

## Mongolia

<b>Status Index</b> (Democracy: 3.6 / Market economy: 2.9)		<b>6.5</b>		<b>Management Index</b>		<b>6.5</b>	
<b>System of government</b>	Parliamentary-presidential democracy	<b>Population</b>	2.5 mill.	<b>GDP p. c. (\$, PPP)</b>	1,740	<b>Unemployment rate</b>	4.6 %
<b>Voter turnout</b>	82.4 %	<b>HDI</b>	0.661	<b>UN Education Index</b>	0.87	<b>Gini Index</b>	44.0 (1998)
<b>Women in Parliament</b>	10.5 %	<b>Population growth<sup>a</sup></b>	2.1 %				
<b>Largest ethnic minority</b>	6.9 %						
Data for 2001 – if not indicated otherwise. <sup>a</sup> Annual growth between 1975 and 2001. Source: UN Human Development Report 2003.							

### 1. Introduction

In the course of the simultaneous economic and political transformations begun in Mongolia in 1990, both the economy and the political system have been liberalized to a great extent. Today, democracy and a market economy constitute dominant characteristics. Mongolia's double transformation is unusual, especially from the point of view of modernization theory. Per capita income is low in Mongolia, and broad sectors of the population became impoverished during the economic transformation. Only a narrow middle class exists today.

As early as 1990, the first multi-party elections were held in Mongolia, and the first steps taken toward a market economy. In 1992, Mongolia passed a new, democratic constitution establishing a mixed, parliamentary and presidential system. The first democratic change in government in favor of the opposition, which formed in 1990 and unified as the Democratic Union Coalition (DUC), took place in 1996. Four years later, power reverted back to the previously monopolistic Mongolian People's Revolutionary Party (MPRP), which, in the meantime, had been extensively converted into a social democratic party. This assessment period thus covers the second half of the DUC regime and the first half of the new MPRP regime under Prime Minister Nambaryn Enkhbayar.

The assessment's overall conclusion is ambivalent. Toward the end of the DUC regime, conflicts within the coalition and between the coalition and an MPRP president considerably impeded the government's ability to govern. Since taking power, the MPRP seems to have improved the country's institutional performance, but it is still too early for a final conclusion.

While political and economic transformations have been successful on the whole, the new political and economic systems' performance has remained generally low. The primary reason for this is long-term structural factors, some of which have been reinforced by the system change. Mongolia's economic potential, and its financial and human resource capacities are limited. Although a high level of education was achieved during the Soviet era, broad sectors of the economic and general administration were run by skilled workers from the Soviet Union. After 1990, dependence on the Soviet Union was transferred to Western and Japanese donors. The transformation also devalued a sizeable portion of Mongolia's accumulated experience because controlling a market economy requires different instruments and skills than controlling a socialist planned economy.

Economic, social, and ecological problems have multiplied in the past; they did so again and to an increased extent after the Russian crisis in 1998. The new donors have tried to help Mongolia overcome these problems. To some extent, though, the external interventions have been mismanaged or simply ineffective. Mongolia has thus incurred considerable debts without yet being able to guarantee sustainable growth.

## **2. History and characteristics of transformation**

Mongolia's political and economic transformations occurred largely in parallel. Transformation in Mongolia was triggered from outside the country. From 1921 to 1989, Mongolia was the "satellite state" most closely linked to the Soviet Union. After Brezhnev's death in the Soviet Union, the longstanding secretary-general of the Mongolian People's Revolutionary Party (MPRP), Yumjaagiyan Tsedenbal, was replaced in 1984 by the then-chairman of the Council of Ministers Jambyn Batmönh, a moderate representative of the ruling regime. Toward the end of the 1980s, the Soviet Union increasingly cut back its troop presence (aimed against China) and its economic support for Mongolia. The external stabilization of the Mongolian communist system disappeared with these cuts. The first oppositional groups formed in 1989, primarily composed of the younger generation of the ruling elites. A moderate opposition was thus formed. Genghis Khan became the key figure of national identification, honored as the country's founder.

After tough battles with the communist regime, the opposition used hunger strikes in the first six months of 1990 to add emphasis to their demands for free elections. The first multiple party elections were finally held in July 1990. The opposition won 22 of 53 seats in the first post-communist parliament (State Little Hural). In January 1998, a new constitution was passed stipulating a mixed parliamentary and presidential system. The government is formed based on parliamentary majority and under a prime minister. The president is elected directly and has the

right to confirm the prime minister in office. The parliament has to confirm the president in office, but also has the authority to dismiss him.

In April 1992, a majority voting system was passed. The new system ensured that the party that won the subsequent elections (1992, 1996, 2000) gained an unusual preponderance of parliamentary seats. The system worked in favor of the MPRP in 1992, the Democratic Union Coalition in 1996, and the MPRP again in 2000. Although the MPRP ruled practically alone from 1992 to 1996 (70 of 76 parliamentary seats), it nevertheless launched radical economic reforms. After the opposition had won the 1996 elections, the MPRP ceded its power to the Democratic Union, a coalition of several opposition parties, in accordance with democratic rules. The DUC's four years in power (fewer than four prime ministers) were defined after 1998 primarily by numerous internal conflicts that diminished its reputation among voters. The MPRP has held all the political power again since 2000 (72 of 76 parliamentary seats, the office of the president, and the majority of the local parliaments), but it continues to abide by democratic rules.

The "shock-like" liberalization and privatization of the economy resulted in serious social differentiation and impoverishment. Herds (primarily sheep and goats) and small businesses were privatized in the early 1990s, but some large operations still remained under state control during the assessment period. Many industrial enterprises fell apart when Comecon aid dried up. Unemployed urban workers drifted back into nomadic pastoralism, dramatically increasing that branch's percentage of the GDP during the transformation. Under the DUC government between 1996 and 2000, practically all limitations on foreign trade were dismantled and taxes were lowered. This did not produce the desired economic upturn, however.

Mongolia has a long tradition of dependence on foreign powers. After 1990, dependence on the Soviet Union and the Comecon countries was transferred to Western nations and Japan. Today, Mongolia has the fifth highest rate of official development aid per capita in the world; the most important donors are the Asian Development Bank (ADB), the IMF, the World Bank, and, bilaterally, Japan, Germany, and the United States. So far, however, this has neither slowed down social differentiation nor established lasting economic growth. Instead, national debt has steadily climbed during the last few years, reaching 90 % of GDP in 2001. Although the debt is mostly made up of "soft credit" from international financial institutions and bilateral donors, servicing it will create problems in the future.

Mongolia's heavy dependence on foreign donors is an important reason why even the successor to the communist party, the MPRP, has followed a course of political and, in part, radical economic transformation since 1990. Democratic values do seem to be strongly anchored both culturally and mentally in Mongolian

society, however. Polls show that despite economic difficulties a clear majority of Mongolians still support the political and economic system change. A lively civil society has formed, primarily in the urban population center Ulaanbaatar.

### **3. Examination of criteria for democracy and a market economy**

#### **3.1 Democracy**

The democratic system in Mongolia increasingly stabilized over the past five years. This is remarkable, particularly when compared with the democratic regressions that have occurred in Central Asia. Electoral law remains a problem, marginalizing the parliamentary opposition between 1992 and 1996, and again since 2000. Some constitutional questions were resolved in 2001 (the president's authority to appoint the prime ministers, and unifiability of political offices and parliamentary mandates). The changes were intended to increase the political system's overall effectiveness. However, the democratic governments, working with foreign donors, have remained unable to resolve many of the country's economic and social problems.

##### **3.1.1 Political organization**

(1) *Stateness*: On the whole, Mongolia does not have any problems with state identity. The sparsely populated country is, however, having trouble controlling its borders, primarily against smugglers. All citizens have the same civil rights. Church and state are largely separated. During the Soviet era, a modern administration was introduced in Mongolia. The economic crisis of the early 1990s has also led to a weakening of the state. Still, Mongolia has retained its public school system. Criminality and corruption have increased substantially since the onset of transition, and stagnated at this high level during the assessment period.

(2) *Political participation*: In contrast to other countries in Central Asia, free and fair elections have taken place regularly in Mongolia since 1992. Its governments generally respect the democratic rules of the game. Elected officials have the power to govern. In terms of decision-making, however, they depend on external financial donors to a considerable degree. In 1997, a progressive law was passed on the activities of civic groups. Freedom of association exists.

Approximately 1800 civil groups are officially registered, and a number of prominent groups are dominated by women. Unions are free to act. Important electronic media (TV, national radio stations) remain under state control and are dominated by the government of the day. The opposition again accused the MPRP of disadvantaging it in state media during the presidential elections in 2001.

Private media also exist in Mongolia, but the private media outlets' effectiveness as a monitoring body is weakened by poor investigative quality.

(3) *Rule of law*: Separation of powers prevails in Mongolia. The MRPR has had an overwhelming parliamentary majority since 2000, and on that basis the government under Prime Minister Enkhbayar. President Natsagiin Bagabandi is also from the MRPR. Nonetheless, there is a certain amount of rivalry between the prime minister and the president. It appears unlikely, however, that the president would attempt to usurp the prime minister's authority. The president's role in appointing the prime minister was limited in 2001 after he interfered in eleven attempted appointments between 1996 and 2000. Mongolia's Supreme Court has been in existence since 1992 and has become increasingly established. The compatibility of a parliamentary office and a position in government became legally permissible in 2001. This made sense considering the low number of outstanding politicians and the small "political class."

Mongolia's judiciary is free of unconstitutional interference from other institutions. There are problems with funding and education adequate training of judges, however. The legal system is also currently in a state of change. Public opinion considers the legal system to be relatively corrupt.

Corruption has been spreading in Mongolia since the start of the 1990s. The country ranked 43rd on Transparency International's 1999 Corruption Perception Index; it has not been evaluated since then. At the start of the assessment period, during the phase of permanent governmental crises in 1998–99, accusations of corruption increased against members of the DUC majority, among other things in connection with a bribery and banking scandal. In October of 1998, Sanjaasuregiin Zorig, one of the leading protagonists in Mongolian democratization, was murdered. Although the murder was never solved, the presumed motive was to cover up corruption. Zorig was considered an advocate of clean politics.

The first Mongolian anti-corruption law was passed in 1996. The law's effectiveness was initially low (very light punishments, no independent anti-corruption authority). In October of 1999, however, in view of the coming elections, three members of the ruling coalition were sentenced to three to five years in prison for taking bribes from a potential foreign investor. Since the change of government, opposition parties have been accusing the MPRP of corruption. Bureaucratic corruption, aided and abetted by the low salaries in civil service, remains a widespread problem, primarily in law enforcement, education, and medicine. Rumors about corruption are frequently spread by the private media but not pursued by the authorities. For some years now, Mongolia's international donors have been increasing pressure to improve the fight against corruption.

Mongolians enjoy civil liberties, which are guaranteed in the constitution and also exist in practice to a great extent. Reports on the human rights situation in Mongolia have repeatedly included reminders about poor conditions in Mongolian prisons (overcrowding, insufficient diet and medical care).

### 3.1.2 Political patterns of behavior and attitudes

(1) *Institutional stability*: In principle, democratic institutions are fundamentally supported by the relevant actors and the citizenry. Beginning in 1999, there was a conflict regarding the compatibility of a parliamentary mandate and government office. In 2001, this was decided in favor of compatibility. At the beginning of the assessment period, conflicts within the DUC as well as the president's refusals to appoint the prime minister repeatedly brought parliamentary work to a standstill. The 2001 constitutional amendment restricting the president's rights on this matter was intended to minimize the efficiency losses in future cohabitations.

Since the MPRP's victory at the polls in 2000, parliament has been working more efficiently again. This was also reflected in an increase of public trust in government institutions and policy. There are, however, problems with general institutional performance (scarce financial resources, limited human resources) that are also caused in part by the tradition of dependence on external donors. The administrative system is also strongly subject to the parties' patronage systems, to the extent that even low-level officials are replaced after every change of government.

(2) *Political and social integration*: Mongolia's party system consists of a group of various opposition parties and the MPRP, the successor to the Communist Party, which today has a social-democratic image. At the end of 2002, the country had three parties with approval ratings above 5 %: the MPRP, the Democratic Party, and the Citizens' Will Party. Of these three, the MPRP is the most rooted in the society.

With the aid of external financing and know-how, numerous associations and interest groups have formed in the past few years. Some of them are active, e.g. in the area of political education. Three trade union alliances represent workers' interests. Mongolia's political class acted in relative isolation from society until 1990. Traces of this political culture have remained, especially in the attitudes of political elites toward the rural population. The circle of political, civil, and academic elites is quite small, however, which promotes exchanges. Increasing social differentiation is hampering the reconciliation of opposing group interests in Mongolian society.

There are numerous civil-society groups, many supported by outside donors. Only a few groups are, however, represented across the country, a difficult feat

considering the vast expanses of land and the sparse settlement. Groups have formed in a broad spectrum of societal interests (welfare, women, health, etc.). Their degree of organization and networking continued to improve during the assessment period. Public approval of the democratic system is high. Almost 90 % still approve of the change in the political system, and 49 % were “very” or “somewhat” satisfied with the existing political system in November of 2002, an increase of 8 % since May 2000.

## **3.2 Market economy**

The economic transformation was already quite advanced before the assessment period, particularly with regard to the formal rules. The period between 1998 and 2000 was marked by economic difficulties including high budget and trade balance deficits, a banking crisis and increases in inflation. Since then, the macroeconomic situation has re-stabilized.

### **3.2.1 Level of socioeconomic development**

Mongolia is a low-income country. Since the mid-1990s, one-third of the population has been living in extreme poverty (income does not cover the necessary food expenses; 1998 Living Standard Measurement Survey). Around 50 % of the population is living on less than two dollars per day. Female-headed households are a particularly large group among poor families.

The collapse of many industrial enterprises at the start of the 1990s caused many Mongolians to return to semi-nomadic pastoral agriculture. Overgrazing and extreme climatic conditions over the last four years have increased the risk of poverty for the rural population. Social differentiation increased in the 1990s and seemed to stagnate during the assessment period. However, in comparison with other developing countries, inequality is not extreme.

### **3.2.2 Market structures and competition**

The foundations for market-oriented competition were created over the course of the transformation. Under DUC rule (1996–2000), the economy experienced another push toward liberalization, among other things via tax reductions and a temporary elimination of all import tariffs. After the MPRP resumed power, taxes were slightly raised again to help compensate for large budget deficits, which had risen to more than 10 % of the GDP. Despite wide-ranging liberalization, entrepreneurs are able to obtain advantages by exerting influence on ministers or parliament (for favors in licensing, exemptions, etc.), a fact that is undermining the standardized rules of the game.

The first law against unfair competition was passed in 1993. In 2000, a new, expanded law was approved. Because the population is so low, large companies (e.g. Erdenet Copper mine, Gobi Cashmere, beverages producer APU) frequently have a dominant position in the market. Due to liberal trade policies, they face foreign competition primarily from China.

Foreign trade is largely liberalized. Import tariffs average 7 %. Tariff procedures are frequently protracted, however, and corruption seems to be extensive among customs officials. Mongolia has been a member of the WTO since January of 1997. Its foreign trade ratio exceeds 100% of the GDP. This high ratio is explained by the small domestic market (low GDP per cap. combined with a small population), the high energy dependency of the country, and the dominance of mining in the monetary economy. Energy (mainly petroleum products) accounts for 20 per cent of total imports; but also most machinery, consumer goods, and non-animal based foodstuffs are imported. Cooper and gold together amount to 40 to 50 per cent of total exports, and account for between 20 and 30 per cent of GDP. At the same time, the Mongolian economy is suffering from the strong competitive pressure from China, which inter alia hinders export diversification.

The banking system is partly privately owned and partly state-owned. There are thirteen commercial banks. Substantial problems persist in the banking sector. For a long time, both loan interest and the percentage of uncollectible loans remained very high. In 1998, banking laws were tightened up (minimum deposits, bank supervision by the Central Bank), and several large banks were liquidated. The situation has improved during the past two years. Bank deposits and loans have risen sharply, and the first foreign credit institutions have become active in Mongolia. Mongolia has accepted the international standards, notably the Basle Agreement. The most important bank for the rural population, the Agriculture Bank, was turned over to USAID to manage at the end of 2000. Afterward, the amount of money it issued in loans increased sharply, with good payback rates. The bank is supposed to be privatized in 2003.

### **3.2.3 Stability of currency and prices**

The annual inflation rate fell under 10 % for the first time in 1998. It increased again slightly in 2000. The 1996 Central Bank Law established an independent Central Bank. The exchange rate is free and influenced to some degree by the Central Bank. The exchange rate is under revaluation pressure, primarily thanks to the strong influence of the Official Development Assistance (ODA). In general, monetary, debt, and fiscal policy are strongly influenced by international financial institutions, primarily the IMF.



Budget deficits are considerable, between 5 % and 15 % of GDP in the last five years. However, they are primarily financed by development aid (grants and loans) and thus do not immediately endanger macroeconomic stability. The debt started growing again primarily at the start of the assessment period.

### **3.2.4 Private property**

Privatization started at the beginning of the 1990s, prior to the creation of an institutional framework had been established. Meanwhile, important elements for such a framework have been established. Since 1991, three laws have been passed on corporate law, thus creating successively better “corporate governance” regulations. Property rights on non-pasture land have been regulated by law since 1995. The government currently plans to fully privatize non-pasture land; however, the issue is highly contested, and the policy planning process was rather poor. (Pasture land is not supposed to be privatized, but the laws need to be improved to prevent overgrazing). In January of 2002, a new civil code came into force. However, the judiciary often lacks capacity to properly deal with the increasing number of cases involving economic issues, which is confounded by frequent changes in the legal basis.

The private sector currently accounts for 75 % of the annual GDP. Privatization of the large-scale enterprises still under state control (Gobi Cashmere, and MIAT, the state-run airline) has been discussed for several years, but made no progress during the assessment period.

### **3.2.5 Welfare regime**

During the Soviet period, a broad network of state-run social security was set up that included pension payments even to nomads and generous child allowances as part of a pro-birth policy. During the transformation and after the Soviet revenue transfers dried up, this network was severely cut back. Uninsured risks for the population have seriously increased. Birth rates have dropped sharply in consequence (from 2.9 % annually in 1989 to 1.4 % annually in 1999). Mongolia nevertheless retains an unusually young population structure (approximately half of the population is under 20) to the present day, which poses serious challenges both for the educational system and for the employment market.

The great impoverishment of broad sectors of the population has put a strain on the informal social networks, those within families and extended networks of relations. Pension system reforms began in 2000. Unemployment benefits are minimal, and many jobless belong to the absolute poorest of the poor. Many of the unemployed do not even bother to register because of the minimal support provided. The low official unemployment rate is thus misleading. Unemployment

and poverty are the socioeconomic problems most frequently cited in polls. Risks for nomads have also been considerably increased by the cutbacks in state provisions, together with the strong climatic fluctuations (loss of animals in hard winters).

A health insurance system was introduced that guarantees at least basic insurance to broad sectors of the population, but it is especially the poorest sections of the population that fall through this net. Immunization rates remain high. Around half of the Mongolian budget is spent on education, health care, and social security, but revenues frequently are not sufficient to keep the system afloat. Reducing poverty and unemployment seems extraordinarily important for long-term assurance of this democratization. Literacy rates are currently falling, primarily for the rural population and the poorest population groups. This is a step toward solidifying the social cleavages that arose over the course of the transformation.

### **3.2.6 Strength of the economy**

During the 1980s, the Mongolian economy reached growth rates of 6.2 % annually. In the first half of the 1990s, economic performance shrank by a total of around 20 %. The GDP has been growing again since 1994, but growth rates remained minimal, primarily in 2000 and 2001. In addition to the extremely small domestic market and high transport costs (land-locked country with weak infrastructure, see Item 3.2.7), performance is primarily influenced by two other factors: First, Mongolia's few important export goods—copper, cashmere wool—are subject to highly fluctuating prices on the world market. Secondly, pastoral agriculture accounts for a high proportion of the GDP (30 %) and is subject to widely fluctuating climatic conditions.

Foreign direct investments have been on the increase since 2000. They are primarily related to raw materials deposits, such as new copper and gold mines. Exploiting these deposits will mean serious ecological risks for the fragile ecosystem, however. Conversely, the strengthening of the banking sector that has been observable for a few years must be seen as a very positive development, as is increasing approval rates for small loans, because this will promote diversification of the economy.

In the early 1990s, the balance of trade was even or positive, primarily due to strong reductions in imports. Since the end of the 1990s, however, it has been clearly negative and will remain so over the medium term, according to IMF estimates. National economic performance remains limited on the whole. Projections from the government and international financial institutions predict the economy will grow faster starting in 2004 (6 % annually). Regular, strong growth seems very unlikely, however.

### **3.2.7 Sustainability**

In Mongolia, people are very conscious of their dependence on natural resources. Environmental protection has been institutionally anchored in the government through the creation of its own ministry. Nevertheless, the economic transformation and impoverishment have led to a worsening of ecological sustainability. The herds were privatized over the course of the transformation, but access to pasture land has been inadequately regulated. According to the National Environmental Action Plan (2002), more than 70 % of all pasture land has degraded, primarily in southern regions.

Forested areas are increasingly shrinking. Widespread poverty is contributing to phenomena such as illegal logging. As an arid country, Mongolia is also hard hit by forest and steppe fires. Institutional and financial capacities for meeting such challenges shrank in the 1990s, which resulted in increased damages. Further exploitation of mineral resources (see above) also threatens to cause more ecological damage.

Human capital is considerable in relation to per capita income. (The UN Education Index is markedly higher than the Human Development Index.) State education expenditures are 8.4 % of the GDP. Reasons for this include the high percentage of school-aged children among the total population. However, the education level, especially of the rural population, continues to fall. At the elementary school level, school attendance has dropped from 94 % to 85 % of eligible children. The education system's physical infrastructure is increasingly obsolete and requires new investments. Especially due to very low wages, well-trained teachers are increasingly scarce, which likewise has a negative influence on the quality of the education sector. Research and development do not play a significant role; annual expenditures are about one-tenth of 1 % of the GDP, or roughly one million euros.

Mongolia's physical infrastructure is meager. There is a north-south train connection linking Russia with China. Mongolia has a total of 11,000 km of roads, of which barely 12 % are paved. In the coming years, a new East-West connection is supposed to be built, the so-called Millennium Line, improving access to remote regions of the country. Access to telecommunications at least improved in the urban population centers over the course of the transformation. Between 1990 and 2000, the number of land-line connections increased from 32 to 56 per thousand inhabitants. Government projects, in cooperation with donors and NGOs, are supposed to connect rural regions as well, particularly schools, to modern telecommunications networks.

#### 4. Trend

(1) *Democracy*: Important characteristics of a democratic political system (regular, free elections; freedom of speech; freedom of assembly; and freedom of association) were already in existence before the assessment period. Both positive and negative tendencies have been observed with regard to political participation. On the one hand, the civil society's organizational capacity further improved. On the other hand, the Mongolian electoral system has been the source of extreme seat allocations in parliament. As a result, the parliamentary opposition has been reduced to a practically meaningless role again since 2000.

The development of state structures to a working system that supports social and economic development has not yet been concluded and has sizeable deficiencies. The constitutional framework has continued to develop over the past few years, with strong involvement from foreign advisers. The ongoing changes, however, represent an additional burden on the already strained judicial system. Various forms of corruption have presumably continued to increase, while control mechanisms and institutions remain too ineffective. By the usual criteria—time since the last free elections, regime change, population and elite approval of democratic values—Mongolian democracy must be considered consolidated.

(2) *Market economy*: The country's development status has slightly improved over the last five years (HDI change: +0.019). This just means that Mongolia has finally reached its 1990 status again and compensated for HDI declines from 1990 to 1995. All in all, the Mongolian economy has been liberalized for several years. What it requires now are not additional reforms but, above all, the construction of working, efficient, and nonpartisan state institutions. The rules of the game, however, are still not the same for all economic participants. During the assessment period, the greatest successes were in strengthening the banking sector. Economic growth was rather low during the assessment period.

**Table: Development of socioeconomic indicators of modernization**

	HDI	GDI	GDP index	UN Education Index	Political representation of women	PPP per capita (\$, PPP)
1998	0.628	n. a.	0.46	0.74	7.9	1541
2000	0.655	0.653	0.48	0.85	10.5	1783

Source: <http://hdr.undp.org/reports/global/2002>

**Table: Development of macroeconomic fundamentals (1998-2002)**

	1998	1999	2000	2001	2002
Growth of GDP in %	3.5	3.2	0.5	1.1	3.0
Export growth in %	-18.7	-1.8	18.0	-2.4	15
Import growth in %	8.2	-2.6	19.2	2.5	10
Inflation (CPI, in %)	9.4	7.6	11.6	8.0	6.0
Unemployment in % <sup>1</sup>	5.7	4.5	4.6	4.7	3.5
Debt in % of GDP	78.1	91.4	86.3	82.9	88.0
ODA in % of GDP	21	24	17	n. a.	n. a.
Budget deficit in % of GDP	14.3	12.2	6.6	6.3	6.6
Current account in billions of \$	-129	-127	-153	-164	-174

<sup>1</sup> According to the 2000 census, real unemployment was 17.5%, see <http://nso.mn/eng/index.htm> (Census and Survey).

Sources: EIU Country Report 2002; [http://www.adb.org/Documents/Books/ADO/2002/stat\\_append.pdf](http://www.adb.org/Documents/Books/ADO/2002/stat_append.pdf); IMF Country Report Country Report No. 2002/252.

## 5. Evaluation of transformation management

### 5.1 Level of difficulty

The level of difficulty is considerable given the low economic development level. Positive characteristics are the high level of education (UN Education Index: 0.85) and the society's ethnic homogeneity. At the beginning of the transformation in 1990, social homogeneity was also high; during the assessment period a great deal of social differentiation developed.

Although civil involvement does not have a long historical tradition in Mongolia and is somewhat hampered by the low per capita income, it has unfolded to an astounding degree since 1990. External financial support and organizational aid contributed significantly toward this goal. When the constitution was approved in 1992, Mongolia created a fundamental, democratic structure that the relevant actors have treated to a great degree as binding. Deficits persist, however, in the areas of the rule of law, as well as institutional stability and efficiency, including curbing corruption.

### 5.2 Reliable pursuit of goals

During the assessment period, substantial changes occurred to the social and economic policy objectives, and above all to the preferred instruments for

achieving them. Both the DUC and MPRP governments' fundamental objectives were economic growth and sustainable reductions in poverty. To achieve these goals, the DUC placed its confidence primarily in further radical liberal economic reforms such as minimizing all import tariffs and reducing taxes. This policy approach, combined with falling world market prices for Mongolia's most important exports, led to sizeable increases in the budget deficits and to further increases in unemployment and poverty. When the MPRP took power, on the other hand, it emphasized better social security and a more gradual continuation of the reform process.

During the second half of its term in office, i.e. after 1998, internal conflicts within the DUC government increased until it was scarcely able to pursue any long-term objectives. When the MPRP came to power in the summer of 2000, many hoped this would lead to more effective political leadership. Hopes rose not only because this marked the end of a conflict-laden cohabitation (MPRP president and DUC government), but also because many MPRP politicians have long-term experience in administration and as decision-makers.

The MPRP increased the tax burden for citizens and businesses. While budget deficits were reduced, the strain on the fragile Mongolian economy was great. Observed economic indicators show contradictory tendencies. One key problem for Mongolian governments is heavy dependence on foreign donors and thus on their priorities. This has both positive and negative effects on the orientation toward long-term goals and consistent pursuit of those goals. Foreign donors' priorities are subject to change, and external support in conjunction with global economic cycles is also subject to fluctuations.

The changes in government have thus resulted in substantial alterations to reform policy. Mongolian electoral law produces even more extreme parliamentary majorities than the British system, thus creating favorable conditions for radical policy changes. Mongolia is not a consensus democracy. The extensive changes in tariff and tax policy during the past five years have resulted in a marked reduction in the reliability of expectations for economic actors.

A sizeable discrepancy also persists in Mongolia between the programs, strategies, and laws passed, and their implementation. This discrepancy is increased by the extensive cooperation with external donors. Thus the National Poverty Alleviation Program implemented from 1994 to 2000 (in cooperation with UNDP) did not succeed in reducing poverty, for reasons that included inadequate coordination with other political areas such as economic and employment policy.

### **5.3 Effective use of resources**

Human, financial, and organizational resources are scarce. Ministries and parliamentary committees have only few trained personnel, including advisors. On the positive side, a parliamentary system saves resources because it does not lead to a phenomenon frequently observed in countries of the former Soviet Union, a doubling of government functions within the presidential administration. Overall, however, scarce resources available are being used only moderately effectively.

Budgetary oversight by Parliament and an independent court of auditors remains underdeveloped. A court of auditors was set up in 1995. An ADB project has been working since 1999 to strengthen the court's function. As mentioned above, budget deficits swelled again at the end of the 1990s but have since been reduced. Debt increased between 1997 and 2001 from 60 % to 90 % of GDP. A significant portion of aid is being used to pay for ongoing expenses and not for investment.

In September 2000, a program initiated by the UNDP was passed called "Good Governance for Human Security." On the one hand, positive effects were produced by the external influence and by the focus, increased in the last few years, on building up working and corruption-free institutions. On the other hand, the extensive cooperation with donors is putting considerable strain on scarce resources and proving a distraction from the government's actual responsibilities. Corruption has increased a great deal since the start of the transformation and remained at this level during the assessment period. Mongolia has started working out an anti-corruption strategy, and plans exist to create an Independent Anti-Corruption Commission (ICAC).

Rebuilding the country's cultural heritage played an important role primarily at the start of the transformation process. Mongolia is one of the few countries in the world that has retained a strong traditional nomadic culture. This is both an important heritage and a considerable challenge for socioeconomic development. Political elites in Ulaanbaatar frequently have an ambivalent relationship with this traditional way of life and tend to consider it backward. The current regime's goal is to reduce the nomadic portion of the population from its current 30 % to 10 % and to increase population density in regional centers. Awareness of historical persons, particularly Genghis Khan, generally has an integrating effect.

### **5.4 Governance capability**

During the assessment period, political change was triggered primarily by changes in government and less by learning processes within a single government. The MPRP's learning process has been remarkable. She gave herself an explicitly social-democratic program in 1997. Conservative currents that tend to represent a

more *dirigiste* policy do remain within the party. Both political camps (MPRP and DUC) have shown a high capacity for learning from international standards. At the same time, both political camps contain patronage-based networks for whom advantages are created. This combination means that official language used frequently does not correspond to actual deeds. Generally, a certain learning process seems to be taking place and reaching the conclusion that the country's problems cannot be solved with standard formulas or only with programs from international donors. The government hardly has any resources to improve the markets' distributive efficiency. Various interventions (taxes on exports of raw cashmere, support of the currency) have enjoyed little success on the whole.

The governments' political authority does not seem to be a problem. The cohabitation from 1997 to 2000 led to substantial friction and associated loss of authority for the government. This hindered both continued implementation of reforms and also led to an overall reduction of government efficiency. The MPRP has held all the government's key positions since 2000 (government, presidency, and majority of the local assemblies). It has rarely attempted constructive cooperation with the opposition for that reason, but it would be wise to do so on the long term.

## 5.5 Consensus-building

All the relevant political camps in Mongolia are pursuing fundamentally similar goals, i.e. a prospering market economy and a democratic political system. The most important political conflicts are the role of the state in a market economy, evaluating and measuring social compensation, and the governing style (transparency, and keeping a close relationship with the people). In other words, conflicts exist about the way to achieve the goals but not about the goals themselves. The substantial exclusion of the opposition from parliamentary politics (see above) after the election results of 2000 is leading to a more confrontational relationship between the two big political camps, however. Anti-democratic veto actors do not exist in Mongolia. Older and conservative politicians who might still be attracted to a communist system are incorporated into the democratic consensus through the MPRP.

The most significant social cleavages run between rich and poor, and between urban and rural. Under the socialist system, the state enforced solidarity. State solidarity networks were seriously hollowed out during the transformation. Attempts are being made at this time to reinforce networks corresponding to the new economic system and also to partially re-integrate the informal sector into public insurance systems. In rural society, after three exceptionally hard winters societal resources are not sufficient for taking care of the thousands of families left destitute each year by the loss of their herds.



As the politically violent period of Mongolian history took place some time ago (primarily in the 1930s), direct reconciliation between offenders and victims does not play an important role in current Mongolian politics.

## 5.6 International cooperation

Mongolia's international situation is marked by its geographic situation between two dominant neighbors, the People's Republic of China and the Russian Federation. There is a history of mistrust of China and the fear of being economically and demographically assimilated like Inner Mongolia, which is now an autonomous Chinese province currently inhabited by approximately 3.6 million Mongolians and 16.4 million Chinese. The various governments have, however, followed a fundamentally pragmatic policy with regard to their dominant southern neighbor. Relations to Russia have intensified again in the last few years. President Putin paid a state visit in November 2000, and Prime Minister Kasyanov visited in March 2002.

Mongolia has to seek good international cooperation, both because of its geographic location between two dominant neighbors and for financial reasons. Mongolia is a member of many international organizations and has signed standard international agreements. Annual donor meetings have been taking place since 1993 and incorporated civic groups during the last few years. Sizeable deficiencies persist, however, in the coordination of development cooperation efforts, both on the Mongolian and international sides.

## 6. Overall evaluation

In view of the starting conditions, this assessment reaches the following overall conclusion regarding the status, evolution, and performance of the actors:

*(1) Starting conditions:* The economic prerequisites for the political and economic transformation as well as for the construction of a working state in a market-economic democracy were and are difficult. Moreover, the considerable geographical challenges must be cited: Mongolia is a land-locked country, its territory is barren and subject to extreme climatic conditions (aridity, extremely cold winter temperatures), and settlement is extremely thin. These aspects result in special challenges for the provision of physical infrastructure and public services. Mongolia also had neither democratic prior experience nor a stable democratic "neighborhood."

On the other hand, favorable starting conditions included the ethnic homogeneity and the high level of education compared with per capita income. During the assessment period, the already impressively advanced political and economic

transformation continued to progress. Problems yet to be resolved include building a working state, reducing corruption and overcoming the poverty and social inequalities that arose over the course of the transformation.

(2) *Current status and evolution:* During the past five years, the democratic system stabilized, but without important qualitative improvements. Another peaceful government change took place. At the same time, the electoral system contributed to excessive exclusion of the opposition from Parliament. Electoral reform thus appears important but has not been initiated yet. In terms of presidential powers, an important constitutional dispute was resolved positively during the assessment period. The decision to permit persons to hold government office and parliamentary mandates also seems very reasonable, considering the lack of highly qualified political personnel.

In terms of the market-economic transformation, the government change was associated with a change in pace and strategy of reforms. The market economy's regulatory structure has continued to improve. However, large deficits persist in its implementation by the government, administration and the judicial system. Corruption and patronage are widespread phenomena, and the discrepancies between formal and informal regulation are considerable. Mongolia made important progress in cooperation with foreign donors in the banking sector. It seems that lessons have been learned from the failures of earlier programs (NPAN, 1994-2000), in which microcredit components were insufficiently effective.

(3) *Management:* Given Mongolia's extremely scarce resources and the high dependence on foreign actors, its governments generally lack much room to maneuver. The Mongolian political elites' relative management performance is not uniform across the board. The DUC governments under different prime ministers tended to pursue radical economic reforms with no regard for their popular acceptance. Especially in the government's final phase, internal coalition disputes overwhelmed its ability to control events. In 2000, the MPRP campaigned on the strength of populist election promises, including rapid income growth. As the ruling party, on the other hand, it is especially subject to pressure from international donors demanding increases in electricity and heating prices, which will put further burdens on the Mongolian population.

## **7. Outlook**

Important aspects of the political and economic transformation in Mongolia have been achieved. Economic transformation, however, is not the same as economic growth and prosperity. Persisting economic difficulties and the associated poverty and inequality constitute a long-term threat to the democratization that has been achieved. Given the Mongolian economy's high dependence on exports and the

fluctuating world market prices for its few important export goods, stable long-term growth will only be achievable with more diversified Mongolian products and exports.

Under the pressure and influence of foreign donors, the situation with regard to corruption might improve once again in the coming years. Appropriate programs have been initiated. In general, the donors have undergone a learning process during the past few years about the significance of institutions, and this could contribute to better results from development programs.

The market economy's regulatory framework improved during the assessment period (new civil code, competition regulations, and bank supervision). Step-by-step improvements in implementation thus appear possible. Fundamentally, it remains important to reduce the discrepancy between strategies and programs, on one hand, and implementation on the other.