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WEEKLY



DeFacto **ARTICLE**

№515

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THE MIDDLE CLASS DRAIN

DeFacto **REVIEW**

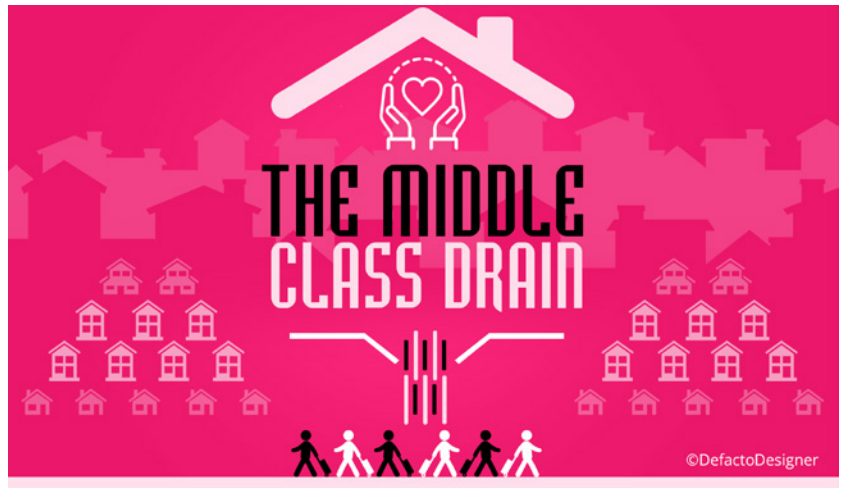
➤ HOW TO ENFORCE FORCE MAJEURE

Due to the spread of the coronavirus, a number of preventive and quarantine measures have been implemented by the Mongolian government as we are in a high risk area of the outbreak. Quarantine measures took a toll on medium and small businesses, leaving owners unable to pay rent and loan repayments. Before going into this topic, I would like to touch on a comment by IMF director Kristalina Georgieva on the V shape recovery of the Chinese economy.

➤ QUALITY OF EDUCATION IN MONGOLIA

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In a democratic society, it is the middle class that scrutinizes the elected authorities and demands accountability. The larger the middle class, the more accessible are social services such as education and health, and the less corruption and bribery of government officials is prevalent. In a country where the middle class is under siege and the income gap is too big, the society becomes more divided and conflicts escalate.

In recent decades, industrialization shifted from the developed countries to the developing ones, and the economy of these regions grew steadily due to the rapid growth of the Chinese economy. As a country's economy grows, the middle class, which is the main consumer, thrives and as the market increases and diversifies, new jobs emerge. Thus, the increased investment and savings formation allow the middle class to drive the economic growth.

WHO IS THE MIDDLE CLASS?

Although economists have emphasized the role and involvement of the middle class in social development, there is no consensus so far as to who exactly comprises the middle class.

For example, the Brookings Institution claims that the middle class earns between \$11-110 per day, as of 2016, 3.2 billion people worldwide join this group, increasing by 140 million people each year.

Another widely accepted definition of the middle class is as those whose household income, is able to pay for food, clothing, housing, education while there remains a rest amount for savings.



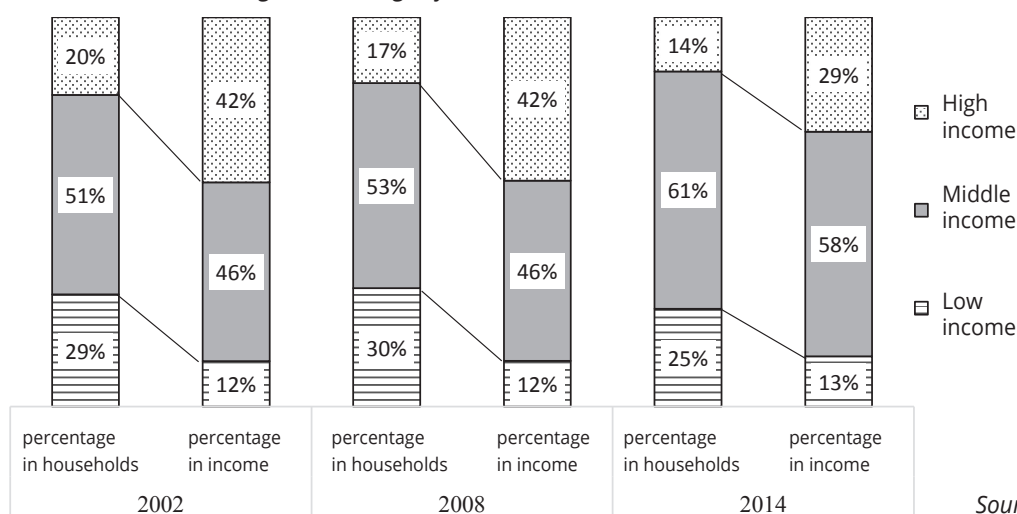
- A citizen from a high developed country with an income below average is wealthier than a citizen from a developing country with an average income. However, the subsistence level and poverty line which is \$1.90 per capita, are accounted as well. While some researchers suggest that the middle class in developing countries earn \$2-13 a day, others claim \$2-10, and yet another contends \$10-100.

The Economic Research Institute (ERI) conducted a survey in 2014 and 2016 to determine the middle class of Mongolia. In this study, the middle class was defined as households with an annual income equal to 67-200% of the median annual income for the respective year. The survey found that in 2002, 20% were high-income

households, 51% were middle-income and 29% were low-income households; in 2014, 14% were high-income households, 61% middle-income ones and 25% low-income households. Households with a median income have increased by 10% over 12 years.

It also demonstrates how household income inequality has changed. From 2002 to 2008, the number of middle-income households increased, despite the decrease in the number of high-income families while their incomes remain at the same level. But between 2008 and 2014, incomes also had risen as the number of middle-income households increased dramatically; high-income families declined while their incomes also dropped as well.

Fig. 1 Percentage of middle class in households and income



And household income inequality exists not only between the rural areas and the city, but also between the capital's districts. The number of low-income households is significantly lower in the districts closest to the center than in the suburbs.

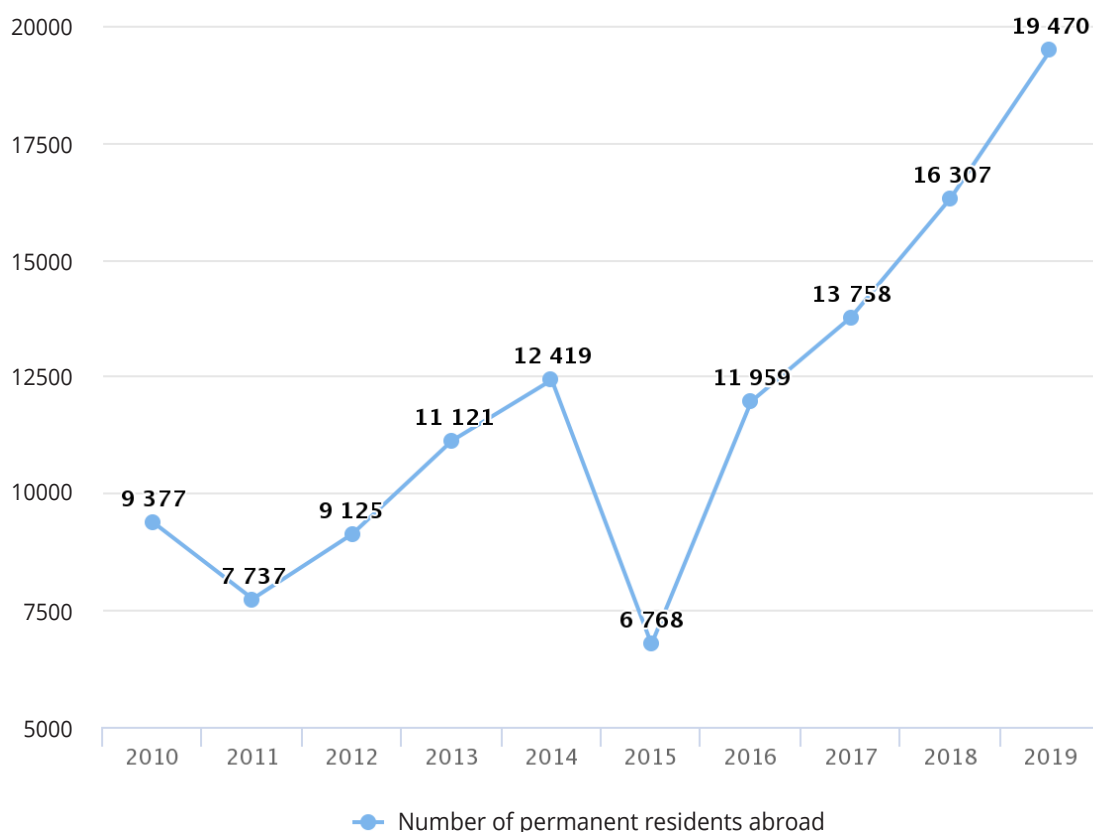
The government is planning for a spring session on its "The Foresight 2050" plans for the next 30 years promising: "to support the employment of the population, steadily increasing household incomes, to cultivate an active creative family, to provide micro-, small and medium-sized businesses in a competitive investment environment held by a self-sufficient family and by 2050 raise middle class to 80% of population". The document is expected to increase the size of the middle class from 16.2% today to 50% by 2030, to 70% by 2040 and to 80% by 2050. How these 16.2% and other percentages are calculated is not clear.

ARE THE OBJECTIVES OF "THE FORESIGHT 2050" REAL?

In addition to measuring income, there is a tendency to determine the middle class by educational level based on the assumption that the educated part of society is more serious about making political and economical decisions. First of all, the middle class demands to be treated by the state as equals and their dignity to be respected. Being the middle class at least implies to have a job, housing, regular income, and savings.

The middle class is the basis of social stability. Currently, instead of having a quality middle-class in Mongolia, citizens are taking their chances and aiming to go abroad in any way possible. Apart from the fact that the number of people going abroad to study, work and travel is increasing dramatically, the number of permanent residents abroad is growing continuously. ►►

Fig. 2 Number of permanent residents abroad by years



Source: National Statistics Committee, 2020

In the last ten years, the number of permanent residents abroad was the lowest at 6768 in 2015 and the highest at 19470 in 2019. About 200 thousand people abroad (Consulate of the Ministry of Foreign Affairs), of which 120 thousand went to live as permanent. Despite having a job in Mongolia, salaries do not always cover sustenance costs, and the pension is not able to cover a day's meals. As a result, people make the choice to move. That means the middle-class is draining.

In other words, the current political and economic system in Mongolia impedes the middle-class household's ability to live well and detracts their hope for the future. Citizens are fleeing a politically oligarchic, *clientelism* system. After obtaining an education, people are going to developed countries such as South Korea and Australia to work in blue-collar jobs, attaining a much higher income and recognition than in Mongolia.

First of all, in order to stop the middle-class drain, it is necessary to abolish the political clientelist system. Then

a radical improvement and upgrade to our education system is needed. Lately, the Mongolian government has been idolizing the elitist education. For instance, by providing scholarships to students who have enrolled to the Top 100 Universities in the world, and by funding (variable costs) private schools with high tuition fees with the public budget when the investment in public schools is clearly insufficient. In the long term, it is more profitable to enable 200 or 300 suburban children to learn as a group of 25 students in one classroom than to fund 2 or 3 children's study at Harvard or Stanford. In public schools there are now 50 students crammed into one classroom. Therefore, it is important to abandon the above-mentioned policy which promotes social inequalities and it is vital that the government focuses to improve the public education which will have a major impact on long-term economic growth and the strengthen the responsible democratic political system.

2020.02.13 ■



DeFacto **REVIEW**

Every Sunday live at 7pm on MNB World television: 16th February, 2020
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Namsrai Tsend

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HOW TO ENFORCE FORCE MAJEURE

Due to the spread of the coronavirus, a number of preventive and quarantine measures have been implemented by the Mongolian government as we are in a high risk area of the outbreak. Quarantine measures took a toll on medium and small businesses, leaving owners unable to pay rent and loan repayments. Before going into this topic, I would like to touch on a comment by IMF director Kristalina Georgieva on the V shape recovery of the Chinese economy. The current Chinese economy cannot be compared to that of the 2003 SARS outbreak as it comprised 8% of a healthy world economy in 2003 but now comprises 19% of an unstable world economy. In this situation, the whole world, especially Asia and Mongolia are dependent on the path of the coronavirus.

Regarding what Mongolian businesses can do in this situation, they can firstly write a letter to their commercial banks with whom they have loans. The Chamber of Commerce states that they will support claims of force majeure as the concept relates to events outside the control of the parties of the contract. However, looking back, the Chamber of Commerce acknowledgement have carried little weight in previous instances. Businesses were in the same situation during the SARS outbreak and banks showed little sympathy for their plight. One reason is the fact that the Chamber of Commerce inherently serves the interests of its members and many of the force majeure claims come from its members, leading to a potential conflict of interests. This raises a question how force majeure situations can be addressed in the future and the need for an independent entity to authenticate claims of force majeure. Moreover, the Arbitration Court also operates under the purview of the Chamber of Commerce so this situation should be restructured to provide its responsibilities to an independent entity.

This is a concern for both big and small companies as the coronavirus is spreading around the world. Recently, Hong Kong's Financial Secretary, Mr. Paul Chan Mo-po called on property owners provide substantial rent

reductions for tenants as a form of social responsibility. Two of Hong Kong's largest real estate developers, Sun Hung Kai Properties and Lan Kwai Fong Group responded to this call by reducing its rents for commercial properties by 50% in February. Mongolian real state companies should follow suit, otherwise it will become difficult for Mongolian companies to pay their rent. Social responsibility is something that matters to all companies, no matter their size and professional, industry unions should contemplate on the social responsibility of their member companies. It is a time that will show the true character of companies and it is my hope that the Bank Association of Mongolia will take action. Banks should evaluate force majeure claims on a case by case basis based on the impact that the impact of the precautions against the coronavirus such as closing the border with China had on their operations.

There is a National Chamber of Commerce and an Ulaanbaatar Chamber of Commerce, membership in which is not obligatory for businesses. This is not ideal as there is a more dynamic business environment in Europe where membership is mandatory. The Ulaanbaatar Chamber of Commerce appealed to the state and the city to reconsider their 2020 budget based on the coronavirus. The border has been closed to people but cargo is still being allowed to cross the border as they are not transmitting disease. The appeal is a well-grounded one as companies affected by the coronavirus precautions will no longer be able to pay their taxes leading to a smaller budget. Therefore, unless expenses are cut, there will be more deficit which would add to our significant foreign debt. I think the appeal is relevant and I think that the budget needs to be reconsidered, especially due to the fact that this is an election year where Members of Parliament spend significant amounts of public funds for local initiatives in the constituencies where they are standing.

QUALITY OF EDUCATION IN MONGOLIA

The Education Evaluation Center held a press briefing after the online registration system of the general exam was launched. A Department Head of the Education Evaluation Center, L. Ganbat stated that there was no national level research to determine the education quality of Mongolian students. This attracted significant interest when you consider that the Ministry of Education and its preeminent agency, the Education Evaluation Center are unaware of the quality of education. A nationwide examination of 9th grade students was only established last year and schools were ranked based on the results of their students. It is promising that there are plans for international standards to be incorporated into Mongolia and for a PISA survey which tests the capacities of 15 year olds across OECD countries to be carried out. It is worth noting that Finland, South Korea and Singapore all consistently lead this ranking.

I also found out that the Minister of Education is in talks with the OECD to incorporate some of their international standards into some Mongolian institutions which is excellent news. Becoming a member of OECD will significantly increase Mongolian institutional capacity which is one of the preeminent issues facing the governance of Mongolia. 7% of general education students study in private schools. There are 643 public schools and 160 private schools in Mongolia meaning there is less than 20 students per class in private schools while there are sometimes 53 students per class in public schools.

Mongolia has had private schools over the last 25 years during which time an interesting picture emerged. This involves politicians and policymakers owning private schools and receiving per capita subsidies from the gov-



ernment despite the fact that their tuition ranges from 1 million MNT to 58 million MNT which approaches the tuition of private schools in the US and the UK. This creates a disparity within society whereby some students receive good quality education while other students have to study at three shift schools in the evening. Finland doesn't have any private schools but its students regularly top various charts so there needs to be a long and hard reflection on the Mongolian education sector.

Mongolian parents believe their student's achievements are limited to their grades but graduation from schools and Universities does not guarantee employment. The goal of education is not to create stars but equality within society. If the quality of education is not tackled in the near future, students will never have an opportunity for an equal, fulfilling life. Rather than providing scholarships to students who are accepted into Ivy League schools, the money should be diverted to students studying in the third shift of classes.

Most Mongolian Universities are private ones and the same issue of private institutions receiving state subsidies arises. Moreover, Mongolia's high graduate unemployment rate is one of the highest in the world. Ironically, Mongolia is also a leading country in terms of university graduates per capita.

UNENDING LAND DISPUTE OF BOGD KHAN MOUNTAIN

The Ministry of Environment and Tourism issued a decree in 2018 and 2019 that annulled land deeds of 140 entities and companies on Bogd Khan mountain. Some of the entities and companies sued the Ministry of Environment and got favorable decisions. A senior legal counsel at the Ministry stated that the situation had reached a stalemate. This is the limbo that all Mongolian ministries are in as previous administrations provided illegal permission to companies. The new administrations attempt to annul the land deeds are hindered by the fact that the initial deeds are legally binding. We have been in this situation for many years and it is no secret that the

Bogd Khan mountain to the south of Ulaanbaatar is already misused, with every single one of its valley serving as a monument to corruption in the country. Individuals within the Ministry were paid under the table and there is little information on the whereabouts of the culprits despite a number of prominent court cases.

They received no punishment and the 140 companies in question own 1 – 60 hectares of land each and are reselling them. However, Mongolian democracy is not mature enough for individuals to enter the streets and demand justice. The government is misusing our public property and there are no mechanisms to reclaim those



lands as they have been bought and sold numerous times. This is undoubtedly an issue of quality of governance and corruption which has reached a level that we cannot solve. The Mongolian National University (МУИС), not to be confused with the Mongolian State University (МУИС) owns 40 hectares of land in Bogd Khan mountain.

As the land was registered under the University, they are exempt from any taxes on the land. The situation has become too convoluted and the owner is protected by a powerful group of current and former politicians from a particular aimag. In Mongolia, each aimag has a council which remains unaffected by changes in administrations and essentially operates as crime syndicates, supporting businesses from their own aimag. They even cleared up access from Zaisan to Bogd Khan mountain following lengthy discussions and disputes. This is a true manifestation of the influence of the Mongolian state.

Bogd Khan mountain is several hundred years old and is one of the oldest protected areas in the world. It is now however protected in name only due to politicians and I

appeal to the politicians to not carry on this facade that it is still protected any longer. Take for example Zaisan and Yarmag which were once empty plains but are now developed to unimaginable extents. However, the public is not made privy to the owners of the land which leads us to assume that it is connected to the political leadership until proven otherwise. If the land was sold through an auction, the money that was generated could have been utilized to solve the ger district situation. It would be difficult to reacquire the land on Bogd Khan mountain as there has been a lot of money invested and it is the most expensive real estate in the country. It may however be prudent to increase the property tax on the area. The taxes on those areas should be increased from 2% to 10% but this is unlikely to happen in the current or the next administration. Hopefully, within the next 20-30 years some politicians with the willingness to fight corruption will come to power.

This review has been edited here for space and clarity. You can watch the full 30-minute review on the Defacto website [\[HERE\]](#).

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