

Kyrgyz Republic: Fifth Review Under the Three-Year Arrangement Under the Poverty Reduction and Growth Facility—Staff Report; and Press Release on the Executive Board Consideration

In the context of the fifth review under the three-year arrangement under the Poverty Reduction and Growth Facility with the Kyrgyz Republic, the following documents have been released and are included in this package:

- the staff report for the fifth review under the three-year arrangement under the Poverty Reduction and Growth Facility, prepared by a staff team of the IMF, following discussions that ended on **May 4, 2004**, with the officials of the Kyrgyz Republic on economic developments and policies. **Based on information available at the time of these discussions, the staff report was completed on June 14, 2004.** The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.
- a Press Release summarizing the **views of the Executive Board** of the staff report that completed the review.

The documents listed below have been or will be separately released.

Poverty Reduction Strategy Paper Annual Progress Report
Joint Staff Assessment of the Poverty Reduction Strategy Paper Annual Progress Report
Memorandum of Economic and Financial Policies by the authorities of the
Kyrgyz Republic*
Technical Memorandum of Understanding*

*May also be included in the Staff Report

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

To assist the IMF in evaluating the publication policy, reader comments are invited and may be sent by e-mail to publicationpolicy@imf.org.

Copies of this report are available to the public from

International Monetary Fund • Publication Services
700 19th Street, N.W. • Washington, D.C. 20431
Telephone: (202) 623-7430 • Telefax: (202) 623-7201
E-mail: publications@imf.org • Internet: <http://www.imf.org>

Price: \$15.00 a copy

**International Monetary Fund
Washington, D.C.**

INTERNATIONAL MONETARY FUND

KYRGYZ REPUBLIC

**Fifth Review Under the Three-Year Arrangement Under
the Poverty Reduction and Growth Facility**

Prepared by the Middle East and Central Asia Department
(in cooperation with other Departments)

Approved by Julian Berengaut and Michael Hadjimichael

June 14, 2004

- Discussions for the fifth review under the Poverty Reduction and Growth Facility (PRGF) arrangement were held in Bishkek, April 20–May 4, 2004. Access under the arrangement is SDR 73.4 million (82.6 percent of quota), of which SDR 54.3 million has been disbursed. The mission assisted the authorities in devising policies for their Supplementary Memorandum of Economic Policies (SMEP) covering the remaining program period through September 30, 2004. The staff team consisted of Messrs. Saavalainen (head), McDonald, Zeuner (MCD), Aiyar (PDR), and Ogata (FAD). Mr. Mukhopadhyay (Resident Representative) and Mr. Dubashev of the Bishkek office assisted the mission. Mr. Steudler (Advisor to the Executive Director) participated in key meetings during the final days of the mission.
- The mission met with President Akayev, Prime Minister Tanaev, Deputy Prime Ministers Otorbaev and Mateev, Minister of Finance Abildaev, National Bank Chairman Sarbanov, other senior officials, members of parliament, and representatives of civil society and the business community.
- The Executive Board completed the fourth review on January 14, 2004. At that time, Directors commended the authorities for their sound macroeconomic policies over the first two years of the program and noted that these policies had contributed to continued low inflation, satisfactory growth, and declining poverty rates. They stressed that the success of the debt reduction strategy, including possible further debt relief, rested on strong program performance. Strict fiscal discipline would be imperative in the run-up to the 2005 elections. Directors considered governance reforms as crucial to investment, growth, and poverty reduction.
- Relations with the IMF, World Bank, Asian Development Bank, and European Bank for Reconstruction and Development are summarized in Appendices I–IV. The Fund’s provision of technical assistance is described in Appendix V. The periodicity, availability, and quality of economic statistics are satisfactory and are discussed in Appendix VI.
- Outreach work conducted by area department missions and the resident representative office comprises media contacts and meetings with representatives of civil society and the diplomatic and business communities.

	Page
Executive Summary	4
I. Performance Under the Program	5
II. Policy Discussions	10
A. Fiscal Policy.....	12
B. Monetary and Exchange Rate Policies	13
C. External Policies	14
D. Structural Reform.....	15
III. Program Monitoring.....	16
IV. Staff Appraisal	17
Box	
1. Recent Developments in the Gold Sector.....	11
Text Tables	
Poverty Indicators, 1998–2003.....	5
Selected Financial Indicators, 2002–2004.....	9
Key Macroeconomic Indicators, 2002–2004	10
Saving-Investment Balance Summary, 2000–2007	12
Text Figures	
Real GDP Growth and CPI Inflation.....	5
Exchange Rate Developments	6
NBKR Purchases and Commercial Banks Excess Reserves	8
NPV of Debt-to-Exports	15
Debt Service-to-Revenues	15
Tables	
1. Third-Year Quantitative Program Targets.....	22
2. Structural Conditionality in the Third Annual Program.....	23
3. Selected Economic Indicators, 2000–2007	24
4. Saving-Investment Balance, 2000–2007	25
5. General Government Finances, 2001–2007	26
6. State Government Finances, 2001–2007 (in million soms)	27
7. State Government Finances, 2001–2007 (in percent of GDP).....	28
8. Social Fund Operations, 2001–2007	29
9. Medium-Term Expenditure Framework for General Government by Functional Classification, 2000–2007	30

10. NBKR Accounts, 2002–2004	31
11. Monetary Survey, 2002–2004	32
12. Quarterly Balance of Payments, 2002–2004	33
13. Medium-Term Balance of Payments, 2000–2010	34
14. Indicators of Fund Credit, 2003–2007	35
15. Prospective Use of Fund Resources, 2004–2007	36
16. Reviews and Disbursements Under the Three-Year PRGF Arrangement	37
 Figure	
1. Performance Under the Program (December 2001–March 2004)	7
 Attachment	
Third-Year Supplementary Memorandum of Economic Policies	38
 Annex	
Supplementary Technical Memorandum of Understanding	52
 Appendices	
I. Fund Relations	68
II. Relations with the World Bank Group	70
III. Relations with the Asian Development Bank	73
IV. Relations with the European Bank for Reconstruction and Development (EBRD)	75
V. Technical Assistance Provided by the Fund, March 2003–May 2004	77
VI. Statistical Issues	78

EXECUTIVE SUMMARY

Macroeconomic performance has remained strong into 2004 and economic developments are in line with earlier staff projections. Growth reached nearly 7 percent in 2003 and continued at a similar rate in the first four months of 2004. The price pressures observed in late 2003 have subsided. Both exports and imports grew robustly in 2003 and the current account deficit declined to below 3 percent of GDP. The nominal exchange rate has remained broadly stable. The sustained strong macroeconomic performance has contributed to a decline in the official poverty rate from 55 percent as recently as 1999 to 41 percent in 2003. Despite progress, however, poverty remains high and the economy faces significant uncertainties, particularly regarding external debt dynamics and the impact of declining gold production on the medium-term balance of payments.

All end-March 2004 performance criteria were observed. Monetary and tax revenue targets were met comfortably. However, despite the fact that the planned spending cuts were only partially implemented, the October 2003–March 2004 state government fiscal deficit target was met. Implementation of the VAT on agriculture and the real property tax remains weak. Progress on the program’s structural agenda, including the reduction of the electricity sector quasi-fiscal deficit, was satisfactory.

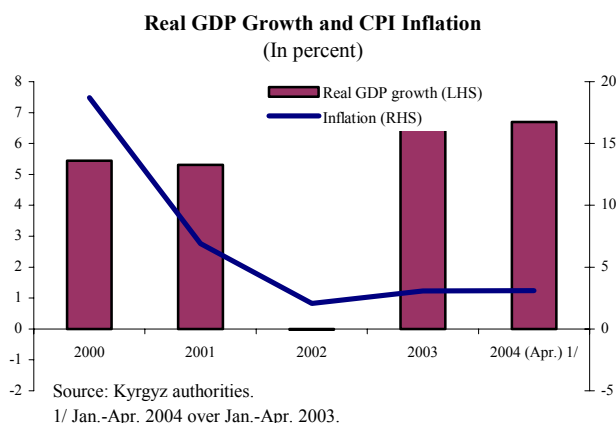
With the program on track, the staff and authorities agreed that the overall policy strategy elaborated in IMF Country Report No. 04/16 remains appropriate. Discussions focused on refining the end-September quantitative targets and extending the structural reform agenda. Reflecting the performance in early 2004, the real GDP growth projection for the year was raised from 4 to 4½ percent. Revisions to quantitative targets were minor, except for changes related to the restructuring of the Kumtor gold mine. This is expected to result in large privatization revenues that would be reflected in higher government deposits with the central bank and stronger NBKR official reserves. The successful completion of the current arrangement could set the stage for the Paris Club debt stock relief in early 2005 that is critical for debt sustainability.

The structural reform agenda will continue to focus on governance, the banking sector, and the electricity sector. Agreement was reached on several key governance-related steps in the mining sector, including the authorities’ adoption of the Extractive Industries Transparency Initiative (EITI) and an external risk assurance and control audit of Kyrgyz Altyn.

I. PERFORMANCE UNDER THE PROGRAM

1. Economic developments have been broadly in line with earlier staff projections and the strong macroeconomic performance of 2003 continued into early 2004.

Following the 6.7 percent real GDP growth in 2003, the authorities estimate that growth continued at the same pace in January-April 2004. Despite declining energy output, real GDP excluding gold production grew 5 percent in the first four months of 2004, suggesting that growth is becoming more broad-based. The price pressures that mainly resulted from supply disruptions in late 2003 have abated. During January–April, cumulative consumer price inflation was less than 1 percent. Money demand has continued to strengthen and the domestic currency has been stable.



2. **The expenditure-based poverty rate declined from 55 percent in 1999 to 41 percent in 2003, helped by 47 percent growth in U.S. dollar per capita GDP.** During the same period, income inequality declined as poverty fell more in rural than in urban areas. A PRSP progress report prepared by the authorities accompanies this report and discusses poverty reduction policies and outcomes in detail.

Kyrgyz Republic: Poverty Indicators, 1998–2003

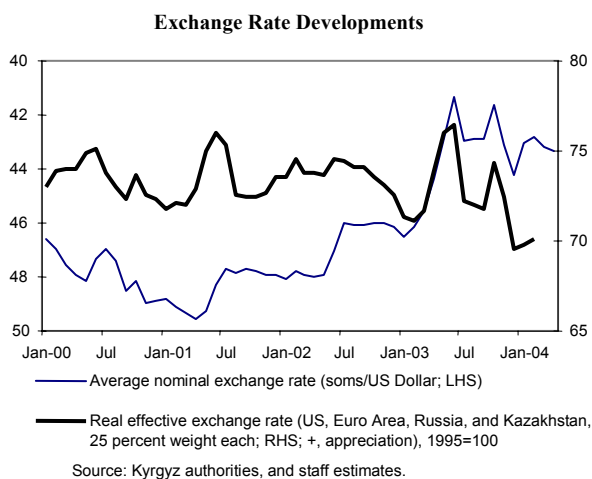
	1998	1999	2000	2001	2002	2003 Est.
Poverty rate (in percent) 1/	55	55	52	48	44	41
GINI coefficient 2/	0.36	0.37	0.33	0.32	0.33	0.30
Per capita GDP (U.S. dollars)	341	257	278	309	324	378

Sources: Kyrgyz authorities; World Bank; and Fund staff estimates.

1/ National definition; based on per capita expenditure adjusted for household size.

2/ Expenditure approach.

3. **The current account deficit declined from 3.9 percent of GDP in 2002 to 2.7 percent in 2003, with both exports and imports registering strong growth.** The strong export performance was underpinned by the recovery of gold production, while strong domestic demand fueled import growth. Gross international reserves increased to 4.8 months of imports by the end of the year. Preliminary data suggest a continuation of strong export and import growth in the first quarter of 2004. The competitiveness of Kyrgyz goods remains satisfactory, as reflected in the low average wage level relative to that of key trading partners¹ and a 4 percent depreciation of the real effective exchange rate during 2003.

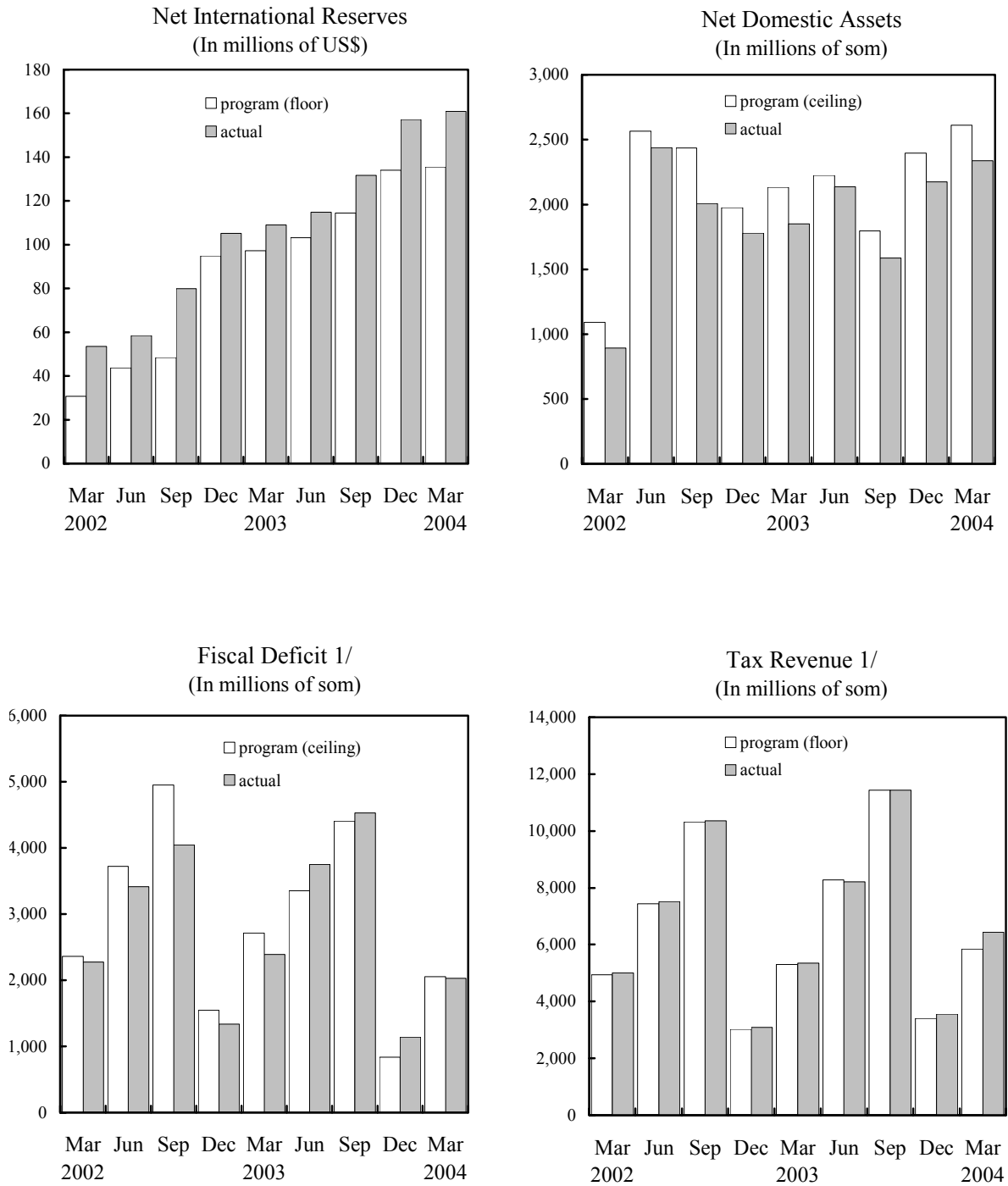


4. **All end-March performance criteria were observed (Table 1, Figure 1).** State tax collections for October–March exceeded the target by 0.5 percent of annual GDP largely owing to higher-than-expected taxable imports. Payroll tax collections also comfortably exceeded the target. Higher-than-expected state expenditures in the first quarter reflected a relatively large carryover of 2003 commitments and the authorities undertook additional spending restraint to meet the end-March fiscal deficit target.² The indicative target for the 2003 electricity sector quasi-fiscal deficit (QFD) was observed. The QFD of som 9,240 million was equal to 11.1 percent of GDP, compared to 12.0 percent in 2002.

¹ The average monthly wage was \$45 compared to \$156 in Kazakhstan and \$180 in Russia.

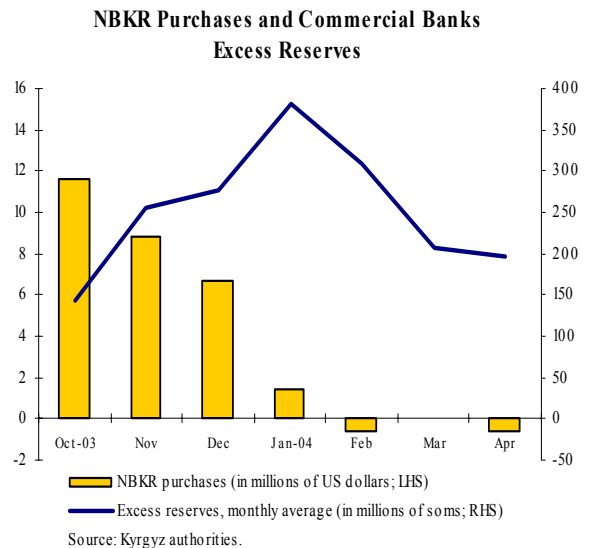
² Planned spending cuts in 2003 Q4 of som 500 million (0.6 percent of GDP) described in (IMF Country Report No. 04/16) were only partly implemented. This, and the delay of the EU Food Aid grant, contributed to a small deviation of the fiscal deficit from the end-December 2003 benchmark.

Figure 1. Kyrgyz Republic: Performance Under the Program
(December 2001– March 2004)



Source: Kyrgyz authorities; and Fund staff estimates.
1/ Cumulative during program period (October-September).

5. **The monetary program's net international reserve (NIR) floor was exceeded by 11 percent of reserve money and the central bank's net domestic assets (NDA) remained below the program ceiling.** Unsterilized foreign exchange interventions contributed to monetary growth in late 2003, but the NBKR has tightened monetary conditions since December and banks' excess reserves have declined. Although reserve money remained 8 percent above the indicative ceiling at end-March, this appears to have been matched by stronger-than-anticipated money demand, keeping inflation expectations at bay. With the continuing remonetization, private sector credit grew by one third in the 12 months to end-March 2004.³



6. **With the preparation and publication in March 2004 of the 2005–07 Medium-Term Fiscal Framework (MTFF) (structural benchmark), the authorities further improved fiscal transparency.** The framework builds on quantitative policy plans prepared for the Ministries of Health, Education, and Agriculture. Most components of the end-March structural benchmark on tax policy were implemented. The general VAT threshold was raised from som 300,000 to som 500,000, aligning it with the threshold applied in agriculture. Also, the zero-rating under the VAT of exports of certain services was clarified by defining the place of supply consistent with international practice, and the authorities reviewed the list of VAT exemptions on goods with a view to limiting such exemptions to those consistent with international practice. In addition, voluntary patent tax rates were increased on April 1, 2004 by an average of 45 percent. The restructuring of small business taxation was delayed in order to be included in the new Tax Code later this year (see paragraph 18).

7. **External public debt (excluding Kumtor) at end-2003 was 89 percent of GDP, down from 111 percent at end-2000.** The third-year consolidation period under the 2002 flow rescheduling was approved by the Paris Club in April 2004. Bilateral negotiations with the Kuwait Fund on debt rescheduling have so far been unsuccessful, but all other agreements have been concluded consistent with the 2002 Paris Club recommendations.

³ Despite high rates of credit growth, the ratio of credit to GDP has remained moderate and rose by just 2 percentage points during 2001–03.

8. **Banking sector reform aims at strengthening financial intermediation and banking competition has intensified following the transfer of three more banks to foreign ownership in 2003.** On the privatization of Kairat Bank, three Kazakh banks have filed bids and the sale is expected to take effect in July, once a banking license has been approved by the NBKR. To strengthen bank supervision, Parliament adopted the Bank Insolvency Law in February 2004 and is considering a revised Anti Money Laundering Law that would incorporate the June 2003 recommendations of the Financial Action Task Force (FATF). The new Bank Supervision Manual has been adopted and commercial banks' IAS-based financial statements are now being published quarterly. Due to a lack of funding, however, the financial accounts of the Savings and Settlement Corporation (SSC) will be audited by an international reputable firm beginning with the 2004 statements, one year later than envisaged. Overall, aggregate financial sector indicators do not suggest any imminent vulnerabilities, although the sector remains small compared with other transition economies.

Kyrgyz Republic: Selected Financial Indicators, 2002–04
(In percent and end-of-period, unless otherwise indicated)

	2002	2003	2004 Feb
Net total capital/risk-weighted assets	36.4	35.2	31.1
Liquidity ratio 1/ 2/	82.7	93.2	91.6
Nonperforming loans/total loans	13.3	11.2	10.8
Return on equity 3/	5.1	8.0	8.5
Loans/deposits	57.0	60.6	57.6
Share of foreign currency loans in total loans	57.9	61.1	59.8

Source: National Bank of the Kyrgyz Republic.

1/ Average weighted liquid assets/average weighted liabilities with maturities under 30 days.

2/ Period average, starting 2003.

3/ Net profits/net Tier 1 capital.

9. **On governance reform, a significant step forward was taken with the adoption on May 14, 2004 of the Extractive Industries Transparency Initiative (EITI).**⁴ Also in May, the National Integrity Council (NIC) approved its Reform Strategy at a meeting chaired by the president. The NIC's work is being supported by an advisory council that includes key

⁴ Launched by UK Prime Minister Blair in 2002 and now led by the UK's Department for International Development, the EITI aims to increase transparency of financial relations and flows between extractive industries and governments.

members of the donor community. The authorities have taken several steps toward improving the business environment, consistent with the Economic Deregulation Concept paper recently approved by the president. These include the adoption by parliament of the Law on the Fundamentals of Technical Regulation, new rules requiring public consultation prior to changes in business legislation, and legal amendments to improve licensing and audit procedures. On corporate governance, all non-financial enterprises listed on the Kyrgyz Stock Exchange (KSE) must apply International Accounting Standards (IAS) 2001 to their 2004 and later financial statements.

10. **Regarding the privatization of Kyrgyz Telecom**, negotiations with the top bidder under the June 2003 tender were unsuccessful. This was due to what the authorities described as concerns over the investor's credibility, differences over the settlement procedure and payment terms, and concerns over the investor's intentions for medium-term tariffs. The authorities continue to negotiate with other tender participants.

II. POLICY DISCUSSIONS

11. **With the program largely on track, the staff and authorities concluded that the overall policy strategy described in IMF Country Report No. 04/16 remains appropriate.**⁵ Discussions for the fifth review focused on refining the end-September quantitative targets and deepening the structural reform agenda.

12. **Reflecting the stronger-than-expected performance in early 2004, the revised program is based on slightly higher growth of 4½ percent for the year.** The projected 12-month consumer price inflation remains at 4 percent. A moderate widening of the current account deficit is envisaged, owing to flat gold exports, while strong domestic

Key Macroeconomic Indicators, 2002–04

	2002 (act.)	2003 (prel.)	2004 (proj.)
Real GDP growth (percent)	0.0	6.7	4.5
CPI inflation (e.o.p., percent)	2.3	5.6	4.0
Current account (percent GDP)	-3.9	-2.7	-3.9
Official reserves (months of imports)	4.1	4.8	5.4

Source: Staff estimates and projections.

demand continues to generate import growth. On the capital account, the macroeconomic framework assumes a \$60 million inflow because of the sale of shares in Centerra—the new company for the restructured Kumtor gold mine project (Box 1). The program also assumes \$25 million of balance of payments support from the AsDB in 2004. These inflows, with

⁵ The strategy for the third annual program rests on: (i) addressing the unsustainable external debt level through continued fiscal consolidation, (ii) offsetting the expected decline in gold production through export diversification, to be achieved through low inflation to preserve cost competitiveness, and (iii) promoting structural reforms to foster productivity growth.

private transfers, foreign financed public investment and Paris Club Debt flow relief, would allow gross reserves to rise to 5.4 months of imports by the end of the year.

Box 1. Recent Developments in the Gold Sector

Two recent developments in the gold sector have macroeconomic implications.

First, the Kyrgyz Government and Cameco Corporation agreed to transfer ownership of the Kumtor gold mine to Centerra, a new company being listed on the Toronto Stock Exchange. The Kyrgyz Government would initially take a one-third equity position in Centerra but would effectively privatize part of its stake by selling Centerra shares. Current plans envisage the Government selling down its share to 20 percent at the time of the listing. Although the amount of sales receipts will depend on market valuation, for purposes of the financial program, receipts of \$60 million (3 percent of GDP) are assumed. The full amount of these receipts is to be transferred to a government account in the NBKR to be used by the budget in the medium term. Thus, the monetary impact of the inflow would be fully sterilized. The restructuring would also increase tax revenues, by 0.2 percent of GDP, as some of the earlier tax provisions will lose force. The restructuring agreement also covers additional gold deposits in the area, effectively lengthening the life of the mine. Sale of the government's Centerra shares would ease financing constraints and allow deficits modestly larger than previously envisaged, without increasing external debt. Correspondingly, the new MTFF accommodates additional health and education investments of 0.3 percent of GDP in 2005, 2006, and 2007.

Second, two new gold projects are being developed. Investment in these projects, estimated at \$60 million in 2004–05 (3 percent of annual GDP), will contribute to strong import growth. Medium term export projections have been raised to reflect the new gold projects. The Jeeroy and Taldy-Bulak projects could begin production in late 2005, with annual output plans during the rest of the decade equivalent to 40 percent of Kumtor's current production. Nevertheless, these projects would be inadequate to halt the declining trend in gold output.

13. **Higher investment ratios over the medium term will support the projected 5 percent medium-term growth.** Investment growth would be facilitated by domestic saving resulting from further fiscal consolidation, even as the non-government savings ratio declines slightly. While the foreign-financed government investment program continues to be streamlined to better manage external debt, other government investments are expected to rise, with capital inflows from Centerra and the reallocation of spending. Reflecting continued macroeconomic stability and credit growth, there are early signs of a rebound in non-government investment, including in new gold projects. In addition, over the next few years foreign direct investment is expected to accelerate with the two new gold projects and the Kyrgyz Telecom privatization. The staff stressed, however, that these trends are subject to risks if the government fails to further improve the business climate through structural reforms.

Saving-Investment Balance Summary, 2000–07

	2000 Act.	2003 Est.	2004 Proj.	2007 Proj.
	In percent of GDP			
Total Investment	20.0	17.6	18.0	19.6
Government	8.1	4.8	4.2	4.5
Non-government	11.9	12.8	13.8	15.1
Total domestic savings	13.4	14.9	14.1	16.3
Government	-2.1	-0.8	-0.7	1.3
Non-government	15.5	15.7	14.8	15.0
Foreign savings	6.6	2.7	3.9	3.3

Source: Staff estimates and projections.

A. Fiscal Policy

14. **Maintaining expenditure discipline, strengthening tax administration, and developing the strategy for small business tax reform were the focus of fiscal policy discussions.** The staff agreed with the authorities that there was scope to modestly increase the end-September and 2004 nominal fiscal deficit targets as the ratio of the 2004 state government deficit to GDP could still be kept at 4.4 percent. This implies a 0.8 percentage point fiscal adjustment in 2004.

15. **The nominal tax revenue target was raised, reflecting strong performance in tax collections and fewer tax breaks in the Kumtor restructuring agreement.** Nevertheless, with two key taxes—the agricultural VAT and the real property tax—still not performing adequately, the ratio of state tax revenues would reach only 14.6 percent, 0.2 percentage point below the level envisaged earlier. Projected receipts from the agricultural VAT for the year were roughly halved, to 0.2 percent of GDP. The Social Fund tax collection target was kept at 4.6 percent of GDP. The staff reached understandings with the authorities to keep cigarette excises unchanged for the time being but reduce gasoline excises to better harmonize indirect taxation with that in neighboring Kazakhstan to reduce smuggling.

16. **On the expenditure side, the authorities have maintained their commitment not to undertake new spending outside the budget unless offsetting cuts are identified.** The

staff and authorities considered that, following the 15 percent increase granted in April, adequate resources were available to carry out the second stage of wage increases for teachers, nurses, and doctors as planned to bring the overall pay rise for the year to 30 percent. No other wage increases are expected this year, and the ratio of the wage bill to GDP is now programmed at 7.2 percent in 2004, below both the 2003 outcome and the earlier 2004 projection.

17. **Opposition to the effective implementation of the agricultural VAT and the real property tax remains entrenched.** Weaknesses in general VAT procedures—in particular, apparent difficulties in managing the invoice credit mechanism and refunding for exporters⁶—exacerbate legislators’ and taxpayers’ opposition to the tax. An FAD technical assistance mission in July will focus on VAT administration as well as the operation of the large taxpayer unit. On the real property tax, valuation guidelines remain under consideration in the parliament, whose action is required before local authorities can impose the new tax.

18. **The staff welcomed the authorities’ initiative in forming a task force to redesign the Tax Code.** The task force is receiving advice from international consultants, including the Moscow-based Institute for Economies in Transition and the USAID. The mission agreed with the authorities to postpone the small business tax reform to undertake it together with other changes to the tax code, which are to be submitted to parliament in parallel with the 2005 budget. The tax code reform will advance on three tracks: (i) revise the code to remove inconsistencies and ambiguities and broaden its coverage; (ii) simplify small business taxation, taking into account the need to realign, and possibly unify, the VAT and small business tax thresholds, define taxes to be replaced, and eliminate the current patent tax system (submission of a draft proposal to the Economic Policy Council is a structural benchmark for end-August 2004); and (iii) consider possible tax rate cuts at the time of finalizing the 2005 budget.

B. Monetary and Exchange Rate Policies

19. **Remonetization of the economy is projected to slow following an increase of the broad money-to-GDP ratio to 18 percent in 2003, from 11 percent in 2001.** Program revisions were based on a projected 5 percent increase in real money demand, supported by low inflation expectations and solid growth. A tighter fiscal stance than in 2003 and the full transfer of receipts from the Kumtor mine restructuring to a government account at the NBKR would contribute to the accumulation of government deposits in the central bank, reducing NDA and helping to sterilize the monetary impact of the anticipated foreign exchange inflows. Largely because of the sale of Centerra shares, the NIR target for end-2004 was revised from \$169 million to \$240 million, or 96 percent of reserve money.

⁶ The authorities agreed to reduce outstanding VAT refund claims by large taxpayers (exporters) from som 78 million at end-March 2004 to som 35 million or less by end-September 2004.

These targets, and the projected further dedollarization, should result in 14 percent growth in some broad money and 9 percent increase in reserve money during 2004. With net claims of the banking system on government declining, there is ample room for private sector credit to expand. Despite the rapid projected growth in private sector credit, the ratio of the stock of credit to GDP would rise only to 5.8 percent, from 4.7 percent at end-2003. The staff and the authorities agreed, however, that if the credit expansion shows signs of negatively affecting banks' loan portfolios, the government will sell more securities in the market to contain credit growth and provide banks with alternative low-risk investment opportunities. Exchange rate policy is expected to continue on its recent course, with the central bank intervening only to smooth short-term fluctuations.

C. External Policies

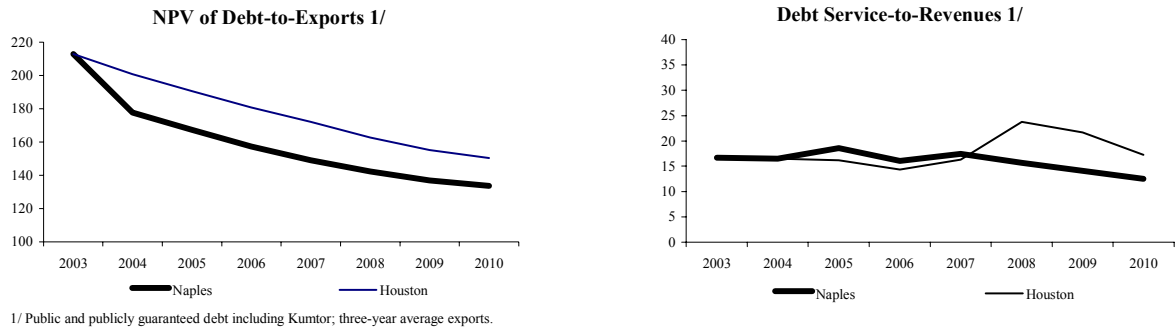
20. **The government intends to continue its efforts to develop regional trade and transit systems, building on recent achievements.** Trade relations between Kazakhstan and the Kyrgyz Republic were improved by a meeting between the two Presidents in December 2003, at which it was decided that Kazakhstan will charge Kyrgyz goods shipped by rail through its territory at domestic tariffs. In January the Kazakh parliament ratified the 1998 International Transport Agreement, establishing permit-free transit of Kyrgyz trucks through its territory. The March 2004 agreement between customs authorities supplemented the earlier meeting between heads of state and settled that transiting trucks will not have to pay a deposit at the border, and will not need to be accompanied by customs escorts. The staff noted, however, that given the ineffectiveness of past regional trade initiatives, it was important to follow through with vigorous implementation.

21. **The staff presented three illustrative external debt scenarios.** They differed according to the assumptions on possible further Paris Club debt rescheduling: (i) no further rescheduling; (ii) rescheduling on Houston terms; and (iii) rescheduling on Naples terms. Compared with earlier debt simulations, solvency ratios improve under all scenarios.⁷ Simulations suggest that the Kyrgyz Republic will need further debt relief if it is to avoid a period of disorderly adjustment and instead continue on a sustainable path of economic growth and poverty reduction.⁸ Rescheduling under Houston terms would temporarily relieve the liquidity constraint, but only a concessional debt stock operation would reduce liquidity ratios permanently and ensure a significant decline in solvency ratios. Nevertheless, stress testing points out that even under Naples terms, debt sustainability would remain vulnerable to internal and external shocks, underscoring that potential debt relief must be accompanied

⁷ This more favorable outcome compared with previous simulations (*Debt-Sustainability in Low-Income Countries—Proposal for an Operational Framework and Policy Implications*, Box 2, (www.imf.org)) mainly reflects exchange rate movements in 2003.

⁸ Without further rescheduling, the ratio of debt service to fiscal revenue would increase to 28 percent in 2005, from 17 percent in 2004.

by strong stabilization policies and cautious external borrowing. To provide a cushion against shocks—and because future debt service obligations would remain high—the official reserves coverage must remain at levels significantly higher than those in other flexible exchange rate regime countries.⁹



D. Structural Reform

22. **Discussions focused on deepening the structural reform agenda, particularly in governance and the banking sector.** The authorities, including the President, agreed with the staff on the importance of strong governance measures in the mining sector, especially in view of the significant macroeconomic role of the sector (40 percent of merchandise exports) and the current Kumtor mine restructuring. In the absence of World Bank conditionality in this area, several key measures were introduced into the program, including as structural benchmarks, with support and technical advice from Bank staff (SMEP, paragraph 28). These measures were derived from the principles of the EITI (paragraph 9). Regarding other areas of governance reform, the authorities will continue to implement their agenda in improving the efficiency of public administration and strengthening the legal system as described in Box 3 of the SMEP. Following the May meeting of the National Integrity Council on the governance reform strategy, the next step is to develop concrete measures to address corruption and governance problems identified in several perception surveys.

23. **There was agreement that further strengthening of bank supervision is needed to ensure that financial deepening remains healthy.** Based on technical assistance from the IMF's Legal Department, the authorities intend (end-September structural benchmarks): (i) to submit to parliament measures aimed at removing legislative inconsistencies that have sometimes stymied effective banking supervision, and (ii) to reduce the scope for such inconsistencies in the future. The authorities have deepened their banking reform program in several other areas as well (SMEP, Box 1).

⁹ In addition, the country's difficult geographic position and its relative lack of export diversification argue for maintaining high levels of official reserves.

24. **Following extensive discussions, the authorities decided to postpone the introduction of a Deposit Insurance Scheme (DIS).** They had planned to present DIS legislation to parliament in June 2004, but staff argued that further development of the banking sector and banking supervision were critical before a DIS could be successfully introduced. The SMEP calls for the identification of specific preconditions for the DIS during the next round of program discussions.

25. **Registration under the depositor compensation scheme has been extended to end-August.**¹⁰ The authorities estimate the claim on the government to total about som 700 million (0.8 percent of GDP), to be settled with 7-year marketable government bonds. Many of the oldest depositors have raised concerns that they may be unable to benefit from redeeming the bonds, and the staff agreed to the authorities' proposal for an early redemption scheme up to som 100 million per year, starting in 2005. Early redemption would also increase the present value of bonds, providing an opportunity to cash them in the market at smaller discounts. The government would use a portion of its central bank deposits (equivalent to a projected 5 percent of GDP at end-2004) to finance this domestic debt repayment.¹¹

26. **The authorities reiterated their commitment to further reduce the electricity sector quasi-fiscal deficit (QFD) in 2004.** In line with the arrangements on the pilot project on energy sector reform, the Fund-supported program includes overall targets on reducing the QFD while the World Bank leads IFI policy advice and conditionality regarding specific policy measures. In this context, the staff urged the authorities to strongly consider World Bank advice regarding the tariff increases this year, noting that these would obviate the need for sharper increases later. The staff also stressed that the fiscal program accommodated social compensation for vulnerable groups to offset the impact of an approximate 10 percent increase in electricity user costs.

III. PROGRAM MONITORING

27. Given the uncertainty of the timing and value of the Centerra shares sale revenue, the program's monetary targets would be fully adjusted for any excess or shortfall of these receipts. There are no other significant changes to program monitoring.

¹⁰ The scheme was approved by parliament in 1997 and later extended (IMF Country Report No. 03/216, Box 2). It covers the deposits of the former Soviet Savings Bank and three smaller banks that failed in the aftermath of the 1998 Russian financial crisis.

¹¹ The annual impact of the interest payments on the fiscal deficit is below 0.1 percent of GDP.

IV. STAFF APPRAISAL

28. **The authorities policy performance during the third-year PRGF-supported program has been commendable.** Monetary policy targets have been observed with comfortable margins and the fiscal program is on track, thanks to strong tax collection. Structural reforms have been carried out broadly as planned. As a result, economic growth has been sustained and broadened, inflation has remained low, and the external position has strengthened. These are significant achievements, but the run-up to 2005 parliamentary and presidential elections may threaten the policy discipline that is needed during the remainder of 2004 to ensure the successful completion of the PRGF arrangement.

29. **Fiscal pressures are the main risk for the remainder of the program.** The 2004 target for fiscal adjustment is ambitious but necessary to keep the external debt under control. While the government has avoided issuing new expenditure decrees without offsetting cuts, it must remain firm in resisting such demands and strictly adhere to its quarterly fiscal deficit targets if it is to avoid a fiscal relaxation that would endanger the significant economic gains achieved during the recent years. At the same time, however, the authorities should ensure that the strong spending discipline does not undermine state expenditures on poverty reduction. The recent improvement in tax collections is encouraging. However, the implementation of the agricultural VAT and the real property tax continue to lag. The authorities' plan to initiate a large-scale audit campaign on the agricultural VAT is welcome but the detailed procedures of the tax must be settled before the audit campaign could yield tangible results. Similarly, the parliament should urgently finalize the valuation regulations of real property tax to provide local governments an opportunity to start implementing this new revenue source.

30. **Monetary policy has successfully accommodated remonetization without rekindling inflation.** Abstaining from intervention in the foreign exchange market has contained liquidity, reduced inflation expectations, and let the nominal exchange rate to float freely. Staff supports the current cautious stance of monetary policy and believes that the floating exchange rate and minimal foreign exchange market intervention remain appropriate.

31. **Updated staff simulations suggest that the Kyrgyz Republic needs concessional debt relief.** Without further rescheduling, the country could face serious difficulties in meeting its external debt obligations, as its debt and debt service ratios would remain very high. Nonconcessional relief would help only temporarily. The contribution of the Kyrgyz authorities should be to preserve macroeconomic stability, deepen structural reforms, reduce corruption, and exercise caution in foreign borrowing to ensure that the potential concessional debt relief would be followed by durable growth and poverty reduction.

32. **Two developments give rise for cautious optimism in the medium term.** First, the financial restructuring of the Kumtor gold mine will ease the country's financing constraint to some extent. Using the related privatization receipts for investment in human capital should strengthen growth potential and is consistent with the authorities' poverty reduction

strategy. Second, recent developments in trade arrangements with Kazakhstan are most welcome for Kyrgyz exporters. Building on this trend could have positive spillover effects in other trade arrangements in the region. The international community's efforts to reduce trade restrictions in central Asia are crucial in this respect.

33. **Governance and corruption problems are the biggest risks for the medium-term success of the Kyrgyz economy.** The National Integrity Council—now led by the President and supported by strong international participation—should urgently develop concrete measures to improve governance in general and to reduce corruption in particular. A significant step was taken with the approval of the Extractive Industries Transparency Initiative. Related program measures are expected to open and properly regulate the country's key economic sector for the benefit of both domestic and foreign investors. The staff also welcomes the deepening of the banking sector reform program focusing, in particular, on improvements to the legislative framework needed to make bank supervision more effective.

34. As the authorities have successfully carried out the first half of the last annual program under the current PRGF arrangement and have presented strong program amendments for the remaining period, the staff recommends completion of the fifth review.

Table 1. Kyrgyz Republic: Third-Year Quantitative Program Targets 1/
(in millions of soms, unless otherwise indicated; eop)

	2003			2004		
	December			March		
	Program	Adjusted	Actual	Program	Adjusted	Actual
I. Performance criteria						
1. Floor on net international reserves of the NBKR in convertible currencies (eop stock, in millions of U.S. dollars)	139.3	134.1	157.2	134.6	135.6	161.0
2. Ceiling on net domestic assets of the NBKR (eop stock)	2,168	2,395	2,174	2,656	2,611	2,338
3. Ceiling on cumulative fiscal deficit of the state government	835	...	1,139	2,052	...	2,027
4. Cumulative floor on state government tax collections in cash	3,398	...	3,559	5,845	...	6,435
5. Ceiling on the stock of central government budget arrears	0	...	0	0	...	0
6. Ceiling on the stock of Social Fund pension arrears	0	...	0	0	...	0
7. Floor on payroll collections in cash of the Social Fund	910	...	958	1,755	...	1,970
8. Ceiling on the stock of Social Fund arrears to the Medical Insurance Fund	0	...	0	0	...	0
9. Ceiling on contracting or guaranteeing by the state government or NBKR of new nonconcessional external debt of less than one year (in millions of U.S. dollars)	0	...	0	0	...	0
10. Ceiling on contracting or guaranteeing by the state government or NBKR of new nonconcessional external debt with a maturity of one year or more (cumulative, in millions of U.S. dollars)	0	...	0	0	...	0
11. Ceiling on accumulation of new external payment arrears (in millions of U.S. dollars)	0	...	0	0	...	0
II. Indicative targets						
1. Ceiling on reserve money (NBKR liabilities)	9,298	...	10,075	9,566	...	10,377
2. Ceiling on the electricity sector quasi-fiscal deficit (in millions of som)	9,645	...	9,240	...	...	...

Sources: Kyrgyz authorities; and Fund staff estimates and projections.

1/ Performance criteria, benchmarks, and indicative targets are defined in the Supplementary Technical Memorandum of Understanding.

Table 2. Kyrgyz Republic: Structural Conditionality in the Third Annual Program

Structural benchmarks for end-March 2004

- Approve and publish 2005-07 Medium Term Fiscal Framework based on quantified policy plans in key line ministries (Ministries of Education, Health, and Agriculture). **Observed.**
- Adopt tax policy package as described in paragraph 21 of the Memorandum of Economic Policies (MEP). **Partially observed.**

Structural benchmarks for end-June 2004

- Complete external audit of the 2003 financial statements of KAFC as well as the assessment of its loan portfolio, both conducted by a reputable international firm.
- Develop and adopt a detailed template for disclosing and reporting to the government Kyrgyz Altyn's financial data, and submit the first semi-annual draft report to Fund staff by end-September 2004.

Structural benchmarks for end-August 2004

- Draft and submit to the Economic Policy Council small business tax reform package, as described in paragraph 21 of the SMEP.

Structural benchmarks for end-September 2004

- Submit to parliament legislative amendments to remove conflicts between banking and other legislation, as identified in Box 1, item 2.
 - Submit to parliament an amendment to the Law on Normative Legal Acts requiring that any new bill approved by parliament incorporate all amendments necessary to bring related laws into conformity with the proposed bill.
 - Complete a risk assurance and control audit with reference to the 2002 and 2003 accounts of Kyrgyz Altyn, conducted by a reputable international firm.
 - Issue regulation for reorganizing mining supervision in line with World Bank 2001 Mining Report recommendations.
-

Table 3. Kyrgyz Republic: Selected Economic Indicators, 2000-2007

	2000	2001	2002	2003		2004		2005	2006	2007
	Actual	Actual	Actual	Prog. 1/	Prel.	Prog. 1/	Rev. Prog.	Curr. Proj.	Curr. Proj.	Curr. Proj.
GDP										
Nominal GDP (in billions of soms)	65.4	73.9	75.4	82.2	83.4	88.9	91.8	100.5	110.3	121.1
Nominal GDP (in millions of U.S. dollars)	1,367	1,525	1,606	1,901	1,911	2,020	2,086	2,284	2,507	2,752
Real GDP (growth in percent)	5.3	5.4	0.0	5.2	6.7	4.1	4.5	4.6	5.3	5.2
GDP per capita (in U.S. dollars)	278	309	324	376	378	400	413	448	488	532
Employment (growth in percent)	0.2	1.1	1.1	0.5	0.9	0.4	0.4	0.4	0.4	0.4
Prices and wages										
Consumer prices (percent change, eop)	9.6	3.7	2.3	3.6	5.6	3.8	4.0	4.0	4.0	4.0
Consumer prices (percent change, avg)	18.7	6.9	2.1	2.7	3.1	3.7	4.9	4.6	4.0	4.0
Nominal exchange rate (soms per U.S. dollar, eop)	48.9	47.7	46.0	...	43.6	...	...	...	...	...
Exchange rate (soms per U.S. dollar, avg)	47.8	48.4	46.9	...	43.7	...	...	...	...	...
Average monthly wage (in U.S. dollars)	24.7	32.3	35.9	49.3	45.2	...	...	...	...	...
Terms of trade (percent change)	8.8	-2.4	0.1	1.1	2.7	-0.8	2.5	0.6	-0.8	0.4
General government finances (percent of GDP) 2/										
Total revenue and grants	18.5	20.4	22.8	21.9	22.2	22.2	22.0	22.1	22.2	22.2
Tax revenue	15.1	15.8	17.6	17.8	17.8	18.2	18.0	18.1	18.3	18.3
Total expenditure (including net lending)	28.5	25.9	28.0	26.7	27.1	26.6	26.3	26.1	25.4	25.1
o/w: Non-interest current expenditure	18.5	19.6	21.1	21.1	21.3	20.5	20.6	20.1	19.5	19.2
o/w: Public Investment Program (PIP)	6.8	4.4	4.7	3.7	3.6	3.6	3.5	3.3	3.0	3.0
Overall fiscal balance (cash basis)	-9.2	-5.1	-5.5	-4.9	-5.2	-4.4	-4.3	-4.0	-3.2	-2.9
Primary balance 3/	-6.9	-3.5	-3.9	-3.3	-3.7	-2.2	-2.4	-2.1	-1.3	-1.2
Money and credit 4/										
Reserve money (percent change, eop)	11.5	11.3	42.9	21.4	31.6	8.9	9.1	...	...	...
Broad money (percent change, eop)	12.1	11.3	35.1	22.7	34.5	15.9	9.9	...	...	...
Som broad money (percent change, eop)	11.3	17.0	34.2	24.8	33.5	15.6	13.5	...	...	...
Velocity of broad money 5/	8.9	9.4	7.0	6.2	6.0	5.8	5.7	...	...	...
Velocity of som broad money 5/	12.4	12.4	9.3	8.1	8.0	7.5	7.4	...	...	...
Money multiplier	1.53	1.53	1.44	1.44	1.45	1.53	1.46	...	...	...
External sector										
Current account balance (percent of GDP)	-6.6	-3.3	-3.9	-3.5	-2.7	-4.2	-3.9	-5.4	-4.2	-3.3
Export growth (GNFS, in U.S. dollar, percent change)	8.6	-2.1	13.5	9.4	17.2	2.3	7.5	5.8	7.5	8.3
Import growth (GNFS, in U.S. dollar, percent change)	-6.5	-13.8	23.3	9.9	16.9	5.4	10.5	8.9	4.2	5.7
Gross reserves (months of imports, eop) 6/	4.4	3.8	4.1	4.7	4.8	5.0	5.4	5.2	4.8	4.7
External public debt outstanding (percent of GDP) 7/	111.1	94.4	98.8	94.7	88.8	87.9	87.2	90.0	88.7	72.8
Debt service-to-export ratio (in percent) 8/	21.7	21.3	14.5	9.7	15.4	11.8	10.7	17.5	16.1	13.8
Debt service-to-fiscal revenue ratio (in percent) 7/	...	19.7	20.2	...	12.9	...	13.9	28.7	24.8	21.7

Sources: Kyrgyz authorities; and Fund staff estimates and projections.

1/ IMF Country Report No. 04/16.

2/ General government comprises state government and Social Fund finances. State government comprises central and local governments.

3/ Overall balance less interest payments.

4/ Projections use program exchange rate.

5/ 12 month GDP over average quarterly broad money.

6/ Gross reserves exclude international reserves of NBKR that are pledged or blocked.

7/ Excluding Kumtor gold mine.

8/ The debt service ratio falls from 2002 through 2004 because this is the consolidation period during which Paris Club flow relief applies.

Table 4. Kyrgyz Republic: Saving-Investment Balance, 2000-2007

	2000	2001	2002	2003		2004		2005		2006		2007	
	Actual	Actual	Actual	Prog. I/	Prel.	Prog. I/	Rev. Prog.	Curr. Proj.	Curr. Proj.	Curr. Proj.	Curr. Proj.	Curr. Proj.	Curr. Proj.
(In percent of GDP)													
Savings and investment balance													
Total Investment	20.0	18.0	17.6	17.2	17.6	18.0	18.0	19.3	19.3	19.4	19.6		
Government	8.1	5.3	5.9	4.6	4.8	4.4	4.2	4.6	4.6	4.6	4.5		
PIP (Public Investment Program)	6.8	4.4	4.7	3.7	3.6	3.6	3.5	3.3	3.3	3.0	3.0		
Capital investment (budget)	1.4	0.9	1.2	0.9	1.2	0.8	0.7	1.3	1.3	1.6	1.5		
Non-government	11.9	12.7	11.7	12.7	12.8	13.6	13.8	14.7	14.7	14.8	15.1		
Total domestic savings	13.4	14.7	13.7	13.7	14.9	13.8	14.1	13.9	13.9	15.2	16.3		
Government	-2.1	-0.6	0.2	-0.9	-0.8	-0.6	-0.7	0.1	0.1	0.8	1.3		
Non-government	15.5	15.2	13.6	14.6	15.7	14.4	14.8	13.8	13.8	14.4	15.0		
Foreign savings	6.6	3.3	3.9	3.5	2.7	4.2	3.9	5.4	5.4	4.2	3.3		

Sources: Kyrgyz authorities; and Fund staff estimates and projections.

Table 5. Kyrgyz Republic: General Government Finances, 2001-2007

	2001		2002		2003		2004				2005				2006		2007	
	Act.	Act.	Act.	Act.	2003		2004		2004		2004		2005		2006	2007	2006	2007
					Annual	Annual	1Q	2Q	3Q	4Q	Annual	Annual	1Q	2Q					3Q	4Q
Total revenue and grants	15,051	17,158	18,004	3,698	4,712	5,393	5,927	19,731	18,489	4,613	4,629	5,041	5,887	20,170	22,157	24,433	26,875	
Of which: tax revenue 1/	11,696	13,231	14,660	3,118	3,812	4,334	4,920	16,184	14,886	3,714	3,769	4,190	4,870	16,542	18,155	20,161	22,211	
Total expenditure	19,630	21,579	22,434	5,108	5,911	6,475	6,631	24,125	23,038	5,577	6,011	6,156	6,820	24,564	26,668	28,623	30,751	
Current expenditure	15,715	17,107	18,686	4,494	4,960	5,326	5,472	20,252	19,039	4,861	5,009	4,930	5,891	20,691	22,047	23,551	25,300	
Capital expenditure (including PIP)	3,915	4,472	3,749	614	951	1,149	1,159	3,873	4,020	717	1,002	1,226	929	3,873	4,621	5,072	5,451	
Net lending	-509	-443	-452	-95	-94	-89	-169	-446	-414	-71	-114	-129	-133	-446	-492	-662	-363	
Accrual surplus (+) / deficit (-)	-4,069	-3,978	-3,979	-1,315	-1,106	-993	-535	-3,948	-4,156	-894	-1,269	-986	-800	-3,949	-4,018	-3,528	-3,513	
Cash surplus (+) / deficit (-)	-3,795	-4,150	-4,068	-1,315	-1,106	-993	-535	-3,948	-4,347	-888	-1,269	-986	-800	-3,943	-4,018	-3,528	-3,513	
Total financing	3,795	4,150	4,068	1,315	1,106	993	535	3,948	4,347	888	1,269	986	800	3,943	4,018	3,528	3,513	
External financing	4,208	3,933	4,102	506	2,069	1,021	1,078	4,674	3,950	629	1,387	1,064	1,568	4,648	3,060	1,490	1,592	
Domestic financing	-834	33	-437	686	-1,028	19	-579	-903	115	189	-2,815	-124	-864	-3,614	-2,146	-1,077	-917	
Change in Social Fund cash balance	121	54	0	98	40	-72	-66	0	-24	0	32	22	-150	-96	0	0	0	
Exceptional Financing 3/	299	130	402	25	25	25	102	177	307	70	2,665	25	245	3,005	340	130	130	
Financing Gap	0	0	0	0	0	0	0	0	0	0	0	0	0	0	2,764	2,985	2,708	
	(In percent of GDP)																	
Total revenue and grants	20.4	22.8	21.9	4.2	5.3	6.1	6.7	22.2	22.2	5.0	5.0	5.5	6.4	22.0	22.1	22.2	22.2	
Total revenue	19.5	21.7	21.3	4.2	5.1	5.8	6.4	21.5	21.7	4.8	5.0	5.4	6.2	21.4	21.5	21.8	21.8	
Of which: tax revenue 1/	15.8	17.6	17.8	3.5	4.3	4.9	5.5	18.2	17.8	4.0	4.1	4.6	5.3	18.0	18.1	18.3	18.3	
Grants	0.8	1.1	0.6	0.0	0.2	0.2	0.2	0.7	0.4	0.2	0.0	0.1	0.2	0.6	0.5	0.4	0.4	
Total expenditure	26.6	28.6	27.3	5.7	6.7	7.3	7.5	27.8	27.6	6.1	6.6	7.4	7.4	26.8	26.5	26.0	25.4	
Current expenditure	21.3	22.7	22.7	5.1	5.6	6.0	6.2	22.8	22.8	5.3	5.5	5.4	6.4	22.6	21.9	21.4	20.9	
Wage	4.8	5.5	6.2	1.3	1.5	1.8	1.7	6.3	5.7	1.0	1.5	1.8	1.8	6.0	6.0	5.8	5.7	
Transfers and subsidies 2/	3.0	3.4	2.7	0.8	0.6	0.7	0.7	2.8	3.2	0.5	0.6	0.7	1.0	2.7	2.8	2.8	2.8	
Social Fund expenditures	5.3	5.9	5.9	1.4	1.5	1.5	1.5	5.9	5.8	1.4	1.4	1.4	1.4	1.5	1.5	1.5	1.5	
Interest	1.7	1.6	1.7	0.3	0.3	0.3	0.3	1.5	1.5	0.1	0.1	0.1	0.1	0.2	0.2	0.2	0.2	
Purchases of other goods and services	6.5	6.3	6.3	1.3	1.0	1.8	1.5	5.5	6.6	2.3	1.1	1.3	1.5	6.2	5.8	5.5	5.6	
Capital expenditure (including PIP)	5.3	5.9	4.6	0.7	1.1	1.3	1.3	4.4	4.8	0.8	1.1	1.3	1.0	4.2	4.6	4.6	4.5	
Financial balance	-6.2	-5.9	-5.4	-1.6	-1.3	-1.2	-0.8	-4.9	-5.5	-1.1	-1.5	-1.2	-1.0	-4.8	-4.5	-3.8	-3.2	
Net lending	-0.7	-0.6	-0.5	-0.1	-0.1	-0.1	-0.2	-0.5	-0.5	-0.1	-0.1	-0.1	-0.1	-0.5	-0.5	-0.6	-0.3	
Accrual surplus (+) / deficit (-)	-5.5	-5.3	-4.8	-1.5	-1.2	-1.1	-0.6	-4.4	-5.0	-1.0	-1.4	-1.1	-0.9	-4.3	-4.0	-3.2	-2.9	
Cash surplus (+) / deficit (-)	-5.1	-5.5	-4.9	-1.5	-1.2	-1.1	-0.6	-4.4	-5.2	-1.0	-1.4	-1.1	-0.9	-4.3	-4.0	-3.2	-2.9	
Total financing	5.1	5.5	4.9	1.5	1.2	1.1	0.6	4.4	5.2	1.0	1.4	1.1	0.9	4.3	4.2	0.5	0.7	
External financing	5.7	5.2	5.0	0.6	2.3	1.1	1.2	5.3	4.7	0.7	1.5	1.2	1.7	5.1	3.0	1.4	1.3	
Domestic financing	-1.1	0.0	-0.5	0.8	-1.2	0.0	-0.7	-1.0	0.1	-0.1	-3.1	-0.1	-0.9	-3.9	-2.1	-1.0	-0.8	
Change in Social Fund cash balance	0.2	0.1	0.0	0.1	0.0	-0.1	-0.1	0.0	0.0	0.0	0.0	0.0	-0.2	-0.1	0.0	0.0	0.0	
Exceptional Financing 3/	0.4	0.2	0.5	0.0	0.0	0.0	0.1	0.2	0.4	0.1	2.9	0.0	0.3	3.3	0.3	0.1	0.1	
Financing Gap	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	2.8	2.7	2.2	
Memorandum items:																		
Social spending	12.1	14.1	13.8	...	...	...	...	13.9	14.0	3.3	3.4	3.4	4.0	14.1	14.4	14.6	14.8
External public debt	112.0	108.6	100.6	...	...	...	...	91.4	94.1	...	...	...	...	89.8	90.6	88.8	72.5
NPV of external public debt	77.3	81.6	71.5	...	...	...	...	62.6	67.8	...	...	...	...	54.5	51.5	47.3	43.9
Primary balance	-3.5	-3.9	-3.3	-1.2	-0.3	-0.9	0.2	-2.2	-3.7	-0.5	-0.5	-0.9	-0.2	-2.4	-2.1	-1.3	-1.2	
Primary balance excluding grant	-4.3	-5.0	-3.9	-1.2	-0.5	-1.1	0.0	-2.9	-4.1	-1.1	-0.8	-0.4	-0.4	-2.9	-2.6	-1.7	-1.6	
Underlying fiscal balance 4/	-0.8	-1.3	-1.1	...	...	...	...	0.3	-1.6	-0.6	0.2	-0.1	0.1	-0.4	-0.1	0.8	0.7
Domestic balance 5/	-0.4	-0.5	-0.1	-0.8	0.2	0.1	1.1	0.6	-0.5	-0.2	0.1	0.2	0.4	0.5	0.7	1.3	1.4	

Sources: Kyrgyz authorities; and Fund staff estimates and projections.

1/ Includes payroll tax revenue (contribution to the Social Fund), net of the government contribution to the Social Fund.

2/ Excludes transfer to Social Fund.

3/ Mainly privatization proceeds. For revised 2004 projection, includes som 2,640 million related to the Kumtor mine restructuring.

4/ Primary balance excluding gold projects, grant and foreign financed PIP.

5/ Overall balance (in cash) excluding foreign financed PIP and foreign interest payments.

Table 7. Kyrgyz Republic: State Government Finances, 2001-2007

	2001		2002		2003		2004				2005				2006		2007	
	Act.		Act.		Annual		2Q		3Q		4Q		Annual		Annual		Annual	
					Act.		Fourth review		2004		2004		2005		2005		2007	
Total revenue and grants	17.0	19.1	18.4	3.4	4.5	5.2	5.7	18.8	18.6	4.1	4.3	4.7	5.4	18.5	18.8	19.0	19.2	
Total revenue	16.1	18.0	17.8	3.4	4.3	4.9	5.5	18.1	18.2	3.9	4.3	4.6	5.2	18.0	18.2	18.6	18.8	
Current expenditure	16.1	17.8	17.7	3.4	4.3	4.9	5.4	18.0	18.0	3.9	4.3	4.6	5.1	17.9	18.1	18.5	18.7	
Tax revenue	12.4	13.9	14.3	2.8	3.5	4.0	4.6	14.8	14.3	3.1	3.4	3.8	4.3	14.6	14.8	15.1	15.4	
Income tax	2.7	2.9	2.7	0.8	0.7	0.7	0.7	2.8	2.9	0.7	0.6	0.6	0.7	2.7	2.9	2.9	3.1	
VAT	5.7	6.4	6.5	1.1	1.7	1.8	2.2	6.8	6.6	1.4	1.6	1.8	2.0	6.9	6.9	7.2	7.2	
Excises	1.5	1.4	1.5	0.3	0.4	0.4	0.5	1.6	1.4	0.3	0.4	0.4	0.4	1.5	1.4	1.4	1.5	
Customs	0.4	0.6	0.5	0.1	0.1	0.2	0.2	0.6	0.5	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	
Land tax 1/	0.3	0.4	0.4	0.0	0.0	0.2	0.2	0.4	0.4	0.1	0.1	0.1	0.2	0.4	0.4	0.4	0.3	
Road tax and Emergency Fund	1.3	1.4	1.5	0.3	0.4	0.4	0.4	1.5	1.4	0.3	0.4	0.4	0.4	1.5	1.5	1.5	1.5	
Retail sales tax 1/	0.4	0.5	0.6	0.1	0.1	0.2	0.2	0.6	0.6	0.1	0.2	0.2	0.2	0.6	0.6	0.6	0.6	
Other 1/	0.1	0.3	0.6	0.1	0.1	0.1	0.2	0.5	0.6	0.2	0.1	0.1	0.2	0.6	0.6	0.6	0.7	
Nontax revenue	3.6	3.9	3.4	0.6	0.8	0.9	0.9	3.2	3.7	0.7	0.9	0.8	0.8	3.3	3.4	3.4	3.4	
Capital revenue	0.1	0.2	0.0	0.0	0.0	0.0	0.1	0.1	0.2	0.0	0.0	0.0	0.0	0.1	0.1	0.1	0.1	
Grants	0.8	1.1	0.6	0.0	0.2	0.2	0.2	0.7	0.4	0.2	0.0	0.1	0.2	0.6	0.5	0.4	0.4	
Total expenditure	22.8	24.8	23.8	4.9	5.8	6.5	6.6	23.8	24.3	5.2	5.8	5.9	6.6	23.4	23.2	22.8	22.4	
Current expenditure	17.5	18.9	19.3	4.2	4.8	5.2	5.3	19.4	19.4	4.4	4.7	4.6	5.6	19.2	18.6	18.2	17.9	
Wages and Social Fund contributions	5.8	6.5	7.3	1.6	1.8	2.2	2.0	7.5	6.8	1.1	1.8	2.2	2.2	7.2	7.0	6.9	6.8	
Transfers and subsidies 2/	3.0	3.4	2.7	0.8	0.6	0.7	0.7	2.8	3.2	0.5	0.6	0.7	1.0	2.7	2.8	2.8	2.8	
Transfers to Social Fund	0.5	1.1	1.4	0.3	0.3	0.3	0.3	1.3	1.3	0.3	0.3	0.3	0.3	1.2	1.1	1.1	1.1	
Interest	1.7	1.6	1.7	0.3	1.0	0.2	0.8	2.3	1.5	0.1	0.9	0.2	0.7	1.9	1.9	1.9	1.7	
Purchases of other goods and services	6.5	6.3	6.3	1.3	1.0	1.8	1.5	5.5	6.6	2.3	1.1	1.3	1.5	6.2	5.8	5.5	5.6	
Capital expenditure (including PIP)	5.3	5.9	4.6	0.7	1.1	1.3	1.3	4.4	4.8	0.8	1.1	1.3	1.0	4.2	4.6	4.6	4.5	
Domestically financed capital expenditure	0.9	1.2	0.9	0.1	0.2	0.2	0.2	0.7	1.2	0.1	0.2	0.2	0.2	0.7	1.3	1.6	1.5	
Foreign financed PIP	4.4	4.7	3.7	0.5	0.9	1.1	1.1	3.6	3.6	0.7	0.9	1.1	0.8	3.5	3.3	3.0	3.0	
Financial balance	-5.9	-5.7	-5.5	-1.5	-1.3	-1.3	-0.9	-4.9	-5.7	-1.1	-1.5	-1.2	-1.2	-4.9	-4.5	-3.8	-3.2	
Net lending	-0.7	-0.6	-0.5	-0.1	-0.1	-0.1	-0.2	-0.5	-0.5	-0.1	-0.1	-0.1	-0.1	-0.5	-0.5	-0.6	-0.3	
Accrual surplus (+) / deficit (-)	-5.2	-5.1	-4.9	-1.4	-1.2	-1.2	-0.7	-4.4	-5.2	-1.0	-1.3	-1.1	-1.0	-4.4	-4.0	-3.2	-2.9	
Cash surplus (+) / deficit (-)	-5.0	-5.4	-4.9	-1.4	-1.2	-1.2	-0.7	-4.4	-5.2	-1.0	-1.3	-1.1	-1.0	-4.4	-4.0	-3.2	-2.9	
Total financing	5.0	5.4	4.9	1.4	1.2	1.2	0.7	4.4	5.2	1.0	1.3	1.1	1.0	4.4	4.2	0.5	0.7	
External financing	5.7	5.2	5.0	0.6	2.3	1.1	1.2	5.3	4.7	0.7	1.5	1.2	1.7	5.1	3.0	1.4	1.3	
Public investment program (PIP)	4.4	4.8	3.8	0.5	0.9	1.1	1.1	3.6	3.5	0.7	0.9	1.1	0.8	3.5	3.3	3.0	3.0	
Disbursements (BOP support)	2.7	0.5	0.3	0.0	1.2	0.0	0.0	1.2	0.3	0.0	0.4	0.0	0.8	1.2	1.3	0.0	0.0	
Total amortization	-2.5	-1.2	-1.8	-0.2	-0.6	-0.2	-0.7	-1.8	-1.7	-0.2	-0.6	-0.2	-0.7	-1.8	-1.6	-1.6	-1.7	
Arrears and rescheduling	1.1	1.1	2.3	0.3	0.8	0.3	0.9	2.2	2.2	0.9	0.3	0.8	0.8	2.2	2.2	0.0	0.0	
Domestic financing	-1.1	0.0	-0.5	0.8	-1.2	0.0	-0.7	-1.0	0.1	0.2	-3.1	-0.1	-0.9	-3.9	-2.1	-1.0	-0.8	
Exceptional financing 3/	0.4	0.2	0.5	0.0	0.0	0.0	0.1	0.2	0.4	0.1	2.9	0.0	0.3	3.3	0.3	0.1	0.1	
Financing Gap	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	2.8	2.7	2.2	

Sources: Kyrgyz authorities, and Fund staff estimates and projections.

1/ In the original program, other tax includes land tax and retail sales tax.

2/ Excludes transfer to Social Fund (columns for original program include transfer to Social Fund).

3/ Mainly privatization proceeds. For revised 2004 projection, includes som 2640 million related to the Kumtor mine restructuring.

(In percent of GDP)

Table 9. Kyrgyz Republic: Medium-Term Expenditure Framework for General Government
by Functional Classification, 2000-2007
(In percent of GDP)

	2000	2001	2002	2003	2004	2005	2006	2007
	Act.	Act.	Act.	Est.	Proj.	Proj.	Proj.	Proj.
Total expenditure 1/	29.9	25.9	28.1	27.1	26.3	26.1	25.4	25.1
I. General public services	3.0	2.6	2.8	2.4	2.2	2.1	2.0	1.9
II. Defense	1.9	1.3	1.4	1.3	1.2	1.1	1.0	1.0
III. Public order and safety affairs	1.1	1.0	1.3	1.1	1.0	1.0	0.9	0.9
Social spending	12.2	12.1	14.1	14.0	14.1	14.4	14.6	14.8
IV. Education	3.5	3.6	4.2	4.2	4.2	4.4	4.6	4.8
V. Health	2.1	1.8	2.0	2.0	2.1	2.2	2.3	2.4
VI. Social security and welfare affairs 2/	1.9	2.0	2.5	2.4	2.5	2.7	2.7	2.8
VII. Pension Fund 3/	4.8	4.8	5.4	5.4	5.3	5.2	5.0	4.8
VIII. Housing and community services	1.1	1.1	1.5	1.3	1.2	1.2	1.1	1.0
IX. Recreational, cultural and religious activities	0.5	0.4	0.5	0.4	0.4	0.4	0.3	0.3
X. Energy complex (electricity production)	0.4	0.5	0.5	0.5	0.4	0.4	0.4	0.4
XI. Agriculture, water resources, forestry	3.2	2.3	2.6	2.3	2.1	2.0	1.8	1.8
XII. Mining and mineral resources	0.2	0.2	0.3	0.3	0.3	0.2	0.2	0.2
XIII. Transportation and communication	3.1	2.0	2.5	2.1	2.0	1.9	1.8	1.7
XIV. Other economic affairs and services	1.3	0.8	0.9	0.8	0.7	0.7	0.6	0.6
XV. Other	1.4	1.3	0.8	0.7	0.7	0.6	0.6	0.6
XVI. Unidentified expenditure	0.5	0.3	-1.1	0.0	0.0	0.0	0.0	0.0

Sources: Kyrgyz authorities; and Fund staff estimates and projections.

1/ Including PIP and net lending.

2/ Excluding net transfer to Pension Fund.

3/ Social Fund operation net of transfers to other funds.

Table 10. Kyrgyz Republic: NBKR Accounts, 2002-04
(In millions of soms, end-period stocks) 1/

	2002		2003		2004		Dec. New Proj.	Dec. Prog.	Dec. New Proj.	
	Dec. Act.	Dec. Act.	Mar. Prog.	Mar. Act.	Jun. Prog.	Jun. New Proj.				Sep. Prog.	Sep. New Proj.
Net foreign assets	5,725	8,090	7,114	8,239	8,186	10,871 6/	8,325	10,894	8,627	11,712
Net international reserves	4,480	6,917	5,924	7,083	7,012	9,730 6/	7,151	9,753	7,453	10,571
Other foreign assets	1,297	1,224	1,241	1,208	1,225	1,192	1,225	1,192	1,225	1,192
Balance with CIS countries	-51	-51	-51	-51	-51	-51	-51	-51	-51	-51
Long-term foreign liabilities	-2,475	-2,441	-2,474	-2,480	-2,452	-2,458	-2,452	-2,458	-2,430	-2,382
Net domestic assets	4,407	4,427	4,925	4,618	4,096	2,277 6/	4,195	2,433	3,930	1,664
Domestic credit (net)	5,530	5,318	5,551	5,268	4,613	2,886 6/	4,682	3,067	4,393	2,328
Claims on government (net), o/w:	5,058	5,046	5,324	5,192	4,296	2,323 6/	4,315	2,199	3,736	1,280
Loan to government in forex (Turkish loan)	1,917	1,956	1,956	1,996	1,956	1,996	1,956	1,996	1,956	1,941
Total government deposits	-1,928	-1,564	-1,281	-1,444	-2,309	-4,259 6/	-2,290	-4,383	-2,869	-5,247
Treasury bills	4,219	4,303	4,298	4,290	4,098	4,036	4,098	4,036	4,098	4,036
Repos	850	350	350	350	350	550	550	550	550	550
Claims on commercial banks	0	-147	-200	-331	-100	155	-50	460	250	640
Other items net 3/	472	419	427	408	417	408	417	408	407	408
Reserve money	-1,123	-891	-626	-650	-517	-609	-487	-634	-463	-664
Currency outside commercial banks	7,658	10,075	9,566	10,377	9,831	10,689	10,069	10,868	10,128	10,993
Deposits of commercial banks in forex	6,874	9,317	...	9,640	...	...	...	...	...	...
Currency holdings of commercial banks	184	306	...	259	...	...	...	...	...	...
Reserves of commercial banks	601	452	...	478	...	...	...	...	...	...
<i>Memorandum items:</i>										
Reserve money growth (12 month)	42.9	31.6	21.5	31.8	16.6	26.8	16.1	25.3	8.9	9.1
Reserve money growth (quarterly, annualized)	...	82.2	12.0	12.5	11.5	12.6	10.0	6.9	2.4	4.7
Gross reserves (in millions of U.S. dollars)	289.7	359.2	318.2	371.2	347.6	437.0 6/	342.9	430.0	354.4	440.0
in months of imports	4.3	4.8	4.5	4.5	4.9	5.3 6/	4.8	5.3	5.0	5.4
Net international reserves (in millions of U.S. dollars) 4/	101.8	157.2	134.6	161.0	159.4	221.1 6/	162.5	221.7	169.4	240.2
change over previous period (in millions of U.S. dollars)	...	27.5	-4.6	3.8	24.7	60.2 6/	3.2	0.5	6.9	18.6
Net domestic assets 4/ 5/	2,143	2,174	2,656	2,338	1,827	-4.6 6/	1,926	152	1,671	-562

Source: National Bank of the Kyrgyz Republic; and Fund staff estimates and projections.

1/ Programmed and actual foreign exchange assets and liabilities are valued at the exchange rate of 44 soms per U.S. dollar, 1.4318 U.S. dollar per SDR and a gold price of U.S. dollar 384.6 per Troy ounce.
2/ As of December 2002, includes government securities issued to replace restructured bonds, as well as those issued for revaluation losses, lost capital in the Central Asia Development Bank, and capitalized past interest arrears on bonds.

3/ As of December 2002, includes revaluation losses, lost capital in the Central Asia Development Bank, and capitalized past interest arrears on bonds.

4/ Non-adjusted.

5/ Excludes counterpart of the loan by the Eximbank of Turkey and the EBRD/IDA enterprise loan which are channeled through the NBKR.

6/ Includes privatization proceeds from the restructuring of the ownership of the Kumtor gold mine.

Table 11. Kyrgyz Republic: Monetary Survey, 2002-04
(In millions of soms, end-period stocks) 1/

	2002		2003		2004		Dec. New Proj.	Dec. Prog.	Dec. New Proj.	
	Dec. Act.	Dec. Act.	Mar. Prog.	Mar. Act.	Jun. Prog.	Jun. New Proj.				Sep. Prog.	Sep. New Proj.
Net foreign assets	7,343	10,374	9,371	10,753	10,566	13,508	10,921	13,702	11,205	14,502
NBKR	5,741	8,090	7,114	8,239	8,186	10,871	8,325	10,894	8,627	11,712
Commercial banks	1,602	2,284	2,257	2,514	2,380	2,637	2,596	2,808	2,578	2,791
Long-term NBKR foreign liabilities	-2,475	-2,441	-2,474	-2,480	-2,452	-2,458	-2,452	-2,458	-2,430	-2,382
Net domestic assets	6,019	6,712	6,908	6,830	6,191	4,476	6,538	4,664	6,704	3,976
Claims on government (net), o/w:	5,556	5,604	5,885	5,819	4,857	2,982	4,876	2,880	4,297	1,812
Credit from the NBKR	5,063	5,046	5,324	5,192	4,296	2,323	4,315	2,199	3,736	1,280
Credit from commercial banks	493	558	561	627	561	659	561	681	561	531
Treasury bonds	126	134	162	118	162	118	162	118	162	118
Treasury bills	438	515	469	646	469	646	469	646	469	646
Other	-71	-91	-70	-137	-70	-105	-70	-83	-70	-233
Credit to the rest of the economy, o/w:	2,999	3,898	3,581	4,147	3,782	4,589	4,080	4,904	4,802	5,315
in forex	2,039	2,670	...	2,711	...	...	...	...	...	...
Other items net	-2,535	-2,790	-2,558	-3,136	-2,449	-3,095	-2,419	-3,120	-2,395	-3,151
Broad money	10,887	14,644	13,806	15,102	14,305	15,526	15,007	15,908	15,480	16,096
Currency outside banks	6,873	9,315	8,962	9,637	9,277	9,818	9,723	10,038	10,010	10,135
Deposits, o/w:	4,014	5,329	4,844	5,465	5,028	5,708	5,284	5,870	5,470	5,962
in forex	2,583	3,558	3,100	3,535	3,218	3,596	3,382	3,581	3,501	3,517
Broad money: som component	8,304	11,086	10,706	11,568	11,087	11,930	11,625	12,327	11,979	12,579
<i>Memorandum items:</i>										
Velocity (quarterly) 2/	7.0	6.0	6.0	5.7	6.0	5.6	6.0	5.7	5.8	5.7
Som velocity (quarterly) 2/	9.3	8.0	7.8	7.5	7.7	7.4	7.7	7.4	7.5	7.4
Broad money growth (12 months)	35.1	34.5	21.2	32.6	18.6	28.7	15.7	22.7	15.9	9.9
Som broad money growth (12 months)	34.2	33.5	22.2	32.1	18.5	27.5	19.7	26.9	15.6	13.5
Multiplier	1.44	1.45	1.44	1.46	1.46	1.45	1.49	1.46	1.53	1.46
Credit to the rest of the economy (in percent of GDP)	4.0	4.7	...	...	...	...	...	...	...	5.8

Source: National Bank of the Kyrgyz Republic; and Fund staff estimates and projections.

1/ Programmed and actual foreign exchange assets and liabilities are valued at the exchange rate of 44 soms per U.S. dollar, 1,4318 U.S. dollar per SDR and a gold price of U.S. dollar 384.6 per Troy ounce.
2/ 12 month GDP over average quarterly broad money.

Table 12. Kyrgyz Republic: Quarterly Balance of Payments: 2002 - 2004
(in millions of USD)

	2002	2003						2004				
	Year Est.	Q1 Act.	Q2 Act.	Q3 Prel.	Q4 Prel.	Year Prog.	Year Prel.	Q1 Prog.	Q2 Prog.	Q3 Prog.	Q4 Prog.	Year Prog.
Current account balance	-62	12	-52	-24	12	-66	-52	-20	-11	-22	-27	-80
(excluding official transfers)	-121	-1	-61	-38	2	-119	-97	-33	-22	-31	-41	-128
Trade balance	-54	3	-41	-40	-6	-51	-83	-25	-13	-28	-54	-120
Exports, fob 1/	498	121	115	142	212	545	590	158	159	148	164	629
CIS countries	170	40	39	49	75	182	202	55	51	59	62	227
Energy	28	3	3	12	8	28	26	2	6	18	5	30
Other	142	37	36	37	67	154	176	53	46	42	57	197
Non-CIS	328	81	77	94	136	363	388	103	107	88	102	402
Gold	163	54	46	68	92	235	260	67	75	57	59	258
Imports, fob	552	118	156	182	217	596	673	184	172	175	218	749
CIS countries	312	64	92	111	128	345	394	115	93	93	126	426
Energy	145	30	38	43	60	148	171	58	35	35	67	195
Other	166	34	54	67	68	197	223	57	58	58	59	231
Non-CIS	240	54	65	71	89	251	279	69	79	83	92	323
Services (net)	-67	-8	-18	4	-9	-65	-32	-13	-14	-8	4	-30
Non-interest service	-7	-1	-2	10	7	-19	13	-1	1	1	21	21
Interest payments (scheduled)	-32	-2	-10	-3	-11	-28	-27	-7	-12	-4	-14	-37
o/w moratorium interest	-2	0	0	0	-1	-2	-2	0	-2	0	-4	-6
Other net income	-27	-4	-6	-3	-4	-18	-18	-5	-3	-5	-3	-14
Transfers (net)	58	16	8	12	27	50	62	18	16	13	23	70
Official	59	12	9	14	11	53	45	13	10	10	14	48
Private	0	4	-1	-2	17	-3	17	5	5	4	8	22
Capital account balance	75	3	1	12	-18	27	-1	20	46	17	11	93
Commercial banks	-10	-5	-2	-14	8	-8	-14	-4	-3	-4	0	-10
Medium-and long-term loans, net	22	9	1	15	-56	19	-31	-9	2	19	-3	10
Disbursement	80	16	14	21	21	73	71	14	19	25	16	74
CIS	0	0	0	0	0	0	0	0	0	0	0	0
Non-CIS	80	16	14	21	21	73	71	14	19	25	16	74
Of which PIP	74	16	14	15	21	67	66	14	18	25	16	73
Amortization (scheduled)	-58	-7	-13	-5	-77	-53	-102	-22	-17	-6	-19	-64
Of which Kumtor	-18	0	0	0	-60	-12	-60	-17	0	0	0	-17
Foreign direct investment	5	4	1	2	14	-7	17	14	60	7	-10	72
Other assets (including acc. pay. & receiv.)	57	-5	1	9	21	22	27	18	-14	-6	24	22
Errors and omissions & short term capital	9	-18	42	18	16	28	59	0	0	0	0	0
Overall balance	22	-3	-8	7	11	-12	6	-1	35	-5	-16	13
Financing	-22	3	8	-7	-11	12	-6	1	-35	5	16	-13
NIR	-63	-4	-6	-17	-28	-36	-54	-4	-60	-1	-19	-83
Gross official reserves (- increase) 2/	-57	-11	3	-26	-19	-36	-53	-13	-65	8	-9	-80
IMF (net)	-6	7	-9	10	-9	0	-1	9	5	-8	-9	-4
Purchases and disbursements	15	16	0	13	0	29	29	14	14	0	0	29
Repurchases and repayments	-21	-9	-9	-4	-9	-29	-30	-5	-9	-8	-9	-32
Release of pledged reserves 3/	13	0	0	0	0	0	0	0	0	0	0	0
Exceptional Financing (including arrears)	21	7	14	5	17	43	43	5	18	6	17	46
Accumulation of arrears (net)	1	0	0	0	0	-1	0	0	0	0	0	0
Debt rescheduling	19	7	14	5	17	44	43	5	18	6	17	46
on arrears	0	0	0	0	0	0	0	0	0	0	0	0
on principal	5	6	9	4	11	29	30	4	11	4	11	30
on interest	13	1	5	1	5	14	12	1	5	1	4	11
on moratorium interest	1	0	0	0	1	1	1	0	1	0	3	4
BOP support (ADB)	8	0	0	0	0	0	0	0	8	0	18	25
BOP support (WB)	0	0	0	5	0	5	5	0	0	0	0	0
Financing gap (-) (after fiscal measures)	0	0	0	0	0	0	0	0	0	0	0	0
Memorandum Items												
Gross reserves in months of imports	4.3	4.0	4.0	4.4	4.8	4.7	4.8	4.5	5.3	5.2	5.4	5.4

Sources: Kyrgyz authorities; and Fund staff estimates and projections.

1/ Gold exports to the CIS and energy exports outside the CIS are negligible.

2/ Valued at end-year exchange rates.

3/ Paris Club savings.

Table 13. Kyrgyz Republic: Medium-Term Balance of Payments, 2000-2010
(In millions of U.S. dollars)

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
	Actual	Actual	Actual	Est.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
Current account balance 1/	-91	-51	-62	-52	-80	-124	-105	-90	-134	-156	-173
Trade balance	4	40	-54	-83	-120	-162	-156	-149	-207	-243	-279
Exports, fob	511	480	498	590	629	660	708	764	765	788	817
CIS countries	214	172	170	202	227	263	282	309	339	371	406
of which : Energy	82	52	28	26	30	46	48	53	55	55	58
Other countries	297	308	328	388	402	397	426	456	427	417	411
Of which : Gold	195	225	163	260	258	231	241	252	188	143	106
Imports, fob	507	440	552	673	749	822	864	913	972	1032	1096
CIS countries	280	250	311	394	426	464	495	528	565	605	648
Other countries	227	190	240	279	323	358	370	385	407	427	448
Services (net)	-171	-110	-67	-32	-30	-33	-9	2	14	29	45
Non-interest service	-87	-45	-7	13	21	20	46	55	65	79	94
Receipts	62	81	138	156	173	188	204	223	243	266	293
Payments	-149	-125	-145	-142	-152	-159	-158	-168	-177	-188	-199
Interest payments (scheduled)	-51	-39	-32	-27	-37	-53	-48	-46	-45	-44	-43
o/w moratorium interest	0	0	-2	-2	-6	-7	-7	-7	-7	-7	-7
Other net income	-33	-26	-27	-18	-14	-9	-8	-8	-6	-6	-6
Transfers (net)	76	19	58	62	70	72	61	57	59	59	61
Official	14	-15	0	17	48	48	33	29	29	29	24
Private											
Capital account balance	64	-10	75	-14	93	46	49	61	84	123	165
Medium- and long-term loans, net	41	-24	22	-10	10	16	-7	18	20	24	39
Disbursement -Projects	131	74	80	71	74	81	78	85	96	108	117
Amortization (scheduled)	-91	-97	-58	-102	-64	-65	-72	-67	-76	-85	-78
Foreign direct investment	-7	1	5	17	22	23	34	36	58	92	119
Other assets (including accounts payable and receivable)	32	28	57	27	22	16	16	13	11	11	11
Errors and omissions and short term capital	10	19	9	59	0	0	0	0	0	0	0
Overall balance	-16	-42	22	6	13	-78	-56	-29	-50	-33	-8
Financing	16	42	-22	-6	-13	20	-3	-29	-17	-24	-33
Net international reserves (- increase)	-14	-18	-67	-54	-83	-21	-16	-39	-17	-24	-33
IMF	-7	-9	-57	-53	-84	-16	-28	-24	-20	-20	-22
Purchases and disbursements	19	15	15	29	29	14	0	0	0	0	0
Repayments and repayments	-11	-17	0	-30	-32	-31	-28	-24	-20	-20	-22
Release of pledged reserves 2/	0	0	13	0	0	0	0	0	0	0	0
Exceptional Financing (including arrears)	30	19	21	43	46	0	0	0	0	0	0
Accumulation of Arrears (net)	1	-15	1	0	0	0	0	0	0	0	0
Debt rescheduling	0	34	19	43	46	0	0	0	0	0	0
on principal	0	0	0	0	0	0	0	0	0	0	0
on interest	0	16	5	30	30	0	0	0	0	0	0
on moratorium interest	0	18	13	12	11	0	0	0	0	0	0
BOP support loans (ADIB) 3/	0	0	1	1	4	0	0	0	0	0	0
BOP support loans (WB) 3/	0	33	8	0	25	10	15	10	0	0	0
Financing gap (-)	0	8	0	5	0	31	15	10	0	0	0
Memorandum items:											
GDP (in millions of U.S. dollars)	1368	1527	1606	1909	2085	2283	2506	2753	3067	3343	3671
Current account balance (in percent of GDP)	-6.6	-3.3	-3.9	-2.7	-3.9	-5.4	-4.2	-3.3	-4.4	-4.7	-4.7
Growth of exports of goods and services (volume, percent)	7.7	-1.4	9.7	6.8	3.0	3.8	6.4	6.1	0.4	3.0	3.5
Growth of imports of goods and services (volume, percent)	-14.8	-13.6	19.3	11.7	8.5	7.6	2.3	4.1	4.5	4.0	4.1
External Public Debt (US\$ million) 4/	1,779	1,710	1,745	1,792	1,868	2,070	2,229	2,004	2,066	2,131	2,205
as percent of GDP	130.0	112.0	108.6	93.9	89.6	90.7	88.9	72.8	67.4	63.7	60.1
External Public Debt (NPV Terms) 4/	1,119	1,181	1,310	1,289	1,132	1,174	1,186	1,213	1,233	1,257	1,287
as percent of GDP	81.8	77.3	81.6	67.5	54.3	51.4	47.3	44.0	40.2	37.6	35.1
External Public Debt/Exports (NPV Terms, percent) 4/	198	213	222	199	155	147	139	132	127	124	122
Gross reserves 5/	205	230	290	359	439	443	449	449	445	450	462
In months of subsequent year's imports	4.4	4.0	5.4	4.8	5.2	5.2	4.8	4.7	4.4	4.2	4.2
Financing gap as percentage of GDP	0.0	0.0	0.0	0.0	0.0	-2.5	-2.4	-2.1	-2.2	-1.7	-1.1

Sources: Kyrgyz authorities and Fund staff estimates and projections.

1/ Including transfers.

2/ Paris Club.

3/ BOP support loans for 2000 are shown as part of disbursements under capital account.

4/ Assuming Paris Club stock relief.

5/ Valued at end-year exchange rates.

Table 14. Kyrgyz Republic: Indicators of Fund Credit, 2003-2007
(In percent, unless otherwise indicated)

	2003	2004	2005	2006	2007
Outstanding Fund credit (end-of-period)					
In millions of SDRs	135.9	142.8	131.6	113.0	96.9
In millions of U.S. dollars	190.0	210.5	194.3	167.3	143.7
In percent of quota	153.0	160.8	148.2	127.3	109.1
In percent of GDP	10.0	10.1	8.5	6.7	5.2
In percent of total exports	25.5	26.3	22.9	18.3	14.6
In percent of external public debt (including Kumtor)	10.6	11.2	9.4	7.5	7.2
In percent of external public debt (excluding Kumtor)	11.2	11.5	9.5	7.5	7.2
In percent of gross reserves at the beginning of the period	68.1	63.3	46.9	40.0	35.1
Debt service due to the Fund					
In millions of SDRs	22.4	22.4	21.4	19.0	16.5
In millions of U.S. dollars	31.3	33.0	31.6	28.2	24.4
<i>Of which:</i>					
Repurchases and repayments	29.0	30.0	31.0	28.0	24.0
Charges/interests	1.0	0.9	0.8	0.6	0.5
In percent of quota 1/	25.2	25.2	24.1	21.4	18.5
In percent of GDP	1.6	1.6	1.4	1.1	0.9
In percent of total exports	4.2	4.1	3.7	3.1	2.5
In percent of total debt service (including Kumtor)	19.8	25.1	21.3	19.3	18.2
In percent of debt service (excluding Kumtor)	32.4	30.8	22.4	20.9	18.9
In percent of gross reserves at the beginning of the period	9.4	8.0	7.5	6.9	5.8

Sources: IMF, Finance Department, and Fund staff calculations.

Table 15. Kyrgyz Republic: Prospective Use of Fund Resources, 2004-2007
(in millions of SDR, unless otherwise stated)

	Outstanding End-Dec. 2003	2004	2005	2006	2007
SBA transactions	0.0				
Purchases		0.0	0.0	0.0	0.0
Repurchases		0.0	0.0	0.0	0.0
STF transactions	0.0				
Purchases		0.0	0.0	0.0	0.0
Repurchases		0.0	0.0	0.0	0.0
PRGF transactions	135.9				
Disbursements		28.7	9.7	0.0	0.0
Repayments		21.7	20.9	18.6	16.1
Total Fund credit outstanding	135.9	142.8	131.6	113.0	96.9
(In percent of quota)					
Total Fund credit outstanding 1/	153.0	160.8	148.2	127.3	109.1
Disbursements under PRGF	0.0	32.3	10.9	0.0	0.0

Sources: IMF, Finance Department; and Fund staff calculations.

1/ Relative to the quota of SDR 88.8 million.

Table 16. Kyrgyz Republic: Reviews and Disbursements
Under the Three-Year PRGF Arrangement

Date	Action	Associated Disbursement
December 2001	Approved three year arrangement.	SDR 11.72 million
July 2002	First review completed, based on end-March 2002 performance criteria.	SDR 11.72 million
February, 2003	Second review completed, based on end-September 2002 performance criteria; conditions and disbursements established for the second year of the arrangement.	SDR 11.72 million
July 2003	Third review completed, based on end-March 2003 performance criteria.	SDR 9.56 million
January 2004	Fourth review completed, based on end-September 2003 performance criteria; conditions and disbursements established for the third year of the arrangement.	SDR 9.56 million
On or after May 15, 2004	Complete fifth review based on end-March 2004 performance criteria.	SDR 9.55 million
June 2004	Indicative targets.	
On or after November 15, 2004	Complete sixth review based on end-September 2004 performance criteria.	SDR 9.55 million

Bishkek, Kyrgyz Republic
June 11, 2004

Mr. Rodrigo Rato
Managing Director
International Monetary Fund
Washington, D.C. 20431

Dear Mr. Rato:

1. This Supplementary Memorandum of Economic Policies (SMEP) updates our Memorandum of Economic Policies (MEP) dated December 15, 2003, which describes the economic policies supported by the International Monetary Fund under a three-year Poverty Reduction and Growth Facility (PRGF) arrangement. The SMEP supplements the policies detailed in the MEP for the period April-September 2004, as well as earlier memoranda under the current IMF arrangement. These policies are consistent with our National Poverty Reduction Strategy (NPRS), presented to the IMF and World Bank in December 2002, and the NPRS Progress Report presented concurrent with this memorandum. We request completion of the fifth review under the PRGF arrangement and modification of the quantitative performance criteria applicable to disbursement of the seventh loan.

I. PERFORMANCE UNDER THE PROGRAM

2. The strong macroeconomic performance of last year, when growth reached nearly 7 percent, has continued into early 2004. Growth helped to reduce the official poverty rate to 41 percent in 2003, from 48 percent in 2001. This year, our tentative estimates indicate that real GDP increased 5.7 percent in January-March (year-on-year). The price pressures that resulted from wheat and gasoline supply disruptions and led inflation to increase abruptly in late 2003 have abated. Despite strong domestic demand, higher gold production and prices helped to reduce the current account deficit in 2003 to under 3 percent of GDP.

Macroeconomic policies

3. All end-March performance criteria were observed. Tax collections in October-March exceeded the cumulative target by som 600 million despite lagging implementation of the agricultural VAT and the real property tax. Payroll tax collections exceeded the target by about som 200 million. The state government fiscal deficit for the period was met by a small margin. There were no central government expenditure arrears, Social Fund pension arrears, or Social Fund arrears to the Medical Insurance Fund, as defined in the program. We have not contracted or guaranteed nonconcessional external debt nor accumulated new external payment arrears.

4. We have issued no decrees or approved legislation that would result in unbudgeted expenditures. We have granted no wage increases, other than the 15 percent increase

effective April 1, 2004, for teachers, nurses, and doctors, which was indicated in our December 2003 MEP. Also in line with the MEP, the base pension was raised from som 200 to som 222.6 on January 1, 2004, and the average monthly pension was increased by an additional 5 percent on April 1, 2004.

5. Monetary conditions have been appropriately tight and remonetization has continued. The National Bank of the Kyrgyz Republic (NBKR) purchased \$28 million from the foreign exchange market during October 2003—March 2004 and the adjusted end-March program floor for net international reserves (NIR) was exceeded by 11 percent of reserve money. The NBKR's net domestic assets (NDA) remained below the adjusted end-March program ceiling by 3 percent of reserve money as the NBKR reduced its foreign exchange market intervention and increased its sales of NBKR bills. Reserve money at end-March exceeded the indicative ceiling by 8 percent. Broad money has continued to expand rapidly—by 33 percent in the year ending March 2004—and private sector credit grew 35 percent during this period.

Structural conditionality

6. We met one end-March structural benchmark and most components of the other. The 2005-07 Medium-Term Fiscal Framework (MTFF) approved and published in March has served as the basis for the update of our NPRS and for our PRGF-supported program. The MTFF is based on quantified policy plans in key line ministries. Regarding the tax policy package described in paragraph 21 of the MEP: (i) the increase of the general VAT threshold from som 300,000 to som 500,000 (the level applied in agriculture) took effect April 1, unifying the VAT threshold throughout the tax system, (ii) we reviewed the current list of VAT exemptions on goods and, as a result, intend to propose to parliament that the new Tax Code contain no VAT exemptions beyond normal international practices, and (iii) a draft law was submitted to parliament in December 2003 to ensure the effective zero-rating of service exports and to define the place of supply consistent with best international practice. We postponed the small business tax reform component in order to undertake this in parallel with the revision of the Tax Code later this year (see below). With effect from April 1, 2004, voluntary patent tax rates were increased on average 45 percent.

7. The 2003 electricity sector quasi-fiscal deficit (QFD) was som 9,240 million (11.1 percent of GDP), compared to the program indicative target of som 9,645 million. This was achieved mainly because energy efficiency improved and the som appreciated against the U.S. dollar (the program's cost recovery tariff is set at 2.3 U.S. cents per kWh).

8. A tender was issued for the sale of Kyrgyz Telecom in November 2003. Negotiations with the winner of the tender took place over several months but were eventually unsuccessful because of differences regarding the investor's medium-term tariff intentions and the payment schedule. We continue negotiating with other tender participants. The privatization of Kairat Bank is proceeding, following the issuance of a tender in November 2003. Final sale of the bank is expected during the third quarter of 2004.

Banking sector reforms

9. Our 2004 banking sector reform program has progressed largely according to schedule. Regarding bank supervision, the new bank supervisory manual adopted by the NBKR in December 2003 is now in effect. Technical assistance from the IMF's Legal Department helped us to identify existing impediments to the effective implementation of our banking legislation. These impediments include conflicts between banking and other legislation and weaknesses in the enforcement and judicial review processes. Beginning with their 2003 accounts, banks are submitting their financial statements in accordance with IAS. Currently under consideration in parliament, amendments to the Law on Banks and Banking Activities would consolidate supervision of banks and bank holding companies and eliminate the 15 percent maximum ownership threshold for financial institutions on bank capital. We are working with parliament on adoption of the revised Anti-Money Laundering Law (reflecting the June 2003 recommendations of the Financial Action Task Force (FATF)) and amendments to the Law on Audits and the Banking Law.

Governance

10. Governance reforms have proceeded. Medium-term quantitative policy frameworks were prepared for the Ministries of Education, Health, and Agriculture and underlie the March 2004 Medium-Term Fiscal Framework (MTFF). A review of the reorganization of the ministries and regulatory agencies with significant economic responsibilities was prepared, reflecting earlier functional analysis reports of these entities. This review contributed to reorganization of government ministries in early 2004 and the establishment of the Ministry of Economic Development and Trade. Its charter is expected to be finalized by end-May. The Permanent Secretary institution is included in the Civil Service Law now before parliament. Regarding agriculture, the National Agricultural Policy Document and Rural Development Strategy will be submitted to the Economic Policy Council (EPC) in June. We have also reorganized the Ministry of Labor and Social Protection as required by our EU Food Security Program.

11. The National Integrity Council approved its work plan in January 2004 and prepared a draft Governance Reform Strategy paper, which was discussed in May at a council meeting chaired by the President. The presidential decree on the NIC structure will be updated to reflect recent changes in its composition.

12. The Economic Deregulation Concept paper was approved by the President in February 2004. A draft law has been prepared requiring that changes to business legislation, regulations, and rates be open to 60 day public consultation and take effect no sooner than 3 months after enactment. A program to reform the "special means" payments and other mandatory non-tax payments related to business operations is expected to be approved by June 2004. Specific steps toward improving the legal framework for business include the adoption by parliament of the Law on the Fundamentals of Technical Regulation in April 2004 and preparation of amendments to the laws on the Procedures for Business Audits and the Law on Licensing, which are expected to be submitted to parliament in June.

We have reviewed the court fee system and intend to reduce fees to 3 percent of par value of collateral by end-June. Under our program with the Asian Development Bank, we have taken important steps regarding corporate governance, including requiring enterprises listed on the Kyrgyz Stock Exchange to apply IAS 2001 to their 2004 financial accounts, and submitting to parliament new laws on national standards for asset valuation and on collateral.

External sector policies

13. We have not imposed any seasonal tariffs or non-tariff barriers. Our m.f.n. import duties were modified slightly with effect from March 2004 in order to meet our WTO commitments. Overall, our average import tariff was reduced from 5.4 to 5.1 percent, while the maximum tariff remains at 15 percent. The third-year consolidation period for our external debt was approved by the Paris Club in April 2004. Bilateral negotiations with the Kuwait Fund on debt rescheduling according to our 2002 Paris Club terms have failed, but all other agreements have been concluded. An agreement to resolve the dispute related to the 1998 aircraft lease and government guarantee has been signed between the Government and DEBIS company.

II. PROGRAM FOR THE PERIOD OCTOBER 2003–SEPTEMBER 2004

Program Objectives, Economic Strategy, and Macroeconomic Framework

14. Nearing the completion of our three-year PRGF-supported economic program, our broad objectives remain much as they were in 2001: (i) further macroeconomic stabilization, (ii) alleviating our external debt situation, and (iii) enhancing future growth by implementing focused structural reforms. Our strategy for achieving these objectives remains as described in the December 2003 MEP.

Revisions to the 2004 macroeconomic framework

15. The 2004 macroeconomic framework in our December 2003 MEP remains broadly appropriate and we have made only minor changes. We now expect real growth in 2004 of 4½ percent and end of period inflation of 4 percent or less. The projected current account deficit of 3.9 percent of GDP is slightly below earlier projections, reflecting the improved balance on non-factor services.

16. We have agreed with the Cameco Corporation, our partner in the Kumtor gold mine, to transfer ownership of the mine to Centerra, a new company to be listed on the Toronto Stock Exchange in June 2004. Through state-owned Kyrgyz Altyn, we would take a one third equity position in Centerra, but would sell down this position at the time of Centerra's initial public offering to 20 percent. The amount of sales receipts will depend on market valuation. For purposes of our financial program, we have assumed the amount of \$60 million. The full amount of these receipts will be transferred to a government account in the NBKR, thus increasing its official reserves, to be smoothly used by the budget over the medium-term, beginning in 2005.

17. The following sections specify further our intentions in fiscal, monetary and exchange rate, external, as well as structural policies for the period ending September 2004. To monitor policy implementation under the remainder of the third-year program, we have set out several quantitative and structural performance criteria and benchmarks through end-September 2004 (Tables 1 and 2). Detailed definitions of the quantitative targets appear in the updated Technical Memorandum of Understanding (TMU) (Annex).

Fiscal Policies

18. We have slightly increased our cumulative October 2003—September 2004 state government cash fiscal deficit target to 4,229 million soms and have slightly increased our 2004 nominal deficit target to 4,039 million soms (4.4 percent of GDP). This fiscal deficit target includes social compensation of som 180 million (0.2 percent of GDP) conditional on increased user costs of electricity. Included in this compensation is an additional transfer to the Social Fund of som 63 million.

19. We intend to build on our recent success in improving tax revenues during the remainder of the 2004 program. In particular, we expect state government tax revenues to reach 14.6 percent of GDP in 2004 and have increased our tax revenue target for end-September (performance criterion) by 4 percent to som 13,008 million because of the higher projected tax base. We are redoubling efforts to fully implement the agricultural VAT by tightening administration over VAT registration through scheduled audits, and the real property tax through Parliamentary approval of the regulation on Real Estate Valuation for Taxation Purposes. We will implement a proper self-assessment system for all large taxpayers by end-2004 and will reduce outstanding VAT refunds due to large taxpayers to som 35 million or less by end-September. In addition, by end-June we will assess our VAT refund mechanism and take steps to improve information sharing between the tax and customs authorities in order to expedite VAT refunds while limiting fraudulent claims. Regarding the Social Fund, we now target payroll tax cash collections of 3,777 million soms for October 2003—September 2004, 2 percent above the original target. For 2004, Social Fund payroll tax collections should reach 4.6 percent of GDP.

20. State government expenditures would be held to 23.4 percent of GDP. This would allow for total expenditures to grow by 1.3 percent in real terms. Following discussions with the Fund staff, we intend to further raise wages for teachers, nurses, and doctors in October 2004, to bring the cumulative increase for the year to 30 percent, as indicated in our December 2003 MEP. We do not intend to raise any other public sector wages in 2004. We will move away from the categorical bases for determining eligibility for social protection and towards means-tested targeting of social benefits. An action plan and schedule for moving to means-tested targeting will be prepared by the Ministry of Labor and Social Protection by end-September 2004. We will continue to abstain from issuing any decrees or other legislation that would result in unbudgeted expenditures unless offsetting expenditure savings are identified in the same decree or legislation. Accordingly, the recent som 38 million increase in war veteran pensions was offset by reducing the transfer to the Social

Fund. We envisage the foreign financing of the public investment program (PIP) to total som 3,212 million in 2004.

21. To consolidate various tax laws into a single piece of legislation and to remove certain inconsistencies, a special task force was appointed to identify and address legal inconsistencies and to ensure the Code covers all spheres of taxation. The task force is receiving valuable input from the public, the private sector, and international consultants in this endeavor. We intend to submit to the Economic Policy Council by end-August 2004 a proposal for a new Tax Code to simplify the small business taxation, taking into account the need to realign, and possibly unify, the VAT and small business tax thresholds, define taxes to be replaced by the small business tax, and eliminate the current voluntary and mandatory patent tax systems (end-August structural benchmark). The small business tax reform package would be considered by parliament together with the Tax Code and the 2005 budget. By end-June we will prepare, for discussion with Fund staff, a scheme that would zero-rate gold exports under the VAT. This principle will be applied in the possible investment agreements with the Jeeroy and Taldy-Bulak gold mine projects. Following a review with staff, we have concluded that no changes to cigarette excises are warranted at this time, but the issue will be revisited in the new Tax Code. Gasoline excise rates will be reduced to better harmonize Kyrgyz excise and sales taxes with those of neighboring countries. We will prepare a specific action plan to curb gasoline and cigarette smuggling by end-September 2004.

Monetary and Exchange Rate Policies

22. Our monetary program is designed to support the targeted 4 percent inflation rate during 2004. The projected increase in money demand this year, reflected in a 8 percent decline in som velocity, would be accommodated by 14 percent som broad money growth. Accounting for a rising money multiplier as a result of more confidence in the banking sector, reserve money is programmed to grow 9 percent. Fiscal consolidation, the expected donor financing, and inflows related to the Kumtor gold mine restructuring should support an increase of NIR by \$61 million during April-September and a build-up of government deposits with the central bank. As a result, NDA would decline by som 2185 million during this period. Credit to the private sector is projected to increase by 36 percent during 2004. To provide alternative low-risk investment opportunities for banks, we intend to increase our net sales of government securities during 2004, helping to diversify banks' assets.

23. The NBKR will continue its exchange rate policy of managed floating. It will not intervene on the foreign exchange market except to smooth temporary variations of the nominal exchange rate. The competitiveness of our tradable goods sector remains adequate, in view of the relatively low wage rates as compared to those of key trading partners. Our stabilization strategy rests on maintaining competitiveness by containing inflation, rather than through nominal exchange rate depreciation. In this respect, some nominal appreciation could occur without harming competitiveness.

Structural Policies

24. We will continue our **banking sector reform** program during the remainder of the third-year program (Box 1). A reputable international firm will finalize by end-June 2004 an external audit of the 2003 financial statements of KAFC and assessment of its loan portfolio (structural benchmark). This will serve as the basis for assessing the viability of KAFC and its future institutional form. No banking license will be issued for KAFC without clear evidence of its viability. SSC's 2003 accounts were audited by a domestic company approved by the World Bank, as budget and scheduling constraints precluded an IAS-based audit by an international reputable firm for SSC's 2003 accounts. This practice will now begin with the 2004 accounts.

25. With IMF Legal Department technical assistance, we have identified legislative amendments and other actions needed to ensure that other legislation is made consistent with banking legislation. We will implement the recommendations of the recent LEG TA mission, as described in Box 1. The NBKR and the Government will continue to adhere strictly to our regulatory response policy, which was developed with IMF technical assistance and was a component of the first-year program under the current PRGF arrangement.

26. In line with IMF staff recommendations, we have concluded that it would be premature to submit to parliament a draft deposit insurance law by June 2004. During the next round of program discussions with IMF staff, we will determine the preconditions for the introduction of the deposit insurance system. These conditions will reflect appropriate financial indicators and other criteria, including criteria for the soundness and stability of the banking system and for individual banks' participation in the DIS.

27. The registration period for depositor compensation has been extended to end-August 2004. The filed claims (currently estimated at som 700 million, or 0.8 percent of GDP) are to be settled with 7-year government bonds to be issued to depositors, as described in our June 2003 SMEP. To reduce domestic debt and to avoid forcing many of the older (and poorest) recipients into selling their bonds in the secondary market at deep discounts, we intend early repurchase of up to som 100 million of these bonds annually, starting in 2005.

28. In the area of **governance**, we are taking several important steps in mining and related areas in the coming months.

- By end-June, the Government will publicly adopt and begin implementing the principles of the Extractive Industries Transparency Initiative.
- In close cooperation with the World Bank, we will develop and adopt a detailed template for disclosing and reporting to the government the financial data of the mining sector (including Kyrgyz Altyn) (structural benchmark), as specified in Box 2. The first draft report will be submitted to Fund staff by end-September 2004 and be published by end-October.

- We will issue a decree reorganizing mining supervision in line with World Bank recommendations (end-September structural benchmark).
- We will ensure that a reputable international firm completes a risk assurance and control audit of Kyrgyz Altyn, with reference to its 2002 and 2003 accounts (end-September structural benchmark).

29. We will continue to implement the governance reform strategy identified in our December 2003 MEP (Box 3). We will also reorganize by end-September 2004 the structure and management system of the Ministry of Agriculture headquarters according to a December 2002 agreement with the EU Food Security Program and, by end-September 2004, we will develop proposals to reorganize the regional structure of the Ministry of Agriculture and all agencies reporting to it, including oblast and rayon subordinated units. Following the completion of the regional agricultural functional reviews in September and November 2004, we will prepare an action plan to transfer part of publicly-financed veterinary and irrigation services to the private sector. We will continue to work with neighboring countries to reach a satisfactory conclusion regarding compensation for our water resources and would welcome the participation of the international financial institutions in this process. Based on our March 2004 MTF, we will develop, by end-September, quantitative expenditure ceilings for the four key ministries (Health, Education, Agriculture, and Labor and Social Protection), as required by the EU Food Security Program.

30. As agreed earlier, in 2004 we will further reduce the electricity sector quasi-fiscal deficit to som 8,650 million (9.4 percent of GDP). To achieve this indicative target under the program, we will use tariff policy and measures to increase cash collection and reduce losses. Reflecting our commitment under the World Bank CSAC, we plan to raise electricity tariffs as of July 1, 2004. Our mid-year quasi-fiscal deficit target for end-June is som 4,900 million.

III. PROGRAM MONITORING

31. The Government and the NBKR believe that the policies set forth in this memorandum are adequate to achieve the objectives of the economic program, but they will take any further measures that may become appropriate for this purpose. The Kyrgyz Republic will consult with the Fund on the adoption of these measures, and in advance of revisions to the policies contained in the MEP, in accordance with the Fund's policies on such consultation.

Yours sincerely,

/s/
Nikolai Tanaev
Prime Minister
Kyrgyz Republic

/s/
Ulan Sarbanov
Chairman
National Bank of the Kyrgyz Republic

Box 1. Remaining Banking Sector Reform Program

Bank supervision and regulatory framework

1. Enhance the transparency of NBKR enforcement actions and the judicial review of these actions by making publicly available all enforcement-related NBKR resolutions and related judicial decisions once these are final—end-June 2004 (IMF).
2. Submit to parliament a legislative proposal that includes amendments to, among others, the Civil Code, the Arbitration Procedure Code, the Civil Procedure Code, the Labor Code, the Tax Code, the Administrative Liability Code, and the Joint-Stock Company Law, in order to eliminate conflicts with banking legislation—end-September 2004 (IMF).
3. Prepare for IMF staff comments amendments to the Banking Law that would establish an impartial internal dispute settlement mechanism—end-September 2004 (IMF).
4. Prepare for IMF staff comments legal provisions that, in accordance with Principle 1 of the Basel Core Principles for Effective Banking Supervision, would ensure the legal protection of the NBKR and its staff against lawsuits for actions taken while discharging their duties in good faith—end-September 2004 (IMF).
5. Submit to parliament amendments to the Bank Secrecy Law and the Law on Banks and Banking Activity to eliminate the provision on bank secrecy that is inconsistent with the Basel Principles. In particular, allow the disclosure of confidential information to foreign banking supervision agencies based on bilateral agreements—end-September 2004. (IMF)
6. Submit to parliament amendments to the Code of Administrative Liability and the Law on Banks and Banking Activity to increase monetary fines levied against employees of banks and financial institutions that are licensed and regulated by the NBKR—end-September 2004. (IMF)

State-owned banks

7. Complete external audit of the 2003 financial statements of KAFC as well as the assessment of its loan portfolio, both conducted by a reputable international auditing firm—end-June 2004. (IMF, WB)
8. Conduct an IAS-based audit by an international reputable auditing firm for the SSC—end-June 2005. (IMF, WB)

Box 2. Line items required to be reported by Kyrgyzaltyn and other Mining Companies

The line items identified in the table below are intended to capture all the significant revenue flows that the Kyrgyz Republic receives from the Mining Sector (i.e. from International and National State-Owned Companies).

REQUIRED TO BE REPORTED BY KYRGYZALTYN AND OTHER MINING COMPANIES		
Non-monetary flows	Produced from:	Volume
Production from mining operations (to be reported separately by mine and commodity)		
Nature of revenue stream	Received from (state where the revenue stream was received from)	Value (US\$ millions)
Taxes on profit and income		
Mineral Resources taxes and royalties		
Other taxes, such as value added taxes (net), withholding taxes, environmental taxes, property taxes, road taxes, employee social payments, customs duties, fuel and excise taxes, emergency taxes etc (to be reported as separate line items if material)		
License fees, rental fees, entry fees and other considerations for licenses/concessions (to be reported separately if material)		
Signing bonuses and production bonuses		
Dividends paid to Kyrgyz Republic/ Kyrgyzaltyn		
Interest/loans paid on behalf of government (or government agency) by mining company/ Kyrgyzaltyn		
Other payments made on behalf of government (or government agency) by mining company/Kyrgyzaltyn (nature of payment to be specified. If more than one type payments to be reported as separate line items if material)		

Box 2 (continued):

REQUIRED TO BE REPORTED BY KYRGYZALTYN AND OTHER MINING COMPANIES (continued)		
Nature of revenue stream	Received from (state where the revenue stream was received from)	Value (US\$ millions)
Proceeds from long term borrowings and other financial operations received on behalf of government and subsequently paid to government		
Lease payments to Kyrgyz Republic		
Proceeds from lease activities received on behalf of government and subsequently paid to government		
Charitable donations		
Contributions to government social funds		
Other significant payments, to be specified: _____ _____ _____		
REQUIRED TO BE REPORTED BY KYRGYZALTYN ONLY		
Nature of revenue stream	Received from (state where the revenue stream was received from)	Value (US\$ millions)
Management fees received from mining interests		
Proceeds from sale of mining interests/assets (100% basis)		
Proceeds from sale of mining interests/assets transferred to government (government % share of total proceeds)		
Dividends received from mining companies		
DISCLOSURES SPECIFIC TO KUMTOR RE-STRUCTURING		
Proceeds from sale of Centerra stock (on 100% basis)		
Other proceeds received related to the Kumtor re-structuring		
Other payments made related to Kumtor re-structuring		

Box 3. Remaining Governance Reform Measures 1/

Institution building

1. Prepare plan to restructure State Commission for Procurement; amend Public Procurement Law in line with EU directives—end-September, 2004. (WB)

Public awareness

2. Draft the National Agricultural Policy Document and Rural Development Strategy for discussion in the EPC—end-June 2004. (IMF)

Efficiency of public administration

3. Approve a program to reform the system of mandatory non-tax payments related to business operations, including so-called “special means” payments—end-June 2004. (IMF, WB)
4. Appoint Permanent Secretaries for key ministries and strengthen role of financial officers in line ministries—end-June 2004. (IMF, WB)
5. Prepare and discuss at the EPC a report on improving registration procedures for businesses—end-June 2004 (IMF).
6. Reorganize the organizational structure and management system of the Ministry of Agriculture headquarters according to a December 2002 agreement with the EU Food Security Program—end-September 2004. (IMF)
7. Develop proposals to reorganize the regional structure of the Ministry of Agriculture and all agencies reporting to it, including oblast and rayon subordinated units—end-September 2004. (IMF)

Legal system

8. Reduce court fees to 3 percent of par value of collateral—end-June 2004. (IMF)
9. Submit to parliament laws on the following matters: “On the Protection of the Rights of Businesses during Inspections and Auditing,” and “On Amendments and Additions to the Law of the Kyrgyz Republic on Licensing.”—end-June 2004. (IMF)
10. Prepare and discuss at the EPC a report on improving the Land Code, Urban Development Code, and the law on State Registration of Real Estate Titles and Transactions, with a view toward ensuring safeguards for private property rights and transparency in real estate operations—end-June 2004 (IMF).
11. Submit to parliament an amendment to the Law on Normative Legal Acts requiring that any new bill approved by parliament incorporate all amendments necessary to bring related laws into conformity with the proposed bill—end-September 2004 (IMF).

1/ Several of the governance measures will be carried out under the World Bank (WB) and Asian Development Bank (ADB) lending operations, as indicated.

Table 1. Kyrgyz Republic: Quantitative Program Targets for April-December 2004 1/
(in millions of soms, unless otherwise indicated; eop)

	2004					
	June		September		December	
	Indicative Targets	Revised Program	Performance Criteria	Revised Program	Indicative Targets	Revised Program
I. Performance criteria						
1. Floor on net international reserves of the NBKR in convertible currencies (eop stock, in millions of U.S. dollars)	159.4	221.1	162.5	221.7	169.4	240.2
2. Ceiling on net domestic assets of the NBKR (eop stock)	1,827	-4	1,926	152	1,671	-562
3. Ceiling on cumulative fiscal deficit of the state government	3,118	3,264	4,183	4,229	600	949
4. Cumulative floor on state government tax collections in cash	8,966	9,513	12,503	13,008	4,063	3,934
5. Ceiling on the stock of central government budget arrears	0	0	0	0	0	0
6. Ceiling on the stock of Social Fund pension arrears	0	0	0	0	0	0
7. Floor on payroll collections in cash of the Social Fund	2,657	2,863	3,703	3,777	1,081	1,175
8. Ceiling on the stock of Social Fund arrears to the Medical Insurance Fund	0	0	0	0	0	0
9. Ceiling on contracting or guaranteeing by the state government or NBKR of new nonconcessional external debt of less than one year (in millions of U.S. dollars)	0	0	0	0	0	0
10. Ceiling on contracting or guaranteeing by the state government or NBKR of new nonconcessional external debt with a maturity of one year or more (cumulative, in millions of U.S. dollars)	0	0	0	0	0	0
11. Ceiling on accumulation of new external payment arrears (in millions of U.S. dollars)	0	0	0	0	0	0
II. Indicative targets						
1. Ceiling on reserve money (NBKR liabilities)	9,831	10,689	10,069	10,868	10,128	10,993
2. Ceiling on the electricity sector quasi-fiscal deficit (in millions of soms)	4,900	4,900	...	....	8,650	8,650

Sources: Kyrgyz authorities; and Fund staff estimates and projections.

1/ Performance criteria, benchmarks, and indicative targets are defined in the Supplementary Technical Memorandum of Understanding.

Table 2. Kyrgyz Republic: Structural Conditionality in the Third Annual Program

Structural benchmarks for end-March 2004

- Approve and publish 2005-07 Medium Term Fiscal Framework based on quantified policy plans in key line ministries (Ministries of Education, Health, and Agriculture). **Observed.**
- Adopt tax policy package as described in paragraph 21 of the Memorandum of Economic Policies (MEP). **Partially observed.**

Structural benchmarks for end-June 2004

- Complete external audit of the 2003 financial statements of KAFC as well as the assessment of its loan portfolio, both conducted by a reputable international firm.
- Develop and adopt a detailed template for disclosing and reporting to the government Kyrgyz Altyn's financial data, and submit the first semi-annual draft report to Fund staff by end-September 2004.

Structural benchmarks for end-August 2004

- Draft and submit to the Economic Policy Council small business tax reform package, as described in paragraph 21 of the SMEP.

Structural benchmarks for end-September 2004

- Submit to parliament legislative amendments to remove conflicts between banking and other legislation, as identified in Box 1, item 2.
- Submit to parliament an amendment to the Law on Normative Legal Acts requiring that any new bill approved by parliament incorporate all amendments necessary to bring related laws into conformity with the proposed bill.
- Complete a risk assurance and control audit with reference to the 2002 and 2003 accounts of Kyrgyz Altyn, conducted by a reputable international firm.
- Issue regulation for reorganizing mining supervision in line with World Bank 2001 Mining Report recommendations.

SUPPLEMENTARY TECHNICAL MEMORANDUM OF UNDERSTANDING

1. The Kyrgyz Republic's performance during the second half of the third-year PRGF-supported program will be assessed by the IMF on the basis of the observance of quantitative performance criteria and structural benchmarks. This annex and the tables attached to the SMEP define the quantitative performance criteria and indicative targets (Table 1 attached to the SMEP), the structural benchmarks (Table 2 attached to the SMEP), as well as the monitoring requirements.¹

I. QUANTITATIVE TARGETS

2. Quantitative targets (i.e., quantitative benchmarks for end-June 2004, quantitative performance criteria for end-September 2004, and indicative targets for end-December 2004) are defined below and summarized in Table 1 of the SMEP.

Floor on net international reserves of the NBKR in convertible currency

3. The program contains a floor on the stock of net international reserves of the NBKR in convertible currencies. This floor will be calculated as the difference between total gross international reserves in convertible currencies at the NBKR and total international reserve liabilities of the NBKR in convertible currencies.

4. Total gross international reserves of the NBKR shall be defined as the NBKR holdings of monetary gold, holdings of SDRs, any reserve position in the IMF, and any holdings of convertible currencies in cash, debt instruments (including accrued interest) or with foreign banks. Amounts pledged as collateral or in swaps or otherwise blocked, capital subscriptions in foreign financial institutions, and non-liquid assets of the NBKR are excluded. Excluded are net forward positions, defined as the difference between the face value of foreign currency denominated NBKR off-balance sheet claims on non-residents and foreign currency obligations to both residents and non-residents. In addition, net claims on other BRO countries are excluded from the ceiling. For program monitoring purposes, gross international reserves shall be valued at a fixed program exchange rate of som 44 per U.S. dollar (\$) and \$1.4318 per SDR. Official gold holdings shall be valued at \$384.6 per troy ounce. Program cross exchange rates are listed in Table 13 below.

¹ Central government and Republican government are synonymous in this memorandum. State government comprises central and local governments. General government comprises state government and Social Fund finances.

5. Total international reserve liabilities of the NBKR in convertible currencies shall be defined as outstanding liabilities to the IMF and other convertible currency liabilities of the NBKR to non-residents with an original maturity of up to and including one year. For program monitoring purposes, total international reserve liabilities shall be valued at the program exchange rates. Thus calculated, the stock of net international reserves in convertible currencies amounted to \$161.0 million as of March 31, 2004.

6. The program floors on the NIR of the NBKR in convertible currencies are reported in Table 1 below.

Table 1. Floors on NIR of the NBKR in Convertible Currencies 1/ 2/

	(In millions of U.S. dollars)
March 31, 2004 (actual)	161.0
June 30, 2004 (indicative target)	221.1
September 30, 2004 (performance criterion)	221.7
December 31, 2004 (indicative target)	240.2

1/ End-of-period stocks.

2/ In the event the base value of March 31, 2004 is revised, the program targets will be revised by the same amount.

7. The floor on net international reserves of the NBKR will be adjusted:
 (i) upward/downward by 100 percent for any excess/shortfall in net foreign financing of the state government budget and cash grants; (ii) upward/downward by 100 percent for any excess/shortfall in cash privatization receipts, and (iii) upward/downward by 100 percent for any excess/shortfall in the proceeds from the sale of the government's Centerra shares. Valued at the program exchange rate, the programmed cash privatization receipts are equivalent to \$5.0 million in the fourth quarter of 2004 and the proceeds from the sale of the government's Centerra shares are equivalent to \$60.0 million in the second quarter of 2004. The adjustment for shortfalls in adjustors (i) and (ii) is to be limited to \$15 million each, valued at the program exchange rate. In the case of a release of the NBKR's pledged foreign reserves, the NIR floor will be adjusted upward/downward by 100 percent for any excess/shortfall in the net effect of the releases and related amortization payments. The programmed net effect is \$0.36 million in the second quarter of 2004, and \$0.12 in the third quarter of 2004.

8. 'Net foreign financing and cash grants' is defined as balance of payment support loans plus cash grants to the state government budget plus any changes in the balance of unused PIP funds held in the NBKR minus amortization payments by the Ministry of Finance and NBKR (excluding repayments to the Fund). This definition applies to the adjustors to

NIR and NDA. The programmed cumulative net foreign financing is as follows (Table 2). The balance of unused PIP funds was equivalent to \$3.5 million on March 31, 2004.

Table 2. Projected Net Foreign Financing and Cash Grants
Cumulative from April 1, 2004

	(In millions of U.S. dollars)
June 30, 2004	4.9
September 30, 2004	5.9
December 31, 2004	23.2

Ceiling on the net domestic assets of the NBKR

9. Net domestic assets of the NBKR are defined as reserve money of the NBKR (defined below) minus the NBKR's net foreign assets² minus the medium- and long-term NBKR obligations (MLT) minus the counterpart of the loan by the Eximbank of Turkey minus the counterpart of the EBRD and IDA enterprise loans (see equation 1 below).

$$(1) \quad NDA = RM - NFA - MLT - \text{Turkish Loan} - \text{EBRD-IDA Enterprise Loan}$$

10. Thus defined, the NBKR's net domestic assets consist of: (a) gross credit to the general government from the NBKR minus deposits of the general government with the NBKR minus the counterpart of the loan by the Eximbank of Turkey; (b) gross credit to domestic banks by the NBKR minus the counterpart of the EBRD and IDA enterprise loans; and (c) all other net assets of the NBKR (other items net). Thus defined, the stock of the NBKR's net domestic assets amounted to som 2,338 million on March 31, 2004.

² The NBKR's net foreign assets consist of net international reserves, as defined in this Supplementary TMU, plus other foreign assets plus the net claims on other BRO countries.

11. The program ceilings on the NDA of the NBKR are reported in Table 3 below.

Table 3. Ceilings on the NDA of the NBKR 1/ 2/

	(In millions of soms)
March 31, 2004 (actual)	2,338
June 30, 2004 (indicative target)	-4
September 30, 2004 (performance criterion)	152
December 31, 2004 (indicative target)	-562

1/ End-of-period stocks.

2/ In the event the base value of March 31, 2004 is revised, the program targets will be revised by the same amount.

12. The ceiling on net domestic assets of the NBKR will be adjusted:
- (i) downward/upward by 100 percent of the excess/shortfall in net foreign financing of the state government budget and cash grants;
 - (ii) downward/upward by 100 percent of the excess/shortfall of cash privatization receipts; and
 - (iii) downward/upward by 100 percent of the excess/shortfall in the proceeds from the sale of the government's Centerra shares, all programmed as described above. The adjustment for shortfalls in adjustors (i) and (ii) is to be limited to \$15 million each, valued at the program exchange rate, excluding the amortization payments for the release of the NBKR's pledged foreign reserves.

Ceiling on the cumulative fiscal deficit of the state government

13. The ceiling on the state government fiscal deficit is defined as the negative sum of:
- (i) the change in the stock of net claims of the domestic banking system and nonfinancial institutions—including state-owned enterprises and public companies—and households on the state government;
 - (ii) the change in the stock of net claims of the foreign banking system and nonfinancial institutions and households on the state government;
 - (iii) net privatization receipts;
 - (iv) net foreign loans disbursed to the state government for budgetary support;
 - (v) net foreign loans disbursed to the state government for project financing; and
 - (vi) rescheduling of bilateral debt (principal and interest payments), following the Paris Club agreement. The fiscal balance will be measured at the program exchange rates, excluding valuation gains and losses on all foreign currency denominated assets and liabilities arising from exchange rate fluctuations. Thus defined, the cumulative fiscal deficit of the state government since October 2003 amounted to som 2,027 million as of March 31, 2004.

14. The change in the stock of net claims of the domestic and foreign banking systems on the state government is defined as the change in the stock of claims of these banking systems

on the state government less the change in the stock of all deposits of the state government with these banking systems. The claims of these banking systems on the state government include: (i) bank loans to state government; (ii) securities or bills issued by the state government held by banks with the exception of those issued in relation with bank rescue operations; and (iii) overdrafts on the current accounts of the state government with banks.

15. The program ceilings on the cumulative fiscal deficit of the state government are reported in Table 4 below.

Table 4. Ceilings on the Cumulative Fiscal Deficit of the State Government 1/ 2/

	(In millions of soms)
June 30, 2004 (indicative target)	3,264
September 30, 2004 (performance criterion)	4,229
December 31, 2004 (indicative target) 3/	949

1/ Cumulative beginning from October 1, 2003.

2/ In the event the base value of September 30, 2003 is revised, the program targets will be revised by the same amount.

3/ Cumulative beginning from October 1, 2004.

Cumulative floor on state government tax collections in cash

16. Tax collections in cash correspond to the line “IV. Tax Receipts” in the Treasury Report and comprise the following categories: 1.0 taxes on income and profits; 2.0 taxes on goods and services; 3.0 specific taxes on services; 4.0 taxes on property; and 5.0 taxes on international trade. Thus defined, cumulative tax collections in cash since October 2003 amounted to som 6,435 million as of March 31, 2004. Cumulative tax collections in cash include collections of tax arrears but exclude tax offsets.

17. The program floors for the cumulative tax collection in cash are reported in Table 5 below.

Table 5. Floors on Cumulative Tax Collections in Cash 1/

	(In millions of soms)
June 30, 2004 (indicative target)	9,513
September 30, 2004 (performance criterion)	13,008
December 31, 2004 (indicative target) 2/	3,934

1/ Cumulative from October 1, 2003.

2/ Cumulative from October 1, 2004.

Ceiling on the stock of central government budget arrears

18. For the purposes of the program, central government budget arrears are defined as an overdue payment obligation of the Republican budget arising since the start of the three-year program period (October 1, 2001) and related to: (i) wages; (ii) Social Fund payroll contributions; (iii) mandatory transfers to the Social Fund; (iv) categorical grants; (v) payments of electricity bills; and (vi) allowances for poor families. A payment is defined to be overdue if it remains unpaid after its due date for (iii) and (iv); for 30 days after its due date for (i) and (ii); for 60 days after its due date for (v); and for 40 days after its due date for (vi). As of March 31, 2004, the stock of thus defined central government budgetary arrears was zero.

19. The program ceilings on the stock of central government budget arrears are reported in Table 6 below. No new arrears will be accumulated by the central government.

Table 6. Stock of Central Government Budget Arrears 1/ 2/

	(In millions of soms)
March 31, 2004 (actual)	0
June 30, 2004 (indicative target)	0
September 30, 2004 (performance criterion)	0
December 31, 2004 (indicative target) 3/	0

1/ Cumulative from October 1, 2003.

2/ In the event the base value of September 30, 2003 is revised, the program targets will be revised by the same amount.

3/ Cumulative from October 1, 2004.

Ceiling on the stock of Social Fund pension arrears

20. A pension payment by the Social Fund is defined as overdue if it has come due since the start of the three-year program period (October 1, 2001) and remains unpaid for 30 days or more after its due date. As of March 31, 2004, the stock of thus defined pension arrears was zero.

21. The program ceilings on the stock of Social Fund pension arrears are reported in Table 7 below. No new pension arrears will be accumulated.

Table 7. Stock of Social Fund Pension Arrears 1/ 2/

	(In millions of soms)
March 31, 2004 (actual)	0
June 30, 2004 (indicative target)	0
September 30, 2004 (performance criterion)	0
December 31, 2004 (indicative target) 3/	0

1/ Cumulative from October 1, 2003.

2/ In the event the base value of September 30, 2003 is revised, the program targets will be revised by the same amount.

3/ Cumulative from October 1, 2004.

Floor on the Social Fund payroll tax collections in cash

22. Payroll tax collections in cash correspond to the total contributions collected by the Social Fund from both employers and employees for a given period. Thus defined, social fund payroll tax collections in cash since October 2003 amounted to som 1,970 million as of March 31, 2004.

23. The program floors for the Social Fund tax collections in cash are reported in Table 8 below.

Table 8. Floor on Social Fund Payroll Tax Collections in Cash 1/

	(In millions of soms)
June 30, 2004 (indicative target)	2,863
September 30, 2004 (performance criterion)	3,777
December 31, 2004 (indicative target) 2/	1,175

1/ Cumulative from October 1, 2003.

2/ Cumulative from October 1, 2004.

Ceiling on the stock of Social Fund arrears to the Medical Insurance Fund

24. Social Fund arrears to the Medical Insurance Fund are defined as overdue transfer obligations of the former to the latter as defined by law and refer to arrears incurred starting January 1, 2002. A transfer is defined to be overdue if the value date of any transfer obligation is more than 5 business days after the due date. As of March 31, 2004, the stock of thus defined arrears of the Social Fund to the Medical Insurance Fund was zero.

25. The program ceiling on the stock of Social Fund arrears to the Medical Insurance Fund are reported in Table 9 below. No new arrears will be accumulated to the Medical Insurance Fund.

Table 9. Ceiling on the Stock of Social Fund Arrears to the Medical Insurance Fund 1/ 2/

	(In millions of soms)
March 31, 2004 (actual)	0
June 30, 2004 (indicative target)	0
September 30, 2004 (performance criterion)	0
December 31, 2004 (indicative target) 3/	0

1/ Cumulative from October 1, 2003.

2/ In the event the base value of September 30, 2003 is revised, the program targets will be revised by the same amount.

3/ Cumulative from October 1, 2004.

Ceiling on the quasi-fiscal deficit of the electricity sector

26. The quasi-fiscal deficit (QFD) of the electricity sector is defined as cost of production minus cash revenues:

$$(1) \text{QFD} = Q * \text{MC} - R;$$

$$(2) Q = 1 / (1 - \ell) * (\sum C_i);$$

$$(3) R = (\sum C_i) * T * C_{\text{cash}},$$

where:

Q is the domestic supply (generation plus import minus export) minus normative losses;

MC is the marginal cost of production required for efficient supply of Q;

R is the total cash revenue;

$\sum C_i$ is the sum of consumption by all end-users (households, industry, agriculture, budgetary institutions, and other);

ℓ is the annual average loss rate of excessive (i.e., above normative) technical and commercial losses in percent of Q;

T is the annual weighted average of posted (or nominal) tariffs for end-users; and

Ccash is the ratio of annual average cash collections to total billing to end-users.

27. For the purposes of the program, the marginal cost is equal to U.S. cents 2.3 per kilowatt hour, and normative losses (including own use) are defined as 15 percent of domestic supply. Total billing of end-users is defined as consumption times the posted nominal tariff. The cash collection component is the amount of bills paid in cash to the energy companies, and excludes any form of cash-to-cash settlements, off-sets, barters, or other non-cash payments. Thus defined, the QFD in the electricity sector amounted to som 9,240 million (or [11.1] percent of GDP) in 2003. The indicative ceiling on the quasi-fiscal deficit in the electricity sector is as follows (Table 10).

Table 10. Ceiling on Quasi-Fiscal Deficit in the Electricity Sector 1/ 2/

	(In millions of soms)
December 31, 2003 (actual)	9,240
June 30, 2004 (indicative target)	4,900
December 31, 2004 (indicative target)	8,650

1/ Annual average.

2/ In the event the actual 2003 figure is revised, the 2004 ceilings will be revised by the same amount.

Ceilings on contracting or guaranteeing of new external debt by the state government of the Kyrgyz Republic or the NBKR or any other agency acting on behalf of the state government

28. In connection with the contracting or guaranteeing of external debt by the state government of the Kyrgyz Republic, the NBKR, or any other agency acting on behalf of the

state government of the Kyrgyz Republic, 'debt' is understood to have the meaning set out in point 9 of the Guidelines on Performance Criteria with respect to External Debt in Fund arrangements (Decision No. 12274-00/85, dated August 24, 2000).³

29. External debt ceilings apply to (i) the contracting or guaranteeing of short term external debt (i.e. external debt with an original maturity of less than one year, except normal import-related credits and NBKR reserve liabilities); and to (ii) contracting or guaranteeing of nonconcessional medium- and long-term external debt (i.e., external debt with an original maturity of one year or more). Disbursements by the Fund from the PRGF Trust are excluded from the ceilings on external debt. Also excluded from these external debt ceilings is the contracting or guaranteeing of new external debt that constitutes a rescheduling or refinancing of existing external debt at terms more favorable to the debtor. The limit on the contracting or guaranteeing of short-term external debt is zero on a continuous basis throughout the period of the arrangement. The limit on the contracting or guaranteeing of medium- and long-term external debt is zero as specified in Table 1 of the SMEP.

³ Debt is understood to mean a current, i.e., not contingent, liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debts can take a number of forms, the primary ones being as follows: (i) loans, i.e., advances of money to the obligor by the lender made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds, debentures, commercial loans and buyers' credits) and temporary exchanges of assets that are equivalent to fully collateralized loans under which the obligor is required to repay the funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements); (ii) suppliers' credits, i.e., contracts where the supplier permits the obligor to defer payments until some time after the date on which the goods are delivered or services are provided; and (iii) leases, i.e., arrangements under which property is provided which the lessee has the right to use for one or more specified period(s) of time that are usually shorter than the total expected service life of the property, while the lessor retains the title to the property. For the purpose of the guideline, the debt is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement excluding those payments that cover the operation, repair or maintenance of the property.

Under the above definition of debt, arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt are debt. Failure to make payment on an obligation that is not considered debt under this definition (e.g., payment on delivery) will not give rise to debt.

30. For program purposes, a debt is considered concessional if the grant element is at least 45 percent, calculated by using currency specific discount rates based on the Commercial Interest Reference Rates (CIRRs) published by the OECD. A lower grant element will be considered only for new debt committed to replace old debt originally contracted at less favorable terms. The average of the CIRRs over the last 10 years will be used for debts with a maturity of at least 15 years and the average CIRR of the preceding six months will be used for shorter maturities.

Ceiling on new external payments arrears

31. For the purposes of the program, external payments arrears will consist of all debt-service obligations (i.e., payments of principal or interest) arising in respect of any debt contracted or guaranteed or assumed by the state government of the Kyrgyz Republic, or the NBKR, or any agency acting on behalf of the state government of the Kyrgyz Republic since the Kyrgyz Republic's independence, including, without limitations, unpaid penalties, interest charges or judicially awarded damages associated with these arrears owed by the state government of the Kyrgyz Republic, or the NBKR, or any agency acting on behalf of the state government of the Kyrgyz Republic, on imports received subsequent to independence. The ceiling on new external payments arrears shall apply on a continuous basis throughout the period of the arrangement. It shall not apply to external payments arrears arising from external debt being renegotiated with external creditors, including Paris Club creditors; and more specifically, to external payments arrears in respect of which a creditor has agreed that no payment needs to be made pending negotiations.

Ceiling on reserve money

32. For the purposes of the program, reserve money consists of currency issued by the NBKR and balances on commercial banks' correspondent accounts with the NBKR. The stock of reserve money amounted to som 10,377 million as of March 31, 2004. The indicative program limits are reported in Table 11 below.

Table 11. Ceilings on Reserve Money 1/

	(In millions of soms)
March 31, 2004 (actual)	10,377
June 30, 2004 (indicative target)	10,689
September 30, 2004 (indicative target)	10,868
December 31, 2004 (indicative target)	10,993

1/ End-of-period stocks.

II. REPORTING REQUIREMENTS UNDER THE PROGRAM

33. The government and the NBKR will provide the Fund with the necessary economic and financial statistical data to monitor economic developments and the quantitative targets. In particular, the government and the NBKR will provide the following specific information:⁴

The balance sheet of the NBKR

34. The NBKR will provide to the Fund its balance sheet every Monday. The information provided will clearly identify the following items in the definitions specified above: the gross foreign assets and liabilities of the NBKR, decomposed by currency and instrument for the assets and by currency and creditor for the liabilities; the net foreign assets of the NBKR; the net international reserves of the NBKR; medium- and long-term liabilities; the net domestic assets of the NBKR; net credit from the NBKR to the general government; net credit from the NBKR to commercial banks; the balance of unused PIP funds held in the NBKR; other items net; and reserve money. The balance sheet will be provided valued at the actual exchange rate as well as according to the valuation applied under the program, as specified in Section I. The above information will be provided to the IMF Resident Representative and/or transmitted by e-mail to the Fund.

Monetary survey

35. Monthly banking system data, in the form of a monetary survey, will be reported to the Fund by the NBKR within 14 days of the end of the month. The information provided will clearly identify the following items: net foreign assets and net domestic assets of the banking system, medium- and long-term liabilities, net credit from the banking system to the general government, financing provided to the rest of the economy, other items net, and broad money. The monetary survey will be provided valued at the actual exchange rate as well as according to the valuation applied under the program, as specified in Section I.

36. The NBKR will provide monthly data to the Fund within seven days after the end of the month on the amount of holdings of treasury bills, GKOs, state obligations, state bonds, and other securities issued by the state government, differentiated by the following categories of holders: the NBKR, resident banks, resident nonbanks, and nonresidents. The information will be provided in both the book (nominal) value and the actual value, where applicable.

⁴Any correction or revisions to the data previously reported should be clearly indicated and documented as to the reasons for revision.

International reserves and key financial indicators

37. The NBKR will provide detailed monthly data within 14 days from the end of the month on the composition of both its gross and net international reserves in convertible currencies and holdings of monetary gold. These data will be provided at two alternative sets of the exchange rates and the gold price: first, at those used to derive the NFA position in the NBKR accounts; second, at those specified in the program (Section I). In addition, weekly reports should be sent to the Fund every Monday on: (a) exchange rates (including the official and interbank exchange rates), foreign exchange interbank market turnover, and the volume of NBKR foreign exchange sales and purchases in the interbank market and with other parties; and (b) treasury bill yields and the amount of treasury bill sales and redemptions. On the 25th day of the month following the reference month, the NBKR will provide indicators of financial soundness of the banking system, including the ratios of regulatory capital to risk-weighted assets, non-performing loans to total loans, and return on equity, as well as data on bank deposit and lending rates by maturity.

Banking system data

38. The NBKR will provide detailed bank-by-bank data within 14 days of the end of the month on commercial banks' compliance with: (a) prudential requirements; and (b) reserve requirements, as well as any penalties, sanctions and other administrative actions imposed on banks.

External debt

39. The Ministry of Finance, together with the NBKR, will provide monthly information on the disbursements, principal and interest payment—both actual and falling due; on contracting and guaranteeing of medium- and long-term external loans by the state government and the NBKR; and any stock of outstanding arrears on external debt service payments within 21 days of the end of each month. In addition, the Ministry of Finance will also report the total amount of outstanding government guarantees and external arrears on a monthly basis. While the NBKR will provide the debt service payment data on private debt, the Ministry of Finance will provide data on debt service on public and publicly guaranteed loans.

Budgetary and extrabudgetary data

40. In addition to the monthly treasury report, the Ministry of Finance and the Social Fund will report monthly on all their recorded expenditure arrears, in particular on those defined above in this TMU. This information will be provided to the Fund staff within 26 days from the end of each reference month. The Ministry of Finance will also provide monthly reports on the disbursements and use under the public investment program and budgetary grants with a one-month time lag.

41. The State Energy Agency, in consultation with the Ministry of Finance and the World Bank, will submit to Fund staff in March and September 2004 their semi-annual report on the QFD in the electricity sector according to the format specified in Table 12 below.

Table 12. Kyrgyz Republic: Electricity Quasi-Fiscal Deficit

	Period
Production (GWh) 1/	
Losses (GWh)	
Loss Rate (in percent) 2/	
Consumption (GWh)	
Tariff (\$ct/kWh) 3/	
Cash Collection Rate (in percent)	
Effective Tariff (\$ct/kWh) 4/	
cash effect. rate	
total effect. rate	
Cost Recovery Tariff (\$ct/kWh) 5/	
Quasi-Fiscal Deficit	
in percent of GDP	
in \$ millions	
in millions of soms	

1/ Generation plus imports minus exports minus normative losses.

2/ Excess technical and commercial losses as percent of production.

3/ Average posted tariff, calculated as quotient of total bill and consumption volume.

4/ Nominal tariff times cash collection rate

5/ Marginal costs, derived from marginal incremental capital cost.

Balance of payments data

42. The NBKR will provide current account and capital account data, including data on foreign trade, services, official and private transfers, foreign investment, and disbursements of public and private loans, on a quarterly basis, with at most a two-month lag. The NBKR will also provide monthly foreign trade data with a two-month lag.

Other general economic information

43. The National Statistics Committee will notify the Fund of the monthly Consumer Price Index by category by the 5th business day of the following month, and convey quarterly GDP estimates within two months of the end of each quarter.

Table 13. Program Cross Exchange Rates

Currency Names		National Currency/US\$	US\$/National Currency
SDR		0.6984	1.4318
GBP	UK pound sterling	0.5903	1.6942
DKK	Danish krone	6.3095	0.1585
EUR	Euro	0.8491	1.1778
INR	Indian rupee	45.3200	0.0221
CAD	Canadian dollar	1.3064	0.7655
CNY	Chinese yuan	8.2768	0.1208
KRW	South Korean won	1,185.6000	0.0008
NOK	Norwegian krone	7.0024	0.1428
TRL	Turkish lira	1,489,255.3957	0.0000
SEK	Swedish krona	7.6810	0.1302
CHF	Swiss franc	1.3144	0.7608
JPY	Japanese yen	109.6752	0.0091
AZM	Azerbaijani manat	4,911.0115	0.0002
AMD	Armenian dram	557.1430	0.0018
BYR	Belarusian rubel	2,124.0150	0.0005
KZT	Kazakh tenge	148.1793	0.0067
LVL	Latvian lats	0.5560	1.7986
LTL	Lithuanian litas	2.9176	0.3427
MDL	Moldavian lei	13.3574	0.0749
RUR	Russian ruble	29.9176	0.0334
TJS	Tajik somoni	3.0640	0.3264
UZS	Uzbek sum	976.4458	0.0010
UAH	Ukrainian hryvnia	5.3320	0.1875
EEK	Estonian kroon	13.2854	0.0753
AUD	Australian dollar	0.7046	1.4193
	Gold (\$/troy ounce)	384.60	

KYRGYZ REPUBLIC—FUND RELATIONS
(As of April 30, 2004)

I. **Membership Status:** Joined: 05/08/1992; Article VIII

II. General Resources Account	SDR Million	Percent of Quota
Quota	88.80	100.00
Fund Holdings of Currency	88.80	100.00
Reserve Position	0.00	0.01

III. SDR Department	SDR Million	Percent of Allocation
Holdings	9.87	N/A

IV. Outstanding Purchases and Loans	SDR Million	Percent of Quota
PRGF Arrangements	138.77	156.27

V. **Latest Financial Arrangements**

Type	Approval Date	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
PRGF	12/06/2001	12/05/2004	73.40	54.28
PRGF	06/26/1998	07/25/2001	73.38	44.69
ESAF	07/20/1994	03/31/1998	88.15	88.15

VI. **Projected Payments to Fund**
(SDR Million; based on existing use of resources and present holdings of SDRs)

	Forthcoming				
	2004	2005	2006	2007	2008
Principal	15.08	20.87	18.61	16.12	14.80
Charges/Interest	0.67	0.57	0.47	0.38	0.30
Total	15.75	21.44	19.08	16.50	15.10

VII. Implementation of HIPC Initiative. Not Applicable.

VIII. Safeguards Assessments

Under the Fund's safeguards assessment policy, the National Bank of the Kyrgyz Republic is subject to an assessment with respect to the PRGF arrangement, which was approved on December 06, 2001 and is currently scheduled to expire on December 05, 2004. A safeguards assessment of the NBKR was completed on January 18, 2002, and identified potential vulnerabilities in the financial reporting framework and in the system of internal controls. Since then, measures to address these vulnerabilities have been implemented.

IX. Exchange Rate Arrangements

The currency of the Kyrgyz Republic has been the som (100 tyiyn =1 som) since May 15, 1993. The Kyrgyz Republic's exchange regime is classified as a managed float with no pre-announced path for the exchange rate. The National Bank of the Kyrgyz Republic publishes daily the exchange rate of the som in terms of the U.S. dollar, which is determined in the interbank foreign exchange market.

X. Article IV Consultations

The Kyrgyz Republic is on the 24-month consultation cycle. The last Article IV consultation discussions were held in October 2002 and the Article IV consultation was completed by the Executive Board on February 20, 2003.

XI. FSAP Participation and ROSC Assessment

The FSAP missions were held in May and September 2002, and the discussions were concluded during the 2002 Article IV consultation. A ROSC Fiscal Transparency mission was held in March 2001 and the ROSC Fiscal Transparency Module was published on March 13, 2002. A ROSC Data mission was held in November 2002 and the ROSC Data Module was published on November 10, 2003.

XII. Resident Representative

The fifth resident representative of the Fund in the Kyrgyz Republic, Mr. Bhaswar Mukhopadhyay, has held his post in Bishkek from March 17, 2001–June 30, 2004. Mr. Michael Mered has been appointed as his successor.

KYRGYZ REPUBLIC—RELATIONS WITH THE WORLD BANK GROUP
(As of May 2004)

1. On May 15, 2003, the World Bank Boards of Directors endorsed a Country Assistance Strategy (CAS) FY 03–06 for the World Bank Group based on the Kyrgyz Government’s National Poverty Reduction Strategy Paper, which aims at assisting the authorities in capitalizing major reforms to date while maintaining a reform and growth course, which will both reduce poverty and enhance prospects for debt sustainability.
2. **International Development Association (IDA).** Between 1992 and 2004, IDA has approved 29 projects totaling approximately \$664 million (after cancellations), of which about \$501 million has been disbursed. Six structural adjustment credits have already been completed, which provided quick disbursing support for the Government’s economic reform programs in privatization, enterprise restructuring, agricultural policy, financial sector, public sector resource management, and pension reform. Seven investment operations have also been completed, supporting reform and rehabilitation of the telecommunication sector, social safety nets, health, rural finance, private enterprises, and livestock development.
3. The active portfolio includes 16 operations:
 - A balance of payments support operation (Consolidation Structural Adjustment Credit, CSAC), assisting with reforms in the power and gas sector and improvements to the business environment (reducing the cost on business from licensing and inspections). The first tranche of the CSAC was disbursed at the end of 2000 and the second at the end of 2001. The disbursement of the third tranche has been delayed. Therefore, at the request of the Government, the closing date of the credit was extended to December 31, 2004.
 - A balance of payments support operation (Governance Structural Adjustment Credit, GSAC) and accompanying Governance Technical Adjustment Credit (GTAC), supporting the Government’s efforts to strengthen the governance framework.
 - Two operations supporting energy sector rehabilitation and reform (Power and District Heating and a Technical Assistance Credit, supporting the CSAC program).
 - Six operations supporting provision of key public goods and reform in agriculture (irrigation rehabilitation, flood emergency, on-farm irrigation, rural finance, agricultural support services, and real estate and land registration—the latter also provides the basis for the introduction of a tax of non-movable property in rural and urban areas).
 - An operation supporting capacity building in the financial and banking system.
 - A second health sector operation continuing support for sectoral restructuring and the authorities’ reform program.

- A rural water supply and sanitation operation (approved together with the CAS Progress Report).
- An urban transport operation.
- A community driven development (CDD) initiative to support the above-mentioned activities (Village Investment Project), designed to empower village communities to identify and implement high priority investments and infrastructure needed to facilitate local enterprise and thereby generate local employment and growth.

4. The World Bank Group's operational objectives for the next 12 months are to support the ongoing structural reforms in energy, the business environment, the banking sector, public expenditure management, health, water and sanitation, and agriculture, and to enhance the portfolio performance. It will continue providing the Government with economic sector work and assisting it with capacity building. In this endeavor, the Bank has recently delivered Public Expenditure Review, Poverty Assessment, Financial Sector Assessment, Country Procurement Assessment, and Country Financial Accountability Assessment reports. The World Bank Group has also delivered a Governance Survey, a Mining Strategy Paper, and engaged in an active dialogue on energy, health, and pension policies. The Bank is in the process of finalizing a study on Growth and Trade.

5. **International Finance Corporation (IFC).** IFC strategy focuses on institution and capacity building through investment and technical assistance, that will promote private sector development, especially SMEs, and support the transformation into a market based economy.

6. IFC's portfolio has grown steadily to \$27.7 million (committed as of July 2003). Building upon IFC's initial investment in the financial sector, the Demir Kyrgyz International Bank, IFC has played an instrumental role in the establishment of the largest bank in the country, the Kyrgyz Investment and Credit Bank, with a \$1.4 million equity investment. IFC developed a strategic partnership with FINCA by investing \$1.0 million in a fund to support microenterprises. This investment was accompanied by technical assistance to FINCA to facilitate its transformation and to the government in developing the appropriate regulatory framework. IFC has also provided technical assistance to review and develop the legal and regulatory framework for leasing. The largest investment in the existing portfolio is the Kumtor gold mine, with additional investments in a packaging plant (Altyn-Ajydar). In 2002, under the Small Enterprise Fund (SEF) procedure, IFC has disbursed a direct investment into a pasta plant (Akun) in the amount of \$1.4 million. The IFC Board also approved in May 2002 a Micro and Small Enterprise facility for Central Asia, with IFC investment of \$45 million. The same year, the Central Asia Small Enterprise Fund (CASEF) was set up on collaboration with other lenders. The amount of IFC's investment into this fund is \$2.5 million. The fund will provide equity, quasi-equity, and debt financing, as well as technical and managerial assistance to growth-oriented SMEs. With financial support from the Swiss Government, IFC draws upon the resources of the Private Enterprise Partnership to advise on improving the business environment, provide training and support services for SMEs, continue past IFC efforts to develop leasing activities, and support agri-business for local and export markets. Technical assistance with a focus on developing tourism has been undertaken in the sector. IFC reviewed the IT sector, including its investment opportunities and development potential.

6. **Multilateral Investment Guarantee Agency (MIGA).** MIGA has supported private sector development in the Kyrgyz Republic by extending guarantees to foreign direct investments in four projects in the manufacturing, services, and mining sectors. Three are currently outstanding – two related to airport services at Manas airport and one related to the Kumtor gold mine. The total amount of foreign direct investment facilitated by MIGA guarantees is over \$360 million. MIGA has also provided capacity building in foreign investment techniques to the State Committee on Foreign Investments and Economic Development, under an initiative supported by the Swiss Government. MIGA plans to continue to assist the development of the Kyrgyz Republic through its guarantee program and capacity building. Data on the Kyrgyz Republic are also featured in MIGA's Privatization Link service, which connects potential investors to information on companies slated for divestiture via the Internet.

World Bank contacts:

Anthony Cholst (acholst@worldbank.org), Senior Country Officer. Phone (202) 458 0324.

Sebnem Akkaya (sakkaya@worldbank.org), Senior Country Economist. Phone (202) 473 2346.

KYRGYZ REPUBLIC—RELATIONS WITH THE ASIAN DEVELOPMENT BANK (ASDB)
(As of May 2004)

1. AsDB operations in the Kyrgyz Republic commenced in 1994. As of end-March 2004, the country received 22 loans totaling a net amount of \$535.9 million. All loans were provided on concessional terms from the Asian Development Fund, the Bank's special fund resources. Seven loans in the AsDB portfolio are program loans totaling \$226.5 million to provide support for policy reforms and to facilitate the transition to a market economy. The remaining 15 loans are project loans totaling \$309.4 million to provide support for various capital investments. The transport and communications sectors account for the largest share of AsDB assistance to the Kyrgyz Republic (27.2 percent of total loans), followed by the financial sector (21.6 percent), and social infrastructure (15.8 percent). AsDB's annual lending levels averaged about \$66 million during 1994-2001. In addition to lending, AsDB has provided 52 technical assistance (TA) grants amounting to about \$31.6 million, of which 13 are project preparatory TA grants amounting to \$9.09 million while the remaining are advisory TA grants for capacity building, policy advice, institutional strengthening and training. At present, 12 loans with a net approved loan amount of \$288 million are ongoing. The overall performance of the Kyrgyz portfolio is satisfactory with none of the projects at risk. However, an analysis of portfolio risk factors where the Kyrgyz performance is below par reveals that half of them are influenced substantially by budget related problems. According to AsDB quarterly reviews, the increasing scarcity of budgetary resources continues to hamper the compliance with some important loan covenants. Other areas where Kyrgyz portfolio performance was below par are compliance with environmental, and social covenants, which could hamper the accomplishment of the country's development objectives.

2. The AsDB, in close consultation with the Government, developed a Country Strategy and Program (CSP) 2004-2006. The CSP was approved by the AsDB Board on November 25, 2003. The overall objective of the CSP is to reduce poverty. This will be addressed primarily by promoting private sector-led economic growth and selective support for human development. AsDB will contribute to private sector-led growth by supporting the following areas: (i) agriculture and rural development to induce further productivity and to expand exports; (ii) the financial sector to strengthen the banking sector, improve depositor confidence, and deepen bank intermediation; and (iii) regional cooperation to reduce cross-border and transport and trade bottlenecks, stimulating overall economic growth and reducing poverty. Through these initiatives, AsDB will assist the Government in meeting the target of the first Millennium Development Goal, i.e., halving income poverty levels. However, given the current constraints to external borrowing, the program envisages a reduced annual lending of only \$30 million in 2004-2006. In 1994-2001, AsDB's average annual lending was around \$66 million. The lending program for 2004-2006 consists of six loans for a total amount of \$90 million. The lending program will be supported by non-lending assistance, including TA for about \$6.5 million. This will include assistance to prepare investment projects as well as advisory and capacity building TA. The geographic focus of the CSP will be on the poorer areas of the country.

3. In 1997, the AsDB initiated support for enhanced subregional economic cooperation among the Central Asian republics and the western-most province of the People's Republic of China. In 1998, the AsDB approved a Private Sector Strategy for Central Asia. The thrust of the strategy is to complement the AsDB's public sector operations with various instruments, including nonguaranteed equity participation and loans to privately sponsored projects.

4. With the adoption in 1999 of poverty reduction as the AsDB's overarching objective, deliberate shifts are being made in the operational program to ensure more explicit support for projects that include beneficiaries living below the poverty line and for projects that will assist others to remain out of poverty.

**KYRGYZ REPUBLIC—RELATIONS WITH THE EUROPEAN BANK FOR
RECONSTRUCTION AND DEVELOPMENT (EBRD)**
(As of May 2004)

1. The EBRD facilitates transition to a market-based economy through its direct support for private sector investments. According to the Strategy for the Kyrgyz Republic, approved in October 2002, the Bank's priorities are: (1) Promote a healthy micro and small and medium-sized enterprise (SME) sector; (2) Facilitate privatization of the remaining major state enterprises; (3) Support the development of the financial sector; (4) Help attract investment to key natural resources projects; and (5) Help the government develop and improve transparency, governance and the investment climate through policy dialogue.

2. As of end-March 2004, the Bank had approved 21 projects for total value of \$710 million, out of which the Bank financed 26 percent and disbursed \$186 million. During the past two years, the Bank expanded its activities in the financial sector as follows:

- Kyrgyz Micro and Small Enterprises Financing Facility (MSEFF) of \$15 million. As of March 2004, more than \$7 million were disbursed to 4,000 small and medium-size enterprises (SMEs) via five participating commercial banks.
- Completion of the Bank's equity investments in Ineximbank and Demir Bank.
- Expansion of the Bank's Trade Facilitation Program (TFP). Four commercial banks participate in the TFP.

The remaining private sector portfolio includes:

- Five investments (equivalent to \$2.6 million) via the Direct Investment Facility.
- Subordinated loan to Kumtor gold mine (senior loan has been fully repaid).
- Loan to Hyatt-Regency Hotel.
- Equity investment in Kyrgyz Investment Credit Bank (KICB).

Four projects are in the public sector:

- Modernization of the telecommunications network.
- Two projects to upgrade electricity transmission networks.
- Development of the agribusiness sector.

3. The Bank also implements grant-funded technical cooperation (TC) to support its investment portfolio, including in the financial sector (MSEFF, among others), natural

resources/environment, agribusiness and infrastructure. Total TC provided is equivalent to more than EUR 15 million.

4. Finally, the Bank has maintained an active dialogue with the government. For example, the Bank was instrumental in founding the International Business Council (IBC) which is devoted to working with the government on improving the investment climate.

**KYRGYZ REPUBLIC—TECHNICAL ASSISTANCE PROVIDED BY THE FUND,
MARCH 2003—MAY 2004**

Dept.	Subject/Identified Need	Timing	Counterpart
FAD	Treasury Management Information System	July 21–29, 2003	Ministry of Finance
	VAT on agriculture	November 3–11, 2003	Ministry of Finance
MFD	Review of the Capital Adequacy and Dividend Arrangements for the National Bank of the Kyrgyz Republic	August 18–28, 2003	National Bank of the Kyrgyz Republic
	Review of Debt Restructuring Operation and 2003 Financial Reporting	October 28–November 10, 2003	National Bank of the Kyrgyz Republic
LEG	Update of the AML/CFT Legislation (jointly with MFD)	February 5-11, 2004	National Bank of the Kyrgyz Republic
	Review of Bank Legislation	March 1-4, 2004 April 26-May 6, 2004	National Bank of the Kyrgyz Republic
STA	SDDS Subscription	January 28–February 5, 2004	National Statistical Committee
	Balance of Payments Statistics	March 15–29, 2004	National Bank of the Kyrgyz Republic
	Monetary and Financial Statistics	April 27-May 11, 2004	National Bank of the Kyrgyz Republic

List of Resident Advisors

MFD	Banking Supervision/Restructuring Advisor	Mr. Svartsman	Jan. 2004–Jan. 2005
MFD	Public Debt Policy and Management	Mr. Azarbajevani	Dec. 2002–Dec. 2004

KYRGYZ REPUBLIC—STATISTICAL ISSUES

General framework

1. The three institutions responsible for collecting, compiling and disseminating macroeconomic statistics have legal and institutional environments that support statistical quality and the respective staffs are well-versed in current methodologies. Unlike staff resources, however, computer and financial resources are not in general commensurate with current needs and constrain future statistical development, especially for the National Statistical Committee (NSC).
2. The NSC maintains a comprehensive and regularly updated data web site largely incorporating international methodological recommendations, with adequate coverage and timeliness (<http://stat-gvc.bishkek.su>). The Kyrgyz Republic have been participating in the Fund's General Data Dissemination System (GDDS) and subscribed to the Special Data Dissemination Standard (SDDS) on February 26, 2004.
3. A data ROSC mission in November 2002 assessed the Kyrgyz Republic's data dissemination practices against the GDDS and undertook an in-depth assessment of the quality of national accounts, price, government finance, monetary, and balance of payments statistics. The mission concluded that the quality of the Kyrgyz Republic's macroeconomic statistics had improved significantly in the last few years. The authorities had established a good track record of implementing recommendations of past technical assistance missions in the area of statistics and had demonstrated commitment to pursue plans and programs to further improve their statistics. The mission recommended that, a program of regular intersectoral consistency checks be introduced to reduce the sometimes significant, unexplained discrepancies between the government finance, monetary and balance of payments datasets. The authorities' response to the data module ROSC (posted on the IMF website (www.imf.org/external/np/rosc)) includes an update on the status of implementation of the ROSC mission's recommendations.
4. The SDDS subscription mission in January/February 2004 found that Kyrgyz Republic met most of the SDDS requirements and made recommendations on two remaining requirements related to the reserves template and external debt. The recommendations were successfully implemented by the authorities prior to Kyrgyz Republic's subscription in late February 2004.

National accounts

5. In general, dissemination of national accounts statistics is prompt. Technical assistance has been received from the IMF, EUROSTAT, OECD, World Bank, and bilateral donors. While significant progress has been made in improving the national accounts estimation process, problems persist with respect to the quality of the source data, due mainly to excessively tight collection deadlines associated with the present national accounts release schedule; efforts are needed to improve the quality of the source data for GDP quarterly

estimates. Difficulties also remain in properly estimating the degree of underreporting, especially in the private sector. To improve the coverage and reliability of primary data, work has been undertaken to introduce scientific sampling procedures. Improved sampling procedures have been adopted for household surveys and new report forms are being introduced for the enterprise survey. The NSC has established a division of sample surveys, which would assist in improving the sampling techniques. However, subannual national accounts statistics are still collected on a cumulative basis rather than by discrete time periods.

Prices, wages, and employment

6. The scope of the new consumer price index (CPI), which has been published since January 1995, is broadly consistent with international standards. The price index covers all urban resident households of all sizes and income levels, but excludes rural households, which comprise the majority of the population. The recent ROSC mission recommended that the authorities expand the coverage of the CPI to include rural households.

7. The new producer price index (PPI), which has been published since October 1996, is compiled broadly in accordance with international standards, although its coverage needs to be improved. The coverage of the PPI was broadened in May 1997 and is expected to be further expanded in the coming years.

8. Progress has been made in computing unit value indices for imports and exports. Work continues with regard to computation of these indices using a standard index presentation and the development of an export price index. However, problems in customs administration have led to incomplete coverage of trade and the lack of an appropriate valuation system. Moreover, the quality of data processing by customs has suffered due to the use of an outdated computer software system.

9. Problems exist in the compilation of the average wage, especially with respect to the valuation of payments in kind and the coverage of the private sector. Monthly and annual data are not comparable because of different coverage and classifications. These problems extend to employment data as well. The coverage of unemployment includes an estimate of unregistered unemployed.

Fiscal accounts

10. The scope of central government statistics falls short of international standards in that it excludes data for the Social Fund and the externally-financed Public Investment Program, although these data are published separately. Among the other limitations are the exclusion of financial transactions with domestic banks and the discrepancies between the deficit and financing data. The authorities do not disseminate any details on financing data. While revenue and expenditure data generally accord with GFS international standards, there are misclassifications in both categories (for example, some nontax revenues are classified as, taxes and certain expenditure items are misclassified in the budget and treasury accounts).

Monthly GFS data for IFS publication have been reported up to July 2003. GFS data are reported each year for the *GFS Yearbook* with the latest data being for 2001.

11. The provision of data on public external debt service has improved. Data on actual debt service, guaranteed debt service, outstanding debt and revised debt projections, are provided on a monthly basis. The quality and timeliness of external debt data are adequate. The External Debt Division of the Ministry of Finance is now solely responsible for monitoring external debt, and this division has benefited from on-site training provided by a Swiss-financed long-term consultant and from the computerization of its database.

Monetary sector

12. The authorities introduced new charts of accounts for the NBKR and the commercial banks during 1997, with the assistance of a resident MAE advisor and USAID. A monetary and financial statistics mission in March 1999 reviewed the compilation of the monetary data and found that the classification of accounts accords with most international best practices, but some areas for improvement remain. In particular, the NBKR's chart of accounts is not sufficiently detailed to support the sectoral breakdown of the monetary statistics and there is a need to improve not only the chart of accounts but also the accompanying instructions.

13. The main findings of the November 2002 ROSC mission were that: (1) the residency criterion was not uniformly applied, as the currency denomination was used to classify some transactions with foreign and domestic units, (2) deposits with banks in liquidation were included in broad money, and (3) source data did not provide sufficient information for a more detailed sectoral breakdown (e.g., subsectorization of nonbanks institutions as recommended in the *Monetary and Financial Statistics Manual*). The mission observed that the use of a residency criterion deviating from international best practices, with the implied risk of misclassification (and, in turn, the over- or under-estimation of the financial system's foreign assets and liabilities), carried over to other macroeconomic datasets (government finance and balance of payments).

14. Monthly monetary data for *IFS* publication are reported on a regular and timely basis. Since December 2002, monetary data are reported electronically to STA.

15. An STA mission on monetary and financial statistics was in Bishkek (April 27–May 11, 2004) to (1) follow up on the implementation of the ROSC mission's recommendations, (2) expand the institutional coverage of the broad money survey, and (3) assist the National Bank of the Kyrgyz Republic in implementing the methodology in the *Monetary and Financial Statistics Manual*.

External sector

16. Data on the balance of payments and international investment position are compiled and disseminated on a quarterly basis. The compilation of balance of payments (BOP) statistics has improved with the assistance of a 1999 technical assistance mission on BOP

statistics. The 2002 data ROSC mission noted that the compilation of BOP statistics broadly follows the *Balance of Payments Manual, Fifth Edition (BPM5)*. The NBKR has good arrangements with other agencies to ensure the timely flow of data. However, because of legal issues related to secrecy provisions, high value transactions cannot be verified with respondents, which limit the ability to cross-check the accuracy of data. Although the data collection program has been expanded in the recent past, coverage deficiencies remain with respect to trade, services, and foreign direct investment. The NBKR enterprise surveys lack an up-to-date register and have inadequate coverage of enterprises, particularly those in free economic zones. There is also a need to improve compilation procedures for achieving temporal consistency of data, and investigating and reconciling discrepancies.

17. The NSC conducts a quarterly sample survey for the estimation of shuttle trade, and uses customs records on the number of people crossing the border with CIS countries to derive the sample. However, the high value limits applied for free import of goods by individuals has resulted in the proliferation of a large industry engaging in shuttle trade, complicating estimation.

18. An STA mission on balance of payments statistics was in Bishkek (March 15–29, 2004) in response to the authorities' request for technical assistance to address compilation issues, and to assess training needs.

KYRGYZ REPUBLIC—CORE STATISTICAL INDICATORS
(As of June 1, 2004)

	Exchange Rates	International Reserves	Central Bank Balance Sheet	Reserve Money	Broad Money	Interest Rates	Consumer Price Index	Exports/Imports	Current Account Balance	Overall Government Balance	GDP/GNP	External Debt/Debt Service
Date of Latest Observation	05/31/04	05/31/04	05/31/04	05/31/04	04/30/04	05/21/04	Apr/04	Q1/04	Q1/05	Apr/04	Apr/04	Apr/04
Date Received	06/01/04	06/01/04	06/01/04	06/01/04	05/15/05	05/28/04	05/10/04	05/15/04	05/15/04	05/28/04	05/10/04	05/19/04
Frequency of Data	D	D	D	D	M	W	M	Q	Q	M	M	M
Frequency of Reporting	D	D	D	D	M	W	M	Q	Q	M	M	M
Source of Update	A	A	A	A	A	A	A	A	A	A	A	A
Mode of Reporting	E	E	E	E	E	E	E	E	E	C	E	C
Confidentiality	C	A	A	A	C	C	C	C	C	C	C	C
Frequency of Publication	W	M	M	M	M	W	M	Q	Q	M	M	Y
Explanation of abbreviations: Frequency of data, reporting and publication: D-daily, W-weekly, M-monthly, Q-quarterly, Y-yearly in conjunction with staff visits. Source of data: A-direct reporting by National Bank, Ministry of Finance, Ministry of Statistics and Analysis or other official agency. Mode of reporting: C-cable or facsimile; E-electronic news reporting; F-floppy provided. Most data are provided to the Resident Representative's office and then forwarded to headquarters. Confidentiality: A for use by the staff only; C-unrestricted use.												



Press Release No.04/133
FOR IMMEDIATE RELEASE
June 30, 2004

International Monetary Fund
Washington, D.C. 20431 USA

IMF Completes Fifth Review of the Kyrgyz Republic's Three-Year PRGF Arrangement and Approves US\$14 Million Disbursement

The Executive Board of the International Monetary Fund (IMF) has completed the fifth review of the Kyrgyz Republic's economic performance under the three-year Poverty Reduction and Growth Facility (PRGF) arrangement. This enables the Kyrgyz Republic to draw an amount equivalent to SDR 9.56 million (about US\$14 million), which will bring the total amount drawn under the arrangement to the equivalent of SDR 63.84 million (about US\$93.6 million).

Completion of the review followed the World Bank's decision on June 29, 2004 that there is a continued basis for the provision of World Bank concessional financial assistance. On June 23, 2004, the IMF's Executive Board also concluded, on the basis of the First Progress Report, that the National Poverty Reduction Strategy paper submitted by the Kyrgyz Republic continues to provide a sound basis for IMF concessional financial assistance.

The Executive Board approved the three-year arrangement effective on December 6, 2001 (see [Press Release No. 01/49](#)) for a total of the equivalent of SDR 73.4 million (about US\$107.6 million).

The PRGF is the IMF's concessional facility for low-income countries. PRGF-supported programs are based on country-owned poverty reduction strategies adopted in a participatory process involving civil society and development partners and articulated in the [Poverty Reduction Strategy Paper \(PRSP\)](#). This is intended to ensure that PRGF-supported programs are consistent with a comprehensive framework for macroeconomic, structural, and social policies to foster growth and reduce poverty. PRGF loans carry an annual interest rate of 0.5 percent and are repayable over 10 years with a 5½-year grace period on principal payments.