

New mining projects will see economy soar

Contract revenues transform Mongolia's landscape

Dependent on mining for a third of its GDP, the Mongolian economy is set to expand even more, with the country's National Development and Innovation Committee predicting growth of around 20.8 percent within three years, thanks to new mines that are coming on-stream.

With plentiful and largely untapped natural resources, mining holds the key to Mongolia's economic sustainable development in the coming years.

The potential transformation of the country on the back of a flourishing mining industry will be huge; energy plants, railroads and rural airports will need to be upgraded to support production, and there will be a strong impact on related sectors, such as transport, energy, construction, and finance.

Subsequent movement of the largely rural population to new growth areas will also impact on the building and staffing of schools,

houses, and hospitals.

Responsible for 80 percent of the country's export returns and a significant provider of jobs, the mining sector needs careful management if it is to fulfil its potential and provide the revenues needed to develop the country.

Dashdorj Zorigt, Minister of Minerals and Energy said: "For the future, we are going to work hard to ensure that deposits that have been discovered in Mongolia come to production and that these deposits benefit the country's economy and the living standards of the population. Secondly, we will create significant national companies that will in turn develop energy and resources.

"We are also looking to make sure these projects benefit things like transit transportation, and the external factors that influence the country's economic course."

Erdenet, the largest state-owned mining company is responsible for



Dashdorj Zorigt,
Minister of
Minerals and
Energy

30 percent of the country's GDP and is a Mongolian success story. A Russian-Mongolian joint venture since the 1970s, Erdenet is now looking to be listed on the Hong Kong Stock Exchange.

Setting new precedents

This year, the government finalized a deal with Rio Tinto and Ivanhoe Mines to mine Oyu Tolgoi (OT) in the south Gobi desert, which has the largest undeveloped copper deposits in the world.

"This is a major investment project that will affect the country's economy in a very significant way from 2013, when the mine is due to come into production," Zorigt said. "We expect the investment plan of the project to



S. Baldandorj,
General
Director of
Mandal-Altai
Group

be around \$700 million and create significant jobs and businesses for Mongolian companies here."

The Oyu Tolgoi company, which is 34 percent state-owned, represents an unprecedented boon for the economy, with GDP slated to rise by a third, year on year. As Minister of Finance Bayartsogt Sangajav said: "I was the chief negotiator in the last stage of the Oyu Tolgoi agreement and finalized the agreement representing government's side. This was a difficult task because of the various interests that were represented from both the government but also between the parties involved in the negotiation. It was a difficult task, but I couldn't be more happy or proud about the achieved result."

The agreement will bring much-needed jobs, infrastructure, education and training initiatives and of course, wealth to the country.

It will also boost relations with China, as the Governor of the central Bank of Mongolia Lkhanaasuren Purevdorj observed: "The OT project will expand the Mongolian Chinese Partnership and increase trade between the two nations."

Another lucrative project, Tavan Tolgoi, boasts the largest undeveloped coal reserves in the region, with an estimated 7 billion tons of coal. Tavan Tolgoi will remain 100 percent state owned, operating as Erdenes MGL and there has been substantial interest from contractors around the world.

"We are working to reserve an opportunity to create capital for our citizens, develop capital market, connecting them with the major creation and projects and establishing national companies," said Minister Zorigt.



Salkhit wind farm developed by Newcom.

"Only if 'Erdenes MGL' remains national and leads in the region and world, we will develop.

"Let's take an example from Hyundai, Mitsui. They are all state-owned companies, but they can distribute their wealth to the people through shares. Now they are recognized around the world.

Erdenet represents Mongolia at the world capital market. Likewise, 'Erdenes MGL,' on an even bigger scale, can represent Mongolia to the world."

area of China, where they hope to become a major supplier. It will be financed 100 percent by the company.

General director of Mandal-Altai Group LLC, S. Baldandorj, said: "Once the refinery is built, we envisage producing a million tons of coking coal per year."

The Mongolian government is now looking at developing capital markets to better facilitate FDI. "Commercial banks are serving as major sources of lending to our



Mongolia is a country that is looking to develop its energy and resources sector through mutually beneficial cooperation between local companies and foreign investors."

DASHDORJ ZORIGT
MINISTER OF MINERAL RESOURCES AND ENERGY

Established in 1990, Mandal-Altai Group LLC has interests in construction—it recently rebuilt Chinggis Khaan airport—services, and agriculture, as well as mining. Mandal Khuder LLC, its mining subsidiary, owns special licences for a coalmine in the Gobi-Altai region, some 156 kms from the Chinese border. The company has extracted more than 6,000 tons of coal since 2005, and is expected to extract 12,000 tons this year alone.

A coal preparation plant is being built in Hami, in the Zhangjiagang

projects, but both domestically and externally we have to look to developing our capital markets, making sure the domestic markets are in place and available for people wishing to invest their money this way," said the mining minister.

"We have announced the international bid for our stock exchange and are planning to privatize this in the near future. We also want to make sure Mongolian companies can access the external capital markets and are able to draw resources from there."

Commodity	Annual Production				Proven Reserve	Probable Reserve
	2006	2007	2008	2009		
Coal	8mt	8.8mt	9.8mt	13.2mt	20bt	152bt
Copper	0.37mt	0.37mt	0.36mt	0.37mt	67.3mt	1.2bt
Gold	22t	17t	15t	10t	136t	125,000t
Iron Ore	0.18mt	0.26mt	1.39mt	1.38mt	264mt	1.6bt
Uranium	0	0	0	0	-	62000t (resource)

Major players				
GOLD	COAL	COPPER	IRON	URANIUM
Centerra Gold MAK Darkhan Steel Mongol Gazar	Tavan Tolgoi South Gobi Energy Resources QGX Mongolia Energy Corp. Peabody Hunnu Prophecy	Erdenet Oyu Tolgoi	Darkhan Steel Iron Ore International Mining North Asia Resources	Cameco Areva

Safeguarding the economy

Tasked with promoting the balanced and sustainable development of the economy, Bank of Mongolia functions independently of government to ensure price stability and a robust financial sector.

Since the global crisis in 2008, which hit Mongolia hard due to a sudden and precipitous slump in mineral prices, the Bank has recovered gross international reserves to the tune of \$1.3 billion, thanks to strong macroeconomic policies and the support of the International Monetary Fund. By December 2009, annual inflation was contained at 2 percent and new reforms have been introduced.

"Bank of Mongolia welcomes a consolidation of the sector which would create a more sound and competitive environment for strategic foreign investors," Bank of Mongolia Governor Lkhanaasuren Purevdorj said.

"The revision of the deposit guarantee system, from general coverage to a more classical one, the capital adequacy ratio requirements increase for banks from 10 to 12 percent and enhanced banking supervision would further stabilize the financial system. Bank of Mongolia is monitoring the credit quality closely and stands ready to take action, as needed, to secure stability and bolster confidence in the banking system."

Optimistic economic forecast

With the country's mining sector recently developed for expansion, the economic forecast is optimistic for this year. Expansion will bring new investment, jobs, export income and a surge in government revenue that could fund social and development spending, but there will be challenges, as the governor explained.

"Increased demand for labor and materials, plus higher incomes and public spending, could easily spur inflation to double-digit rates, while wages in mining and public services are likely to go up," he said. "An increase in the role of mining in the country would also amplify the economy's vulnerability to fluctuations in global copper prices. Managing windfall revenue and smoothing public expenditure will be critical to avoid such boom-and-bust cycles."

The government has proposed strategies to combat these challenges, including the introduction of a fiscal responsibility law. It has also put in place a stabilization fund to manage revenue volatility, although it will take



Lkhanaasuren Purevdorj,
Governor of
Bank of
Mongolia

several years to build up enough reserves to buffer the economy.

A liberalized economy

As one of the most open economies in the region, Mongolia benefits from a liberalized financial system and favorable investment legislation. The absence of capital controls would, Governor Purevdorj believes, provide excellent and competitive investment

opportunities.

"Mongolia is a country on the point of transformation. It has some of the richest mineral deposits of copper, coal, gold and uranium reserves, rivaling those of Kazakhstan and Australia," he said. "As these resources are brought to market, Mongolia stands a good chance of becoming the fastest-growing economy in the world over the next decade.

"The government has already taken action to pursue a policy to support foreign investors' interests in Mongolia by creating an attractive legal environment, upgrading the economic competitiveness of the country, making trade more efficient, increasing investment and involving foreign investment in proper ratios for the implementation of mining and other projects."

The recent abolition of the windfall profits tax law is a further proof of the government's willingness to promote an attractive legal environment for foreign investors in the mining sector. Parliament is also expected to adopt an integrated budget law and a fiscal stability law that will put a framework for managing mining revenues in place.

Toward a strong financial sector

While Mongolia's financial system has been growing rapidly, commercial banks hold 90 percent of the financial sector's assets. Insufficient development of the sector has been a key constraint to stable and broad-based economic growth.

Early this year, Bank of Mongolia was given more powers to regulate the financial sector. A restructuring strategy has been submitted to improve the functioning of the banking sector and put in place a transparent mechanism for timely and cost-efficient bank resolution techniques. Meanwhile, the Financial Regulation Committee, set up in 2006, has undertaken several initiatives to improve the legal, regulatory and supervisory environment of the non-bank financial sector.

Oyu Tolgoi: A catalyst for change

The Oyu Tolgoi copper-gold project, Mongolia's largest ever mining development, marks "one step forward for the economy", according to the President of Mongolia, Tsakhiagiin Elbegdorj.

Following a landmark agreement between Canada's Ivanhoe Mines Mongolia Inc and Rio Tinto, which took effect in March this year, the South Gobi desert mine will become operational in 2013.

Its lifespan has been set at 65 years, and it will require an initial capital outlay of approximately \$5 billion, making it not only the largest mine development project, but also the largest foreign investment in the country's history.

The discovery of major mineral deposits in 2001 by Ivanhoe was made after an intensive exploration program in the country. The local company was renamed Oyu Tolgoi LLC in December 2009, and today, the project is 34 percent owned by the Mongolian government.

Mining a brighter future

The mammoth project will be a catalyst for Mongolia to expand its manufacturing and industrial sectors.

Mongolia's gross domestic product is projected to rise by an average of 34 percent per year, and national employment levels are slated to go up by 10.3 percent a year. Of the 4,000 jobs created for the construction phase, 67 percent have gone to Mongolian nationals.

"Oyu Tolgoi respects the needs and customs of the local communities and will ensure Mongolia and Mongolians benefit from this investment," said Keith Marshall, CEO of Oyu Tolgoi and a "mining nomad" who has been in the business for over 30 years.

The project will benefit regional infrastructure, generating new road links, electricity generating stations and power transmission lines.

Oyu Tolgoi is committed to community support initiatives, with priorities in education, health, rural business, small and medium enterprise and herder-support programs.

The company recently signed a Memorandum of Understanding with the Ministry of Education which will see Oyu Tolgoi invest a minimum of \$58 million over the next five years to develop a strong Mongolian workforce suitable for Oyu Tolgoi and other mining projects throughout Mongolia.

Plans are afoot for the setting up



Keith Marshall,
CEO of
Oyu Tolgoi LLC

of two mining-focused professional training and vocational centers and a student scholarship scheme.

"It is a great pleasure to be in Mongolia and to be dealing with such a phenomenal country with so much tradition, pride and history," Marshall said.

"Within Oyu Tolgoi and Tavan Tolgoi, a coal mine also in South Gobi, we have world-class mineral deposits that could run for 50-100

years. Mongolia has a population of 2.7 million people. It is very unusual to find two major deposits like that coupled with such a small population. The per capita potential is enormous."

High production yields

With the future mine sitting just 120 km north of the Chinese border, and relations continually being strengthened between the two countries, China is an important potential customer.

To facilitate access, Oyu Tolgoi LLC will be developing a road system to link the mine to China at the point where many of the goods and services come in.

"We have a huge advantage in relation to the low freight costs involved, compared to other countries that have to put their concentrate on a ship for 6-8 weeks for example," Marshall said. "We haven't yet developed our marketing strategy, but we will certainly be in discussion with China."

Oyu Tolgoi believes production yield will be somewhere between 450 and 555,000 tons of copper, and around 650,000 ounces of gold per year for the first 10 years and that the mine may become one of the three largest copper mines in the world.

In July this year, the company began construction on a \$1.2 billion copper-gold concentrator. One of the most significant parts of the Oyu Tolgoi mining process, the concentrator enriches mined copper ore to produce a concentrate that is then sold to clients for smelting and refining. Once up and running, the device will treat up to 100,000 tons of ore a day.

"The concentrator will be one of the best of its kind," Marshall said. "We are aiming to use only world-class technology at Oyu Tolgoi."

Oyu Tolgoi has pledged to ensure Mongolia's sustainable development and will be complying with local and international standards to safeguard the South Gobi environment and the mine's employees.



www.ot.mn