CHAPTER 2
A NEW ERA: 1991–2000

Country at a Glance

After 7 decades of close ties with the Soviet Union, the 1990s ushered in a remarkable period of transformation as Mongolia began a shift away from a centrally planned system to one based on market economy principles.

With the end of aid from the Soviet Union in 1991, financing for energy, food, raw materials, and capital equipment abruptly ended, and subsidies that had sustained state-owned enterprises were terminated. Public social services were sharply curtailed, living standards slumped, food shortages ensued, and poverty increased. Electricity and other basic utility services were cut off for lengthy periods in some regions.

The end of the command economy affected different sectors in many different ways. Herders privatized their herds and increased the number of animals to take advantage of price trends, while the service sector expanded significantly. Many new small private enterprises were established, although they faced financing hurdles due to a lack of access to credit.

Demonstrations in Ulaanbaatar. Mongolia made a peaceful transition to democracy in 1991 (photo by Monsudar).
Recognizing the need for rapid and major change in the face of economic distress, the Government of Mongolia launched a series of reforms to privatize state-owned enterprises, end the monobank system, liberalize prices and exchange rates, introduce free trade, remove capital controls, revise the tax system, restructure the civil service, and ease rules on setting up private businesses. The new Constitution, adopted in 1992, paved the way for Parliamentary elections, the creation of a free press and judicial reform, as well as the establishment of private land ownership for the first time in Mongolian history.

These dramatic changes of swift liberalization, deregulation, and privatization caused significant economic instability in the first years of the transition period. There was a 20% drop in real GDP between 1990 and 1993 while the inflation rate exceeded 325% and unemployment reached 9%. Poverty rates also spiked, as the government cut the funding of social welfare programs and undertook a mass voucher privatization program, which transferred over 40% of state-owned assets, primarily in state farms, cooperatives, and small and medium-sized enterprises, to the private sector from 1991 to 1994.

The need for urgent financing and expertise to stabilize the economy and push forward reforms meant external support was required so Mongolia approached a range of development partners, including the Asian Development Bank (ADB).

Following the sharp contraction from 1990 to 1993, the economy recorded stable growth for the rest of the decade. The second half of the decade saw rapid development of the private sector, especially in the extractive industries with the passage of the Minerals Law in 1995, as well as the service sector, which accounted for about half of GDP by 2000.

This commendable progress was interrupted by the onset of the Asian and Russian economic crises in 1997 and 1998, which led to a sharp drop in demand and prices for the country’s main commodity exports, copper and cashmere, causing a slump in export earnings. The fiscal position deteriorated for 3 years in a row starting in 1997, and the banking sector came under severe strain from the export shock, causing a drawdown on bank deposits and a rise in nonperforming loans. In the last 2 years of the decade, eight of 20 commercial banks closed.

Despite these stresses, the economy was still able to post positive real GDP growth of over 3% in 1998 and 1999. As Mongolia moved into the 21st century, it looked forward with hope, having made significant strides towards creating a market-based economy, with the private sector accounting for 75% of the economy by the turn of the decade.

However, much unfinished business remained in areas including job creation, poverty reduction, infrastructure development, financial sector reform, and unresolved environmental problems.

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2 Footnote 1, pp. 239–240.
4 Footnote 1, p. 20.
Fresh pastures. Animals and herders on the move to new pasture land in Khovd aimag (photo by Oktyabri Dash).

Demchog monastery. The monastery, in Khanbogd soum, Umnugovi aimag, was built in 1836 by the Holy Lama of the Gobi Danzanravjaa (photo by Oktyabri Dash).
Ulaanbaatar in the 1990s. The traffic was light with mostly Russian cars on the streets, a legacy of 7 decades of close ties with the Soviet Union (photo by Monsudar).
Shifting to a New Economic System — Personal Views

The severing of financial support and preferential trading arrangements with the Soviet Union in 1991 was a pivotal moment for Mongolia as the economy fell into a recession and there were widespread shortages of key goods including food, fuel, medicines, and industrial materials.

Recognizing the need for outside assistance, the Government of Mongolia reached out to the international community.

An initial Mongolia Assistance Group Meeting held in Tokyo in September 1991 under the joint chairmanship of the Government of Japan and the World Bank, saw multilateral institutions, including ADB, come together to discuss how best to provide and coordinate assistance.

The shift to a market-oriented economy led by a vibrant private sector, after decades of central planning under the Soviet Union, required a complex overhaul of existing macroeconomic policies and legal frameworks, improved governance, and close cooperation with donor partners.

Overseeing this process were leading government and financial officials, who recall the challenges they faced, the priority actions they targeted, and the role that ADB and other international financial institutions played in the country’s metamorphosis.
Mongolia and ADB — First Encounters

Ochirbat Punsalmaa
President of Mongolia, 1990–1997

When Mongolia made the decision to embrace democracy and transition to a market-based economy at the start of the 1990s, it faced extremely tough challenges.

A new Constitution had to be drafted and adopted, and over 500 new laws had to be enacted to create the legal framework for the new system. This had to be done at a time when there was a shortage of educated and experienced professionals with the skills needed to draft market economy laws.

Following the adoption of the Constitution establishing representative democracy, elections were held and Parliament and the government were formed.

Given the extremely difficult economic circumstances we were facing as a country, a decision was made to approach international financial institutions for assistance. During my visit to the United States in 1991, I met with the management of the International Monetary Fund (IMF) and the World Bank and requested that Mongolia be admitted as a member. These requests were accepted, and soon after we also joined ADB. As a result, we were able to receive direct international and regional financial support for our economic transition.

This was critical as the country had almost no national economic and financial savings following the dissolution of the Soviet Union and the Council for Mutual Economic Assistance.

With the support from international financial institutions, Mongolia was able to overcome the difficult transition period in a relatively short period time, moving from economic downturn to growth.
Our relationship with ADB, our largest and closest multilateral partner, has been especially fruitful, and there have been tremendous achievements and results over the past 30 years. Working together, we have carried out wide-ranging policy reforms and improvements in the banking sector, upgraded infrastructure, emphasized environmental protection to improve air quality in Ulaanbaatar, expanded agricultural production, and taken steps to deepen Mongolia’s economic integration in the region.

Our partnership with ADB has resulted in projects that strengthened the quality of education, connected citizens to water supplies, upgraded urban services, and provided social welfare for people with disabilities. ADB is also an important partner for Mongolia’s drive to green its economy, with an ongoing project to turn Ulaanbaatar’s ger areas into affordable, low-carbon, climate-resilient and livable eco-districts, including the construction of thousands of affordable homes.

I am grateful for ADB’s ongoing support in areas including agriculture, energy, finance, health, transport, and social security, which will open up new opportunities, and which represent a strong vote of confidence in Mongolia’s future.
Laying the Groundwork for Change

Molomjamts Demchigjav
Governor of the Bank of Mongolia, 1992–1996
ADB Governor for Mongolia, 1992–1996

At the initial stage of Mongolia’s shift to a market-based economy, the country was in a difficult situation, with the end of aid from the Soviet Union causing huge disruption to supplies of imported goods, along with shortages of food and other consumer goods. There were no foreign currency or cash reserves, inflation was extremely high, and Mongolia was effectively insolvent and in default on its debt.

This was the backdrop against which the country reached out to international financial institutions for assistance in 1991. Mongolia joined ADB that year, and as the Governor of the Bank of Mongolia, I served as Governor for Mongolia in ADB until November 1996.

In this initial period, I was involved in laying the groundwork for the areas where we would work together. That included establishing priorities for assistance that matched Mongolia’s immediate needs with ADB’s own goals.

At ADB’s Annual General Meeting in 1992, I met with ADB President Kimimasa Tarumizu and expressed interest in working with ADB to address pressing banking and infrastructure needs. The following year, President Tarumizu visited Mongolia, meeting the Prime Minister and heads of relevant ministries. This was an important visit for establishing the initial areas for ADB operations in Mongolia, and paved the way for assistance that helped alleviate shortages of basic imported goods and fuel.

I also had important meetings with President Tarumizu’s successor, President Mitsuo Sato, where we discussed other areas of cooperation, including civil aviation and communications.

Along with these top-level contacts, there were regular ADB missions to Mongolia 3–4 times a year for fact finding and research.

Critical Financial Reforms

Preparing the financial sector, including banks, to operate along market-economy principles was one of the most immediate challenges Mongolia faced.

ADB’s first technical assistance helped provide capacity building support for the establishment of the Mongolian Stock Exchange. This was followed by assistance to establish a two-tier banking system and to set up supervision functions at the Bank of Mongolia to oversee the activities of commercial banks.
Infrastructure Upgrades

Upgrading underdeveloped air and road networks to improve access to foreign markets and boost trade was another important government priority in the first phase of the transition.

At the country’s gateway airport, Buyant-Ukhaa in Ulaanbaatar, the runway in the early 1990s could not accommodate large commercial aircrafts. This resulted in some visitors, including Japanese Prime Minister Toshiki Kaifu in 1991, having to fly to the People’s Republic of China to change to smaller planes before traveling on to Buyant-Ukhaa.

ADB’s first transport sector project started in 1993 and focused on ensuring the airport could handle large planes safely and efficiently. It was the first large infrastructure loan from an international financial institution following Mongolia’s transition to a market economy.

This successful project was followed by others in air navigation, road transport, and telecommunications.

Future Cooperation

ADB’s cooperation with Mongolia has been extremely wide-ranging over the past 30 years, covering most sectors.

As the partnership moves forward, we should be looking at areas where there is unfinished business, including development of the education and health sectors. The COVID-19 pandemic has shown how unprepared and ill-equipped our health care system is for handling a major health crisis.

A deterioration in poverty rates in recent years has to be addressed as well, with programs needed to improve the living standards of the poorest and most marginalized groups.

The environment also needs urgent attention. Over the past 30 years, many ecosystems have become badly degraded, harming economic growth prospects and public health. Protecting the environment is now a matter of national security, and the partnership can take appropriate measures to strengthen efforts in this area.
**Tarbosaurus.** This 70-million-year-old fossilized skeleton was found in Nemegt valley of Bulgan soum, Umnugovi aimag (photo by Oktyabri Dash).
Khongor sand dunes. The dunes are in Govi Gurvan Saikhan National Park, which is located in Umnugovi aimag (photo by Oktyabri Dash).
Rehabilitation and Overcoming Isolation: ADB Operations

Mongolia joined ADB in 1991 and, in the first 10 years of its partnership, ADB approved $469 million in sovereign loans for 25 projects, $2 million for 1 grant, and almost $46 million for 99 technical assistance projects.

The initial assistance was in the form of quick disbursing program loans, with the first loan funding badly needed foreign exchange to pay for basic necessities including wheat, medicine, and fuel, as well as for raw materials and parts needed by the construction and processing industries. This was followed by loans to ease budgetary and balance of payments pressures. From 1991 to 2000, nearly 40% of ADB’s total lending was in the form of budget support loans.

ADB played a leading role in banking sector reforms, with support provided to restructure and recapitalize banks and help them develop commercial banking capabilities. This included the creation of a supervisory framework for the newly commercialized institutions.

Operations were conducted in tandem with other partners, particularly the IMF, which provided program assistance to help stabilize the country’s fiscal position.

Working with the Government of Mongolia and development partners, ADB also helped to rehabilitate and modernize the country’s ageing and dilapidated civil aviation, telecommunications, and energy systems. This was crucial for Mongolia’s economic development, quality of life, and improved connectivity, both at home and abroad.


<table>
<thead>
<tr>
<th>Sector</th>
<th>Amount</th>
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<tbody>
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<td>Transport</td>
<td>22.2%</td>
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<tr>
<td>Energy</td>
<td>19.2%</td>
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<tr>
<td>Agriculture, Natural Resources and Rural Development</td>
<td>13.5%</td>
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<td>Finance</td>
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<td>Industry and Trade</td>
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<tr>
<td>Water and Other Urban Infrastructure and Services</td>
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Total sovereign assistance $517 million.

Civil Aviation — Flying High

As its only international aviation gateway, the Ulaanbaatar airport plays a pivotal role in linking Mongolia to the rest of the world. But in a country with widely scattered communities and low demand for air travel, providing high quality, financially viable airports is not easy.

In the early 1990s, there was growing interest in Mongolia, with both international passenger arrivals and freight increasing. However, a lack of funding for air traffic control, obsolete equipment, and inadequate staff training had resulted in a spate of near accidents.

To improve safety and to open up the country to new markets and international tourism, the government partnered with ADB to overhaul the country’s aviation sector.

The Ulaanbaatar Airport Project, which upgraded and extended the runway and built other key infrastructure, was ADB’s first construction project in the country. It resulted in the entry of wide-bodied Airbus and Boeing aircraft, which had previously been unable to land at the airport.

The construction of a new maintenance hangar, allowed for all-weather aircraft checks and repairs, and a modern cargo terminal increased cargo handling capacity.

These initial steps were followed by a second project that financed modern air navigation and traffic control systems for both domestic and international flights, sharply improving safety.

As a result of these measures, there was a large uptick in flights across the Mongolian airspace, with the country earning around $20 million a year in revenues from overflight rights. The Ulaanbaatar airport posted average annual revenue growth of over 50% from 1994 through to 1998.

ADB also played a major role in helping Mongolia introduce civil aviation regulations and laws, which have paved the way for private investment and commercialization of the sector.

Currently, Mongolia has three privately owned commercial carriers providing domestic and international travel services, on top of the state-owned flag carrier MIAT Mongolian Airlines. Eight international commercial airlines also operate in and out of the country.

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Telecommunications — Making New Connections

In an era where the vast majority of people own or have the use of mobile or fixed phones, a world without ready access to basic telecommunications seems hard to imagine.

But in the early 1990s, that was the reality that nearly all Mongolians faced. Mongolia had just one outbound phone line to Moscow and nearly all of the 70,000 telephones in the country were in offices, with just a handful of households having them. The system itself was an aged analog network owned and operated by the government.

The difficulties of communicating in those days are vividly recalled by Batbayar Demchig who managed the Erdenebulgan soum telephone branch in Khuvsgul aimag for 33 years.

“Only the soum’s administration office and the bank had telephones, and personal calls had to be placed through my office, with a request for a call having to be made 24 hours beforehand,” said Batbayar. “Connecting to Ulaanbaatar was even more challenging as there were only three channels connecting soums to the capital so calls had to be scheduled, allotting one hour per day for each soum.”

To enable citizens to communicate quickly and efficiently, both at home and abroad, modern and commercially oriented telecommunications systems were needed. Regulations were also required to govern the new system and to help attract private investors into the sector.

ADB played a direct and early role in this process by financing, along with other development partners, new digital-based telecommunications systems, covering six main urban centers. The result was a substantial increase in the volume of traffic and speed of calls that could be handled. In the largest centers of Ulaanbaatar, Erdenet, and Darkhan, subscriber numbers surged from over 41,000 in 1993 to nearly 74,000 in 2000, with the number of landline calls from five aimags growing more than four-fold between 1997 and 2000.

Keeping in touch. Herders using cellphones in Ilkh-Uul soum, Khuvsgul aimag (photo by ADB).
These initial physical improvements were complemented by important national reforms, supported by ADB and other development partners, which put the sector on a commercial footing and paved the way for private investment, with Korea Telecom taking a 40% stake in the state-owned company, Mongolia Telecom, in 1995.9 By 2000, over 100 telecommunications and information technology companies were operating in Mongolia, including two mobile phone operators, established with foreign direct investment.

Today, there are more mobile phone accounts than people and 85% of the population is connected to the internet—a world away from the situation the country faced just 3 decades before.10

To take advantage of fast emerging new technologies, the government, with ADB technical assistance, successfully introduced a mobile banking system, which has been widely embraced. As of 2020, all 12 commercial banks were offering mobile banking services, through the internet, short message services, and telephone banking. There are now 4.4 million active mobile bank users in the country.11

These new services have been especially significant for the country’s large semi-nomadic herder population, as well as for the elderly and disabled, who typically have mobile phones but have little or no access to physical banks.

Businesses, including small and medium-sized enterprises, and consumers have also taken advantage of the opportunities that mobile banking and the internet provide for e-commerce, with 10 online shopping platforms established as of June 2020. Facebook has become an important tool for business transactions, particularly among smaller enterprises.

The shift to digital banking and e-commerce services, however, still has some way to go, as the COVID-19 pandemic has shown that many people still rely on physical bank branches to do financial transactions.

Only the soum’s administration office and the bank had telephones, and personal calls had to be placed through my office, with a request for a call having to be made 24 hours beforehand.

~Batbayar Demchig

10 Footnote 1, p. 204.
On the road. A camel travels along a road in Sainshand, Dornogovi aimag. These hardy animals play an important role in transporting heavy loads in many parts of the country (photo by ADB).

Wild weather. A summer storm in Arkhangai aimag (photo by ADB).

Cranes at Gun Galuut, Tuv aimag. Mongolia’s wetlands are home to rare species of cranes and other birds (photo by Mookiah Thiruchelvam).
Energizing Ulaanbaatar. This combined heat and power plant in Ulaanbaatar was rehabilitated with ADB support in 1993 (photo by ADB).

**Energy — Building Stability and Security**

In the winter of 1993, one of Ulaanbaatar’s three coal-fired power plants, which supply the city with both heat and power, stood on the brink of total collapse. Years of inadequate maintenance, caused by a lack of foreign exchange to buy spare parts, had led to an explosion at the plant, which was unable to provide the city with electricity and heat. In addition, sections of the over 400-kilometer-long network of pipes that deliver heat to both industry and households had deteriorated badly, resulting in widespread leaks.

The result was near daily blackouts and subzero temperatures in residential buildings, forcing residents to wrap up in heavy coats and boots in their own homes to survive the harsh conditions.

Restoring and modernizing energy systems was essential for the welfare of citizens and to ensure the country’s economy could grow. To support Ulaanbaatar’s urgent needs, ADB provided a project loan to rehabilitate the crippled generating plant and to replace degraded pipes, both of which were needed to avert a full-scale collapse of the district heating system.

As a result of the Power Rehabilitation Project, gross power output from the plant rose by 73% between 1994 and 2001. The overall power and heating system became more stable, efficient, and reliable, helping to cut fuel consumption and reduce energy imports from the Russian Federation, which fell by over 50% between 1997 and 2001.¹²

Along with stabilizing and improving power and heating supplies to urban dwellers, Mongolia has also sought to address the challenge of meeting the energy needs of remote rural communities. Many baghs, or villages, are far from larger soum centers and relied in the past on diesel generators, which only delivered power for a few hours a day.

Connecting these distant communities to traditional grid-supplied electricity systems was not economically viable, so steps were taken to explore alternatives. One approach was demonstrated under an ADB-supported project, funded by the Japan Fund for Poverty Reduction, which was able to deliver a reliable supply of electricity from the grid through a single-earth wire system.

As it looks to the future, Mongolia is moving to tap its abundant wind and solar power resources to reduce its near total reliance on coal as an energy source, which is taking a heavy toll on the environment and people’s health.

The country is estimated to have renewable resources equivalent to 2,600 gigawatts, which if fully utilized could meet all the country’s future power needs. But the limited flexibility of the existing power system is preventing full utilization of even the modest amount of renewable energy currently produced.


Coal briquettes. The introduction of coal briquettes, which emit less smoke and ash than raw coal, has been a step forward in reducing air pollution in Ulaanbaatar (photo by ADB).
A new ADB project, which will finance Mongolia’s first large-scale battery energy storage system, will allow the full take up of power generated from renewable sources. Once in operation, the system—which will be among the largest of its kind in the world—will store and discharge 44 gigawatt-hours of clean peaking power annually into the country’s central energy system grid.

This initiative is expected to deliver multiple benefits for Mongolia over time, including ending power outages, improving air quality, and delivering a more efficient and decarbonized energy system.

It is also expected to pave the way for future renewable energy investments by the private sector, as well as offering a blueprint for other emerging economies looking to develop and operate large-scale battery energy storage systems.
Megjid Janraisig. This statue of the Buddha is located in the Gandantegchinlen monastery in Ulaanbaatar (photo by ADB).

Gandantegchinlen monastery. Located in Ulaanbaatar, it was the only Buddhist monastery allowed to function during the period of control by the Soviet Union (photo by ADB).
**Tsam ceremony.** The tsam mask dance is a ceremony performed to soothe the spirits of lands and waters (photo by Oktyabri Dash).

**Bright forecast.** According to legend, the old white man’s dance can forecast the weather of the coming winter (photo by Oktyabri Dash).

**A tsam dancer.** The tsam dance ceremony depicts different characters, including devils, animals and people (photo by Oktyabri Dash).

**Khuree tsam.** This is the largest tsam ceremony, held every August, with dancers, performing 108 roles (photo by Oktyabri Dash).