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An Analysis of Mongolia's Resource-Led Development: the Impact of Foreign Direct Investment in the Extraction Industry

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Abstract:

It has been 26 years since Mongolia transitioned to democracy. I decided to evaluate the progress of Mongolia's development since the transition to evaluate whether the country of only 3 million people with vast land and natural resources successfully implemented policies to attain growth and societal wellbeing. In order to evaluate Mongolia's development progress, this thesis uses FDI in Mongolian development since 1990 as a case study to examine the relationship between FDI, state development strategies, and development outcomes. My research questions encompass a series of interrelated inquiries including 1) whether *human* development can be achieved through extraction industries 2) whether the source of FDI has a strong impact on development outcomes, and 3) whether FDI influences state-led development efforts and decision making to the extent that it threatens the development of Mongolian sovereignty.

I conclude that Mongolia is at a crossroads. Foreign direct investment in the extraction industry can either help or harm Mongolian development; the long-term results of FDI will depend upon the Mongolian government's actions. The source of the FDI does not have a strong impact on development outcomes. There are some differences in industry conduct regarding transparency and corporate social responsibility based upon the source of funding. The main responsibility for attaining development falls to the Mongolian government. However, my research indicates that FDI could have a corrosive impact on state sovereignty if the state is weak in enforcing rule of law. Surprisingly, I find that a strong, active civil society is necessary to maintain the integrity of development strategies in the face of significant FDI.

TABLE OF CONTENTS

Figures / Tables

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CHAPTER I: INTRODUCTION

The year 1990 was a turning point for the Mongolian people. The fall of the Soviet Union allowed its longtime satellite state, Mongolia to create its own path towards development. Like many postcolonial states, Mongolia adopted a democratic system of governance and a capitalist free market economy to advance the country's economic growth and societal progress. Fast-forward 26 years later, I decided to evaluate the progress of Mongolia's development. I wanted to address whether a country of only 3 million people with vast land and natural resources has successfully implemented policies to stimulate economic growth and development.

In the past, the Mongolian economy depended on agriculture and traditional herding. Today, Mongolia is a developing country with abundant mineral resources. The recent mining boom in Mongolia has helped the Mongolian Gross Domestic Product (GDP) grow at a double-digit rate in 2011 and 2012. Some have gone as far calling Mongolia "Minegolia" (Langfitt, 2012). Mongolia's natural resources are exported to its southern neighbor, China, whose rapid industrialization requires significant amount of natural resources. The insatiable Chinese demand for natural resources became the perfect market for Mongolia's export sector. The vast amount of mineral riches quickly turned the Mongolian extraction industry to become the biggest contributor to the country's GDP.

In order to develop its extraction industries, the Mongolian government increasingly relies on Foreign Direct Investment (FDI) for infrastructure and technology development. Foreign investors have provided a substantial amount of funds to develop Mongolia's extraction industry. Currently, copper and coal are the top export commodities that provide a significant contribution to the Mongolian economy (The Observatory of Economic Complexity, n.d.).

Given Mongolia's abundant natural resources, Mongolia has the opportunity to use extraction industries to jumpstart development. This thesis evaluates Mongolia's development progress by examining the promise and pitfalls of FDI in the extraction industry by using post-1990 Mongolia as a case study. This thesis employs comparative case study of the mines to investigate whether the extraction industry can lead an effective and sustainable development strategy. Additionally, I look at whether the source of the FDI makes a difference in development efforts. Finally, I look at the factors of state regulation and management of FDI, and the involvement of civil society in creating accountability for state sponsored development strategies.

Thus, the research questions encompasses series of interrelated inquiries including 1) whether *human* development can be achieved through extraction industries 2) whether the source of FDI has a strong impact on development outcomes, and 3) whether FDI influences state-led development efforts and decision making to the extent that it threatens the development of Mongolian sovereignty. These series of inquiries will help in understanding the relationship between FDI, state led development strategies and development outcomes.

In the end, I conclude that the extraction industry can either help or harm Mongolian development; the long-term results of FDI will depend upon the Mongolian government's actions in managing the FDI. In terms of understanding FDI's role in development outcomes, I conclude that the source of FDI does not significantly impact the development outcomes. There are some variances in the business conduct of the companies' transparency and corporate responsibility. However, the development outcome depends more on the state's ability to manage foreign investments. Finally, my investigation into whether FDI can influence state decision-making process showed that FDI could have an adverse effect on the state sovereignty. The comparative case study showed that foreign investors could diminish state sovereignty by challenging rule of law in the host country. Such hindrances to the exercise of state sovereignty by the foreign investors could result in erosion of the state. However, most importantly, the case study showed that it requires a strong civil society to hold the government accountable for maintaining the integrity of development strategies in the face of large FDI.

The following chapter will begin by drawing knowledge from existing bodies of literature on development theories, Chinese Foreign Direct Investment patterns, and extraction industries. Chapter Three will consist of background information on the current state of political and economic development in Mongolia. Chapter Four contains the methodology this research utilizes to examine the case studies. Chapter Five contains a comparative case study of two prominent mines in Mongolia to demonstrate the dynamics of FDI in the extraction industry. Finally, Chapter Six analyzes the results of this comparison and concludes this research.

CHAPTER II: LITERATURE REVIEW

This thesis draws knowledge from three existing bodies of literature to help assess current trends in development in Mongolia. The first section of this literature review surveys the evolution of ideas about development to aid in understanding the recent trends in Mongolia. I also review recent literature on Chinese foreign direct investment in order to provide an understanding of how Chinese influence has expanded over the years and how Mongolia is impacted by their economic influence. The final section explains the role of extraction industries in the development process. Together, this literature provides a background for understanding current development conditions in Mongolia.

Development Theories

Economic development discourse became a central issue following World War II. It was shaped by the Western Allies' efforts to provide financial support to exert political influence in newly emerging independent states (Staples, 2006). American foreign policy sought to ensure that the newly independent states would not fall under the communist bloc. Cold War politics encouraged the promotion of capitalism in emerging developing countries (Staples, 2006). Although there have been different approaches to development, five main theories are most prominent: modernization, structuralism, dependency theory, neoclassical theory, and recently, theories concerning sustainable human development. Over time, development theories evolved as scholars differed over the best means of attaining economic, social and political progress in underdeveloped countries. In the more established notions of development, stimulating economic growth was given significant emphasis (Staples, 2006). However, current development discourse is shifting towards a stronger consensus that rejects the exclusive focus on economic growth and moves towards sustainable development that also prioritizes human rights, sustainable environment, and social, political and economic freedoms (Sachs, 2015; Stiglitz et al., 2010; Hosseni, 2003; Alkire and Deneulin, 2009).

In the 1950 to 1960s, modernization theory was the dominant development concept. Modernization theory stemmed from the American foreign policy that encouraged developing countries to industrialize to foster economic growth and at the same time, to discourage Communist affiliation (Engerman et al., 2003). Modernization theory urged a complete break from traditional societies to embrace modernity as defined by the West. One of the most influential modernization theorists, Walt W. Rostow, established the model of linear “stages of growth” which asserted that developing countries must go through certain stages of growth to achieve full development. The initial stage involved breaking away from traditional society (Rostow, 1960). Additionally, modernization theorists believed that all societies could achieve sustainable development through implementing liberal capitalist policies (Engerman et al., 2003). Modernization also meant mirroring the Western lifestyle by reforming the economic, political and social structures of traditional society for “genuine development” including industrialization, the adoption of western technology, and education centering on capitalist economic development theories (Gilman, 2003).

In Inglehart and Baker’s (2000) analysis of modernization theory, they argued that modernization is “probabilistic, not deterministic.” Unlike the modernization theorist who believed in a mechanistic and linear process of development, they argue that economic growth does not have a predictable growth pattern because there are too many factors that can influence the outcome of development. Finally, they argued that economic growth does change some aspects of culture, but the values of a country do not change easily due to fundamental differences in the value systems of rich and poor nations (Ingelhart and Baker, 2000). Other critics of modernization theory postulate that the linear development model is incorrect. Matunhu (2000) argues that the oversimplification of modernization theory is its greatest fault. Not all countries follow the same explicit linear path. The structural makeup of a particular developing country is significantly different from rich, as well as other developing countries.

At the end of 1960's to 1970's, structuralist theorists gained popularity. Structuralist discourse centered on Keynesian economics and advocated for government intervention in some economic sectors and recommended institutional and market structural reform (Lin, 2012; Fischer, 2015; Cimoli and Porcile, 2010; Storm, 2015). Structuralist theorists maintained that the failure of previous development theories was due to inapplicable development models imposed by Western dominance. In developing countries, capitalist economic policies were not successful in stimulating economic growth due to structural makeup of the developing countries.

Additionally, structuralist scholars argued that underdevelopment of developing countries persists due to the technological and industrial structure differences. Developed countries have superior industrial market and technology over the developing countries (Cimoli and Porcile, 2010). The developed countries use their superior industrial markets and technology to suppress the developing countries' economies. Therefore, the authors argue that the best strategy for development is to reduce the technology gap, increase international competitiveness and encourage developing countries' export industry to compete in the global market. (Cimoli and Porcile, 2001).

In the recent structuralist discourse, authors Lin (2012) and Ghose (2010) argue that the inequality between developed and developing countries is due to a substantial income and technology gap. The authors agree that structural adjustment is necessary for eliminating the gap between the rich and poor countries. Previous theory on modernization advocated for a complete break from the traditional society, however, Ghose (2010) argues that traditional industry can coexist with modern industries. The simultaneous development of both traditional and modern industries can help close income inequality.

Following the 1970s, international dependency theory emerged to explain development. Dependency theory argues that in the capitalist world, there is an uneven division of labor between developed and developing countries (Todaro and Smith, 2009). The World Systems Theory developed by Immanuel Wallerstein argues that the world is divided into core, semi-periphery, and periphery based upon an international division of labor (Wallerstein, 2004). Core (developed) countries have a strong central government with capital-intensive industries and a highly skilled workforce. Peripheries are the developing countries that lack strong government, labor-intensive industries and a low-skilled workforce. Semi-peripheries are developing countries that are industrializing countries that fall between the core and the periphery. They all operate in a capitalist world economy where the core controls international markets and develop unequal trade relations benefitting the core, but not the rest of the world (Wallerstein, 2004). Todaro and Smith add that the core's exploitive activities in the (periphery) countries perpetuate underdevelopment of the developing countries. In other words, the authors contend that underdevelopment was an externally induced phenomenon by the developed countries as a result of the power imbalance. (Todaro and Smith, 2009). Vernengo (2006) adds that the core conducts its power through the means of financial dependency. Developing countries require a substantial amount of financial loans to develop technology, infrastructure, and industrial sectors.

At the end of the 1970s, neoliberalism became the central development discourse. The framework for neoliberal theory relied on adopting the Westernization tenets from modernization theory; however, neoliberal theorists relied on market forces rather than state actions. The theorists argued that too much state intervention, inefficiency in resource allocation, and lack of economic incentives to stimulate economic growth causes underdevelopment (Lin, 2012; Todaro and Smith, 2009). Lin (2012) writes that the neoliberal school of thought firmly believed that free markets, privatization, free trade and deregulation of government would stimulate economic growth, and the growth would eventually “trickle down” to alleviate poverty (Lin, 2012).

Critics of neoliberal policies argue that such policies are often unsuccessful in developing countries because of the fundamental nature of the institutional, economic and the social structure of the developing countries (Todaro and Smith, 2009). Many of the developing countries in Latin America failed to develop through neoliberal policies due to the political structure of central government and economies heavily controlled by the government. Similarly, Lin (2012) argued that in the 20th century, countries like China and India achieved remarkable economic growth without following the basic guidelines of neoliberal policies. While the neoliberal theorists claim that the invisible hand of the free market promotes the general welfare of the people, critics like Todaro and Smith (2009) contend that on the contrary, the free market strategy helps those who are already well off (Todaro and Smiht, 2009). Similarly, John Rapley (2007) argued that although neoliberal policies resulted in some positive gains in some of the more advanced developing countries, in poorer countries, it was less effective, and in some places did more harm than good. The neoliberal policies that opened up their market to cheap international goods hurt local businesses and had an adverse effect on economic growth. Additionally, Ruccio (2011) argued that economic policies imposed by Structural Adjustment Programs (SAP) did not solve development problems but intensified income inequality, social injustice, and environmental degradation.

In general, most development theories have a great emphasis on economic growth as the answer to underdevelopment. However, starting in the 1980s, various development theories questioned the previous development theories that were developed by the Western countries. The post-development school of thought questioned theories such as industrialization, modernization, and neo-liberalization and has expressed discontent with the status quo (Schneider, 2010). Post-development theorists emphasize alternatives to development that involve more local participation (Ziai, 2009).

Much like post-development theory, sustainable development theories appeal for the reduction of capitalist production and consumption to focus on policies that benefit the well-being of humans, as well as the sustainability of the environment. Schneider et al. (2010) argue that sustainable development rejects principles that give prominence to economic growth as the primary objective and argue that “sustainable degrowth” exposes “growth fetishism” as the main problem of underdevelopment. Ross (2009) and Perkins (2013) advocate for sustainable environment policies to curb consumption of energy, environmental degradation, and air pollution. Additionally, Sachs (2015) contributes to sustainable development theories by advocating for good "economic prosperity, social inclusion and cohesion, environmental sustainability, and good governance by major social actors, including governments and business" (Sachs, 2015, pg.4). The author accords responsibility to individual states and also to the international actors, such as multinational corporations, that have the power to change policies.

Amartya Sen (1999) argues that development is distinct from economic growth. His broader concept of development encompasses economic growth, but also prioritizes improving the conditions of individuals by addressing poverty, unemployment, social and economic inequality, and various forms of discrimination (Sen, 1999; Hosseni, 2003). Additionally, Aknuluy et al. (2015) argued for alternative forms of development by advocating the necessity of addressing the environmental cost of prioritizing economic growth.

Similarly, prominent scholars like Stiglitz, Sen, Fitoussi (2010) and Hosseini (2003) questioned the validity of using of Gross Domestic Product (GDP) as the proper means to measure growth and progress. Stiglitz et al. (2010) contended that there are too many nuances to societal progress that an exclusive focus on GDP fails to include. The authors explained that the multifaceted nature of societal wellbeing needs not only aggregate data on income, but also its distribution (Stiglitz, et al., 2010).

Critics of these models of development like Sampath question the feasibility of constructing a new vision for development with an emphasis on societal wellbeing. Sampath (2014) states that it is not feasible for scholars to produce a development discourse based on assessing societal wellbeing due to its multidimensional nature. However, scholars Alkire and Deneulin (2009) posit that evaluating people's freedoms could assess societal well-being. According to Alkire and Deneulin, enriching people's freedom of self-determination to a healthy life, education, employment and political and social participation is the foundation of development (Alkire and Deneulin, 2009). The principle argument is to reimagine growth, not in economic terms, but as social and political improvement. Societal growth includes economic sustainability, environmental protection, addressing income inequality, poverty measurement, and advocating for quality of life for all (Stiglitz et al., 2010; Hosseni, 2003; Alkire and Deneulin, 2009). Additionally, some have attempted to incorporate human rights into development discourse. Marks (2010) argues that human rights and development studies share a common goal towards progress in societal well-being.

> Marks (2010) states the following: … human rights and development share a common finality and a concern with the potential of empowerment, suggesting a more hopeful role for human rights in development, as a vehicle for empowerment and social transformation in which human rights *are* development objectives. (p.2)

The evolution of development theories post WWII suggests that economic growth is no longer the singular focus of development. History has shown that capitalist policies were not successful in stimulating economic growth, but rather perpetuated underdevelopment. In recent years, development has surpassed the significance of economic growth to embrace societal well-being, people's freedoms and protection of human rights.

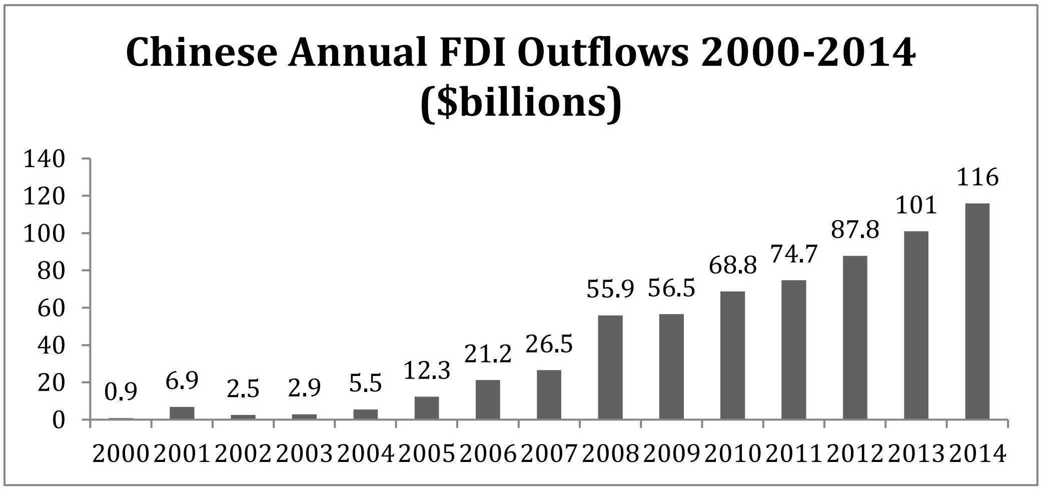
The following section surveys literature on Chinese foreign direct investment. Since the early 2000s, China has been rapidly industrializing and expanding its international power. One of its strategies for expansion is outward foreign direct investment. China has become an alternative to the existing Western financial institutions for international aid, loans, and investment. The following section will help assess Chinese investment practices overseas, and help contextualize its practices in Mongolia.

Chinese Foreign Direct Investment

Some scholars have argued that the source of FDI matter in foreign investment practices. The following bodies of literature focuses on Chinese foreign direct investment due to the strong political and economic ties between China and Mongolia. Since China is the biggest trading partner of Mongolia, the Mongolian economy is highly dependent on the Chinese demand for Mongolia's export commodity. Therefore, it is important to take a look at Chinese FDI specifically.

China's outward direct investment (ODI) has grown substantially over the last decade. According to the 2016 World Investment Report from the United Nations Conference on Trade and Development (UNCTAD), China is the third largest outward investor in the world, following the United States and Japan respectively (UNCTAD, 2016). The scale and the extent of Chinese investment grew exponentially since the introduction of the "Going-Out" economic policy of 2001. The chart in Figure 1 shows the growth of Chinese outward investment. The Chinese government actively encouraged foreign investment in the developing countries through loans, bilateral and multilateral trade and various forms of debt cancellation. The Chinese ODI has been rapidly growing in three distinct sectors: service, manufacturing, and mining. These Chinese industries invest all over the world in areas ranging from developed countries like United States, Canada and Australia to developing poor nations like Sudan, Nigeria, and Myanmar. Although China's investment contributes significantly to the developing countries, there have been common concerns over its investment motivations and implications.

Figure 1



Source: Congressional Research Service

According to Jiang (2009), Chinese strategy for ODI is an externalization of its development paradigm. The author contends there is a linkage between Chinese domestic development policies and its actions overseas. Chinese extraction strategy is driven by its need to secure natural resources and its aggressive measures to secure them is evident in its domestic and international practices. These aggressive measures can result in detrimental social consequences in the host countries, such as unsafe work conditions that can lead to industrial accidents, environmental disasters from extraction industries, and economic inequality (Jiang, 2009).

Kolstad and Wiig's (2012) research reveals that there is a distinct political pattern to the investment decisions of Chinese ODI. First, Chinese companies are attracted to large markets of the Organisation for Economic Co-operation and Development (OECD) countries. Chinese manufacturing services target large markets to export cheap commodities.

Second, Chinese foreign direct investment in natural resources target countries with weak institutions and abundant natural resources. Further analysis indicates that this second pattern is valid to non-OECD countries (Kolstad & Wiig, 2012). Additional research by the authors finds that Chinese oil extraction industries in Africa are likely to prop up repressive regimes, benefiting a few elites while the majority of Africans see little to no benefit to their investment (Kolstad & Wiig, 2011). For example, the authors assert that China invests in the Sudanese oil industry even though other Western investors condemned Sudanese human rights violations and terminated their trade deals (Wiig and Kolstad, 2011). China used the investment vacuum as an opportunity to import Sudanese oil, while exporting manufactured good and weapons to Sudan (Wiig and Kolstad, 2011).

Tan (2012) posits that another motivation for China's overseas investment is to diversify Chinese markets and strengthen Chinese financial positions in the international arena. The author adds that the Chinese global expansion is to create an alternative financial framework to the one developed by Western countries. China's strategy to increase its competitiveness in the international market involves various financial assistance to African countries in the form of debt relief, loans with longer terms than the Western financial organizations, and loans with little to no political restrictions (Peh and Eyal, 2010). Similarly, Mol (2011) adds that Chinese banks gain an advantage by providing lower ethical and environmental standards than an international organization such as WB, IMF and EU Investment Bank. Consequently, Western financial institutions claim that China's "no strings attached policies" undermine international standards and promote widespread corruption (Peh and Eyal, 2010).

The employment practices of Chinese investment overseas are questionable. Peh and Eyal (2010) explain that many Chinese migrant workers are often assigned managerial jobs, while hired African workers work in negligent and unsafe work environments. In addition to the improper work environment, some Chinese companies force workers to work overtime and disregard local labor laws (Anshan, 2007). In 2011, Human Rights Watch (HRW) reported labor abuses in the Chinese Copper Mines in Zambia. In the report, HRW claimed that Chinese companies provided insufficient protection for workers' safety and wellbeing. Many of the workers risked their health by working without a proper gear (HRW, 2011). Anshan (2007) adds many workers were threatened with termination if the employees voiced complaints or refused to work.

Additionally, Anshan (2007) argues that local employment suffers due to Chinese company managers' preference for hiring Chinese nationals. Often, the local communities do not believe that the Chinese companies contribute sufficiently to the local economy when locals do not have employment opportunities (Adisu et al., 2010). Jiang (2009) explains that the Chinese exploitative domestic policies on low wageworkers are reflected in their overseas employment practices.

Chinese presence has also had an adverse impact on the economic conditions of the host countries. Adisu et al., (2010) argue that the expansion of trade relations between China and the African nations have benefited China more than the African countries. Peh and Eyal (2010) reason that Chinese trade could lead to a low-cost manufacturing base in a host country that could hurt existing industries. For example, hypothetically, a Chinese textile factory in Vietnam can hurt existing Vietnamese textile business by providing cheaper, low-cost manufactured goods. Additionally, cheap Chinese commodities can enter the host countries' market and compete with the domestic businesses. Adisu et al. (2010) revealed that the African markets became flooded with cheap Chinese products causing competition between domestic markets and Chinese manufacturers. Local industries cannot compete with the low prices of Chinese commodities and ultimately lose business to the Chinese manufacturers (Adisu et al., 20.10).

One of the most criticized aspects of Chinese investment practices overseas is their lack of environmental consideration. Jiang (2009) argues that Chinese domestic environmental policies (or the lack there of) translate to its lackluster international environmental policies. The author argues that since the structure of domestic Chinese environmental policies entails lax regulations and the absence of strong enforcement, Chinese companies are unlikely to promote effective environmental consideration in their business practices abroad (Jang, 2009). Accordingly, Chinese enterprises exploit African countries that do not possess strict environmental regulations.

In 2014, the Chinese government introduced “Guidelines for Social Responsibility in Outbound Mining Investments” to address human rights, labor issues, and environmental issues. However, the guidelines are recommendations and are not enforceable (Moi, 2011). Tang-Lee (2015) adds that the policies are more of a placation than a resolution. Chinese companies provide short-term concessions while neglecting major community grievances. Consequently, the scholars recommend a serious change in the regulation practices of Chinese enterprises and stricter policy regulations in the host countries (Tang-Lee, 2015).

The literature on Chinese foreign investment practices in natural resources reveals interesting results. First, Chinese investment is motivated by the need to secure natural resources for its rapid industrialization. Often, this motivation leads to aggressive measures to attain natural resources. Second, China is not only enhancing its domestic power, but it is also expanding its international power. Until recently, China was an investor seeker, but recently, it has positioned itself to become an investment provider. The China has become a global player through its successful “going out” policy.

The following section presents literature on the extraction industries. The scholarly work analyzes the effect of extraction-led development. The knowledge drawn from this investment discourse can help explain how Mongolia can attain development by prioritizing extraction industries, and the risks associated with resource-led development.

Extraction Industries

Many capital-scarce developing countries attempt economic growth through extraction industries with very limited success. The economic underperformance of resource-rich countries has garnered much attention and research. Many have debated the failure of economic growth in resource-rich countries. Most studies suggest that there is evidence of a “resource curse” where countries with abundant natural resources tend to experience slower economic growth (Bhattacharyya and Collier, 2011). Others argue resources themselves are not a curse; they can bring opportunities for economic growth, but the weak political and regulatory structure can lead to a slow economic development (Mehlum, Moene, and Torvik, 2006). Countries with weak institutions are hurt by resource abundance because weak institutions are susceptible to corruption and the revenue from the resources can enrich elite few. Therefore, the resource boom becomes a “resource curse.” However, in institutionally strong countries, resource revenue is invested into the domestic economy and can become a “blessing.”

Some scholars argue that natural resource revenues can contribute to national economic growth if the government of the resource-rich country takes advantage of it. Bhattacharyya and Collier (2011) argue that conceptually, it is simple to image economic growth through a resource boom. The government can tax resource rent for potential investors, and use the revenues to invest domestically, which can encourage economic growth. However, this scenario has not usually panned out. Natural resource-led development alters the structure of the economy. Venables (2016) explains that this phenomenon is considered a "Dutch Disease" where extraction industries' displace other tradable industries, causing a decline in the country's competitiveness in the international market. Similarly, Sachs and Warner (2001) also argued that resource abundant countries tend to focus on extraction industries and are likely to neglect developing other export industries. Fast revenues from mining encourage more profit allocations to develop the mining sector further while other tradable sectors like agriculture become defunded and neglected. Extraction-led development creates a new economic structure highly dependent on the revenues of one sector (Venables, 2016; Sachs and Warner, 2001).

The problem of dependency is that resource revenues can be highly volatile. Pegg (2006) reasons that when countries become dependent on an extractive industry, they also become more vulnerable to economic shock. Resource revenues depend on the stability of the international market prices of the product. A price of a commodity can be highly unstable and unpredictable. If the market price of a product falls, so does the resource revenue. Therefore, the government is dependent upon highly risky income to meet its budget (Pegg, 2006). Additionally, Venables (2016) contend that weak governments have a difficult time with fiscal discipline. The increase in revenues allows the government to postpone crucial economic policies and push policies to that advance extraction industry (Venables, 2016).

There is a significant amount of research that argues that the institutional makeup of a country determines if a resource boom is a blessing or a curse. The failures of African resource rich countries are well known. However, countries like the United States, Australia, and Canada were once resource wealthy countries and were able to achieve substantial economic growth. Pegg (2006) argues that countries like the United States, Canada, and Australia differ from the African countries because of stable legal and financial institutions existed in those countries before their extractive industries developed.

Venables (2016) argue that resource politics can play out in democratic as well as autocratic countries. However, adverse resource politics are more apparent in authoritarian states. Ross (2001) explains that authoritarian governments are more likely favor the needs of the wealthy than the poor. In such countries, the poor do not have the power to voice their concerns to influence government policies (Ross, 2001). Resource-dependent countries spend revenues bolstering their security to help suppress protestors and activist against the government. Venables (2016) also argue that resource revenues can encourage autocratic leaders to consolidate power and often, increase the risk of conflict. Pegg (2006) cites a World Bank study that revealed countries with greater dependency on resource revenue are significantly more at risk of conflict. Furthermore, a primary cause of the conflict was related to the allocation of resource revenues. Ferguson (2006) takes the argument further and explains that many extractive industries in Africa use private militaries to ensure control over the extraction industries. Ferguson (2006) recalls the security-led approach of the Angolan model, featuring private corporations that exploit natural resource rich territories and then employ private militaries to ensure security while corrupt government officials provide legal rights to the corporation as a bribe. Sachs and Warner (2001) similarly argue that the in such conditions, the country is no longer in a developmental state, but a predatory one.

According to scholars, resource dependence has a negative effect on poverty. Ross (2015) concluded that in the analyses of resource dependence and Human Development Index (HDI), there was a strong correlation on mineral dependence with a lower standard of living and a high rate of poverty. The author argues that in corrupt, resource-rich countries, revenues from the resources are unlikely to be invested in public programs such as health, education, and poverty alleviation (Ross, 2015). The revenues from resource extraction stay in the pockets of few elites, while a majority of the public do not benefit from the resource profits.

One of the social benefits of economic development through extractive industries is the promise of infrastructure development. However, Pegg (2006) argues investors often develop infrastructure in strategic methods where infrastructure primarily benefits corporate use. For example, newly built roads and transportation systems are targeted towards helping the investors rather than the locals (Pegg, 2006).

Additionally, some scholars argue that extractive industries can create jobs in the mining sector and income from employment will generate economic growth. While it is certainly true that a resource boom creates employment, Pegg (2006) argues that extractive industries are not labor intensive but capital intensive. Thus, the creation of jobs is rather small in comparison to other industries such as agriculture. Furthermore, extractive industries can have an adverse impact on the unemployment rate. Since the non-mining sectors lose competitiveness in the international market, industries close down causing an increase in the level of unemployment. Additionally, some corporations bring foreign workers to work in the mines and do not contribute to the local economy.

The literature on extraction industries provided insightful knowledge. Developing economies need a sustainable economic growth to decrease poverty and to advance public capital. However, resource-led development is not sustainable since it depletes the natural resources. Also, as mentioned above, overdependence on one industry is highly precarious. Additionally, countries with a limited ability to control all parts of government administration are at risk of an increase in corruption.

The existing scholarly work on development, Chinese foreign direct investment, and extraction industries provided great insight into how resource-rich countries develop. The knowledge drawn from the review will contextualize Mongolia’s current development.

CHAPTER III: HISTORY OF MONGOLIA SINCE 1990

Background information

In 1990, Mongolia peacefully transitioned from seven decades of socialism to democracy. The transition was internationally praised for the absence of violence and commended for its swift transition after the fall of Soviet Union. The democratic transition entailed significant political and economic reform. Politically, Mongolia decentralized from a one party system to a multiparty parliamentary system. The Prime Minister who is appointed by the President heads the government. Parliamentary elections are based on a parallel voting system. Economically, Mongolia adopted a free market economy where government plays a smaller role, and private companies spearhead economic growth. The government quickly privatized state enterprises and reformed tax policies to transition to the market economy.

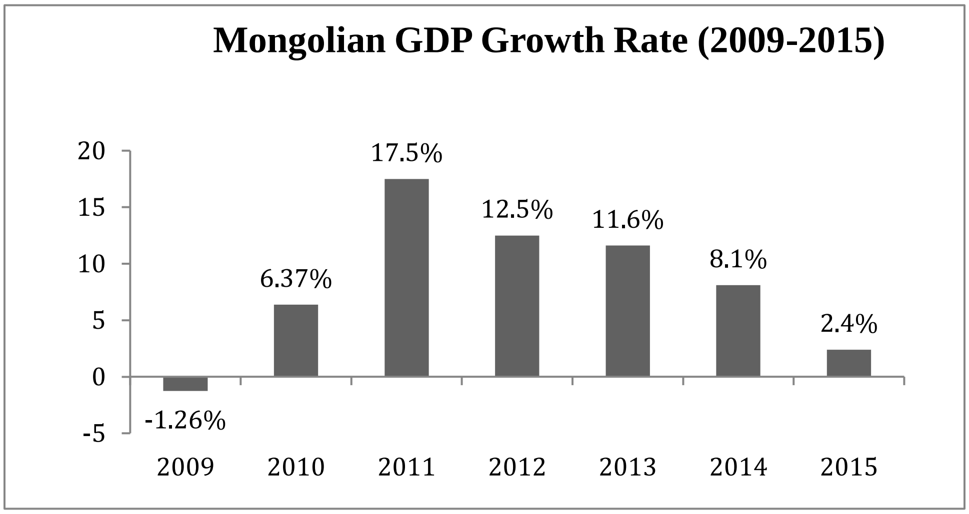
Following the fall of the Soviet Union, Mongolia needed substantial aid to repair the country's economic, social and political structure. As a Soviet satellite state, the Mongolian economy relied on the Soviet subsidies that totaled one-third of Mongolia's Gross Domestic Product (GDP) (Wagner, 2012). After the evaporation of Soviet financial support, Mongolia fell into a deep recession with high unemployment rate, and widespread poverty. The newly formed democratic government turned to international financial institutions like the World Bank (WB), Asian Development Bank and the International Monetary Fund (IMF) for financial assistance. International aid came with a conditional structural adjustment program that imposed implementation of neoliberal policies like rapid privatization, a free market economy and the deregulation by the

Mongolian government. The international lending institutions believed that the only path for development was through an implementation of these neoliberal economic policies.

Until recently, the Mongolian economy was largely dependent on traditional industries such as agriculture and herding. However, in the early 2000s, the Mongolian mining industry experienced a dramatic boom after it discovered vast untapped reserves of natural resources including gold, copper, high-quality coking coal, uranium, tin, and iron. In 2009, the government saw the opportunity to develop its mining industry and invited foreign governments to invest in the untapped natural resources. The benefits of foreign direct investment showed in the double-digit growth of the economy in 2011 and 2012 ("Mongolia"). The mining industry quickly became the primary contributor to the GDP. According to United Nations Development Programme, Mongolian mining sector is responsible for estimated 40% of government revenues as well as 80% of exports from the country ("About Mongolia"). Although the profit from the mining industry has encouraged economic growth, as I explored in my literature review, excessive dependence on a single sector can be a problem to the economy. The overreliance on one sector can expose the Mongolian economy to the unpredictable nature of commodity price fluctuations.

As a landlocked country with limited transportation infrastructure, Mongolia faces many challenges in developing efficient export industries. Located between the two of the biggest markets, Russia and China, Mongolia's export market is mainly limited to these two countries. The implications of limited trading partners can have negative consequence as economic and political change in either country can have a significant effect on the Mongolian economy. For example, Figure 2 indicates GDP of Mongolia from 2013 to 2015. The economic slowdown in 2014 to 2015 is largely due to the decrease in Chinese demand for Mongolian minerals.

Figure 2



Source: Trading Economics

The relationship between China and Mongolia is complex. Over 200 years of subjugation under Chinese rule has lead to mistrust of Chinese presence in the country. However, the Mongolian economy is heavily dependent on China's import of Mongolian natural resources. The rapid industrialization of China created a unique opportunity for Mongolia's top export minerals such as copper ore and coal to China. Since 2004, Mongolia has consistently exported over 95% of all production of both minerals to China. According to 2014 data, China has purchased 99.5% of Mongolian copper ore and 99.8% of its coal production. Collectively, Mongolia exported over $3 billion (over half of its exports) worth of minerals to China in 2014. Consequently, the Mongolian economy is heavily dependent on the Chinese demand for copper and coal ("Mongolian Export").

The danger of depending on one market for economic growth was realized in the years 2014 and 2015 when Chinese demand for Mongolian natural resources decreased.

The decline in demand caused the Mongolian GDP growth rate to plummet from 17% in 2011 to 2.3% in 2015 (Bernard, 2016). The GDP growth rate continued to slow down, as economists forecast the likelihood of a continual decrease due to diminishing Chinese demand. On September 3, 2016, President Xi Jinping signed the Paris climate agreement deal that promises to decrease emissions production in China by 2030. The commitment did not include specific targets for China, however, the President pledged to curb their emissions production by restricting the burning of fossil fuels. The Chinese commitment is alarming to the Mongolian economy as China is their number one natural resource export partner. Mongolian coal production depends on the Chinese demand for coal. If China ceases to import Mongolian coal, the Mongolian economy will shrink significantly. In order to avoid a further economic slump, the Mongolian government needs to reform its export industries where it can avoid overreliance on one industry by developing other export sectors such as agriculture and herding.

The Mongolian political environment has not been without a fair share of controversy. Party fraction, corruption, nepotism and political instability have plagued the country. Mongolian politics often experience turbulent parliamentary politics in the State Ih Khural (the state assembly). The dominant parties are the Mongolian People's Party (MPP) (current ruling party), the Democratic Party (DP), and the Mongolian People's Revolutionary Party (MPRP). The Mongolian electoral process is highly contentious, and rules change frequently. At the beginning of the 2000s, the Mongolian political environment started disintegrating due to internal disagreements. The Grand Coalition formed in 2004 collapsed due to contention over party leadership. The collapse of the coalition left the parliament without a clear majority, leaving it unable to function.

In response, 25 members of the DP switched party to join the MPRP, declaring it the ruling party. Some citizens, as well as other parliamentary members, denounced the controversial move. However, it did help overcome a government impasse. The compromise did not last long, as the parliament again went through major political upheaval in 2008.

The political dysfunction continued in 2008 as a controversial parliamentary election took place. Scandals involving voter fraud questioned the election result that declared MPRP as the ruling party. On July 1, 2008, peaceful protestors gathered to oppose the election results in the streets of Sukhbaatar square. The peaceful rally quickly turned into a violent riot as a group of people threw rocks and set fires to the MPRP headquarters and the Cultural Museum Building beside it. In the end, five people died, and hundreds were injured. The government called its first-ever state of emergency that lasted four days ("Mongolia calls state of emergency," 2008).

Another political controversy followed the next election in 2012, over the arrest of the former president Enkhbayar Nambar (MPRP) on allegations of corruption and nepotism. The international community widely condemned the April 13th, 2012, arrest procedure and the accusation of the former president for violating fundamental human rights ("Amnesty International Public Statement"). Amnesty International criticized the lack of due process and the treatment of Mr. Nambar following his arrest. The supporters of Mr. Nambar claimed that the motivation to charge him was to exclude him from the upcoming parliamentary election (Levin, 2012). The Ulaanbaatar district court convicted Mr. Nambar of corruption, embezzlement, and misappropriation of government properties. The initial court sentence was seven years in prison, and a monetary fine but

Mr. Nambar spent less than a month in prison and was transferred to a private hospital to finish off his sentence. However, on August 1, 2013, President Elbegdorj Tsakhia pardoned Mr.Nambar and released him from his convictions (Erkhes, 2013).

Throughout the political upheaval, the Mongolian civil society played a significant role in voicing discontent over government incompetence in dealing with a stagnant economy, unemployment, inequality and most of all, corruption. According to 2015 Transparency International corruption index, Mongolia scored 39 out of 100, indicating rampant corruption in the public and private sector (Transparency International). A survey conducted by the Asia Foundation in June 2015 found that 59% of the respondents believed that corruption has increased from previous years and think it will continue to grow in the coming years (Nara, 2015). In 2006, the Independent Authority Against Corruption (IAAC) was established to fight against corruption and bribery. Under the attorney general, the IAAC has the power to investigate public officials and private businesses and refer appropriate cases to the General Prosecutor's office ("IAAC").

Although the IAAC has made significant strides in combatting the ubiquitous corruption, international communities like Anti-Corruption Network for Eastern Europe and Central Asia (ACN) believe stronger measures can be taken to prevent and fight corruption. Critics believe that the current criminal law of Mongolia does not meet the standard of the international criminalization of corrupt practices and appropriate enforcement is lacking in serious corruption cases. Additionally, political party financing is often unregulated. Nepotism and bribery also plague the Judiciary organ ("Anti-Corruption Reforms in Mongolia," 2015).

According to Transparency International's most recent data, in 2013, 65% of Mongolians that were surveyed felt political parties were corrupt. Similarly, 73% of the interviewees felt that judiciary was "extremely" corrupt (Transparency International). Civil society organizations agree that to achieve true economic and social equality, a culture of transparency and accountability must be created at all levels of government, and in the judicial and executive sectors.

In the last two decades, Mongolian society has experienced major social transformation. As a Soviet satellite, Mongolian people's social standing was relatively equal. Although the country was experiencing a significant shortage of food and relied on the Soviet Union for most of the county's nutritional needs, Mongolians had universal health care and education. Additionally, the centrally planned economy provided jobs to the people and kept the unemployment rate low. Following democratization in 1990, citizens had high hope of an increase in the living standards. However, achieving development through a free market economy proved to be a challenge. According to July 2016 data, the Mongolian unemployment rate is at 10.4%, indicating a higher rate than the previous three years.

Additionally, the 2016 survey from Mongolian NGO Sant Maral Foundation reported that citizens' primary concern was unemployment (36% of responders) and number two was standards of living/poverty/income with 15.1% (Sant Maral Foundation, 2015). Regional disparity is also apparent. Urban dwellers have better access to social programs than the pastoral herders who live far from cities and have limited access to resources. Also, 55.9% of the respondents answered that the government fails to solve the most urgent problem "always" and 28.1% responded the government failed to solve them "often." A staggering 84% of the respondents felt that the government is incompetent in addressing the country's most pressing social issues.

In Mongolia, access to quality health and education is unequal. The Mongolian literacy rate is 98% for both men and women. Compulsory primary education has been beneficial for literacy rate of the country. However, secondary education has an unequal attendance. Despite high literacy rate, there are disparities in access to quality education. According to Mongolia's 2016 Human Development report, access to education among disabled youth is significantly lower. The study reveal that estimated only 66.2% of youth with disabilities are enrolled in compulsory education (Mongolia Human Development Report, 2016). Urban residents are more likely to continue education and attend secondary education than the rural residents. The increasingly high cost of living and housing deters rural residents from attending school (Mongolia Human Development Report, 2016). Following democratization, private education became highly sought out in Mongolia. Parents are encouraged to send their children to private school with better education curricula. However, urban residents are more likely to be able to afford better education than the poor rural residents.

Similarly, in the health sector, most of the population depends on national health care. As a Soviet satellite, Mongolia benefited from modern medicine for disease control and prevention. The decentralization of the government has lead to private and public partnership health care reform. The World Health Organization's 2013 analysis indicated that instability in the government set back the improvement of the health care system. Changes in ruling parties often make the process of meaningful health care reform slow and ineffective. Additionally, the quality of health care can vary in urban to rural areas.

Urban residents have better options for health care, as hospitals are easily accessible in the capital city. Rural residents have either one hospital in the nearest town, or a limited number of doctors that visit from town to town. Also, a person's income level can determine whether they can afford to go to private hospitals for better and faster care.

According to most recent data, in 2014, the Mongolian poverty rate was 21.6% (UNDPMN). However, a sharp increase in the poverty rate is expected as GDP growth rate decreased to a single digit in 2015 and continued to drop in early 2016. Additionally, in the most recent data on income inequality, by 2012, the richest 20% of the population held 41.66% of the national income, while the bottom 20% held 7.6% of the national income. The inequality gap continues to widen as the economy continues to slow down.

The capital city, Ulaanbaatar, is home to an estimated 1.38 million people out of the total Mongolian population of 3.02 million people. A significant number of individuals have moved from the rural areas to live in the capital city in search of jobs and better life opportunity. As of 2015, 72.5 % of the population is living in the capital city (the World Bank). Traditional herders are unable to sustain rural life as extreme weather conditions in the winter and desertification threatens the sustainability of their traditional lifestyle. During harsh winters, thousands to a million livestock can perish due to extreme cold or starvation. The herders are also facing desertification as lands become increasingly arid due to climate change and human-made factors (BBC, 2016).

Unfortunately, government-housing organizations are not able to provide adequate shelter to the flood of the newcomers, forcing them to create ger (yurt) slums surrounding the metropolis. Within few miles of the developing capital lie the slum dwellers that live without proper access to health, sanitation, education and employment opportunity. The conditions in the ger slums can get extremely dire during the winters where the temperature could fall as low as -40 Celsius. Due to the extreme cold, residents are forced to burn coal for warmth and cooking which significantly intensifies the existing air pollution. Pollution levels can go up to a hazardous level where it is 6-7 times higher than the World Health Organization (WHO) standards (WB, 2012). Consequently, the population is vulnerable to many respiratory illnesses, lung cancer and in some extreme cases, spontaneous abortion.

Mongolia is at a crossroads. Economically, the country is suffering from a recession due to a slowing of economic growth. Socially, the persistence of high unemployment rate continues to concern the citizens. Politically, the instability in the parliament decreases the functionality of the government. The notable exception is that civil society continues to practice its democratic rights and demonstrate its dissatisfaction through electoral participation and public demonstrations. Mongolian voter turnout in a parliamentary and presidential election is estimated at 70%. Additionally, many NGOs continue to fight for social wellbeing. In a historic 2016 parliamentary election, 85% of the vote went to the opposition party MPP that took 65 of the 76 seats in the parliament. The citizens openly voiced their discontent with the ruling DP on how it mismanaged economic policies and their lack of competence in addressing social problems. The new ruling party has the unique opportunity to establish stability in the government and to promote foreign investment that encourages multiple export sectors without over-relying on mining industries. Additionally, fiscal discipline is required to curb national spending and allocate resources for societal wellbeing. Much faith is placed on the new government to address the most urgent problems of society.

The background information provided a broad overview of the Mongolian society. Since 1990, Mongolia has achieved great success in poverty reduction and democratic representation of the people. However, there are still problems concerning even development. The following section contains the case study to answer the research questions. The case study will provide an answer to whether extraction-led development can lead to development.

CHAPTER IV. Methodology

This thesis engages in a comparative case study to investigate the promise and pitfalls of FDI in creating development, using Mongolia as a case study. The research questions encompasses series of interrelated inquiries including 1) whether *human* development can be achieved through extraction industries 2) whether the source of FDI has a strong impact on development outcomes, and 3) whether FDI influences state-led development efforts and decision making to the extent that it threatens the development of Mongolian sovereignty

The principle research methodologies utilize qualitative and quantitative analysis of primary and secondary sources. Primary sources include contract agreements, Mongolian mining laws and legislation, government and independent investigator reports, official public complaints, data collected from the World Bank, the government of Mongolia, and independent arbiter decisions. Secondary sources include news reports and academic journals addressing Mongolian foreign investment, extraction industry, social and environmental concerns, corruption, political instability and economic development.

In order to assess whether foreign investment in the extraction industries has contributed to the development of Mongolia and to evaluate whether differences in foreign investor affect the impact of the investment, my comparative case study analyzes two prominent mines. In order to measure the impacts of the investments, the two mines are analyzed by their contribution to Mongolia's (1) political environment, (2) economic growth, (3) societal progress and (4) environmental sustainability. Also, to address the second research question, the foreign investors are evaluated based on their business conduct. The foreign investors will be examined by their regulatory compliance and corporate social responsibility.

The first section will identify the two foreign invested mining operations in my case study. The second section will analyze the impact of both mines on Mongolian development, and their relationship to the Mongolian government's enforcement efforts. The final section will include concluding analysis and address the research questions.

The two mines were selected based on their significant contribution to the Mongolian GDP. As discussed in the background information, Mongolia's export sector relies heavily on the international demand for its two major natural resources: copper and coal. The Oyu Tolgoi (hereafter OT) is Mongolia's biggest mine extracting copper, gold, and ore. However, copper is the principal natural resource for extraction. So far, mining giant Rio Tinto and Ivanhoe Mines together invested $6.6 billion to develop OT's open pit (Els, 2014). In May 2016, the Mongolian government and the investors signed off on a $5.3 billion investment to further development of OT's underground pit. With the development of the underground pit, revenues are expected to significantly increase revenues for both parties ("Rio Tinto approves the development of Oyu Tolgoi underground mine," 2016).

The Khushuut mine is the second largest coal deposit in Mongolia.[1] The Khusuut mine is under 100% ownership of the Chinese mineral and energy exploration company, Mongolia Energy Corporation (MEC). The Khushuut's production supplies Xinjiang's rapid industrialization that demands quality-coking coal for steel production (Daily

[1] The largest coalmine, Tavan Tolgoi is eliminated due to its beginning exploration stage as of 2016. There are not enough data available to evaluate the mine's operation.

China, 2008). The Khushuut mine is expected to produce 3 to 8 million tons of coking coal each year for the Xinjiang coal market.

Additionally, the two mines extract two different natural resources. The OT deposit's primary mineral is copper. Copper is an essential mineral for infrastructure development. Although the copper market is historically unstable, prices can soar with the increase in demand. The recent rapid Chinese industrialization increased the demand of copper, making copper production profitable. Therefore, Mongolia has been supplying more than 99% of its copper production to China for the last ten years (The Observatory of Economic Complexity, n.d.).

The Khushuut's deposit is rich with coal. Independent researchers revealed that Khushuut contains premium quality coking coal (Mining Technology, n.d.). Historically, the coal market is stable, and prices are low. Most developing countries rely on the affordable nature of coal for power generation and industrialization. Therefore, the demand for coal remains constant (World Coal Association, n.d.). Transportation costs also affect market price. Khushuut is located only 310km from the Yarany Border of Xinjiang, China where coal demand is high. Over the past five years, over 99% of Mongolia's coal was exported to China (The Observatory of Economic Complexity, n.d.). The map in Figure 3 illustrates locations of the two mines.

In order to address the second research question, the mines were selected based on their difference in foreign investors. The comparative analysis is to evaluate how the difference in national origin of mine of ownership impact Mongolia's development. As discussed in the literature review, Chinese foreign investments have a particular pattern when it comes to natural resources. Therefore, I chose to conduct a comparative analysis of Chinese-owned Khushuut coalmine, and Anglo-Australian owned OT copper mine. The comparative analysis will reveal whether the pattern of Chinese foreign investment holds in Mongolia and reveal if there are significant differences in Chinese businesses' conduct towards the government when compared to Anglo-Australian investors.

Figure 3

Source: NPR (Langfitt)

The Khushuut Coal Mine is owned and operated by a Chinese mining and energy investment holding company, Mongolian Energy Corporation (MEC). The mine is located in Khovd province in the Western Mongolia. The Khushuut mine is approximately 190 miles from the Chinese Yarant Border Station. The MEC began its acquisition of 330,000 hectares of the mining area in 2007 with the intent to explore and mine coal from the open pit mine (Daily China, 2008). In addition to the Khushuut mine, MEC is also owner and operator of mines located in Olon bulag and Bayan Ulgii provinces of Western Mongolia. The Khushuut mine is considered the second largest coal deposit in Mongolia, following Tavan Tolgoi coking coal mine.

Prior to its natural resource investments, MEC was a property investment and a private jet service corporation called the New World CyberBase Limited (NWCB)(Mongolia Energy Corporation, 2007). In 2007, the company changed course to invest in mining coal and ferrous and non-ferrous metals resource in Western Mongolia and Xinjiang, China. Figure 4 illustrates the structure of the MEC. The MEC began its exploration of the Khushuut mine in 2006 and commenced extraction in 2008. Although the MEC is a multiple license holder of mines in Western Mongolia, the contracts are not publically available. The most recent contract available to the public is the renegotiation of terms in 2014. The contract is between the local government of the Khovd province and the MEC subsidiary MoEnCo LLC. The duration of the agreement is for three years, from February 2014 to December 2016 (Mongolia Energy Corporation, 2014).

At the inception of the Khushuut mine development, the MEC contracted mining consultant John T.Boyd Company to determine the future output of the mine. The investigation determined that the Khushuut mine has a coal deposit of 460 million tons and 141 million tons were considered premium-coking coal. Additionally, the Khushuut mine's estimated lifespan is 19 years (Boyd, 2009). Currently, the MEC has eight licensing rights to mine Khushuut with a 100% share of the Khushuut mine. The MEC is required to pay local and government taxes as well as license royalties. By 2008, the Khushuut mine became operational with the extraction goal of 3 million ton of premium coal per year. In 2010, the MEC created a long-term coal supply contract with Baosteel Bayi. Under the contract, the MEC agreed to provide at least 9.6 million to 10 million tons from the year 2010 to 2020 (Mongolian Energy Corporation, 2010).

The OT is one of the world's largest copper, gold and ore mines located in Omnogovi province within South Gobi, Mongolia. The OT is estimated to be the biggest copper deposit in the world. The development of the OT has been in exploration since the 1990s, but the growth possibilities were not apparent until 2001 when Canadian Ivanhoe Mines became involved. In 2009, Ivanhoe Mines and Rio Tinto merged to form Turquoise Hill Resources and formed a cooperation agreement with the Mongolian government. Turquoise Hill Resources owns 66%, and the Mongolian government owns the remaining 34% of the mine. Within Turquoise Hill Resources, Rio Tinto controls 51% of the share making it the manager of the OT (Jamasmie, 2012). Figure 5 illustrates the structure of the OT ownership.

Figure 4

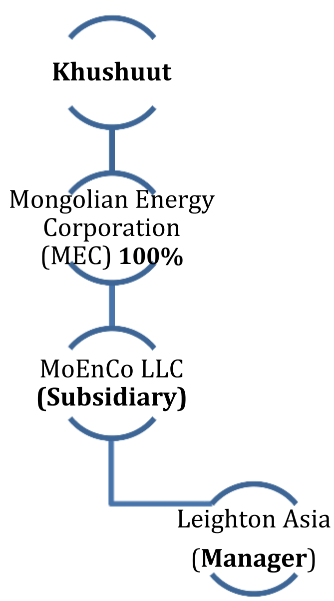
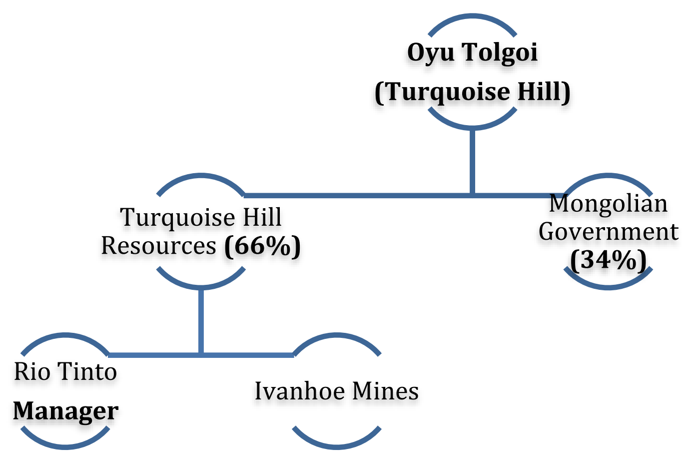


Figure 5



On October 9th, 2009, all parties signed the cooperation contract. It is valid for 30 years with the possibility of additional 20-year renewal. However, Turquoise Hill Resources must abide by all provisions of the agreement during the initial 30 years for contract renewal (Oyu Tolgoi LLC, 2009). Rio Tinto estimated that the OT's reserves could produce 1.2 billion pounds of copper and 650,000 ounces of gold yearly over a lifespan of 50 years (Els, 2013). The OT became operational by March 2010 and started its extraction of copper, ore, and gold.

Limitations and Further Research Questions

This research’s goal is to find out the impact of the mining boom in Mongolia’s development. The case study selected two prominent mines operating in Mongolia to conclude results. However, there are limitations. The methodology is limited to assessing primary and secondary sources available through websites and academic journals. The case study lacks on the ground research in Mongolia.

The case study analyzed two mines that have been operational for six years. Further research is required to find out long-term effect of the extraction industry on the Mongolian development. Given time, more data will be available to assess the broader impact of the mining boom.

CHAPTER IV: Case Study

Regulatory Compliance of Khushuut and Oyu Tolgoi

The Mongolian President Elbegdorj Tsakhia has been a proponent of foreign direct investment to grow Mongolia's economy. In the early 2000s, Mongolia's mining boom attracted numerous foreign investors to take part in the natural wealth. The foreign attraction has encouraged the government to pass various mineral laws both to regulate and to promote foreign investment.

In 2007, the Parliament implemented a significant mineral law to take control of the natural resources. Under the "Strategic Importance" law, a mineral deposit that may have potential impact on national security, economic and social development of the country at regional or national levels, or has the capability of producing greater than 5% of the GDP in a single year, it is identified as a mine of "Strategic Importance." If a mineral deposit qualifies for any of the characteristics, the state government must have a certain amount of shares in the mineral deposit (Mongolian Mining Law, 2006). Under the said mineral law, Article 5.4 indicates that the state may hold up to 50% of the shares if state funds are applied for the exploration of mineral reserves. Additionally, Article 5.5 states that the state may own up to 34% of the shares of the investment if the mine is determined to be of "strategic importance" and the exploration of mineral reserves were not funded by the state budget. The amount of investment determines the percentage share (Mongolian Mineral Law, 2006). In the event of a "Strategic Importance" ruling, the license holder and the government will negotiate government participation in production and profit sharing.

The Khushuut mine was not classified as a mineral deposit of "Strategic Importance" at the beginning of the operation. However, on December 6, 2012, the Mining Ministry of Mongolia requested information on the Khushuut mine to assess its qualification on strategic importance. In June 2013, the Government of Mongolia (GOM) announced its intent to add the Khushuut coal mine to the list of mineral deposits of "Strategic Importance" (Mongolian Energy Corporation "Annual Report," 2014. pg 91). The parliament declared that the Khushuut mine contributes significant economic and social development to the country. The Khushuut mine was estimated to bring 2,514.4 billion tukrig to local and national development through royalties, taxes, and fees. Additionally, the Khushuut mine's transport infrastructure, power transmission line, power plants, industrial buildings, communication system and industrial water supply network all have a social impact on the development of Khovd province. Therefore, the Parliament believed that the Khushuut mine should be included under the "Strategic Importance" category. In the same month, the Khushuut mine stopped its operation to deliberate with the government. During the halt in operation, over half of the 500 staff became temporarily out of work. On March 31, 2014, the GOM decided to exclude the Khushuut mine from the "strategic importance" list because the government stated that the economic benefit from resuming the mine operation is valuable, and the government wished the mine to resume operation to generate revenue.

In July 2009, the GOM adopted the "Mining Prohibition Law" to address environmental protection concerns. The law prohibits mineral exploration and extraction in areas of headwaters of rivers and lakes and forested areas. Additionally, any previously granted licensed that overlap the prohibited areas will be terminated within five months of the implementation of the law. In 2015, the government passed an amendment to the law and added a clause for the license holder to continue to operate in said prohibited areas if the license holder takes appropriate measure to restore the environment. The license holder must submit a request to continue its operation in prohibited areas to the Mongolian Ministry of Environment, Green Development and Tourism within three months from the effective date. The licenses can be revoked if said obligations are not met (Lovells, 2015).

In 2014, the government identified four mining concessions in the Khushuut mine that overlapped the prohibited areas: license number 2913A, 4322A, 11888A and 15289A. The Khushuut mine continued to operate in the mining areas due to an unclear boundary definition of the prohibited areas. The MEC stated that they should continue to mine in the specified areas until licenses are revoked, and in the event of revocation of license, the MEC determined that GOM should pay compensation to the MEC (Mongolia Energy Corporation "Annual Report", 2014. Pg 91). As of November 2016, three of the four mines identified as overlapping prohibited areas continue to be operational.

The OT agreement was signed in October 2009 and entered into force in March 2010. On September 2011, 20 members of the Mongolian parliament petitioned the government to increase the government share in Turquoise Hill from 34% to 50%. The petition came ahead of Mongolia's parliamentary election for June 2012 (Stanway, 2011). According to the cooperation agreement of 2009, contract terms can be renegotiated between the parties only when the initial 30-year contract term expires. Turquoise Hill Resources requested that the government honor the agreement.

In June 2011, the GOM passed Resolution 175, which stated certain land areas are for “state special needs.” The indicated areas are to be used for infrastructure facilities. As of June 2011, the GOM passed Resolution 175, which stated certain land areas are for “state special needs.” The indicated areas are to be used for infrastructure facilities. As of 2011, some areas identified, as “state special needs” are under exploration and mining license of the OT. Turquoise Hill Resources indicated that infrastructure developed in some areas might adversely affect the mining and exploration process. The GOM claimed that if the infrastructure adversely affects the progress of OT; the GOM will be responsible for compensation.

The intent to renegotiate the share dividends was raised again in October 2012. The deliberation of the shareholders continued into 2013 (Kosich, 2012). In addition to the disagreement, Turquoise Hill Resources voiced concerns about the uncertainty regarding the approval process and timing required to resolve the complex outstanding issues. The unresolved issues create uncertainty about the mine’s future and slow down the development process.

In 2013, the Government of Mongolia proposed a budget that included additional royalty revenue from the OT. However, the 2009 OT agreement clearly indicates that the royalty rate is capped at 5% throughout the duration of the contract. Also, new laws regarding royalties made after the agreement will not apply to the OT. Turquoise Hill Resources claimed that any change in royalty fees requires approval from all parties involved in the contract (Entrée Gold Inc., 2013, pg. 6).

In August 2013, the production of OT was delayed to resolve outstanding issues concerning development and operation of OT and its project financing. The GOM stated that the parliament must approve the project funding. The OT temporarily halted production until the financial matters were resolved. On May 18, 2015, the Turquoise Hill Resources and GOM reinforced Investment Agreement and the Amended and Restated Shareholders Agreement (ARSHA) (("Amended and Restated Shareholders' Agreement," 2011). The agreement resolved outstanding issues from prior years and agreed on project funding.

In the comparative analysis of the two mines, the OT investors, Rio Tinto and Ivanhoe are clearly well-established investors with a lot of experience investing in foreign mines. The Khushuut mine owner, the MEC is a new company that started in the mineral exploration business in 2007. The Turquoise Hill Resources has a clear and transparent method for publishing the contract agreement, independent investor’s report, worker safety procedures and various documents related to the operation of the mine. However, there is a clear lack of accessible documents from the MEC. The company puts out yearly financial reports but the information provided does not adequately include the citizen’s complaints and the effort it took to address the concerns.

The analysis of both mines’ regulatory compliance shows that the Mongolian government’s instability is a big hindrance factor to the development effort of both mines. Since 2009, the Mongolian government passed various laws addressing economic, social and environmental concerns. On the one hand, due to the demands from civil society, the government passed legislation to ensure economic benefit is ensured at the national as well as the provincial level. On the other hand, the laws passed became increasingly conservative, making it hard for the foreign investors to purchase licensing rights and provided stricter guidelines for shared dividends.

The increasingly restrictive laws have had a discouraging effect on foreign investment. Many foreign investors criticized that the uncertainty of future regulatory system has decreased investor confidence in the country. The investment share disagreement between the Mongolian government and Turquoise Hill Resources caused a temporary halt in the production, which cost revenue for both parties. Similarly, the Mongolian government and the MEC disagreed over enforcing "Strategic Importance" law to the Khushuut mine. However, these actions were the Mongolian government's effort to manage the foreign investors and to protect the national interest of Mongolia.

The regulatory compliance analysis yields larger implications for Mongolia's political environment. First, the failure to include the Khushuut mine to the "Strategic Importance" category indicates the MEC's blatant disregard for the Mongolian law. The MEC was able to exhort economic dominance over the Mongolian law to ensure 100% ownership of the mine. But most importantly, the inability of the Mongolian government to enforce its law indicates the larger issue of "state erosion." The government of Mongolia's inability to enforce its own national law indicates a weak institution.

Second, the majority of the conservative laws and its stronger effort of enforcement are due to citizen's demand. As demonstrated in the June 2016 election, civil society has the power to influence parliamentary elections. The Mongolian government's reaction to the citizens' demands resulted in drafting stronger measures to enforce environmental protection, local level economic benefits and stronger regulations in foreign investment practices. Although there are instances of failure to enforce some of the regulations, the government is receptive to the demands of the people. Therefore, the relationship between the government and the people has the political impact of "state building."

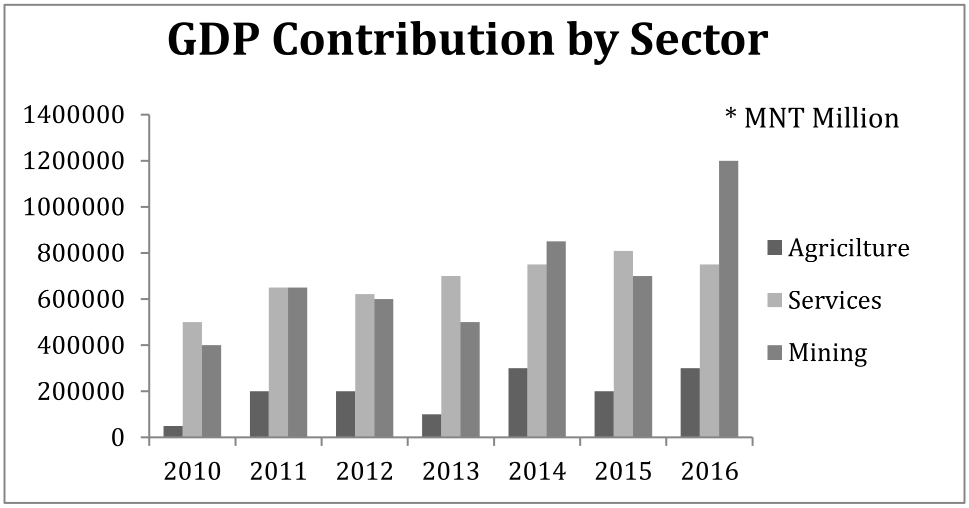
Oyu Tolgoi and Khushuut's Economic Impact on the Mongolian Economy

The most important part of foreign investment is its contribution to the host country's economic growth. Under the Mineral Law of Mongolia, 20% of extraction industry royalties go to the host province government and 10% is given to the local district government (Mineral Law of Mongolia, 2006). The fees provide financial assistance to developing regional social and economic infrastructure. Mongolian mining legislation requires foreign investors to sign "local-level agreements" where local civil society and community groups voice their interest in hosting mining explorations. The goal of the regulation is to contribute to the local economy of the host province directly. The MEC signed such an agreement with the Khovd province in 2014. Under the contract, the MEC is required to contribute to local economic development by contracting 50% of the goods and services related to the mine from the local companies. Additionally, the MEC is required to invest US$0.6 (60 cents) per each ton of coal if exported coal is over 100,000 tons to the Khovd Khushuut Development Fund ("Cooperation Agreement Between Khovd Aimag and MOENCO LLC," 2014). Also, the government generates revenue through taxes and royalties. A similar contract was signed with Turquoise Hill Resources over the OT production. The GOM gains economic benefit through taxes, license royalties, share dividends, and local business contracts ("Oyu Tolgoi Investment Agreement - Turquoise Hill Resources," 2009).

The economic impact of foreign investors in Mongolia is apparent in the years 2010 and 2011 (Figure 2) ("Mongolian GDP"). The GDP rate grew to extraordinary double digits during these years. In 2010 both of the mines made significant deals with Chinese businesses to sell coal and copper respectively. The MEC created a long-term coal supply contract with Baosteel Bayi and promised to provide an estimated 10 million tons of coal by 2020 (Asia Miner, 2010). Similarly, Turquoise Hill Resources committed to two large Chinese smelters to export an undisclosed sum of ore. The mining industry became one of the top contributors to the GDP growth. In 2013, Mongolian National University and Australian economist Brian Fisher estimated that by 2020, revenue from OT would represent more than one-third of the Mongolian economy (Economist, 2012).

According to data from 2010 to 2016, mining, agriculture and the service sectors are the biggest contributors to Mongolia’s GDP. As shown in Figure 6, the mining and service sectors outperformed the agriculture industry (Trading Economics, n.d.). The slight decrease in the mining profit was caused by the separate disagreement between the OT and the Khushuut mine with the GOM. The growth in the mining industry significantly contributes to the service sector, as the service sector benefitted from the business opportunities stimulated by the mining boom. The variance between the revenue from mining and the service industry can be attributed to the high unemployment rate in 2016.

Figure 6



Source: Trading Economics

The Khushuut mine's profit margins are significantly lower than OT's profit margins (Rio Tinto, n.d.). The decline in the Chinese market demand for coal affected the MEC profit. Since coal prices are significantly lower than copper prices, the OT's revenue is much higher. Also, Turquoise Hill Resources conducts a more transparent operation than the MEC, and yet it yields a higher profit. The OT operation shows that transparency and profit can go hand in hand.

The production size of the Khushuut mine is smaller than OT. Turquoise Hill Resources invested estimated $6.4 billion in developing the OT. The full investment efforts of the Turquoise Hill Resources reaffirm the commitment of Turquoise Hill Resources to the OT.

According to Rio Tinto data, OT project development brought an estimated US$1.4 billion revenue to the Mongolian government through taxes and fees (Rio Tinto, n.d.). Since the production began in 2010 for both mines, the national poverty rate has declined steadily. According to the World Bank data, since 2010, the national poverty rate dropped from 38.8% to 21.6% by 2014 (Table 1)(World Bank, 2015). While the decline of national poverty is a sign of societal progress, there are disparities between the urban and rural residents. According to the Asia Foundation, rural residents have a greater poverty rate than urban residents (Theunissen, 2014). Rural residents have fewer employment opportunities, as the traditional herding lifestyle is no longer sustainable. Many rural residents lack access to quality education and skills training.

Table 1. Mongolian Poverty Rate

	2010	**2011**	**2012**	**2014**
National Average	38.8%	33.7%	27.4%	21.6%
Urban	33.2%	28.7%	23.3%	18.8%
Rural	49.0%	43.2%	35.4%	26.4%
Region				
Western	52.7%	40.5%	32.3%	26.0%
Khangai/Highlands	51.9%	49.1%	38.5%	25.3%
Central	29.9%	28.1%	28.2%	22.2%
Eastern	43.3%	40.0%	33.4%	31.4%
Ulaanbaatar	31.2%	25.8%	19.9%	16.4%

Source: World Bank

The increase in foreign investment began in the mid-2000s. The mining boom attracted many foreign investors and with that, the promise of job creation. Both of the mines' agreements indicate specific provisions that require employment of a certain percentage of Mongolian nationals. The OT is obliged to have at least 90% of employees be Mongolian, and the Khushuut mine requires at least 70% Mongolian citizens comprise the mine workforce. These provisions secure employment opportunities, but do not seem to have a positive effect on the employment rate. In August 2013, the Turquoise Hill Resources fired 1700 employees due to the disagreement with the GOM over the division of the mining revenue (Santhebennur, 2013). Its production has contracted, and so has its workforce.

2011 and 2012 were the years when the Mongolian GDP experienced a double-digit growth rate. The graph in Figure 7 indicates the increase in the unemployment rate in 2012, rather than decrease in the unemployment rate. According to foreign investment proponents, increase in economic growth will improve business opportunities and create more jobs. On the contrary, the unemployment data from 2007 to 2016 indicates that the unemployment rate is the highest it has been in the last ten years (Trading Economics, n.d.).

Figure 7

Source: Trading Economics

My analysis of the economic impact suggests that the Mongolian economy benefited greatly from the mining boom for approximately three years. The decrease in the national poverty rate due to economic growth is a notable success towards social progress. However, inclusive growth has been difficult to achieve. The results show that rural residents are reported to live under much higher poverty rate than the urban dwellers (World Bank, 2015). According to the 2014 data, one in four people live in poverty in urban areas versus one in three people in rural areas.

The GDP growth can be attributed to the attraction of foreign investors in the extraction industry during the mining boom. The large profit margins from natural resources led the Mongolian government to prioritize extraction-led development.

The case study suggests that the Chinese demand for coal and Mongolian economic growth is positively correlated. The increase in the Chinese market demand for copper and coal increases the growth of the Mongolian economy. Accordingly, the decrease in Chinese demand can slow down the Mongolian economic growth. The GDP data from 2014 to 2016 proves the deduction. As indicated in the economic performance, the Chinese demand for such natural resources steadily declined in 2014 and plummeted in 2015 due to Chinese economic growth contraction, and as a consequence, the Mongolian GDP sharply decreased.

The data from 2015 and 2016 demonstrate that single industry reliance is extremely volatile. The revenue from extraction industry can vary with any change in either the commodity price or the international political environment. My analysis indicates that the current Chinese effort to utilize alternative energy sources to coal would have a detrimental effect on Mongolia's export sector.

Furthermore, a focus on extraction-led development neglects the development of other exportable sectors of the economy. The data on sectors that contribute to the GDP indicates that the agriculture failed to develop in a meaningful way in the last five years.

Social Impact: Civil Society in Action

Foreign investment can bring opportunities for social development. Especially in a developing country, the infusion of infrastructure, technology, and skills training resources, bring a significant opportunity for progress. Both mines contributed to the infrastructural development of their host provinces. In 2011, Turquoise Hill Resources began its construction of electrical lines for OT development and the local community. The power source is connected to China's power source (Mining.com, 2011). The construction of electric power replaced the community's traditional means of diesel-generated electricity. The introduction of a new source of energy is far more reliable and delivered at a lower cost than the previous source. Additionally, it provides a more efficient form of energy that leads to emissions reduction.

In 2010, the Turquoise Hill Resources constructed 97km of paved road from the OT mine to the Mongolia-China border. The local community can utilize the road, but under the agreement, the Turquoise Hill Resources can impose toll fees at any time. In 2011, a domestic airport was built as transportation infrastructure. Additionally, as a worker safety measure, the OT provides housing for workers who qualify for assistance. In November 2016, a hospital financed by Turquoise Hill Resources opened in order to tend to the local and worker's health needs (Oyu Tolgoi, 2016).

Under the 2009 Agreement between the GOM and Turquoise Hill Resources, 90% of the mine staff must be Mongolian nationals. Hence, the contract secured employment opportunities for the residents. As of May 2016, an estimated 95% of 3000 employees were Mongolian citizens (Rio Tinto, 2016). However, in the same year, Mongolian national unemployment rate has been at its highest in the last decade.

During the development and expansion of the OT, the herding community of Gobi raised important issues concerned with the OT's social impact. Their complaints included displacement of local herders from their land, disruption of seasonal migration routes, and limiting access to grazing land and other natural resources required to sustain a traditional livelihood. In October 2012, a community of herders delivered a complaint to World Bank's International Finance Corporation (IFC) and Multilateral Insurance Guarantee Agency (Mines and Communities, 2012). The complaint stated that adequate compensation should be provided to the displaced herders whose livelihood is endangered by the Turquoise Hill project. However, the herders claimed that the compensation provided was not appropriate to sustain their traditional way of life. The monetary compensation given so far is a temporary concession that does not solve long-term issues. The herders demand access to grazing areas for their livestock and access to water supply in order to survive. Land and water are especially scarce in the Gobi desert and with the OT projects, resources are dwindling for the locals.

The community relations between the Khushuut mine owners and the local community has been contested from the start. In 2010, a 14-year-old boy fell into a Khushuut mine's unsecured pit filled with water and drowned while playing around the mine. The family brought a complaint to the MEC, but the MEC accepted no fault. The MEC responded that the death was in an accident and is not the responsibility of the MEC. The MEC did not offer any compensation, and the case was not pursued further (Shuurhai, 2011). Henceforth, the MEC gained notoriety among the local people.

The community voiced its disapproval of the Chinese company's 100% ownership of one of the biggest mines in Mongolia. In 2012, the residents of Khovd province wrote a letter to the President of Mongolia and his administration; voicing community disapproval of the MEC's 100% ownership of the Khushuut mine (VIP76, 2012). The letter indicated that 100% foreign ownership violates the Mongolian mining law 4.1.12 of "strategic importance." Although the 2012 government report noted that the Khushuut deposit fits the characteristics of the "strategic importance" through its economic contribution, it continues to be under full Chinese ownership. Additionally, the community argued that the MEC failed to pay local taxes in the years 2011 and 2012.

Therefore, the community demanded that the government address the issue of "strategic importance" and enforce the MEC to pay the required local taxes. In the event the GOM does not adequately respond to the demands, the community threatened to close off the Khushuut road that is used to transport coal to Xinjiang border (VIP76, 2012).

In 2012 the GOM initiated a process to include the Khushuut mine on the "strategic importance" list. The Khushuut mine operation was temporarily put on hold during the deliberation between the MEC and GOM through 2012 and 2013 (Mongolia Energy Corporation, 2013). In the end, the GOM decided that the Khushuut mine would not be listed as of "strategic importance." The Mongolian people demand the GOM to take control of the Khushuut mine, but the government responded that the economic benefit from mine is valuable and any further disruption to the production will hurt the economy. National and local sentiments indicate resentment of the government for giving away country's national resource wealth. Particularly in the Khovd province, at the local town hall meetings, locals expressed their cynicism of the Khushuut mine's contribution to the Mongolian development (Shuurhai, 2012). The lack of control over country's national resources continues to the present day. In a 2016 national survey, 64.6% of the subjects answered that the Mongolian government should own more than 51% of foreign owner strategic mine deposits (Sant Maral Foundation, 2016). Furthermore, the respondents responded that the benefit from the mineral wealth should focus on improving economic development and focus on long-term social programs through investment in education, health, etc.

The 2014 renegotiated contract included provisions that required the MEC to contribute to local development. Under the 7.9 clause, the MEC is obligated to contribute to the development of Khovd by investing in education, healthcare, culture, sports, tourism and the traditional herder lifestyle ("Cooperation Agreement Between Khovd Aimag and MOENCO LLC," 2014). The local administration is responsible for enforcing the regulations. However, the many of the locals expressed their loss of their confidence in the benefits of Khushuut mine (Shuurhai, 2012).

As a public infrastructure development, the MEC built a paved road to transport coal to the Xinjiang Chinese-Mongolian border more efficiently. In May 2010, the MEC contracted 700 Chinese nationals began the construction of the "Khushuut Road." The road was finished by November 2011 and became accessible to the community. However, the locals were required to pay a toll fee to access the Khushuut road (Bolod, n.d.).

In analyzing the social impact of both mines, the Mongolian civil society's effort to fight on behalf of the public is tremendously notable. The community is outspoken against unjust investor conduct and often addresses the GOM to present the citizens' concerns. Civil society pressured the Mongolian government to enforce the "Strategic Importance" law to the Khushuut mine. Although it was unsuccessful, the Khovd province government was able to renegotiate the contract with the MEC to include provisions that required a contribution to the local development fund.

Environmental Impact: Preservation of Mongolian Traditional Livelihood

Extraction industries have a significant impact on the environment. Often, the effects are detrimental to a sustainable environment. In 2009, the GOM passed the Mining Prohibition law provided strict guidelines on protecting biodiversity and the water resources of Mongolia. However, in January 2015, the GOM voiced its intention to weaken the environmental protection law to encourage more mining opportunities (Els, 2013; Woolley&Gulguu, 2015). Mongolian citizens responded with hunger strikes and protests in the capital city. Thousands of citizens came to show support for the protest and over 22,000 people signed a petition to demand that the President of Mongolia protect Mongolia's wildlife, ecology, and cultural heritage (Shourd & Rhoades, 2015).

Unfortunately, the presence of both mines has threatened the traditional herders' way of life through environmental degradation and competition for natural resources. Water management is crucial due to the location of the mine. In the Gobi desert, there is low average precipitation. The OT project developed a bore field to help with water supply and dust suppression. Also, the OT diverted the Undai River to accommodate project facilities. On January 2nd, 2013 seven residents of Umnugobi contacted the government to submit a legal complaint of the Undai River diversion project (Compliance Advisor Ombudsman, 2013). The residents are local herders who stated that the river diversion has a significant adverse effect on the traditional nomadic livelihood and water supply in the arid land. The river diversion can dry up other water supplies that stem from the Undai River, and can severely impact the already limited water supply for livestock and forests. The complaint includes that Turquoise Hill Resources needs the community and the government's approval for the Undai River diversion. However, Turquoise Hill Resources claimed that the river is on the territory licensed to the Turquoise Hill and its flow is under a legal right to the license holder.

In 2015, the local government representatives, complainants, and Turquoise Hill Resources were able to agree that it is Turquoise Hill Resources' responsibility to re-construct a spring that dried up due to the river diversion and provide water tanks to herders affected by the diversion. Additionally, Turquoise Hill Resources promised to implement a water-monitoring system (A New Climate for Peace, n.d).

The contract between the Khushuut mine and the Khovd government included provisions to that required the MEC to respect the environmental protection laws of the land. The MEC implemented a project “Green Office Guideline” that closely monitors the company’s mining and metal waste, plastic, and water recycling process. However, the local community does not believe that the Khushuut mine adequately protects the broader environment. The construction of the mine has increased dust storms in the area. The frequent dust storms have a negative effect on the residents' and the livestock’s health. The locals demand that the government enforce stricter environmental regulations, but the government fails to address the issues properly. The Khovd residents fought to add the Khushuut mine to the “strategic importance” mine list so that the government can regulate and enforce environmental protection policies, but the GOM failed to take control of the mine. The inability of the government to protect the rights of the people left the community frustrated with the GOM.

In regards to environmental protection, both mines fail to adequately implement policies that ensure corporate responsibility in addressing environmental degradation. The community voiced concerns of competing for scarce water supply, limited grazing land for livestock, poor air quality caused by raised dust and overall environmental degradation due to the nature of extraction industry. The government passed “Mining Prohibition Law” to ensure prevention of water contamination and forest degradation, but weak enforcement mechanisms prevent accountability.

CHAPTER V: CONCLUSION

The Mongolian democratic transition changed the economic and political fabric of the country. In 1990, the country decided to reverse 70 years of socialism to modernize its economic and political policies. The goal of the newly established country was to stimulate economic growth and strive for social progress, with increasing its citizens' living standards as the ultimate goal. Additionally, fair and democratic representation was adopted to ensure everyone had the equal opportunity to participate in the political process and had the power to challenge the government if the administration did not adequately ensure societal wellbeing.

This thesis' research questions encompassed series of interrelated inquiries including 1) whether *human* development can be achieved through extraction industries 2) whether the source of FDI has a strong impact on development outcomes, and 3) whether FDI influences state-led development efforts and decision making to the extent that it threatens the development of Mongolian sovereignty.

The results showed that successful economic growth and societal progress depends on the government's ability to manage resources. As a relatively young democracy, the research indicates that Mongolia is struggling to maintain a stable political environment. Mongolia's abundant natural resources provided an opportunity for foreign investors to invest in developing the extraction industry. However, the inexperience of Mongolia's government and a lack of regulatory procedures hindered a smooth partnership. The mining boom and increasing international attention forced the government to experiment with various investment and mining laws. Unfortunately, the laws were often inconsistent and without adequate clarifications for enforcement guidelines. The uncertain investment environment discourages foreign investors. The consequence of losing foreign investment can diminish economic growth and subsequently, the funding for social welfare programs.

Although foreign investment can provide much economic benefit, the research indicated that it could also erode state sovereignty if the country has weak enforcement protocols. The research case study shows that the Chinese mining company undermined state sovereignty by its unwillingness to comply with the Mongolian "strategic importance" mining law. The Chinese company was able to assert its economic dominance over the government to force the government to make an exception on its behalf. A multinational corporation with financial power to force the government to subvert its authority is dangerous for sovereignty.

The relationship between the Chinese corporation and the Mongolian government clearly demonstrated the world systems theory in action. As the literature review indicated, the core countries actively undermine the periphery to ensure underdevelopment. The Chinese corporation's action that undermined the Mongolian law clearly indicates a core country exerting its power over a periphery. If Mongolia wants to become a semi-periphery nation and compete in the international arena, the government must act to protect its sovereignty.

A resolution can be found in Mongolia's vibrant civil society. As demonstrated in the background chapter and the case study, the Mongolian public is highly active in the political sphere. In June 2016, the discontent with the ruling DP forced the public to oust the DP and vote MPP in a landslide victory as the ruling party. The civil society held the government accountable by participating in their civic duty through voting. Furthermore, citizens saw the increasing foreign influence in the Mongolian mining industry and demanded laws that protect the interest of the Mongolian people and the environment. Consequently, the government adopted more conservative laws in the mining sector. Although some of the laws discouraged foreign investors, the public had the power to force the government to act. These actions by the citizens are the reason that they play a major role in the crucial "state building" process. Civil society engagement can help combat government instability.

The literature review on development theory in Chapter 2 indicated the rise of human development theory that prioritized societal wellbeing. Although the traditional neoliberal development indicator, GDP will suggest that the increase in the Mongolian GDP indicates development progress, the Mongolian citizens are pushing for a more sophisticated form of human development. They demand policies that advance societal wellbeing, such as better employment opportunities and environmental protection.

The literature and the data collected clarify the economic impact of foreign direct investment. The data collected indicated that the economy did experience remarkable growth thanks to the foreign direct investment in the extraction industry. However, as literature indicates, resource-led development can be volatile. Mongolia's overreliance on one industry is one of the indicators of a "resource curse." Chinese demand for Mongolia's copper and coal prioritized the mining industry as the main contributor to national economic growth. Although natural resources yield fast cash and can be extremely lucrative at times, it is based on market demand and the international political environment. Either a decrease in commodity price or change in law of a major natural resource importer can have a detrimental effect on an extraction-led economy. As demonstrated in Mongolia's economy in 2015 and 2016, the decrease in China's demand for copper and coal contracted Mongolia's double-digit GDP rate.

The government must work towards diversifying the industries that contribute to economic growth. The lack of development of the agriculture sector has few harmful consequences. First, the extraction industry is not sustainable. Eventually, the natural resources will be exhausted. If there is not an alternative source of revenue, the economy will inevitably collapse. Second, the mining sector is capital intensive and does not require a large workforce. The revenues from the mining industry must be invested towards the development of domestic industries such as agriculture. The existence of diverse industries can create more employment opportunities. Adequate domestic investment in the agriculture sector can alleviate the high unemployment rate because agriculture is labor intensive. The necessity of agriculture development is outside the scope of this thesis, however, it is an important topic for Mongolia's food security. Further research can provide additional information on the benefits of encouraging agriculture sector. Nonetheless, considering long-term, future economic growth is necessary for sustainable development.

Furthermore, the Mongolian tradition has always called for the preservation of the ecosystem and the creatures that live among the herders. The conservation of cultural heritage is an important aspect of Mongolian identity. The development of extraction industries has had a detrimental effect on the environment and the lifestyle of the traditional herders. Therefore the government of Mongolia should have a strict enforcement procedure on environmental protection laws that hold foreign and domestic investors accountable for any environmental degradation.

Most importantly, equal societal progress must be one of the highest priorities of the government. The remarkable economic growth did alleviate poverty and increased the overall living standard of the people. However, there are regional disparities in access to quality education, health care, and employment opportunity. There needs to be effective social programs that target rural residents to improve their living standards. The success of the government depends on the wellbeing of its citizens.

According to the results of the case study, the Chinese and Anglo-Australian investors had a difference in regulatory compliance and corporate social responsibility. In regards to compliance, the Anglo-Australian investor actions were more transparent than the Chinese investor's. The accessibility of documents, statistics, revenue reports and company information was more readily available for OT. However, there is a variable that the OT investors are well-established company with years of investment experience. On the other hand, the Chinese investors are new to the extraction industry, and the Khushuut mine was the first of its development projects. I argue that "inexperience" is not an adequate explanation for the lack of transparency. I resolve that all multimillion-dollar corporations in the extraction industry should maintain a high standard of transparency, due to the inherently exploitative nature of the mining business. Therefore, the lack of transparency should create suspicion and mistrust in the company.

As discussed in Chapter Three, the relationship between China and Mongolia is complex. The Mongolian people are suspicious of the presence of Chinese investors. The inherent pessimism alone could have swayed the locals to have a negative attitude towards the Chinese mine, but the Chinese investors did not take genuine actions to build a relationship with the community. The death of the boy might have set the tone for all future interactions, but the Chinese efforts to encourage community relationships were seen as a conciliatory rather than genuine. The biggest objection towards the Chinese presence is its 100% ownership of Mongolian natural resources. However, regarding the OT development, the society has had a more accepting attitude. The people did not think the Mongolian government had big enough shares, but it still had control of 34%. The Anglo-Australian investor did provide skills training, housing, and a community hospital, which had a positive reception from the locals.

The OT had a bigger influence in contributing to the economy than the Khushuut mine. The Chinese investor was accused of not paying the appropriate amount of taxes for years 2011 and 2012. The Chinese actions raise more questions than praise.

In regards to the environmental impact, the inherent nature of the extraction industry is destructive to the environment. Environmental degradation is a part of the mining business. Both mines are guilty of lacking appropriate measures to ensure environmental protection. The government of the host country has the responsibility to regulate environmental protection, but the environment destructive nature of extraction business makes it hard to contain the damage.

The overall conclusion of the research indicates that Mongolia is at crossroads. The mining boom provides significant revenue for economic growth. However, the revenue is not sustainable, and it is highly volatile. The government of Mongolia needs to decide what kind of agent it wants to be. Now, more than ever, the Mongolian government has the opportunity to become one of the success stories like the "Asian Tigers." Not many countries succeed with the resource-led development, but Mongolia has only three million people. The proper management of mining revenue and willingness to invest in domestic markets can have a significant influence on the growth of the country.

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