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Mongolian Dependence a Threat

By The Moscow Times

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ULAN BATOR, Mongolia — Mongolia's growing dependence on neighboring Russia and China for fuel and power poses a major risk to its booming mining sector that investors need to consider, foreign business executives said.

Landlocked Mongolia, which hopes to raise some $25 billion over the next five years to build roads, railways and mining towns, imports about 90 percent of its petroleum products from Russia, while the rest comes from China.

The sprawling country, which produces only about 4 billion kilowatt hours of power annually, already relies on imports from its northern neighbor Russia for about 4 percent of its current consumption and is in talks to import power from China.

Officials say electricity import needs are set to rise sharply.

Reliance on essential energy supplies makes Mongolia vulnerable to supply shocks and price rises, especially as Russia has been known to turn off supply taps, for example during price disputes with Ukraine, according to Paul Aston, a partner at law firm Holman Fenwick William, which helps conduct risk assessments for mining companies.

This vulnerability has been felt acutely this year, after Russia cut oil and diesel exports to Mongolia in April due to shortages on its own domestic market, a move that crimped mining activity while driving up pump prices and bus fares.

The continued shortfall has come at a critical time, with diesel demand from construction, agriculture and mining peaking during the summer months when productivity is at its peak.

According to local media, the diesel shortage has forced the Mongolian government to order a temporary halt of diesel supplies to some miners, suspend some railway operations and dip into its emergency stockpile.

Supplies from Russia have yet to resume. Some miners have now resorted to refueling their trucks from China, and the Mongolian government has also been buying small amounts from China — although they are 40 percent more expensive than those from Russia.

"There is a real shortage of diesel ... and the impact is felt across wide sectors in the country, especially miners," said Jim Dwyer, executive director of the Business Council of Mongolia, representing foreign firms.

"Mongolia needs its own refinery, and that's the only way it can break out of its dependence on Russia for its fuel needs," he said earlier this week.

Mongolia has suffered numerous fuel shortages since the 1990s after the dismantling of the communist system, and the government has drawn up plans to build its own refineries.

The earliest start of its first refinery is set for fall 2014, under a plan by Japan's Marubeni, Toyo Engineering and Mongolian Mongol Sekiyu to build a $600 million plant in Darkhan, a city about 200 kilometers north of Ulan Bator.

"These sorts of fuel shortages can threaten the project timeline and push up mining costs, so it's a risky business. There may be plans for a refinery, but that will only come three years later, and its not uncommon to see construction delays," said a mining executive who asked not to be identified.

Mongolia uses about 1 million tons of petroleum products annually, with diesel accounting for up to 60 percent of such consumption.

To feed growing demand for electricity from miners, the Mongolian government is looking to build new power plants in the south Gobi region and as well as near the massive Oyu Tolgoi copper-gold mine project.

The government has also given approval for Oyu Tolgoi investors Rio Tinto and Ivanhoe Mines to build an electricity line to the Mongolia-China border to import power from China.

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