

# Challenges and Countermeasures of China's Direct Investment in Mongolia in the Background of the Belt and Road Initiative

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## ABSTRACT

In recent years, with the development of the Chinese economy and the build of The Belt and Road, Chinese investment and trade in Mongolia have come into focus. Even with many favorable conditions, China's direct investment in Mongolia still has some challenges. Based on these, this paper analyzed the challenges of investing in Mongolia for Chinese investors and propose the countermeasures.

First it studied the current situation of Chinese investment in Mongolia, including the scale and characteristics. Then it analyzed the challenges, which included the contradiction between Mongolian cultural customs and Chinese investment activities, contradictory and unstable laws in Mongolia, poor infrastructure in Mongolia, concentrating investment of China and challenges from other competitors. Finally, it put forward some countermeasures including increasing the research and developing understand of Mongolia, as well as increasing assistance to Mongolia's infrastructure, diversifying enterprises' investments and improving the competitiveness of enterprises, to control the risks.

**Keywords:** *Mongolia, direct investment, the Belt and Road Initiative, risk analysis*

## 1. INTRODUCTION

Mongolia is rich in resources, especially mineral resources. By 2018, more than 80 kinds of minerals have been discovered, with 6,000 mining sites. The mining sector plays an important role in the Mongolian economy, with an annual growth rate of 8% to 12% of mineral output. Mongolia's mining development has attracted a great interest from international mining community. Nearly 5,000 companies from 20 countries have invested in Mongolia [1]. With the increasing size of China's economy, Chinese enterprises have become more and more eager to go abroad. In 2018, China's outbound direct investment reached \$143.04 billion, ranking among the top three in the world in terms of both flows and stocks [2].

With the continuous progress of The Belt and Road Initiative, Grassland Road in Mongolia and the construction of China-Mongolia-Russia Economic Corridor, China has become the largest direct investor in Mongolia. But the road of Chinese investment is not completely smooth. Political, legal, infrastructure, the local people's attitude and other factors all bring challenges for China's investment. This paper analyzes

the investment situation and challenges for China. It also puts forward the countermeasures, hoping to help the Chinese investors to clearly understand the environment of investment in Mongolia, formulate corresponding strategies, and make a correct judgment for investing in the Mongolian market. It hopes to help improve the scale of the investment in Mongolia, promote regional cooperation and expand China-Mongolia trade.

2. ANALYSIS

2.1. Current Situation of Chinese Investment in Mongolia

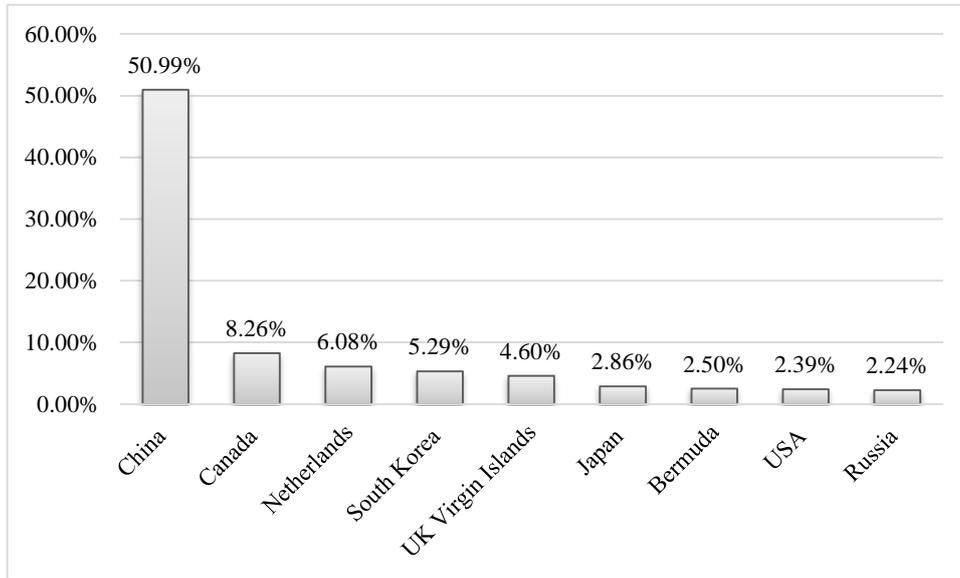


Figure 1 Ten major countries investing in Mongolia (1990-2010) [3]

It can be seen that China is the largest investor of Mongolia. According to Mongolian statistics, from 2013 to 2017, Mongolia's foreign trade totaled \$48.88 billion, while China-Mongolia trade totaled \$29 billion, accounting for as much as 59.3%. One Belt and One Road boosted in major China-Mongolia cooperation projects. By the end of 2017, China's direct investment in Mongolia had exceeded \$4 billion, accounting for about 30 percent of the total foreign investment. Chinese companies' direct investment or contracted projects in Mongolia have created nearly 100,000 jobs and paid nearly \$2 billion in taxes. Since the Belt and

Road Initiative was put forward, China has greatly increased its assistance to Mongolia and granted preferential export buyer's credit, and implemented a number of important projects in Mongolia that are conducive to the local social and economic development. From 2013 to 2017, the number of Chinese personnel training in Mongolia increased significantly, and the five-year training target of 1,000 Mongolian personnel announced by President Xi during his 2014 visit to Mongolia was completed in 2016 [4]. It can be said that one of the characteristics of Chinese investment in Mongolia is its large scale.

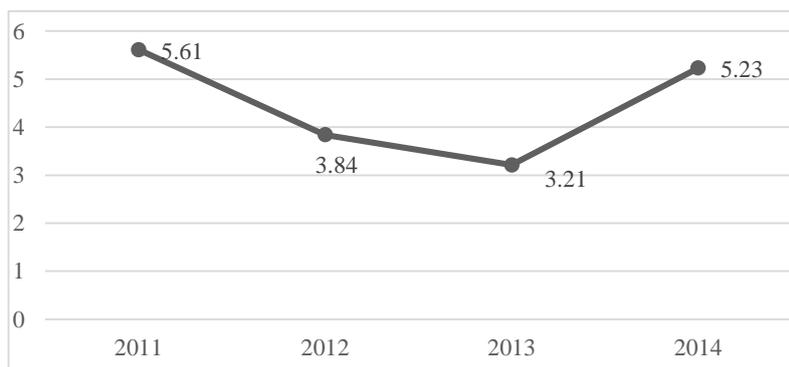


Figure 2 China's direct investment in Mongolia (\$100 million) [5]

Chinese investment in Mongolia is not always rising or falling, but existing volatility. This is largely due to changes in political laws in Mongolia. For example, the increase of Chinese investment to \$523 million in 2014 was due to the improvement of the legal environment for investment in Mongolia.

So far, seven foreign investment companies have signed product-sharing contracts with the Mongolian petroleum administration and engaged in mining and oil exploration on Mongolian territory. Of the seven, four are Chinese investment companies.

**Table 1** Chinese investment companies [6]

Company Name	Investment Volume
Daqing tamucag co. LTD	More than \$7.423 million (1994-2008)
Sinopec Shengli oil field Dongsheng company	Over \$100 million totally
China Golden C Petroleum	\$9.16 million totally
Zong Hen Yu Tan	The company signed a product-sharing contract on 20 May 2009 and plans to invest \$43 million in Mongolia over five years

Therefore, the third characteristic of Chinese investment in Mongolia is the concentration of mining industry. Due to the high cost of mineral investment, there are certain scale and technical requirements for investment enterprises, so the number of enterprises investing in mineral resources is relatively small but with large investment intensity.

## **2.2. Challenge of China's Investment in Mongolia**

### *2.2.1. The Contradiction Between Mongolian Cultural Customs and Chinese Investment Activities*

The nomadic mode of life is deeply rooted in Mongolian society, which gives the Mongolian people great respect for their land and a strong desire to protect resources. Such cultures and traditions have led to a sense of xenophobia among some Mongolians. The most intuitive phenomenon is the opposition to foreign participation in the development of natural resources, and that China's development and investment in Mongolia is the plunder of local resources. Many Mongolians want to maintain national control of their natural resources. Many locals resent the presence of Chinese companies in the zone, causing friction that increases the risk of Chinese investment. There is an intuitive example. In 2012, in the face of rising nationalism, Mongolia enacted the great Foreign Investment Coordination Law in Strategic Areas, which completely closed the door to Chinese investors in mining, financial and other communication industries.

However, after kicking out the foreign investors, Mongolia's foreign direct investment fell 55% year on year and Mongolia's economy immediately stagnated. Not only did the economy grow slowly, but it also ran up huge foreign debts. Although the rule was repealed the following year, the enthusiasm of foreign investors has been completely extinguished. People always worry about the conflicts of investment activities and cultural norms.

Another point that cannot be ignored is that some companies did not investigate the national conditions of Mongolia in advance, resulting in disputes, which undoubtedly increased people's resistance to Chinese investment in Mongolia.

### *2.2.2. Contradictory and Unstable Laws in Mongolia*

Mongolia has a multi-party system, with a four-year transition, and the new government will often overturn the policies of the previous government in order to promote their political objectives. The changeable policies hit the enthusiasm of Mongolian investment enterprises. Take the mineral resources law as an example. Mongolia promulgated different mineral resources laws in 1994, 1997 and 2006. The current mineral resources law has been amended more than 10 times since it came into force in July 2006, including twice a year in 2010, 2011 and 2014 [8].

For another example, after the Mongolian parliament passed the law on coordination of foreign investment in strategic areas restricting foreign investment in May

2012, Mongolian coal companies unilaterally suspended contracts with Chinese companies that had been approved by the two governments in early 2013. They halted coal exports and demanded higher coal prices, resulting in heavy losses to both sides.

### *2.2.3. Poor Infrastructure in Mongolia*

In 2013, Mongolia transported about 21 million tons of goods by rail, including 10.7 million tons domestically, 6 million tons for export, 2.5 million tons for import and 1.8 million tons for transit. In 2013, Mongolia's railways transported 3.781 million passengers, including 3.609 million domestic passengers and 173,000 international passengers. Due to the aging of railway equipment and technology, coupled with the adoption of wide-gauge standard in Mongolia, the cost of railway transportation between China and Mongolia has increased, which restricted the development of Mongolia's economy, especially the export of mineral products [9]. Power supply in Mongolia is mainly composed of power systems in central, western and eastern regions. Currently, 2 provinces and more than 40 counties are still not connected to the central power system. Backward transportation and communication conditions have created challenges for enterprises to invest.

### *2.2.4. International Challenges*

International capital has never given up its competition for Mongolia's resources and market. With the expansion of China's direct investment in Mongolia, it is facing increasing competitive pressure from companies from other countries. Compared with developed countries, Chinese enterprises are relatively weak in technology and management, and lack of professional and compound talents, all of which make it riskier for Chinese enterprises to invest in Mongolia.

Since the establishment of diplomatic ties between the republic of Korea and Mongolia, major breakthroughs have been made in economic cooperation. In August 2011, the two countries upgraded to a comprehensive partnership, implementing a medium-term cooperation plan on energy development and natural resources. The United States granted permanent most-favored-nation status to Mongolia, and signed a series of documents including customs cooperation agreements, supporting investment agreements, and economic and trade cooperation agreements [10]. Japan is increasing its aid to Mongolia, even free of charge, and Japan is the largest donor to Mongolia. Japan has a shortage of natural resources and their market has a strong need for them. The two countries signed an economic partnership agreement,

giving Japan a big advantage in developing oil and uranium [11].

## **3. SUGGESTION**

### *3.1. Strengthen Communication with Mongolia*

Economic and cultural exchanges are essential. Companies are supposed to broaden the channels of cultural exchanges, strengthen cooperation in the cultural field. Enterprises can carry out educational cooperation such as establishing cultural schools in Mongolia in order to reduce the Mongolian people's defensive mentality towards China and then to make more Mongolian people know about Chinese culture and people.

Companies can also increase assistance to the region to gain local inhabitants' acceptance and support for investment by Chinese companies. For example, companies can set up some jobs for local people to improve the problem of employment and even raise employment benefits of Mongolia.

Having a deep understanding of the investment objects is of great importance. Before going abroad, Chinese enterprises should organize training for Chinese personnel to make them understand the national conditions of Mongolia, including its cultural customs and etiquette. Also, it is crucial that investors should know Mongolia's policies on absorbing investment clearly before making investment plans. After going abroad, employees of Chinese Enterprises should respect others' culture and civilization and keep good behaviors. In addition, they should attach importance to environmental protection, putting environmental protection in the first place and make the mining area green and ecological restoration, considering the interests of local residents [12].

### *3.2. Increase Assistance to Mongolia's Infrastructure*

Chinese companies can increase assistance for infrastructure construction in Mongolia, which has a fragile natural environment and poor infrastructure. China can increase the low-interest loans and free assistance for Mongolia's infrastructure, which can increase the goodwill of the Mongolian people towards China, and at the same time, provide convenience for Mongolia's mineral exploitation, so as to facilitate future investment activities.

### *3.3. Diversify Enterprises' Investments*

Many large state-owned enterprises in Mongolia invest too much in mining industry, while small and medium-sized enterprises invest more in light industry. Fierce competition between each other brings more risks

to the development of enterprises. Chinese enterprises should diversify their investment and explore other backward industries in Mongolia. This cannot only help enterprises to expand the Mongolian market, but also to disperse the investment risk of enterprises.

### **3.4. Improve the Competitiveness of Investors**

The overall management level of Chinese enterprises is generally not high, which directly affects the development of investment. Investors should improve their scientific decision-making ability, develop their core business, build their own brand, increase their market share in Mongolia, so as to enhance their competitiveness and build a brand with high quality performance and industry influence. In addition, due to the situation of Mongolia, Chinese enterprises should train foreign investment management personnel who are familiar with Mongolia's policies and environment. They can also recruit overseas students to provide greater guarantee for investment in Mongolia

## **4. CONCLUSION**

China's investment in Mongolia is currently concentrated in mineral resources and accounts for a relatively high share of Mongolia's investment. The reasons for China's investment risk are as follows. First, the nomadic culture and nationalism of Mongolia sometimes make Mongolians hate and do not cooperate with China's investment activities. Second, Mongolia's laws are not stable, often changing, increasing investment risk. Third, Mongolia's backward infrastructure restricts China's investment activities to some extent. Fourth, China's investment activities face competition from developed countries. In view of these, the following suggestions are put forward: First, the two governments should conduct in-depth and effective communication and, as far as possible, work out stable and sound laws and regulations on Chinese investment through consensus. Secondly, Chinese investors need to strengthen the research on Mongolia, respect the Mongolian culture in their investment activities, and protect the natural resources of Mongolia. In addition, China can help Mongolia in infrastructure construction. Enterprises can choose to diversify investment, diversification of risk, at the same time, should also strengthen their competitiveness.

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