Project Information Document/ Identification/Concept Stage (PID)

Concept Stage | Date Prepared/Updated: 30-Jan-2019 | Report No: PIDC165991

BASIC INFORMATION

A. Basic Project Data

Project ID	Parent Project ID (if any)	Environmental and Social Risk Classification	Project Name
P168248		Low	Strengthening Governance in Mongolia
Region	**Country**	**Date PID Prepared**	**Estimated Date of Approval**
EAST ASIA AND PACIFIC	Mongolia	30-Jan-2019	
Financing Instrument	**Borrower(s)**	**Implementing Agency**	
Investment Project Financing	Ministry of Finance	Ministry of Finance of Mongolia	

PROJECT FINANCING DATA (US$, Millions)

SUMMARY

Total Project Cost	2.44
Total Financing	2.44
Financing Gap	0.00

DETAILS

Non-World Bank Group Financing

Trust Funds	2.44
Miscellaneous 1	2.44

B. Introduction and Context

Country Context

Mongolia is a resource rich country with vast mineral resources, but it is facing short-term challenges due to fiscal vulnerabilities and external risks.. The country's economy expanded by an average of 14 percent during 2011–13, boosted by surging FDI inflows that averaged 32 percent of GDP accounting for almost 70 percent of gross investment, and strong commodity exports. The strong external environment, however, began to deteriorate from mid-2013. FDI inflows dried up to less than 2 percent of GDP during 2014–16 as new foreign investment projects were delayed. Meanwhile, a continued and sharp drop in commodity prices (mostly copper and coal) and slower growth in China, dampened commodity exports, which accounted for almost 90 percent of total exports. Growth dropped to 1.8 percent in 2015–16 following the decline in investment and net exports triggered by the precipitous drop in FDI and weak commodity exports, as well as a contraction of private consumption explained by negative household income growth and high unemployment in 2016. With these developments, the Mongolian government did not implement the most appropriate countercyclical policies. In fact, Mongolia, which stands out as a country with high public spending, low tax rates, and high exemptions, was unable to generate substantial savings for future years when booming mineral production and exports stimulated growth and increased government revenue.

An expansionary policy to counter the global commodity price decline, while there was little fiscal space, led to an unsustainable public debt dynamic. It was difficult for the country to cope with lower export volumes and prices for its mineral production after 2012. The growth rate of the economy, which averaged 15 percent in 2011–12, fell to 7.9 percent in 2014, 2.2 percent in 2015, and 1.3 percent in 2016. Total government revenue fell from 31 percent of GDP in 2011–12 to 26.6 percent in 2014–15. To mitigate the economic impact of the commodity crisis, the government kept public spending at a high level (about 37.5 percent of GDP in 2014–16). The combination of sharply reduced government revenue and expansionary fiscal policies led to high (consolidated) budget deficits (averaging 12 percent of GDP during 2014–16), and unsustainable public debt and debt service ratios.

Mongolia has good fiscal management laws, which have been in disuse to prevent external shocks. In 2010, the Parliament adopted a Fiscal Stability Law (FSL). Its objective was to ensure fiscal discipline by setting up a structural deficit ceiling (2 percent of GDP) calculated on the basis of average commodity prices over 16 years. Strict implementation of that rule was expected to create savings during good times that would be used to mitigate the economic and fiscal impact of low export prices and sharply reduced government revenue during bad times. However, this law, which went into effect in 2012, could not be implemented, as the government used a series of off-budget financing techniques to bypass the FSL, and fund high levels of public spending. Recurrent expenditures rose from 23.1 percent of GDP in 2010 to 27.4 percent in 2016. Capital spending, largely financed by off-budget resources (through the Development Bank of Mongolia [DBM]), increased from 6.1 percent of GDP in 2010 to 11 percent in 2016. High domestic and foreign borrowing led to sharp increases in public debt (up to 87.2 percent of GDP in 2016 from 24.1 in 2011). Interest payments rose from 0.3 percent of GDP in 2011 to 4 percent in 2016.

Sectoral and Institutional Context

The recent SCD highlights that are three broad governance issues in Mongolia. First, policies in election campaigns with promises combining general social benefits and more specific ‘club goods’ that benefit certain groups of citizens without the appropriate fiscal funding. Second, legislative processes that have led to enactment of laws, which have worked in some countries, without sufficient policy analysis of the country context, risk assessment and consultation. Third, forms of state capture by some politicians and businesses, with frequent shifts following changes in parliamentary majorities. These translate into a low Transparency International Corruption Perception Index (where Mongolia ranks 103, in the bottom half), and below the average of the East Asia and the Pacific countries in the Worldwide Governance Indicators on government effectiveness, regulatory quality, rule of law and control of corruption.

From a more operational point of view, these governance issues translate into problems in terms of credibility of fiscal budget, quality of regulations, capabilities of civil service and investor confidence. Despite recent advances, there are challenges to improve efficiency, effectiveness and transparency of Public Financial Management. Particularly, lack of budget credibility due to poor alignment of expenditures to revenue outturns and weak implementation of Public Sector Accounting Standards. Similarly, the Government of Mongolia (GoM) has over the last few years implemented several reforms to improve regulatory frameworks, but these reforms have revealed the need for a more systemic approach to the preparation, coordination, transparency, and enforcement of regulations. There are limitations in terms oversight, analysis and impact assessment of regulations as well as mechanisms of effective consultation.

The Government of Mongolia (GoM) has also undertaken reforms to gradually bring about fiscal discipline and strengthen the PFM system. The first phase of reforms between 2003 and 2008 established the basic elements of the system, including strengthening internal controls, cash management, and accounting and reporting. The second phase of reforms between 2008 and 2011 included some improvements in fiscal policy, budget planning, and decentralization of roles and resources to subnational governments. The GoM, however, does not currently have an overall PFM strategy that builds on the progress made in the past and focuses on strategizing and sequencing the ongoing and future interventions necessary to further strengthen the PFM system in the country.

Relationship to CPF

The proposed operation builds on the long standing relationship between the Bank and the government of Mongolia . As highlighted in the Performance and Learning Review of the Country Partnership Strategy FY13-FY for Mongolia (Report No. 106796-MN); one of the main emerging lessons was the need to address governance challenges in the country. This report paved the way to an IDA lending operation (SFFS) that had macroeconomic and governance issues at the heart of the intervention. The Performance and Learning Review also highlighted the need that the new CPF should tackle governance issues in creative ways. Within this context, it has been discussed that the new CPF under preparation will cover improving public and economic governance areas to support the government's fiscal stability efforts.

C. Project Development Objective(s)

Proposed Development Objective(s)

The Program Development Objective is to support the Government’s efforts to improve fiscal discipline, public financial management (PFM), and transparency and accountability processes for strengthened governance in Mongolia.

Key Results

1.Adopt and implement a new five-year PFM reform plan.

2. Improve transparency in the budget process.

D. Preliminary Description

Activities/Components

In order to support the on-going efforts of the government to achieve fiscal stability, **enhance Public Financial Management (PFM) and strengthen transparency and citizen engagement**, the World Bestablished an EU-funded hybrid TF073029. This new TF will complement the on-going activities under the "Strengthening Fiscal and Financial Stability Project" (SFFS) (P161048) and provide additional support to the government's PFM reform efforts.

This new Recipient Executed (RE) TF will serve two main purposes: The first one will be to complement and expand the ongoing technical assistance the WB is providing through the SFFS Project with a number of activities that are deemed critical to support Mongolia in achieving the objectives the country has agreed to in its Economic Recovery Plan (ERP) as well as the development partners' support including the EMSO of the World Bank and the EFF of the IMF. The second purpose of this TF is to support the GoM in advancing the current efforts toward increasing transparency and participation in fiscal matters.

The recipient executed grant will have 2 technical components detailed below:

Component 1: Will focus on supporting operationalization of the recently established Fiscal Council and strengthening the capacity of MoF in areas such as debt management and revenue forecasting, among others.

Component 2: Will focus primarily on the design and implementation of a PFM reform plan; improving budget preparation and execution; improving the management of contingent liabilities, and strengthening public investment management.

Environmental and Social Standards Relevance

E. Relevant Standards

ESS Standards		Relevance
ESS 1	Assessment and Management of Environmental and Social Risks and Impacts	Relevant
ESS 10	Stakeholder Engagement and Information Disclosure	Relevant

ESS 2	Labor and Working Conditions	Not Currently Relevant
ESS 3	Resource Efficiency and Pollution Prevention and Management	Not Currently Relevant
ESS 4	Community Health and Safety	Not Currently Relevant
ESS 5	Land Acquisition, Restrictions on Land Use and Involuntary Resettlement	Not Currently Relevant
ESS 6	Biodiversity Conservation and Sustainable Management of Living Natural Resources	Not Currently Relevant
ESS 7	Indigenous Peoples/Sub-Saharan African Historically Underserved Traditional Local Communities	Not Currently Relevant
ESS 8	Cultural Heritage	Not Currently Relevant
ESS 9	Financial Intermediaries	Not Currently Relevant

Legal Operational Policies

Safeguard Policies	Triggered	Explanation (Optional)
Projects on International Waterways OP 7.50	No	
Projects in Disputed Areas OP 7.60	No	

Summary of Screening of Environmental and Social Risks and Impacts

To be built on the ongoing SFFS project, this new TF project will neither finance civil works, nor lead to physical activities or other activities likely to involve environmental and social risks and impacts. The project is anticipated to involve induced social benefits associated with improved financial stability, and given the nature, type and scale of the project, it is expected that potential adverse risks to and impacts on human populations and/or the environment are likely to be minimal or negligible.

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