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Mongolia, the Next Leg of Growth in Asia

Executive Summary:

- Over the past ten years, Mongolia's gross domestic product (GDP) has been growing at an average rate of 8% per annum. In 2011, the country has become one of the fastest-growing economies in the world with its GDP growing at 17% year on year (yoy). However, **in order for Mongolia to sustain its growth and fully benefit from its untapped mineral deposits, significant investment in infrastructure** (roads and railways**), energy network** (power plants and power grids) **and related value-added sectors** (e.g. mineral processing) **is required.** This presents unique opportunities for long-term investors to capitalize on Mongolia's potentially substantial economic growth.

- **Investment opportunities:** Aside from investing in bonds offered by the Development Bank of Mongolia (the first foreign currency bond was offered in March 2012 and investor interest was immense), **we believe the case for private sector investment is strong** as the country would need to maintain its liability at a reasonable level under the Fiscal Stability Law passed in 2010.
  - **Road and railway infrastructure:** At least 398 kilometers (km) of roads are up for tender or under planning in 2012 in the Dundgobi and Southgobi Provinces. Moreover, approximately 5,684 km of new railways are to be built between 2011 and 2014.
  - **Energy network:** We believe there is a huge need for capacity addition in electricity-generating facilities and the power grid network in coming years, as Mongolia's electricity demand is estimated to double from approximately 800 megawatt (MW) in 2011 to approximately 1,600 MW in 2020. Furthermore, electricity demand could reach 3,000 MW by 2030.
  - **Value-added sectors:** Sainshand Industrial Park (SIP), a US$9.86 billion (bn) project, would consist of a variety of value-added factories such as a coke plant, a copper smelter, an iron ore pelletizing plant, an iron ore plant, a cement plant and a coal gasification plant. When most of the processing plants in SIP become operational, coal will be transported from the Tavan Tolgoi mine, iron ore from the Tomertei mines and copper concentrate from the Oyu Tolgoi mine to produce metallurgical coke, iron ore pellets and copper anodes respectively.

- **Mongolia's competitive advantages:** Mongolia has some of the largest untapped mineral resources in the world, including copper, uranium, coal and gold. Together with a young and growing working population, we believe Mongolia is in a solid position to transform itself into an industrial economy.
  - **Rich natural resources:** Oyu Tolgoi and Tavan Tolgoi are one of the largest copper and coking coal deposits in the world respectively. We believe there will be more investment opportunities to come as Mongolia develops its not yet exploited western regions.
  - **A young and growing population:** About 58% of Mongolia's population is under age 30, and 27% of whom is under 14. In addition, working population accounts for about 69% of the population. We estimate that the proportion of working population would continue to grow until it reaches over 75% in 2022.
  - **Ease of doing business:** According to the Doing Business survey 2013 by the World Bank, Mongolia's overall ranking is 76th out of 185 economies (up from 88th in 2012), higher than its neighbors, namely China (ranks 91) and Russian Federation (ranks 112). In particular, Mongolia ranks high in protecting investors (ranks 25), enforcing contracts (ranks 29) and paying taxes (ranks 70).

- **Key challenges on Mongolia's economic growth:** Key challenges include a slowdown in the growth of the Chinese economy (China accounted for 93% of Mongolia's exports in 2011) and inflation (at 16% as in August 2012). However, we note that the Mongolian government is proactive in tackling these issues, including the implementation of the "third neighbor" policy to build closer ties with countries other than Russia and China and passing the Integrated Budget Law and Fiscal Stability Law to be more disciplined in fiscal spending and avoid hefty public debt.