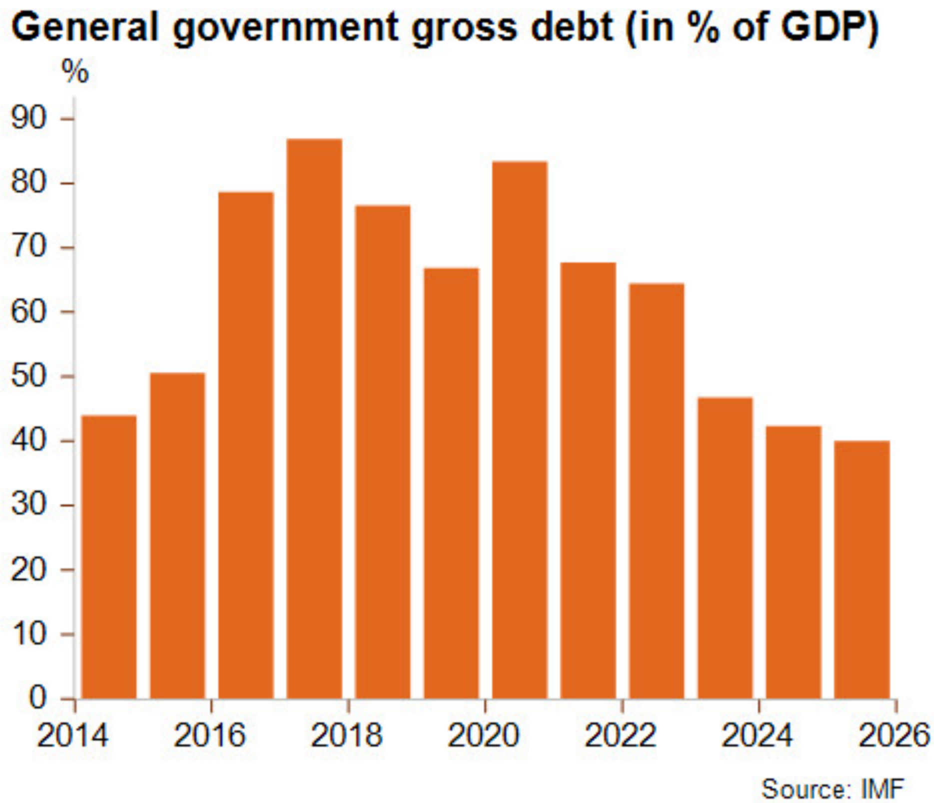
Mongolia: A gradual macroeconomic improvement drives an upgrade in the MLT political risk to 6/7 | Credendo

Heading to a more sustainable macroeconomic path

Mongolia has been on a bumpy road since spring 2017, when it was bailed out by multilateral and bilateral creditors to avoid a sovereign debt default. During the following years, while the authorities strived to reduce the country's heavy debt burden, the economy was hit hard by the Covid-19 pandemic due to the border closure with China, its top export market (accounting for more than 80% of Mongolian goods exports). However, since 2021, the country has gradually seen its macroeconomic performances improve and now seems to have turned the corner. Real GDP growth is back to sustained high rates, recording a 6% average across 2022-24, a rate which is also forecast for the next three years. The economy remains highly reliant on the mineral commodity sector (coal, copper, gold and iron ore) as the main growth driver, although this is also a major weakness as it means that Mongolia is dependent on price fluctuations – this risk is mitigated by high prices for gold, huge market potential for copper in the green transition and rising demand for critical minerals from neighbouring China. Moreover, the large mining production expansion – after the launch of the huge Oyu Tolgoi mine in 2023, one of the world's largest copper and gold mines – will be a valuable buffer in making Mongolia more resilient to future commodity demand and price fluctuations. The government also wants to boost economic diversification, notably by developing the country's high tourism potential and untapping huge renewable potential (such as hydropower and solar) to reduce external energy dependency. These current and future mining and energy projects will boost exports and GDP growth in the MLT, thereby keeping the current account deficit at more acceptable levels. The deficit is much lower than its pre-Covid level, having halved from 16% to an expected 8% of GDP between 2019 and 2024, although a slow, gradual widening is forecast in the future. That said, FDI is expected to remain high and therefore finance the current account deficit in the MLT. Foreign exchange reserves are therefore likely to remain around an adequate level of three months of import cover.

A sharply squeezed public debt alleviates the heavy external debt burden

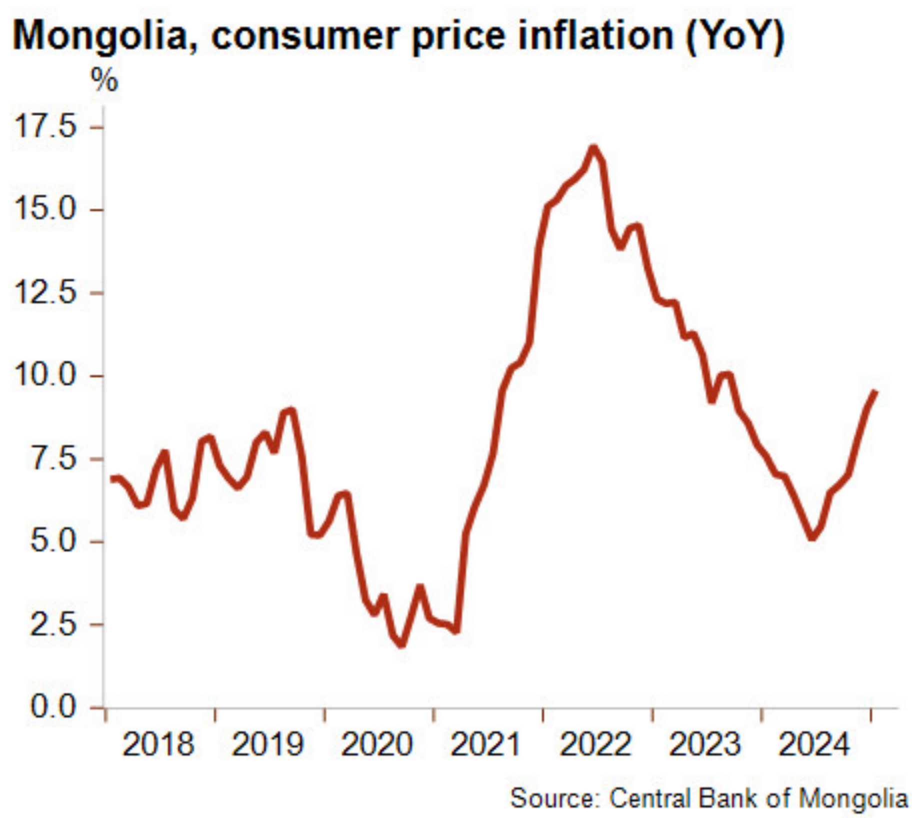
Stronger GDP and exports growth, combined with contained new borrowing, have contributed to reducing the heavy external debt ratios, resulting in a reduction in the external debt-to-GDP ratio from 237% in 2016 to 169% in 2023 since Mongolia's sovereign debt crisis. A gradual but limited increase is however expected from 2026. It is worth noting that most debt is private, and an important decline in external debt comes from the decrease in public debt. Meanwhile, fiscal consolidation has enabled a remarkable improvement in public finances as public debt has dropped from 77.8% of GDP in 2020 to an estimated level of less than 40% in 2024. The fiscal balance has been in surplus since 2021 (a small deficit is forecast in the MLT), with government revenue surging to more than 35% of GDP so that the public debt-to-revenue ratio now amounts to just 112% (compared to over 300% at the time of Mongolia's debt crisis). Looking ahead, public debt sustainability is projected to weaken a fraction, but without endangering the successful achievements of recent years. Therefore, the concrete progress towards a more sustainable external public debt and an upbeat outlook for Mongolia's mineral sector led to an upgrade in the MLT political risk category to 6/7 last December.



Global trade protectionism and deteriorating monetary conditions remain downside risks

While external debt service reached more than half of current account receipts between 2017 and 2023, it is expected to sit at a much lower level comparatively in the coming years, although future external debt repayments will be monitored closely since they are projected to be equal to the level of foreign exchange reserves. In this context, Mongolia should benefit from easing US interest rates and a largely stable tugrik close to its levels of two years ago – albeit partly resulting from the central bank interventions.

Nevertheless, improved market conditions and confidence in the country could be exposed to a global trade war led by Trump's import tariff hikes which could harm the Chinese economy, fuel inflation pressures and compel a pause in the Fed's easing rate cycle. A stronger US dollar is also a concern, given the ever-challenging debt service. These are important downside risks to watch this year and beyond in the light of Mongolia's external debt, which is still high. Although inflation has eased away from double-digit figures since 2023 amid monetary tightening, it still rose to 9.6% in January 2025. Inflation is likely to persist at relatively high levels, a chronic feature for the deadlocked economy.



Political stability and geostrategic position

Mongolia's currently favourable outlook is supported by heightened political stability. Already in control of the presidency, the victory of the ruling Mongolian People's Party in the June 2024 elections strengthened prospects of cautious policy continuity and a preserved democratic system. Nonetheless, in spite of finalised negotiations with Rio Tinto regarding the Oyu Tolgoi mine, the authorities have yet to show long-term commitment to strengthening institutions, which have been volatile in the past, in order to maintain appeal for foreign investors in the LT. Moreover, the government will continue to face protests in the absence of progress in tackling structural problems such as the high cost of living, the lack of socioeconomic benefits from commodity extraction and air pollution.

Externally, Mongolia is expected to continue to reap benefits from its geostrategic and transit location between Russia and China (its dominant trade and investment partner), notably as part of the Belt and Road Initiative. The authorities are also committed to diversifying their trade and economic links with the West as they aim to mitigate the risks associated with economic reliance on two partners. However, looking ahead, a chaotic geopolitical environment could complicate the authorities' attempts to navigate between Mongolia's partners.

Analyst: Raphaël Cecchi – r.cecchi@credendo.com