) Progress made by the government in achieving the key structural reforms <p>The high-level policy dialogue will occur, on a quarterly basis, at least until the audit of the 2022 national budget has been prepared (expected in June 2023).</p> <p>The high-level policy dialogue group will be supported by a technical group that will prepare materials, updates, and suggestions for the consideration of the high-level group, including a comprehensive assessment of the delivery of the selected expenditure items of the CDEP and an update on the structural reforms. The technical group will be responsible for collation of all necessary data for the high-level dialogue.</p> <p>Donor coordination and link with other ADB work. ADB and the government may invite representatives of international financial institutions, development partners, beneficiaries, and other key stakeholders, as and when needed, to participate in the strategic/policy dialogue.</p>

ADB = Asian Development Bank, ADO = Asian Development Outlook, BOM = Bank of Mongolia, CDEP = Countercyclical Development Expenditure Program, CMP = Child Money Program, COVID-19 = coronavirus disease

2019, DMF = design and monitoring framework, EFF = Extended Fund Facility, GDP = gross domestic product, IMF = International Monetary Fund, MOF = Ministry of Finance, MNT = togrog, MSME = micro-, small-, and medium-sized enterprise, NPL = nonperforming loans, PBL = policy-based loan, Q = quarter, WB = World Bank.

- ^a ADB. 2020. [Assessment of the Social Protection Response to COVID-19 in Mongolia](#). Technical Assistance Consultant's Report. Manila; and World Bank. 2021. [Mongolia Economic Update: From Relief to Recovery](#). Washington, D.C.
- ^b National Statistics Office of Mongolia and the World Bank. [Mongolia Poverty Update 2018: Main Report of the Household Socio-Economic Survey 2018](#). 2020. Ulaanbaatar and Washington D.C.
- ^c In 2021, a total of 137,000 public support service employees in Mongolia consisting of 51,500 employees from ECE and compulsory education; 1,500 employees from science; 2,100 employees from vocational training; 32,200 employees from health; 4,700 employees from art and culture; 43,500 employees from public service. Under this measure, all public service servants that account for 66% of the overall civil service will benefit.
- ^d ADB research also shows that increasing female labor force participation would also significantly increase economic growth in Mongolia. ADB. 2020. [Boosting Mongolia's Long-Term Economic Growth through More Equal Labor Force Participation between Men and Women](#). Manila.
- ^e Under the law, the structural budget deficit shall not exceed 2% of GDP.
- ^f [Mongolia: 2021 IMF Article IV Consultation Staff Report. November 2021](#) and [Mongolia: Concluding Statement of 2022 IMF Staff Visit. May 2022](#).
- ^g Proposed Programmatic Policy-based loan: Strengthening Economic, Fiscal, and Financial Resilience Programmatic Policy-Based Lending is scheduled for Board consideration in November 2022.