



MONGOLIA

The Warrior Spirit

In the second part of its report on Mongolia, *Business Outlook* showcases the opportunities and challenges of this huge, resource-rich emerging economy.

With a strategic location and excellent potential for development, thanks to abundant mineral resources that include coal, copper, feldspar, fluorite, gold, iron ore, oil and uranium, Mongolia continues to make headway on the international stage. Double-digit growth is still the norm and widespread modernization is under way, with important infrastructural changes transforming the landscape.

The government, led by Prime Minister Norovyn Altankhuyag, is plowing ahead with reforms that will lift the country out of poverty.

“Last year was a very important milestone for Mongolia,” the prime minister says. “A general election took place and the Democratic Party came to lead the government after four years as part of a coalition. This victory has created greater stability in the country. We have managed to raise \$1.5 billion from international markets that will strengthen Mongolia and help support the infrastructure needed for a fully functioning mining sector, as well as diversifying the economy.

“The government prioritized three main areas. The first is to fight corruption: We want to reduce it to an absolute minimum and ensure the government is transparent. The second is to create as many jobs as possible to help ensure the future of Mongolian citizens. The third is to continue developing infrastructure.”



Norovyn Altankhuyag
Prime Minister

With the new administration came a five-year action plan, a road map for the government to implement and achieve its stated targets. In 2013, the main focus is on the development of infrastructure, in the shape of roads, railways and urban development, but particularly railways.

With China and Russia, Mongolia's vast and powerful neighbors, requiring raw materials, the need for new railroads is important to allow Mongolia to reach those neighbors—and world markets. This will ultimately fuel

competition for access to Mongolia's natural resources, as Minister for Mining Davaajav Gankhuyag explains: “The establishment of new railroads will make us more competitive in terms of natural resources trading, and the government has already started basic works for the development of new processing plants that will begin to add value to our mineral wealth in 2013 for coal, iron and copper.”

Mongolia's mining sector suffered setbacks last year due to the application of stricter controls. The perceived negative attitude toward the private sector and especially foreign investors slowed growth to 12% (the previous year it was 17%) although the government is keen



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to rectify the situation.

Speaking during the Mongolia Investment Summit 2013 in London in April, Vice Minister of Economic Development Chuluunbat Ochirbat explained how the government is planning a new investment law for parliamentary approval by the summer that aims to give foreign investors more assurance about the rules governing their investments.

“We want to send a very strong message [regarding] the stability and in the clarity of treatment of foreign investors in Mongolia,” Ochirbat told journalists, explaining that the government has already drafted the law and plans to submit it to Parliament for approval before the spring plenary session closes on July 10.

Investor confidence does appear to be returning. Says Gankhuyag: “The government is focused on promoting sustainable mining and the mining reform policy is clearly defined. Within this framework, we have announced to investors that we want the mining sector to be environmentally friendly, harmless to human health, transparent, accountable, adhere to the rule of law and be mutually beneficial for stakeholders. At the moment, new amendments are being discussed publicly as part of a consultation process.

“We want mining to be positive for investors as well. We will continue to provide favorable tax systems bearing in mind that Mongolia is already one of the lowest. So it will provide excellent opportunities for international investors.”

The pursuance of opportunities to add value is crucial for the economy and to maximize profits for investors, Gankhuyag says: “It is important to consider that value addition means prices remain more stable. We currently have two factories producing copper concentrate. One is the Erdenet, the other is Oyu Tolgoi.”

“We have managed to raise \$1.5 billion from international markets that will strengthen Mongolia.”

Norovyn Altankhuyag, Prime Minister of Mongolia

The minister has revealed plans for the construction of a steelworks that will allow Mongolia to import iron and create steel for domestic use or export. “We are also working with the aim of building a crude oil refinery to supply the domestic needs of oil products,” Gankhuyag says, adding that in the midterm, mining will drive the Mongolian economy. “It is my vision to promote a multi-structural economy based on the mining sector and to develop the agricultural and services sectors as well,” he says.

For Enkhbold Erdene-Ochir, executive director of Mining National Operator (MNO), a mining and construction company formed in 2012, the undeveloped infrastructure is the most pressing challenge. “We have only a single railway, and the condition of the roads is less than



Ulaanbaatar, Mongolia's modernizing capital.

ideal,” he says. “We are just beginning to connect the regions. However, increasing rail capacity is the priority. Right now rail currently moves 20 million tons of freight per annum, while road transportation moves about 22 million tons of coal. We are expecting a considerable increase in the amount of coal transported by 2015. It should double in both cases. Hence, the railways must be upgraded.”

Funding will obviously be a pivotal factor in the company's growth. As Erdene-Ochir explains: “The development bank will provide us with a considerable amount of money, but it's not enough. When you look at the Tianjin Railway, which will connect Mongolia to this Chinese port, it requires an outlay of \$1.4 billion. The longer railway that connects our neighbors, which is 1,100 kilometers, would require about \$4 billion to build. Mining is booming and rail is struggling to keep up. The output is growing exponentially.

“Obviously, all of this is an opportunity and we are quite optimistic. We have seen a lot of legal and political changes that created a slow-down last year. However, in 2013, we have big plans to grow. There will be a lot of activity and a lot of new business for us.

“In my experience, foreign investment is good for the country. It helps to build the business sector and brings a variety of skills, strategies and technology that help to establish a foundation for emerging economies. I don't believe in separating local companies from foreign ones. Everyone is doing business, and as long as it is fair, we should permit it.

“MNO is a local company, and we want to provide a top-quality service to anyone doing business in Mongolia. We are new players, but we have an experienced team. We want to be business partners to companies that want to come in. We are a contract mining company; it is a new concept in Mongolia and the first companies are being

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With 10 years in the mining business, the MNO executive director has seen many changes and is convinced that the new law will be beneficial for everyone. "It will provide more transparency and hold both the private and public sector to account," he says.

The need for a specialist contractor, like MNO, is crucial, however, he adds: "Every country has its obstacles. People want the coal but don't want to work at getting it out in an efficient manner. We therefore want to make it easy for people, to be the solution they don't have to think about."

Mongolrostsvetmet LLC (Monros), a Mongolian-Russian joint venture, is reassuring about Mongolia's investment climate. And, with more than 40 years in the business, it is in a good position to comment about the situation. Monros is a leading fluorspar and gold mining company in Mongolia, with a portfolio of two underground mines and three open pits across the country, as well as a sizable mineral processing plant.

"Mongolia is the fourth-largest producer of fluorspar in the world and has the potential to continue growing. Fluorspar is the main component of aluminum and in two or three years demand will amount to 6 million tons. It increases every day," says Bolor-Erdene.Kh, general director. "Our company has extensive experience in that area. We are currently generating a lot of attention around our other products, such as gold and iron ore, and with the improvement in transparency, there is serious potential for iron ore and gold mining."



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Expanding Retail

Although it is mining and the lucrative raw materials that hit the international headlines, Mongolia does boast strong business opportunities across all sectors. Naran Group is a case in point. Although initially focused on retail, it has diversified into a variety of sectors, including construction, real estate and

media, and is investigating food processing and cosmetics as future growth areas.

With more than 23 years' retail experience, the company is well placed to benefit from Mongolia's rising economy as the standard of living and disposable incomes grow. Through its "affordable luxury" philosophy, Naran has been a pioneer in introducing new products to the market over the years and played a pivotal role in changing the mindset of consumers as Mongolia moved from behind the Iron Curtain to become a capitalist market.

"I've had a lot of experience living in different countries and exposure to a lot of different consumer markets, so when I looked at Mongolia, it was obvious there was a lot of room for growth," says Sereeter Boldkhet, Naran's founder and chairman of the board of directors and a former diplomat.

"People wanted to eat nice food and drive nice cars, live in decent houses. When I left my job, I decided to form a private business with my wife, a chemist, and Naran was the result. We were one of the first private entities in this country."

It was a slow beginning, but retail proved to be a logical start. "We only had a few thousand dollars and sold the first lots of goods in hard currency, because Mongolia's currency was dropping so rapidly, but this gave us a good start," Boldkhet remembers. "We had no savings at all, and we had to shift the mentality, habits and traditions.

"We started by selecting products normal consumers needed—color TVs, for example, and sold 44,000 as Naran Electronics. We then started looking into what products would be good for Mongolia. Very slowly, we started changing the way of life for Mongolians. We had to teach consumers what to wear and what to eat. In the early 1990s, there was no middle class, so disposable income and living standards were very low."

"In the early 1990s, there was no middle class so disposable income and living standards were very low."

Sereeter Boldkhet, Founder and Chairman, Naran Group

The slow-but-careful approach allowed Naran to survive bumps in the road where other companies failed. "We introduced more food-stuffs, like fruit juice and dried fruits. We developed the motto 'Your best choice.' We figured out what worked," Boldkhet says.

The company also saw the potential for real estate and launched the first serviced apartments in the capital that were a far cry from the dilapidated Soviet buildings.

"We spent a lot of money renovating and rebuilding decaying retail space so that it looked nice and the consumers appreciated this," Boldkhet says. "We opened several stores. One of our biggest successes was the Naran Department Store, which was a joint venture with Singaporeans. We worked with them again on several projects."

Now with 14 companies and 1,400 staff, Naran's biggest operation is fashion. In terms of investment opportunities for the U.K., the chairman sees the best synergies in hospitality and housing.

"We are hoping to go into the hotel business and already have experience in restaurants, having brought five different types of cuisine to the market," he says. "As for housing, almost 60% of the population lives in yurts. It will be a long time before our population has enough accommodation. We want to build a lifestyle. Mongolia presents a strong case for mixed real-estate developments."

Mining Revenues for Mongolia's Growth

Having built Erdenet City on rock and ore, Mongolia's premier mining corporation keeps the community, and the environment, firmly in mind.

Since it was founded 35 years ago, Erdenet Mining Corp. has proved itself to be a role model for Mongolian companies. The firm, which produces 500,000 tons of copper concentrate and 26 million tons of ore a year, has been pivotal to the country's growth and development, providing jobs, homes and services, as well as huge and healthy revenues.

Where Erdenet differentiates itself, however, is in the quality of the infrastructure it provides. Erdenet City now boasts 100,000 inhabitants who benefit from excellent roads, railways, thermal power plants, schools, hospitals, a university—even a carpet factory. The area, which is also building up an agricultural sector and other smaller-scale industrial projects, is now so attractive, people from the capital, Ulaanbaatar, often move there when they retire.

Moreover, sustainability is much more than a trending watchword for the company's management—it is at the heart of the company's strategy and philosophy.

"The planning process is really important to mining companies," says general director and mining veteran Ts Davaatseren. "If we plan properly, we create a strong economic backbone, but if we just extract, we risk the curse that comes with so many areas that are blessed with mineral wealth. Our growth has come about naturally, and we have created

and solidified the labor regulation within the company." Erdenet also addresses environmental issues as a priority. "We pay the utmost attention to the environment," Davaatseren says. "We've started a program for citizens and staff to plant trees to make Erdenet a greener city. We conduct a number of surveys to measure air and water pollution and ensure all steps to reduce pollution are being taken. In terms of waste control, we have been working with international and domestic firms to make sure we keep the white dust associated with mining at a low level."

Innovation is also a large part of the company's makeup. Erdenet has an R&D office next to the factory and a legion of engineers who look at ways to increase value through new product lines. "We are in the process of building a factory that will melt copper," Davaatseren says. "At the same time, we are building a small-scale hydrometallurgy factory, funded through a variety of investors, and a copper cathode operation. We already produce 200 tons of copper threads for the domestic market. Molten molybdenum and ore processing are also focuses of ours. We work with many foreign investors and are committed to boosting productivity."

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Ts Davaatseren
General Director



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