

Kyrgyz Republic: 2011 Article IV Consultation and Request for a Three-Year Arrangement Under the Extended Credit Facility—Staff Report; Supplement; Staff Statement; Public Information Notice and Press Release on the Executive Board Discussion; and Statement by the Executive Director for the Kyrgyz Republic.

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of a combined discussion of the 2011 Article IV Consultation and Request for a Three-Year Arrangement Under the Extended Credit Facility, the following documents have been released and are included in this package:

- The staff report for the combined 2011 Article IV Consultation and Request for a Three-Year Arrangement Under the Extended Credit Facility, prepared by a staff team of the IMF, following discussions that ended on May 4, 2011, with the officials of Kyrgyz Republic on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on June 2, 2011. 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 supplement on the Debt Sustainability Analysis
- A staff statement of June 20, 2011
- A Public Information Notice (PIN) and Press Release, summarizing the views of the Executive Board as expressed during its June 20, 2011 discussion of the staff report on issues related to the Article IV consultation and the IMF arrangement, respectively.
- A statement by the Executive Director for the Kyrgyz Republic.

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

Letter of Intent sent to the IMF by the authorities of the Kyrgyz Republic*
Memorandum of Economic and Financial Policies by the authorities of the Kyrgyz Republic*
Technical Memorandum of Understanding*
Selected Issues Paper

*Also included in Staff Report

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

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INTERNATIONAL MONETARY FUND

KYRGYZ REPUBLIC

Staff Report for the 2011 Article IV Consultation and Request for a Three-Year Arrangement Under the Extended Credit Facility

Prepared by the Middle East and Central Asia Department
(In consultation with other departments)

Approved by David Owen and Tom Dorsey

June 2, 2011

EXECUTIVE SUMMARY

Background: The Kyrgyz economy is recovering from a deep political crisis last year. In April 2010, a popular uprising toppled the previous regime and internal ethnic conflict in June 2010 exacerbated the already difficult political situation. The subsequent constitutional referendum and parliamentary elections in October 2010 have helped to stabilize the political situation and put the economy on a path of recovery, though the political situation remains fragile. Following the Joint Economic Assessment and the donor conference in mid-2010, the Fund provided post-crisis support to the Kyrgyz Republic under the Rapid Credit Facility (RCF). The successful implementation of the RCF-supported policies helped to catalyze donor assistance and allowed the new authorities to build a track record.

Staff views: Expansionary fiscal policy and rising inflation have raised concerns about the policy mix going forward. While a limited fiscal expansion in 2011 will support the nascent economic recovery, consolidation from 2012 will be critical to ensure medium-term fiscal and debt sustainability and support the central bank's efforts to curb inflation. Moreover, reducing underlying vulnerabilities in the banking sector, addressing governance issues, and improving the business environment will be key to enhancing the role of the private sector in the economy and fully realizing the economy's growth potential. Productivity enhancing structural reforms are needed to safeguard external sustainability and support medium-term growth prospects.

The authorities' views: The authorities shared staff's concerns about the risks associated with expansionary fiscal policy in 2011 and rising inflation, but emphasized that the 2010 fiscal deficit and the cumulative deficit for 2010–11 is significantly lower than anticipated earlier. They saw merit, however, in withdrawing fiscal stimulus during 2012 and over the medium term, highlighting that strong growth and appropriate measures will help boost revenues and reduce the fiscal deficit. They also agreed that vulnerabilities in the banking sector need to be dealt with swiftly and effectively and that addressing governance issues, including through the commitment to not create any new extra budgetary funds, will be important for supporting economic development.

New ECF arrangement: The ECF-supported program (75 percent of quota, SDR 66.6 million) draws from the authorities' priorities and supports their efforts to restore macroeconomic stability, rebuild policy buffers, promote inclusive growth in a low inflation environment, achieve medium-term fiscal consolidation, address weaknesses in the financial sector, bolster reserves, and catalyze critical donor support. The ECF arrangement entails risks, but strong conditionality in macrocritical areas, including prior actions, provides sufficient safeguards.

Relations with the Fund: The Kyrgyz Republic has accepted the obligations of Article VIII, Sections 2, 3, and 4, and its exchange rate system is free of restrictions on payments and transfers for current transactions. The *de jure/de facto* exchange regime is floating/other managed. The official exchange rate may differ by more than 2 percent from market rates, giving rise to multiple currency practice, because the official rate is based on the average transaction weighted rate of the preceding day. In practice, the official and market rates have never differed by more than 2 percent.

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I. EMERGING FROM THE POLITICAL CRISIS¹

The Kyrgyz Republic suffered from a deep political crisis last year. In April 2010, a popular uprising toppled the previous regime and internal ethnic conflict in June 2010 exacerbated the already difficult political situation. The crisis adversely affected economic activity and near-term growth prospects, straining the government's financial position, which was further worsened by critical reconciliation, recovery and reconstruction needs. Parliamentary elections took place in October 2010 and a new coalition government took office in December 2010. The shift to a parliamentary democracy provides a unique opportunity to break with the past and strengthen governance and reform the economy. The political situation remains fragile, with presidential elections scheduled for October 2011.

1. **The 2010 political turmoil disrupted economic activity and negatively affected near-term growth prospects.** Border closures, especially with Kazakhstan, hampered the business of Kyrgyz companies and households involved in trade. The security situation led to the lowest tourist arrivals in almost a decade. Interruptions in the spring farming season and problems in harvesting and marketing have led to losses in agricultural production. Rising global food and fuel prices have posed additional challenges. The banking sector also suffered from diminished depositor confidence and the economic effects from the events in the south. Subsequently, the economy contracted by 1.4 percent and inflation rose to nearly 20 percent in 2010.

2. **Timely and well coordinated efforts by the international community have helped to prevent the Kyrgyz economy from plunging into a much deeper recession.** The Fund, together with the World Bank and the Asian Development Bank led two Joint Economic Assessment missions to evaluate economic damage from the shocks in 2010. The US\$1.1 billion worth of pledges made by the international community at the donor conference in July 2010 (US\$380 million of which have been contracted so far) have provided important financial underpinnings for implementing the government's anti-crisis program. Along with technical assistance, the Fund provided important financial support (in the amount of 25 percent of quota, SDR 22.2 million) under the RCF in September 2010. The support under the RCF helped to catalyze pledged donor assistance and allowed the Kyrgyz authorities to build a track record ahead of a medium-term program engagement with the Fund.

¹ Discussions were held in Bishkek during April 20–May 4, 2011. The staff team comprised Mr. Beddies (head), Messrs. Amaglobeli and Shukurov (MCD), Mr. Rota Graziosi (FAD), Ms. Knight (LEG), Ms. Kongsamut (MCM), Mr. Rayner (SPR), and Mr. Gvenetadze (Resident Representative). The team met with President Otunbayeva, Prime Minister Atambaev, Minister of Finance Mambetjanov, Acting Chairperson of the National Bank of the Kyrgyz Republic (NBKR) Jeenbaeva, Minister of Economic Regulation Tashbaev, other senior government officials, and representatives of the donor community and civil society. The mission also organized a public seminar to present the findings of a recent study on inflation in the region.

3. **Stabilization of the security situation allowed the interim government to conduct a constitutional referendum and parliamentary elections, which led to the formation of a new coalition government.** The outcome of the June 2010 constitutional referendum shifted the balance of powers toward the parliament and set the stage for the first parliamentary democracy in Central Asia. The recent changes in the political landscape present a unique opportunity to address long-standing governance problems that were the root cause for not completing the two remaining reviews under the 2008 Exogenous Shocks Facility (ESF).²

4. **Against this background, one of the main objectives of the new Kyrgyz coalition government is to restore and maintain macroeconomic stability.** While supporting the nascent economic recovery in the near term is essential to maintain political stability, fiscal consolidation in 2012 and beyond will be critical to rebuild policy buffers and promote inclusive private sector-led growth in a low inflation environment. To support this effort, the authorities have requested Fund support under a three-year ECF arrangement, which will be instrumental in securing much-needed donor assistance. The ECF arrangement draws from the government's priorities and builds on the findings of the recently concluded Ex Post Assessment (EPA) of Longer Term Program Engagement. EPA findings are summarized in Box 1.

² The government's decision to entrust the management of the bulk of bilateral donor assistance received in 2009 to a newly created extra-budgetary fund became the main stumbling block for completing the remaining ESF reviews. Ultimately, the sovereign funds invested overseas have been returned to the central bank; the ESF expired on June 9, 2010.

Box 1. Kyrgyz Republic: Lessons Learned from the Ex Post Assessment

The EPA report reviewed the Kyrgyz Republic's economic performance under Fund-supported programs from early 2005 to mid-2010. Two Fund-supported programs were assessed: the March 2005 arrangement under the Poverty Reduction and Growth Facility (PRGF, which expired in May 2008), and the December 2008 ESF arrangement (which expired in June 2010). The main conclusions of the EPA are as follows:

- Macroeconomic performance under Fund-supported programs in the Kyrgyz Republic in the period under review (2005–10) was generally satisfactory.
- However, progress in promoting structural reforms and in improving the transparency of government operations was disappointing. Lack of progress in economic governance could jeopardize macroeconomic stability over the medium term, and exposes the Fund to reputational risk.
- A new three-year Fund supported program could be very helpful during the reconstruction period. Given the Kyrgyz Republic's protracted balance of payments need, an ECF arrangement that could help to finance this need, catalyze support from other donors and address structural issues would play a key role in supporting macroeconomic management over the next few years. Such a Fund-supported program should ensure fiscal consolidation over the medium term to avoid a renewed build-up of debt, and rebuild macroeconomic policy buffers.

Structural reform of key sectors will need to be addressed forcefully under a new ECF arrangement. Structural conditionality will need to be carefully designed, be based on a homegrown development strategy, take into account implementation capacity, and be coordinated with other donors, in particular the World Bank. It must be meaningful without being perceived as intrusive—ownership of reforms remains crucial. In particular:

- In the financial sector, a level playing field needs to be maintained, including by strengthening the central bank's independence and supervisory capacity. The role of the courts in financial stability matters should be reduced, and financial sector transparency and accountability standards raised.
- In the energy sector, below cost recovery tariff levels, high technical and commercial losses, and poor governance need to be addressed. However, given the Fund's limited expertise in energy sector issues, close cooperation with key donors will be important.

The EPA also highlighted that key risks associated with renewed engagement under an ECF arrangement will need to be carefully managed.

- The resolution of security issues, especially through reconciliation in the south, is a precondition for sustainable economic development.
- Weak governance remains a key concern—while reducing corruption and the perception of corruption will need to be a top priority for the new government, progress in the area has proven elusive in the period under review in the EPA.
- Program design and monitoring of implementation will need to be mindful of the risks associated with weak governance.
- Exogenous shocks will likely continue to affect program performance. A solid performance under the RCF provides some comfort, but no guarantees.

II. RECENT ECONOMIC DEVELOPMENTS

While there are early signs of recovery from the economic contraction in 2010, the situation remains fragile with inflation at more than 20 percent. The political crisis has disrupted trade flows, agricultural production, construction, and tourism, which led to a shift in the current account from surplus to deficit. Fiscal policy has been expansionary, albeit less than anticipated, and monetary policy was tightened toward the end of the year to counter rising inflation.

5. **Following the economic contraction in 2010 the Kyrgyz Republic is showing signs of a gradual recovery.**

Growth and inflation

- Domestic instability and trade disruptions resulted in nongold GDP contracting by 2 percent in 2010 and overall GDP by 1.4 percent. The gradual normalization of the political situation and the reopening of borders boosted growth in the first four months of 2011 with nongold GDP increasing by 3.7 percent and overall GDP by 3.2 percent.
- Following the global spike in food and fuel prices, annual inflation has increased from 3.5 percent in June 2010 to 22.6 percent in April 2011. Latest developments in 2011 suggest that core inflation (excluding food and fuel) has stabilized, and May is likely to be the first deflationary month in more than a year (see below).

External sector

- Agricultural exports, tourism, transportation receipts, and shuttle trade declined as a result of a lack of security and border closures.³ However, higher international gold prices mitigated the decline in exports, while remittance inflows increased as Russia, the source of more than 90 percent of remittances, recovered from the international financial crisis in 2010.
- The border closures also slowed import growth, while the imposition by Russia of a fuel export duty reduced the volume of fuel imports. The import volume decrease, however, was outweighed by higher fuel prices leading to an overall increase in the value of imports.
- Consequently, the current account deficit (excluding official transfers) in 2010 deteriorated to almost 4 percent of GDP. Reserve coverage declined somewhat, but remained at 4.2 months of prospective imports.

³ The Kyrgyz Republic is the only World Trade Organization (WTO) member in Central Asia and also has free trade arrangements with the Commonwealth of Independent States (CIS) countries. As a result, the Kyrgyz Republic has a comparative advantage to transit Chinese exports to CIS countries.

Fiscal policy

- Tax revenue collections in 2010 turned out somewhat better than projected, in part due to advance payments made by the largest gold-mining company and efforts to strengthen tax and customs administration. Moreover, absorptive capacity constraints to implement capital projects in a highly insecure environment, delays in the government capitalization of a problem bank, and slow disbursements of external financing led to expenditure underexecution.
- Thus, the overall budget deficit in 2010 was significantly lower than envisaged under the RCF (6.5 percent versus 12 percent of GDP) and allowed the coalition government to announce plans to raise wages for education and healthcare employees shortly after taking office.

Monetary policy and exchange rate

- In response to growing inflationary pressures, the NBKR has tightened monetary policy. Beginning in December 2010 the NBKR has significantly increased sales of its short-term notes and raised reserve requirements from 8 percent to 9 percent in February 2011.⁴ Yields on the NBKR notes, which form the basis for the policy rate, rose to 9.5 percent in early May of this year from 2 percent in August 2010. Yields on treasury bills have followed suit.
- The exchange rate had been depreciating and the NBKR intervened to smooth short-term volatility, which helped to absorb some liquidity. Subsequently, interventions combined with active open market operations and a tighter fiscal stance in the first quarter of 2011 resulted in a slowdown in year-on-year reserve money growth from 18.5 percent in December 2010 to 14.5 percent in March 2011. More recently, the exchange rate has been appreciating, in part owing to strong remittances inflows but it is uncertain how sustainable this trend will be. While remaining above 50 percent, deposit dollarization has somewhat declined.

Financial sector

- The crisis contributed to a change in the banking sector landscape. During the April 2010 events, seven banks—including the largest and systemic Asia Universal Bank (AUB), which was allegedly connected with the outgoing regime—were placed under temporary administration to prevent capital flight. Ultimately, two banks were released from temporary administration, four were placed under conservatorship, and AUB was nationalized. Deposits in those banks shifted to banks perceived as safer, particularly foreign

⁴ In the absence of a deep and liquid money market, the current monetary policy framework relies on monetary targeting. The operational framework is primarily based on open market operations and foreign currency interventions.

banks and the largest state-owned bank, the Settlement and Saving Company (SSC), which has emerged as the second largest bank in the system. AUB lost more than half of its deposits.

- Despite the stress on the system, financial sector stability has been maintained and depositor runs avoided. The share of nonperforming loans (NPL) increased in the aftermath of the political events, and the system's liquidity declined. However, the NPL ratio appears to have stabilized recently (excluding AUB/Zalkar, which is the newly created "good bank" resulting from the split of AUB) and system capital adequacy appears comfortable (Text Table 1).

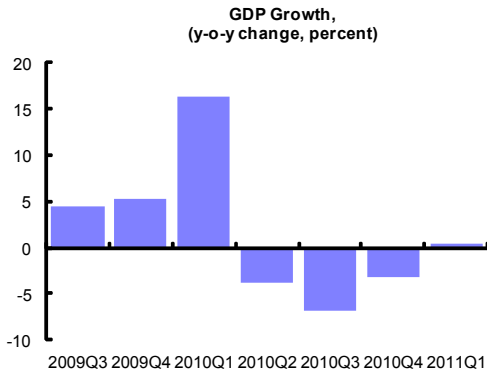
Text Table 1. Kyrgyz Republic: Financial Soundness Indicators, 2009–11
(In percent, unless otherwise indicated)

	System					System excluding AUB/Zalkar					System excluding banks under conservatorship and Zalkar				
	Dec-09	Apr-10	Sep-10	Dec-10	Mar-11	Dec-09	Apr-10	Sep-10	Dec-10	Mar-11	Dec-09	Apr-10	Sep-10	Dec-10	Mar-11
<i>Capital Adequacy</i>															
Regulatory capital / RWA (CAR)	33.5	35.3	23.1	30.4	30.4	37.3	38.4	32.2	32.2	32.3	37.0	38.2	31.4	31.4	31.4
<i>Asset Quality</i>															
NPLs (gross) / total loans	8.2	9.4	16.8	15.8	13.8	8.6	8.7	11.7	11.8	11.7	8.9	9.1	10.1	10.2	10.1
<i>Liquidity</i>															
Liquid assets / total assets	45.5	41.4	32.5	35.7	38.1	35.4	35.8	33.0	34.9	37.3	33.5	33.6	33.3	35.0	37.3

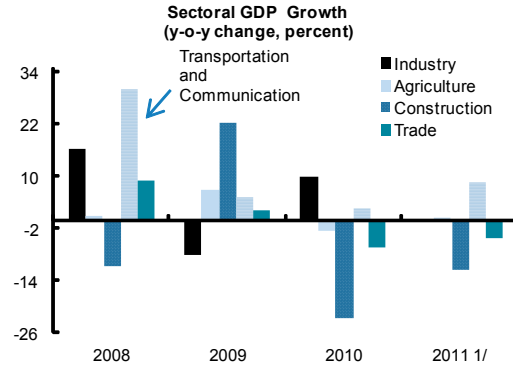
Source: Kyrgyz authorities.

Figure 1. Kyrgyz Republic: Real Sector Developments
(In percent)

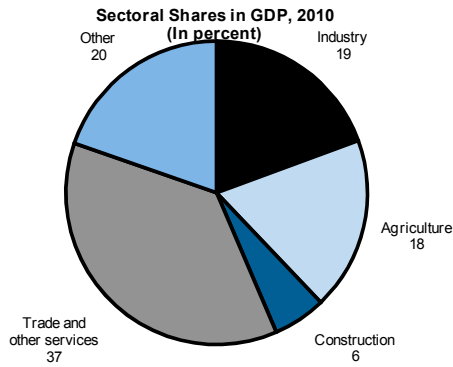
The economy has started to recover



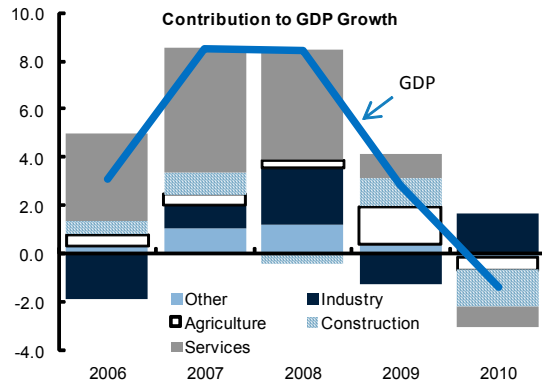
Growth is led by industry and transportation



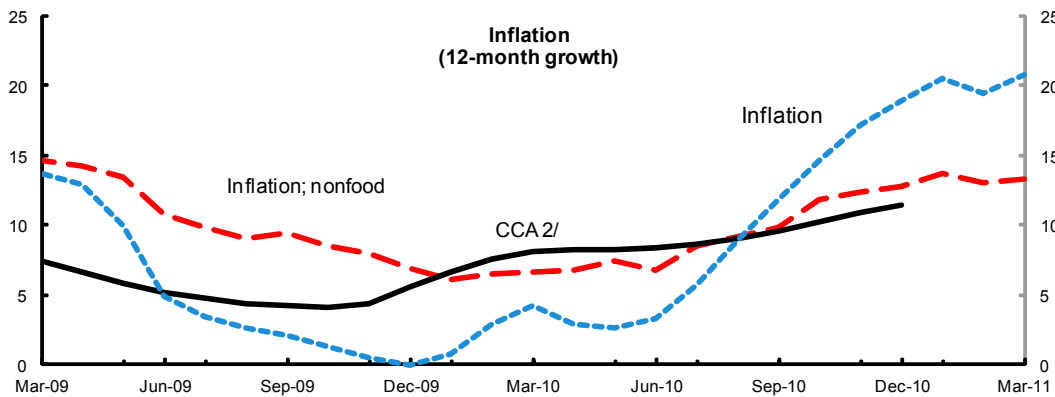
Agriculture, construction and services account for more than 60 percent of GDP



Contraction in these sectors resulted in large negative contributions to GDP growth in 2010



Inflation accelerated quickly following the increase in the world food and fuel prices



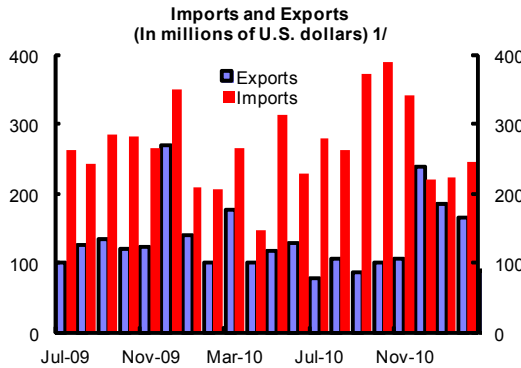
Sources: Kyrgyz authorities, Fund staff estimates and projections.

1/ Q1 2011

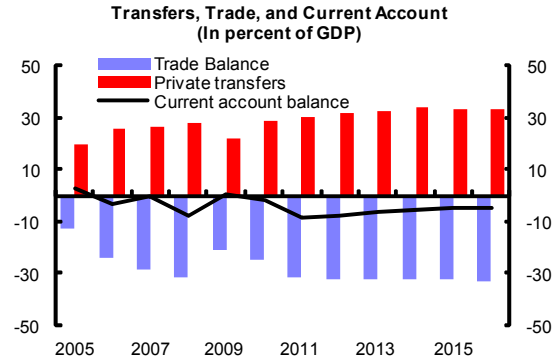
2/ Caucasus and Central Asia. Excludes Turkmenistan. Updated to December 2010.

Figure 2. Kyrgyz Republic: External Sector Developments and Projections

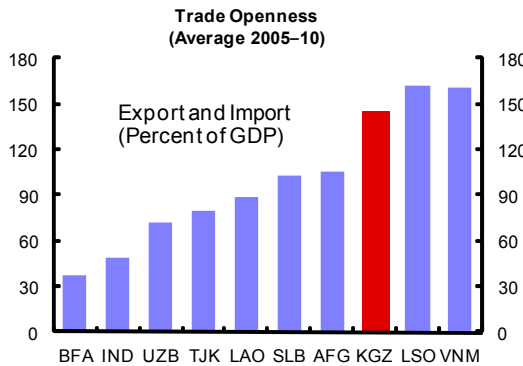
External trade is stabilizing



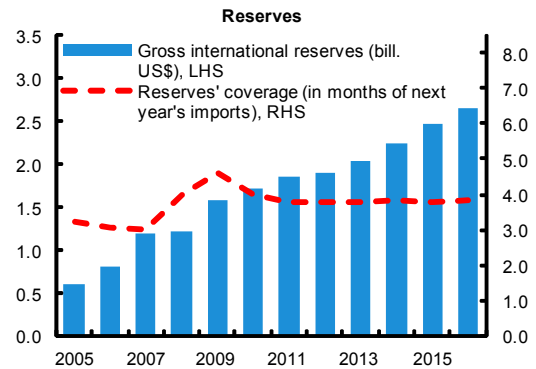
Remittances finance a significant portion of the trade deficit



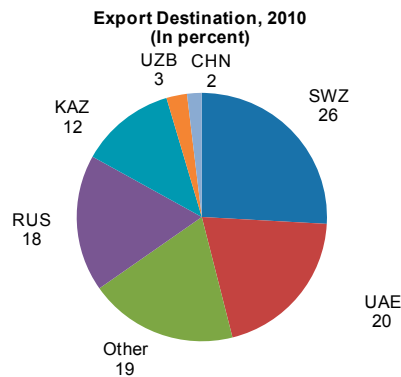
The Kyrgyz Republic is one of the most open economies in the world



Reserve coverage is estimated to have declined in 2010



The share of non-CIS countries in Kyrgyz Republic's exports is high due to gold exports

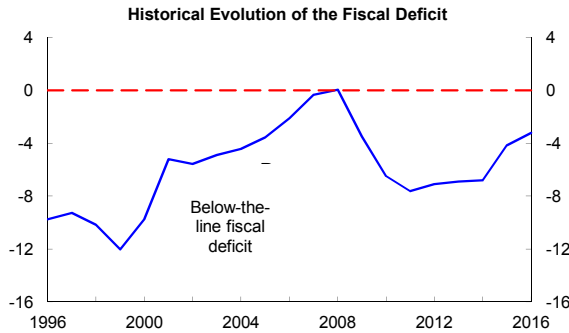


Sources: Kyrgyz authorities, Fund staff estimates and projections.

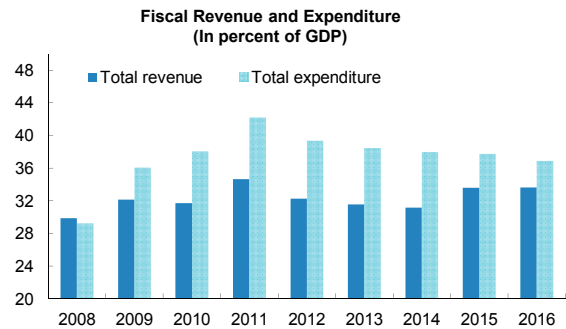
1/ There was a large, one-off upward revision of exports in November, 2010.

Figure 3. Kyrgyz Republic: Fiscal Sector Developments and Projections

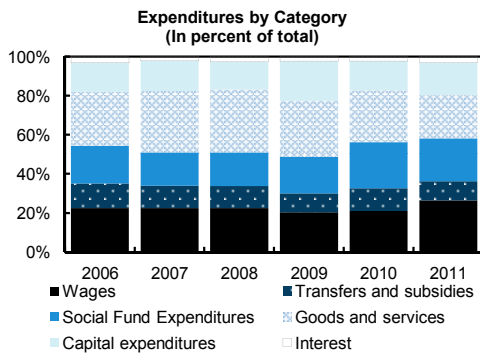
Tight fiscal policy in 2007–08 created fiscal space for expansion later. Consolidation is expected from 2012



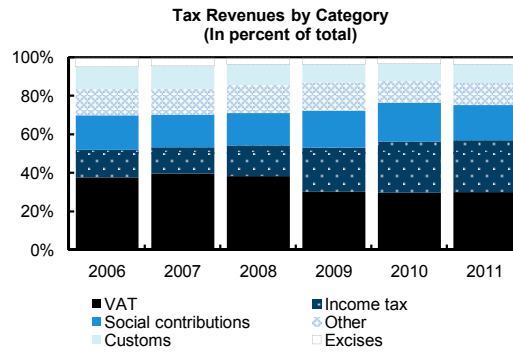
Both revenue and expenditure measures will contribute to consolidation



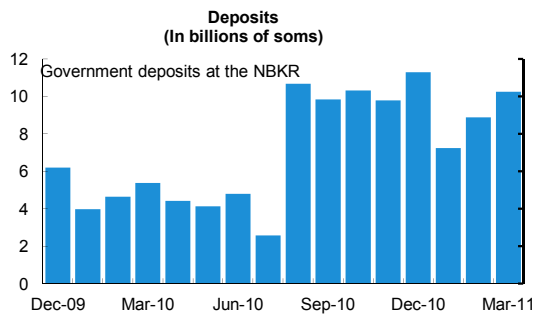
Wages will account for more than a quarter of the 2011 budget, while the share of goods and services will decline



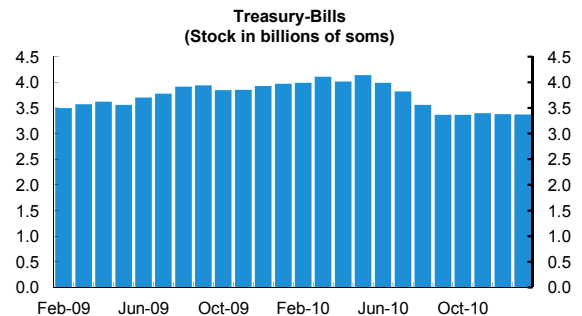
VAT revenues declined after the rate cut in 2009, while income tax revenues increased due to gold company payments



Government deposits at the NBKR have been increasing



The stock of treasury bills remains broadly stable

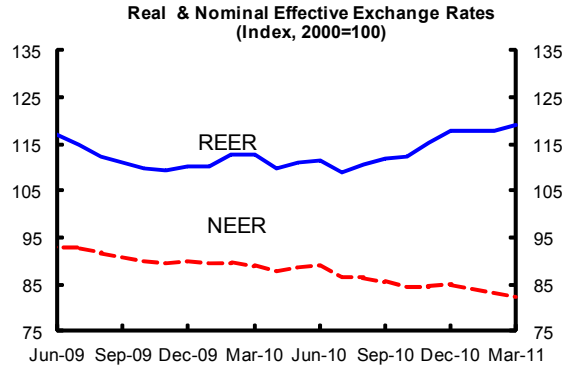
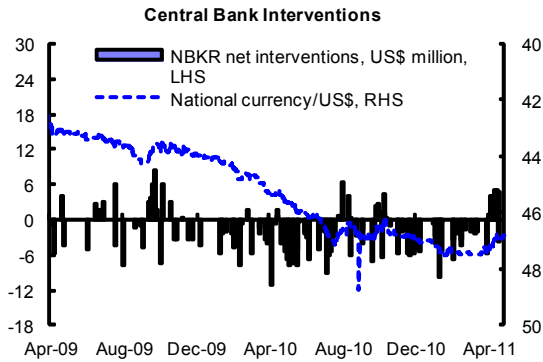


Sources: Kyrgyz authorities, and Fund staff projections.

Figure 4. Kyrgyz Republic: Monetary and Exchange Rate Developments

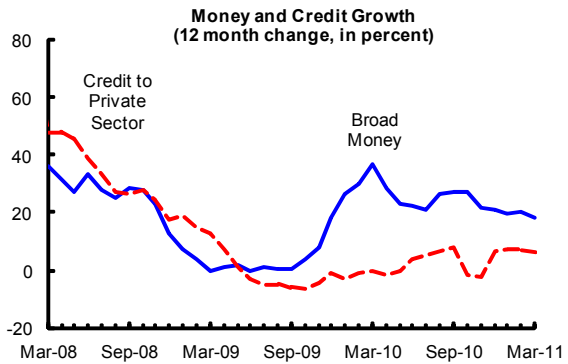
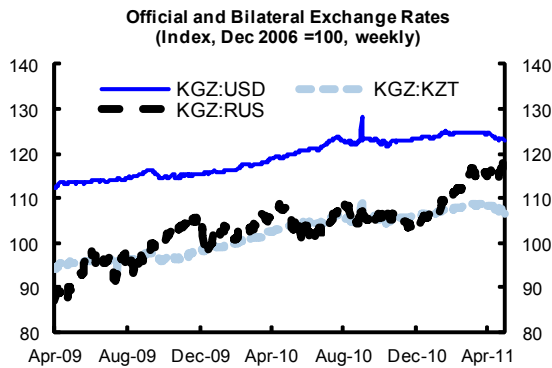
The Som has been depreciating gradually while the NBKR intervened only to smooth short-term fluctuations in exchange rate

The REER appreciated because of rapidly rising domestic inflation



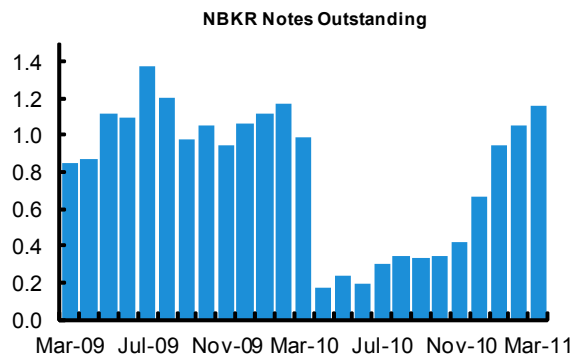
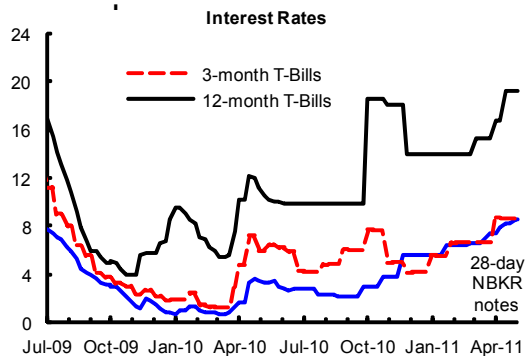
The exchange rate has been depreciating also against major trading partner currencies

Money supply growth declined from its peak in March 2010 and credit growth stabilized at low levels



Following monetary policy tightening, interest rates have been gradually increasing...

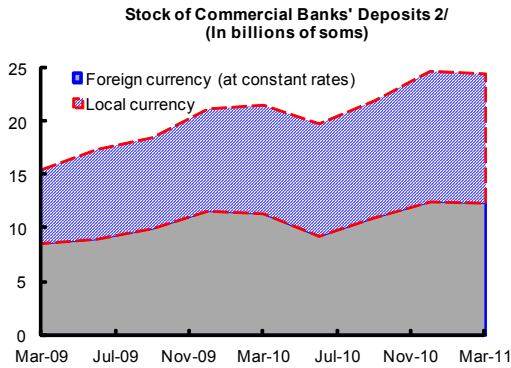
...which allowed the NBKR to withdraw liquidity from the banking sector



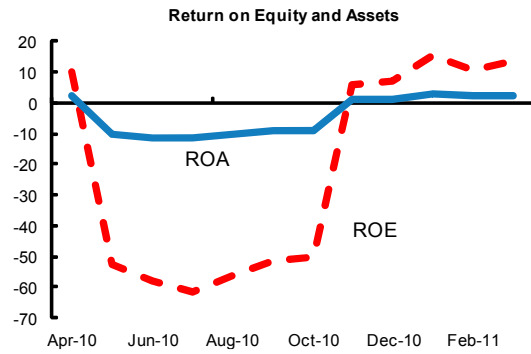
Sources: Kyrgyz authorities, and Fund staff projections.

Figure 5. Kyrgyz Republic: Financial Sector Development 1/

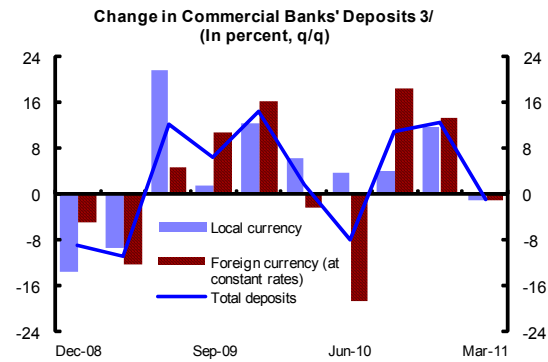
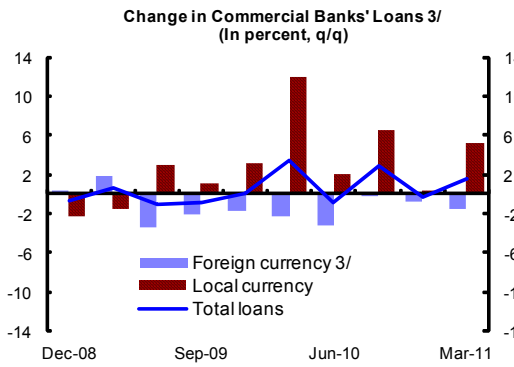
Deposit dollarization remains high



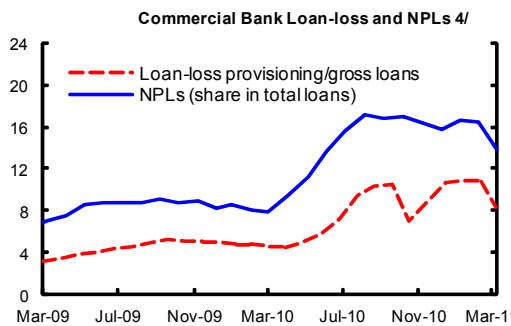
Return on equity and assets dropped substantially due to the 2010 events but have returned to positive levels recently



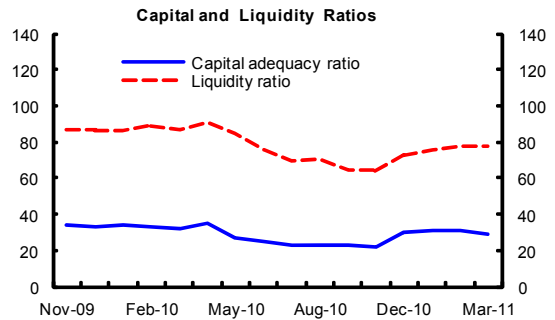
Deposits and credit remain largely stagnant



NPLs increased sharply in 2010 but have declined lately



Capital adequacy and liquidity ratios have been improving in recent months



Source: Kyrgyz authorities, Fund staff estimates and projections.

1/ Includes the problem bank—AUB.

2/ Total deposits exclude government deposits.

3/ Adjusted for changes in exchange rate.

4/ In March 2011, some nonperforming loans were transferred from Zalkar Bank to AUB and left the system.

III. POLICY DISCUSSIONS

Policy actions have been broadly consistent with the recommendations of the 2009 Article IV consultation, although there were setbacks owing to the political crisis in 2010. The fallout from the crisis has posed significant near- and medium-term challenges. Against this background medium-term policies should focus on rebalancing the policy mix to restore macroeconomic stability and rebuild policy buffers. While limited fiscal expansion in 2011 is needed to support the nascent economic recovery, consolidation in 2012 and beyond will be critical to ensure medium-term fiscal and debt sustainability and support the central bank's efforts to curb inflation. Moreover, reducing underlying vulnerabilities in the banking sector, addressing governance issues, and improving the business environment will be key to enhancing the role of the private sector in the economy and fully realizing the economy's growth potential. The authorities plan to prepare a medium-term country development strategy which would form the basis for a PRSP.

A. Medium-term objectives⁵

6. **Political stability following this year's presidential elections and a favorable external environment should allow the Kyrgyz economy to grow by 6 percent in the medium term.** With continued high oil prices, Russia and Kazakhstan—two large oil exporting countries in the region—will have positive spillovers on the region, including the Kyrgyz Republic. Agriculture, tourism, mining and textile production will be important drivers of growth. Realizing the yet untapped hydro power potential would yield additional growth dividends. Planned large infrastructure projects and a revival of private sector credit will also support the authorities' medium-term growth objectives.

7. **The authorities agreed that addressing corruption and long-standing governance problems will be instrumental in ensuring sustainable growth.**⁶ The new political landscape presents a fresh opportunity to introduce governance reforms, which are likely to generate significant immediate and long-term benefits. In addition to producing budgetary gains, reducing fiscal risks and improving the business environment, these reforms will help to instill confidence in public institutions and strengthen resilience to potential shocks.

8. **The authorities realize that despite recent progress in reducing poverty, much work remains.** During 2005–09 aggregate poverty and extreme poverty declined from 43 percent to 32 percent and from 11 percent to 3 percent, respectively. The 2010 events, followed by a large increase in inflation, have likely resulted in a partial reversal of these gains. On the other hand, wage increases for social sector employees and the planned increase in targeted cash transfers to the poor, along with expanded coverage under this

⁵ Tables 1 through 9 present all key macroeconomic data.

⁶ The Kyrgyz Republic ranks 164 out of 178 countries according to the latest transparency international corruption perception index.

program, will be mitigating factors. Emigration of the younger population has likely mitigated the adverse impact on unemployment and poverty from the political crisis last year. Strong growth in the medium term, further development of social safety nets, and improvements in governance will help to reduce poverty.

9. **Strong export-oriented growth and fiscal consolidation will help to reduce the current account deficit in the medium term.** Continued increases in gold prices and output along with strong remittance growth will further contribute to deficit reduction. However, large energy infrastructure projects, which are expected to start from 2012 and have a significant import component, as well as high food and fuel prices, will prevent the current account deficit from declining faster. Official development assistance, while slowing, will remain an important source of financing the current account deficit and will help to maintain an adequate reserves level. The planned accession to the Belarus-Kazakhstan-Russia customs union would adversely impact the volume of transit trade from China to the CIS leading to a deceleration of both import and export growth (Box 2).⁷

10. **Given a very low level of financial intermediation, further financial deepening is necessary to support economic growth and help improve monetary policy effectiveness.** Credit to GDP stood at a mere 13 percent in 2010 and is projected to increase to about 20 percent in the medium term. The authorities plan to swiftly address financial sector legacy issues and create a transparent and level playing field. This should help restore public confidence in banks. To support financial deepening, the government will increasingly involve banks in its operations, including by using their services for all government collections and payments. The authorities will also further develop banking infrastructure, primarily through the ongoing payment system reform, which will encourage the public to rely more on banking services.

11. **The authorities acknowledge the importance of an independent and effective monetary policy as the key anti-inflation instrument.** Strengthening *de facto* independence will help to boost NBKR credibility and will make combating inflation in the future less costly. The NBKR will continue to further develop the monetary policy transmission channel through its efforts to deepen the financial sector and to improve its policy toolkit. The NBKR and the government will also closely coordinate their policies and actions. In the medium term, the NBKR will focus on maintaining price stability, as the primary objective of monetary policy.

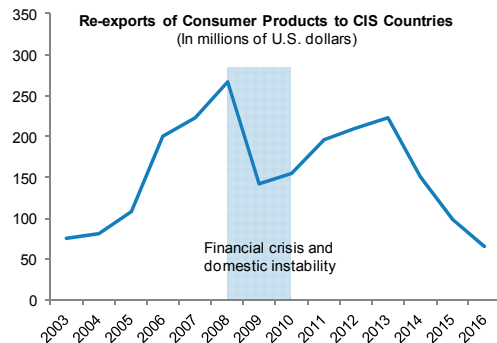
⁷ In April 2011, the authorities submitted an application to the customs union. The negotiation strategy is currently under preparation, with accession expected in about two years.

Box 2. Kyrgyz Republic: The Customs Union (CU)

The Kyrgyz Republic has submitted an application to join the Belarus-Kazakhstan-Russia CU, which became effective on July 1, 2010. Accession to the CU, which is expected in about two years, may have effects on external trade and fiscal revenues. Accession may also raise procedural issues, since the Kyrgyz Republic would be the only member of the CU that is also a member of the WTO. However, because accession discussions are at a very early stage, the effects of accession remain highly uncertain.

Joining the CU will improve external trade relations with Russia and the other CU members, but will hamper trade relations with nonmembers, most notably China. The most apparent benefit to the Kyrgyz economy would be the preservation of petroleum import supplies and prices from other CU members. The Kyrgyz textile industry may also benefit as the higher common external tariff (CET) under the CU would likely reduce textile imports from nonmember countries, notably China. There could also be an increase in foreign direct investment if (manufacturing) businesses in other CU members were to relocate to the Kyrgyz Republic to take advantage of lower labor costs. The most significant cost of accession would be the loss of transit trade from re-exporting (mostly Chinese) goods to Russia and other CIS countries, caused by the higher external tariff. The Kyrgyz Republic would lose its advantage as a cheap access route to the larger markets of Russia and other CIS countries, with which the Kyrgyz Republic has preferential trade agreements. This transit trade is estimated to have totaled US\$267 million before the effects of the international financial crisis in 2009 and domestic instability in 2010 (Figure 1).

The effects of the CU on fiscal revenues are unclear at this stage and will depend on the outcome of negotiations. The current CET is much higher than the average tariff applied by the Kyrgyz Republic, but the potential reduction in volume of the transit trade could have an adverse impact on domestic revenue collections. Furthermore, it is not yet known how revenues collected at the common customs border will be shared with the Kyrgyz Republic. Options include sharing based on the final destination or the port of entry of the imported goods, or some combination thereof. Regardless of the eventual sharing method, however, the bargaining position of the Kyrgyz Republic would be improved by efforts to increase revenues collected by customs prior to accession.



Since the Kyrgyz Republic would be the only member of the CU that is also a member of the WTO, there may be significant procedural obstacles related to accession. If the Kyrgyz Republic were to adopt the higher CET of the CU, it would have to offer a compensatory adjustment to WTO members so that the regime would not be less favorable to trade than the status quo. Typically this compensation would take the form of a reduction in particular tariff lines, but is not automatic and would require another WTO member to file a grievance against the Kyrgyz Republic. Since the other CU members have expressed interest in jointly negotiating entry to the WTO, it might be possible for the Kyrgyz Republic to renegotiate its WTO commitments as part of the entry of the other CU members to the WTO.

Tariffs of the Kyrgyz Republic and the Customs Union
(In percent)

	Kyrgyz Republic	Customs Union
Agriculture	7.9	10.8
Industry	4.3	10.8
Overall	5.1	10.6

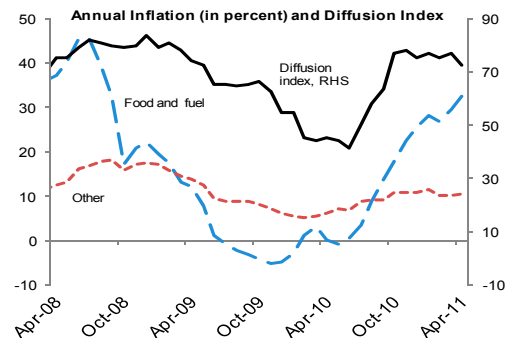
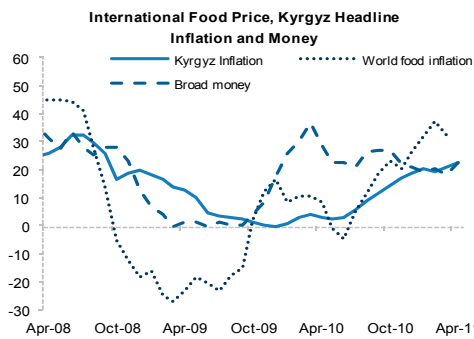
Source: Kyrgyz authorities.

B. Addressing immediate challenges to restore macroeconomic stability

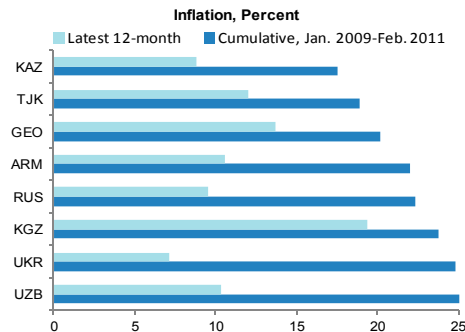
12. **The risk of continued high inflation in the remainder of the year is a concern.** Projections for international food and fuel prices combined with fiscal expansion in the second half of the year will put upward pressure on prices. The recent inflation spike was mainly driven by exogenous factors, but there have been signs that inflation expectations are rising, pushing up prices on items in the core basket as well (Box 3). However, the latest core and headline inflation developments and the expected base effect from July, 2011 onwards would help the NBKR to achieve its end-year inflation objective.

Box 3. Kyrgyz Republic: Inflation—Causes and Outlook

The surge in international food and fuel prices and political instability in 2010 explain the bulk of the recent hike in inflation.¹ Food constitutes 48 percent of the CPI basket and the Kyrgyz Republic is a net food importer. Moreover, internal unrest caused shortages and supply bottlenecks in key agricultural products. Subsequently, food contributed almost 18 percentage points to 22.6 percent headline inflation in April 2011. However, inflation started to propagate to nonfood components of the CPI basket pointing to higher inflationary pressures, thereby warranting a policy response. Based on a diffusion index, more than 50 percent of items in the basket experience price increases. More recent data suggest that prices of items other than food and fuel have started to stabilize.



The pass-through from international to domestic prices is quick and relatively complete in the Kyrgyz Republic, unlike in some neighboring countries. Cumulative inflation in the Kyrgyz Republic from end-2008 to date, the period covering two opposite episodes of rising and declining international food and fuel prices, is comparable with other countries in the region and the CIS, where the latest inflation reading is much lower than in the Kyrgyz Republic. Downward rigidity in prices is less pronounced in the Kyrgyz Republic than in most of the other countries in the region, which helps domestic inflation to drop quickly when international food and fuel prices decline.



With international food and fuel prices expected to remain high in 2011, achieving disinflation quickly will be a challenge. The fiscal expansion in 2011, especially the shift in the composition of spending from capital to current, will add to inflationary pressures. However, the recent removal of the export fuel duty by Russia, the expected recovery in agriculture, and an improved security situation along with the timely tightening of monetary policy, which appears to be already bearing fruit, are important mitigation factors.

¹In response to rising wheat prices, the Kyrgyz authorities reduced the customs duty on wheat flour in the third quarter of 2010.

*The 12-month diffusion index is calculated as the number of items in the CPI basket experiencing price increases and one-half of the items with prices unchanged divided by all items. The “unchanged” category includes items experiencing inflation of 7 percent or less based on the understanding that 7 percent inflation is a benign level of inflation for the Kyrgyz Republic. A rising index implies that an increasing number of items are experiencing above normal price increases.

13. **The NBKR agreed to stand ready to tighten monetary policy further, particularly in light of inflationary pressures stemming from the fiscal expansion in 2011** (MEFP ¶20). The actions already taken to slow reserve money growth, combined with higher reserve requirements, should translate into a deceleration of broad money growth in 2011, compatible with the projected decline in inflation. However, should the wage increase lead to renewed inflationary pressures, the NBKR will further tighten monetary policy. Tight monetary policy will also help ease exchange market pressures and limit the effect on inflation from depreciation.

14. **The approved 2011 budget includes a large wage increase and entails risks on both revenues and financing.** Following the underexecution of last year's budget, the authorities decided on a sizable wage increase for social sector workers, effective May 2011, which will add about 3 percent of GDP to the annual public sector payroll in 2011. Moreover, the authorities have continued the policy of nominal annual raises in pensions, implying an additional 0.4 percent of GDP increase in social fund expenditures. The government recently adopted specific revenue enhancing measures for this year, but there are risks that revenue projections, external financing and privatization plans may not fully materialize.⁸

15. **The authorities concurred that the expansionary 2011 budget may put additional pressures on inflation.** The salary increase helps to mitigate potential risks to social stability, but it will likely contribute to inflationary pressures.⁹ While limited fiscal expansion with a deficit of 7.6 percent of GDP in 2011 is needed to support the nascent economic recovery, the expansion needs to be moderate compared to the authorities' earlier plans. More importantly, significant fiscal consolidation in 2012 and beyond will be critical to ensure medium-term fiscal and debt sustainability and support the central bank's efforts to curb inflation.

16. **Despite a sizable wage bill increase, the magnitude of fiscal expansion this year is more moderate than earlier projections.** Because of significant under-spending in 2010 and a less expansionary fiscal stance in 2011 (largely due to windfall revenues from the gold-mining company), the authorities noted that the cumulative fiscal deficit for 2010–11 is much lower than envisaged at the time of RCF (MEFP ¶10). Recognizing absorptive capacity constraints, the authorities adjusted their capital budget in favor of an increase in the spending on wages and pensions. While some of the capital expenditures were crisis related,

⁸ These include measures to strengthen customs administration through better customs valuation, limit VAT exemptions, and increase collections from higher weight-based customs duties and taxes collected from mining companies. The wage increase is expected to generate additional personal income tax revenue.

⁹ The wage increase has important social implications, as the current salary levels for teachers and doctors are very low and barely exceed the minimum subsistence level.

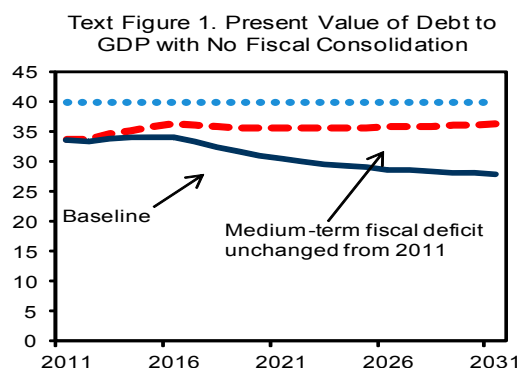
which would automatically dissipate with the completion of these projects, the increase in wages and pensions are irreversible, thus complicating the task of medium-term fiscal consolidation.

17. **The government has developed a contingency plan and will respond proactively should revenue and financing risks materialize.** In case of a shortfall in tax revenues, privatization proceeds, or external financing, and in light of limited space for mobilizing additional domestic financing, the authorities agreed to restrain spending and submit to parliament a supplementary budget with proposed cuts in current (e.g. goods and services) and, if necessary, domestic capital expenditures to maintain the agreed 2011 overall deficit. To compensate for potential shortfalls in privatization receipts, the government is considering selling its equity stake in the largest mobile phone operator company. Mindful of macroeconomic risks stemming from the fiscal expansion, the government will save the majority of windfall revenues during 2011 (MEFP ¶12).

18. **Rising commodity prices will lead to deterioration in the external sector outlook in 2011.** While exports are expected to rebound with domestic stability and in line with high gold prices, the import bill will increase, primarily because of rising commodity prices,¹⁰ but also as a result of the reopening of the borders, and rebounding economic growth, which will contribute to import volume growth. As a result, the current account deficit (excluding official transfers) in 2011 is projected to deteriorate to about 9 percent of GDP.

C. Safeguarding medium-term fiscal and debt sustainability

19. **The authorities agreed that the proposed medium-term fiscal consolidation path will help to avoid excessive debt accumulation and to achieve sustained disinflation.** The general government overall fiscal balance, excluding foreign financed energy infrastructure projects, is projected to decline from 7.6 percent in 2011 to 4.4 percent in 2014.¹¹ Adjustment of this magnitude will improve the debt



¹⁰ The increase in the fuel import price due to higher global oil prices is only partly offset by the removal of the fuel export duty by Russia.

¹¹ Foreign-financed energy infrastructure projects, which predate the current government, are excluded to adequately assess the government's medium-term fiscal adjustment effort. This narrower measure is more relevant to the domestic economy because these projects involve heavy imports, including labor. Initially the energy sector loans were intended to be provided directly to the relevant state-owned enterprises with a government guarantee. More recently, it became apparent that the ministry of finance will have to act as a borrower and subsequently onlend the resources to state-owned enterprises (SOEs). Thus, the SOEs, which are outside the defined general government sector, are effective borrowers under these projects. The projects are expected to commence in the second half of 2012.

outlook, while allowing the authorities to finance critical development and social needs. Without this adjustment, the debt outlook would deteriorate significantly with the PV of debt-to-GDP following an upward trend (see Text Figure 1 and the DSA in Supplement 1). Moreover, as economic activity rebounds, higher fiscal deficits would limit the NBKR's ability to meet its inflation objectives.

20. While counter-cyclical fiscal policies since 2009 have helped to mitigate the adverse impact of the global financial and domestic crises, medium-term fiscal consolidation is necessary to bring fiscal policy back on a sustainable path. With the economy recovering from 2011, the authorities acknowledge the importance of starting fiscal consolidation from 2012 (MEFP ¶13). The consolidation strategy, which includes measures to increase revenues and restrain expenditure growth, will aim to bring the general government deficit, excluding foreign financed energy infrastructure projects, to about 4½ percent of GDP by 2014 (Text Table 2).

Text table 2. Kyrgyz Republic: General Government Finances, 2009–14
(In percent of GDP)

	2009	2010	2011	2012	2013	2014
	Act.	Prel.	Proj.	Proj.	Proj.	Proj.
Total revenue and grants	32.1	31.7	34.6	32.3	31.6	31.2
Total revenue	27.1	28.8	30.4	30.1	30.4	30.5
Tax revenue	22.2	23.2	24.0	25.0	25.3	25.4
Nontax revenue	4.5	5.2	6.0	4.7	4.7	4.7
Capital revenue	0.3	0.4	0.4	0.4	0.4	0.4
Grants	5.1	2.9	4.3	2.1	1.1	0.7
Total expenditures and net lending	36.1	38.1	42.3	39.4	38.5	38.0
Current expenditures	28.4	32.2	34.9	32.8	31.8	31.1
Capital expenditures	5.0	5.6	6.9	5.7	5.3	4.5
Net lending 1/	2.6	0.3	0.4	0.9	1.3	2.4
Discrepancy	0.4	-0.2	0.0	0.0	0.0	0.0
Overall balance	-3.5	-6.5	-7.6	-7.1	-6.9	-6.8
Overall balance excluding energy infrastructure projects	-3.5	-6.5	-7.6	-6.2	-5.6	-4.4
Domestic fiscal balance 2/	-6.2	-5.2	-7.1	-5.8	-5.1	-5.5
Financing	3.5	6.5	7.6	7.1	6.9	6.8
External	7.4	3.2	5.2	3.7	3.9	3.8
Domestic (including privatization)	-1.5	0.5	2.4	3.4	3.0	3.0
Use of KRDF resources abroad (-, investment)	-2.4	2.8	0.0	0.0	0.0	0.0

Source: Kyrgyz authorities, and Fund staff estimates.

1/ Includes foreign financed energy infrastructure projects starting from 2012. Ministry of Finance will act as a borrower for these loans, which will be subsequently onlent to SOEs.

2/ Defined as domestic revenues minus spending excluding foreign financed PIPs.

21. The fiscal consolidation strategy is underpinned by tax policy measures and expenditure restraint. Simplified customs clearance procedures, which were introduced in 2004 to encourage “corridor” trade in Chinese goods, will be largely reversed so that the majority of imported goods are subject to a price based, instead of weight based, valuation system. This measure will encourage formalization of economic activity, expand the tax base, and help prepare the Kyrgyz Republic for joining the customs union. Other measures include (a) reforming excise taxation on tobacco and alcohol; (b) removing turnover tax

exemptions on electricity, heat, and natural gas for commercial users and VAT exemptions on communication services; and (c) moving to a contract-based tax regime for food services (MEFP ¶13). These measures (a structural benchmark) are expected to generate additional revenues in the amount of 1 percent of GDP in 2012. The authorities agreed that the 2012 public sector wage bill will reflect only the full year impact of the 2011 wage increase (MEFP ¶13). The ongoing civil service reform, which aims at downsizing the public sector, will help raise efficiency and generate additional fiscal savings (Text Tables 3 and 4).

Text table 3. Kyrgyz Republic: Fiscal Adjustment, 2012–14

Measures	Change		Comments
	2012/2011	2014/2012	
	Percent of GDP		
I. Policy adjustment	-2.4	-1.8	
Revenues	0.6	0.4	
Tax revenues	1.0	0.4	See text table 4 for details
Other revenues	-0.4	0.0	Outsourcing part of government services leads to decline in revenues collected from fees
Expenditures	-1.8	-1.4	
Current spending	-1.5	-1.7	
Wages	-0.1	-0.7	Nominal wage restraint in 2012 and modest nominal increase in 2013–14
Transfers and subsidies	-0.4	-0.4	Efficiency gains at SOEs leading to less subsidies
Social Fund expenditures	0.0	-0.1	Nominal pensions increase at a rate of projected inflation
Purchases of other goods and services	-1.1	-0.5	Efficiency gains from improved government procurement and smaller civil service
Capital spending	0.1	0.2	
Net lending	-0.5	0.0	
II. Exogenous factors	0.9	0.0	
Revenues	-2.8	-1.4	
Grants	-2.1	-1.4	Decline in donor support (2012–14)
Other revenues	-0.7	0.0	Decline in 2012 due to base effect in 2011, as the latter includes a large windfall revenue
Expenditures	-1.9	-1.5	
Interest	-0.4	0.0	Decline in 2012 due to base effect in 2011, as the latter includes arrears clearance
Externally financed capital expenditures	-1.5	-1.4	Decline in donor support (2012–14)
Total change in fiscal deficit (I+II)	-1.5	-1.8	

Source: Kyrgyz authorities; and Fund staff estimates.

Text table 4. Kyrgyz Republic: Planned Tax Policy and Administration Measures for 2012

	Revenue estimate	
	KGS Mln	Percent of GDP
Strengthening customs administration and shift from weight-based to price-based customs valuation	1,000	0.3
Introduction of combined system of excise taxation on tobacco	538	0.2
Increase of excise tax and shift to contract-based tax assessment for alcohol	591	0.2
Shift from simplified to contract-based taxation for food service companies	150	0.1
Removal of turnover tax exemption on electricity, heat and natural gas for commercial users	250	0.1
Removal of VAT exemptions on communications (internet and roaming services)	250	0.1
TOTAL	2,780	1.0

Source: Kyrgyz authorities, and Fund staff estimates.

22. **Reforming tax administration could yield significant additional revenue and help improve the business environment.** In this context, the authorities believe that focusing on large taxpayers by expanding coverage by the Large Taxpayers' Office would be particularly effective in achieving revenue gains (MEFP ¶14). The government's efforts to improve the quality and reduce the frequency of tax audits will ease the administrative burden on businesses and limit opportunities for rent seeking. Regular communication with taxpayers and enhancing access to information will raise confidence in the tax authorities and encourage taxpayer self-compliance (structural benchmark).

23. **Social spending will be safeguarded and the existing targeted social assistance system strengthened with the support of key development partners.**¹² While the recent wage and pension increases are expected to offset some of the negative impact on poverty, the authorities agreed to focus more on targeted social assistance programs. In that vein, the authorities plan to raise the Guaranteed Minimum Income (GMI) by 20 percent from June 1, 2011 and subsequently increase spending on targeted social assistance programs, i.e. the Unified Monthly Benefit (UMB) and the Monthly Social Benefit (MEFP ¶15). The government will continue to further expand the coverage under the UMB and work together with the World Bank and EU to improve targeting of social assistance programs.

24. **The government's efforts to increase transparency of public finances through improved reporting and monitoring of large SOEs will help to minimize fiscal risks.** In this context, the authorities noted the progress made under the extractive industries transparency initiative (EITI). The Kyrgyz Republic became a compliant country in March 2011 (MEFP ¶28). The largest Kyrgyz mining companies will undertake the reconciliation of their financial statements in accordance with the EITI requirements. Furthermore, the government will develop new reporting requirements for the ten largest SOEs at the first stage, which should help mobilize additional nontax revenues and reduce potential fiscal costs (structural benchmark, MEFP ¶16).

25. **Additional structural policy measures will strengthen budget preparation and improve transparency.** The authorities recognize the importance of strengthening the fiscal framework and plan to consolidate the social fund operations into the state budget and consider moving tax policy function back to the Ministry of Finance. These measures will help to improve ability of the Ministry of Finance to develop annual- and medium-term budgets (MEFP ¶17). Moreover, staff stressed—and the authorities agreed—that selection of an external auditor for the Kyrgyz Republic Development Fund (KRDF) (prior action),

¹² The Kyrgyz Republic currently has two main targeted social assistance programs: Unified Monthly Benefit (UMB) and Monthly Social Benefit (MSB) programs. The UMB is a means tested program and targets households with children. If the household income is below the Guaranteed Minimum Income (GMI) level (linked to the extreme poverty line), the family receives the difference between the actual income and the GMI. The MSB provides for cash transfers to defined categories of individuals unable to work and not entitled to pensions (e.g. children with disabilities, large families, children who lost the breadwinner).

publication of the audit report (structural benchmark), completion of its liquidation, and a commitment not to create any extra budgetary funds in the future are important measures to raise transparency of public finances and strengthen budgetary discipline (MEFP ¶30).

26. The debt outlook is expected to improve significantly in 2011 and beyond, despite large energy infrastructure borrowing (see the DSA in Supplement 1). While there are still large development needs, which will require external public borrowing going forward, the authorities are committed to maintaining debt sustainability (MEFP ¶19).¹³ To finance energy infrastructure investments and related imports, the authorities intend to borrow about US\$450 million from China, including a recently approved US\$208 million loan over the next four to five years.¹⁴ The terms of the Chinese loans are expected to be marginally nonconcessional with a grant element of nearly 34 percent and will therefore be incorporated in the ECF-supported program under a (tied) nonconcessional debt limit. At the same time, they have cleared approximately US\$14.4 million in arrears to Russia to pave the way for debt relief of about US\$194 million, which will likely be finalized in 2011.¹⁵ The authorities also reached an agreement with the government of Turkey in April 2011 for debt relief of approximately US\$50 million and have agreed with the government of Belarus to restructure debt of US\$207,649. They have contacted, and are awaiting a response from, the governments of Korea and China to clear arrears totaling about US\$7.6 million.¹⁶ The return of economic growth and the programmed fiscal consolidation in the medium term will

¹³ Total public debt in 2012–14 rises by 2.4 percent of GDP, which merely reflects a gradual, albeit small, increase in the share of domestic debt in total public debt in line with the projected development of the domestic market.

¹⁴ These energy infrastructure projects will expand the potential for exporting electricity, improve the reliability of the transmission system and ensure a smooth supply of electricity to remote parts of the country. Neighboring Uzbekistan has repeatedly indicated its intention to withdraw from the regional power grid, which would leave the southern part of the Kyrgyz Republic without electricity, given that the only way to supply electricity to the south is through the Uzbek electricity grid.

¹⁵ Under the debt-for-equity swap agreement signed between the previous Kyrgyz administration and the Russian authorities in 2009, the Russian side agreed to relinquish claims on the Kyrgyz Republic in the amount of US\$193.5 million in exchange for a 100 percent stake in two state-owned companies in the Kyrgyz Republic. However, in early 2010, the Russian side called into question the implementation of the agreement and declared the outstanding debt disputed. Since then the parties have been in close consultations to resolve this issue and a settlement is expected in 2011, as also assumed in the previous DSA.

¹⁶ The precise timing of the Turkish debt relief is still to be determined, but it is assumed that it will become effective in 2011. The authorities only recently became aware of the Belarusian debt and took prompt action to resolve it. The arrears to China and Korea have existed since the Agreed Minutes were signed on March 11, 2005 within the Paris Club framework. In March of this year, official letters were sent to the governments of China and Korea by the MOF requesting negotiations to restructure those arrears, but no replies have been received so far. No penalties or fines are accruing on these arrears.

further improve the debt outlook. Development and adoption of a medium-term debt management strategy (MTDS) will guide the authorities in their future borrowing decisions (structural benchmark, MEFP ¶19).

D. Ensuring financial sector stability and supporting financial deepening¹⁷

27. **Staff and the authorities agreed that developments in the banking sector after the political upheaval last year exposed shortcomings in the bank resolution framework and the NBKR's *de facto* lack of independence.** The experience has demonstrated that the central bank is susceptible to political influence. The deficient legal framework for problem bank resolution, and frequent interference by the courts have prevented the NBKR from taking prompt and resolute actions to deal with the banks placed under official control. In addition, bank supervisors lack adequate legal protection from prosecution for actions taken in performance of their official duties. Staff and the authorities agreed that reforms are needed to address weaknesses in the legal framework for bank resolution, including by limiting the role of the judiciary and providing adequate legal protection for NBKR supervision staff (structural benchmark, MEFP ¶26). As parliamentary confirmation of the acting chairperson of the NBKR failed recently, staff encouraged the authorities to expedite the appointment of the NBKR chair.¹⁸

28. **The resolution of AUB and the four banks currently under conservatorship remains incomplete.** A recently concluded forensic audit suggested that AUB was used to conduct large scale criminal activities, and that it was likely insolvent even before the April 2010 events. The resolution process so far has involved a split of the balance sheet into AUB (bad bank) and the newly created Zalkar Bank (good bank). However, the new bank's balance sheet was not "clean" at its creation, making it less attractive to a prospective buyer, and the authorities have agreed to take resolute actions to deal with these legacy issues (MEFP ¶23). While Zalkar is not considered to be systemic, staff noted that resolution in line with international best practices would help to rebuild the NBKR's credibility and lay the groundwork for a financial system that is better able to support economic growth.¹⁹ Along these lines, the authorities are in the process of commissioning a financial audit of Zalkar Bank (prior action). Staff recommended that the audit results inform a resolution strategy (structural benchmark):

¹⁷ Selected issues paper I provides an assessment of how the banking sector fared during the crisis and of the challenges ahead.

¹⁸ An NBKR chairperson must be nominated by the president and confirmed by the parliament.

¹⁹ AUB/Zalkar is no longer considered systemic because (i) its share of private deposits has fallen from 44 percent at end-2009 to Zalkar's 2.7 percent in January 2011; (ii) its interconnections with other banks is minor; and (iii) the services it provides can be provided by other components of the system.

- If Zalkar is confirmed to be solvent, it should be sold as a going concern to a reputable bank. The authorities preferred to open the door to acquirers other than banks to increase the chance of a successful privatization. Staff responded that the significant risk of a repeat of the circumstances surrounding the failure of AUB was the main reason to recommend limiting the sale of Zalkar to a reputable bank. However, staff noted that if no such buyer comes forward within the specified timeframe, Zalkar should be liquidated and any interested investors would be able to purchase assets and liabilities of Zalkar through the liquidation process.
- If the audit results determine that Zalkar is insolvent, bankruptcy proceedings should be commenced.²⁰

With respect to the four banks under conservatorship, the authorities noted that no further actions can be taken until pending litigation is resolved. The delays suggest that at least some of these banks will no longer be viable by the time the court cases are resolved, and these banks will likely eventually need to be liquidated.

29. **The authorities highlighted that the rest of the banking system seems to have successfully weathered the 2010 downturn and prospects are improving, but also agreed that capital buffers should be rebuilt, particularly with respect to the largest state-owned bank.** Its balance sheet more than doubled between December 2009 and March 2011 (partly because of the acquisition of some large loans from AUB), and the bank is now among the largest in the system. There was agreement that, as the bank's loan portfolio matures, it is likely that performance will deteriorate, and thus capital buffers should be rebuilt, while asset growth should be restrained with supervisory measures. The authorities cautioned that the bank was to play a critical role in channeling loans to entrepreneurs who suffered damage in the south, and therefore some growth in assets should be allowed. They agreed to start preparations for its privatization (structural benchmark, MEFP ¶23).

30. **Staff and authorities agreed that the Special Bank Refinancing Fund (SBRF), which has made the NBKR more susceptible to political interference, should be wound down** (MEFP ¶25). The SBRF was set up by a resolution of the NBKR Board in 2009 to provide loans to commercial banks and micro finance institutions. While the initial capital injections were provided by the NBKR, the government recently provided funding to the SBRF for highly concessional onlending to farmers. The existence of such a vehicle has allowed the government to interfere in the NBKR's activities, including for the purpose of financing the budget. Therefore, the plan to announce the SBRF liquidation process (prior action) and subsequently refund the portions to the respective contributors (structural benchmark), will help further strengthen the NBKR's *de facto* independence. The authorities also support the view that the NBKR should not be used as a financing source for public or private uses.

²⁰ The current projections assume recapitalization of Zalkar Bank by the government, financed through the issuance of domestic securities (KGS 1.3 billion).

E. Structural reforms to improve the business environment and strengthen competitiveness

31. **Imperfect enforcement of laws and regulations is the main constraint on the business environment.** Although business climate reforms are quite advanced, as evidenced by the Kyrgyz Republic’s favorable rankings (e.g. ranked 44 according to the World Bank “Doing Business” survey), governance and corruption problems have been preventing the country from fully benefiting from this improved regulatory environment. Tackling these longstanding problems will be vital to promote private sector activity and achieve inclusive and sustainable growth. Moreover, the Kyrgyz Republic would benefit from reforms to strengthen property rights, further cut red tape, and create a level playing field for all businesses (Box 4).

32. **Exchange rate flexibility has helped to cushion the impact of external shocks and will be important for maintaining competitiveness going forward.** The exchange rate came under pressure in 2008 and the NBKR allowed the som to depreciate against the U.S. dollar by more than 25 percent in 12 months since August 2008. Staff’s findings suggest that the exchange rate is broadly in line with fundamentals. While the macroeconomic balance approach and the external sustainability approach indicate a small undervaluation, the equilibrium real exchange rate approach indicates a small overvaluation. Overall, the results suggest a small undervaluation of 2.9 percent on average (see selected issues paper II for details). Improving productivity through market-oriented reforms should bolster the competitiveness of the Kyrgyz economy. According to the World Economic Forum Global Competitiveness Report 2011, the Kyrgyz Republic is ranked 121 out of 139 countries.

33. **Energy sector reforms would not only remove an important constraint on growth, but also create an important driver for growth in the medium-term.** The energy sector still remains in a poor condition with unreliable supplies, especially during the winter season. Below cost-recovery tariff levels, extremely high technical and commercial losses, and poor governance lead to high quasi-fiscal deficits. Initial efforts to address these challenges have failed and eroded the public confidence in the reform process.²¹ The ongoing efforts focus on increasing transparency and efficiency of the largest energy companies with the assistance from key development partners in light of the Fund’s limited expertise in energy sector issues (MEFP ¶29).

²¹ Starting from 2009 the previous Kyrgyz authorities embarked on comprehensive reforms in the energy sector which included (i) two-round increase in electricity tariffs for all end-users in 2010, which would have resulted in a cumulative growth in the household electricity tariffs of 171 percent; (ii) privatization of six large energy companies—with two of them completed in early 2010—the interim government annulled the privatization and suspended the privatization program altogether; (iii) wage and pension supplements to compensate for the tariff increase; and (iv) new public investments in power generation (Kambarata 2 project) and transmission (Datka-Kemin project). However, such a colossal tariff increase announced at the dawn of the global economic crisis, led to massive protests and the ouster of the previous regime. Consequently, the interim government returned the energy tariffs to their previous levels, while maintaining wage and pension supplements.

Box 4. Kyrgyz Republic: Business Environment

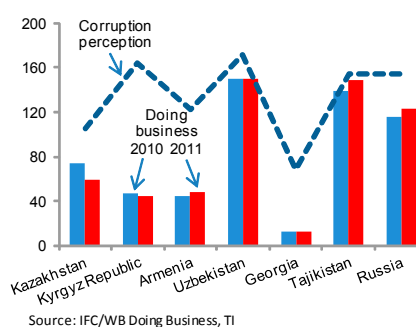
While the Kyrgyz Republic has made important strides to improve standard indicators of the business climate, the situation on the ground does not yet reflect these efforts. Registration formalities (seal, publication, notarization, inspection, and other requirements) have been simplified and the processes of starting a business, registering property, and protecting investors, received high ratings in the 2011 *Doing Business* survey. However, the good performance in *Doing Business* reforms did not translate into an actual improvement of the business environment. Most amended laws and regulations are not implemented or implemented poorly. The Kyrgyz Republic's Corruption Perception Index has deteriorated in recent years, which has put a heavy burden on businesses and has undermined the trust in the public sector. Although anticorruption legislation was put in place with the assistance of key development partners, its enforcement remains problematic. Customs procedures are burdensome, which encourages corruption, while restricting trade.

Kyrgyz Republic: Doing Business Ratings

	2010	2011
Ease of Doing Business rank	47	44
Starting a business	14	14
Dealing with construction permits	46	43
Registering property	19	17
Getting credit	14	15
Protecting investors	12	12
Paying taxes	156	150
Trading across borders	155	156
Enforcing contracts	54	54
Closing a business	139	138

Source: IFC/WB, Doing Business 2011.

Doing Business and Corruption Ratings, 2010–11



Source: IFC/WB Doing Business, TI

Competitiveness Indicators



Source: WEF, Global Competitiveness Report 2010-2011; 1-best, 139-worst

Weak institutions are also a constraining factor. According to the *Global Competitiveness Report*, the Kyrgyz Republic ranks 121 out of 139 countries. Property rights and public trust in politicians, judicial independence and efficiency of the legal framework, strength of auditing and reporting standards, and protection of minority shareholders' interests are among the main areas that remain major obstacles. Local competition is weak and the effectiveness of the anti-monopoly policy is limited.

Going forward, the authorities need to translate the good legal and regulatory framework into tangible improvements on the ground. Efforts are already underway to address the perception of corruption and strengthening institutions. The authorities need to identify, with the assistance from the development partners, and eliminate (instead of amending) redundant regulations and rules. Crime and disorder that followed the unrest in 2010 should effectively and continuously be dealt with. The government also needs to simplify customs regulations easing export and import procedures.

IV. THE NEW ECF ARRANGEMENT

Access and financing

34. **The ECF-supported program is expected to catalyze significant donor assistance, which will help to finance the current account deficits in 2011 and the medium term and maintain reserves at comfortable levels.** Although reserve coverage is expected to decline slightly (by 0.3 months of imports) from 2011, it will stabilize at 3.8 months of imports in 2013. The projected level of international reserves after donor support meets the majority of reserve adequacy indicators. However, as a small open economy, the Kyrgyz Republic is particularly vulnerable to exogenous shocks (selected issues paper III). Anticipated external official development assistance in 2011 will total about US\$271 million, including a US\$107 million loan from the Eurasian Economic Community's Anti-Crisis Fund (Text Table 5). Donor financing appears to be frontloaded, as a significant part of the financing earmarked for 2010 has been delayed to 2011.²² The proposed access of 75 percent of quota (SDR 66.6 million), to be disbursed in equal semiannual installments with the first disbursement expected in June 2011 (Table 10), would finance the residual balance of payments gap. Given the prohibition on central bank financing of the budget, constraints in domestic market financing, and the urgent budgetary need until donor disbursements commence, the authorities have requested that both 2011 disbursements be channeled to the budget, i.e. disbursed to the treasury account in the NBKR. The Kyrgyz Republic's capacity to repay the Fund is adequate (Table 11) and the DSA concludes that the country remains at a moderate risk of debt distress.

Text table 5. Kyrgyz Republic: Balance of Payment Financing Gaps, 2011–14

	2011		2012		2013		2014	
	US\$ Mn	Percent of GDP	US\$ Mn	Percent of GDP	US\$ Mn	Percent of GDP	US\$ Mn	Percent of GDP
Financing Gap	271.2	5.2	149.0	2.6	117.8	1.9	74.8	1.1
Identified budget support	241.4	4.7	-	-	-	-	-	-
<i>World Bank</i>	30.0	0.6	-	-	-	-	-	-
<i>Asian Development Bank</i>	50.6	1.0	-	-	-	-	-	-
<i>EURASEC Anti Crisis Fund</i>	106.7	2.1	-	-	-	-	-	-
<i>European Union</i>	44.1	0.9	-	-	-	-	-	-
<i>Other</i>	10.0	0.2	-	-	-	-	-	-
Unidentified budget support	-	-	119.3	2.1	88.1	1.4	60.0	0.9
IMF ECF purchase	29.8	0.6	29.7	0.5	29.7	0.5	14.8	0.2

Source: Kyrgyz authorities, and Fund staff estimates.

²² The budget support disbursements of the Asian Development Bank, the ACF, and part of the EU Food Security grant, earmarked for 2010, were delayed to 2011.

Monitoring, safeguards, and risks

35. **Program monitoring will be performed on a semi-annual basis. The first review is expected to be completed by November 30, 2011 based on continuous and end-June 2011 quantitative performance criteria and the second review is expected to be completed by April 16, 2012 based on continuous and end-December 2011 quantitative performance criteria.** Conditionality will focus on the critical aspects of the Fund-supported program and will include quantitative performance criteria on (i) net international reserves; (ii) net domestic assets; (iii) the overall cash deficit; and (iv) external nonconcessional borrowing and external arrears. Indicative targets apply to (i) reserve money; (ii) state government tax revenues; and (iii) spending on targeted social assistance. On the structural side, conditionality will focus on tax policy and administration reform, strengthening management of SOEs, transparency of public finances, completion of problem bank resolution, bolstering banking supervision, and central bank independence (MEFP Tables 1 and 2).

36. **A safeguards assessment is in progress and will be completed no later than by the time of the first review.** The last safeguards assessment was completed in 2009. The authorities plan to update the February 6, 2010 memorandum of understanding between the ministry of finance and the NKBR on the respective responsibilities for servicing their respective obligations to the IMF (MEFP ¶34).

37. **Risks to the Fund-supported program are considerable, especially in the near term.** Potential for renewed political turbulence remains high in the run up to the presidential elections later this year and the foundation for the current coalition government remains fragile. The adoption of tax policy reforms, which contain unpopular measures, could be delayed jeopardizing medium-term fiscal consolidation. The resolution of problem banks may be postponed further while delays in addressing growing vulnerabilities in other systemically important banks could destabilize the financial sector leading to fiscal costs and a decline in credit. However, strong conditionality under the ECF arrangement in macrocritical areas mitigates these risks.

V. STAFF APPRAISAL

38. **In the aftermath of the deep political crisis last year, the Kyrgyz authorities' immediate priority should be to restore macroeconomic stability.** While there are early signs of recovery from the economic contraction in 2010, the situation remains fragile with inflation at more than 20 percent. Staff noted that the initially planned fiscal expansion in 2011 should be scaled back and contingency measures prepared, and that consolidation in 2012 and beyond will be critical. Moreover, reducing underlying vulnerabilities in the

banking sector, addressing governance issues, and improving the business environment will be key to enhancing the role of the private sector in the economy and fully realizing the economy's growth potential.

39. **Fiscal consolidation in 2012 and beyond will be critical to ensure medium-term fiscal and debt sustainability and support the central bank's disinflation objectives.** The consolidation strategy is underpinned by strong tax policy and administration measures, which will yield about 1 percent of GDP in 2012, and prudent spending plans. Exercising nominal wage restraint in 2012 and moderate wage and pension growth in subsequent years will also be needed to support fiscal consolidation. Other current spending should be adjusted downward through better public financial management, while social spending should be safeguarded and focused on further developing targeted assistance programs. Staff noted that the civil service reform will allow for a smoother fiscal consolidation, as it is likely to generate significant efficiency gains. Reform efforts to strengthen budget preparation and improve transparency through the consolidation of the social fund into the state budget, return of tax policy to the ministry of finance and better monitoring of SOEs, will also be critical.

40. **Sound monetary policy supported by the flexible exchange rate regime will be key to contain inflation.** Staff welcomes the recent monetary tightening, but the NBKR should stand ready to tighten further in light of inflationary pressures stemming from the fiscal expansion in 2011. To further develop the effectiveness of monetary policy, the NBKR should strengthen its policy toolkit and work toward deepening the financial sector. Staff notes that the exchange rate is broadly in line with fundamentals and the flexible exchange rate regime, which has served the Kyrgyz Republic well, should be maintained.

41. **Staff urges the authorities to take the necessary actions on the banking sector without delay.** AUB/Zalkar resolution should proceed promptly once the results of the audit are known. Resolute action on problem banks, along with passage of amendments to the banking laws to strengthen the NBKR's supervisory independence and address weaknesses in the resolution framework, are critical to a well-functioning banking sector and will help to provide a sound basis for further financial deepening. Capital buffers should be rebuilt, particularly for the largest state-owned bank, and its growth rate contained through supervisory measures. The vigorous pursuit to recover the assets wrongfully taken from AUB would also send a strong signal of a break with the past.

42. **Potential accession to the Belarus-Kazakhstan-Russia customs union creates risks for economic growth and for future budgets.** Membership in the customs union may significantly reduce shuttle trade from China and lead to lower growth and tax revenues at customs. Therefore, revamping the Kyrgyz tax system, by expanding the tax base and strengthening administration, should become a priority in this highly uncertain context. Increasing customs revenues would help strengthen the bargaining position of the Kyrgyz Republic during the accession negotiations.

43. **Staff welcomes the authorities' cautious approach to external borrowing and efforts to resolve outstanding bilateral debt disputes.** A cautious approach is needed to maintain the Kyrgyz Republic's lower debt vulnerabilities as indicated by the moderate external risk of debt distress rating. The clearance of arrears to Russia, the restructuring of the debt to Belarus, and efforts to clear arrears to China and Korea are important developments in this regard. While substantial prospective external borrowings, staggered over time, are not likely to jeopardize the country's debt outlook, any future large-scale borrowing decisions should carefully consider potential growth dividends.

44. **The recent political changes provide an opportunity to address governance issues.** A similar but forgone opportunity presented itself after the "Tulip Revolution" in 2005. The shift to a parliamentary form of government, which is new to the Kyrgyz Republic, may slow down the reform effort, simply because parliamentary involvement in the policy-making process and the diverse nature of the coalition may prolong decision-making. It is therefore important for the new government to instill confidence and obtain popular support for important reforms.

45. **Staff welcomes the authorities' commitment to phase out the SBRF and not to create any new development/investment vehicle without prior consultation with IMF staff.** The use of the SBRF for directed lending and government financing has hampered central bank operations. The creation and operation of the KRDF was a major obstacle for completing reviews under the ESF because of the substantial governance issues involved. The authorities are aware that failure to observe this commitment could jeopardize the completion of future program reviews.

46. **The proposed ECF arrangement entails significant risks, but strong conditionality in macrocritical areas, including prior actions, should provide sufficient safeguards.** While the period ahead is marked by uncertainty and political fragility, the Fund-supported program will be important to help the authorities to put the economy back on a sustainable path and secure much-needed donor support. Based on the authorities' good track record under the RCF and the strong medium-term policies and structural program, staff supports the authorities' request for an ECF arrangement and the request to channel the first two disbursements to the budget. It is proposed that the next Article IV consultations be held on the standard 24-month cycle, in accordance with the Decision on Article IV Consultation Cycles (Decision No. 14747-(10/96), (9/28/2010)), as amended.

Table 1. Kyrgyz Republic: Selected Economic Indicators, 2008–16

	2008	2009	2010	2011	2012	2013	2014	2015	2016
	Act.	Act.	Prel.	Proj.					
Nominal GDP (in billions of soms)	188.0	201.2	212.2	250.5	286.0	320.1	360.5	401.7	444.9
Nominal GDP (in millions of U.S. dollars)	5,131	4,683	4,615	5,187	5,695	6,187	6,766	7,319	7,870
Real GDP (growth in percent)	7.6	2.9	-1.4	6.0	6.0	6.0	5.8	5.8	5.7
Nongold real GDP (growth in percent)	5.4	3.4	-2.1	5.8	6.1	6.1	5.9	5.9	5.8
GDP per capita (in U.S. dollars)	972	880	863	960	1,044	1,123	1,216	1,302	1,386
Consumer prices (12-month percent change, eop)	20.1	0.0	18.9	13.0	8.0	7.5	7.1	6.0	6.0
Consumer prices (12-month percent change, average)	24.5	6.8	7.8	20.0	8.7	7.5	7.5	6.6	6.0
Investment and savings (in percent of GDP)									
Investment	20.3	23.0	24.9	26.5	26.0	26.0	26.5	25.3	25.5
Public	4.1	5.0	5.6	6.9	5.7	5.3	4.5	4.9	5.0
Private	16.2	17.9	19.3	19.6	20.4	20.7	22.1	20.3	20.5
Savings	12.3	23.6	22.7	17.8	17.9	19.9	21.1	20.5	20.9
Public	5.1	3.8	-0.4	-0.2	-0.5	-0.3	0.0	1.9	2.8
Private	7.2	19.8	23.2	18.0	18.4	20.2	21.1	18.6	18.1
Savings-investment balance	-8.1	0.7	-2.1	-8.7	-8.2	-6.1	-5.4	-4.7	-4.6
General government finances (in percent of GDP) 1/									
Total revenue and grants	29.9	32.1	31.7	34.6	32.3	31.6	31.2	33.6	33.6
Of which: Tax revenue	23.0	22.2	23.2	24.0	25.0	25.3	25.4	25.6	25.8
Total expenditure (including net lending)	29.2	36.1	38.1	42.3	39.4	38.5	38.0	37.7	36.9
Of which: Current expenditure	24.8	28.4	32.2	34.9	32.8	31.8	31.1	31.7	30.9
Capital expenditure	4.1	5.0	5.6	6.9	5.7	5.3	4.5	4.9	5.0
Overall fiscal balance	0.0	-3.5	-6.5	-7.6	-7.1	-6.9	-6.8	-4.2	-3.2
Primary balance	0.8	-2.7	-5.6	-6.3	-6.2	-6.0	-5.9	-3.3	-2.4
Primary balance excluding grants	-1.1	-7.8	-8.6	-10.6	-8.3	-7.1	-6.6	-4.6	-3.7
Overall balance excluding energy infrastructure projects	0.0	-3.5	-6.5	-7.6	-6.2	-5.6	-4.4	-3.1	-2.2
Total public debt 2/	48.5	58.0	62.6	56.5	56.1	57.5	58.4	58.2	57.8
Banking sector									
Reserve money (percent change, eop)	11.3	18.9	18.4	16.4	17.0	17.3	18.1	18.0	17.3
Broad money (percent change, eop)	12.6	20.9	21.1	15.7	16.2	19.7	20.5	19.8	19.1
Credit to private sector (percent change, eop)	26.4	-2.8	6.3	18.0	17.9	27.2	21.0	21.2	20.1
Credit to private sector (in percent of GDP)	14.2	12.9	13.0	13.0	13.4	15.2	16.4	17.8	19.3
Velocity of broad money 3/	4.0	3.5	3.1	3.1	3.1	2.9	2.7	2.5	2.3
Interest rate 4/	19.2	1.9	5.5	...	...	...	...	...	...
External sector									
Current account balance (in percent of GDP)	-8.1	0.7	-2.1	-8.7	-8.2	-6.1	-5.4	-4.7	-4.6
Export of goods and services (in millions of U.S. dollars)	3,037	2,695	2,529	3,133	3,407	3,684	4,221	4,748	5,324
Export growth (percent change)	35.4	-11.3	-6.2	23.9	8.7	8.1	14.6	12.5	12.1
Import of goods and services (in millions of U.S. dollars)	4,747	3,683	3,904	4,948	5,400	5,763	6,393	7,050	7,754
Import growth (percent change)	47.5	-22.4	6.0	26.7	9.1	6.7	10.9	10.3	10.0
Gross International reserves (in millions of U.S. dollars)	1,222	1,584	1,716	1,862	1,889	2,042	2,244	2,462	2,651
Gross reserves (months of next year imports, eop)	4.0	4.9	4.2	4.1	3.9	3.8	3.8	3.8	3.8
External public debt outstanding (in percent of GDP)	41.2	52.8	57.3	51.0	50.3	50.5	50.1	49.4	48.9
External public debt service-to-export ratio (in percent)	2.4	3.2	3.6	2.8	2.5	2.4	2.3	2.2	2.3
Memorandum items:									
Exchange rate (soms per U.S. dollar, average)	36.6	43.0	46.0	...	...	...	...	...	...
Real effective exchange rate (2000=100) (average)	121.7	117.7	112.1	...	...	...	...	...	...
Gold related tax receipts of the general government (percent of GDP)	0.8	1.3	2.2	2.1	...	...	...	...	...

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

1/ General government comprises State Government, Social Fund and Development Fund (starting from September 2009) finances.

State government comprises central and local governments.

2/ Calculated at end-period exchange rates.

3/ 12-month GDP over end-period broad money.

4/ Interest rate on 3-month treasury bills.

Table 2. Kyrgyz Republic: Balance of Payments, 2008–16
(In millions of U.S. dollars)

	2008	2009	2010	2011	2012	2013	2014	2015	2016
	Act.	Act.								Prel.	Proj.
Current account balance 1/ excluding transfers	-413	30	-98	-453	-464	-380	-364	-347	-363
	-1,890	-1,177	-1,489	-2,012	-2,245	-2,374	-2,678	-2,753	-2,938
Trade balance	-1,612	-978	-1,144	-1,640	-1,849	-1,973	-2,163	-2,348	-2,571
Exports, fob	2,141	1,835	1,837	2,271	2,429	2,609	2,920	3,214	3,526
CIS countries	1,279	894	842	1,063	1,139	1,207	1,350	1,469	1,589
Of which: energy products	269	180	74	88	90	98	102	111	115
Of which: Re-exports of consumer goods	267	141	154	196	210	223	151	98	65
Non-CIS countries	863	941	995	1,207	1,291	1,403	1,571	1,745	1,938
Of which: Gold	463	529	668	852	908	975	1,036	1,100	1,168
Of which: Re-exports of oil products	126	46	43	0	0	0	0	0	0
Imports, fob	3,754	2,814	2,981	3,911	4,278	4,582	5,083	5,562	6,097
CIS countries	2,025	1,594	1,590	2,200	2,247	2,308	2,518	2,770	3,021
Of which: Energy (including for re-exports)	1,081	722	772	1,145	1,207	1,242	1,334	1,433	1,538
Non-CIS countries	1,728	1,220	1,391	1,711	2,031	2,274	2,565	2,792	3,076
Of which: Goods for re-exports	243	128	140	178	191	202	137	89	59
Services	-97	-9	-231	-175	-145	-106	-10	47	141
Receipts	896	860	693	863	977	1,074	1,301	1,534	1,798
Payments	-993	-869	-923	-1,037	-1,122	-1,181	-1,310	-1,487	-1,657
Income	-180	-190	-114	-198	-251	-295	-506	-451	-508
Interest payments	-29	-44	-36	-58	-36	-44	-53	-60	-68
Other net income	-151	-146	-78	-140	-215	-251	-453	-391	-440
Current Transfers (net) 1/ Of which: Private	1,477	1,208	1,391	1,559	1,780	1,994	2,314	2,406	2,575
	1,431	1,013	1,313	1,550	1,782	1,996	2,315	2,408	2,576
Capital Account	-18	14	10	289	-1	-21	-46	-11	-9
Official	72	84	129	369	79	59	34	69	71
Private	-89	-70	-120	-80	-80	-80	-80	-80	-80
Financial account	145	376	318	60	362	457	555	528	535
Commercial banks	15	-106	-4	-10	15	15	15	15	15
Medium- and long-term loans, net	34	283	74	-149	107	182	257	208	205
Disbursement 1/ Of which: Loan financed PIP	92	408	219	202	253	306	380	340	372
Of which: Energy and other investments financed by China and Eurasec	38	70	158	144	138	146	122	140	161
...	...	...	0	0	50	79	160	81	81
Amortization	-58	-125	-145	-351	-146	-124	-123	-132	-168
Foreign direct investment	265	190	234	219	240	260	283	305	315
Portfolio investment 2/ Other (including SDR allocation)	-26	-21	103	0	0	0	0	0	0
Net short-term flows	0	131	0	0	0	0	0	0	0
Net short-term flows	-134	-100	-79	0	0	0	0	0	0
Errors and omissions	386	-130	-127	0	0	0	0	0	0
Overall balance	100	291	102	-104	-104	57	145	170	163
Financing	-100	-291	-102	104	104	-57	-145	-170	-163
Net international reserves	-103	-291	-102	-167	-45	-174	-219	-239	-210
Gross official reserves (-, increase)	-121	-293	-112	-146	-27	-153	-202	-217	-189
IMF (net)	18	2	10	-21	-18	-21	-17	-22	-21
Exceptional Financing (including arrears)	3	0	0	0	0	0	0	0	0
Financing gap 1/ Memorandum items:	0	0	0	271	149	118	75	70	47
GDP (in millions of U.S. dollars)	5,131	4,683	4,615	5,187	5,695	6,187	6,766	7,319	7,870
Current account balance (percent of GDP)	-8.1	0.7	-2.1	-8.7	-8.2	-6.1	-5.4	-4.7	-4.6
Current account balance excl. official transfers (percent of GDP)	-8.9	-3.5	-3.8	-8.9	-8.1	-6.1	-5.4	-4.7	-4.6
Growth of exports of GNFS (volume, percent)	17.4	-3.1	-20.0	9.7	9.8	9.0	8.8	7.4	7.0
Growth of imports of GNFS (volume, percent)	23.2	-13.2	-15.8	8.3	9.9	9.1	8.4	7.8	7.6
Terms of trade (goods, percentage change)	-4.0	4.0	-8.8	-6.0	0.2	1.5	0.6	0.4	0.4
Gold price (U.S. dollars per ounce)	871.7	973	1,225	1,427	1,446	1,478	1,530	1,596	1,670
External Public Debt (in millions of U.S. dollars) 3/ as percent of GDP	2,113	2,472	2,644	2,647	2,867	3,126	3,390	3,619	3,852
Public debt service-to-exports ratio 3/ 4/	41.2	52.8	57.3	51.0	50.3	50.5	50.1	49.4	48.9
Gross reserves 5/ in months of subsequent year's imports	2.4	3.2	3.6	2.8	2.5	2.4	2.3	2.2	2.3
	1,222	1,584	1,716	1,862	1,889	2,042	2,244	2,462	2,651
	4.0	4.9	4.2	4.1	3.9	3.8	3.8	3.8	3.8

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

1/ Budget support is included in the financing gap (see text table 5).

2/ Includes return of KRDF investments abroad.

3/ Public and publicly-guaranteed debt.

4/ Net of rescheduling.

5/ Valued at end-period exchange rates. The discrepancy between the difference in year-end stocks and the change in reserves under financing is caused by movements in prices and exchange rates.

Table 3. Kyrgyz Republic: NBKR Accounts, 2009–12

	2009		2010				2011			2012	
	Dec. Act.	Mar. Act.	Jun. Act.	Sep. Act.	Dec. Act.	Mar. Act.	Jun. Proj.	Sep. Proj.	Dec. Proj.	Dec. Proj.	
	(In millions of soms)										
Net foreign assets	54,308	58,115	57,626	63,026	65,127	69,733	73,317	75,531	77,497	81,050	
Net international reserves	62,329	66,129	65,657	71,135	73,475	78,297	81,834	84,153	86,207	89,759	
Long-term foreign liabilities	-8,154	-8,138	-8,175	-8,501	-8,482	-8,761	-8,717	-8,824	-8,915	-8,915	
Other foreign assets	133	124	144	392	134	197	199	202	205	205	
Net domestic assets	-13,248	-18,760	-16,620	-18,920	-16,529	-24,617	-22,927	-23,067	-20,927	-14,847	
Net claims on general government	-1,644	-6,878	-5,931	-5,147	-2,053	-5,850	-2,790	-2,340	-895	1,305	
<i>Of which:</i> Total government deposits (including FX deposits)	-3,976	-4,415	-2,566	-10,311	-7,243	-10,904	-7,695	-8,580	-7,152	-4,743	
<i>Of which:</i> Securitized government debt 1/	2,908	3,164	2,995	3,022	3,027	2,873	2,659	3,965	3,957	3,624	
Claims on commercial banks	-1,264	-854	-188	52	87	-1,575	-2,208	-1,867	-1,676	-1,666	
<i>Of which:</i> NBKR Notes	-1,060	-986	-200	-335	-668	-1,163	-1,645	-1,307	-1,150	-986	
Claims of other financial corporations	-1,476	-1,477	-1,545	-1,027	-523	-687	-746	-875	-521	-250	
Other items net	-8,864	-9,551	-8,956	-12,797	-14,040	-16,505	-17,183	-17,985	-17,835	-14,236	
Reserve money	41,061	39,355	41,005	44,107	48,597	45,117	50,390	52,464	56,571	66,203	
Currency in circulation	35,739	34,510	36,943	39,992	43,290	40,846	45,620	47,498	51,216	58,259	
Commercial banks' reserves	5,322	4,845	4,063	4,115	5,307	4,270	4,770	4,966	5,355	7,944	
<i>Of which:</i> Required reserves	3,526	4,057	2,270	2,452	2,174	2,737	2,509	2,635	2,791	3,426	
	(Contribution to reserve money growth, in percent) 2/										
Net foreign assets	42.4	9.3	8.1	21.2	26.3	9.5	16.9	21.4	25.5	6.3	
Net domestic assets	-23.5	-13.4	-8.2	-13.8	-8.0	-16.6	-13.2	-13.5	-9.0	10.7	
<i>Of which:</i> Net claims on general government	-6.4	-12.7	-10.4	-8.5	-1.0	-7.8	-1.5	-0.6	2.4	3.9	
Reserve money	18.9	-4.2	-0.1	7.4	18.4	-7.2	3.7	8.0	16.4	17.0	
<i>Of which:</i> Currency in circulation	14.3	-3.0	2.9	10.4	18.4	-5.0	4.8	8.7	16.3	12.4	
<i>Memorandum items:</i>											
Reserve money (12-month change, in percent)	18.9	32.9	20.6	21.7	18.4	14.6	22.9	18.9	16.4	17.0	
Gross International Reserves (in millions of U.S. dollars)	1,584	1,617	1,564	1,676	1,716	1,798	1,825	1,847	1,862	1,889	
Net international reserves (in millions of U.S. dollars)	1,414	1,462	1,415	1,525	1,526	1,622	1,644	1,671	1,678	1,727	
Exchange rate, Som per USD, end of period	44.1	45.2	46.4	46.6	47.1	...	...	...	...	...

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

1/ Includes the problem bank capitalization through the issuance of a domestic bond in the amount of KGS 1300 million. This makes a change in net claims on government and domestic financing between monetary and fiscal tables noncomparable.

2/ Contribution is defined as change of asset stock relative to previous end-year reserve money stock (in percent).

Table 4. Kyrgyz Republic: Monetary Survey, 2009–12

	2009		2010			2011			2012	
	Dec. Act.	Mar. Act.	Jun. Act.	Sept. Act.	Dec. Act.	Mar. Act.	Jun. Proj.	Sept. Proj.	Dec. Proj.	Dec. Proj.
	(In millions of soms)									
Net foreign assets	60,114	63,697	61,419	69,254	71,425	76,377	80,057	82,418	84,530	87,318
<i>Of which:</i> Long-term foreign liabilities (-)	-2,291	-2,343	-2,380	-2,386	-2,386	-2,387	-2,452	-2,482	-2,508	-2,508
Net domestic assets	-2,988	-7,364	-4,287	-6,345	-2,217	-9,729	-8,503	-7,661	-4,483	5,697
Domestic credit	19,960	15,791	16,986	19,017	23,379	20,361	25,765	27,408	30,437	42,356
Net claims on general government	-5,992	-10,927	-9,649	-8,538	-4,195	-7,997	-5,509	-4,309	-2,111	3,996
Credit to the rest of the economy	25,952	26,718	26,635	27,555	27,575	28,358	31,273	31,717	32,547	38,360
<i>Of which:</i> In forex	15,474	14,980	14,592	14,633	14,599	14,758	16,244	16,443	16,841	20,331
Other items net	-22,948	-23,155	-21,274	-25,362	-25,596	-30,090	-34,268	-35,070	-34,920	-36,659
Broad money (M2X)	57,126	56,333	57,132	62,909	69,208	66,648	71,554	74,757	80,047	93,015
<i>Of which:</i>										
Broad money, excluding forex deposits (M2)	43,490	42,767	45,916	49,387	53,745	51,159	56,098	58,697	63,224	72,935
Currency held by the public	33,882	32,563	35,341	38,389	41,471	39,014	43,679	45,477	49,037	54,948
Total domestic currency deposit liabilities	9,608	10,204	10,575	10,998	12,274	12,145	12,418	13,220	14,188	17,987
	(Contribution to broad money growth, in percent) 1/									
Net foreign assets	43.0	6.3	2.3	16.0	19.8	7.2	12.5	15.9	18.9	3.5
Net domestic assets	-26.5	-7.7	-2.3	-5.9	1.3	-10.9	-9.1	-7.9	-3.3	12.7
Domestic credit	-8.3	-7.3	-5.2	-1.7	6.0	-4.4	3.4	5.8	10.2	14.9
Net claims on general government	-6.7	-8.6	-6.4	-4.5	3.1	-5.5	-1.9	-0.2	3.0	7.6
Credit to the rest of the economy	-1.6	1.3	1.2	2.8	2.8	1.1	5.3	6.0	7.2	7.3
Other items (net)	-18.2	-0.4	2.9	-4.2	-4.6	-6.5	-12.5	-13.7	-13.5	-2.2
Broad money (M2X)	20.9	-1.4	0.0	10.1	21.1	-3.7	3.4	8.0	15.7	16.2
<i>Of which:</i>										
Broad money, excluding forex deposits (M2)	13.8	-1.3	4.2	10.3	18.0	-3.7	3.4	7.2	13.7	12.1
Currency held by the public	9.5	-2.3	2.6	7.9	13.3	-3.5	3.2	5.8	10.9	7.4
Total deposit liabilities	4.2	1.0	1.7	2.4	4.7	-0.2	0.2	1.4	2.8	4.7
<i>Memorandum items:</i>										
Broad money (M2X) (12-month change, in percent)	20.9	37.0	22.6	27.0	21.1	18.3	25.2	18.8	15.7	16.2
Credit to the rest of the economy (12-month change, in percent)	-2.8	-0.2	3.8	7.8	6.3	6.1	17.4	15.1	18.0	17.9
Credit to the rest of the economy (in percent of GDP)	12.9	12.9	12.8	13.2	13.0	12.9	13.8	12.9	13.0	13.4
M2X velocity 2/	3.5	3.7	3.7	3.3	3.1	3.3	3.2	3.3	3.1	3.1
M2X multiplier	1.39	1.43	1.39	1.43	1.42	1.48	1.42	1.42	1.41	1.41
Dollarization indicators (in percent)										
Loan dollarization	59.6	56.1	54.8	53.1	52.9	52.0	51.9	51.8	51.7	51.5
Deposit dollarization	58.7	57.1	51.5	55.1	55.7	56.0	55.4	54.8	54.2	52.7

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

1/ Contribution is defined as change of asset stock relative to previous end-year broad money stock (in percent).

2/ 12-month GDP over end-period broad money.

Table 5. Kyrgyz Republic: General Government Finances, 2009–14

	2009 1/	2010					2011					2012	2013	2014
	Act.	Q1 Prel.	Q2 Prel.	Q3 Prel.	Q4 Prel.	Year Prel.	Q1 Proj.	Q2 Proj.	Q3 Proj.	Q4 Proj.	Year Proj.	Year Proj.	Year Proj.	Year Proj.
	(In millions of soms, unless indicated otherwise)													
Total revenue and grants	64,678	15,284	15,769	16,287	19,953	67,293	18,280	21,736	21,724	25,036	86,777	92,243	100,995	112,388
Total revenue	54,431	14,502	14,446	14,868	17,300	61,117	15,877	19,965	19,046	21,209	76,098	86,107	97,315	109,823
Current revenue	53,749	14,375	14,258	14,510	17,087	60,230	15,718	19,798	18,792	20,767	75,075	84,960	96,049	108,416
Tax revenue	44,645	12,256	11,207	12,076	13,694	49,233	13,286	14,288	15,460	17,131	60,165	71,544	80,883	91,579
Income tax	10,261	4,202	3,137	2,884	2,887	13,110	4,213	3,730	3,826	4,346	16,114	18,475	20,997	23,645
VAT 1/	13,467	3,108	3,134	3,826	4,534	14,602	3,858	4,348	4,827	5,092	18,125	21,119	23,825	27,138
Excises	1,669	370	367	449	504	1,689	494	556	583	600	2,233	3,200	3,626	4,088
Customs	4,139	871	896	1,109	1,472	4,348	998	1,386	1,561	1,856	5,801	7,837	8,646	9,878
Land tax	917	199	144	222	235	799	159	151	248	360	919	1,056	1,215	1,458
Road tax and Emergency Fund 1/	403	13	13	23	-6	42	0	0	0	0	0	0	0	0
Retail sales tax 1/	0	0	0	0	0	0	0	0	0	0	0	0	0	0
New turnover tax 1/	3,933	1,100	811	848	939	3,699	919	1,035	1,166	1,272	4,392	5,479	6,105	6,867
Social Fund (excl. gov. contribution)	8,547	2,148	2,392	2,391	2,939	9,870	2,323	2,644	2,735	3,343	11,046	12,688	14,529	16,273
Other	1,309	244	314	325	190	1,073	321	438	514	262	1,535	1,689	1,942	2,234
Nontax revenue 2/	9,104	2,119	3,051	2,434	3,393	10,997	2,432	5,509	3,333	3,636	14,910	13,417	15,165	16,836
Capital revenue	682	128	188	358	213	887	159	167	254	443	1,023	1,147	1,266	1,407
Grants	10,247	782	1,323	1,419	2,653	6,176	2,403	1,771	2,678	3,827	10,679	6,136	3,680	2,565
Program grants	7,653	397	966	678	1,713	3,753	1,581	492	1,123	2,376	5,571	3,229	1,712	1,865
PIP grants	2,595	385	357	741	940	2,423	822	1,279	1,555	1,451	5,108	2,907	1,968	701
Total expenditure (including net lending and KRDF)	72,561	15,004	18,310	21,704	25,723	80,741	16,882	26,787	30,770	31,449	105,888	112,550	123,079	136,902
Total expenditure (excluding net lending)	71,599	15,242	18,021	21,068	25,844	80,175	16,951	26,910	29,642	31,261	104,765	110,039	118,992	128,393
Current expenditure	57,076	12,908	16,655	17,025	21,658	68,246	14,106	22,902	23,266	27,124	87,399	93,813	101,885	112,271
Wages	14,669	3,063	4,853	3,758	5,229	16,903	3,887	8,278	7,298	8,343	27,806	31,490	34,639	37,237
Transfers and subsidies	6,850	2,231	2,284	2,052	2,746	9,313	1,689	3,384	2,486	2,724	10,283	10,679	11,424	12,001
Social Fund expenditures	13,361	4,170	4,501	4,855	5,466	18,993	4,755	5,904	5,786	6,499	22,944	26,261	29,413	32,628
Interest	1,612	415	526	490	381	1,812	420	1,260	681	880	3,240	2,668	2,909	3,265
Purchases of other goods and services	20,583	3,030	4,491	5,870	7,836	21,226	3,357	4,076	7,015	8,678	23,126	22,714	23,500	27,140
Capital expenditure	10,159	2,334	1,366	4,043	4,186	11,929	2,845	4,008	6,376	4,137	17,365	16,226	17,107	16,122
Domestically financed capital expenditure	4,582	535	754	842	1,179	3,310	420	1,021	2,084	1,825	5,350	6,397	7,566	8,944
Foreign financed PIP loans	2,982	1,414	255	2,459	2,068	6,196	1,602	1,708	2,736	861	6,907	6,923	7,573	6,478
Foreign financed PIP grants	2,595	385	357	741	940	2,423	822	1,279	1,555	1,451	5,108	2,907	1,968	701
Net lending 3/	962	-239	289	636	-121	565	-69	-123	1,128	188	1,123	2,511	4,087	8,509
KRDF (total spending) 4/	4,364	0	0	0	0	0	0	0	0	0	0	0	0	0
Discrepancy	830	67	-377	548	-582	-345	0	0	0	0	0	0	0	0
Primary balance excluding grants	-15,689	-19	-3,715	-5,799	-8,624	-18,157	-585	-5,562	-11,042	-9,360	-26,550	-23,775	-22,855	-23,814
Primary balance	-5,442	762	-2,392	-4,380	-5,971	-11,981	1,818	-3,791	-8,364	-5,533	-15,870	-17,639	-19,175	-21,249
Overall balance	-7,053	347	-2,918	-4,869	-6,352	-13,792	1,399	-5,051	-9,046	-6,413	-19,111	-20,308	-22,084	-24,514
Overall balance excluding energy infrastructure projects	-7,053	347	-2,918	-4,869	-6,352	-13,792	1,399	-5,051	-9,046	-6,413	-19,111	-17,796	-17,997	-16,005
Total financing	7,053	-347	2,918	4,869	6,352	13,792	-1,399	5,051	9,046	6,413	19,110	20,308	22,084	24,514
External financing	14,877	1,199	-326	3,802	2,142	6,818	2,131	1,603	7,655	1,680	13,069	10,478	12,436	13,660
Public investment program (PIP)	2,982	1,414	255	2,459	2,068	6,196	1,602	1,708	2,736	861	6,907	6,923	7,573	6,478
Program support loans	13,367	0	0	1,547	735	2,282	807	721	5,185	1,535	8,248	3,516	3,104	1,598
China financed energy loans	0	0	0	0	0	0	0	0	0	0	0	2,511	4,087	8,509
Total amortization	-1,472	-215	-581	-204	-661	-1,660	-278	-826	-266	-716	-2,086	-2,472	-2,327	-2,926
Domestic financing	-2,839	-5,597	1,260	1,061	4,195	918	-3,802	2,488	1,200	2,198	2,084	6,106	6,069	7,166
NBKR	-1,827	-5,889	1,018	758	3,028	-1,085	-3,797	3,060	-850	1,445	-142	2,200	600	0
Commercial banks	-1,160	299	331	327	1,248	2,205	-4	-572	2,050	753	2,227	3,906	5,469	7,166
Nonbank	148	-8	-89	-25	-80	-202	0	0	0	0	0	0	0	0
Privatization	-253	138	13	6	15	173	272	960	190	2,535	3,957	3,724	3,579	3,688
Use of KRDF investments abroad 5/	-4,732	3,912	1,971	0	0	5,883	0	0	0	0	0	0	0	0

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

1/ In 2009, the road, emergency and retail taxes have been abolished, the VAT tax rate reduced from 20 to 12 percent, and a new turnover tax introduced.

Median turnover tax rate was reduced from 2.5 percent to 2 percent from January 1, 2010.

2/ Completion of the ongoing investigation involving confiscated assets of the previous government's officials in 2010 could yield additional nontax revenues in 2011.

3/ Includes costs of problem bank through the issuance of a domestic bond in the amount of KGS 1,300 million in 2011. From 2012 through 2014 includes onlending for China financed energy projects.

4/ Unaudited data.

5/ Negative numbers indicate outflow of assets overseas.

Table 6. Kyrgyz Republic: General Government Finances, 2009–14

	2009	2010				2011					2012	2013	2014	
	Act.	Q1 Prel.	Q2 Prel.	Q3 Prel.	Q4 Prel.	Year Prel.	Q1 Proj.	Q2 Proj.	Q3 Proj.	Q4 Proj.	Year Proj.	Year Proj.	Year Proj.	Year Proj.
	(In percent of GDP)													
Total revenue and grants	32.1	39.4	36.9	25.9	29.5	31.7	39.2	43.3	26.7	34.6	34.6	32.3	31.6	31.2
Total revenue	27.1	37.4	33.8	23.6	25.6	28.8	34.1	39.8	23.4	29.3	30.4	30.1	30.4	30.5
Current revenue	26.7	37.0	33.4	23.1	25.2	28.4	33.7	39.5	23.1	28.7	30.0	29.7	30.0	30.1
Tax revenue	22.2	31.6	26.2	19.2	20.2	23.2	28.5	28.5	19.0	23.7	24.0	25.0	25.3	25.4
Income tax	5.1	10.8	7.3	4.6	4.3	6.2	9.0	7.4	4.7	6.0	6.4	6.5	6.6	6.6
VAT	6.7	8.0	7.3	6.1	6.7	6.9	8.3	8.7	5.9	7.0	7.2	7.4	7.4	7.5
Excises	0.8	1.0	0.9	0.7	0.7	0.8	1.1	1.1	0.7	0.8	0.9	1.1	1.1	1.1
Customs	2.1	2.2	2.1	1.8	2.2	2.0	2.1	2.8	1.9	2.6	2.3	2.7	2.7	2.7
Land tax	0.5	0.5	0.3	0.4	0.3	0.4	0.3	0.3	0.3	0.5	0.4	0.4	0.4	0.4
Road tax and Emergency Fund	0.2	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
Retail sales tax	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
New turnover tax	2.0	2.8	1.9	1.3	1.4	1.7	2.0	2.1	1.4	1.8	1.8	1.9	1.9	1.9
Social Fund (excluding government contribution)	4.2	5.5	5.6	3.8	4.3	4.7	5.0	5.3	3.4	4.6	4.4	4.4	4.5	4.5
Other	0.7	0.6	0.7	0.5	0.3	0.5	0.7	0.9	0.6	0.4	0.6	0.6	0.6	0.6
Nontax revenue	4.5	5.5	7.1	3.9	5.0	5.2	5.2	11.0	4.1	5.0	6.0	4.7	4.7	4.7
Capital revenue	0.3	0.3	0.4	0.6	0.3	0.4	0.3	0.3	0.3	0.6	0.4	0.4	0.4	0.4
Grants	5.1	2.0	3.1	2.3	3.9	2.9	5.2	3.5	3.3	5.3	4.3	2.1	1.1	0.7
Program grants	3.8	1.0	2.3	1.1	2.5	1.8	3.4	1.0	1.4	3.3	2.2	1.1	0.5	0.5
PIP grants	1.3	1.0	0.8	1.2	1.4	1.1	1.8	2.5	1.9	2.0	2.0	1.0	0.6	0.2
Total expenditure (including net lending and KRDF)	36.1	38.7	42.9	34.5	38.0	38.1	36.2	53.4	37.8	43.5	42.3	39.4	38.5	38.0
Total expenditure (excluding net lending)	35.6	39.3	42.2	33.5	38.2	37.8	36.4	53.6	36.4	43.2	41.8	38.5	37.2	35.6
Current expenditure	28.4	33.3	39.0	27.0	32.0	32.2	30.3	45.7	28.5	37.5	34.9	32.8	31.8	31.1
Wages	7.3	7.9	11.4	6.0	7.7	8.0	8.3	16.5	9.0	11.5	11.1	11.0	10.8	10.3
Transfers and subsidies	3.4	5.7	5.3	3.3	4.1	4.4	3.6	6.7	3.1	3.8	4.1	3.7	3.6	3.3
Social Fund expenditures	6.6	10.7	10.5	7.7	8.1	9.0	10.2	11.8	7.1	9.0	9.2	9.2	9.2	9.1
Interest	0.8	1.1	1.2	0.8	0.6	0.9	0.9	2.5	0.8	1.2	1.3	0.9	0.9	0.9
Purchases of other goods and services	10.2	7.8	10.5	9.3	11.6	10.0	7.2	8.1	8.6	12.0	9.2	7.9	7.3	7.5
Capital expenditure	5.0	6.0	3.2	6.4	6.2	5.6	6.1	8.0	7.8	5.7	6.9	5.7	5.3	4.5
Domestically financed capital expenditure	2.3	1.4	1.8	1.3	1.7	1.6	0.9	2.0	2.6	2.5	2.1	2.2	2.4	2.5
Foreign financed PIP loans	1.5	3.6	0.6	3.9	3.1	2.9	3.4	3.4	3.4	1.2	2.8	2.4	2.4	1.8
Foreign financed PIP grants	1.3	1.0	0.8	1.2	1.4	1.1	1.8	2.5	1.9	2.0	2.0	1.0	0.6	0.2
Net lending	0.5	-0.6	0.7	1.0	-0.2	0.3	-0.1	-0.2	1.4	0.3	0.4	0.9	1.3	2.4
KRDF (total spending)	2.2	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
Discrepancy	0.4	0.2	-0.9	0.9	-0.9	-0.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Primary balance excluding grants	-7.8	0.0	-8.7	-9.2	-12.7	-8.6	-1.3	-11.1	-13.5	-12.9	-10.6	-8.3	-7.1	-6.6
Primary balance	-2.7	2.0	-5.6	-7.0	-8.8	-5.6	3.9	-7.6	-10.3	-7.7	-6.3	-6.2	-6.0	-5.9
Overall balance	-3.5	0.9	-6.8	-7.7	-9.4	-6.5	3.0	-10.1	-11.1	-8.9	-7.6	-7.1	-6.9	-6.8
Overall Balance excluding energy infrastructure projects	-3.5	0.9	-6.8	-7.7	-9.4	-6.5	3.0	-10.1	-11.1	-8.9	-7.6	-6.2	-5.6	-4.4
Total financing	3.5	-0.9	6.8	7.7	9.4	6.5	-3.0	10.1	11.1	8.9	7.6	7.1	6.9	6.8
External financing	7.4	3.1	-0.8	6.0	3.2	3.2	4.6	3.2	9.4	2.3	5.2	3.7	3.9	3.8
Public investment program (PIP)	1.5	3.6	0.6	3.9	3.1	2.9	3.4	3.4	3.4	1.2	2.8	2.4	2.4	1.8
Program support loans	6.6	0.0	0.0	2.5	1.1	1.1	1.7	1.4	6.4	2.1	3.3	1.2	1.0	0.4
China financed energy loans	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.9	1.3	2.4
Total amortization	-0.7	-0.6	-1.4	-0.3	-1.0	-0.8	-0.6	-1.6	-0.3	-1.0	-0.8	-0.9	-0.7	-0.8
Domestic financing	-1.4	-14.4	2.9	1.7	6.2	0.4	-8.2	5.0	1.5	3.0	0.8	2.1	1.9	2.0
NBKR	-0.9	-15.2	2.4	1.2	4.5	-0.5	-8.2	6.1	-1.0	2.0	-0.1	0.8	0.2	0.0
Commercial banks	-0.6	0.8	0.8	0.5	1.8	1.0	0.0	-1.1	2.5	1.0	0.9	1.4	1.7	2.0
Nonbank	0.1	0.0	-0.2	0.0	-0.1	-0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Privatization	-0.1	0.4	0.0	0.0	0.0	0.1	0.6	1.9	0.2	3.5	1.6	1.3	1.1	1.0
Use of KRDF investments abroad	-2.4	10.1	4.6	0.0	0.0	2.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0

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

Table 7. Kyrgyz Republic: State Government Finances, 2009–14

	2009		2010					2011					2012	2013	2014
	Act.	Q1	Q2	Q3	Q4	Year	Q1	Q2	Q3	Q4	Year	Year	Year	Year	
		Prel.	Prel.	Prel.	Prel.	Prel.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	
(In millions of soms, unless indicated otherwise)															
Total revenue and grants	55,719	13,066	13,302	13,830	16,967	57,165	15,900	19,034	18,931	21,635	75,501	79,312	86,212	95,849	
Total revenue	45,471	12,284	11,979	12,411	14,314	50,989	13,497	17,263	16,253	17,808	64,821	73,176	82,532	93,283	
Current revenue	45,159	12,227	11,866	12,118	14,148	50,360	13,395	17,154	16,057	17,423	64,029	72,272	81,520	92,143	
Tax revenue	36,098	10,108	8,815	9,685	10,755	39,363	10,963	11,644	12,724	13,788	49,119	58,855	66,355	75,307	
Income tax	10,261	4,202	3,137	2,884	2,887	13,110	4,213	3,730	3,826	4,346	16,114	18,475	20,997	23,645	
VAT	13,467	3,108	3,134	3,826	4,534	14,602	3,858	4,348	4,827	5,092	18,125	21,119	23,825	27,138	
Excises	1,669	370	367	449	504	1,689	494	556	583	600	2,233	3,200	3,626	4,088	
Customs	4,139	871	896	1,109	1,472	4,348	998	1,386	1,561	1,856	5,801	7,837	8,646	9,878	
Land tax	917	199	144	222	235	799	159	151	248	360	919	1,056	1,215	1,458	
Road tax and Emergency Fund	403	13	13	23	-6	42	0	0	0	0	0	0	0	0	
Retail sales tax	0	0	0	0	0	0	0	0	0	0	0	0	0	0	
New turnover tax	3,933	1,100	811	848	939	3,699	919	1,035	1,166	1,272	4,392	5,479	6,105	6,867	
Other	1,309	244	314	325	190	1,073	321	438	514	262	1,535	1,689	1,942	2,234	
Nontax revenue	9,061	2,119	3,051	2,434	3,393	10,997	2,432	5,509	3,333	3,636	14,910	13,417	15,165	16,836	
Capital revenue	312	57	113	293	166	629	101	109	197	385	792	905	1,012	1,140	
Grants	10,247	782	1,323	1,419	2,653	6,176	2,403	1,771	2,678	3,827	10,679	6,136	3,680	2,565	
Program grants	7,653	397	966	678	1,713	3,753	1,581	492	1,123	2,376	5,571	3,229	1,712	1,865	
PIP grants	2,595	385	357	741	940	2,423	822	1,279	1,555	1,451	5,108	2,907	1,968	701	
Total expenditure (including net lending)	71,789	12,640	15,906	18,776	22,307	69,630	14,606	24,757	27,427	27,895	94,685	100,704	109,550	121,761	
Total expenditure	70,826	12,879	15,617	18,140	22,428	69,064	14,675	24,880	26,299	27,707	93,562	98,193	105,463	113,252	
Current expenditure	48,365	10,545	14,251	14,097	18,242	57,135	11,830	20,872	19,923	23,571	76,196	81,966	88,356	97,129	
Wages and Social Fund contributions	16,911	3,491	5,535	4,200	5,884	19,110	4,507	10,370	7,760	9,321	31,958	36,758	40,522	43,657	
Transfers and subsidies	6,850	2,231	2,284	2,052	2,746	9,313	1,689	3,384	2,486	2,724	10,283	10,679	11,424	12,001	
Transfers to Social Fund	2,410	1,378	1,416	1,485	1,395	5,674	1,858	1,783	1,980	1,968	7,589	9,147	10,001	11,066	
Interest	1,612	415	526	490	381	1,812	420	1,260	681	880	3,240	2,668	2,909	3,265	
Purchases of other goods and services	20,583	3,030	4,491	5,870	7,836	21,226	3,357	4,076	7,015	8,678	23,126	22,714	23,500	27,140	
Capital expenditure (including PIP)	10,159	2,334	1,366	4,043	4,186	11,929	2,845	4,008	6,376	4,137	17,365	16,226	17,107	16,122	
Domestically financed capital expenditure	4,582	535	754	842	1,179	3,310	420	1,021	2,084	1,825	5,350	6,397	7,566	8,944	
Foreign financed PIP loans	2,982	1,414	255	2,459	2,068	6,196	1,602	1,708	2,736	861	6,907	6,923	7,573	6,478	
Foreign financed PIP grants	2,595	385	357	741	940	2,423	822	1,279	1,555	1,451	5,108	2,907	1,968	701	
Financial balance	-15,108	187	-2,315	-4,310	-5,461	-11,899	1,225	-5,845	-7,368	-6,072	-18,061	-18,880	-19,251	-17,403	
Net lending	962	-239	289	636	-121	565	-69	-123	1,128	188	1,123	2,511	4,087	8,509	
Transfer to the KRDF	12,302	0	0	0	0	0	0	0	0	0	0	0	0	0	
Discrepancy	-156	-182	924	125	-537	330	0	0	0	0	0	0	0	0	
Primary balance	-14,614	659	-1,155	-4,332	-5,495	-10,323	1,714	-4,463	-7,814	-5,380	-15,943	-18,723	-20,429	-22,647	
Primary balance excluding grants	-24,862	-123	-2,478	-5,751	-8,148	-16,499	-689	-6,234	-10,492	-9,207	-26,623	-24,859	-24,109	-25,213	
Overall balance	-16,226	244	-1,681	-4,821	-5,877	-12,135	1,294	-5,723	-8,495	-6,260	-19,184	-21,391	-23,337	-25,912	
Overall Balance excluding energy infrastructure projects	-16,226	244	-1,681	-4,821	-5,877	-12,135	1,294	-5,723	-8,495	-6,260	-19,184	-18,880	-19,251	-17,403	
Total financing	16,226	-244	1,681	4,821	5,877	12,135	-1,294	5,723	8,495	6,260	19,184	21,391	23,337	25,912	
External financing	14,877	1,199	-326	3,802	2,142	6,818	2,131	1,603	7,655	1,680	13,069	10,478	12,436	13,660	
Public investment program (PIP)	2,982	1,414	255	2,459	2,068	6,196	1,602	1,708	2,736	861	6,907	6,923	7,573	6,478	
Program support loans	13,367	0	0	1,547	735	2,282	807	721	5,185	1,535	8,248	3,516	3,104	1,598	
China financed energy loans	0	0	0	0	0	0	0	0	0	0	0	2,511	4,087	8,509	
Total amortization	-1,472	-215	-581	-204	-661	-1,660	-278	-826	-266	-716	-2,086	-2,472	-2,327	-2,926	
Domestic financing	1,602	169	1,605	-8,252	3,722	-2,757	-3,697	3,160	650	2,045	2,158	7,190	7,323	8,564	
NBKR	794	-774	1,806	-7,720	3,028	-3,660	-3,797	3,060	-850	1,445	-142	2,200	600	0	
Commercial banks	659	951	-112	-508	774	1,106	100	100	1,500	600	2,300	4,990	6,723	8,564	
Nonbank	148	-8	-89	-25	-80	-202	0	0	0	0	0	0	0	0	
Use of KRDF resources	...	-1,751	389	9,265	-2	7,901	0	0	0	0	...	...	...	...
Privatization 1/	-253	138	13	6	15	173	272	960	190	2,535	3,957	3,724	3,579	3,688	

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

1/ Negative number means unwinding of previous privatizations.

Table 8. Kyrgyz Republic: State Government Finances, 2009–14

	2009		2010					2011					2012	2013	2014
	Act.	Q1 Prel.	Q2 Prel.	Q3 Prel.	Q4 Prel.	Year Prel.	Q1 Proj.	Q2 Proj.	Q3 Proj.	Q4 Proj.	Year Proj.	Year Proj.	Year Proj.	Year Proj.	
	(In percent of GDP)														
Total revenue and grants	27.7	33.7	31.1	22.0	25.1	26.9	34.1	37.9	23.2	29.9	30.1	27.7	26.9	26.6	
Total revenue	22.6	31.7	28.0	19.7	21.1	24.0	29.0	34.4	19.9	24.6	25.9	25.6	25.8	25.9	
Current revenue	22.4	31.5	27.8	19.3	20.9	23.7	28.8	34.2	19.7	24.1	25.6	25.3	25.5	25.6	
Tax revenue	17.9	26.0	20.6	15.4	15.9	18.6	23.5	23.2	15.6	19.1	19.6	20.6	20.7	20.9	
Income tax	5.1	10.8	7.3	4.6	4.3	6.2	9.0	7.4	4.7	6.0	6.4	6.5	6.6	6.6	
VAT	6.7	8.0	7.3	6.1	6.7	6.9	8.3	8.7	5.9	7.0	7.2	7.4	7.4	7.5	
Excises	0.8	1.0	0.9	0.7	0.7	0.8	1.1	1.1	0.7	0.8	0.9	1.1	1.1	1.1	
Customs	2.1	2.2	2.1	1.8	2.2	2.0	2.1	2.8	1.9	2.6	2.3	2.7	2.7	2.7	
Land tax	0.5	0.5	0.3	0.4	0.3	0.4	0.3	0.3	0.3	0.5	0.4	0.4	0.4	0.4	
Road tax and Emergency Fund	0.2	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	
Retail sales tax	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	
New turnover tax	2.0	2.8	1.9	1.3	1.4	1.7	2.0	2.1	1.4	1.8	1.8	1.9	1.9	1.9	
Other	0.7	0.6	0.7	0.5	0.3	0.5	0.7	0.9	0.6	0.4	0.6	0.6	0.6	0.6	
Nontax revenue	4.5	5.5	7.1	3.9	5.0	5.2	5.2	11.0	4.1	5.0	6.0	4.7	4.7	4.7	
Capital revenue	0.2	0.1	0.3	0.5	0.2	0.3	0.2	0.2	0.2	0.5	0.3	0.3	0.3	0.3	
Grants	5.1	2.0	3.1	2.3	3.9	2.9	5.2	3.5	3.3	5.3	4.3	2.1	1.1	0.7	
Program grants	3.8	1.0	2.3	1.1	2.5	1.8	3.4	1.0	1.4	3.3	2.2	1.1	0.5	0.5	
PIP grants	1.3	1.0	0.8	1.2	1.4	1.1	1.8	2.5	1.9	2.0	2.0	1.0	0.6	0.2	
Total expenditure (including net lending)	35.7	32.6	37.2	29.8	32.9	32.8	31.4	49.3	33.7	38.6	37.8	35.2	34.2	33.8	
Total expenditure	35.2	33.2	36.6	28.8	33.1	32.6	31.5	49.6	32.3	38.3	37.3	34.3	33.0	31.4	
Current expenditure	24.0	27.2	33.4	22.4	26.9	26.9	25.4	41.6	24.4	32.6	30.4	28.7	27.6	26.9	
Wages and Social Fund contributions	8.4	9.0	13.0	6.7	8.7	9.0	9.7	20.7	9.5	12.9	12.8	12.9	12.7	12.1	
Transfers and subsidies	3.4	5.7	5.3	3.3	4.1	4.4	3.6	6.7	3.1	3.8	4.1	3.7	3.6	3.3	
Transfers to Social Fund	1.2	3.6	3.3	2.4	2.1	2.7	4.0	3.6	2.4	2.7	3.0	3.2	3.1	3.1	
Interest	0.8	1.1	1.2	0.8	0.6	0.9	0.9	2.5	0.8	1.2	1.3	0.9	0.9	0.9	
Purchases of other goods and services	10.2	7.8	10.5	9.3	11.6	10.0	7.2	8.1	8.6	12.0	9.2	7.9	7.3	7.5	
Capital expenditure (including PIP)	5.0	6.0	3.2	6.4	6.2	5.6	6.1	8.0	7.8	5.7	6.9	5.7	5.3	4.5	
Domestically financed capital expenditures	2.3	1.4	1.8	1.3	1.7	1.6	0.9	2.0	2.6	2.5	2.1	2.2	2.4	2.5	
Foreign financed PIP loans	1.5	3.6	0.6	3.9	3.1	2.9	3.4	3.4	3.4	1.2	2.8	2.4	2.4	1.8	
Foreign financed PIP grants	1.3	1.0	0.8	1.2	1.4	1.1	1.8	2.5	1.9	2.0	2.0	1.0	0.6	0.2	
Financial balance	-7.5	0.5	-5.4	-6.8	-8.1	-5.6	2.6	-11.7	-9.0	-8.4	-7.2	-6.6	-6.0	-4.8	
Net lending	0.5	-0.6	0.7	1.0	-0.2	0.3	-0.1	-0.2	1.4	0.3	0.4	0.9	1.3	2.4	
Transfer to the KRDF	6.1	...	...	...	...	...	...	...	...	...	...	...	...	...
Discrepancy	-0.1	-0.5	2.2	0.2	-0.8	0.2	0.0	0.0	0.0	0.0	0.0	...	...	...
Primary balance	-7.3	1.7	-2.7	-6.9	-8.1	-4.9	3.7	-8.9	-9.6	-7.4	-6.4	-6.5	-6.4	-6.3	
Primary balance excluding grants	-12.3	-0.3	-5.8	-9.1	-12.0	-7.9	-1.5	-12.4	-12.9	-12.7	-10.6	-8.7	-7.5	-7.0	
Overall balance	-8.0	0.6	-3.9	-7.7	-8.7	-5.9	2.8	-11.4	-10.4	-8.7	-7.7	-7.5	-7.3	-7.2	
Overall Balance excluding energy infrastructure projects	-8.0	0.6	-3.9	-7.7	-8.7	-5.9	2.8	-11.4	-10.4	-8.7	-7.7	-6.6	-6.0	-4.8	
Total financing	8.1	-0.6	3.9	7.7	8.7	5.7	-2.8	11.4	10.4	8.7	7.7	7.5	7.3	7.2	
External financing	7.4	3.1	-0.8	6.0	3.2	3.2	4.6	3.2	9.4	2.3	5.2	3.7	3.9	3.8	
Public investment program (PIP)	1.5	3.6	0.6	3.9	3.1	2.9	3.4	3.4	3.4	1.2	2.8	2.4	2.4	1.8	
Program support loans	6.6	0.0	0.0	2.5	1.1	1.1	1.7	1.4	6.4	2.1	3.3	1.2	1.0	0.4	
China financed energy loans	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.9	1.3	2.4	
Total amortization	-0.7	0.0	0.0	0.0	0.0	-0.8	-0.6	-1.6	-0.3	-1.0	-0.8	-0.9	-0.7	-0.8	
Domestic financing	0.8	0.4	3.8	-13.1	5.5	-1.3	-7.9	6.3	0.8	2.8	0.9	2.5	2.3	2.4	
NBKR	0.4	-2.0	4.2	-12.3	4.5	-1.7	-8.2	6.1	-1.0	2.0	-0.1	0.8	0.2	0.0	
Commercial banks	0.3	2.5	-0.3	-0.8	1.1	0.5	0.2	0.2	1.8	0.8	0.9	1.7	2.1	2.4	
Nonbank	0.1	0.0	-0.2	0.0	-0.1	-0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Privatization	-0.1	0.4	0.0	0.0	0.0	0.1	0.6	1.9	0.2	3.5	1.6	1.3	1.1	1.0	
Use of KRDF resources	...	-4.5	0.9	14.7	0.0	3.7	...	...	...	...	...	...	...	...

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

Table 9. Kyrgyz Republic: Social Fund Operations, 2009–14

	2009	2010					2011					2012	2013	2014
	Act.	Q1 Prel.	Q2 Prel.	Q3 Prel.	Q4 Prel.	Year Prel.	Q1 Proj.	Q2 Proj.	Q3 Proj.	Q4 Proj.	Year Proj.	Year Proj.	Year Proj.	Year Proj.
(In millions of soms)														
Total revenue	11,178	2,647	3,149	2,899	3,641	12,336	3,001	4,793	3,255	4,379	15,428	18,198	20,666	22,959
Total contribution	10,808	2,576	3,074	2,834	3,594	12,078	2,943	4,736	3,197	4,321	15,198	17,956	20,412	22,693
Other revenue	370	71	75	65	47	258	58	58	58	58	231	242	254	267
Total expenditure	13,361	4,170	4,501	4,855	5,466	18,993	4,755	5,904	5,786	6,499	22,944	26,261	29,413	32,628
Pension Fund	12,644	4,080	4,234	4,703	5,205	18,222	4,476	5,626	5,507	6,220	21,829	24,941	27,954	31,054
Medical Insurance Fund (including old Funds)	675	90	227	117	256	690	248	248	248	248	990	1,173	1,297	1,398
Workers' Health Recovery Fund	42	0	41	35	5	81	31	31	31	31	124	147	163	175
Financial balance	-2,183	-1,523	-1,352	-1,956	-1,825	-6,657	-1,753	-1,111	-2,531	-2,120	-7,515	-8,063	-8,747	-9,668
Budgetary transfer	2,395	1,378	1,416	1,485	1,395	5,674	1,858	1,783	1,980	1,968	7,589	9,147	10,001	11,066
Discrepancy	150	249	-608	423	-46	18	0	0	0	0	0	0	0	0
Overall balance	362	104	-544	-48	-476	-965	104	672	-550	-152	73	1,084	1,254	1,398
Financing	-407	-104	544	48	476	965	-104	-672	550	152	-73	-1,084	-1,254	-1,398
Commercial bank deposits	-547	-104	544	48	476	965	-104	-672	550	152	-73	-1,084	-1,254	-1,398
Government bonds	140	0	0	0	0	0	0	0	0	0	0	0	0	0
(In percent of GDP)														
Total revenue	5.6	6.8	7.4	4.6	5.4	5.8	6.4	9.6	4.0	6.1	6.2	6.4	6.5	6.4
Total contribution	5.4	6.6	7.2	4.5	5.3	5.7	6.3	9.4	3.9	6.0	6.1	6.3	6.4	6.3
Other revenue	0.2	0.2	0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Total expenditure	6.6	10.7	10.5	7.7	8.1	9.0	10.2	11.8	7.1	9.0	9.2	9.2	9.2	9.1
Pension Fund	6.3	10.5	9.9	7.5	7.7	8.6	9.6	11.2	6.8	8.6	8.7	8.7	8.7	8.6
Medical Insurance Fund (including old Funds)	0.4	0.2	0.6	0.2	0.4	0.4	0.0	0.0	0.0	0.0	0.4	0.5	0.5	0.4
Workers' Health Recovery Fund	0.0	0.0	0.1	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financial balance	-1.1	-3.9	-3.2	-3.1	-2.7	-3.1	0.0	0.0	0.0	0.0	-3.0	-2.8	-2.7	-2.7
Budgetary transfer	1.2	3.6	3.3	2.4	2.1	2.7	0.0	0.0	0.0	0.0	3.0	3.2	3.1	3.1
Discrepancy	0.1	0.6	-1.4	0.7	-0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	0.2	0.3	-1.3	-0.1	-0.7	-0.5	0.0	0.0	0.0	0.0	0.0	0.4	0.4	0.4
Financing	-0.2	-0.3	1.3	0.1	0.7	0.5	-0.2	-1.3	0.7	0.2	0.0	-0.4	-0.4	-0.4
Commercial bank deposits	-0.3	-0.3	1.3	0.1	0.7	0.5	0.0	0.0	0.0	0.0	0.0	-0.4	-0.4	-0.4
Government bonds	0.1	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

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

Table 10. Kyrgyz Republic: Proposed Reviews and Disbursements Under the
Three-Year Extended Credit Facility Arrangement

Date	Action	Associated Disbursement	Share of Access (percent)
On or after June 20, 2011	Approved three-year ECF arrangement	SDR 9.514 million	14.3
On or after November 30, 2011	Completed the first review based on end-June, 2011 performance criteria	SDR 9.514 million	14.3
On or after April 16, 2012	Completed the second review based on end-December, 2011 performance criteria	SDR 9.514 million	14.3
On or after November 15, 2012	Completed the third review based on end-June, 2012 performance criteria	SDR 9.514 million	14.3
On or after April 15, 2013	Completed the fourth review based on end-December, 2012 performance criteria	SDR 9.514 million	14.3
On or after November 15, 2013	Completed the fifth review based on end-June, 2013 performance criteria	SDR 9.514 million	14.3
On or after April 30, 2014	Completed the sixth and final review based on end-December, 2013 performance criteria	SDR 9.516 million	14.3
Total		SDR 66.600 million	100.0

Source: International Monetary Fund.

Table 11. Kyrgyz Republic: Indicators of Capacity to Repay the Fund, 2009–16 1/

	2009	2010	2011	2012	2013	2014	2015	2016
	Act.	Act.	Projections					
Fund obligations based on existing credit								
<i>(in millions of SDRs)</i>								
Principal	16.9	14.1	15.3	13.5	11.4	13.3	11.0	14.0
Charges and interest	0.5	0.0	0.0	0.2	0.2	0.2	0.1	0.1
Fund obligations based on existing and prospective credit								
<i>(in millions of SDRs)</i>								
Principal	16.9	14.1	15.3	13.5	11.4	13.3	11.0	15.0
Charges and interest	0.5	0.0	0.0	0.3	0.3	0.3	0.3	0.3
Total obligations based on existing and prospective credit								
<i>In millions of SDRs</i>								
In millions of U.S. dollars	26.8	21.2	22.8	20.5	17.4	20.4	17.0	22.8
In percent of Gross International Reserves	1.7	1.2	1.2	1.1	0.9	0.9	0.7	0.9
In percent of exports of goods and services	1.0	0.8	0.7	0.6	0.5	0.5	0.4	0.4
In percent of debt service 2/	31.6	23.3	6.4	23.0	18.8	19.6	15.9	17.8
In percent of GDP	0.6	0.5	0.4	0.4	0.3	0.3	0.2	0.3
In percent of quota	19.6	15.9	17.2	15.5	13.1	15.4	12.8	17.2
Outstanding Fund credit 2/								
<i>In millions of SDRs</i>								
In billions of U.S. dollars	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2
In percent of Gross International Reserves	10.4	10.1	9.5	9.8	9.6	8.5	7.1	5.7
In percent of exports of goods and services	6.1	6.8	5.6	5.4	5.3	4.5	3.7	2.9
In percent of debt service 2/	193.6	189.4	49.8	206.5	212.2	183.6	163.2	118.9
In percent of GDP	3.5	3.7	3.4	3.2	3.2	2.8	2.4	1.9
In percent of quota	120.1	129.2	133.4	139.6	148.2	143.9	131.5	114.7
Net use of Fund credit (in millions of SDRs)								
Disbursements	16.7	22.2	19.0	19.0	19.0	9.5	-	-
Repayments and Repurchases	16.9	14.1	15.3	13.5	11.4	13.3	11.0	15.0
Memorandum items:								
Nominal GDP (in millions of U.S. dollars)	4,683	4,615	5,187	5,695	6,187	6,766	7,319	7,870
Exports of goods and services (in millions of U.S. dollars)	2,695	2,529	3,133	3,407	3,684	4,221	4,748	5,324
Gross International Reserves (in millions of U.S. dollars)	1,584	1,716	1,862	1,889	2,042	2,244	2,462	2,651
Debt service (in millions of U.S. dollars) 2/	84.9	91.1	354.2	89.5	92.6	104.0	107.0	128.0
Quota (millions of SDRs)	88.8	88.8	88.8	88.8	88.8	88.8	88.8	88.8

Sources: IMF staff estimates and projections.

1/ Assumes seven semi-annual disbursements under the ECF facility of 75 percent of quota (SDR 66.6 million) starting in June 2011. Projections of interest payments incorporate the temporary interest relief initiative and interest rate structure under the new architecture of LIC facilities and financing.

2/ Total external public debt service includes IMF repurchases and repayments.

APPENDIX I. KYRGYZ REPUBLIC: LETTER OF INTENT

June 2, 2011

Mr. John Lipsky
Acting Managing Director
International Monetary Fund
700 19th Street, N.W.
Washington, DC 20431

Dear Mr. Lipsky:

The Kyrgyz Republic suffered from a deep political crisis last year. In April 2010, a popular uprising toppled the previous regime and the tragic events of June 2010 exacerbated the already difficult political situation. Following the joint economic assessment and the donor conference in mid-2010, the IMF was the first international financial institution to support the Kyrgyz Republic. Financial assistance provided under the Rapid Credit Facility (RCF) in September 2010 supported our country at a very difficult time in our history and was instrumental in mobilizing much-needed donor assistance. Parliamentary elections took place in October 2010 and a new coalition government took office in December 2010. We believe that the shift to a parliamentary democracy provides new opportunities to break with the past and strengthen governance and reform the economy.

The fallout from the domestic crisis has posed significant challenges. The economy contracted last year, straining the government's financial position, further exacerbated by critical reconciliation, recovery and reconstruction needs. Moreover, the global food and fuel price shock triggered a sharp rise in inflation, eroding real incomes of the most vulnerable part of the population. Business confidence deteriorated, hampering prospects for private sector-led economic recovery.

The Kyrgyz authorities are determined to take prompt actions and implement a macroeconomic and structural reform program that will support the economic recovery in the short term and place the country on the road to stronger sustained and inclusive growth in the medium term, while preserving macroeconomic stability and debt sustainability. We will also develop a comprehensive Country Development Strategy. Governance problems that had been mounting in the past also need to be addressed in a comprehensive manner.

Against this background, we hereby request Fund support under a new three-year Extended Credit Facility (ECF) arrangement in an amount equivalent to SDR 66.6 million and the first disbursement in an amount equivalent to SDR 9.514 million upon the approval of the arrangement. We also request that the first two disbursements under the ECF arrangement be channeled to the budget. The new Fund-supported program (June 2011–June 2014) will

provide a coherent macroeconomic framework that will support our efforts to restore macroeconomic stability, rebuild macroeconomic policy buffers, promote inclusive growth in a low inflation environment, achieve medium-term fiscal consolidation, address weaknesses in the financial sector, and catalyze critical donor support, which would allow us to keep reserves at a comfortable level.

The observance of all end-2010 indicative targets under the RCF allowed the new government to build a track record, which we consider an important prerequisite for a medium-term program engagement with the IMF.

The attached Memorandum of Economic and Financial Policies (MEFP) outlines our macroeconomic objectives for 2011–14 and provides specific measures for 2011–12. We are committed to the objectives of our Fund-supported program recognizing that disbursements under the ECF arrangement are subject to observance of performance criteria, fulfillment of prior action(s), and completion of program reviews. The government believes that the policies set out in the attached MEFP are adequate to achieve the objectives of the Fund-supported program, but stands ready to take additional measures. The Kyrgyz Republic will consult with the Fund on such measures and in advance of any revision to policies contained in the MEFP, in accordance with the Fund's policies. During the Fund-supported program period the government will not introduce any exchange rate restrictions, multiple currency practice, and import restrictions for balance of payments purposes, and will continue to comply with all obligations under Article VIII of the IMF's Articles of Agreements.

In line with our commitment to transparency in government operations, which we believe is essential for good governance, we consent to the publication of all ECF-related documents circulated to the IMF Executive Board on the IMF's web site.

/s/

Almazbek Atambaev
Prime Minister of the Kyrgyz Republic

/s/

Melis Mambetjanov
Minister of Finance of the
Kyrgyz Republic

/s/

Baktygul Jeenbaeva
Acting Chairperson of the National Bank of
the Kyrgyz Republic

APPENDIX II. KYRGYZ REPUBLIC: MEMORANDUM OF ECONOMIC AND FINANCIAL POLICIES (MEFP) FOR 2011–14

June 2, 2011

I. INTRODUCTION

1. This Memorandum sets out the economic and financial policies of the government of the Kyrgyz Republic for 2011–14, which aim at rebalancing the policy mix to restore macroeconomic stability and rebuild policy buffers through fiscal consolidation while protecting social outlays, strengthening financial sector stability, and addressing governance problems. These policies form the basis for a new three-year Fund-supported program under an Extended Credit Facility (ECF).

II. BACKGROUND AND PROGRAM OBJECTIVES

2. **The interim government, which took office following the April 2010 revolution, faced a difficult task to restore security in the country and to transfer power to the newly elected government.** The new constitution approved in June 2010 balanced the power between the parliament and the government and established the first Central Asian parliamentary democracy. We also conducted successful parliamentary elections, which were assessed by international observers as fair and democratic. Following the elections, a three-party ruling coalition was formed and a new government appointed at the end of 2010. The overarching objective of the caretaker government to ensure a smooth transition to a new political system with minimal social cost and economic damage was met, enabling us to focus on key economic issues.

3. **While the Kyrgyz economy showed signs of recovery from the global economic crisis in the first quarter of 2010, the events of 2010 took a heavy toll on growth.** During the first quarter of 2010 real GDP grew by an impressive 16 percent, driven by strong gold production and a pickup in industrial production and construction. The collapse of the government in April 2010 and the tragic events of June 2010 reversed these positive developments and the economy contracted by 1.4 percent in 2010, primarily due to negative growth in construction, agriculture, and trade. Border closures and internal security concerns disrupted normal trade flows, resulting in losses by the traditional export industries and a sharp drop in supply.

4. **The external position deteriorated in 2010.** The current account shifted from a surplus of about 1 percent of GDP in 2009 to a 2 percent of GDP deficit. Reserve coverage dropped from 4.9 to 4.2 months of imports, although the decline would have been larger without external financial assistance from bilateral and multilateral donors following the July 2010 donor conference in Bishkek. In addition, high gold prices, coupled with increasing gold production, boosted export earnings and the economic recovery in Russia helped to bolster remittance inflows.

5. **Rising international food and fuel prices led to a surge in inflation from 3.5 percent in June 2010 to 20.8 percent in March 2011.** While the removal of the fuel export duty by Russia in January of this year partially offset the impact from rising commodity prices, supply shortages stemming from security concerns aggravated the problem and we are concerned that inflationary expectations have become entrenched. We have therefore tightened monetary policy by raising reserve requirements, increasing the policy rate and intensifying open market operations.
6. **The Joint Economic Assessment prepared by the international community with the Fund's active participation identified significant financing needs for reconciliation, recovery, and reconstruction.** Donors pledged US\$1.1 billion in assistance over the period of 18 months to deal with the consequences of the 2010 events. As of April 2011, the total contracted amount was US\$380 million. We call upon the donor community to fulfill their pledges.
7. **We are committed to restoring macroeconomic stability and have already taken number of measures towards this end.** We realize that a comprehensive and homegrown medium-term country development strategy is necessary to set the foundation for putting the economy back on a sustainable growth path. Work on such a strategy has already begun with the assistance of our development partners and we expect it to be finalized by the end of this year. Meanwhile, in March, the government approved an Action Plan for Economic Security (APES) for 2011, which puts forward measures intended to remove the immediate obstacles to economic growth and poverty reduction. These measures, some of which are included in this memorandum, aim at strengthening public finances and improving governance. We will rigorously monitor the implementation of this plan, which can be considered as our short-term work program.
8. **Over the medium term, we are committed to implementing sound macroeconomic and structural policies.** These policies will allow us to reestablish macroeconomic stability, fully utilize the economic growth potential, curb inflation, reduce the fiscal deficit, strengthen the financial sector, improve the external position, and enhance the role of the private sector in the economy. The shift to a more democratic political system enables us to break with the past and strengthen governance, which will be the cornerstone of our reforms. We also believe that the ECF arrangement will help mobilize official external financing to support these objectives. We read with interest the Ex Post Assessment of Longer-Term Program Engagement report for the Kyrgyz Republic prepared by IMF staff and incorporated the main findings of the report into the design of our new Fund-supported program.

III. POLICIES FOR 2011 AND BEYOND

9. **A gradual economic recovery and return to a stable macroeconomic position is the cornerstone of our Fund-supported program.** In particular:

- We expect real GDP to grow by about 6 percent on average during 2011–14 on the back of continued political stability and a rebound in agriculture, trade and construction.
- Our tight monetary policy stance will help to reduce inflation in 2011 but it is still expected to remain in the lower double digits. In 2012 inflation will continue to subside and stabilize at about 7.5 percent in 2013–14, largely reflecting normalization of trade, stabilization of international food and fuel prices, and prudent fiscal policies.
- The general government deficit, excluding Chinese-financed investment projects, will be brought down to 4.4 percent of GDP by 2014, primarily on account of tax administration and tax policy measures (see below).
- The current account deficit will increase in 2011 and gradually decline over the medium term. However, strong import demand including foreign-financed energy related public investments will prevent the current account deficit to improve faster. The ECF-supported program is expected to catalyze significant donor support, which will help to finance the current account deficits and maintain comfortable reserve levels.

A. Fiscal policy

10. **We wish to emphasize that the 2010 fiscal deficit was significantly lower than anticipated under the Rapid Credit Facility (RCF).** The caretaker administration's cautious approach, a shortfall in planned external financing, solid gold related tax receipts, including advance payments, and delays in the capitalization of Zalkar bank created from Asia Universal Bank (AUB), resulted in a fiscal deficit of less than 7 percent of GDP in contrast to 12 percent of GDP projected earlier. In addition, capacity constraints, which did not allow us to fully execute capital expenditure projects in the south to rebuild housing and infrastructure damaged during the events of June 2010, led to spending underexecution. At the same time, we have fully executed our social commitments.

11. **Recognizing risks to macroeconomic stability, we envisage a less expansionary fiscal stance in 2011 compared to the projections at the time of the RCF.** The general government overall deficit is now projected at 7.6 percent of GDP. On the back of rapidly rising inflation and public discontent from the previous governments' inaction to address pressing social problems, we substantially raised salaries for teachers, healthcare workers, and other social sector workers. This decision, which became effective on May 1, 2011, will allow the majority of about 180,000 social sector employees to earn incomes just above the subsistence level. At the same time, mindful of the capacity limitations and to accommodate the salary increase we revised downward capital expenditures. While the salary reform helps

to mitigate potential risks to social stability, it will likely contribute to inflationary pressures. To this end the government and the National Bank of the Kyrgyz Republic (NBKR) will closely coordinate fiscal and monetary operations to mitigate the inflationary impact from the expansionary fiscal stance, while supporting the fragile recovery.

12. **Given the ambitious reform agenda, the 2011 budget contains financing risks, which we plan to address through contingency measures.** We have already adopted several tax policy and administration measures and begun fighting corruption and tax evasion that should yield additional revenues of about 1 percent of GDP. Moreover, we plan to privatize KyrgyzTelecom through an open and competitive bidding process. We will carefully analyze revenue performance on a monthly basis and should additional tax revenues, privatization proceeds, and external financing not materialize, we will either compensate the shortfall through the sale of additional government shares of the mobile phone operator MegaCom or immediately submit to the parliament a supplementary budget proposing sequestration of nonpriority spending, while preserving expenditures on protected items. At the same time, we commit not to initiate any supplementary budget that may lead to an increase in total government spending beyond the amounts agreed with the IMF. We also commit to save 75 percent of the recent dividend payment received from Centerra Gold Inc. and any additional windfall receipts above the amounts envisaged in the approved budget.

13. **Our medium-term fiscal policy aims to bring the fiscal position back on a sustainable path.** To achieve this goal, we recognize that substantial fiscal consolidation from 2012 will be necessary. To this end, we will introduce additional revenue measures and restrain expenditures. Given that a large part of the domestic economy remains outside the tax system, our efforts will focus on broadening the tax base, which should help improve the efficiency of our tax system. Our measures will encourage formalization of the economy, limit tax evasion, spread the tax burden more evenly and simplify the tax system. The main element of our reform will be to improve the customs valuation system. In particular, we will move the majority of imported goods from weight-based to price-based valuation for raising revenues collected by customs (0.3 percent of GDP). We also plan to introduce additional measures by (i) reforming excise taxation on tobacco and alcohol in line with the draft tax code amendments (0.4 percent of GDP); (ii) removing the turnover tax exemption on electricity, heat and natural gas for commercial users (0.1 percent of GDP) and VAT exemptions on communication services (0.1 percent of GDP); and (iii) moving to a contract-based tax regime for food services (0.1 percent of GDP). These tax revenue measures, which in total will yield revenue of 1.0 percent of GDP, will become effective by January 1, 2012 (amendments to be submitted to Parliament by end-October, 2011, structural benchmarks). We also commit not to introduce new tax exemptions for the duration of the Fund-supported program.

14. **We will further bolster tax administration by strengthening the large taxpayers' office, deterring noncompliance through improved audits, and enhancing communication with, and assistance to, taxpayers (structural benchmark).** Moreover,

we will exercise nominal wage restraint for public sector employees in 2012, reduce spending in other areas and generate additional fiscal savings through the civil service reform, which will result in at least 10 percent reduction of the civil service. We will begin to outsource part of government services to the private sector starting from 2012, which will result in a decline in revenues from fees and expenditures on services. The consolidation strategy will help to bring the fiscal deficit, excluding the Chinese-financed investment projects, from almost 8 percent of GDP in 2011 to 4.4 percent of GDP by 2014.

15. **Strong inclusive growth will aid in reducing poverty.** To ensure that the growth dividends from our reform efforts also benefit the poor, we plan to further develop our key targeted social assistance programs with the support of our development partners. Recently we modified the Unified Monthly Benefits (UMB), the central targeted assistance program, to introduce elements of a proxy means tested system. We plan to raise the size of the Guaranteed Minimum Income by almost 20 percent and increase spending on UMB and Monthly Social Benefit (MSB) to catch up with the rising cost of living. We plan to continue a gradual increase in spending on targeted social assistance programs and expand the coverage to nearly 0.5 million recipients (9 percent of the population) in the medium term.

16. **We believe that strengthening management of State-Owned Enterprises (SOEs) and Joint Stock companies (JSCs) with majority government equity participation will improve their efficiency, enhance the revenue base and minimize fiscal risks.** A recent study of their operations revealed shortcomings in their budget planning and accountability. The shortcomings stem from operational inefficiencies related to noncore expenditures. While external audits are mandatory for these companies, there is no procedure or mechanism in place to perform effective budget planning, analyze audit results, and take appropriate actions. We plan to develop a uniform procedure for budget planning and accountability to be used by these companies to increase their accountability. We will strengthen corporate governance principles. We will establish new reporting requirements for the 10 largest (in terms of assets) of these companies, which will include procedures to submit, approve, and monitor their budgets (structural benchmark). As these companies become more efficient, the budget will benefit from increased revenues from dividends. During the program period we will expand coverage to all SOEs and JSCs with majority government equity participation. Subsequently, we will prepare a transparent privatization plan with the assistance of our development partners.

17. **Additional structural reforms will aid the process of fiscal consolidation and put public finances on a stronger footing.** As a step towards further budgetary consolidation, we plan to integrate the social fund into the state budget framework by bringing its operations under the central treasury (envisaged under APES). At the same time, to strengthen the role of the Ministry of Finance as the key agency responsible for fiscal policy, we will consider returning the tax policy function to the Ministry of Finance.

18. **We also intend to advance public financial management (PFM) reform to increase the effectiveness of public spending.** The events of 2010 prevented us from focusing on implementing PFM reforms, particularly the recommendations provided by the IMF's Fiscal Affairs Department (FAD) technical assistance mission in December 2009. We have requested a follow-up mission to take a fresh look at PFM issues and update the recommendations. PFM reform measures would strengthen budget design and implementation and increasing transparency of budgetary operations. The donor trust fund will be instrumental in revitalizing PFM reforms.

19. **We are committed to maintaining debt sustainability.**

- In this regard, we will prepare a medium-term debt management strategy (MTDS) in consultation with the World Bank and IMF. We will also step up efforts to conduct our own debt sustainability analysis.
- We are actively working with the Russian authorities to find a resolution of the outstanding debt issue. We have already cleared arrears in the amount of US\$14.4 million thereby removing a key impediment for the disbursement of budget support loan from the Eurasia Economic Community Anti Crisis Fund (ACF). We have also signed an agreement with the Belarusian government to settle debt obligations in the amount of US\$207,649. We have contacted the governments of China and Korea to discuss and negotiate the settlement of technical arrears totaling approximately US\$7.6 million.
- We are in discussions with China to borrow US\$208 million for energy infrastructure investments. We may consider borrowing an additional US\$240 million for related investments in a few years time. While the terms of these borrowings are not yet finalized, we will make every effort to ensure that the borrowing occurs on concessional terms. We are committed to contracting only external debt that is consistent with maintaining lower external debt vulnerabilities, i.e., maintaining or improving the moderate risk of external debt distress rating.

B. Monetary and Exchange Rate policies

20. **We are concerned with the recent inflation developments, largely driven by the food and fuel price shock.** Inflation has become widespread, encompassing a larger share of the basket and will likely be amplified by this year's fiscal expansion. But the recent inflation trends, which show core inflation stabilizing, are encouraging. We have already started to tighten monetary policy. In particular, we have raised the policy rate since October 2010 by almost 500 basis points, which has allowed us to substantially increase liquidity absorption through sales of NBKR notes. We also raised reserve requirements in February of this year by 1 percentage point. We anticipate that the combination of these policies will slow the growth of monetary aggregates and help to reduce inflation. Nonetheless, we stand ready to tighten further if inflation does not revert to a declining path in the second half of 2011. The

adverse impact on NBKR profits will not be a constraining factor on implementing monetary policy. To strengthen the effectiveness of monetary policy, we intend to work on deepening financial markets and increasing competition in the banking sector. We recognize that the best way to reduce high dollarization is to establish a track record of macroeconomic stability and to maintain exchange rate flexibility.

21. **The floating exchange rate system has served us well in mitigating the impact of external shocks without a sharp deterioration in the external position.** Exchange rate flexibility will help to maintain the real exchange rate in line with fundamentals. We will therefore intervene in the foreign exchange market only to smooth short-term exchange rate movements.

C. Financial Sector

22. **Political developments in 2010 tested our financial system, severely disrupted the regular course of supervisory activities, and undermined the NBKR's credibility.** Seven commercial banks, including the largest and systemically important one, AUB, were put under official control. The situation in five of these banks has not been fully resolved. As expected, the banking system's performance weakened and nonperforming loans increased. Some commercial banks experienced liquidity problems. However, there are signs of improvement.

23. **We have taken actions to isolate and resolve the problems in the banking system; but the process remains incomplete.** We will decisively deal with these legacy issues and ensure that the banking system is sufficiently resilient to withstand possible further shocks. We are taking the following steps:

- *Asset recovery.* The forensic audit of AUB revealed that the bank was insolvent ahead of the April events. It also suggests that shareholders and senior bank officials may have used the bank to engage in money-laundering activities. Based on these findings, we are actively working with the Basel Institute of Governance to determine whether any assets could be recovered.
- *Resolution of AUB/Zalkar.* We will complete the resolution of AUB/Zalkar in line with international best practices and as agreed with Fund staff. We will commission a financial audit to determine the financial position of Zalkar Bank, the new bank created from the AUB split (prior action). The audit will be conducted by a reputable big-four international accounting firm, and the results will be shared with IMF staff. Regardless of how these issues are resolved, the budget will bear the financial responsibility.
 - If the audit determines that the bank is solvent, it will be offered for sale, to a reputable bank, through a transparent and competitive privatization process (structural benchmark).

- If the privatization is not successful within the allotted timeframe, the assets and liabilities will be disposed of in a transparent and competitive tender process to interested investors within a reasonable time frame (structural benchmark).
- If the audit determines that the bank is insolvent, we will dispose of its assets and liabilities in a transparent and competitive tender process within a reasonable time frame (structural benchmark).
- *Resolution of banks currently under conservatorship.* We will continue to maintain the banks under conservatorship until they are fully compliant with the regulatory requirements or placed under liquidation.
- *Strengthen supervision, particularly of systemically important banks.* After an interruption due to the heavy volume of work on the problem banks, we have restored a regular cycle of supervisory inspections in a prioritized manner. In this context, we agree that SSC's rapid growth requires close monitoring and supervisory actions to contain its rate of growth and ensure its soundness. We will inject capital only to the extent necessary to allow the bank to extend loans to the entrepreneurs who suffered damages during June 2010 events. Going forward, we plan to privatize the bank and, in this context, will develop a strategy by end-April 2012.

We recognize that the NBKR should have sufficient financial resources to employ necessary staff and experts to tackle the difficult problems.

24. **We acknowledge the need to strengthen mechanisms to deter money laundering.** We will work towards enhancing interagency coordination between relevant government agencies by reestablishing the Interagency Commission for Combating the Financing of Terrorism and Legalization (laundering) of Proceeds from Crime, composed of the State Financial Intelligence Service, the NBKR, the National Security Service, the General Prosecutor's Office, the State Financial Market Supervision and Regulation Service and other relevant agencies, if any. The commission will meet on a regular basis and will prepare proposals on developing and implementing an AML/FT national strategy to strengthen the AML/CFT system and ensure interaction between government authorities on AML/CFT issues. The SFIS will streamline the financial analysis of the AML/CFT-related information it receives.

25. **We recognize that the Special Bank Refinancing Fund (SBRF), which was set up in 2009 by the NBKR to provide loans to commercial banks and micro finance institutions, should be phased out.** We will therefore announce the liquidation of the SBRF by issuing the relevant NBKR Board decision (prior action). Subsequently, we will transfer the loan portfolio to the NBKR and the government, in proportion to their funding

contributions (structural benchmark). We will not create any development/investment vehicle without prior consultation with IMF staff to ensure consistency with our program commitments.

26. **The recent experience with the banking sector revealed that the NBKR's supervisory independence had been compromised and that there are weaknesses in the legal framework for early intervention and resolution of problem banks.** Gaps, overlaps and inconsistencies in the banking laws render them difficult to interpret and apply, and may inadvertently hinder the protection of the interests of depositors and the maintenance of financial stability. We will submit to Parliament banking legislation to remedy these shortcomings as follows (structural benchmark):

- *Banking Code.* We will compile our banking laws into a Banking Code to ensure that only the Constitution and/or Constitutional Laws will supersede the banking laws.
- *Early Intervention and Bank Resolution.* The Banking Code will strengthen the existing powers of the NBKR with respect to the early intervention and resolution of problem banks, in line with international best practice and based on technical assistance from Fund staff. The Banking Code will provide for the appointment of an official administrator to a problem bank who will be empowered to use a range of restructuring tools, under the direction of the NBKR, such as recapitalization, purchase and assumption transactions and the establishment of a bridge bank, without preemptive rights of shareholders or creditors. In the event that a problem bank cannot be restructured as a going concern, the NBKR will be empowered to commence out-of-court liquidation proceedings against the bank.
- *The role of the judiciary.* The Banking Code will limit the scope of judicial review of actions taken by the NBKR to better align it with international best practice. This would entail limiting the courts' review of technical matters within the competence of the NBKR.
- *Rights of bank shareholders and creditors.* The Banking Code will ensure that the rights of bank shareholders and creditors are adequately protected and appropriately balanced against the public interest in depositor protection and financial stability. Shareholders and creditors will retain their rights to challenge the lawfulness of actions taken by the NBKR in court and to seek monetary damages.
- *Legal Protection for NBKR staff and agents.* The Banking Code will contain provisions that ensure that the NBKR, rather than its individual staff members or agents, is liable for actions taken by those individuals in the performance of their official duties.

D. Governance

27. **We fully recognize that our country's image has been damaged by the high level of perceived corruption, impeding the prospects of economic growth and sustainable development.** International agencies have been ranking the Kyrgyz Republic very low for

the last five years due to the widespread perception of corruption. Addressing this issue remains one of the biggest challenges for our government, but we are working hard to improve this image. Addressing governance issues will ensure the efficient use of public resources and improve the business climate, which will be instrumental to attract high-quality domestic and foreign investments in the country.

28. **Increasing transparency will play a pivotal role in reinforcing governance reforms.** Shortly after the new government came to power, we stepped up efforts to become an Extractive Industries Transparency Initiative (EITI) compliant country. While the formal launch of the EITI for The Kyrgyz Republic was announced in 2004, the process stalled. We undertook corrective actions in October 2010 and we were accepted by the EITI Board as a compliant country on March 1, 2011. Given the Kyrgyz Republic's natural resource endowment being an EITI compliant member demonstrates our commitment to enhance transparency.

29. **As part of the Fuel Energy Sector Transparency Initiative, we have requested USAID's Regional Energy Security, Efficiency and Trade project to undertake phase one management diagnostics of the main companies in the electricity sector of the Kyrgyz Republic.** The primary purpose of this appraisal is to identify ways to improve the governance and performance of each state-owned company and thus, establish the basis for the entire sector to become more efficient, self-sustaining and customer-oriented. The appraisal revealed many shortcomings in management practices of the companies, including weak control over procurement, exaggeration of reported technical losses, and lack of credible strategic planning. We will address these deficiencies in the course of phase two and three of the project, thus improving governance in energy sector crucial for the Kyrgyz economy. In addition, we hope to get World Bank support to improve energy sector transparency, accountability, and operational efficiency, and to enhance financial discipline through its planned Economic Recovery Support Operation.

30. **Governance issues related to the financial activities and reporting procedures of the Kyrgyz Republic Development Fund (KRDF), currently undergoing liquidation, prevented the previous government from completing reviews under the program supported by the Exogenous Shocks Facility (ESF).** We recognize the Fund's constructive role in helping to safeguard bilateral assistance received from Russia in 2009. We believe that there are still many unknowns in KRDF's operations. In line with our commitment under the RCF (see RCF MEFP, ¶17 (b)), we will select a reputable international auditing firm (big-four) to conduct a forensic audit of the KRDF from its inception through end-April 2011 (prior action). We will provide all the necessary information to the external auditor. Once finalized, we will publish the forensic audit report (structural benchmark). Mindful of the implications for the Fund-supported program, we will not create any other extra budgetary fund throughout the duration of the ECF arrangement and will ensure that all public finances are channeled through the budget.

31. **Despite the favorable rankings the Kyrgyz Republic enjoys in business climate indicators, the business community is very vocal about the problems encountered in their activities.** We are analyzing the reasons behind this in close consultation with representatives of the business community. Recognizing the importance of improving the business climate our APES envisages measures to reduce administrative burdens on taxpayers, strengthen property rights and, and streamline business registration and operations.

E. Other Structural Reforms

32. **The caretaker government partially reversed the large electricity tariff increase implemented by the previous government in January 2010 because of the heavy burden placed on socially vulnerable citizens.** This reversal has postponed much-needed reforms and worsened the financial condition of the energy sector. We will design energy sector reform with the objective to reduce losses in the sector, and increase its competitiveness and attract foreign investors, which should help to generate funding for its rehabilitation. The reform will be designed in close consultation with our development partners. We also intend to export summer surplus power to new markets.

33. **We have carefully weighed pros and cons of joining the Belarus-Kazakhstan-Russia Customs Union (CU).** We have submitted an application and plan to launch membership negotiations shortly. We have set up a working group headed by the ministry of economic regulation to conduct the negotiations. We will consult with the World Trade Organization during this process.

F. Safeguards Assessment

34. **We recognize the importance of completing an updated safeguards assessment of the NBKR by the first review under the ECF arrangement.** The NBKR has provided the IMF's Finance Department all the requested information, including the authorization to speak with its external auditor and stands ready to receive a safeguards mission, if needed. We are also committed to implement recommendations emerging from the safeguards assessment and include priority ones in future measures under the Fund-supported program. We also agree to update the February 6, 2010 memorandum of understanding between the ministry of finance and the NKBR on the management of foreign exchange reserves, including those for budgetary support.

IV. PROGRAM MONITORING

35. **The Fund-supported program will be monitored through prior actions, quantitative performance criteria, indicative targets, and structural benchmarks.** Prior actions and structural benchmarks are set out in Table 1; the quantitative targets (performance criteria and indicative targets) for end-June 2011, end-September 2011, end-December 2011, end-March 2012, and end-June 2012 and continuous performance

criteria, are set out in Table 2. The reviews will be conducted semi-annually based on end-June and end-December test dates. The first and second reviews will be expected to take place by November 30, 2011 and April 16, 2012, respectively. The understandings between the Kyrgyz authorities and IMF staff regarding the quantitative performance criteria and the relevant structural measures described in this memorandum and reporting requirements are further specified in the technical memorandum of understanding (TMU) attached to this memorandum.

Table 1. Kyrgyz Republic: Prior Actions and Structural Benchmarks under the Extended Credit Facility for 2011 and 2012

Measure	Timing	Macroeconomic rationale
Prior Actions		
Select a reputable international auditing firm (big-four) to conduct a forensic audit of the Kyrgyz Republic Development Fund (KRDF).		Strengthen transparency of public finances.
Select a reputable international auditing firm (big-four) to conduct a financial audit of the opening and end-April 2011 balance sheets of Zalkar Bank.		Expedite a complete and transparent resolution of the AUB/Zalkar.
Announce the liquidation of the SBRF by issuing the relevant NBKR Board decision.		Remove distortions in the central bank operations.
Structural Benchmarks		
I. FISCAL POLICY		
Submit to Parliament amendments to the tax and customs codes and issue relevant government resolutions to raise additional revenues by:	End-October, 2011	Revenue measures are critical to achieve medium-term fiscal consolidation without sizable downward adjustments of expenditures.
(a) Improving the customs valuation system and moving the majority of imported goods from weight-based to price-based valuation.		Introduce best international practices in customs valuation of imported goods.
(b) Removing the turnover tax exemption on electricity, heat and natural gas for commercial users.		Raise revenues in an easy to administer way.
(c) Removing VAT exemptions on communication (internet and roaming) services.		Broaden the tax base.
(d) Reforming excise taxation on tobacco and alcohol in line with the draft tax code amendments.		Raise revenues in an easy to administer way.
(e) Moving to a contract-based tax regime for food services.		Strengthen enforcement of the tax legislation.
Strengthen tax administration by:	End-September, 2011	Tax policy measures alone will be insufficient to generate additional revenues in support of fiscal consolidation.
a) Strengthening the large taxpayers office (LTO) by: (i) reviewing the current criteria for identifying large taxpayers and modifying, if necessary; (ii) expanding the LTO coverage of the large taxpayers to achieve at least 60 percent of the number of taxpayers meeting the established criteria; (iii) ensuring that LTO participation is mandatory; (iv) reviewing organization charts and making changes, if necessary.		Raising revenues from large taxpayers is fundamental to sound revenue administration.
(b) Deterring non-compliance through improved audits by introducing best practices in the taxpayer audits by: (i) completing the first phase of computer-based risk scoring system; (ii) measuring and closely monitoring audit performance.		Increase the quality of taxpayer audits.
(c) Enhancing communication with taxpayers, staff and other stakeholders by: (i) publicizing information for the taxpayers on the existing guidance and assistance on tax issues available at the tax offices; (ii) regular briefings of industry associations, tax accountants and other third parties; (iii) preparing quarterly reports to the public about the communication activities.		Increase transparency of tax administration.
Adopt a government resolution on the procedures for submission of budgets of the 10 largest SOEs to be approved and monitored by the government.	End-October, 2011	Reduce fiscal risks stemming from state-owned enterprises and boost revenues from dividends.
Develop and adopt a medium-term debt management strategy.	End-March, 2012	Strengthen macroeconomic management and ensure debt sustainability.
Publish the external audit report on the KRDF.	End-September, 2011*	Strengthen transparency of public finances.
II. FINANCIAL SECTOR		
Refund in the process of liquidation the portions of the SBRF financed by the NBKR and the government, respectively.	End-October, 2011	Remove distortions in the central bank operations.
Based on the audit results, resolve Zalkar Bank as follows:		Complete resolution of the AUB/Zalkar.
1) If the bank is solvent, then:		
a) sell to a reputable bank, or	End-February, 2012	
b) if no acquirer is found, initiate disposal of assets and liabilities to interested investors.	End-February, 2012	
2) If the bank is insolvent, then initiate closure and liquidation.	End-September, 2011	
Submit to the Parliament a draft Banking Code (including Law on Banks and Banking Activity, Law on Conservatorship, Liquidation, and Bankruptcy of Banks, Law on NBKR) consistent with Fund TA advice, to (i) strengthen the legal framework for early intervention and resolution of problem banks; (ii) limit the scope of judicial review of actions taken by the NBKR; (iii) enhance legal protection for NBKR staff and agents.	End-April, 2012	Strengthen bank resolution framework and supervisory independence of the NBKR.
Develop a sales strategy for the SSC bank.	End-April, 2012	Reduce the government's involvement in the commercial banking activity.

* For compliance monitoring purposes, delays directly caused by the audit company will be acknowledged.

Table 2. Kyrgyz Republic: Quantitative Performance Criteria and Indicative Targets under the Extended Credit Facility (In millions of soms, unless otherwise indicated; eop)

	2010		2011		2012	
	December	June	September	December	March	June
	Actual	QPC	Indicative Targets	QPC	Indicative Targets	Indicative Targets
<i>Quantitative performance criteria 1/</i>						
1. Floor on net international reserves of the NBKR (eop stock, in millions of U.S. dollars)	1,526	1,586	1,612	1,617	1,637	1,657
2. Ceiling on net domestic assets of the NBKR (eop stock)	-14,933	-16,016	-15,189	-11,327	-11,681	-10,761
3. Ceiling on cumulative overall cash deficit of the general government	13,792	3,652	12,698	19,111	-1,108	7,188
4. Ceiling on contracting or guaranteeing of new nonconcessional external debt by public sector (continuous, in millions of U.S. dollars) 2/	0	450	450	450	450	450
5. Ceiling on accumulation of new external payment arrears (continuous, in millions of U.S. dollars)	0	0	0	0	0	0
<i>Indicative Targets 1/</i>						
1. Ceiling on reserve money	48,597	50,390	52,464	56,571	57,155	59,014
2. Cumulative floor on state government tax collections	39,363	22,607	35,332	49,119	15,299	31,789
3. Floor on cumulative state government spending on targeted social assistance, Unified Monthly Benefit (UMB) and Monthly Social Benefit (MSB) programs	2,303	1,255	2,027	2,800	772	1,544

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

1/ As defined in the TMU.

2/ External debt contracted or guaranteed with a grant element less than 35 percent. The limit is cumulative from end-December 2010 and tied to energy infrastructure projects only. Should the total borrowings for these projects be less than US\$450 million, the remaining space cannot be used to borrow for other projects. While exact terms are still under negotiation, the grant element on these loans is expected to be slightly less than 35 percent, but will not be lower than 30 percent.

APPENDIX III. KYRGYZ REPUBLIC: TECHNICAL MEMORANDUM OF UNDERSTANDING**June 2, 2011****I. INTRODUCTION**

1. This memorandum defines the quantitative performance criteria, indicative targets and adjustors, and establishes the content and frequency of the data to be provided to IMF staff for program monitoring related to the economic program supported by an arrangement under the Extended Credit Facility (ECF). The indicators presented in Table 2 of the Memorandum of Economic and Financial Policies dated June 2, 2011 reflect the understandings on quantitative performance criteria reached between the authorities of the Kyrgyz Republic and staff of the IMF.

II. QUANTITATIVE PERFORMANCE CRITERIA**A. Definitions and concepts**

2. **Test dates.** Quantitative performance criteria are set semi-annually starting June 30, 2011 through June 30, 2012, and are to be met at the end of each period.

3. **National Bank of the Kyrgyz Republic (NBKR).** The NBKR is the central bank of the country and is responsible for the formulation and implementation of monetary policy, bank supervision, and the payment system. For the purpose of the program, the NBKR includes all its central and regional offices.

4. **Public sector.** For the purpose of the program, the public sector comprises the general government, the NBKR, and 10 largest nonfinancial public enterprises (enterprises and agencies in which the government owns more than 50 percent of the shares, but which are not consolidated in the budget, as listed in Table 1). The State budget comprises central and local government budgets. The general government budget includes the State, Social Fund and the Development Fund (hereinafter, KRDF) budgets.¹

5. **Foreign-financed Public Investment Program (PIP) loans and grants.** The foreign financed PIP is a program of investments in infrastructure and social sectors agreed by the general government of the Kyrgyz Republic and its donors (including but not limited to international financial organizations). The PIP is fully financed by related grants and loans.

6. **Program loans and grants** are loans and grants received by the general government for direct budget support from external donors and not related to PIP financing.

¹ KRDF will be included for the duration of its existence.

7. The stock of **external payment arrears** for program monitoring purposes is defined as the end-of-period amount of external debt service due and not paid within the grace period specified in the relevant debt contract, including contractual and late interest. For arrears to exist, a creditor must claim payment of amounts due and not paid. Amounts in dispute are not considered arrears. Arrears for which a clearance framework/rescheduling or restructuring has been agreed with the creditor are not considered arrears for program monitoring purposes. Program arrears would include any debt service due under such agreements that has not been paid.

8. **Concessional and nonconcessional debt.** Concessional debt is defined as debt with a grant element equivalent of 35 percent or more. The grant element of a debt is the difference between the present value (PV) of the debt and its nominal value, expressed as a percentage of the nominal value of the debt. The PV of debt at the time of its contracting is calculated by discounting the future stream of payments of debt service due on this debt. The discount rates used for this purpose are the currency specific commercial interest reference rates (CIRRs), published by the Organization for Economic Cooperation Development (OECD). For debt with a maturity of at least 15 years, the ten-year-average CIRR will be used to calculate the PV of debt and, hence, its grant element. For debt with a maturity of less than 15 years, the six-month average CIRR will be used. To both the ten-year and six-month averages, the same margins for differing repayment periods as those used by the OECD need to be added (0.75 percent for repayment periods of less than 15 years, 1 percent for 15 to 19 years, 1.15 percent for 20 to 29 years, and 1.25 percent for 30 years or more). The debt refers also to commitments contracted or guaranteed and for which value has not been received. The calculation of concessionality will take into account all aspects of the loan agreement, including maturity, grace period, payment schedule, upfront commissions, and management fees. The calculation is performed by the authorities and verified by the IMF staff based on the data provided by the authorities.

9. **Valuation changes (program exchange rates).** For program monitoring, U.S. dollar-denominated components of the NBKR's balance sheets will be valued at the program exchange rates. The program exchange rate of the KGS to the U.S. dollar is set at the end-2010 exchange rate of KGS 47.0992 = US\$1. The corresponding cross exchange rates and program gold price for the duration of the program are provided in Table 2.

B. Quantitative performance criteria

Floor on net international reserves of the NBKR in convertible currencies²

Definitions

10. **Net international reserves (NIR) of the NBKR.** The floor on NIR will be calculated as the difference between total international reserve assets and total international reserve liabilities of the NBKR in convertible currencies. Total international reserve assets of the NBKR are defined as the NBKR holdings of monetary gold, holdings of SDRs, reserve position in the IMF, and any holdings of convertible foreign currencies in cash or with foreign banks, and debt instruments issued by nonresidents that are liquid. Accrued interest on deposits, loans, and debt securities are included in reserve assets and liabilities, correspondingly. Reserve assets pledged as collateral or otherwise encumbered, capital subscriptions in foreign financial institutions, and illiquid assets of the NBKR are excluded. Also excluded are net forward positions, defined as the difference between the face value of foreign-currency denominated NBKR off-balance sheet claims on nonresidents and foreign currency obligations to both residents and nonresidents. Total international reserve liabilities of the NBKR in convertible currencies are defined as the sum of Kyrgyz Republic's outstanding liabilities to the IMF and other convertible currency liabilities to nonresidents with an original maturity of up to and including one year. NIR is not affected when foreign assets are received by the NBKR through foreign currency swaps with resident financial institutions. Total international reserves and NIR decline with the provision of foreign assets by the NBKR through foreign currency swaps with resident financial institutions.³ For program monitoring purposes, total international reserve assets and liabilities will be valued at the program exchange rates as described in paragraph 9 above. Thus calculated, the stock of net international reserves in convertible currencies amounted to US\$1,526 million on December 31, 2010.

11. **Net foreign assets (NFA) of the NBKR.** NFA consist of net international reserve assets plus other net foreign assets, including the medium- and long-term foreign obligations of the NBKR, other net claims on CIS countries, reserve assets pledged as collateral or otherwise encumbered, capital subscriptions in foreign financial institutions, and illiquid

² Convertible currencies are defined as currencies that are freely usable for settlements of international transactions.

³ In case of a foreign currency swap that involves receipt of foreign currency by the NBKR and transfer of local currency to a resident financial institution, total international reserves increase, NIR is unchanged, and net claims on domestic banks in soms increase. In case of a foreign currency swap that involves transfer of foreign currency by the NBKR and receipt of local currency from a resident financial institution, total international assets and NIR decline, while the NBKR net claims on resident banks remain unchanged.

assets. For program monitoring purposes, other NFA will also be valued at program exchange rates. Thus defined, other NFA is projected to amount to minus KGS 8280 million at end-June, end-September, and end-December 2011.

Adjustors

12. The floor on NIR will be adjusted upward/downward to the full extent of any excess/shortfall in program grants and program loans, as given in Table 3 and upward/downward to the full extent that amortization and interest payments of public external debt is less/more than the amortization and interest payments given in Table 3.

Ceiling on the net domestic assets of the NBKR

Definitions

13. **Net domestic assets** of the NBKR (NDA) are defined as reserve money of the NBKR (defined below), minus NFA as defined above. Items in foreign currencies will be valued at program exchange rates.

14. Thus defined, NDA consist of: (a) gross credit to the general government from the NBKR, minus deposits of the general government with the NBKR; (b) gross credit to domestic banks by the NBKR; c) net claims on other financial corporations and (d) all other net assets of the NBKR (other items net). Thus defined, the stock of NDA amounted to minus KGS 14,933 million on December 31, 2010.

Adjustors

15. The ceiling on NDA will be adjusted downward/upward to the full extent of any excess/shortfall in program grants and program loans, as given in Table 3 and downward/upward to the full extent that amortization and interest payments of public external debt is less/more than the amortization and interest payments given in Table 3.

Ceiling on the cumulative overall cash deficit of the general government

Definitions

16. **The overall cash deficit of the general government** will be measured from the financing side (below the line) at current exchange rates and will be defined as the sum of:

- a) the change in the stock of net claims of the domestic banking system and nonfinancial institutions and households on the general government. The change in the stock of net claims of the domestic banking system on the general government is defined as the change in the stock of the banking system claims on the general government, less the change in the stock of all deposits of the general government with the banking system. The claims of the banking system on the general government include: bank

- loans to the general government; any securities issued by the general government and held by domestic banks, with the exception of those issued in relation with bank rescue operations; and overdrafts on the current accounts of the general government with banks;
- b) the change in the stock of net claims of foreign governments, banking systems, and nonfinancial institutions and households on the general government;
 - c) net privatization receipts, i.e. any new sales net of purchases of shares;
 - d) net foreign loans disbursed to the general government for budgetary support; and
 - e) net foreign loans disbursed to the general government for PIP financing.

The quantitative performance criteria for the fiscal balance are calculated on the projected exchange rate. Reporting and adjustments, as defined above, will be made using current exchange rates.

Adjustors

17. The ceiling on the cumulative overall cash deficit of the general government will be adjusted downward to the full extent of any excess in program grants, as given in Table 3. The ceiling on the cumulative overall cash deficit of the general government will be adjusted downward to the full extent of any shortfall in program loans, as given in Table 3 and upward/downward to the full extent that PIP loans are more/less than PIP loans given in Table 3.

Ceiling on contracting or guaranteeing of new nonconcessional external debt by the public sector (continuous quantitative performance criteria)

Definitions

18. **Debt.** In connection with the contracting or guaranteeing of short-, medium-, and long-term external debt by any entity of the public sector, for program purposes, the definition of debt is set out in Executive Board Decision No. 6230–(79/140, Point 9, as revised on August 31, 2009 (Decision No. 14416–(09/91)) and reads as follows:

- a) For the purpose of this guideline, the term “debt” will be 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.
- b) Under the definition of debt set out in point 9 (a) above, 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.

For program purposes, external debt is defined based on the residency of the creditor.

19. **External debt ceilings** apply to the contracting or guaranteeing by the public sector (as defined in section II. A., paragraph 4) of nonconcessional external debt, i.e. external debt with grant element of less than 35 percent (see section II. A., paragraph 7), except normal short-term import-related credits and NBKR international reserve liabilities. The current nonzero ceiling (US\$450 million) is tied to infrastructure projects in the energy sector. Should the total borrowings for these projects be less than US\$450 million, the remaining space cannot be used to borrow for other projects. The grant element on these loans is expected to be slightly less than 35 percent but will not be lower than 30 percent.

20. **Exclusions from the external debt limits.** Disbursements by the IMF are excluded from the ceilings on external debt. Also excluded from external debt ceilings is the contracting or guaranteeing of new external debt that constitutes a rescheduling or refinancing of existing external debt on the terms more favorable to the debtor.

21. **Guarantees.** For program purposes, the guarantee of a debt arises from any explicit legal obligation of the public sector to service a debt in the event of nonpayment by the

debtor (involving payments in cash or in kind), or from any implicit legal or contractual obligation of the public sector to finance partially or in full a shortfall incurred by the debtor.

22. **New external payments arrears.** Ceiling on accumulation of **new external payments arrears** is a continuous quantitative performance criterion.

C. Indicative targets

Ceiling on reserve money

23. **Reserve money** is defined as the NBKR's national currency liabilities to the economy, which includes currency issued and liabilities to other depositary corporations.

Cumulative floor on state government tax collections

24. **Tax collections** in cash correspond to the line "Tax Receipts" in the Treasury Report and comprise the following categories: tax on income and profits; taxes on goods and services; specific taxes on services; turnover taxes; taxes on property; taxes on international trade; and other taxes. Tax collections include collections of tax arrears but exclude tax offsets.

Cumulative floor on state government spending on targeted social assistance

25. **Targeted social assistance spending** comprises state government spending on Unified Monthly Benefit (UMB) and Monthly Social Benefit (MSB) programs.

III. REPORTING REQUIREMENTS UNDER THE ARRANGEMENT

26. The government and the NBKR will provide the IMF with the necessary economic and financial statistical data to monitor economic developments and the quantitative targets (Table 4). In particular, the government and the NBKR will provide the following specific information.⁴

A. The balance sheet of the NBKR

27. The NBKR will provide to the IMF its analytical balance sheet on a daily basis. 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 (decomposition provided on a monthly basis); the net foreign assets of the NBKR; the net international

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

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, disaggregated by state government and the KRDF; net credit from the NBKR to commercial banks; net claims to other financial corporations; other items net; and reserve money. The balance sheet will be provided using both actual and program exchange rates. The above information will be provided to the IMF Resident Representative and/or transmitted by e-mail to the IMF.

B. Monetary survey

28. Monthly banking system data, in the form of monetary surveys of the banking sector and other depository corporations, will be reported to the IMF by the NBKR within 16 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 disaggregated by the state government, the social fund and the KRDF, net claims to the rest of the economy, other items net, and broad money. The monetary survey will be provided using both program and actual exchange rates.

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

C. International reserves and key financial indicators

30. The NBKR will provide detailed monthly data within 20 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; and second, at those specified in the program (Section I). The NBKR will also provide data on net foreign financing flows, including disbursements of program loans and grants, amortization, interest payments on external debt, interest income on reserves, other direct foreign currency payments by the government and the NBKR. In addition, weekly reports should be sent to the IMF on (a) nominal 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 domestic interbank market and with other parties, on a daily basis; and (b) treasury bill yields and the amount of treasury bill sales and redemptions on a weekly basis every Monday. On the twenty-fifth 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, nonperforming loans to total loans, and return on equity, as well as data on bank deposit and lending rates by maturity.

D. External debt

31. 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, nonfinancial public enterprises, 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 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.

E. Budgetary and extra budgetary data

32. In addition to the monthly treasury report, the Social Fund will report monthly on its operations. 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.

F. Balance of payments data

33. 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 three-month lag. The NBKR will also provide monthly foreign trade data with a two-month lag.

G. Other general economic information

34. The National Statistics Committee will notify the IMF of the monthly Consumer Price Index by category by the fifteenth business day of the following month, and convey monthly GDP estimates within 30 days of the end of each month.

Table 1. Kyrgyz Republic: Ten largest SOEs

	Name of SOE
1.	JSC KyrgyzAltyn
2.	JSC KyrgyzNefteGaz
3.	JSC "Electrical Stations"
4.	JSC "National Electrical Grid of Kyrgyzstan"
5.	JSC "Manas International Airport"
6.	JSC KyrgyzTelecom
7.	JSC SeverElectro
8.	SOE "National Company Kyrgyz Temir Jolu"
9.	JSC KyrgyzGaz
10.	JSC BishkekTeploset

Table 2. Kyrgyz Republic: Program Cross Exchange Rates and Gold Price

Abbreviation	Currency Name	Currency/US\$	US\$/Currency
AUD	Australian Dollar	0.9971	1.0029
CAD	Canadian Dollar	1.0098	0.9903
CNY	Chinese Yuan	6.6387	0.1506
JPY	Japanese Yen	83.0287	0.0120
KZT	Kazakh Tenge	147.4129	0.0068
KGS	Kyrgyz Som		47.0992
LVL	Latvian Lat	0.5406	1.8500
MYR	Malaysian ringgit	3.1012	0.3225
RUB	Russian Ruble	30.6345	0.0326
CHF	Swiss Franc	0.9635	1.0379
GBP	UK Pound Sterling	0.6487	1.5416
TRY	New Turkish Lira	1.5499	0.6452
SDR	SDR	0.6551	1.5266
BYR	Belarusian Ruble	3011.5757	0.0003
EUR	Euro	0.7622	1.3120
UAH	Ukrainian Hryvnia	7.9783	0.1253
XAU	Gold (\$/troy ounce)	1405.5000	...

Table 3. Kyrgyz Republic: Projected Budget Support, PIP, and Amortization
(In millions of U.S. dollars)

	2011 1/		
	June	September	December
Program grants	43.8	66.9	115.2
Program loans	17.1	123.8	140.3
PIP loans	69.7	126.0	143.5
Amortization of public external debt	23.2	28.7	43.2
Interest payments	26.2	41.3	46.5

1/ Cumulative disbursements since the beginning of the year

Table 4. Kyrgyz Republic: Reporting Requirements/Frequency under the Arrangement

Reporting Agency	Data	Frequency	Timing
NBKR	Analytical balance sheet of NBKR	Daily	The following working day
NBKR	Monetary surveys of the banking sector and other depository corporations	Monthly	Within 16 days of the end of each month
NBKR	The amount of holdings of treasury bills, treasury bonds and other securities issued by the state government	Monthly	Within 7 days of the end of each month
NBKR	The composition of both its gross and net international reserves in convertible currencies and holdings of monetary gold Net foreign financing flows	Monthly	Within 20 days of the end of each month
NBKR	Nominal exchange rates Foreign exchange interbank market turnover Volume of NBKR foreign exchange sales and purchases in the domestic interbank market and with other parties, on a daily basis; Treasury bill yields and the amount of treasury bill sales and redemptions	Weekly	The following working day
NBKR	Indicators of financial soundness of the banking system	Monthly	Within 25 days of the end of each month
MOF NBKR	Disbursements, principal and interest payment (external debt) Contracting and guaranteeing of medium- and long-term external loans Any stock of outstanding arrears on external debt service payments Total amount of outstanding government guarantees and external arrears	Monthly	Within 21 days of the end of each month
Social Fund	Social Fund operations report	Monthly	Within 26 days of the end of each month
MOF	Disbursements and use under the public investment program and budgetary grants	Monthly	Within 30 days of the end of each month
NBKR	Current account and capital account data	Quarterly	Within 90 days of the end of each quarter
NBKR	Foreign trade data	Monthly	Within 30 days of the end of each month
NSC	Consumer Price Index by category	Monthly	Within 15 days of the end of each month
NSC	GDP	Monthly	Within 30 days of the end of each month

INTERNATIONAL MONETARY FUND

KYRGYZ REPUBLIC

**Staff Report for the 2011 Article IV Consultation and Request for a Three-Year
Arrangement under the Extended Credit Facility
Informational Annex**

June 2, 2011

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ANNEX I. KYRGYZ REPUBLIC—RELATIONS WITH THE FUND
(As of April 30, 2011)

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
Net cumulative allocation	84.74	100.00
Holdings	105.10	124.04

IV. Outstanding Purchases and Loans	SDR Million	Percent of Quota
ESF Arrangements	33.30	37.50
RCF Loans	22.20	25.00
ECF Arrangements	52.79	59.44

V. Latest Financial Arrangements

	Approval	Expiration	Amount Approved	Amount Drawn
Type	Date	Date	(SDR Million)	(SDR Million)
ESF	12/10/2008	06/09/2010	66.60	33.30
ECF 1/	03/15/2005	05/31/2008	17.76	17.76
ECF 1/	12/06/2001	03/14/2005	73.40	73.40

1/ Formerly PRGF.

VI. Projected Payments to Fund 2/

(SDR million; based on existing use of resources and present holdings of SDRs)

	Forthcoming				
	2011	2012	2013	2014	2015
Principal	8.89	13.48	11.36	13.33	11.04
Charges/Interest	0.00	0.23	0.20	0.17	0.14
Total	8.89	13.71	11.56	13.50	11.19

2/ When a member has overdue financial obligations outstanding for more than three months, the amount of such arrears will be shown in this section.

VII. Status of HIPC and MDRI Assistance

Based on end-2004 data, the Kyrgyz Republic is potentially eligible for HIPC relief. The Executive Board considered the preliminary HIPC document on October 13, 2006. However, in 2007, the authorities indicated that they did not wish to avail themselves of debt relief under the HIPC Initiative.

VIII. Safeguards Assessments

Under the Fund's safeguards assessments policy, an update assessment of the National Bank of the Kyrgyz Republic (NBKR) was completed on April 9, 2009. Previous assessments were completed in October 2005 and in January 2002. The 2009 assessment found a strengthened safeguards framework at the central bank, but raised concerns and made recommendations about the need for updated terms of reference for audits of program data, and the lack of a benchmark financial reporting framework and multi-year audit appointments. An update assessment is currently underway with respect to the request for an ECF.

IX. Exchange Rate Arrangements

The currency of the Kyrgyz Republic has been the som (100 tyiyn = 1 som) since May 15, 1993. The de jure exchange rate arrangement is floating arrangement. The NBKR participates and intervenes in the interbank foreign exchange market to limit exchange rate volatility as necessary. The de-facto exchange rate arrangement is classified as other managed arrangement. The NBKR publishes daily the exchange rate of the som in terms of the U.S. dollar, which is determined in the interbank foreign exchange market. The official exchange rate of the som against the dollar is calculated as the daily weighted average of the exchange rates used in the purchase and sale transactions of dollars conducted in the foreign exchange market through the Trade Information Electronic System (TIES) of the NBKR for the reporting period from 3.00 pm of the previous trading day to 3.00 pm of the current trading day. The government uses the official exchange rate for budget and tax accounting purposes as well as for all payments between the government and enterprises and other legal entities. The official rate may differ by more than two percent from freely determined market rates, because the official exchange rate is set based on the average transaction-weighted rate of the preceding day, which may give rise to a multiple currency practice. In practice, the official and market rates have never differed by more than 2 percent.

The Kyrgyz Republic maintains an exchange system that is free of restrictions on the making of payments and transfers for current international transactions, except for exchange restrictions maintained for security reasons relating to the restriction of financial transactions and the freeze of accounts of certain individuals or organizations associated with terrorism pursuant to (i) relevant UN Security Council resolutions, and (ii) the list of current terrorist

organizations designated by the U.S. Secretary of State. The authorities have notified these measures to the Fund.

X. Article IV Consultations

The Kyrgyz Republic is on the 24-month consultation cycle. The last Article IV consultation discussions were held in March 2009 and were completed by the Executive Board in May 2009 (see Country Report No. 09/209, 5/11/09).

XI. FSAP Participation and ROSC Assessment

An FSAP update mission in October 2006 reviewed progress since the 2002 assessment, and the Board considered the Financial System Stability Assessment (FSSA) along with the fourth PRGF review in May 2007. A fiscal ROSC mission was held in March 2001 and the ROSC Fiscal Transparency Module was published on March 13, 2002. A data ROSC mission was held in November 2002 and the ROSC Data Module was published in November 2003. A fiscal ROSC reassessment was held in September 2007.

XII. Resident Representative

The eighth resident representative of the Fund in the Kyrgyz Republic, Mr. Gvenetadze, took up his post in Bishkek in October 2009.

ANNEX II. KYRGYZ REPUBLIC—RELATIONS WITH THE WORLD BANK GROUP
(As of May 19, 2011)

World Bank Group Strategy: A Joint Country Support Strategy 2007–10 (JCSS)—one of the earliest in the Bank—was prepared for the Kyrgyz Republic by a group of six donors and presented to the Board in mid-2007. Currently The Kyrgyz Country team is working on preparation of the Interim Strategy Note (ISN). The proposed ISN builds on the achievements of the JCSS and the lessons drawn from its experience. It is intended to cover two fiscal years: 2012 and 2013. Its need arises from the acute political and social uncertainties faced by the country following turmoil in mid-2010, and the absence of a medium term development framework upon which a full IDA strategy could be based. The ISN is built around the near-term program of an elected government as well as strong donor partnerships, characterized by joint IMF and IDA funding of budgetary needs together with other multilateral donors, and well developed joint initiatives in high poverty-impact investment programs, in such areas as health and community development.

IDA allocation: IDA-15 allocations for the Kyrgyz Republic were on a 45 percent grant and 55 percent credit basis. IDA allocations for the FY11 were US\$136 million, including US\$10.4 million from Crisis Response Window (CRW) facility and US\$56 million from reallocation of IDA-15 envelope.

IDA Portfolio: The active portfolio consists of 19 IDA financed investment projects and one budget support operation, totaling US\$302.6 million out of which US\$165.9 million has been disbursed.

FY11 Lending Program: In FY11, following the Donors Meeting in 2010 (see below) and in response to the considerable needs of the country for financial assistance, the Bank prepared two emergency operations: an Emergency Recovery Project (ERP) in the amount of US\$70 million (US\$54.40 million from IDA and US\$15.60 million from CRW), and an Additional Financing for the National Road Rehabilitation Project (Osh-Batken-Isfana) in the amount of US\$10 million, both processed under Operational Policies; OP.8.0, *Rapid Response to Crises and Emergencies* and approved in September 2010. In addition, the second Education for All- Fast Track Initiative (EFA-FTI) grant in the amount of US\$6 million to support the Government's introduction of the national school preparation program has been approved this FY.

Trust Funds: In addition to IDA funds, the Bank manages a significant number of co-financing and stand-alone Trust Funds. To date, the TF Portfolio has a total value of US\$98.4 million including 17 Bank Executed TFs and 20 Recipient Executed TFs, out of which US\$72.6 million has been disbursed. The largest TF donors are EU, SDC, DFID and Japan.

AAA Program: The Bank led the preparation of a Joint Economic Assessment (JEA), together with the Asian Development Bank and the International Monetary Fund, with the

participation of four other donors. The JEA, which followed the principles of the European Commission-United Nations-World Bank agreement Joint Declaration on Post-Crisis Assessments and Recovery Planning, 2008, was presented at the High Level Donors Meeting on July 27, 2010, where donors pledged US\$1.1 billion over a 30-month period including US\$200 million pledged by the World Bank. The FY11 AAA program also includes a Poverty Update; an Agricultural Policy Update, Financial Sector Reform and Strengthening (FIRST) Initiative TAs on: (i) Strengthening Bank Supervision and Resolution, (ii) Strengthening the Legal, Regulatory, Supervisory and Market Infrastructure Framework for Non-Bank Financial Institutions (NBFIs) and Securities Markets, and (iii) Deposit Protection Agency (DPA) Capacity Building.

Pipeline projects: The Kyrgyz Republic has received an additional US\$56 million from the IDA-15 reallocation. There are five IDA operations under preparation, scheduled for Board presentation in May–June, 2011:

1. Central Asia Hydrometeorology Modernization project (US\$2 million of IDA country allocation and US\$4 million of CA regional allocations) with an objective: (i) to improve coordination, information sharing and training between NMHSs of the Central Asian countries; and (ii) strengthen the hydromet service delivery in Kyrgyz Republic and Republic of Tajikistan and in other participating Central Asia countries.
2. Additional Financing for Health and Social protection SWAP (US\$24 million) to finance the implementation of expanded activities that scale-up the project's impact and its development effectiveness. Specifically, it would finance activities associated with the conflict in the Osh and Jalalabad provinces in June 2010, which exacerbated the already poor health, nutrition and social conditions in the South of the country.
3. Additional Financing for Disaster Hazard Mitigation project (US\$1 million) to cover a financing gap in the original DHMP.
4. The Second Additional financing for National Road Rehabilitation project (US\$16 million) to scale up of NRRP project activities to improve road infrastructure, reduce travel time, lower vehicle operating costs, and provide reliable access to social services and economic activities for the population (in particular living along the road corridor in Batken and Osh oblasts), as well as improve management of the road network in the country.
5. Additional Financing for On-farm Irrigations project (US\$15 million) to finance the costs associated with scaling up of OIP-2 project activities to enhance the impact of this well-performing project, especially on vulnerable rural communities in the south of the Kyrgyz Republic which have been affected by ethnic clashes in the summer of 2010.

In addition to IDA financed operations, two projects, financed by TFs are also under preparation:

1. Food Security and Agriculture Productivity Assistance project in the amount of US\$6.85 million is being prepared for financing under the Russia Food Price Crisis Rapid Response Trust Fund made available to the Kyrgyz Republic.
2. Health Result based Financing project (US\$12 million) to assess the impact of the RBF pilot on quality of health care.

The ISN is scheduled for Board presentation on July 26, 2011 along with Economic Recovery Support Operation (ERSO). The ERSO (US\$30 million), a budget support operation, will support the Government's efforts to strengthen public sector governance, address urgent social and reconstruction needs and restore private sector confidence, all critical to put the country back on track to recovery, growth and poverty reduction.

IFC Program and Portfolio

1. The International Finance Corporation (IFC) continues to contribute to sustainable private sector development with long-term financing and advisory services to local financial institutions, and direct financing to small enterprises for the expansion and modernization of their operations. **The engagement of IFC has accelerated in the period of 2007–10, and these efforts have been complimentary to WB efforts in private sector development and development of the financial sector.** IFC will continue focusing on private sector development and aiming to increase its investments with a particular focus on the banking, manufacturing, mining, and agribusiness sectors. In addition, IFC is planning to participate in financing investment programs of privatized entities if privatization is undertaken in an open and transparent manner and in line with international best practice. In infrastructure, IFC is exploring opportunities, primarily on a subnational basis, in power transmission, hydropower plants, and municipal utilities. In addition, an IFC Infrastructure Advisory program is being implemented in the Central Asia region and IFC is seeking to engage with the Kyrgyz government to assist with privatizations and concessions.

2. IFC STRATEGY AND PROGRAM:

- **Increase access to finance for MSMEs** by strengthening local financial institutions and providing credit lines for MSME financing to local banks and expanding microfinance institutions.
- **Develop institutional capacity** and support capacity building of financial institutions (including leasing and insurance, if there are opportunities) and microfinance companies and **improve corporate governance** in local enterprises.
- Increase private sector participation in **infrastructure** through selective advisory and investment climate engagement.
- Assist the **agribusiness** sector directly and through MSMEs finance to banks and microfinance companies.
- Support the improvement of **business environment and investment climate**.

Since becoming a member of IFC in 1993, the Kyrgyz Republic has received commitments totaling more than US\$90 million from IFC's own funds to finance more than 25 projects in the financial, banking and microfinance, oil, gas and mining sector, agribusiness, pulp and paper sectors. **New commitments in 2007–10 amounted to US\$27.4 million.** As of April 1, 2011, IFC's committed portfolio was US\$28 million, which includes investments in six companies, representing banking, microfinance and real sector companies.

IFC will continue its advisory services work in the financial sector, developing corporate governance and improving the business environment. The Azerbaijan-Central Asia Financial Infrastructure Project is planning to complete its work on the Code of Conduct, strengthen the institutional capacity of the private credit bureau, and possibly work on the special law on credit bureaus. The Investment Climate project will continue working with the government on ensuring higher transparency standards by helping to draft the new Law on Inspections and working with inspectorates on introducing risk-based criteria for inspections and using checklists during inspections. In order to address the revenue transparency and financial disclosure challenge in the Kyrgyz Republic, a new Project on Regulatory Reform and Tax Transparency has been launched in 2011 to identify the main policy constraints and root causes of low formalization and poor tax compliance by real sector companies and define a set of actionable policy options to increase compliance and formalization. The project is expected to complement the efforts of IFC's Investment Climate work and facilitate an increase in IFC investments in the real sectors of the economy.

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. The total amount of foreign direct investment facilitated by MIGA guarantees is over US\$360 million.

MIGA's current portfolio in the Kyrgyz Republic consists of guarantees for two projects in the transport sector: an airline (Kyrgyz Airlines) and an airport services company (Manas Management Company). The projects are owned by Austrian and Italian investors. The combined gross exposure from these projects is US\$14.8 million. Both of these projects were the subject of disputes between the investors and the Government during the last four years. The settlement between the Kyrgyz Government and investors, which was worked out in May of 2008 with MIGA's mediating role, has now been fully implemented by both sides. This finally resolves this matter that had been pending for more than four years. In August 2009 MIGA's guarantee holders withdrew their claim against MIGA and released MIGA from any liability. In addition, they have dismissed their claims against the government, which had been pending in the London Court of International Arbitration. At present, there are no new projects in the Kyrgyz Republic in MIGA's FY11 pipeline.

**Table 2: Active Project Portfolio
As of February 2010
(USD Equivalent)**

#	Project Name	Commitment Amount	Total Disbursed	Total Undisbursed
1.	Second Rural Water Supply & Sanitation	\$10,000,000.00	\$248,802.76	\$9,751,197.24
2.	Emergency Energy Assistance	\$15,000,000.00	\$10,112,315.00	\$4,887,685.00
3.	Second Land and Real Estate Registration Project	\$5,850,000.00	\$1,263,968.98	\$4,586,031.02
4.	Capacity Building for Economic Management Grant	\$3,000,000.00	\$308,379.16	\$2,691,620.84
5.	Agricultural Investments and Services Project	\$13,000,000.00	\$5,895,444.35	\$7,104,555.65
6.	Bishkek and Osh Urban Infrastructure Project	\$12,000,000.00	\$2,861,339.18	\$9,138,660.82
7.	Second On-farm Irrigation Project	\$16,000,000.00	\$4,460,318.81	\$11,539,681.19
8.	Reducing Technical Barriers for Entrepreneurship and Trade	\$5,000,000.00	\$1,162,874.60	\$3,837,125.40
9.	Second Village Investment Project	\$23,000,000.00	\$14,149,797.43	\$8,850,202.57
10	Water Management Improvement Project (WMIP)	\$19,000,000.00	\$4,534,815.76	\$14,465,184.24
11	Avian Influenza Control & Human Pandemic Preparedness & Response Project	\$4,000,000.00	\$2,512,726.90	\$1,487,273.10
12	Health & Social Protection Project	\$21,000,000.00	\$14,782,145.97	\$6,217,854.03
13	Small Towns Infrastructure & Capacity Building Project	\$19,000,000.00	\$15,333,696.28	\$3,666,303.72
14	Rural Education Project	\$15,000,000.00	\$12,568,366.91	\$2,431,633.09
15	Agribusiness & Marketing Project	\$8,100,000.00	\$4,387,640.94	\$3,712,359.06
16	Disaster Hazard Mitigation Project	\$6,900,000.00	\$2,325,626.40	\$4,574,373.60
17	Payments & Banking System Modernization Project	\$9,000,000.00	\$4,871,485.05	\$4,128,514.95
18	Governance Technical Assistance Project	\$7,775,000.00	\$1,349,812.39	\$6,425,187.61
19	National Road Rehabilitation (Osh-Batken-Isfana)	\$25,000,000.00	\$336,800.00	\$24,663,200.00
	Total:	\$237,625,000.00	\$103,466,356.87	\$134,158,643.13

Table 3: Active Trust Funds Portfolio
As of February 2010
(USD Equivalent)

#	Fund	Fund Name	Disbursements	Grant Amount
Bank Executed Trust Funds			17,894,849.31	23,803,327.16
1	TF094665	READ FUNDING FOR THE KYRGYZ REPUBLIC	22,784.83	250,000.00
2	TF095028	JAPAN CTF - FY10: GENERAL BBMC (ALL BANK BORROWING MEMBER COUNTRIES/ALL SECTORS AND THEMES)	341,861.19	2,318,500.00
3	TF055016	CARBON FINANCE ASSIST (DISBURSING FUND UNDER TF054846)	9,308,062.17	9,571,226.54
4	TF094477	KG FTI CF - SUPERVISION COST	61,245.17	100,000.00
5	TF054857	EFA FTI EDUCATION PROGRAM DEVELOPMENT FUND-EUROPE/CENTRAL ASIA	1,004,933.47	1,060,000.00
6	TF091980	KYRGYZ (EFA FTI EPDF-ECA): CAPACITY DEVELOPMENT	54,726.71	120,000.00
7	TF091981	KYRGYZ (EFA FTI EPDF-ECA): MONITORING EVALUATION & KNOWLEDGE SHARING	36,270.19	324,000.00
8	TF091982	KYRGYZ (EFA FTI EPDF-ECA): STRENGTHEN PARTNERSHIPS	29,655.70	264,000.00
9	TF092574	KRYGYZ EPDF -- EDUCATION SECTOR PLAN	32,277.19	80,000.00
10	TF090581	KYRGYZ REPUBLIC: SUPPORT TO DEVELOPMENT OF THE NATIONAL STRATEGY ON SECONDARY USE OF RANGELAND	93,377.48	130,000.00
11	TF054664	EXTRACTIVE INDUSTRIES TRANSPARENCY INITIATIVE - CHILD TF	3,291,980.09	3,397,192.50
12	TF090446	BANK EX.SUPPORT FOR EITI IN COUNTRY IMPLEMENTATION	2,663,240.51	3,000,000.00
13	TF091286	KYRGYZSTAN: NBFICAPACITY BUILDING	301,959.02	450,100.00
14	TF058124	DISBURSING CHILD FUND - LEGACY PROJECTS	4,741.04	145,451.20
15	TF094017	FIRST 8106: KYRGYZ REPUBLIC: PRE-PRIVATIZATION ADVICE - AIYL BANK	63,394.91	124,000.00
16	TF094144	W2-INFORMATION MATTERS - TRANSPARENCY AND ACCOUNTABILITY IN THE KYRGYZ REPUBLIC	64,397.21	1,351,000.00

17	TF094769	KYRGYZ REPUBLIC HRBF PILOT ACTIVITIES	107,753.75	400,000.00
18	TF093593	BUILDING INSTITUTIONAL CAPACITY FOR TRADE POLICY ANALYSIS IN THE KYRGYZ REPUBLIC	28,224.70	41,000.00
19	TF050683	NORWAY/WORLD BANK INSTITUTE (WBI) PROGRAMME IN GOVERNANCE - PHASE II	366,581.98	356,824.33
20	TF096039	EU TF Food Security: Global Food Crisis Response	17,382	320,032.59
Recipient Executed Trust Funds			55,033,831.16	74,935,001.09
1	TF091994	KYRGYZ REPUBLIC - AVIAN INFLUENZA CONTROL AND HUMAN PANDEMIC PREPAREDNESS AND RESPONSE PROJECT	202,130.00	352,000.00
2	TF091995	KYRGYZ REPUBLIC - AVIAN INFLUENZA CONTROL AND HUMAN PANDEMIC PREPAREDNESS AND RESPONSE PROJECT	501,718.36	798,000.00
3	TF090141	KYRGYZ REPUBLIC: EDUCATION FOR ALL FAST TRACK INITIATIVE CATALYTIC FUND	8,761,953.97	9,000,000.00
4	TF090545	KYRGYZ REPUBLIC - SUPPORT TO THE EXTRACTIVE INDUSTRIES TRANSPARENCY INITIATIVE	128,203.53	265,725.00
5	TF056540	DFID TRUST FUND, KYRGYZ HEALTH AND SOCIAL PROTECTION PROJECT	9,735,137.29	12,822,669.58
6	TF056799	SDC: KYRGYZ REPUBLIC - HEALTH AND SOCIAL PROTECTION PROJECT	2,999,971.06	3,000,000.00
7	TF090119	SWEDISH TRUST FUND, KYRGYZ HEALTH AND SOCIAL PROTECTION PROJECT	7,515,701.25	12,544,586.35
8	TF091613	SDC TRUST FUND, KYRGYZ HEALTH AND SOCIAL PROTECTION PROJECT	2,179,729.00	3,724,000.00
9	TF095472	Capacity Building in Public Financial Management	0	4,555,957.00
10	TF090072	SECOND VILLAGE INVESTMENT PROJECT IN THE KYRGYZ REPUBLIC	12,361,679.21	13,622,463.16
11	TF055171	GEF MSP-KYRGYZ REPUBLIC : DISASTER HAZARD MITIGATION PROJECT	902,121.18	1,000,000.00
12	TF091930	GEF PPG - TIEN SHAN ECOSYSTEM DEVELOPMENT PROJECT - KYRGYZ REPUBLIC	44,385.22	50,000.00
13	TF057893	KYRGYZ REPUBLIC: IDF GRANT FOR HEALTH SECTOR MONITORING AND EVALUATION CAPACITY BUILDING PROJECT	29,001.79	130,000.00

14	TF090667	KYRGYZ REPUBLIC: IDF GRANT FOR CAPACITY BUILDING IN PUBLIC SECTOR AUDITING	128,690.64	370,000.00
15	TF053437	PHRD-KYRGYZ REPUBLIC: NATURAL DISASTER MITIGATION PROJECT	1,949,919.20	1,950,000.00
16	TF053554	PHRD-KYRGYZ REPUBLIC: AGRIBUSINES AND MARKETING PROJECT	2,872,614.95	4,750,000.00
17	TF056157	PHRD-KYRGYZ REPUBLIC: AVIAN INFLUENZA CONTROL AND HUMAN PANDEMIC PREPAREDNESS AND RESPONSE (AIPP)	725,695.07	1,000,000.00
18	TF056324	PHRD-KYRGYZ REPUBLIC: WATER MANAGEMENT IMPROVEMENT PROJECT	3,747,432.02	4,400,000.00
19	TF090641	PHRD-KYRGYZ REPUBLIC: REDUCING TECHNICAL BARRIERS FOR ENTREPRENEURSHIP AND TRADE	115,163.54	299,600.00
20	TF091817	KYRGYZ REPUBLIC: IMPLEMENTATION OF STATISTICAL MASTER PLAN	132,583.88	300,000.00

**ANNEX III. KYRGYZ REPUBLIC—RELATIONS WITH THE ASIAN DEVELOPMENT BANK
(ADB)**
(As of May 1, 2011)

The Kyrgyz Republic joined ADB in 1994. ADB's country partnership strategy for the Kyrgyz Republic is presented in the joint country support strategy¹ (JCSS) for 2007–10. The JCSS was prepared in cooperation with four development partners—the Swiss Cooperation, the United Kingdom's Department for International Development, the United Nations Agencies, and the World Bank Group. Three other development partners—the European Commission, the German Government (presented by GTZ and KfW), International Monetary Fund, and United States Agency for International Development joined the JCSS at the later years. In line with the country development strategy, the JCSS identifies four priority areas: (i) promoting economic management consistent with strong and sustained pro-poor growth; (ii) improving governance, promoting effective public administration, and reducing corruption; (iii) building sustainable human and social capital; and (iv) ensuring environmental sustainability and natural resources management.

ADB's country operations business plan (COBP) 2011–12 updates the country strategy and program 2007–10 to better help the country address challenges that arose after political disturbances in April 2010 and a conflict in June 2010, while maintaining consistency with the priorities set out in ADB's Strategy 2020.² The program for 2011–12 continues support to public infrastructure and institutional reforms, which will contribute to creating a favorable environment for sustainable growth with broader private sector participation, thereby generating more jobs and income. ADB will continue to support: (i) transport, (ii) water supply and other municipal infrastructure and services, (iii) energy, and (iv) public sector management. Continued support for the education sector, especially for skills development, is being discussed.

ADB is one of the major development partners in the country. All assistance provided to the Kyrgyz Republic is from concessional ADB's special fund resources—Asian Development Fund (ADF). As of 31 March 2011, the country has received 31 loans worth US\$736.2 million, 14 ADF and 1 GEF grants worth US\$249.1 million. The Kyrgyz Republic has also received seven grants from Japan Fund for Poverty Reduction (JFPR grants) amounting to US\$7 million. Nine operations totaling US\$252 million provided to support policy reforms to facilitate the transition to a market economy. The remaining operations (worth US\$733.3 million) were provided to support various investment activities. At present, 6 loans and 11 grants with approved amount of US\$370.3 million are ongoing.

¹ ADB. 2007. *Joint Country Support Strategy (2007–10): Kyrgyz Republic*. Manila.

² ADB. 2008. *Strategy 2020: The Long-Term Strategic Framework of the Asian Development Bank, 2008–2020*. Manila.

The Kyrgyz Republic has been eligible for 50 percent grant and 50 percent ADF loan since 2009. The indicative allocation for the two years 2011–12 is US\$120 million.

In addition to investment loans and grants, ADB has provided 74 technical assistance (TA) projects amounting to US\$42.7 million as of today.

The performance of ADB's portfolio is generally satisfactory with no loans or grants rated at risk. ADB's annual lending began with US\$40 million in 1994 and reached the peak level of US\$167.8 million in 2010.

The Kyrgyz Republic was selected as one of the pilot countries during the February 2003 Rome Conference on Harmonization. Since then key development partners have learned to better coordinate and harmonize procurement procedures, oversee financial management and monitoring, share project implementation units, and conduct joint country portfolio reviews. The JCSS for the Kyrgyz Republic has been prepared by five funding agencies. The areas identified for harmonization in the immediate future are: (i) procedures for procurement of goods and services; (ii) financial management and monitoring of projects; and (iii) project implementation units. World Bank and ADB procurement documentation has been harmonized in these areas.

ADB cooperates extensively with civil society organizations in the Kyrgyz Republic to strengthen the effectiveness, quality, and sustainability of the services it provides.

**ANNEX IV. KYRGYZ REPUBLIC—RELATIONS WITH THE EUROPEAN BANK FOR
RECONSTRUCTION AND DEVELOPMENT (EBRD)**

(As of May 1, 2011)

Overview of EBRD Activities to Date

The Bank has been actively supporting the transition in Kyrgyz Republic since 1995. From 1995 to the end of 2010, the Bank signed 72 projects accounting for a net cumulative business volume of €338 million at end 2010. Over the past three years the Bank signed on average 9–10 projects per year with a total of 29 projects and €154 million in volume over the period with an average project size of €5.3 million. The Bank has continued to disburse commitments at approximately €15 million per year. The current private sector portfolio ratio (as a percentage of the total portfolio) is 84 percent which is well above the Bank's 60 percent mandated ratio.

Fostering the Private Sector: The Bank's operations in support of local private enterprises took advantage of the ETC Initiative, which was instrumental in enabling the Bank to deliver a number of small projects with significant transition impact, particularly in the areas of corporate governance and business conduct. In all, the Bank supported eight local operations under the ETC Initiative. The impact of the global financial crisis and the domestic socio-political crisis impeded the Bank's ability to generate the volume of projects originally anticipated. In particular, a number of private sector projects under preparation when the crises hit—under DLF, DIF or MCFF—were cancelled or postponed as they became unbankable.

- Under the Direct Lending Facility (DLF), the Bank supported two property sector operations (a local hotel at the Issyk Kul Lake and a residential compound in Bishkek), a glass manufacturer, a construction materials producer, and a local food and beverages producer. As a result of the two crises, the Bank supported fewer DLF operations than expected: following the global financial crisis in 2008–09, the number of potential property projects decreased; following the socio-political turmoil in 2010, several DLF projects under preparation were cancelled and/or postponed.
- Under the Medium-sized Co-Financing Facility (MCFF), the Bank supported a leading food retailer with two MCFF loans. These were the Bank's first deals in the country's retail sector and the first sub-project with a new MCFF partner bank (Demir Kyrgyz International Bank). This was a modest achievement, with fewer deals under MCFF than expected coming to fruition. Following the 2010 crisis, it was particularly difficult to identify larger size investment projects that could be well supported by MCFF.
- Under the Direct Investment Facility (DIF), the Bank took a 34 percent equity stake in a local dairy producer and provided technical assistance under the TAM program to help it expand its processing plant. This operation complimented an initiative by the Swiss Government to revive the local economy in remote regions. DIF has proven to be a

difficult instrument to deploy widely, as potential clients in the country are not yet ready to discuss the market value of their companies in accordance with international standards. Implementation of DIF operations in Kyrgyz Republic have also been quite labor intensive.

- Under the TAM/BAS program, the Bank facilitated the skill transfers to the local consultancy industry and improved the know-how and management of the MSME sector through the provision of management and advisory services to over 500 small local enterprises under the TAM/BAS grant-funded program. This included a successful crisis response initiative in the South in 2010. Despite the difficult business climate, turnover increased in nearly 50 percent of TAM/BAS in the year following project completion, and 16 percent of the clients secured external investments. The Bank has supported the growing professionalism of local advisory services to serve the MSME sector on a sustainable basis and introduced more sophisticated advisory services in areas such as quality management and energy efficiency.
- The Bank supported a landmark large scale operation with a foreign strategic investor in 2010: a US\$150 million three-year revolving credit facility with Centerra Gold Inc. in support of the company's ongoing operations and potential acquisitions of mining assets, signed in 2010. The company, 33 percent owned by the Kyrgyz state, owns the Kumtor gold mine, which generates 30 percent of country's foreign currency reserves and 10 percent of its GDP. One of the major achievements of the project was to improve the reporting of taxes paid by the mining industry under the "Extractive Industries Transparency Initiative (EITI)" and on March 2011, the Kyrgyz Republic became "EITI Compliant". The EBRD supported this process through the active policy dialogue with the authorities and Centerra, the largest mining company in the country.

Strengthening Financial Institutions: The Bank provided crucial support to financial institutions during the previous strategy period at a time when the country was feeling the impact of the global financial crisis in 2008–09 and the domestic socio-political crisis in 2010. The global financial crisis affecting Russia and Kazakhstan had a knock-on effect on the Kyrgyz Republic, in terms of lower demand for Kyrgyz exports and a fall in inflows of remittances to fund private consumption. As the Kyrgyz banking system was dominated by banks with foreign capital, particularly from Kazakhstan, all banks and nonbank micro financial institutions reduced or stopped lending by the end of 2008. The Bank's crisis response included:

- In 2009, provision of local currency financing to banks. The Bank provided three local banks and three non-bank micro financial institutions (NBMFIs) with local currency credit lines totalling the equivalent of €22.7 million at a time of scarce alternative commercial funding.
- In 2010, the Bank disbursed US\$6.5 million equivalent (mainly in local currency) under four existing committed credit facilities in support of local enterprises. The Bank's

continued support to the financial sector after the events of April and June 2010 was seen as a strong signal to the Bank's clients as well as other lenders to the sector.

- In the context of ongoing work to address local currency lending broadly across the region under the Bank's Local Currency and Local Capital Market Initiative, the Bank developed a proposal for local currency financing mechanisms, which was approved in February 2011. The Bank aimed to ensure more competitively priced and less volatile local currency operations and to decrease systemic dollarization risk in the financial sector by introducing a risk-sharing scheme supported by donor funds.
- In response to the crisis in 2010, the Bank supported the National Bank with technical assistance, including through supporting its efforts to restructure Asia Universal Bank (AUB), the largest bank in terms of assets prior to the events in 2010, with a forensic audit of its accounts. This has helped contain a possible systemic crisis in the banking system.

During the past strategy period, the Bank continued moving its partners forward in area of corporate governance, through strengthening external and internal audit, improving shareholder transparency, and implementing better internal policies and procedures. The Bank also conducted training courses for its partner banks in the area of anti-money laundering (AML), which will continue to support better AML standards both at Government and bank levels, and may help to reduce crime and corruption. AML is important in helping local banks and NBMFIs with their transition to more transparent and commercially oriented operations.

Support for Critical Infrastructure: During the previous strategy period, the Bank financed two key infrastructure projects, the first projects to be financed by the Bank in this sector since 1997. However, intentions to finance infrastructure projects on the basis of PPPs turned out to be overly ambitious, given the very weak legal and regulatory framework and the early stage of transition.

- The Bank provided a US\$35 million sovereign loan to finance the renovation of the highway linking the towns of Osh, Batken and Isfana. This road plays a crucial role as an international transit route in the region by linking Uzbekistan, Tajikistan and China. Through its financing and policy dialogue the Bank sought the following transition objectives: (i) introduction of tendering procedures for periodic road maintenance, (ii) refining road user charges and reform of the Road Fund, (iii) formulating the privatization plan for maintenance units, and (iv) introducing service level agreements for routing maintenance.
- In the municipal infrastructure sector, the Swiss Government and the EBRD provided €11.8 million to improve the water supply in Bishkek. The project is financed by a grant of €5.7 million from the Swiss Government and a €5.5 million sovereign loan from the

EBRD. Projects in the water sector enabled the Bank to make progress with water tariff reforms, meeting IFRS accounting standards, and promoting efficiency in the Bishkek water company.

- Despite the difficult domestic situation following the events in April and June 2010, the Bank continued the implementation of the municipal water project and the preparation of projects in urban transport and solid waste in Bishkek. In May 2011, the Bank signed new water/wastewater projects for Osh and Jalalabad.

Policy Dialogue: In line with the 2007 strategic priorities for policy dialogue described above, the Bank has been working to enhance its dialogue with the government to improve the investment climate and address bottlenecks affecting local and regional investors, coordinating with other international financial institutions, donors and the business community. With generous support from donors, the Bank has provided critical assistance to the secretariat for the Investment Council since its establishment in early 2007 and implemented legal TC for the training of judges.

- The Investment Council has been providing local and international business representatives (representing the mining, industry, agro-processing and tourism sectors) with a forum to discuss the main barriers to doing business with top officials of the government. Following the political events and subsequent changes in 2010, the new government acknowledged its commitment to improve the investment climate in the country and renamed the council as the Council for Business Development and Investment. The donor community expressed its readiness to continue its full support to the Council under the new government.
- The Bank participated in the IFIs Joint Economic Assessment (JEA), which set out a strategic framework for reconciliation, recovery and reconstruction after the April and June events of 2010. The JEA identified the need for external support in three major areas, including essential public expenditures, social needs, and critical investments. The JEA helped the government to achieve economic recovery more quickly than expected after months of political turmoil.
- The Bank continued to actively engage in policy dialogue with the government and local authorities to promote the further reform agenda in corporate and infrastructure sectors, although reform efforts were temporarily suspended due to the internal political crisis.
- The Bank strengthened its collaboration with the Kyrgyz Supreme Court with a view to increasing capacity in the judiciary dealing with commercial disputes. Since 2007, the Bank provided technical advice to the Judicial Training Centre, trained judicial trainers, delivered commercial law training seminars for up to 240 existing judges, created a law library at the Supreme Court, organized internships in the courts of Kazakhstan and Russia, and published a bench book on commercial law. The Bank expanded its assistance in 2010 to help establish a training system for candidate judges, and implement a fair and transparent judicial selection process.

ANNEX V. KYRGYZ REPUBLIC—TECHNICAL ASSISTANCE PROVIDED BY THE FUND

February 2003–May 2011

Dept.	Subject/Identified Need	Timing	Counterpart
FAD	Improving the Effectiveness of the Large Taxpayer Unit	February 24–March 7, 2003	Ministry of Finance
	Treasury Management Information System	July 21–29, 2003	Ministry of Finance
	VAT on agriculture	November 3–11, 2003	Ministry of Finance
	Priorities for Tax Administration Reform	July 22–August 5, 2004	Ministry of Finance
	Supporting Tax Administration Reform and installing new Expert Advisor	January 16–28, 2006	Prime Minister's office
	Fiscal ROSC Reassessment (Fiscal Transparency Module)	September 11–25, 2007	Ministry of Finance
	Securing Tax Revenues During the Economic Downturn	March 9–20, 2009	Ministry of Finance
	Strengthening the Link between Fiscal Policy and Budget Preparation	October 12–23, 2009	Ministry of Finance
	Monitoring Expenditure Arrears; Adjusting the new BO-COA	October 20–23, 2009	Ministry of Finance
	IMF peripatetic assignment to support overall LTO (large taxpayer office) enhancement	February 22–March 12, 2010	State Tax Service
	Reviewing Treasury's Work and Advising the Authorities on COA Issues	February 15–18, 2011	Ministry of Finance
	Tax Policy Advice	April 20–May 4, 2011	Ministry of Finance, State Tax Service, State Customs Service
MFD/ MCM	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
Monetary Operations, Banking System Development, and Central Bank Autonomy	September 13–23, 2004	National Bank of the Kyrgyz Republic
Review of NBKR Debt Restructuring Arrangements, Options for Deepening Financial Markets and Amendments to the NBKR Law	December 7–18, 2004	National Bank of the Kyrgyz Republic
Payments System	January 25–February 7, 2005, April 12–25, 2005, October 18–27, 2005, February 20–March 5, 2006, October 16–27, 2006, March 3–17, 2007, December 9–15, 2007, May 19–June 3, 2008, February 23–March 11, 2009, September 22–October 9, 2009	National Bank of the Kyrgyz Republic
Bank Supervision and Regulation	February 23–March 8, 2005, May 18–28, 2005, July 17–28, 2005, October 02–13, 2005, January 15–26, 2006, February 12–23, 2006, March 20–30, 2006	National Bank of the Kyrgyz Republic
FSAP update	September 5–15, 2005 October 10–23, 2006	National Bank of the Kyrgyz Republic
AML/CFT	April 19–25, 2006	National Bank of the Kyrgyz Republic
Monetary Framework, Operations, and Liquidity Management	June 25–July 15, 2007	National Bank of the Kyrgyz Republic
Islamic Banking Framework	February 4–12, 2008	National Bank of the Kyrgyz Republic
Assessment of the Government Primary and Secondary Market Arrangements in the Kyrgyz Republic	May 6–16, 2008	National Bank of the Kyrgyz Republic

	Public Debt Management	July 14–31, 2009	Ministry of Finance & others
	Risk Management within the Islamic Banking Framework	July 6–15, 2009	National Bank of the Kyrgyz Republic
	Financial Stability Analysis and Stress Testing	March 10–18, 2010	National Bank of the Kyrgyz Republic
	Improving the Bank Resolution Framework	March 31–April 9, 2010	National Bank of the Kyrgyz Republic
	Bank Resolution	May 31–June 3, 2010	National Bank of the Kyrgyz Republic
	Bank Resolution	July 26–August 1, 2010	National Bank of the Kyrgyz Republic
	Bank Resolution	August 10–19, 2010	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
	Review of Tax Legislation	July 27–August 5, 2004	Ministry of Finance
	Assisting in drafting Tax Code	December 4–10, 2005	Prime Minister's office
	AML/CFT Follow-up	July 2–6, 2007	National Bank of the Kyrgyz Republic
	AML/CFT Follow-up	September 3–6, 2007	National Bank of the Kyrgyz Republic and Financial Intelligence Unit
	AML/CFT Framework	February 11–15, 2008 March 3–7, 2008	National Bank of the Kyrgyz Republic and Financial Intelligence Unit
	Review of the draft Tax Code	April 22–30, 2008	Ministry of Finance
	AML/CFT capacity building	March 25–31, 2009	National Bank of the Kyrgyz Republic and Financial Intelligence Unit

	AML/CFT Follow-up	May 18–29, 2009	NBKR and State Service for Regulation and Financial Market Supervision
	AML/CFT Follow-up	August 3–14, 2009	NBKR and State Service for Regulation and Financial Market Supervision
	AML/CFT follow-up	September 22–25, 2009	Financial Intelligence Unit
	AML/CFT Follow-up	October 5–16, 2009	NBKR, Financial Intelligence Unit, and State Service for Regulation and Financial Market Supervision
	AML/CFT Follow-up	January 27–29, 2010	Financial Intelligence Unit
	AML/CFT Follow-up	February 22–March 4, 2010	NBKR, Financial Intelligence Unit, and State Service for Regulation and Financial Market Supervision
	AML/CFT Follow-up	January 18–20, 2011	NBKR, Financial Intelligence Unit, and State Service for Regulation and Financial Market Supervision
	Legal Framework for Crisis Management and Bank Resolution	March 9–23, 2011	NBKR, MoF, Deposit Protection Agency, Debt Enterprise Bank Resolution Agency, Ministry of Foreign Affairs, Union of Banks
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

National Accounts Statistics	November 17–28, 2008	National Statistics Committee
Government Finance Statistics	November 11–14, 2008	Ministry of Finance
National Accounts Statistics	March 1–12, 2010	National Statistics Committee

List of Resident Advisors

MFD	Banking Supervision/Restructuring Advisor	Mr. Svartsman	January 2004–January 2005
MFD	Public Debt Policy and Management	Mr. Azarbayejani	December 2002–December 2004
MCM	Debt Management and Development of Government Securities Management	Mr. Riecke	August 2006–present
MCD	Macroeconomic Analysis and Forecasting	Mr. Petkov	January 2010–January 2011
MCM	Banking Supervision/Restructuring Advisor	Mr. Svartsman	October 2010–present

ANNEX VI. KYRGYZ REPUBLIC—STATISTICAL ISSUES

1. Data provision is adequate for surveillance. The four institutions responsible for collecting, compiling and disseminating macroeconomic statistics—the National Statistics Committee (NSC), the Ministry of Economic Regulation (MER), the Ministry of Finance (MOF), and the National Bank of the Kyrgyz Republic (NBKR)—have legal and institutional environments that support statistical quality, and their respective staff are well-versed in current methodologies.
2. The NSC maintains a comprehensive and regularly updated website with data that largely incorporate international methodological recommendations with adequate coverage and timeliness (<http://www.stat.kg>). In February 2004, the Kyrgyz Republic subscribed to the SDDS.
3. A data ROSC mission in November 2002 concluded that the quality of the macroeconomic statistics had improved significantly in the last few years. The authorities' response to the data ROSC (posted on the IMF website (www.imf.org/external/np/rosc)) includes an update on the status of implementation of the ROSC recommendations.

National accounts

4. In general, dissemination of national accounts statistics is timely. Technical assistance has been received from the IMF, EUROSTAT, OECD, the World Bank, and bilateral donors. While significant progress has been made in improving the national accounts estimation process, problems persist regarding the quality of the source data, due mainly to excessively tight collection deadlines associated with the release schedule. Efforts are needed to improve the quality of the source data for quarterly GDP estimates. Moreover, while the quarterly GDP estimates are disseminated on a discrete basis for SDDS purposes, these estimates are still derived from cumulative data. 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 sampling procedures. Improved sampling procedures have been adopted for household surveys and new report forms have been introduced for the enterprise survey. The NSC has established a division of sample surveys, which would assist in improving the sampling techniques.
5. The November 2008 STA mission on national accounts assisted the staff of the National Accounts Division in NCS to produce discrete quarterly GDP estimates at current and constant prices, using both the production and expenditure approaches. The mission made a number of recommendations, including: (a) need to introduce the new establishment surveys; (b) disseminate the industrial production index (IPI) as a chain-linked indices, in line with international standards; (c) investigate the inconsistency between the IPI and the producer price index (PPI); (d) fully computerize the calculation of volume estimates for agriculture in line with international practice; and (e) obtain time series data for loans and deposits of financial institutions.

Price and labor market statistics

6. The concepts and definitions used in the CPI, which has been published since January 1995, are broadly consistent with international standards. The price index covers all urban resident households of all sizes and income levels, but needs to cover rural households, which comprise the majority of the population.
7. The 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 data processed by customs have 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.

Government finance statistics

10. The scope of central government statistics falls short of international standards because it excludes data for the Social Fund (these data are published separately). Other limitations involve the discrepancies between the deficit and financing data. While revenue and expenditure data generally accord with the *GFSM 1986*, 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 are reported to STA for publication in the *IFS*; the latest data reported for publication in the *GFS Yearbook* were for 2006, and covered general government and its subsectors; the data were compiled using the *GFSM 2001* analytical framework.
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 (including timeliness) of external debt data is adequate. The External Debt Division of the MOF is now solely responsible for monitoring external debt, and has benefited from on-site training provided by a Swiss-financed long-term consultant and the computerization of its database.

Monetary and financial statistics (MFS)

12. The 2002 data ROSC mission found that: (a) the residency criterion was not uniformly applied, as the currency denomination was used to classify some transactions with foreign and domestic units; (b) deposits with banks in liquidation were included in broad money; and (c) source data did not provide sufficient information for a more detailed sectoral breakdown (e.g., subsectorization of nonbank institutions as recommended in the *MFSM*).

13. The April/May 2004 STA mission on MFS found that the NBKR had made substantial progress in implementing ROSC recommendations pertaining to monetary statistics. To address the outstanding issues, the mission further recommended that the NBKR (a) improve the basic source data to allow for proper classification of the transactions with foreign and domestic units; (b) fully implement the *MFSM*'s methodology concerning accrual accounting; (c) exclude deposits with banks in liquidation from monetary aggregates and classify them as restricted deposits; and (d) set up a working group to follow up on consistency between monetary and balance of payments statistics. The mission also recommended expanding the current broad money survey to include the accounts of credit unions and microfinance companies.

14. The new accounting framework for banks implemented in January 2009 revealed some problems in classification of a part of the Social Fund deposits. Efforts are under way to address the consequences of the introduction of the new accounting rules.

15. Monetary data have been reported electronically to STA using Standardized Report Forms (SRFs). STA identified classification issues in the reported SRF data, which were communicated to the authorities. The data will be published in *IFS* and *IFS Monetary and Financial Statistics Supplement* as soon as these issues are resolved.

External sector statistics

16. Data on the balance of payments and international investment position are compiled and disseminated on a quarterly basis. The 2002 data ROSC mission noted that the compilation of balance of payments statistics broadly follows the methodology recommended in the *BPM5*. However, deficiencies remain with respect to data on remittances, trade, services, and foreign direct investment. There is also a need to improve compilation procedures for achieving temporal consistency of data, and investigating and reconciling discrepancies. The March 2004 STA mission on balance of payments statistics noted that while progress had been made in several areas, further improvements were needed in the international transactions reporting system; data sampling methods; and data validation and coverage, particularly on trade, services, private sector external debt, and foreign direct investment.

Kyrgyz Republic: Table of Common Indicators Required for Surveillance
(As of May 12, 2011)

	Date of latest observation	Date received	Frequency of Data ⁷	Frequency of Reporting ⁷	Frequency of publication ⁷	Memo Items:	
						Data Quality—Methodological soundness ⁸	Data Quality—Accuracy and reliability ⁹
Exchange Rates	5/10/11	5/11/11	D	D	W		
International Reserve Assets and Reserve Liabilities of the Monetary Authorities ¹	5/10/11	5/11/11	M	M	M		
Reserve/Base Money	5/10/11	5/11/11	D	D	M	LO, O, LO, LO	LO, O, O, LO, LO
Broad Money	3/30/11	4/30/11	M	M	M		
Central Bank Balance Sheet	5/10/11	5/11/11	D	D	M		
Consolidated Balance Sheet of the Banking System	3/30/11	4/30/11	M	M	M		
Interest Rates ²	5/4/11	5/11/11	W	W	W		
Consumer Price Index	4/30/11	5/10/11	M	M	M	O, LO, O, O	LO, LO, O, O, O
Revenue, Expenditure, Balance and Composition of Financing ³ —General Government ⁴	3/30/11	4/26/11	M	M	A	O, LNO, LO, O	LO, O, O, LO, LO
Revenue, Expenditure, Balance and Composition of Financing ³ —Central Government	3/30/11	4/26/11	M	M	M		
Stocks of Central Government and Central Government-Guaranteed Debt ⁵	3/30/11	4/30/11	Q	Q	Q		
External Current Account Balance	12/30/10	3/30/11	Q	Q	Q	LO, LO, LO, LO	O, LO, LO, LO, LO
Exports and Imports of Goods and Services	12/30/10	3/30/11	Q	Q	Q		
GDP/GNP	4/30/11	5/10/11	M	M	M	O, O, LO, O	LO, LO, LO, O, O
Gross External Debt	12/30/10	3/30/11	Q	Q	A		
International Investment Position ⁶	12/30/10	3/30/11	Q	Q	Q		

¹ Any reserve assets that are pledged or otherwise encumbered should be specified separately. Also, data should comprise short-term liabilities linked to a foreign currency but settled by other means as well as the notional values of financial derivatives to pay and to receive foreign currency, including those linked to a foreign currency but settled by other means

² Both market-based and officially determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.

³ Foreign and domestic financing only.

⁴ The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.

⁵ Including currency and maturity composition.

⁶ Includes external gross financial asset and liability positions vis-à-vis nonresidents.

⁷ Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Annually (A), Irregular (I); Not Available (NA).

⁸ Reflects the assessment provided in the data ROSC (published in November 2003, and based on the findings of the mission that took place during November 2002) for the dataset corresponding to the variable in each row. The assessment indicates whether international standards concerning concepts and definitions, scope, classification/sectorization, and basis for recording are fully observed (O), largely observed (LO), largely not observed (LNO), or not observed (NO).

⁹ Same as footnote 7, except referring to international standards concerning source data, statistical techniques, assessment and validation of source data, assessment and validation of intermediate data and statistical outputs, and revision studies

INTERNATIONAL DEVELOPMENT ASSOCIATION AND
INTERNATIONAL MONETARY FUND

**Kyrgyz Republic—Debt Sustainability Analysis Under the Debt Sustainability
Framework for Low Income Countries**

Prepared by the Staffs of the International Monetary Fund
and the World Bank

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Yvonne Tsikata and Jeffrey Lewis (World Bank)

June 2, 2011

Based on the joint IMF-World Bank Low-Income Country Debt Sustainability Framework, the Kyrgyz Republic is assessed to remain at a moderate risk of debt distress.¹ Stress tests suggest that the country is still vulnerable, particularly to a combination of exogenous shocks. Further improvement of the debt outlook will depend on maintaining sound macroeconomic policies, including fiscal consolidation and prudent borrowing, as well as ensuring continued concessional financing to support the country's large development needs.

I. BACKGROUND

The Kyrgyz Republic's nominal stock of public and publicly guaranteed (PPG) external debt declined from about 100 percent of GDP in 2003 to 41 percent in 2008. This decline was mainly the result of an acceleration in the pace of economic growth and a nominal appreciation of the domestic currency, but also reflected firm fiscal discipline and Paris Club support.

The Kyrgyz Republic had two debt restructuring agreements with the Paris Club. The first was in December 2002 under Houston terms and provided for flow rescheduling in three phases. The second was in March 2005, under the Evian approach. The Kyrgyz authorities indicated in early 2007 that they did not wish to avail themselves of the HIPC initiative, but subsequently expressed interest in the MDRI.

Since end-2008, the nominal stock of PPG external debt has increased, reaching 57 percent of GDP at end-2010. The increase in this ratio largely reflects the decline in nominal (dollar) GDP in 2009 and 2010 as a result of the international financial crisis and

¹ This DSA has been produced jointly by Fund and Bank staffs, in consultation with Asian Development Bank and the Kyrgyz authorities. The fiscal year for the Kyrgyz Republic is January 1–December 31. The risk rating would not change with the inclusion of remittances (Figure 2).

domestic political instability which negatively impact real growth, but also reflects an uptick in external borrowing to finance infrastructure development and crisis-related fiscal deficits. The present value (PV) of PPG external debt was equivalent to US\$1.5 billion (34 percent of GDP) at end-2010, of which 66 percent is owed to international financial institutions (IFIs), and the remaining 34 percent to bilateral creditors. At end-2010, indebtedness indicators were estimated to be below the applicable HIPC Initiative thresholds, while income levels were estimated to be above the IMF MDRI thresholds.

II. UNDERLYING DSA ASSUMPTIONS

The macroeconomic assumptions reflect the framework underlying the ECF-supported program and World Bank and IMF staff projections through 2031. They have been updated to incorporate recent developments and changes to the medium-term outlook, but long-term assumptions are broadly similar to the framework used in the last DSA. The data on the stock of external debt at end-2010 and debt payment schedule were provided by the Kyrgyz authorities, except for the data on the World Bank and Asian Development Bank debt, which were provided directly by the two institutions.

The framework assumes implementation of sound macroeconomic policies—including fiscal consolidation and prudent public debt management—as a basis for sustaining growth. Near- and medium-term growth would be underpinned by recovery from the shocks of 2009 and 2010, including a rebound in agricultural production and tourism, and would be supported by infrastructure investments and strong mining production. Long-term growth will be generated by firm implementation of structural reforms to remove impediments to private investment, stimulate economic diversification, and improve the business climate, including increased financial stability and deepened financial intermediation. The energy sector, which has large potential, is also envisioned to add positively to growth in the long run. The framework features average medium-term GDP growth of around 6 percent per year and average long-term growth over 2017–31 of about 5 percent, as in the previous DSA.

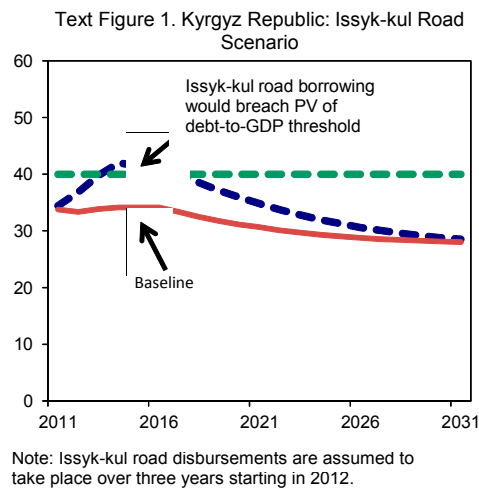
The main updates relative to the last DSA reflect new information regarding the authorities' infrastructure development plans and debt relief. Specifically, energy-related investments have been delayed, partly because of the domestic political unrest in 2010. The Kyrgyz government is still in discussions with the Chinese authorities to finance and assist in the construction of substations and transmission lines linking to the south.² The latest information indicates total investments in this area to be about US\$450 million (compared to

² These energy infrastructure projects will expand the potential for exporting electricity, improve reliability of the transmission system and ensure smooth supply of electricity to remote parts of the country. Neighboring Uzbekistan has been threatening repeatedly to withdraw from the regional power grid that would leave the southern part of the Kyrgyz Republic without electricity, given that the only way to supply electricity to the south is through the Uzbek electricity grid.

US\$550 million in the previous DSA), including US\$208 million likely to be disbursed over the next two to three years. These investments would be financed with loans from China and are expected to contain a grant element slightly less than 35 percent, but not less than 30 percent. This borrowing would be accommodated in the ECF-supported program under a tied, nonzero, nonconcessional debt limit in the equivalent amount. In April 2011, the authorities reached an agreement with Turkey for a debt write-off in the amount of about US\$49.5 million, which is likely to be effected in 2011.

Planned energy sector investments will ensure smooth supply of electricity within the country and contribute to economic growth. During the construction period (2012–16), the energy infrastructure projects are estimated to contribute around a quarter of a percentage point to GDP growth annually.³ The electricity transmission lines, when built, will reduce system overloading and increase the self-sufficiency of supply. The impact on exports and long-term growth from the energy projects would be more significant if new large electricity generation facilities are built.⁴

The authorities have also explored the possibility of investing in transportation infrastructure around a main tourist destination (Lake Issyk-kul). Borrowings in this area could total approximately US\$600 million and be financed on terms similar to those of the energy infrastructure projects. Given the uncertain growth effects and the possibility of a significantly worse debt outlook (Text Figure 1), the authorities have decided not to pursue this investment further at this stage. Consequently, this borrowing is not included in the baseline DSA projections.



³ The contribution to economic growth will come from increased domestic spending, which is not likely to be significant, as only around 10 percent of the disbursed financing from China will be spent domestically (the rest will be used to purchase imported equipment and labor).

⁴ Kambarata-II (hydropower) was put in operation in 2010, but does not generate substantial volumes of electricity. Its contributions to exports and growth are therefore limited. Kambarata-I is a much larger project, but remains highly uncertain and is therefore excluded from this DSA, as from previous DSAs.

Box 1. Kyrgyz Republic: Baseline Macroeconomic Assumptions

Real GDP growth is projected to average about 6 percent over the medium term, underpinned by economic recovery from the shocks of 2009 and 2010, including a rebound in agricultural production and tourism and in line with strong recent growth in the main trading partners. Growth in the medium term would also be supported by infrastructure investments and strong mining production. Long-term growth would be generated by firm implementation of structural reforms to remove impediments to private investment, stimulate economic diversification, and improve the business climate, and is broadly in line with the historical average and with assumptions in the previous DSA.

After two successive years of contraction, exports would rebound somewhat in 2011, in line with developments in the mining and tourism sectors, and reflecting strong growth in the main trading partners. In the medium term, export growth will decelerate as the Kyrgyz Republic joins the Russia-Kazakhstan-Belarus customs union and transit trade declines. Import growth in 2011 would be strong, consistent with growth projections and reflecting the high price of crude oil. In the medium term, import growth will also decelerate with the loss of transit trade, but the high import content of energy infrastructure projects will dampen the deceleration somewhat. In the long-term, import growth would be in line with assumptions in the previous DSA, averaging around 6½ percent. As a result of these trends, the current account deficit would increase in 2011, but gradually improve, averaging about 5 percent of GDP in the long term.

With the exception of the energy infrastructure borrowing from China, medium-term public borrowing is assumed to be on highly concessional terms. Over the longer DSA horizon, concessionalities of new external public borrowing would gradually decline from around 38 percent in 2011 to around 20 percent by 2031, as more borrowing is assumed to be contracted at less concessional terms.

In line with the programmed fiscal consolidation, government revenues are projected to increase from about 30 percent of GDP in 2011 to about 32 percent by 2016 and remain broadly stable at that level through 2031. After a wage-related increase in 2011, noninterest current expenditure would increase temporarily to about 33 percent of GDP before declining to about 30 percent of GDP by 2016. As a result, the primary fiscal deficit would deteriorate to 6.3 percent of GDP in 2011, but gradually improve to 2.4 percent of GDP by 2016. Fiscal consolidation and appropriately tight monetary policy will also help to maintain (GDP deflator) inflation at an average of around 7 percent over the medium term.

Text Table 1. Underlying DSA Assumptions

	2010		2011	2012	2013	2014	2015	2016	Long-term average	
	2010 DSA Proj.	Actual	2011 DSA Proj.							2010 DSA Proj.	2011 DSA Proj.
Real GDP growth (in percent)	-3.5	-1.4	6.0	6.0	6.0	5.8	5.8	5.7	5.0	5.1
Growth of exports of G&S (US dollar terms, in percent)	1.9	-6.2	23.9	8.7	8.1	14.6	12.5	12.1	6.1	6.3
Growth of imports of G&S (US dollar terms, in percent)	12.2	6.0	26.7	9.0	6.7	10.9	10.3	10.0	5.7	6.7
Primary deficit (percent of GDP)	10.9	5.5	6.3	6.2	6.0	5.9	3.3	2.4	-1.1	2.2
Inflation rate (GDP deflator, in percent)	9.3	6.9	11.4	7.7	5.5	6.5	5.3	4.8	4.1	4.1

Source: Country authorities and staff projections.

III. EXTERNAL DEBT SUSTAINABILITY ANALYSIS

A. Baseline

The baseline scenario points to a cautiously favorable improvement in the external debt outlook over time. At end-2010, the PV of debt-to-exports and the PV of debt-to-revenue ratios, at 62 and 119 percent respectively, were well below their policy-based indicative thresholds.⁵ Only the PV of PPG debt-to-GDP ratio, at 34 percent in 2010, is close to its relevant threshold of 40 percent. This latter ratio then remains broadly stable through the medium term as energy-related disbursements offset growth gains, before returning to a sustainable path underpinned by solid growth, fiscal consolidation, and prudent debt management.

Debt service is expected to remain manageable throughout the DSA horizon. This reflects the high concessionality of both the outstanding multilateral debt and the assumed new borrowing over the medium term. The PPG debt service ratio would decline slightly from 3.6 percent of exports in 2010 to 2.9 percent in 2011 following debt relief from Russia and Turkey, and remain broadly at that level through the medium and long term.⁶

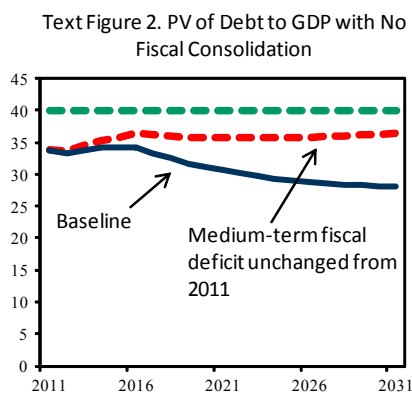
B. Alternative Scenarios and Stress Tests

Stress tests and alternative scenarios show that the Kyrgyz Republic's external debt is vulnerable to large shocks or substantially less favorable assumptions. The PV of the external debt-to-GDP ratio and the PV of the external debt-to-revenue rise above the relevant indicative thresholds under some tests. The PV of debt-to-GDP ratio rises above the indicative threshold of 40 percent in the medium term (or even over the longer term) when (i) export value growth is at historical average minus one standard deviation in 2012–13; (ii) the net non-debt creating inflows over 2012–13 are one standard deviation below their historical average; and (iii) under a shock over 2012–13 combining lower GDP and export growth, a decline in the US dollar GDP deflator, and lower net non-debt creating inflows. The ratio of PV of debt-to-revenue would also approach the relevant indicative threshold of

⁵ The Kyrgyz Republic is rated as a *medium performer* based on the World Bank's Country Performance and Institutional Assessment Index for low income countries. The relevant policy-dependent thresholds for countries in this category are 40 percent for the PV of the debt-to-GDP ratio, 150 percent for the PV of debt-to-exports ratio, 250 percent for the PV of debt-to-revenue ratio, 20 percent of the debt service-to-exports ratio, and 30 percent of the debt service-to-revenue ratio.

⁶ Under the debt-for-equity swap agreement signed between the previous Kyrgyz administration and the Russian authorities in 2009, the Russian side agreed to relinquish claims on the Kyrgyz Republic in the amount of US\$193.5 million in exchange for a 100 percent stake in two state-owned companies in the Kyrgyz Republic. However, in early 2010, despite the Kyrgyz Republic appearing to have fulfilled all its obligations, the Russian side called in question the implementation of the agreement and declared the outstanding debt disputed. Since then the parties have been in close consultations to resolve this issue and a settlement is expected in 2011, as also assumed in the previous DSA.

250 percent in the medium term under the last two conditions. However, the PV of debt-to-exports ratio is robust and does not breach its threshold under various tests. Debt service ratios also prove resilient, staying below their indicative threshold levels under various tests. The historical scenario—where key macro variables evolve according to their historic averages—points to a more benign external debt outlook than the baseline scenario. However, an alternative scenario that assumes no fiscal consolidation in the medium term, financed by external borrowing, results in an unsustainable debt outlook, with the PV of debt-to-GDP following an upward trend (Text Figure 2).



IV. PUBLIC DEBT SUSTAINABILITY ANALYSIS

A. Baseline

Domestic debt is projected to increase and will play a more important role in financing the budget deficit in the medium and long term. Domestic debt accounted for around 3 percent of total public debt at end-2010. However, by 2031, domestic debt is projected to reach about 9 percent of total public debt as domestic financial markets deepen.

The Kyrgyz Republic's public debt outlook is projected to be manageable in the medium and long term. Under the baseline scenario, the PV of public debt-to-GDP ratio would increase slightly in the medium term from about 38 percent of GDP at end-2010 to a maximum of about 42 percent of GDP in 2016 following disbursements for energy-sector infrastructure. It would then decline gradually to about 37 percent by 2031 reflecting fiscal consolidation.

B. Alternative Scenarios and Stress Tests

Alternative scenarios and stress tests show that Kyrgyz Republic's public debt remains highly sensitive to shocks that reduce real GDP growth and result in unsustainable debt burden trajectories. The standard sensitivity analysis based on the historical variation of key parameters, including real GDP growth and exchange rate, shows that debt ratios would rise considerably in the long run. Under stress tests and scenarios, the PV debt-to-GDP ratio in 2031 could increase to about 80 percent under the permanent real GDP growth shock

scenario and the fixed (at 2011 level) primary deficit scenario. In addition, debt burden trajectories are ever increasing if the long run growth rate turns out 0.8 percentage points below the current estimate.

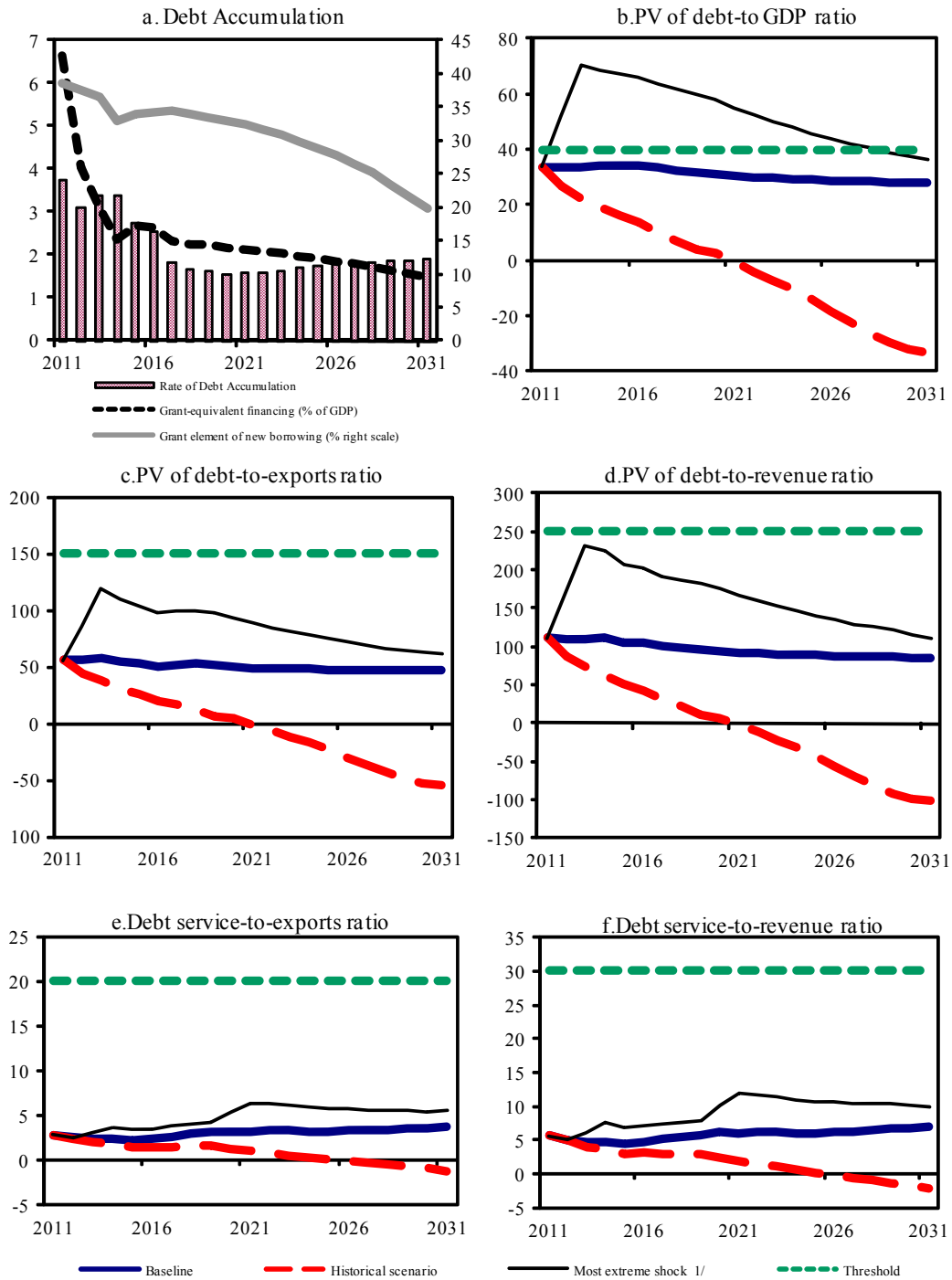
V. DEBT DISTRESS CLASSIFICATION AND CONCLUSIONS

Based on the projected external debt burden indicators, the Kyrgyz Republic is assessed to be at moderate risk of debt distress. All PV-based external debt indicators in the baseline are projected to stay below their indicative thresholds over the DSA horizon. Moreover, the debt service burden would remain well below the thresholds, reflecting the high concessionality of the external debt. Nevertheless, alternative scenarios and stress tests show that the external public debt indicators could approach or breach the thresholds if the Kyrgyz Republic were to experience large adverse exogenous shocks or relax its prudent debt management policy. This conclusion is consistent with the last DSA. When adding domestic debt to the analysis, total public sector debt seems manageable in light of the dynamics of the domestic debt stock. This said, debt burden trajectories are highly sensitive to real GDP shocks and a somewhat smaller long-run real growth rate.

Low-concessionality loans from bilateral and commercial creditors to finance large public investment projects continue to pose a risk to the debt outlook. Staff recognizes that the Kyrgyz Republic has large developmental needs, but considers paramount to lock in the recent progress towards achieving and maintaining debt sustainability. Even if loans have a grant element of at least 35 percent, it would be important to ensure that the underlying projects are viable and that market risks, including exchange rate risk, are accounted for, so as to avoid the buildup of an unsustainable debt burden. Similarly, it would remain important for the government to seek highly concessional loans, including in the energy sector.

The authorities broadly concurred with this analysis. They are highly concerned about maintaining debt sustainability and will remain vigilant on the debt outlook. Indeed, given the uncertain growth benefits and negative debt impact of the potential Issyk-kul road borrowing, the authorities do not plan to pursue that project further at this point. Looking forward, the authorities intend to make every effort to contract only concessional loans.

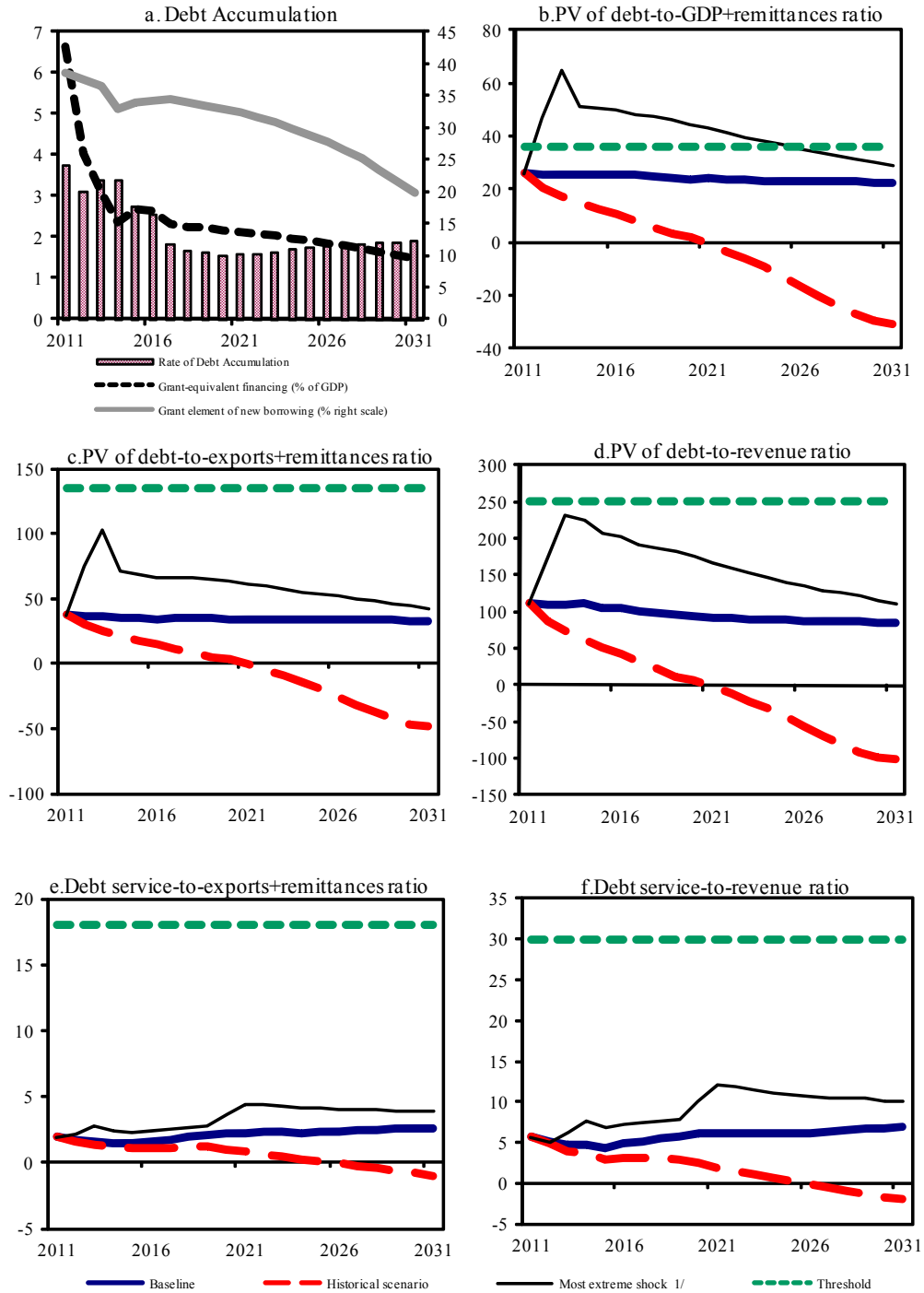
Figure 1. Kyrgyz Republic: Indicators of Public and Publicly Guaranteed External Debt under Alternatives Scenarios, 2011-2031 1/



Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in 2021. In figure b. it corresponds to a Non-debt flows shock; in c. to a Non-debt flows shock; in d. to a Non-debt flows shock; in e. to a Non-debt flows shock and in figure f. to a Non-debt flows shock

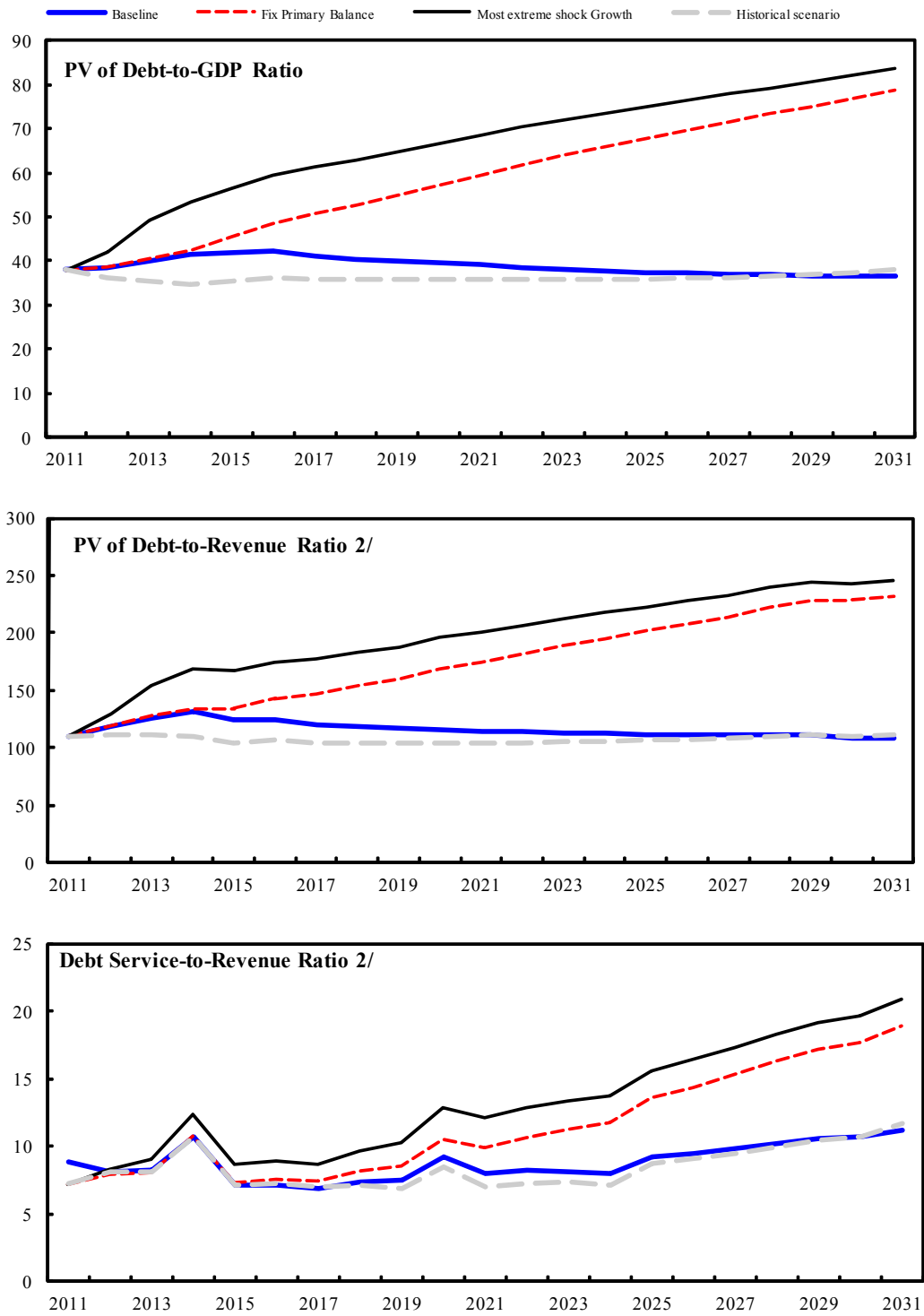
Figure 2. Kyrgyz Republic: Indicators of Public and Publicly Guaranteed External Debt under Alternatives Scenarios Including Remittances, 2011-2031



Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in 2021. In figure b. it corresponds to a Non-debt flows shock; in c. to a Non-debt flows shock; in d. to a Non-debt flows shock; in e. to a Non-debt flows shock and in figure f. to a Non-debt flows shock

Figure 3. Kyrgyz Republic: Indicators of Public Debt Under Alternative Scenarios, 2011-2031 1/



Sources: Country authorities; and staff estimates and projections.
 1/ The most extreme stress test is the test that yields the highest ratio in 2021.
 2/ Revenues are defined inclusive of grants.

Table 1a. Kyrgyz Republic: Public Sector Debt Sustainability Framework, Baseline Scenario, 2008-2031
(In percent of GDP, unless otherwise indicated)

	Actual			Average 5/ Standard Deviation	Standard Deviation	Estimate					Projections			
	2008	2009	2010			2011	2012	2013	2014	2015	2016	2011-16 Average	2021	2031	2017-31 Average
Public sector debt 1/	45.1	56.6	61.2			55.2	55.4	56.8	57.6	57.4	57.1		51.4	45.8
o/w foreign-currency denominated	42.2	53.8	58.2			51.8	51.0	51.1	50.7	49.9	49.4		43.1	37.2
Change in public sector debt	-14.6	11.5	4.6			-6.0	0.2	1.4	0.9	-0.2	-0.3		-0.8	-0.2
Identified debt-creating flows	-9.9	5.5	7.0			-1.4	0.3	1.2	0.8	-0.6	-1.0		-0.5	-0.2
Primary deficit	-1.4	3.0	5.5	2.3	1.9	6.3	6.2	6.0	5.9	3.3	2.4	5.0	2.2	2.1
Revenue and grants	29.9	32.1	31.7			34.6	32.3	31.6	31.2	33.6	33.6		33.8	33.8
of which: grants	1.8	5.1	2.9			4.3	2.1	1.1	0.7	1.3	1.2		1.0	0.7
Primary (noninterest) expenditure	28.5	35.1	37.2			41.0	38.4	37.5	37.1	36.9	36.1		36.0	35.9
Automatic debt dynamics	-8.7	2.4	1.6			-6.2	-4.6	-3.6	-4.1	-3.7	-3.3		-2.7	-2.3
Contribution from interest rate/growth differential	-5.1	-0.9	1.3			-3.3	-3.2	-3.4	-3.4	-3.5	-3.5		-2.7	-2.3
of which: contribution from average real interest rate	-0.9	0.4	0.5			0.1	-0.1	-0.2	-0.3	-0.4	-0.4		-0.3	-0.1
of which: contribution from real GDP growth	-4.2	-1.3	0.8			-3.5	-3.1	-3.2	-3.1	-3.2	-3.1		-2.4	-2.2
Contribution from real exchange rate depreciation	-3.5	3.3	0.3			-2.8	-1.4	-0.2	-0.7	-0.1	0.1		...	...
Other identified debt-creating flows	0.1	0.1	-0.1			-1.6	-1.3	-1.1	-1.0	-0.3	-0.1		0.0	0.0
Privatization receipts (negative)	0.1	0.1	-0.1			-1.6	-1.3	-1.1	-1.0	-0.3	-0.1		0.0	0.0
Recognition of implicit or contingent liabilities	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0
Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0
Residual, including asset changes	-4.7	6.0	-2.4			-4.6	-0.1	0.1	0.1	0.4	0.7		-0.3	0.0
Other Sustainability Indicators														
PV of public sector debt	32.5	37.6	38.1			37.9	38.3	40.0	41.6	42.0	42.2		39.1	36.7
o/w foreign-currency denominated	29.6	34.7	35.1			34.5	34.0	34.4	34.6	34.5	34.5		30.9	28.1
o/w external	28.5	33.7	34.2			33.7	33.3	33.8	34.0	34.1	34.1		30.6	28.0
PV of contingent liabilities (not included in public sector debt)	...	...	...			...	...	...	...	...	...		...	...
Gross financing need 2/	1.4	6.6	9.1			10.7	10.4	10.8	12.3	8.8	8.2		8.2	7.0
PV of public sector debt-to-revenue and grants ratio (in percent)	108.8	116.9	120.1			109.4	118.9	126.8	133.3	125.1	125.6		115.8	108.4
PV of public sector debt-to-revenue ratio (in percent)	115.9	138.9	132.2			124.8	127.3	131.6	136.4	130.2	130.4		119.4	110.9
o/w external 3/	101.8	124.7	118.6			110.9	110.6	111.2	111.8	105.5	105.2		93.4	84.7
Debt service-to-revenue and grants ratio (in percent) 4/	5.5	7.1	7.1			8.7	8.2	8.2	11.1	7.2	7.2		8.1	11.2
Debt service-to-revenue ratio (in percent) 4/	5.9	8.5	7.8			9.9	8.8	8.5	11.4	7.5	7.5		8.3	11.5
Primary deficit that stabilizes the debt-to-GDP ratio	13.2	-8.5	0.9			12.3	6.0	4.6	5.0	3.5	2.7		3.0	2.3
Key macroeconomic and fiscal assumptions														
Real GDP growth (in percent)	7.6	2.9	-1.4	4.0	3.7	6.0	6.0	6.0	5.8	5.8	5.7	5.9	4.7	5.1
Average nominal interest rate on forex debt (in percent)	0.9	1.2	1.1	1.3	0.4	0.7	0.7	0.8	0.8	0.9	1.0	0.8	1.2	1.7
Average real interest rate on domestic debt (in percent)	-7.8	10.4	5.5	0.1	5.5	3.8	9.6	7.4	3.8	1.7	1.5	4.7	0.1	0.1
Real exchange rate depreciation (in percent, + indicates depreciation)	-6.9	8.1	0.6	-5.7	7.0	-5.1	...	...	...	...	...	...	...	...
Inflation rate (GDP deflator, in percent)	23.2	4.0	6.9	8.4	6.3	11.4	7.7	5.5	6.5	5.3	4.8	6.9	4.0	4.0
Growth of real primary spending (deflated by GDP deflator, in percent)	0.0	0.3	0.0	0.1	0.1	0.2	0.0	0.0	0.0	0.1	0.0	0.1	0.0	0.1
Grant element of new external borrowing (in percent)	...	...	...	...	...	38.3	37.5	36.4	32.9	33.9	34.2	35.5	32.3	19.7

Sources: Country authorities; and staff estimates and projections.

1/ [Indicate coverage of public sector, e.g., general government or nonfinancial public sector. Also whether net or gross debt is used.]

2/ Gross financing need is defined as the primary deficit plus debt service plus the stock of short-term debt at the end of the last period.

3/ Revenues excluding grants.

4/ Debt service is defined as the sum of interest and amortization of medium and long-term debt.

5/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

Table 2a. Kyrgyz Republic: Sensitivity Analysis for Key Indicators of Public Debt 2011-2031

	Projections							
	2011	2012	2013	2014	2015	2016	2021	2031
PV of Debt-to-GDP Ratio								
Baseline	38	38	40	42	42	42	39	37
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	38	36	35	35	35	36	35	38
A2. Primary balance is unchanged from 2011	38	39	41	42	45	48	60	79
A3. Permanently lower GDP growth 1/	38	39	41	44	45	47	53	80
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2012-2013	38	42	49	53	57	60	68	83
B2. Primary balance is at historical average minus one standard deviations in 2012-2013	38	37	37	39	39	40	37	35
B3. Combination of B1-B2 using one half standard deviation shocks	38	37	38	42	44	47	53	64
B4. One-time 30 percent real depreciation in 2012	38	52	52	52	52	52	46	43
B5. 10 percent of GDP increase in other debt-creating flows in 2012	38	46	48	49	49	49	44	40
PV of Debt-to-Revenue Ratio 2/								
Baseline	109	119	127	133	125	126	116	108
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	109	111	112	111	104	107	104	110
A2. Primary balance is unchanged from 2011	109	120	128	136	134	144	176	233
A3. Permanently lower GDP growth 1/	109	121	131	140	134	139	155	236
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2012-2013	109	130	155	171	168	176	202	245
B2. Primary balance is at historical average minus one standard deviations in 2012-2013	109	114	118	124	117	118	109	105
B3. Combination of B1-B2 using one half standard deviation shocks	109	115	120	134	132	139	156	189
B4. One-time 30 percent real depreciation in 2012	109	161	165	168	155	153	137	127
B5. 10 percent of GDP increase in other debt-creating flows in 2012	109	144	151	157	146	145	131	118
Debt Service-to-Revenue Ratio 2/								
Baseline	9	8	8	11	7	7	8	11
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	7	8	8	11	7	7	7	12
A2. Primary balance is unchanged from 2011	7	8	8	11	7	8	10	19
A3. Permanently lower GDP growth 1/	7	8	8	11	8	8	10	19
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2012-2013	7	8	9	13	9	9	12	21
B2. Primary balance is at historical average minus one standard deviations in 2012-2013	7	8	8	11	7	7	8	11
B3. Combination of B1-B2 using one half standard deviation shocks	7	8	8	11	8	8	9	16
B4. One-time 30 percent real depreciation in 2012	7	9	10	13	9	10	11	16
B5. 10 percent of GDP increase in other debt-creating flows in 2012	7	8	9	12	8	8	10	12

Sources: Country authorities; and staff estimates and projections.

1/ Assumes that real GDP growth is at baseline minus one standard deviation divided by the square root of the length of the projection period.

2/ Revenues are defined inclusive of grants.

Table 3a.: External Debt Sustainability Framework, Baseline Scenario, 2008-2031 1/
(In percent of GDP, unless otherwise indicated)

	Actual			Historical 0 Standard		Projections							2011-2016		2017-2031	
	2008	2009	2010	Average	0 Deviation	2011	2012	2013	2014	2015	2016	Average	2021	2031	Average	
External debt (nominal) 1/	45.1	58.2	68.3			61.2	58.6	58.2	57.6	56.9	56.2		51.4	55.0		
o/w public and publicly guaranteed (PPG)	41.2	52.8	57.3			51.0	50.3	50.5	50.1	49.4	48.9		42.9	37.1		
Change in external debt	-15.1	13.1	10.2			-7.2	-2.5	-0.4	-0.6	-0.7	-0.6		-0.4	1.1		
Identified net debt-creating flows	-12.7	-0.4	-2.1			0.9	0.6	-1.3	-1.9	-2.5	-2.4		-0.2	3.0		
Non-interest current account deficit	7.5	-1.6	1.3	-0.4	4.0	7.7	7.2	5.2	4.6	3.9	3.8		5.0	7.8	6.7	
Deficit in balance of goods and services	33.3	21.1	29.8			35.0	35.0	33.6	32.1	31.4	30.9		31.3	32.5		
Exports	59.2	57.5	54.8			60.4	59.8	59.5	62.4	64.9	67.6		62.6	60.2		
Imports	92.5	78.6	84.6			95.4	94.8	93.1	94.5	96.3	98.5		94.0	92.7		
Net current transfers (negative = inflow)	-28.8	-25.8	-30.1	-19.1	9.8	-30.1	-31.3	-32.2	-34.2	-32.9	-32.7		-27.9	-26.4	-27.0	
o/w official	-0.9	-4.2	-1.7			-0.2	0.0	0.0	0.0	0.0	0.0		-0.4	-0.2		
Other current account flows (negative = net inflow)	2.9	3.1	1.7			2.8	3.5	3.9	6.7	5.3	5.6		1.6	1.7		
Net FDI (negative = inflow)	-5.2	-4.0	-5.1	-3.6	2.4	-4.2	-4.2	-4.2	-4.2	-4.2	-4.0		-3.8	-3.2	-3.5	
Endogenous debt dynamics 2/	-15.0	5.3	1.6			-2.6	-2.4	-2.4	-2.3	-2.3	-2.2		-1.5	-1.6		
Contribution from nominal interest rate	0.6	0.9	0.8			1.0	0.9	0.9	0.8	0.8	0.8		0.8	0.9		
Contribution from real GDP growth	-3.4	-1.4	0.8			-3.6	-3.3	-3.3	-3.1	-3.1	-3.0		-2.3	-2.5		
Contribution from price and exchange rate changes	-12.2	5.7	0.1			...	...	...	...	...	...		...	...
Residual (3-4) 3/	-2.5	13.5	12.3			-8.0	-3.1	0.9	1.3	1.8	1.8		-0.2	-1.9		
o/w exceptional financing	-0.1	0.0	0.0			-4.7	0.0	0.0	0.0	0.0	0.0		0.0	0.0		
PV of external debt 4/	...	...	45.2			43.8	41.6	41.5	41.5	41.5	41.4		39.2	45.9	
In percent of exports	...	...	82.5			72.6	69.5	69.6	66.5	63.9	61.1		62.5	76.2	
PV of PPG external debt	...	...	34.2			33.7	33.3	33.8	34.0	34.1	34.1		30.6	28.0	
In percent of exports	...	...	62.3			55.8	55.6	56.8	54.6	52.5	50.4		48.8	46.6	
In percent of government revenues	...	...	118.6			110.9	110.6	111.2	111.8	105.5	105.2		93.4	84.7	
Debt service-to-exports ratio (in percent)	3.6	7.1	8.1			6.1	6.4	5.5	4.6	4.5	4.8		7.2	15.1		
PPG debt service-to-exports ratio (in percent)	2.5	3.2	3.6			2.8	2.5	2.4	2.3	2.2	2.3		3.2	3.8		
PPG debt service-to-revenue ratio (in percent)	5.2	6.7	6.9			5.7	5.0	4.7	4.8	4.4	4.9		6.2	6.9		
Total gross financing need (Billions of U.S. dollars)	0.2	-0.1	0.0			0.4	0.4	0.3	0.2	0.2	0.2		0.6	3.0		
Non-interest current account deficit that stabilizes debt ratio	22.6	-14.7	-8.8			14.9	9.8	5.7	5.2	4.6	4.4		5.4	6.7		
Key macroeconomic assumptions																
Real GDP growth (in percent)	7.6	2.9	-1.4	4.0	3.7	6.0	6.0	6.0	5.8	5.8	5.7	5.9	4.7	5.1	5.1	
GDP deflator in US dollar terms (change in percent)	25.4	-11.3	-0.1	9.2	10.6	6.0	3.6	2.5	3.4	2.3	1.7	3.2	2.0	2.0	2.0	
Effective interest rate (percent) 5/	1.3	1.9	1.3	1.6	0.4	1.7	1.7	1.7	1.5	1.5	1.6	1.6	1.7	1.9	1.8	
Growth of exports of G&S (US dollar terms, in percent)	35.4	-11.3	-6.2	17.8	21.5	23.9	8.7	8.1	14.6	12.5	12.1	13.3	7.7	6.5	6.3	
Growth of imports of G&S (US dollar terms, in percent)	47.5	-22.4	6.0	22.2	25.7	26.7	9.1	6.7	10.9	10.3	10.0	12.3	7.0	7.6	6.7	
Grant element of new public sector borrowing (in percent)	...	...	...	...	...	38.3	37.5	36.4	32.9	33.9	34.2	35.5	32.3	19.7	28.9
Government revenues (excluding grants, in percent of GDP)	28.0	27.1	28.8			30.4	30.1	30.4	30.5	32.3	32.4		32.8	33.1	32.6	
Aid flows (in Billions of US dollars) 7/	0.1	0.6	0.3			0.4	0.3	0.3	0.2	0.2	0.3		0.3	0.4		
o/w Grants	0.1	0.2	0.1			0.2	0.1	0.1	0.0	0.1	0.1		0.1	0.2		
o/w Concessional loans	0.0	0.4	0.1			0.2	0.2	0.2	0.2	0.1	0.2		0.2	0.3		
Grant-equivalent financing (in percent of GDP) 8/	...	...	...			6.6	4.0	3.1	2.3	2.7	2.6		2.1	1.5	1.9
Grant-equivalent financing (in percent of external financing) 8/	...	...	...			63.8	56.1	47.9	41.3	49.8	49.5		47.8	33.0	43.7
Memorandum items:																
Nominal GDP (Billions of US dollars)	5.1	4.7	4.6			5.2	5.7	6.2	6.8	7.3	7.9		11.2	22.1		
Nominal dollar GDP growth	34.8	-8.7	-1.4			12.4	9.8	8.6	9.4	8.2	7.5	9.3	6.8	7.1	7.1	
PV of PPG external debt (in Billions of US dollars)	...	...	1.5			1.7	1.9	2.1	2.3	2.5	2.6		3.4	6.1	
(PVA-PV-1)/GDPt-1 (in percent)	...	...	...			3.6	3.1	3.4	3.4	2.8	2.5	3.1	1.6	1.9	1.7
Gross remittances (Billions of US dollars)	1.4	1.0	1.3			1.5	1.8	2.0	2.3	2.4	2.6		3.1	5.8		
PV of PPG external debt (in percent of GDP + remittances)	...	...	26.6			25.9	25.3	25.6	25.4	25.6	25.7		24.0	22.2	
PV of PPG external debt (in percent of exports + remittances)	...	...	41.0			37.3	36.5	36.8	35.2	34.8	33.9		34.0	32.5	
Debt service of PPG external debt (in percent of exports + remittances)	...	...	2.4			1.9	1.7	1.6	1.5	1.4	1.6		2.2	2.6	

Sources: Country authorities; and staff estimates and projections.

1/ Includes both public and private sector external debt.

2/ Derived as $[r - g - \rho(1+g)] / (1+g+\rho+g\rho)$ times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, and ρ = growth rate of GDP deflator in U.S. dollar terms.

3/ Includes exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets; and valuation adjustments. For projections also includes contribution from price and exchange rate changes.

Also includes the effect of the financing gap, which is assumed to create debt, but does not enter the current or financial account.

4/ Assumes that PV of private sector debt is equivalent to its face value.

5/ Current-year interest payments divided by previous period debt stock.

6/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

7/ Defined as grants, concessional loans, and debt relief.

8/ Grant-equivalent financing includes grants provided directly to the government and through new borrowing (difference between the face value and the PV of new debt).

Table 3b. Kyrgyz Republic: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2011-2031
(In percent)

	Projections							2031
	2011	2012	2013	2014	2015	2016	2021	
PV of debt-to GDP ratio								
Baseline	34	33	34	34	34	34	31	28
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2011-2031 1/	34	26	22	19	16	13	-1	-33
A2. New public sector loans on less favorable terms in 2011-2031 2	34	34	36	37	38	39	40	45
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2012-2013	34	35	37	37	38	38	34	31
B2. Export value growth at historical average minus one standard deviation in 2012-2013 3/	34	38	48	47	47	46	40	31
B3. US dollar GDP deflator at historical average minus one standard deviation in 2012-2013	34	34	36	37	37	37	33	30
B4. Net non-debt creating flows at historical average minus one standard deviation in 2012-2013 4/	34	52	71	69	67	66	55	36
B5. Combination of B1-B4 using one-half standard deviation shocks	34	50	68	67	66	64	54	37
B6. One-time 30 percent nominal depreciation relative to the baseline in 2012 5/	34	46	47	47	47	47	43	39
PV of debt-to-exports ratio								
Baseline	56	56	57	55	52	50	49	47
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2011-2031 1/	56	44	38	31	25	20	-1	-55
A2. New public sector loans on less favorable terms in 2011-2031 2	56	57	60	59	59	58	63	75
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2012-2013	56	55	56	54	52	50	48	46
B2. Export value growth at historical average minus one standard deviation in 2012-2013 3/	56	72	102	96	91	86	81	66
B3. US dollar GDP deflator at historical average minus one standard deviation in 2012-2013	56	55	56	54	52	50	48	46
B4. Net non-debt creating flows at historical average minus one standard deviation in 2012-2013 4/	56	86	119	110	104	97	88	61
B5. Combination of B1-B4 using one-half standard deviation shocks	56	82	111	104	98	92	84	60
B6. One-time 30 percent nominal depreciation relative to the baseline in 2012 5/	56	55	56	54	52	50	48	46
PV of debt-to-revenue ratio								
Baseline	111	111	111	112	105	105	93	85
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2011-2031 1/	111	88	74	63	50	41	-2	-100
A2. New public sector loans on less favorable terms in 2011-2031 2	111	113	118	122	118	120	121	136
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2012-2013	111	115	122	123	116	116	103	94
B2. Export value growth at historical average minus one standard deviation in 2012-2013 3/	111	126	157	155	144	142	122	94
B3. US dollar GDP deflator at historical average minus one standard deviation in 2012-2013	111	115	120	120	114	113	101	92
B4. Net non-debt creating flows at historical average minus one standard deviation in 2012-2013 4/	111	171	232	226	208	204	169	110
B5. Combination of B1-B4 using one-half standard deviation shocks	111	165	225	220	203	199	166	112
B6. One-time 30 percent nominal depreciation relative to the baseline in 2012 5/	111	153	154	155	146	146	130	118

Table 3b. Kyrgyz Republic: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2011-2031 (continued)
(In percent)

Debt service-to-exports ratio								
Baseline	3	3	2	2	2	2	3	4
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2011-2031 1/	3	2	2	2	1	1	1	-1
A2. New public sector loans on less favorable terms in 2011-2031 2	3	3	2	3	2	3	4	5
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2012-2013	3	3	2	2	2	2	3	4
B2. Export value growth at historical average minus one standard deviation in 2012-2013 3/	3	3	3	4	3	4	6	6
B3. US dollar GDP deflator at historical average minus one standard deviation in 2012-2013	3	3	2	2	2	2	3	4
B4. Net non-debt creating flows at historical average minus one standard deviation in 2012-2013 4/	3	3	3	4	3	3	6	6
B5. Combination of B1-B4 using one-half standard deviation shocks	3	3	3	4	3	3	6	5
B6. One-time 30 percent nominal depreciation relative to the baseline in 2012 5/	3	3	2	2	2	2	3	4
Debt service-to-revenue ratio								
Baseline	6	5	5	5	4	5	6	7
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2011-2031 1/	6	5	4	4	3	3	2	-2
A2. New public sector loans on less favorable terms in 2011-2031 2	6	5	5	5	5	6	7	9
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2012-2013	6	5	5	5	5	5	7	8
B2. Export value growth at historical average minus one standard deviation in 2012-2013 3/	6	5	5	6	5	6	8	8
B3. US dollar GDP deflator at historical average minus one standard deviation in 2012-2013	6	5	5	5	5	5	7	8
B4. Net non-debt creating flows at historical average minus one standard deviation in 2012-2013 4/	6	5	6	8	7	7	12	10
B5. Combination of B1-B4 using one-half standard deviation shocks	6	5	6	8	7	7	12	10
B6. One-time 30 percent nominal depreciation relative to the baseline in 2012 5/	6	7	7	7	6	7	9	10
<i>Memorandum item:</i>								
Grant element assumed on residual financing (i.e., financing required above baseline) 6/	25	25	25	25	25	25	25	25

Sources: Country authorities; and staff estimates and projections.

1/ Variables include real GDP growth, growth of GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.

2/ Assumes that the interest rate on new borrowing is by 2 percentage points higher than in the baseline, while grace and maturity periods are the same as in the baseline.

3/ Exports values are assumed to remain permanently at the lower level, but the current account as a share of GDP is assumed to return to its baseline level after the shock (implicitly an offsetting adjustment in import levels).

4/ Includes official and private transfers and FDI.

5/ Depreciation is defined as percentage decline in dollar/local currency rate, such that it never exceeds 100 percent.

6/ Applies to all stress scenarios except for A2 (less favorable financing) in which the terms on all new financing are as specified in footnote 2.

Statement by the IMF Staff Representative on the Kyrgyz Republic
June 20, 2011

1. This statement briefly summarizes recent developments since the issuance of the Staff Report for the 2011 Article IV Consultation and Request for a Three-Year Arrangement Under the Extended Credit Facility (www.imf.org). In the staff's view, none of these developments warrant any change in the Staff Appraisal.
2. **All three prior actions have been observed.** The National Bank of the Kyrgyz Republic (NBKR) Board adopted a resolution announcing the liquidation of the Special Bank Refinancing Fund on June 10, 2011. The authorities/NBKR have selected big-four companies to conduct a forensic audit of the Kyrgyz Republic Development Fund (PWC) and a financial audit of Zalkar bank (KPMG).
3. **Consumer prices fell in May for the first time in more than a year.** Month-on-month deflation in May was 0.3 percent and was broad based, with the 12-month rates of both core and headline inflation declining (headline inflation declined to 22.1 percent). These developments were expected and suggest that the end-year inflation objective is attainable. However, the NBKR will need to remain vigilant to ensure that reserve money targets are met, especially in the face of a recent rebound in foreign exchange inflows.
4. **The president nominated the current NBKR deputy chairperson for the position of NBKR chairperson.** The parliamentary hearing on the nomination is currently scheduled for June 16. Any further delays could exacerbate uncertainties surrounding NBKR management, thereby hindering the NBKR's ability to take resolute actions on the problem banks.
5. **The authorities have continued to press for more concessional terms on planned borrowing from China for large energy infrastructure projects.** The latest information from the Ministry of Finance indicates that the lender has agreed to extend the grace period on these loans, which will raise the grant element to above the 35 percent threshold.
6. **Recently released official data confirm an increase in poverty in 2010.** Following the economic contraction in the aftermath of the 2010 events and an increase in inflation, aggregate poverty increased from 31.7 percent to 33.7 percent and extreme poverty increased from 3 percent to 5.3 percent in 2010 compared to 2009.



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IMF Executive Board Concludes 2011 Article IV Consultation with Kyrgyz Republic

On June 20, 2011, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with the Kyrgyz Republic.¹

Background

The Kyrgyz Republic is recovering from a deep political crisis last year. In April 2010, a popular uprising toppled the previous regime and internal ethnic conflict in June 2010 exacerbated the already difficult political situation. The subsequent constitutional referendum and parliamentary elections in October 2010 have helped to stabilize the political situation and put the economy on a path of recovery, though the political situation remains fragile with presidential elections scheduled for later this year.

The fallout from the domestic crisis has posed significant challenges. Border closures, especially with Kazakhstan, hampered Kyrgyz companies and households involved in trade. The security situation led to the lowest tourist arrivals in almost a decade. Interruptions in the spring farming season and problems in harvesting and marketing have led to losses in agricultural production. Rising global food and fuel prices have posed additional challenges. The banking sector also suffered from diminished

¹ Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summing up can be found here: <http://www.imf.org/external/np/sec/misc/qualifiers.htm>.

depositor confidence and the economic effects from events in the south. Subsequently, the economy contracted by 1.4 percent and inflation rose to nearly 20 percent in 2010. To counter rising inflation, monetary policy was tightened toward the end of 2010. Early signs of recovery have started to appear this year, with the economy growing by 3.2 percent in the first four months of 2011.

On the back of political and macroeconomic stability, the Kyrgyz economy is expected to grow by 6 percent in the medium term with positive spillovers from its larger partners in the Region. Agriculture, tourism, mining and textile production will be important drivers of growth. Strong export oriented growth and fiscal consolidation will help to reduce the current account deficit in the medium term. Official development assistance, while slowing, will remain an important source of financing the current account deficit and will help to maintain an adequate reserves level.

Executive Board Assessment

Executive Directors noted that the economy is recovering from a deep political crisis, which disrupted activity and negatively affected near-term growth prospects. Directors commended the authorities for their efforts to restore macroeconomic stability and acknowledged the timely and coordinated assistance by the international community, which helped prevent the economy from falling into a deeper recession. Directors noted that the recovery remains fragile and a steadfast implementation of prudent policies and structural reforms are crucial to improving growth prospects.

Directors acknowledged the importance of supporting the nascent recovery, but underscored that fiscal consolidation is needed to rebuild policy buffers, reduce vulnerabilities, and promote inclusive growth over the medium term. In this context, Directors welcomed the revenue and expenditure measures prepared by the authorities, and encouraged them to follow through with contingency plans, possibly based on reductions in low-priority spending, if risks to the fiscal position materialized.

Directors noted the risks and governance issues associated with extra-budgetary funds and underscored the importance of channeling all public finances through the budget. They welcomed the authorities' decision to liquidate the Special Bank Refinancing Fund and their efforts to increase the transparency of public finances through improved reporting and monitoring of large state-owned enterprises. They also encouraged the authorities to strengthen the existing targeted social assistance system, with the support of key development partners.

Directors expressed concerns on continued high inflation, and welcomed the central bank's timely tightening of monetary policy in response to growing inflationary pressures. Most Directors agreed with the need for further policy tightening if inflation fails to decline in the period ahead. Directors noted the staff assessment that the

exchange rate is broadly in line with fundamentals and highlighted that exchange rate flexibility has served the Kyrgyz Republic well.

Directors noted that developments in the banking sector have exposed shortcomings in the bank resolution framework and the central bank's de facto lack of supervisory independence. They encouraged the authorities to take decisive action to resolve problem banks and restore confidence in the financial system, and welcomed the selection of an external auditor for Zalkar Bank. Directors stressed the need to reform the legal framework for early intervention and resolution of problem banks, and highlighted the need for enhanced supervisory vigilance and increased capital buffers for the largest state-owned bank.

Directors endorsed the authorities' structural reform agenda, emphasizing that steadfast implementation is critical to the success of the economic program. They welcomed plans to improve the business environment, which is key to supporting private sector-led growth, and stressed that energy sector reform would create an important driver for growth in the medium term. Directors also welcomed the ongoing efforts to increase transparency and efficiency of the largest energy companies, with assistance from key development partners.

Public Information Notices (PINs) form part of the IMF's efforts to promote transparency of the IMF's views and analysis of economic developments and policies. With the consent of the country (or countries) concerned, PINs are issued after Executive Board discussions of Article IV consultations with member countries, of its surveillance of developments at the regional level, of post-program monitoring, and of ex post assessments of member countries with longer-term program engagements. PINs are also issued after Executive Board discussions of general policy matters, unless otherwise decided by the Executive Board in a particular case.

Kyrgyz Republic: Selected Economic Indicators, 2008–11

	2008	2009	2010	2011
	Act.	Act.	Prel.	Proj.
Real GDP (growth in percent)	7.6	2.9	-1.4	6.0
Nongold real GDP (growth in percent)	5.4	3.4	-2.1	5.8
Consumer prices (12-month percent change, eop)	20.1	0.0	18.9	13.0
Consumer prices (12-month percent change, average)	24.5	6.8	7.8	20.0
General government finances (in percent of GDP) 1/				
Total revenue and grants	29.9	32.1	31.7	34.6
<i>Of which:</i> Tax revenue	23.0	22.2	23.2	24.0
Total expenditure (including net lending)	29.2	36.1	38.1	42.3
<i>Of which:</i> Current expenditure	24.8	28.4	32.2	34.9
Capital expenditure	4.1	5.0	5.6	6.9
Overall fiscal balance	0.0	-3.5	-6.5	-7.6
Primary balance excluding grants	-1.1	-7.8	-8.6	-10.6
Banking sector				
Reserve money (percent change, eop)	11.3	18.9	18.4	16.4
Broad money (percent change, eop)	12.6	20.9	21.1	15.7
Credit to private sector (percent change, eop)	26.4	-2.8	6.3	18.0
Credit to private sector (in percent of GDP)	14.2	12.9	13.0	13.0
External sector				
Current account balance (in percent of GDP)	-8.1	0.7	-2.1	-8.7
Export growth (percent change)	35.4	-11.3	-6.2	23.9
Import growth (percent change)	47.5	-22.4	6.0	26.7
Gross International reserves (in millions of U.S. dollars)	1,222	1,584	1,716	1,862
Gross reserves (months of next year imports, eop)	4.0	4.9	4.2	4.1
External public debt outstanding (in percent of GDP)	41.2	52.8	57.3	51.0

Sources: Kyrgyz authorities and IMF staff estimates and projections.

1/ General government comprises State Government, Social Fund and Development Fund (starting from September 2009) finances. State government comprises central and local governments.



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International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Approves US\$106 Million Extended Credit Facility Arrangement for the Kyrgyz Republic

The Executive Board of the International Monetary Fund (IMF) today approved a three-year SDR 66.6 million (about US\$106 million) arrangement under the Extended Credit Facility for the Kyrgyz Republic to support the economic recovery in the short term and place the country on the road to stronger sustained and inclusive growth in the medium term. The Board's approval enables the immediate disbursement of SDR 9.514 million (about US\$15.2 million).

The Kyrgyz Republic suffered from a deep political crisis in 2010. The fallout from the domestic crisis has posed significant challenges. The economy contracted last year, straining the government's financial position, further exacerbated by critical reconciliation, recovery and reconstruction needs. The banking sector also suffered from diminished depositor confidence and the economic effects from the events in the south. Moreover, the global food and fuel price shock triggered a sharp rise in inflation, eroding real incomes of the most vulnerable part of the population.

The new Fund-supported program will provide a coherent macroeconomic framework that will support the authorities' efforts to sustain economic recovery, promote inclusive growth in a low inflation environment, restore macroeconomic stability, achieve medium-term fiscal consolidation, address weaknesses in the financial sector, improve the country's governance, and catalyze critical donor support.

Following the Executive Board's discussion on the Kyrgyz Republic, Mr. Naoyuki Shinohara, Deputy Managing Director and Acting Chair, stated:

“Domestic political turmoil in the Kyrgyz Republic in 2010 disrupted economic activity and negatively affected near-term growth prospects. Real GDP contracted, the current account shifted to a deficit, international reserves coverage declined, and credit growth stalled. Moreover, rising international food and fuel prices have increased inflation and eroded real

incomes. Faced with these challenges, the authorities have developed a strong program, which aims at restoring macroeconomic stability, rebuilding policy buffers, catalyzing donor assistance, and promoting private sector-led inclusive growth.

“A limited fiscal expansion in 2011 will support the nascent economic recovery, but policies will need to be carefully balanced to curb inflationary pressures. Significant fiscal consolidation in 2012 and beyond will be critical to ensure medium-term fiscal and debt sustainability and support efforts to reduce inflation. The central bank has already tightened monetary policy and stands ready to tighten further if necessary.

“Last year’s political turmoil exposed weaknesses in the financial sector. Strengthening the supervisory independence of the central bank will play a pivotal role in restoring confidence in the financial sector, mitigating vulnerabilities, and ultimately enabling banks to perform their key function of intermediating scarce resources.

“While the authorities have made progress in reforming the regulatory framework related to the business environment, addressing longstanding governance issues will be key to enhancing the role of the private sector and fully realizing the economy’s long-term growth potential.”

ANNEX

Recent Economic Developments

While there are early signs of recovery from the economic contraction in 2010, the situation remains fragile with inflation at more than 20 percent. The political crisis has disrupted trade flows, agricultural production, construction, and tourism, which led to a shift in the current account from surplus to deficit. Fiscal policy has been expansionary, albeit less than anticipated and monetary policy was tightened toward the end of the year to counter rising inflation. The latter is already yielding tangible results with May 2011 having been the first deflationary month in over a year.

Program Summary

Sustain economic recovery and foster inclusive growth to help reduce poverty.

The program foresees a slight fiscal expansion in 2011 to further support the nascent economic rebound. The authorities expect real GDP to grow by about 6 percent on average during 2011–14 on the back of continued political stability and a rebound in agriculture, trade and construction. To ensure that the growth dividends also benefit the poor, the government plans to further develop key targeted social assistance programs with the support of development partners. The authorities also plan to raise the size of the Guaranteed

Minimum Income by almost 20 percent and increase spending on Unified Monthly Benefits and Monthly Social Benefit to catch up with the rising cost of living.

Bring the fiscal position back on a sustainable path in the medium term. To achieve this goal, the authorities will introduce additional revenue measures and restrain expenditures. Given that a large part of the domestic economy remains outside the tax system, the Kyrgyz government efforts will focus specifically on broadening the tax base, which should help improve the efficiency of the Kyrgyz tax system. The main elements of the reform will be to improve the customs valuation system, removing tax exemptions and reforming excise taxation on tobacco and alcohol. Such measures will encourage the formalization of the economy, limit tax evasion, spread the tax burden more evenly and simplify the tax system.

Improve the resilience of the country's financial sector. Political developments in 2010 tested the Kyrgyz financial system and severely disrupted the regular course of supervisory activities. The authorities are taking actions to isolate and resolve the problems in the banking system to ensure that the banking system is sufficiently resilient to withstand possible further shocks. Such actions include resolution of troubled banks, asset recovery measures from fraudulent transactions and strengthening supervision, particularly of systemically important banks.

The authorities are committed to improving governance in the country. Addressing this issue remains one of the biggest challenges for the Kyrgyz government. Ensuring the efficient use of public resources and improving the business climate will be instrumental to attract high-quality domestic and foreign investments in the country.

Statement by Mr. Weber, Executive Director, and Mr. Duperrut, Advisor to Executive Director
June 20, 2011

On behalf of our Kyrgyz authorities, we thank management and staff for the candid set of reports and for the constructive discussions on a medium-term program engagement. This intensive dialogue, building on the recent Rapid Credit Facility (RCF) and the Ex Post Assessment (EPA) of Longer-Term Program Engagement, has resulted in clear and welcome policy guidance. The authorities concur with the staff's appraisal, including on the necessity for fiscal consolidation beyond 2011, the importance of financial sector stability, the thrust of the required structural reforms, and the extent of the balance of payments need. In support of their strategy, our Kyrgyz authorities ask the Executive Board to favorably consider their request for an Extended Credit Facility (ECF) in the amount of SDR 66.6 million (75 percent of quota). All three prior actions for this program request have been met.

The authorities are grateful to the Fund for rapidly providing financial support to the Kyrgyz Republic under difficult circumstances last summer, which was instrumental for restoring macroeconomic stability and building a sound track record. They are equally thankful to the international donor community for the solidarity shown at the Development Forum held in Bishkek in July 2010. The authorities are pleased that US\$380 million of the US\$1.1 billion pledged at the Forum have so far been contracted. However, given their substantial financing needs and the fact that donor support represents the major source to cover the projected financing gap, they hope that the pledges made will be fully and expeditiously validated. The ECF provides a strong policy framework and sufficient assurances to donors, also with regard to shortcomings in the areas of implementation capacity and ownership. The new program will serve to anchor sound macroeconomic policies over the medium-term as the political transition to a Parliamentary democracy is being completed.

Macro-economic situation

In the past year, the Kyrgyz Republic faced a number of shocks, political and economic, external and internal. These shocks occurred in the context of a world economy slowly emerging from the global crisis, which significantly affected its major trading partners. Nonetheless, the economy is recovering more quickly than expected and the decline in growth was measured. The major impact of the shocks was felt on prices, with overall inflation rising above 20 percent. Decisive monetary policy actions since December 2010 should reduce the inflation rate towards the authorities' end-year objective, thus re-anchoring inflationary expectations. While fiscal policy is still expansionary, the deficit outcome for 2010 and 2011 is notably more benign compared to earlier projections. Increased public spending is geared towards much needed salary adjustments in the education and health care sectors as well as targeted social assistance programs, in an effort to promote more inclusive growth. The authorities have prepared contingency measures to deal with potential revenue shortfalls, including the possibility to privatize state-owned enterprises, and have signaled

their intention to save the bulk of revenue over-performance.

In the financial sector, the largest bank was involved in fraudulent activities related to the previous regime and a significant number of commercial banks had to be put under temporary administration. Although these events exposed problems of bank supervision, there was no deposit run thanks to the authorities' credible assurances that financial stability was not at risk. The resolution of the troubled banks has started, most notably with the separation of the largest bank into a good bank and a bad bank.

The authorities are well aware that the country, currently at moderate risk of debt distress, remains vulnerable to exogenous shocks which could impact debt sustainability. They reached an agreement with Turkey to cancel bilateral debts and are in contact with Russia and other creditors to reach similar agreements. They intend to contract only concessional loans and, in that regard, have been able to agree with their Chinese creditor that the terms of the energy sector loan be extended on concessional terms.

Request for an ECF Arrangement

The Kyrgyz authorities acknowledge a weak track record in terms of implementing structural reforms and economic governance, as pointed out in the recent EPA. The EPA also highlighted key policy priorities, particularly medium-term fiscal consolidation, and noted that conditionality in a future Fund program should be streamlined, focused on core elements of the Fund's mandate, based on a homegrown development strategy, and not be overly intrusive. The authorities believe that the new ECF appropriately follows this guidance. The program will support the authorities Action Plan for Economic Security for 2011 and form a major pillar of their upcoming Country Development Strategy (PRSP).

- Fiscal consolidation will start in 2012 with the implementation of ambitious measures on both the revenue and expenditure sides. Tax policy and tax administration, particularly towards large taxpayers, will be strengthened further by expanding the role of the Large Taxpayer's Office. The social fund will be consolidated into the budget and no new extra budgetary funds will be created. Fund technical assistance financed by the new Topical Trust Fund on Tax Policy Administration will be most welcome.
- Responding to concerns about past rent seeking behavior, the President of the Kyrgyz Republic introduced in each governmental body a supervisory board that will oversee the practice of resource allocation, procurement, recruiting, and promotions. The Kyrgyz Republic has become compliant under the extractive industries transparency initiative (EITI) in March 2011.
- Regarding the necessary reforms in the energy sector, the authorities take good note of the division of labor with other international institutions, based on comparative advantage. The World Bank, through its Economic Recovery Support Operation, and

other development partners will predominantly contribute in this area.

- The authorities commit to refrain from using the National Bank of the Kyrgyz Republic (NBKR) as a financing source for public uses by closing down the Special Bank Refinancing Fund (SBRF). They aim to ensure the independence of the NBKR, including in its role as financial sector supervisor.

The Kyrgyz authorities appreciate the importance of strengthening democracy, improving governance as well as the rule of law, strengthening oversight over public resources based on the lessons from the past, and managing public assets in a transparent way. Progress in these areas will greatly help promote political stability and social peace. Our Kyrgyz authorities are committed to further close cooperation with the Fund that will help achieve these objectives in the context of a Fund arrangement.