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INTERNATIONAL DEVELOPMENT ASSOCIATION

PROGRAM DOCUMENT

FOR

**A PROPOSED CREDIT
IN THE AMOUNT OF SDR 8.99 MILLION
(US\$13.89 MILLION EQUIVALENT)**

AND

**A PROPOSED GRANT
IN THE AMOUNT OF SDR 7.19 MILLION
(US\$11.11 MILLION EQUIVALENT)**

TO

THE KYRGYZ REPUBLIC

FOR THE

SECOND DEVELOPMENT POLICY OPERATION

May 12, 2014

**Poverty Reduction and Economic Management
Europe and Central Asia Region**

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THE KYRGYZ REPUBLIC – GOVERNMENT FISCAL YEAR

January 1 – December 31

CURRENCY EQUIVALENTS

(Exchange rate effective as of April 29, 2014)

Currency Unit = Kyrgyz Som (KGS)

US\$1.00 = KGS54.1181

ABBREVIATIONS AND ACRONYMS

ADB	Asian Development Bank	KfW	German Development Bank
CAD	Current Account Deficit	KGS	Kyrgyz Som
CoI	Conflict of Interest	LAC	Latin America and Caribbean
CoA	Chamber of Accounts	LDP	Letter of Development Policy
CPS	Country Partnership Strategy	MoE	Ministry of Economy
CR	Credit Registry	MoEI	Ministry of Energy and Industry
DfID	Department for International Development	MoF	Ministry of Finance
DB	Doing Business	MTTP	Medium-Term Tariff Program
DPA	Deposit Protection Agency	M&E	Monitoring and Evaluation
DPO	Development Policy Operation	NATO	North-Atlantic Treaty Organization
DPO1	First Development Policy Operation	NBKR	National Bank of the Kyrgyz Republic
DPO2	Second Development Policy Operation	NEGK	National Electric Grid of Kyrgyzstan
DPS	Deposit Protection System	NGO	Non-government Organization
DSA	Debt Sustainability Analysis	NPL	Non-performing Loan
EaDB	Eurasian Development Bank	NSDS	National Sustainable Development Strategy
EBRD	European Bank for Reconstruction and Development	OECD	Organisation for Economic Cooperation and Development
EC	European Commission	PEFA	Public Expenditure and Financial Accountability
ECA	Europe and Central Asia	PER	Public Expenditure Review
ECF	Extended Credit Facility	PFM	Public Financial Management
ERSO	Emergency Recovery Support Operation	PIFC	Public Internal Financial Control
ESW	Economic and Sector Work	PPL	Public Procurement Law
EU	European Union	PRAF	Prompt Remedial Action Framework
FDI	Foreign Direct Investment	PSD	Private Sector Development
EPP	Electric Power Plants	PSRR	Public Sector Reform Roadmap
FIRST	Financial Sector Reform and Strengthening Initiative	ROSC	Report on the Observance of Standards and Codes
FSAP	Financial Sector Assessment Program	SIDA	Swedish International Development Agency
FY	Fiscal Year	SDR	Special Drawing Rights
GDP	Gross Domestic Product	SPS	State Personnel Service
GNI	Gross National Income	TA	Technical Assistance
GoKR	Government of the Kyrgyz Republic	UNDP	United Nations Development Program
IDA	International Development Association	US	United States of America
IFC	International Finance Corporation	USAID	United State Agency for International Development
IMF	International Monetary Fund	VAT	Value Added Tax
IPSAS	International Public Sector Accounting Standards	WB	World Bank
ISN	Interim Strategy Note	WGI	Worldwide Governance Indicators
JICA	Japan International Cooperation Agency	WTO	World Trade Organization
JSDP	Judicial Sector Development Plan		

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THE KYRGYZ REPUBLIC
SECOND DEVELOPMENT POLICY OPERATION

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SUMMARY OF PROPOSED CREDIT/GRANT AND PROGRAM

THE KYRGYZ REPUBLIC SECOND DEVELOPMENT POLICY OPERATION

Borrower	The Kyrgyz Republic
Implementation Agency	Ministry of Finance
Financing Data	IDA Credit (SDR8.99 million, \$13.89 million equivalent) of 40 years maturity including a 10-year grace period and IDA Grant (SDR 7.19 million, \$11.11 million equivalent).
Operation Type	The second in a series of two Programmatic Development Policy Operations.
Pillars of the Operation And Program Development Objective	<p>The proposed DPO2 supports government efforts in the following two pillars:</p> <ol style="list-style-type: none"> i. Improving public sector governance ii. Enhancing the business environment. <p>The main Program Development Objective is to promote sustainable growth through more accountable use of public resources and an improved environment for doing business. The first pillar supports increased accountability and transparency in the use of public resources which is expected to improve the quality of public service and generate savings that will strengthen fiscal sustainability and allow re-allocation of some spending to priority areas. The second pillar supports actions to address the constraints to a more vibrant development of the private sector, including through improved business inspection systems, a more effective judiciary, improved banking supervision, and a stronger deposit protection framework. The program is consistent with the priorities of the National Sustainable Development Strategy and is closely aligned with the FY13-17 CPS and is expected to contribute to reducing poverty and sharing prosperity.</p>
Result Indicators	<ol style="list-style-type: none"> 1. Worldwide Governance Indicator Control of Corruption – percentile rank Baseline: 9.95 (2011) Target: 15 (2014) 2. Effectiveness of internal audit increased (PEFA PI-21) Baseline: D (2009) Target: C (2014) 3. MoF public procurement report shows increasing compliance with PPL Baseline: no information provided on effectiveness of public procurement. (2011) Target: information available on effectiveness of public procurement. (2014) 4. Key operational and financial performance indicators and key decisions of the power sector are regularly disclosed. Baseline: no indicators are disclosed (2011) Target: key operational and financial performance indicators are disclosed. (2014) 5. Increase in the budget for the judiciary. Target: Annual rate of increase of 10 percent (2015) 6. Strength of investor protection index (sub-indicator of DB) improved. Baseline: score 7 (DB2011) Target: score 8 (DB2015) 7. Risk-based inspection by MoE and pilot agencies reduces inspection burden. Baseline: inspections are not risk-based (2011) Target: inspections are risk-based (2014) 8. NBKR regularly collects credit information from banks and microfinance institutions and enhances supervision. Baseline: no records on parallel loans (2011) Target: parallel loans are tracked (2014) 9. Increased confidence in banks as evidenced by increasing deposits to GDP ratio.

	Baseline: 16 percent (November 2013) Target: 20 percent (December 2014)
Overall risk rating	This is a high risk operation. This rating reflects the fragile political situation, concerns about the sustainability of growth and the macroeconomic framework, a weak fiduciary environment and a low, albeit evolving, institutional capacity.
Operation ID	P126274

**IDA PROGRAM DOCUMENT FOR A
PROPOSED SECOND DEVELOPMENT POLICY OPERATION
TO THE KYRGYZ REPUBLIC**

1. INTRODUCTION AND COUNTRY CONTEXT

1. **This program document describes the Second Development Policy Operation in a programmatic series of two operations, which aims to address Kyrgyz Republic's key development policy challenges.** The operation supports the efforts of the Kyrgyz authorities to improve public sector governance and enhance the business environment. The program is anchored in the 2013-17 National Sustainable Development Strategy (NSDS) which aims to lay foundations for faster, more sustainable growth, more and better jobs and reduced poverty. The medium-term fiscal policy under the program is supportive of macroeconomic stability while safeguarding key social spending. The amount of the proposed Second Development Policy Operation (DPO2) is US\$25 million with a 55-45 percent credit-grant element. The first operation in the series, in the amount of US\$25 million, was approved in July 2013.

2. **The DPO series is a pivotal element in the World Bank Group's strategy for the Kyrgyz Republic.** It is aligned with the objective of the FY13-17 Country Partnership Strategy (CPS) of improving governance along three areas: i) public administration and service delivery; ii) business environment; and iii) management of natural resources and infrastructure. The DPO program was a central pillar of the FY12-13 Interim Strategy Note (ISN) and its focus on governance and private sector growth addresses some of the key causes of the 2010 revolution.

3. **The Kyrgyz Republic is a young democracy undergoing a significant transformation and the DPO2 design reflects this process and the country's ambitions.** Growth performance has been volatile and poverty remains high, at least partly contributing to the outbreak of two revolutions since 2005. While the changes that followed the April 2010 events transferred power to a popularly elected parliament, expectations of a significant improvement in living conditions have been only partially met and the Kyrgyz Republic remains one of the poorest countries in Europe and Central Asia with a GNI per capita in 2012 of around US\$1,000. In addition, the country's institutions need to be strengthened further to ensure effective implementation of the new political arrangements. Reflecting this, the proposed DPO2 supports reforms that are feasible in the existing complex political setting and are accompanied with technical assistance activities in various areas. Clearly, the reform agenda in these areas will need to continue beyond this DPO series.

4. **The political situation has improved since 2010, but remains challenging.** The October 2011 parliamentary elections were regarded as free and fair, and in September 2012 and April 2014 new governments were formed expeditiously demonstrating the country's growing capacity for democratic governance. In addition, the new system has put greater emphasis on consensus building among various stakeholders resulting in largely shared vision for the strategic priorities among key constituencies. However, the parliament and other newly empowered institutions are still learning how to effectively use the acquired powers and institutional checks

and balances are not always effective. Still, by 2012, 57 percent of the population felt the country was going in the right direction, compared to 30 percent in November 2010.¹

5. Numerous shocks have kept economic performance volatile and poverty rates high.

The Kyrgyz economy remains characterized by significant informality, reliance on a few sectors (gold, agriculture, and trade), and remittances.² The prudent fiscal stance until 2008 was replaced by significant fiscal expansion in response to the 2008-09 global recession and the 2010 domestic crisis, with the budget deficit averaging 5.0 percent of GDP during 2009-12, one of the highest in the Europe and Central Asia (ECA) region. Frequent shocks in recent years, including food price spikes and instability, also stunted progress in poverty reduction. About 38 percent of the population lived in poverty in 2012, down from nearly 60 percent in 2005 but up from 32 percent in 2008. An estimated 4.4 percent of the population lives in extreme poverty.

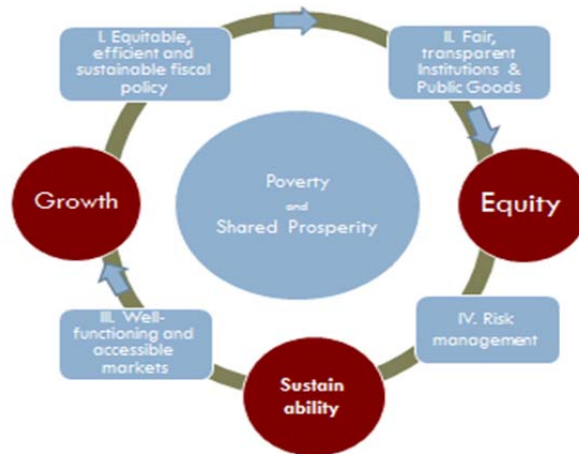
6. The Kyrgyz Republic has experienced some progress on social development since 2010. Although the prospect for economic growth and social progress looks more favorable going forward, fiscal imbalances and political risk, though lowered, may threaten the stability of growth.

7. The overall framework of this operation is aligned with the goals of reducing poverty and boosting shared prosperity. Achievement of these goals rests on the three pillars of growth, equity, and sustainability (see Figure 1). These in turn require appropriate fiscal policies, functioning public institutions and private markets, and effective risk management. The policies supported by this operation are expected to promote economic *growth* and its *sustainability*. Strengthening public sector governance will improve allocation of public resources and combined with measures to enhance the business environment and boost private sector activity, will promote sustained and higher growth. Previous episodes of growth in the Kyrgyz Republic have been closely associated with poverty reduction and growth in the consumption of the bottom 40 percent. Finally, governance failures in the country have led to poor quality of public services and contributed to the turmoil over the last decade. Thus, a focus on governance and lowering barriers to economic activity is also critical to promoting greater *equity* and inclusiveness of the country's economic progress.

¹ International Republican Institute, Kyrgyzstan National Opinion Poll, April 2012, available at: <http://www.iri.org/news-events-press-center/news/iri-releases-post-presidential-election-survey-kyrgyzstan-public-opini>.

² According to "Shadow economies all over the world – new estimates for 162 countries from 1999 to 2007," WB PRWP 5356, the informal economy in the Kyrgyz Republic between 1999 and 2007 hovered around 40 percent.

Figure 1: Poverty Reduction and Shared Prosperity Policy Framework



Source: www.worldbank.org (LAC equity lab).

2. MACROECONOMIC POLICY FRAMEWORK

A. RECENT ECONOMIC EVENTS

8. **Following a strong rebound in 2013, as gold production recovered, economic activity moderated in early 2014.** Gold production at the main gold mine Kumtor recovered from the glacier movement in early 2012 which disrupted gold production, adding 5.1 percentage points to the 10.5 percent GDP growth rate in 2013. This followed a GDP decline of 0.1 percent in 2012, confirming the pattern of volatile growth due to heavy reliance on gold, remittances, and re-exports. The non-Kumtor economy grew by 5.8 percent in 2013, the third year of growth rates of 5-6 percent, with construction and trade leading economic activity. GDP growth moderated to 5.6 percent year-on-year in the first quarter of 2014 as gold production stabilized.

9. **Private consumption, public investments and gold exports fueled economic activity.** Official international money transfers grew by 7.9 percent in 2013 while the 12-month growth rate of credit to the private sector increased to 44.2 percent y-o-y by March 2014. In response, private consumption grew by 5.1 percent in 2013. Government consumption was largely flat, reflecting a wage freeze for most of the public sector and stronger controls over spending on goods and services. Public investments in energy and transport and a recovery in foreign direct investment (FDI) kept investment levels strong. Net exports continued to be a drag on growth.

10. **Buoyant domestic demand and stagnating non-gold exports are keeping the current account deficit large.** The dollar value of exports grew by 4.8 percent in 2013 as the recovery of gold exports was offset by lower gold prices and a fall in non-gold exports. Terms of trade losses from lower gold prices amounted to about 2 percent of GDP, while non-gold exports fell by 6 percent in 2013 as Russia's accession to the World Trade Organization (WTO) increased competition for Kyrgyz garments producers and stricter Customs Union standards affected Kyrgyz dairy exports. Imports increased by 8.9 percent keeping the trade deficit high. Despite strong remittances and improved tourism receipts, the current account deficit is estimated to have

remained in double-digits. Still, large errors and omissions suggest that the actual current account deficit may not be as high.

Table 1: Key Macroeconomic Indicators and Projections

(In percent of GDP unless otherwise noted)

	2009	2010	2011	2012	2013	2014	2015	2016
	Act.	Act.	Act.	Act.	Prel.	Proj.	Proj.	Proj.
<u>Real sector</u>								
GDP, in US\$ million	4,683	4,794	6,199	6,603	7,225	7,531	7,946	8,531
GDP per capita, in US\$	864	875	1,120	1,182	1,280	1,321	1,380	1,467
GDP growth, in percent	2.9	-0.5	6.0	-0.1	10.5	4.4	4.9	5.0
Investment	22.9	23.9	24.0	26.2	25.6	27.3	29.3	29.4
<u>Fiscal accounts</u>								
Revenues and grants	32.1	30.5	31.8	33.8	33.9	32.1	31.2	31.0
Expenditures	36.1	36.6	36.3	39.0	37.6	36.4	34.7	33.9
Balance 1/	-3.5	-6.3	-4.6	-5.3	-4.0	-4.3	-3.5	-2.9
Public debt	58.1	59.7	49.4	49.0	47.7	51.9	51.9	52.6
<u>External accounts</u>								
Exports of goods and services	54.5	52.7	54.7	53.6	55.1	57.9	56.3	56.4
Imports of goods and services	78.9	81.7	82.3	97.7	95.9	99.7	96.4	95.5
Current account balance	-2.5	-6.4	-6.0	-15.0	-13.5	-15.7	-14.5	-12.6
External debt	89.3	92.7	76.7	81.3	84.4	82.6	81.3	82.0
<u>Prices and exchange rates</u>								
Inflation, period average	6.8	7.8	16.6	2.8	6.6	6.1	6.6	6.0
Exchange rate, KGS/US\$	44.1	47.1	46.5	47.4	48.6			

Source: Bank staff calculations based on data from national authorities.

1/ Includes statistical discrepancy.

11. **The large external imbalance and weaker currencies of Kyrgyz Republic's key trading partners due to the ongoing formalization of US monetary policy put a pressure on the som in early 2014.** Capital and financial inflows exceeded the current account deficit for most of 2013, resulting in an increase in foreign exchange reserves. Net FDI increased to above 10 percent of GDP with trade credits and borrowing providing additional capital inflows. However, the recent gradual normalization of the US monetary policy affected capital inflows to many developing countries and weakened their exchange rates. The currency of Russia, a key partner of the Kyrgyz Republic, was further affected by the developments in Ukraine with the ruble losing around 20 percent of its value over the last year. The exchange rate of Kazakhstan, another important partner was devalued by 20 percent in February 2014, as the tenge weakened by nearly 28 percent against the dollar since early 2013. These developments pushed up demand for foreign exchange in the Kyrgyz Republic causing the som to lose more than 10 percent of its value against the dollar since the start of 2014. The central bank used around 2 percent of

foreign exchange reserves to allow an orderly adjustment in the exchange rate. Reserves remain above 3 months of imports and provide decent coverage of broad money and imports.

12. **The authorities are taking steps to reverse the post-2008 fiscal expansion.** A surge in government spending between 2009 and 2012 increased the fiscal deficit to 5.0 percent of GDP on average, one of the highest in the ECA region. Robust revenues, a wage freeze, and spending restraint helped reduced the deficit to around 4 percent of GDP in 2013, compared with a target of 5.2 percent of GDP. Tax policy changes and improvements in tax administration in recent years increased revenues. Still, the tax base remains narrow due to large informality and numerous exemptions increasing the reliance on few entities (Kumtor, the Manas Transit Center). Expenditures are high, reflecting the large number of social programs, a large wage-bill and significant capital expenditures. Some of the policies that contributed to the surge in spending after 2009 were envisaged to be temporary but ended up as permanent fixtures to the budget, making the adjustment more difficult. The deficit is expected to increase in 2014 due to the closure of the Manas Transit Center which is unlikely to be fully offset through lower expenditures given existing rigidities.

Table 2: Fiscal Accounts

	(In percent of GDP)						
	2010	2011	2012	2013	2014	2015	2016
	Act.	Act.	Act.	Prel.	Proj.	Proj.	Proj.
Total revenue and grants	30.5	31.8	33.8	33.9	32.1	31.2	31.0
Tax revenues	22.3	23.1	25.5	25.6	25.7	25.5	25.8
Non-tax revenues	5.4	5.8	5.8	5.8	4.3	3.7	3.2
Grants	2.8	3	2.5	2.5	2.1	2.0	2.0
Total expenditure	36.6	36.3	39.0	37.6	36.4	34.7	33.9
Current expenditure	31	30.9	31.8	30.5	29.1	27.4	26.6
Wages	7.7	8.3	8.7	7.9	7.5	7.4	7.3
Transfers and subsidies	4.2	3.8	3.5	3.5	3.3	3.4	3.3
Social Fund expenditures	8.6	8.3	9.7	9.4	9.4	9.3	9.3
Interest	0.8	1	0.9	0.9	0.9	0.8	0.9
Purchases of goods and services	9.6	9.5	9.1	8.8	8.0	6.5	5.8
Capital expenditure and net lending	5.4	5.5	7.3	7.2	7.3	7.3	7.3
Statistical discrepancy	-0.2	-0.1	-0.1	-0.3	0	0	0
Overall balance	-6.3	-4.6	-5.3	-4.0	-4.3	-3.5	-2.9

Source: Bank staff calculations based on data from national authorities.

13. **Monetary policy was recently tightened in response to pressures on the currency.** The National Bank of the Kyrgyz Republic (NBKR) increased its discount rate to 6.0 percent in March 2014 from 4.2 percent at the end of 2013.³ Higher policy rates should help moderate the

³ In March 2014, the NBKR changed its monetary policy implementation framework defining the discount rate as an intermediate target for its monetary policy and assigning the authority for setting it to the Board of the NBKR.

rapid credit growth, though the effectiveness of the interest rate channel is limited. While the banking sector appears sound (adequate capital, reasonable profits and low NPLs), the loan-to-deposit ratio has been increasing from the late-2012. The establishment of a credit registry by the NBKR supported by this operation will help improve banking supervision and risk management.

14. **Headline inflation eased as international food and fuel prices moderated.** Following three food price shocks over the last five years, pressures from international markets eased during 2013 and early 2014. In March-2014, wheat prices were 20 percent below the peak levels registered in mid-2012, while oil prices remained largely unchanged. As a result, annual average inflation in the Kyrgyz Republic moderated to 6.6 percent on average in 2013 and in early 2014.

B. MACROECONOMIC OUTLOOK AND DEBT SUSTAINABILITY

15. **GDP growth is expected to moderate to about 5 percent a year as gold production stabilizes and remittances, FDI and credit to the private sector support demand.** Remittances and to a lesser extent exports are expected to grow, although with sizable downside risks. While Russia's growth is projected to dip to 1.1 percent in 2014 (and further to -1.8 percent in case the turmoil in Ukraine is extended), construction activity (where most Kyrgyz migrants are employed) is expected to be robust and growth in Kazakhstan is projected to remain at about 5-5.5 percent. China's growth is projected to moderate to a still high 7.5 percent and not cause disruptions to ongoing and planned projects in the Kyrgyz Republic. A strong public investment program and more credit to the private sector will add to demand.

Box 1: Emerging Macroeconomic Risks

Recent global developments can affect economic prospects of the Kyrgyz Republic. Tensions between Russia and Ukraine and slower growth in traditional partners could result in drop in remittances and exports, currency volatility, and higher wheat and energy prices exposing the Kyrgyz Republic to a scenario of low growth and high inflation. Russia is the main host country for the large Kyrgyz migrant population (15 percent of labor force) and a traditional export market for Kyrgyz garments. Remittances have been resilient and have grown despite slowing Russian GDP growth, due to robust performance in sectors that employ migrants (trade, construction, domestic services). However, a larger loss of confidence in response to a prolonged Crimean crisis would see investments declining by 10 percent in 2014 and consumption remaining largely flat. According to the team's estimates, a 10 percent reduction in remittances is likely to half the growth rate of the Kyrgyz economy to around 2.5 percent. In addition, Kyrgyz exports to Russia are already being affected by Russia's WTO accession and could further suffer if the slowdown is extended.

The loss in value of the Russian ruble and higher commodity prices will affect the Kyrgyz som and inflation. A 2005 study (Barhoumi, 2005) estimated the average long-run pass-through from exchange rate changes in developing countries at around 0.6-0.8. However, the Kyrgyz Republic shares some of the characteristics (small size, import dependent, limited domestic production) of countries that had higher pass-through rates. Also, wheat prices increased by 8.9 percent since the beginning of January while oil prices increased in late-February, but have since retreated. With food and fuel accounting for 48.9 percent of the consumer price index (CPI), higher world prices will translate into higher inflation and hardship for the country's poor. On the other hand, increased demand for gold, a typical safe-haven at times of distress could increase inflows and support fiscal accounts. By mid-March, gold prices reached US\$1,347, an 11.8 percent increase from end-2013.

Source: Bank staff.

16. **Better human, physical and institutional assets will promote diversification and reduce vulnerability over the medium term.** Excessive reliance on a few sectors and large informality exacerbate volatility and vulnerability to shocks. Gold accounts for 40 percent of

exports, remittances are 30 percent of GDP and the informal economy is estimated at 40 percent of GDP. The Kyrgyz Republic needs more and better institutional, physical and human assets to realize the potential of its economy, including in agriculture, trade and transit, natural resources while strengthening social cohesion. Stronger institutions, also supported by the DPO2, will address some of the main obstacles to doing business, including bureaucracy and corruption. Better physical infrastructure would relieve connectivity issues such as unreliable electricity, poor access to remote areas, and high costs of transportation. Education and health sector reforms will create a better-skilled labor force, a rapidly growing constraint to doing business.

17. More and better jobs are needed to reduce poverty and share prosperity and to enhance people's voice and participation, a critical ingredient of the post-2010 governance framework. Not enough quality jobs are created at present and a significant part of the population migrates out of the country. The unemployment rate was 8.4 percent in 2012, with close to a fifth of the population employed in agriculture. Demographics are making the challenge more acute as the working age population is expected to increase by 30 percent between 2010 and 2030. A recent World Bank report concluded that more and better jobs require: i) sustained market reform; ii) harnessing entrepreneurship; iii) better skills; iv) a functioning labor market and affordable labor taxes; and v) mobility.⁴ The Kyrgyz population is entrepreneurial and mobile and there are few labor market disincentives and barriers. However, critical elements of the business environment remain difficult, labor taxes are high, and skills are inadequate.

18. Improving efficiency of government spending will be critical for growth, inclusion, and stability. The medium-term fiscal framework envisages a reduction in the deficit to below 3 percent of GDP by 2016, a task made more difficult by the 3–6 percent reduction in revenues (or about 1.7 percent of GDP a year) due to the mid-2014 closure of the Manas Transit Center. The authorities, supported by the IMF, are preparing a tax strategy that will outline tax policy and administration reforms that can support revenues with gains expected on income taxes, excises and Value Added Tax (VAT). However, most of the adjustment would need to come from expenditures. On the other hand, public investment needs to remain high to address infrastructure bottlenecks and social inclusion policies need to be promoted to strengthen cohesion. This will require improved efficiency of public expenditures, including through reforms supported by the DPO2. The new framework for public procurement is expected to reduce the significant amount of resources currently spent on purchases of goods and services, while a stronger internal audit function improves the control systems in the public sector. Beyond the DPO2, the authorities expect savings from improved targeting of social protection; already the authorities limited the allocations to non-targeted transfers and are developing a registry of beneficiaries that will improve administration, cut costs of the system and allow for streamlining of the number of social programs. In addition, implementation of the 2013 civil service pay strategy introduces a harmonized approach to wage bill management, stronger controls over hiring and a broader HR reform. While a number of measures will be difficult and are yet to be designed, the favorable medium-term growth prospects provided an opportunity to

⁴ Arias, Omar S., Carolina Sánchez-Páramo, María E. Dávalos, Indhira Santos, Erwin R. Tiongson, Carola Grun, Natasha de Andrade Falcão, Gady Saiovicci, and Cesar A. Cancho. 2014. Back to Work: Growing with Jobs in Europe and Central Asia. Washington, DC: World Bank. (doi:10.1596/978-0-8213-9910-1) License: Creative Commons Attribution CC BY 3.0.

implement the necessary reforms. Fiscal financing needs are expected to decline, as the deficit is reduced with financing from the World Bank, IMF, ADB and bilateral infrastructure loans expected to cover the needs (Table 3).

Table 3: Financing Needs and Sources

(In percent of GDP)

Fiscal Financing					External Financing				
	2013	2014	2015	2016		2013	2014	2015	2016
	Prel.	Proj.	Proj.	Proj.		Prel.	Proj.	Proj.	Proj.
Requirements	4.2	4.9	4.2	3.7	Requirements	23.4	23.2	22.2	21.4
Deficit	3.5	4.3	3.5	2.9	CAD	13.5	15.7	14.5	12.6
Amortization	0.7	0.6	0.7	0.8	Amortization*	7.5	5.4	5.9	6.8
					Reserves	2.4	2.1	1.7	2.0
Sources	4.2	4.9	4.2	3.7	Sources	23.4	23.2	22.2	21.4
Loans	5.0	5.1	4.4	3.4	FDI	10.4	12.2	11.4	13.0
PIP	3.7	4.1	4.0	3.0	Disbursements	10.3	9.6	9.9	9.6
Budget sup.	1.3	1.0	0.5	0.4	Capital grants*	1.3	1.3	1.4	0.9
Privatization	0.0	0.0	0.0	0.0	Other flows**	1.3	0.0	-0.5	-2.1
Domestic*	-0.9	-0.2	-0.2	0.3					

Source: Bank staff calculations based on data from MoF, NSC and IMF.

*/ negative value refers to deposits increase.

Source: Bank staff calculations based on data from MoF, NSC and IMF.

*/ excludes debt forgiveness in 2012 and 2013.

**/ includes errors and omissions.

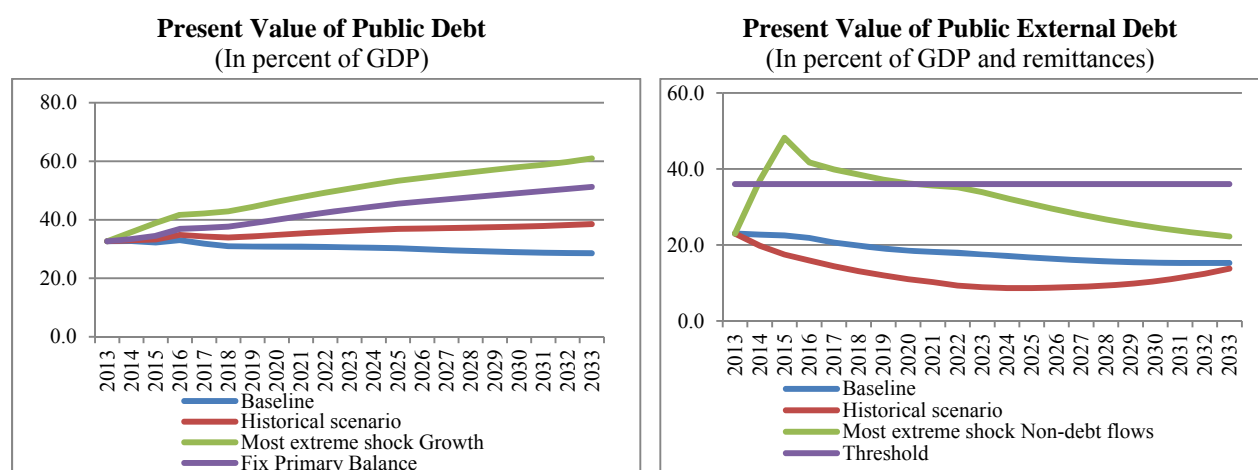
19. **Monetary policy will need to be responsive to price and exchange rate pressures while financial sector policies should support growth.** Over the medium term, inflation is expected to remain in the 5-7 percent range, as the NBKR remains committed to price stability, though global price shocks or changes in the exchange rate could increase inflation. Continuing with the flexible exchange rate policy with interventions only to smooth out large fluctuations will contribute to the economy's competitiveness while further de-dollarization and improvements in the transmission mechanism for monetary policy will enable the NBKR to be more effective. Better supervision and regulation of the financial sector will help increase the availability of credit while keeping risks manageable.

20. **The current account deficit will remain high but will be fully financed with increased private investment and concessional borrowing.** Exports are expected to grow as gold output remains strong and as reforms support expansion of non-gold exports. According to the IMF, the real exchange rate was in line with the economy's fundamentals prior to the recent devaluations of currencies of key trading partners. The adjustment in the Kyrgyz som since early 2014 should help with price competitiveness. Strong FDI and public borrowing to upgrade the capital stock will keep imports and the current account deficit high over the next few years. Under a reform scenario and given the proximity to China, access to markets in Russia and Kazakhstan, and low labor costs, the Kyrgyz Republic is well positioned to attract increasing inflows of FDI, including from China. Chinese investments in the energy sector (oil-refinery and a pipeline worth US\$3 billion – 40 percent of 2013 GDP) were recently agreed and are expected to significantly increase capital inflows into the Kyrgyz Republic. The country should also be able to attract investment to develop its natural resources, including in mining and hydro-power. Trade credits and loans will cover the remaining financing gap (Table 3).

21. **The risks to this outlook are significant, both external and domestic.** Remittances have so far been resilient to the slowdown in Russia (source of around 95 percent of private transfers), but a protracted slowdown and larger tensions with Ukraine could lower remittances and exports. Gold prices add another layer of uncertainty. In the absence of global shocks, prices are projected to moderate over the medium-term and this will affect the external and fiscal accounts. The situation in the region remains fragile and could become more so after the planned pull-out of NATO troops from Afghanistan in 2014. Domestically, the still evolving political institutions may limit the ability of the government to implement reforms. A repeat in the global food price increases would pose a serious threat to poverty reduction, given the large share of food in the consumption basket.⁵ The country has limited instruments to effectively respond to these risks in case they materialize.

22. **The 2013 debt sustainability analysis (DSA) update confirmed that the country is at a moderate risk of debt distress, but with strong volatility in growth and remittances.** Under the baseline scenario, public debt is on a downward trajectory with the net present value of debt projected to decline from 33 percent of GDP in 2013 to 31 percent in 2018. Still, failure to consolidate fiscal accounts or a lower GDP growth (i.e. keeping the deficit around the average for the last five year period) will test fiscal sustainability. External debt burden indicators are below indicative thresholds for countries with large inflows of remittances such as the Kyrgyz Republic under the baseline, with the present value of external debt projected to decline from 59 percent of GDP in 2013 to around 50 percent in 2018. External debt is vulnerable to extreme shocks such as significantly lower non-debt flows (FDI or transfers). Steady growth of remittances and maintaining a prudent borrowing strategy are essential to mitigate risks and to keep the debt outlook sustainable.

Figure 2: DSA Summary Chart



Source: Bank-Fund 2013 DSA update.

23. **The macroeconomic policy framework is considered adequate for this operation.** The set of macroeconomic policies strike an appropriate balance between the need to safeguard economic activity and the need to gradually re-build buffers and strengthen prospects for fiscal

⁵ The population is extremely dependent upon purchases of staple food items. Food counts for up to 60 percent of household expenditure, and wheat products (bread, flour, etc.) are a large part of Kyrgyz households' caloric intake.

and external sustainability. The Bank will closely monitor the situation and coordinate with the IMF and other partners to ensure that the environment remains adequate for such an operation.

C. IMF RELATIONS

24. **Bank and Fund staff collaborate closely to support the government in its reform agenda.** This close coordination has resulted in largely shared views of the economic situation and the priorities for the country. The IMF has broadly endorsed the country's macroeconomic policies and supported these by an Extended Credit Facility (ECF). The ECF was approved in June 2011 to support economic recovery in the short term and a stronger, sustained and inclusive growth in the medium term by promoting gradual fiscal consolidation and strengthening of the financial sector resilience. The fifth review of the ECF was completed in December 2013 and noted that economic recovery is underway with robust growth in a low inflation environment. As of end-March 2014 the program remains on track. The engagement of the IMF beyond the completion of the ECF in mid-2014 will be discussed during the next visit of the IMF team, with fiscal policy and the financial sector likely to remain the main focus of engagement.

3. THE GOVERNMENT'S PROGRAM

25. **The Kyrgyz authorities aim to establish a democratic state with a stable political system, dynamic economic growth and growing incomes of its citizens in the next five-year period.** The 2013-17 National Sustainable Development Strategy (NSDS) provides the strategic framework for the achievement of these objectives. The NSDS puts emphasis on anti-corruption activities and judicial reform that would establish the rule of law, as well as reforms in education, health care, social policies and gender that will enhance social prosperity (see Box 2). The authorities expect that poverty could fall to 25 percent by 2017, from 38 percent in 2012, if the NSDS is effectively implemented, reflecting strong job and real wage growth.

26. **A number of sector strategies, which are increasingly being aligned with the NSDS, guide the efforts on specific areas.** Reforms in anti-corruption, the judiciary and energy are being more clearly articulated in specific action plans adopted by the authorities. Encouragingly, there is greater harmonization between these documents, though this is yet to be systematically ensured. For example, the draft Public Sector Reform Roadmap (PSRR), prepared with technical assistance from the World Bank, aims to create a unified platform for support of public sector reforms from development partners.⁶

⁶ In the PSRR project, the Bank provided advice to the GoKR on prioritization of public sector reforms for 2014-16 in the following areas of public sector reform: anti-corruption reform; legal and judicial reform (as affected by the executive branch); public administration reform; civil service reform; public financial management reform; and reforms of strategic sectors with a large proportion of government ownership (extractive industries and energy).

Box 2: The Kyrgyz Republic NSDS 2013-17 – Main Areas of Reform

To establish a state governed by the rule of law, with strong national unity and social cohesion among various social groups and ethnicities, the NSDS envisages reforms aimed at:

- ensuring stability of the Constitution and laws and their effective enforcement;
- ensuring free democratic elections and freedom of speech;
- combating corruption and increasing effectiveness and transparency and cooperation with the civil society;
- strengthening the legal system and reforming the judiciary; and
- promoting equitable economic development of regions.

The NSDS also sets the strategic direction for sustainable development, sovereignty and national security through appropriate economic policies, building up of human capital and strengthening environment protection and crisis preparedness. It envisages robust economic development through:

- prudent macroeconomic policies;
- improvements in the business environment (reduction in informal economy, tax and investment policy, legal and regulatory framework for SME developments, managing of public resources etc.);
- financial sector development; and
development of strategic industries (agriculture, power, mining, transport and tourism).

Reforms in education and in health care, combined with increasing effectiveness of social protection and pensions are expected to improve the human capital and facilitate the achievement of the social objectives of the NSDS.

Source: National Sustainable Development for the Kyrgyz Republic 2013 – 17.

4. THE PROPOSED OPERATION

A. LINK TO GOVERNMENT PROGRAM AND OPERATION DESCRIPTION

27. **The proposed DPO2 program has two pillars that are closely linked to the objectives of the NSDS and sector strategies: (i) improving public sector governance and ii) enhancing the business environment.** The program includes measures to improve transparency and accountability in managing public resources and to promote efficient business regulation, stronger property rights and a resilient financial sector. The reforms will lay the foundation for stronger growth, and reduced poverty and shared prosperity. The DPO2 program is largely the program envisaged at time of DPO1 preparation with some adjustment of prior actions in the energy and financial sectors due to timing constraints and priorities of the authorities.

28. **The design and content of this operation have benefitted from Bank-wide experience with other DPOs as well as the experience of the first operation in the series.** Reflecting the findings of the recent retrospective on development policy lending and from the World Bank's World Development Report 2011 on Conflict, Security and Development, the proposed operation embeds the following general principles: i) avoid pushing for unrealistic and ambitious reforms that would not be politically feasible in the current context; ii) concentrate on priority areas that have full ownership and thus a greater chance of success; iii) deepen reforms that were initiated in previous operations; and iv) complement the DPO with other instruments for Bank support, including technical assistance (TA), economic and sector work (ESW), and investment operations.⁷ Reflecting the lessons learned from the earlier operation in the series, the DPO2

⁷ The Kyrgyz Republic is not officially classified as a Fragile or Conflict-Affected State; however, it bears some characteristics of such countries.

preparations process ensured more frequent interactions with the counterparts and upstream collaboration in formulating the program.

29. **The DPO instrument brings significant benefits through the engagement process, ahead of the expected enactment and implementation of legislation, which may extend to beyond the DPO program.** It establishes the structure for policy dialogue in a number of sectors, allowing for progress in areas not under the jurisdiction of the legislative branch. In addition, the DPO-engagement provides a framework for coordination of the government's activities and strengthening capacity in government agencies, including in better articulating their proposals to the parliament. During the drafting of the deposit insurance bill, one of the prior actions of DPO2 and supported by a Financial Sector Reform and Strengthening Initiative (FIRST) technical assistance grant, the Bank provided advice on the Agency's corporate governance structures, institutional arrangements and fund management strategy. Similarly, the Bank's involvement in the context of the DPO program in developing the framework for public procurement has helped build capacity in the future regulator and advance the dialogue on e-procurement. Still, sustainability of reforms would require the passage of legislation as well as longer term engagement and commitment. Ability to process follow-up budget support operations would also depend on progress in enacting the legal changes by the parliament. The shared vision on the strategic priorities of the country is; however, providing assurances that the direction for reforms would be maintained and that prior actions requiring parliamentary approval will eventually be enacted in a satisfactory manner.

30. **The post-2010 arrangements in the Kyrgyz Republic are increasing implementation risks for DPOs, while providing opportunity for broader support of reform.** With decision-making authority in a number of areas being transferred to an increasingly more active parliament, the government's ability to push through policies has diminished and the time to adopt legislation has increased. Specific to the proposed DPO2, this is increasing the implementation risk for actions requiring parliamentary approval and the risk that the expected results will not be achieved within the projected timeframe.

31. **Due to longer than expected preparation times required for certain legislation, a few changes have been made to the program since the preparation of DPO1.** The trigger on the draft insolvency law was removed from the program as it requires a longer term engagement and technical assistance. Similarly the trigger on the electricity law was replaced with a new prior action on publication of performance data by energy companies. Another change that was introduced to the policy matrix was the replacement of the trigger related to the Prompt Remedial Action Framework (PRAF) with the action on credit registry, upon request by NBKR. NBKR stated that more time would be needed to adopt a formal framework in some areas including crisis preparedness and management. Finally, the trigger on the resolution regulating the issuance of sovereign guarantees was dropped since revisions to the draft Budget Code in the Parliament eliminated the issuance of guarantees.

B. PRIOR ACTIONS, RESULTS AND ANALYTICAL UNDERPINNINGS

PILLAR 1: IMPROVING PUBLIC SECTOR GOVERNANCE

32. **This pillar supports increased accountability and transparency in the use of public resources through improved public sector governance structures.** More efficient use of public resources, both in the public administration and in the energy sectors, is expected to generate savings that will strengthen the sustainability of the fiscal accounts and allow re-allocation of spending to priority areas and improve quality of public services, which will help reduce poverty and promote shared prosperity. The DPO2 supports four key actions under this pillar: (i) implementing and monitoring the anticorruption plan; (ii) improving the functioning of the internal audit system; (iii) bringing public procurement in line with international good practice and (iv) increasing the transparency of the public companies in the energy sector.

Anti-corruption

33. **Acute governance failures and high perceptions of corruption were at the core of the 2010 turmoil.** In response, the governance structure in the country was revamped and the authorities embarked upon a process of building policies and institutions for implementation of the new governing structures. In 2012, the authorities adopted an Anti-Corruption action plan (supported by DPO1) and the proposed DPO2 is supporting the implementation of this plan. More specifically, the DPO2 supports verification of asset declarations of civil servants in political functions which is being undertaken for the first time in the Kyrgyz Republic and has the potential to significantly strengthen the role of asset declarations as a tool in the fight against corruption. As part of this action, the State Personnel Service (SPS) coordinated the work of an interagency commission with representatives of 11 agencies and identified a number of cases of wrongful declarations. The authorities are also strengthening the monitoring and evaluation framework for the implementation of the government's action plan and have adopted a government resolution that mandates the regular reporting by agencies on their implementation progress. The authorities are revising the framework for conflict of interest that aims at clarifying the definition of conflict of interest for civil servants and bringing legislation in line with international standards. Future development lending operations may support these reform efforts.

Prior action 1: State Personnel Service, has completed the first round of verification of asset declarations of civil servants in political functions and submitted the summary results to the government.

Internal Audit

34. **The proposed DPO2 supports reforms in internal audit and internal financial control that can, over time, make an important contribution to improved governance.** The 2009 Law on Internal Audit set the framework for the development of this important function. Still, apart from the establishment of internal audit units in public entities, there has been limited progress in implementation and institutional capacity remains weak across the public sector. Recent activities are giving a renewed impetus to this area. The statute of the internal audit unit in the Ministry of Finance (MoF) was upgraded to a department under the Minister providing for a stronger institutional setting for advancing the internal audit reform. The law on internal audit is currently being revised, in an effort to align it with international good practice. As part of the

DPO2 supported program, a government resolution in September 2013 established an independent Internal Audit Council as an advisory body that would oversee the development of internal audit and propose improvements in the internal audit framework. In addition, in December 2013, the government adopted the regulations on the system for Public Financial Management and Control and by-law of a Code of Ethics for internal auditors. These regulations will bring the legal framework for internal audit in line with good international practice and over time should result in stronger systems to evaluate controls and processes in the public sector.

***Prior action 2:** The Government, through Resolution No. 498, dated September 9, 2013, approved a Regulation on Internal Audit Council establishing the said council; through Resolution No. 722 dated December 31, 2013, has adopted a regulation on Financial Management and Control in Budget Organizations; and through Resolution No. 721, dated December 31, 2013, adopted ethical standards for internal auditors in public agencies of the Kyrgyz Republic.*

Public Procurement

35. Bringing the Kyrgyz public procurement framework in line with good international practice will be a major stride towards enhancing transparency and generating fiscal savings. The legal framework for public procurement has come a long way since the introduction of the first law on public procurement in 1997. Still, a number of weaknesses continue to exist and a Country Procurement Status Review by the World Bank in August 2012 found that the legal framework continues to have features that are not compliant with international standards. In response, with support from the World Bank, the government adopted a public procurement development strategy (supported by DPO1) and in February 2014 submitted to the Parliament a new draft law on public procurement that brings the Kyrgyz legislation in line with international good practice. The authorities also adopted in February 2014, a regulation that upgrades the institutional framework of the public procurement regulator within the MoF. At the same time, the authorities have drafted the implementing legislation for the new Law on Public Procurement (to be effective following the enactment of the Law) which envisages establishment of an independent complaint review commission. The authorities have also committed to continue developing a reporting system to monitor the key indicators of the procurement process and its outcomes. These measures are expected to enhance transparency through proper reporting on the use of public funds and the clarification of roles and responsibilities of regulatory and oversight bodies; reduce corruption in public procurement; and improve public procurement performance and efficiency.

***Prior action 3:** The Government, through Resolution No. 69, dated February 3, 2014, “On draft Public Procurement Law of the Kyrgyz Republic,” has approved and submitted to Parliament a draft of said law, and through the Resolution No. 68, dated February 3, 2014 “On Public Procurement Department under the Ministry of Finance of the Kyrgyz Republic”, has strengthened the role of the public procurement regulatory body within the Recipient’s Ministry of Finance.*

Energy Sector Reform

36. Implementation of the Power Sector Development Strategy can transform the sector into a source of growth and investment. The sector is endowed with a significant hydro-

generation potential; however, inadequate governance arrangements and regulatory environment have made it a large contingent liability to the budget. The regulator is not independent and tariffs are below recovery levels resulting in severe underinvestment, high losses and non-transparent contractual arrangements. The government's 2012-15 Power Sector Development Strategy (supported under DPO1) outlined an ambitious agenda to address these issues, including: (i) improvements in efficiency and transparency of the sector; (ii) adoption of a medium-term tariff policy accompanied by an adequate social protection scheme; and (iii) increased investments in energy infrastructure. The government is amending the legal framework (Law on Energy, Law on Electric Energy and Law on Natural and Allowed Monopolies) to provide clear delineation of powers and responsibilities and to create a settlement center for transparent accounting and monitoring of electricity and financial flows. In addition, the authorities are increasing the transparency of the power sector companies (DPO2 prior action) by requiring them to make available to the public extensive information on their performance. This will help address some of the main causes of the populations' low trust in power sector entities.

37. In addition to improved governance, gradually adjusting tariffs to cost-recovery levels can improve the financial position of the sector. The government is preparing a four-year Medium-Term Tariff Policy (MTTP) with the objective of ensuring progressive cost-recovery. The MTTP will be accompanied with a communication strategy, as well as targeted social protection program for the poor and vulnerable groups. While not a part of the proposed DPO2, the Bank remains committed to assisting the authorities in these processes by providing technical assistance in the design of the MTTP as well as the social program.

Prior action 4: The Ministry of Energy and Industry has issued the Order No. 174, dated October 10, 2013, which aims to increase the transparency of the energy sector by requiring Energy Companies to regularly publish on their respective websites the following information: (i) monthly balances of the special accounts of EPP and NEGK and transit accounts of Sevelelectro, Vostokelektro, Oshelectro, and Jalalabatelectro; (ii) quarterly operational and technical performance data of the Energy Companies; and (iii) annual financial statements together with audit reports.

PILLAR 2: ENHANCING THE BUSINESS ENVIRONMENT

38. Reform efforts in recent years are yet to translate into a business environment conducive for private investment, job creation and growth. Starting a business has been simplified and now takes 8 days (exceeding the expected result for this DPO-series of 10 days) and other reforms have been pushed through. However, implementation has not been consistent. Procedures remain complicated and involve a high number of interactions between government officials and entrepreneurs, and therefore entail corruption risk, with inspections being especially vulnerable. In addition, protection of property rights is not always guaranteed, including due to a poorly functioning judiciary and inadequate corporate governance arrangements. Finally, growth of the private sector is hampered by an underdeveloped financial sector, including due to low confidence and stability issues. Pillar 2 of the proposed DPO2 is addressing some of the bottlenecks to a more vibrant development of the private sector, including through: i) improved functioning of the judiciary; ii) facilitating risk-based inspections; iii) increased accountability of executive directors; iv) stronger deposit protection arrangements and v) enhanced ability of

NBKR to supervise the financial sector. Going forward, business environment reforms need to be supported by complementary reforms in education and skills and access to infrastructure, both areas in which the World Bank has extensive engagement with the authorities.

Judicial Reform

39. **Implementation of the 2012 Judicial Reform Action Plan will, over time, improve efficiency of the sector.** While currently the judicial system is underfunded, perceived as corrupt and an obstacle to doing business, recent steps are encouraging.⁸ The parliament is revising the process of selection of judges in response to concerns regarding its objectivity, a number of courts have begun publishing their decisions on their web-sites and the wages of judicial staff were increased. The authorities are committed to strengthening the financial independence of the court system envisaged in the Judicial Reform Action Plan (supported by the earlier operation, DPO1). Subsequently, on March 19, 2014, the government adopted the program on development of the judicial system for 2014-2017, that essentially introduces an independent judicial budget and envisages a gradual increase in the budget allocation for the depleted court infrastructure. Implementation of these measures is expected to improve the functioning of the system and enable it to regain the confidence of individuals and businesses.

Prior action 5: The Government, through Resolution No. 174 “On Draft State Target Program on Development of the Judicial System of the Kyrgyz Republic for 2014-2017”, dated March 19, 2014, has submitted to Parliament the draft of said program which aims to increase the financial independence of the judicial sector.

Corporate Governance

40. **Strengthening corporate governance can improve property rights and stimulate private sector growth.** The 2013-2014 World Economic Forum Global Competitiveness Report ranks the Kyrgyz Republic 128th on efficacy of corporate boards and 121st on protection of minority shareholder’s interests (out of 148 countries). Amendments to the Law on Joint Stock Companies supported by the DPO2 outline: (a) how directors should carry out their duties; (b) what their obligations are in cases of related-party transactions; and (c) what the consequences of such transactions. These amendments are expected to increase the transparency in the management of joint stock companies, facilitate easier access to capital and financial markets and strengthen the rights of shareholders. The amendments were submitted to the Parliament through Government Resolution No.610 dated November 11, 2013.

Prior action 6: The Government, through Resolution No.610 dated November 11, 2013 “On Draft Law of the Kyrgyz Republic On Introducing Amendments to the Law on Joint Stock Companies of the Kyrgyz Republic,” has submitted to Parliament a draft of said law that aims to strengthen the responsibilities of members of management bodies.

⁸ 89 percent of respondents to the 2013 Global Corruption Barometer felt that the judiciary was corrupt or extremely corrupt. Available at: <http://www.transparency.org/gcb2013/country//?country=kyrgyzstan>.

Business Inspections

41. **Enterprise surveys have identified the inspections process as one of the most significant burden for businesses.** System of inspections has not been systematic and has been nontransparent, creating room for rent seeking. Ongoing measures are overhauling the system. Amendments to the legislative framework in 2011 and 2012 reduced the number of inspections and allowed for the introduction of risk based inspections (supported by DPO1) with risk criteria serving as a basis for assessing and differentiating risk level of businesses and determining the frequency of inspections by controlling agencies. The launch of the risk-based inspection coordination module (KontrPro3) in January 2014 supported by DPO2 is facilitating effective implementation of the risk-based approach to inspections. Inspections plans of participating inspections services are now risk-based and are monitored and coordinated by the Ministry of Economy using a unified database of entities including their risk profiles. The system initially covers six inspectorates in the Bishkek region; however, the system will be rolled-out to the remaining six inspectorates and their regional offices once technical capacity constraints are addressed. The use of KontrPro3 will allow improved efficiency in coordination of inspections with a reduction in required staff time and electronic control of duplications. Complementing this reform, the authorities, with IFC support, are planning to launch a public campaign for KontrPro3 and are also revising the checklists setting out the requirements for businesses during inspections. The checklists will streamline and increase the transparency of the inspection process and reduce the potential for rent-seeking. So far, checklists have been revised for two inspection services.

Prior action 7: The Government has operationalized the single automated database for inspections of businesses (KontrPro3) in the Ministry of Economy and six inspectorates in the City of Bishkek that aims to reduce the burden of inspections on businesses.

Credit Registry

42. **The political upheavals of 2010 led to significant financial sector instability from which the sector is yet to fully recover.** The crisis caused a large deposit outflow, deterioration in the quality of the portfolio and substantial losses for the sector. The NBKR responded by taking over seven banks (accounting for 45 percent of the system's assets) under temporary administration. While the sector has returned to growth, access to finance remains a constraint to doing business and the NBKR still remains involved in legal processes of three commercial banks.⁹ This highlights issues in the bank resolution legal framework which are being addressed in the new Banking Code currently reviewed by the parliament.¹⁰ The crisis also highlighted weaknesses in the supervisory and regulatory framework for the banking sector, including in onsite and offsite supervision, stress testing, contingency planning and crisis management which may lead to understatement of NPLs or risks. At the same time, the regulatory framework in a number of areas (Basel II, consolidated and risk-based supervision etc.) is yet to be established.

43. **The establishment of a credit registry will enhance the ability of the NBKR to effectively supervise the financial sector.** The NBKR has lacked timely and exhaustive

⁹ One of the banks is still undergoing liquidation while three other banks remain under conservatorships as the NBKR cannot take action to resolve these banks because of pending court cases from their shareholder.

¹⁰ The development of the Banking Code is supported by the IMF program and is not included in this DPO. The World Bank and IMF teams are closely coordinating their assistance to NBKR on legal and other reforms.

information on the credit exposure of banks and regulated financial institutions, which has limited its ability to effectively supervise the sector, identify potential problems, manage risks and take remedial measures. In June, 2013, the NBKR Board revised the regulation on periodic reporting of commercial banks to the NBKR and in August 2013 it amended the regulation on methodological guidelines for periodic reporting of banks and mandated banks to start delivering on a monthly basis to the NBKR granular data on loans extended beginning from December 2013. At the same time, the NBKR developed a credit registry (CR) that started functioning in January 2014. Despite the existence of some errors in the database and the need to enhance the software supporting the database in the medium term, the system is functional and reported to be a useful tool for banking supervision in the Kyrgyz Republic. The system holds information on all banks except one, which is currently solving some technological problems. The new CR helps the NBKR: a) to respond rapidly in case of detecting over-crediting and/or parallel loans within the database b) to conduct off-site analysis of the commercial bank's loan portfolios; c) to receive combined loan-related information on various indicators by borrowers/loans and on the banking system as a whole; d) to evaluate credit development and concentration of loans and e) to reduce the time spent for conducting reviews of the commercial banks' loan portfolios.

***Prior action 8:** The National Bank of the Kyrgyz Republic (NBKR), through Resolution No. 20/7 of the Board of the NBKR “On Amending the Regulation on Periodic Bank Reporting”, dated June 26, 2013, and through Resolution No. 27/1 of the Supervision Committee of NBKR “On Amending the Methodological Guidelines for Periodic Bank Reporting”, dated August 7, 2013 has strengthened bank reporting to support the functions of the NBKR's newly established credit registry.*

Deposit Protection

44. **The proposed DPO2 supports increasing protection of depositors to enhance the confidence in the system.** The World Bank's Emergency Recovery Support Operation (ERSO), approved in 2011, supported the independence of the Deposit Protection Agency (DPA) with an appropriate supervisory board providing oversight, thus paving the way to improve governance in the deposit protection system through clarified roles, responsibilities, and accountability of DPA, the NBKR, and the government. Building on this, the authorities are introducing improvements that increase protection of depositors and improve governance and procedures in the DPA, including by clarifying: i) the powers and qualifications of its management; ii) the requirements to “coordinate” with other entities and iii) the definition of an insurance event and timing of paying depositors.

***Prior action 9:** The Government, through Resolution No. 528 “On Draft Law on Introducing Amendments to the Law on Protection of Bank Deposits”, dated September 27, 2013, has approved and submitted to Parliament a draft of said law that aims to strengthen governance, coordination and operations of the deposit protection scheme.*

Table 4: DPO Prior Actions and Analytical Underpinnings

Prior Actions	Analytical Underpinnings
Operation Pillar 1: Improving Public Sector Governance	
State Personnel Service has completed the first round of verification of asset declarations of civil servants in political functions and submitted the summary results to the government.	Public Sector Reform Roadmap (2013), Capacity Building for Economic Management TA (ongoing).
The Government, through Resolution No. 498, dated September 9, 2013, approved a Regulation on Internal Audit Council establishing the said council; through Resolution No. 722 dated December 31, 2013, has adopted a regulation on Financial Management and Control in Budget Organizations; and through Resolution No. 721, dated December 31, 2013, adopted ethical standards for internal auditors in public agencies of the Kyrgyz Republic.	Multi-donor trust fund on PFM (2009). Public Expenditure and Financial Accountability (PEFA, 2009).
The Government, through Resolution No. 69, dated February 3, 2014, “On draft Public Procurement Law of the Kyrgyz Republic,” has approved and submitted to Parliament a draft of said law, and through the Resolution No. 68, dated February 3, 2014 “On Public Procurement Department under the Ministry of Finance of the Kyrgyz Republic”, has strengthened the role of the public procurement regulatory body within the Recipient’s Ministry of Finance.	Multi-donor trust fund on PFM (2009). Public Expenditure and Financial Accountability (PEFA, 2009). Country Procurement Status Review (2012).
The Ministry of Energy and Industry has issued the Order No. 174, dated October 10, 2013, which aims to increase the transparency of the energy sector by requiring Energy Companies to regularly publish on their respective websites the following information: (i) monthly balances of the special accounts of EPP and NEGK and transit accounts of Severelectro, Vostokelektro, Oshelectro, and Jalalabatelectro; (ii) quarterly operational and technical performance data of the Energy Companies; and (iii) annual financial statements together with audit reports.	Power Sector Review (2014).
Operation Pillar 2: Enhancing the Business Environment	
The Government, through the Resolution No. 174 “On Draft State Target Program on Development of the Judicial System of the Kyrgyz Republic for 2014-2017”, dated March 19, 2014, has submitted to Parliament the draft of said program which aims to increase the financial independence of the judicial sector.	Judicial Reform Diagnostic (2010).
The Government, through Resolution No.610 dated November 11, 2013 “On Draft Law of the Kyrgyz Republic On Introducing Amendments to the Law on Joint Stock Companies of the Kyrgyz Republic,” has submitted to Parliament a draft of said law that aims to strengthen the responsibilities of members of management bodies.	PSD Dialogue (2012), Background Paper for the PSD Strategy (2013).
The Government has operationalized the single automated database for inspections of businesses (KontrPro3) in the Ministry of Economy and six inspectorates in the City of Bishkek that aims to reduce the burden of inspections on businesses.	IFC Advisory Services on Business Enabling Environment.
The National Bank of the Kyrgyz Republic (NBKR), through Resolution No. 20/7 of the Board of the NBKR “On Amending the Regulation on Periodic Bank Reporting”, dated June 26, 2013, and through Resolution No. 27/1 of the Supervision Committee of NBKR “On Amending the Methodological Guidelines for Periodic Bank Reporting”, dated August 7, 2013 has strengthened bank reporting to support the functions of the NBKR’s newly established credit registry.	Financial Sector Monitoring (2010, 2011). FSAP (ongoing).
The Government, through Resolution No. 528 “On Draft Law on Introducing Amendments to the Law on Protection of Bank Deposits”, dated September 27, 2013, has approved and submitted to Parliament a draft of said law that aims to strengthen governance, coordination and operations of the deposit protection scheme.	ROSC (2010).

C. LINKS TO CPS AND OTHER BANK OPERATIONS

45. **The DPO program is structured around the main pillars of the CPS.** The DPO series supports the government in implementing a medium-term multi-sector reform agenda to improve management of public resources and to improve the business environment. These areas were central both in the FY12-13 ISN as well as the FY13-17 CPS and its main objective to improve governance, focusing on: i) public administration and service delivery; ii) business environment and iii) management of natural resources and infrastructure.

46. **The reforms supported under several other projects under implementation are complementing DPO2.** The *Governance Technical Assistance Project* aims to strengthen the capacity of the government in budget formulation and budget execution, with critical policy dialogue support provided by the DPO series. Internal audit reforms supported by the proposed DPO2 are linked to the *Capacity Building for Public Financial Management* project and *Capacity Building for Public Sector Internal Audit* (not yet effective). Also, the introduction of risk-based approach to inspections has been the focus of assistance from the International Financial Corporation (IFC). In addition to the existing portfolio, future activities will also allow the Bank to remain engaged. The *Financial Sector Development Project* and IFC projects on supporting the development of credit bureaus and microfinance institutions will continue the dialogue on financial sector issues. The planned *FY15-17 DPO series* will continue to focus on governance, advancing further the dialogue on anti-corruption and judiciary.

D. CONSULTATIONS, COLLABORATION WITH DEVELOPMENT PARTNERS

Consultations

47. **In a sign of increasing participatory processes, the NSDS benefited from extensive input from various stakeholders.** The strategy document was developed with participants from a broad political spectrum, as well as from the development partners and the civil society. This appears to be part of a broader change in the country aimed at achieving a more inclusive, open and representative government. While these are early beginnings, at present, any new legislation, regulation, or by-law, or any amendments to legislation are shared with the public for discussion via government or ministry websites. The government also holds round tables with NGOs and civil society. Business legislation and regulations are discussed with the business community and business associations. Public Supervisory Councils established for all ministries and most government entities to introduce public oversight over government policies and activities also include representatives of the civil society. The authorities shared the draft 2014 Republican budget for public discussion in advance of its adoption by the government. More specifically to the DPO series, most of the strategic documents supported under DPO1 (anti-corruption, judiciary, energy) benefited from extensive involvement of various stakeholders. In addition, the draft budget code was discussed at a public hearing organized by the Parliament, while the Ministry of Finance also allowed for stakeholder involvement in the drafting of the legislation on public procurement.

Collaboration with other Development Partners

48. **The Bank collaborated closely with other donors on the design of the DPO2.** The Department for International Development (DfID), the European Commission (EC) and the Swiss Cooperation are supporting the multi-donor trust fund which is helping advance the reform agenda on PFM and informing the DPO2 program. The Bank, jointly with the ADB and EBRD, is supporting the reform of the public procurement process. A donor working group on energy, consisting of the ADB, the Bank, Japan International Cooperation Agency (JICA), Germany Development Bank (KfW), and the United States Agency for International Development USAID is active. The Bank works closely with the European Union (EU), UNDP and USAID in the areas of governance and judicial reforms. The team also maintained frequent dialogue with the IMF as well as the Eurasian Development Bank (EaDB).

5. OTHER DESIGN AND APPRAISAL ISSUES

A. POVERTY AND SOCIAL IMPACT

49. **The areas of policy reforms supported under the DPO2 appear well aligned to areas of concern for the Kyrgyz population.** The consultations with the civil society undertaken as part of the preparation of the FY13-17 CPS identified that public sector governance and reform is a top development priority for 40 percent of respondents, with business climate issues, such as inefficient financial sector, corrupt business registrations and inspections, also featuring prominently. In the latest round of the World Bank's enterprise survey (2013) respondents identify political instability and corruption as the top business environment constraints.¹¹ Also, according to an independent survey on life satisfaction, the Kyrgyz Republic's population was the least satisfied with the quality and efficiency of public service delivery among the countries in Central Asia and the South Caucasus. Citizens' feedback on the quality and responsiveness of the judicial, police and document requesting services were particularly low in the Kyrgyz Republic. Progress in judicial reforms supported by the proposed DPO2 has the potential to improve citizen satisfaction significantly. Finally, the fiscal policy supported under the program envisages gradual adjustment that protects social spending.

¹¹ <http://www.enterprisesurveys.org>.

Table 5: Satisfaction with Quality and Efficiency of Public Service Delivery

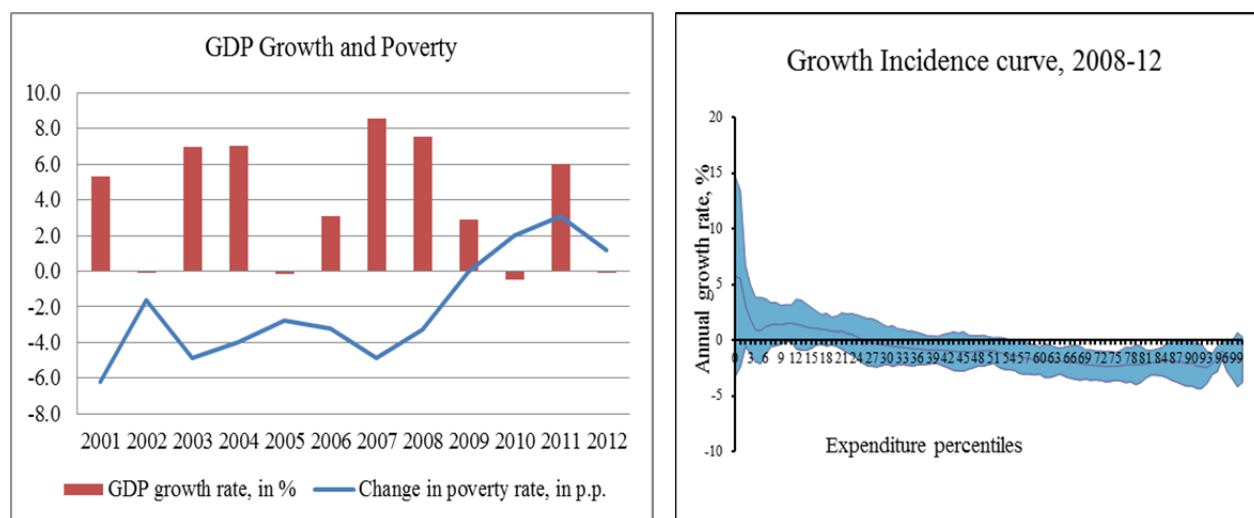
(In percent of the population)

	Health	Education	Police	Official Documents	Vocation Training	Social	Unemployment	Courts
Armenia	61	72	44	70	70	43	39	30
Georgia	75	82	75	92	83	28	0	36
Kazakhstan	54	69	40	50	62	50	43	27
Kyrgyz Republic	53	58	21	36	56	46	44	5
Tajikistan	57	62	36	62	51	42	38	29
Uzbekistan	64	74	43	54	65	48	14	29
Western Europe	80	76	55	80	78	67	52	40
ECA	61	73	45	67	70	51	45	41

Source: <http://www.ebrd.com/pages/research/publications/special/transitionII.shtml>.

50. **Improved governance and reduction in corruption are at the heart of the equity and inclusiveness agenda.** Corruption can adversely impact prosperity through at least two main channels. First, it stymies the improvement in performance of public sector institutions that are meant to serve the population whether through enhancing their living conditions or productivity. These institutions become less effective and serve those who are able to pay rather than treating the population equally. This not only raises the cost of services to the population without improvements in quality but also skews public expenditures away from those who are least likely—or able—to pay. This is of particular concern since about 20 percent of all poor in the Kyrgyz Republic are chronically poor due to lack of opportunities and low human capital. Second, when corruption becomes prevalent, it threatens the rule of law, property rights, and enforcement of contracts in a country. Thus, for a market economy to function properly, it has to be supported by appropriate institutions. An estimated 59 percent indicated that corruption was a major constraint and 30 percent of firms identified the court system as a major constraint (vs. 18 percent for all countries).

Figure 3: Economic Growth, Poverty and Growth Incidence



Source: World Bank staff calculations based on data from households' surveys.

51. **Economic growth in the Kyrgyz Republic has been pro-poor.** Episodes of growth have been correlated with poverty reduction and with growth in the consumption of the bottom 40 percent (Figure 3). Price shocks in 2009 and 2011-12, have weakened this relationship somewhat; however, during 2000 - 2012 the semi-elasticity of growth on poverty was a relatively high -0.7.¹² Also, on average, between 2006 and 2011, the real consumption of the bottom 40 percent increased by 5.8 percent, compared to a 2.5 percent increase in the consumption of total population. Thus, while the direct and immediate distributional impact of the actions supported by DPO2 is broadly neutral, in the medium term the measures aimed at strengthening governance and the business environment will improve the institutional basis for economic growth and also have positive repercussions for equity and shared prosperity. Moreover, the Kyrgyz Republic is not an exception to the general case when corruption practices disproportionately affect the most vulnerable groups who have the least ability to make informal payments and limited access to justice system. While it is difficult to measure the direct impact on poverty and shared prosperity of the reduction in corruption and improvement in efficiency of public finance institutions, weak governance and high levels of corruption were major stress factors underlying the political and social upheavals of 2005 and 2010, which may have negatively affected poverty rates. A more accountable public sector will reduce the risk of repeat of the 2005 and 2010 developments and the accompanying negative implications for growth, poverty reduction and shared prosperity.

B. ENVIRONMENTAL ASPECTS

52. **The specific policies supported by the DPO program will not have adverse effects on the environment and natural resources.** The operation supports reforms in management of public resources and improving the environment for doing business. None of the sectors included in the Operation are expected to have any direct significant links to the environment.

C. PFM, DISBURSEMENT AND AUDITING ASPECTS

Accounting, Recording, and Reporting

53. **Improvements in the systems of accounting, recording and reporting are necessary.** Although limited computerisation of treasury functions now enables partial reconciliation of information between regional treasuries, local transit banks, the central treasury and the National Bank, there is no comprehensive automation of accounting, recording, and reporting. Monthly and quarterly reconciliations between budgetary organisations' records and those of the central treasury take place, though the arrangements are cumbersome and probably do not resolve all data errors. A fully integrated system is being developed; though progress needs to accelerate. Quarterly reports are submitted to the president, the parliament and the prime minister. By mid-May of each year, the government submits report for the execution of the budget (cash-based) for the previous year to the parliament. It includes extensive information on revenues and expenditures; however, it does not include accounting policies and is not supported by commentary that would assist in the interpretation. The Republican government budget is

¹² This implies that a 1 percent growth in GDP per capita associated with reduction of the headcount poverty rate by 0.7 percentage points based on authors' calculations.

published on the MoF's web site (www.minfin.kg) and monthly execution tables are published on the web-site of the central treasury (www.kazna.kg) within a month.

54. **National accounting and reporting standards for the public sector are not fully developed yet.** While the 2012 amendments to the Law on Accounting mandated the adoption of IPSAS as accounting standards by all budget organizations, the legal and methodology framework as well as institutional mechanisms for transition to international standards are insufficient. The ongoing PFM Trust Fund supports a few IPSAS related activities, including development of the methodological base and a limited number of introductory trainings to familiarize public accountants.

Public Sector Auditing

55. **Public sector auditing is performed by the Chamber of Accounts (CoA), the equivalent of supreme audit institution.** The Chamber of Accounts audits the budget execution report prepared by the Ministry of Finance and submits its findings to the Parliament. No audit opinion is given; instead a report of errors and violations is submitted. The absence of a set of financial statements prepared in accordance with internationally recognised accounting standards (only a budget execution report is prepared) limits what the Chamber can do. Its audit of revenues and expenditure each year is not complete as only the consolidated statement of the MoF is audited annually; the policy in relation to other financial statements is not transparent. In addition to this, the Chamber undertakes audits of budget organisations, but does not separate reporting on its work on the financial statements from compliance and the efficient use of resources. Ongoing technical assistance (provided by the Bank, USAID and UNDP) should enable the CoA to develop capacity to conduct audits in accordance with international standards.

56. **Internal audit is weak; however, recent measures, also supported by the DPO operation, should gradually strengthen this function.** As noted earlier, following the 2009 adoption of the Law on Internal Audit, internal audit units were established in a number of agencies. However, institutional capacity for effective internal audit practices is limited, including in the Ministry of Finance, which is resulting in limited awareness of this function within the public sector. Recent measures, also supported by the proposed DPO2, could reinvigorate the agenda, but institutional change takes time.

Foreign Exchange Control Environment

57. **The last safeguards assessment update concluded that the NBKR has established important safeguards in financial reporting, external and internal audits.** The IMF completed the update on October 28, 2011 and, in addition, highlighted some areas for improvement in NBKR operations, including more effective reporting by the audit committee. The proposed new Banking Code is expected to strengthen institutional autonomy and give the NBKR sole responsibility for the governance of official foreign exchange reserves.

58. **The NBKR has been audited regularly by internationally recognized audit firms.** The 2012 audit of the consolidated financial statements was conducted by LLC KPMG Bishkek, who issued unmodified opinion on the financial statements. Previous audited financial statements have also been unmodified with no major issues raised in the management letter.

Public Procurement

59. **Recent changes to the legal and institutional framework for public procurement are bringing it in line with international good practices.** Recent improvements have included the option to publish procurement plans, bidding opportunities and contract awards on the MoF website, the collection of minutes of tender commission meetings by the MoF Public procurement department and the publication of an annual report on public procurement in 2011. In addition, with the changes supported by the DPO2, the legal framework will considerably improve with the creation a strong regulatory body as well as an independent redress mechanism. This should strengthen the adherence to procurement rules, a critical weakness in the existing system and reduce corruption in procurement.

Budget

60. **Enactment of the Budget Code (preparation and submission to Parliament of which was supported by DPO1) will significantly strengthen budget processes in the future.** The draft submitted to the Parliament in October 2012 strengthens controls over non-allocated funds in the treasury, advances the introduction of internal audit and medium-term budgeting, and provides more clarity to the overall budget cycle. While subsequently changes were made to this draft that moved it away from international good practice, the authorities have indicated that they will bring the draft in line with the earlier agreed version.

Disbursement and Audit

61. **The credit and grant proceeds would be made available to the Kyrgyz Republic upon the effectiveness of the Financing Agreement and submission of withdrawal applications for the credit and grant.** IDA will disburse the amount into a foreign currency deposit account that forms part of the country's official foreign exchange reserves and is opened for that purpose in NBKR. This account is available for budget financing and will be managed by and subject to the control of the MoF. The Recipient shall ensure that upon deposit of the proceeds of the credit and grant into the said account, and conversion into national currency, an equivalent amount will be credited in the Recipient's budget management system, in a manner acceptable to the IDA, that is: the current Treasury account will be credited with the Kyrgyz som equivalent at the official exchange rate within 30 days of disbursement. The foreign exchange proceeds of the proposed DPO2 will be sold by the NBKR or held in reserves, in accordance with the objectives of monetary policy. The authorities will report to the World Bank the amount deposited in the account and confirm its availability to finance budget expenditures within 30 days of receiving such funds. If, after depositing funds in this account, the proceeds of the credit and/or grant are used for ineligible purposes as defined in the Financing Agreement, the World Bank will require the authorities to refund the amount to the World Bank.

62. **The administration and accounting of the credit will be the responsibility of the MoF.** The MoF will be responsible for the credit and grant administration and for preparing the withdrawal application. The MoF, with the assistance of NBKR, will maintain records of all transactions under the credit in accordance with sound accounting practices.

63. **Auditing.** Considering the Bank's knowledge of the public finance management systems and the ongoing improvements of these systems, the positive assessment of the NBKR made by IMF, previous unmodified audit issued by the NBKR's auditor on the recent years' financial

statements, no additional fiduciary arrangements including audit will be required for the deposit account. Given that this is a high risk fiduciary operation, the Bank reserves the right to request an audit of the deposit account.

Overall Assessment

64. **Though the overall fiduciary environment is weak, the existing arrangements are adequate for the purposes of the DPO while the operation supports key reforms to strengthen the control environment over the medium-term.** Functioning foreign exchange control environment in the NBKR in which the DPO2 proceeds are deposited as well as current budget execution reporting requirements are sufficient and adequate for the purposes of the proposed DPO2 funds flow. Furthermore, measures supported by this DPO series should over time strengthen critical aspects of the fiduciary environment. Consequently, the country's PFM system, combined with the commitment to PFM reforms, is adequate to support the operation.

D. MONITORING AND EVALUATION

65. **The Ministry of Finance is responsible for overall monitoring and evaluation of the proposed operation and for coordinating actions among other ministries and agencies.** The operation design and Policy Matrix reflect the limited capacity of institutions to monitor outcomes of policies. Hence, there is significant reliance on external indicators (Worldwide Governance Indicators (WGI), Doing Business (DB), etc.) to measure progress as well as inclusion in the broader DPO supported policy dialogue of actions that establish baselines to measure performance and results, for example in, public procurement and judiciary. The Bank will monitor actions and review progress of the implementation of the proposed operation, as well as the subsequent actions of the government program by using the baseline and expected overall program outcomes to be outlined in the Policy Matrix. The World Bank is also assisting the authorities in strengthening the national systems, including through providing advice on monitoring indicators for performance of the judiciary, energy sector and public procurement.

6. SUMMARY OF RISKS AND MITIGATION

66. **This is a high risk operation.** This overall rating reflects several factors:

- (a) Political and governance risks. The environment has stabilized since 2010, but the nascent democracy continues to face challenges. Stability will depend upon the state's ability to fight corruption, improve public services and sustain broad-based growth and employment. While government changes are likely to remain frequent as the society adjusts to the post-2010 arrangements, the shared vision on the strategic priorities among key political parties and the increasing evidence of the establishment of democratic norms are gradually reducing these risks. In addition, this DPO supports measures designed to strengthen transparency and accountability and support growth; however, the residual risk remains high given the evolving institutional infrastructure.
- (b) Macroeconomic risks have increased recently. Lower growth in Russia and Kazakhstan could weaken inflows of remittances and Kyrgyz exports. Another

disruption in gold production or a significant decline in gold prices will negatively impact the external balance. A large fiscal deficit and failure to control expenditures could jeopardize sustainability. Bank and IMF budget support programs partly mitigate these risks.

- (c) Sector policies and institutions are still evolving. The ability of the government to build consensus and coordinate across key implementing agencies, and weak institutional and technical capacity are critical limiting factors. The government seems to be improving internal coordination and achieving political consensus over time. The strong emphasis on coordination put in the preparation of the DPO and the twinned technical assistance operations serve as an organizing framework by helping the authorities better coordinate reform efforts. Still, beyond this, further progress in this area is needed.
- (d) Operational design, implementation and sustainability risks are high. Weaknesses in institutional capacity and evolving governing arrangements have affected the design of the operation, which was mitigated by strong emphasis in the preparation process on reaching precise agreement and close coordination with authorities. However, the stronger role of the parliament is increasing risks that actions requiring parliamentary approval may not be enacted in the manner agreed and within the expected timeline. The team has actively communicated with the parliament; however, the risk remains high, creating uncertainty in terms of the development impact and putting in question ability to provide DPOs in the future.
- (e) Fiduciary risks. The fiduciary environment is reflecting identified weaknesses across the entire range of PFM (accounting, auditing, procurement etc.). Adoption by Parliament of a Budget Code that retains the good international practices agreed during the preparation of DPO1 is essential to improve the fiduciary environment. In addition, the proposed DPO2 supports measures to reduce these risks; however, these reforms take time to produce visible results. Specific to this DPO2, fiduciary arrangements appear reasonable.
- (f) Environment and social risks are low. The operation is not expected to have environmental impact while social impact, if any, should be positive.
- (g) Stakeholder risks also exist. The operation is well aligned with the government strategy which is increasingly benefiting from improved participatory and consultative processes. However, despite an active outreach to all stakeholders, risks remain. The government's operating arrangements remain complex and actual implementation of some measures remains beyond the scope of the government because of the roles of parliament, judicial bodies, and other entities.

ANNEX 1: POLICY AND RESULTS MATRIX

Reform Areas	Prior Actions		
	DPO1	DPO2	Expected Results
<i>Pillar 1 – Program Development Objective 1 – Improving Public Sector Governance</i>			
Governance/ Anticorruption reform	Government, through Resolution No. 596 dated August 30, 2012, adopted the Anticorruption Program and Action Plan for 2012–14 and has established a framework for monitoring its implementation that includes independent experts and non-governmental organizations.	State Personnel Service has completed the first round of verification of asset declarations of civil servants in political functions and submitted the summary results to the Government.	Worldwide Governance Indicator Control of Corruption – percentile rank. Baseline: 9.95 (2011). Target: 15 (2014).
Improve budget discipline and transparency in use of budget resources	<p>A Protocol of cooperation dated October 23, 2012 signed between Ministry of Finance and the National Bank of the Kyrgyz Republic (NBKR), specifying the roles and responsibilities of the treasury, banking and accounting functions, and the oversight of payments/settlements, including the financial and information security controls for operation of the Single Treasury Account at the NBKR.</p> <p>Government, through Resolution No. 605 dated September 4, 2012, delegated authority to approve a Unified Chart of Accounts to the Ministry of Finance of the Kyrgyz Republic, and through Order No. 177-II dated September 4, 2012 the Ministry of Finance of the Kyrgyz Republic approved a Unified Chart of Accounts.</p> <p>Government through Resolution No. 718 dated October 15, 2012, “On Enactment of the Budget Code of the Kyrgyz Republic” submitted to Parliament a revised draft Budget Code that strengthens controls over non-allocated funds in the treasury, eliminates non-transparent reserve funds, advances the introduction of internal audit and medium term budgeting, and provides greater clarity to the overall budget cycle.</p> <p>The Prime Minister through letter No. 1-4118 to the Speaker of Parliament dated November 30, 2012, has requested an amendment to the proposed Budget Code that would require prior Parliamentary approval of the issuance of sovereign guarantees.</p>	The Government, through Resolution No. 498, dated September 9, 2013, approved a Regulation on Internal Audit Council establishing the said council; through Resolution No. 722 dated December 31, 2013, has adopted a regulation on Financial Management and Control in Budget Organizations; and through Resolution No. 721, dated December 31, 2013, adopted ethical standards for internal auditors in public agencies of the Kyrgyz Republic.	<p>Composition of expenditure out-turns compared to original approved budget. (PEFA PI-2)</p> <p>Baseline: C Target: B</p> <p>Effectiveness of internal audit increased (PEFA PI-21).</p> <p>Baseline: D (2009). Target: C (2014).</p>

Reform Areas	Prior Actions		
	DPO1	DPO2	Expected Results
Transparency in public procurement	<p>The Ministry of Finance published a Public Procurement Report on the use of the 2011 allocated budget.</p> <p>Government, through Resolution No. 661 of September 27, 2012, adopted the Public Procurement Development Strategy for 2012- 14 in line with international best practice.</p>	<p>The Government through Resolution No. 69, dated February 3, 2014, “On draft Public Procurement Law of the Kyrgyz Republic,” has approved and submitted to Parliament a draft of said law, and through the Resolution No. 68, dated February 3, 2014 “On Public Procurement Department under the Ministry of Finance of the Kyrgyz Republic”, has strengthened the role of the public procurement regulatory body within the Recipient’s Ministry of Finance.</p>	<p>MoF public procurement report shows increasing compliance with the PPL.</p> <p>Baseline: no information provided on effectiveness of public procurement (2011). Target: information made available on effectiveness of public procurement (2014).</p>
Increasing energy sector transparency, governance and accountability	<p>Government, through Resolution No. 611 dated September 7, 2012, adopted an action plan to enhance transparency, accountability and governance in the energy sector, including through: (i) carrying out annual audits of financial statements of energy companies following international accounting practices and making the audit reports public; (ii) setting up and maintaining web-sites for the Ministry of Energy, the Energy Regulatory Department, and the energy companies; (iii) ensuring transparent and competitive procurement of fuel resources; (iv) maintaining escrow accounts for power export revenues for the National Electrical Grid of Kyrgyzstan Joint Stock Company and the Power Plants Joint Stock Company; and (v) selecting the general directors and executive bodies of the energy companies based on transparent and competitive procedures.</p>	<p>The Ministry of Energy and Industry has issued the Order No. 174, dated October 10, 2013, which aims to increase the transparency of the energy sector by requiring Energy Companies to regularly publish on their respective websites the following information: (i) monthly balances of the special accounts of EPP and NEGK and transit accounts of Severelectro, Vostokelektro, Oshelectro, and Jalalabatelectro; (ii) quarterly operational and technical performance data of the Energy Companies; and (iii) annual financial statements together with audit reports.</p>	<p>Key operational and financial performance indicators and key decisions of the power sector are regularly disclosed.</p> <p>Baseline: no indicators are disclosed (2011). Target: key operational and financial performance indicators are disclosed (2014).</p>
<i>Pillar 2 – Program Development Objective 2 – Enhancing the Business Environment</i>			
Judicial reform	<p>The Presidential Decree No. 147 dated August 8, 2012, “On the Measures to Improve Justice in the Kyrgyz Republic,” has established the Judicial Reform Council and identified priorities for judicial reform. The Judicial Reform Council under the President approved a Strategic Action Plan on reforming the judicial system (Resolution No. 2, dated October 12, 2012).</p>	<p>The Government, through Resolution No. 174 “On Draft State Target Program on Development of the Judicial System of the Kyrgyz Republic for 2014-2017”, dated March 19, 2014, has submitted to Parliament the draft of said program which aims to increase the financial independence of the judicial sector.</p>	<p>Increase in the budget of the judiciary.</p> <p>Target: 10 percent annual increase (2015).</p>
Business startup and operations	<p>Government through the Ministry of Justice issued Order No. 134 dated October 11, 2012, containing: (i) a checklist for registry offices to clarify on what basis a registration application for the establishment</p>		<p>Reduction in the number of days to register a business.</p> <p>Baseline: 20 days.</p>

Reform Areas	Prior Actions		
	DPO1	DPO2	Expected Results
	of a business can be rejected; and (ii) instructions that applicants will receive upon the first submission of all requests identifying what additional information is required.		Target: Reduced by 10 days.
Access to finance		The Government, through Resolution No.610 dated November 11, 2013 “On Draft Law of the Kyrgyz Republic On Introducing Amendments to the Law on Joint Stock Companies of the Kyrgyz Republic,” has submitted to Parliament a draft of said law that aims to strengthen the responsibilities of members of management bodies.	Strength of investor protection index (sub-indicator of DB) improved. Baseline: score 7 (DB 2011). Target: score 8 (DB 2015).
Business inspections	Government, through Resolution No. 108 dated February 18, 2012, introduced transparent, risk-based criteria for planning and conducting business inspections and has developed a risk-based inspections coordination module (Kontr Pro 3) within the MoE, including a database of businesses subject to inspection.	The Government has operationalized the single automated database for inspections of businesses (KontrPro3) in the Ministry of Economy and six inspectorates in the City of Bishkek that aims to reduce the burden of inspections on businesses.	Risk-based inspection by MoE and pilot agencies reduces inspection burden. Baseline: inspections are not risk-based (2011). Target: inspections are risk-based (2014).
Reinforcement of the NBKR supervisory function and enhancing financial sector stability		The National Bank of the Kyrgyz Republic (NBKR), through Resolution No. 20/7 of the Board of the NBKR “On Amending the Regulation on Periodic Bank Reporting”, dated June 26, 2013, and through Resolution No. 27/1 of the Supervision Committee of NBKR “On Amending the Methodological Guidelines for Periodic Bank Reporting”, dated August 7, 2013 has strengthened bank reporting to support the functions of the NBKR’s newly established credit registry.	NBKR regularly collects credit information from banks and microfinance institutions and enhances supervision. Baseline: no records on parallel loans (2011). Target: parallel loans are tracked (2014).
Strengthening of the Deposit Protection System (DPS) legal framework		The Government, through Resolution No. 528 “On Draft Law on Introducing Amendments to the Law on Protection of Bank Deposits”, dated September 27, 2013, has approved and submitted to Parliament a draft of said law that aims to strengthen governance, coordination and operations of the deposit protection scheme.	Increased confidence in banks as evidenced by increasing deposits/GDP. Baseline: 16 percent (November 2013). Target: 20 percent (December 2014).

ANNEX 2: LETTER OF DEVELOPMENT POLICY

/Unofficial translation/

**His Excellency Jim Yong Kim,
President of the World Bank Group
1818 H Street, N.W.
Washington DC, 20433**

[Date]

RE: LETTER OF DEVELOPMENT POLICY

Your Excellency,

The Government of the Kyrgyz Republic would like to accord its highest respect and compliments to the World Bank for the ongoing assistance for the social and economic development of the Kyrgyz Republic.

I am writing to request on behalf of the Government of the Kyrgyz Republic a Development Policy Operation of US\$25 million to support our program that strengthens management of the public sector, and supports improvement in the environment for private sector growth.

Recent Economic Developments

Last year was a successful year for the Kyrgyz Republic. Our efforts to overcome the crisis in the economy and bring the economy to positive growth are showing results with the economy registering strong and broad-based recovery. Based on preliminary data of the National Statistics Committee of the Kyrgyz Republic for 2013, real GDP growth reached 10.5 percent, compared to a 0.1 percent contraction in 2012, while nominal GDP reached the level of KGS350.0 billion (US\$7.2 billion). Growth was led by a strong recovery in production at the country's main gold mine which alone contributed 5.1 percentage points of the overall growth. Encouragingly, our non-gold economy continued to grow strongly for a third consecutive year with output increasing by 5.8 percent, reflecting an increase in the industrial output (without Kumtor) (3.5%), agriculture (2.9%), services (5.4%), and construction (12.4%).

On the expenditure side, we were able to maintain high investment levels, increasing them further by 2.9 percent in 2013, while growth in remittances, improved access to credit and modest labor market improvements supported consumption. Despite recovering gold exports, our non-gold exports declined. With imports growing faster due to strong domestic demand, the trade increased further compared to the same period of 2012.

Our macroeconomic policies and favorable global food and energy price developments also resulted in lower inflation with annual inflation falling to 4.0 percent in December 2013 (year-over-year) and down from 7.5 percent in December 2012. The exchange rate of the Kyrgyz som against the US dollar depreciated 3.9 percent in 2013 as we continued our exchange rate policy of limited interventions aimed at preserving the competitiveness of the real exchange rate.

According to preliminary data of the National Statistics Committee of the Kyrgyz Republic, economic performance has moderated, but remains strong in 2014. Real GDP growth reached 5.9 percent in January-February 2014, or 5.2 percent excluding Kumtor and we expect growth to be around 6.9 percent in 2014. However, challenges have emerged, including devaluations of the currencies of major trading partners as well as reduced growth projections in Russia. The Kyrgyz som also depreciated; while preserving our competitiveness at traditional export markets, this can lead to higher inflation and hurt growth.

This Letter of Development Policy sets out the key actions that our Government is committed to undertake to maintain macro-fiscal stability and improve public sector management and the environment for private sector growth. The reform agenda is firmly embedded in our National Strategy for Sustainable Development and is a continuation of the program that was supported by the First Development Policy Operation (DPO1) in 2013. Our program envisages a fiscal policy stance that supports macroeconomic stability while safeguarding critical social spending, as well as reforms that improve transparency and accountability of the public sector, strengthen the judiciary, reduce burden of inspection and lower risks to the financial sector.

Country Development Goals and Indicators

Our broader priorities and development objectives are guided by National Strategy for Sustainable Development of the Kyrgyz Republic for 2013-2017. The NSSD was approved by Presidential Decree No.11 of January 21, 2013, and outlines strategic guidelines for sustainable development of the country, the key priorities and major investment projects over this period. In accordance with this development strategy, the primary objective for the next five years is to establish itself as a state with strong democratic principles and lay a foundation for successful development of Kyrgyzstan. This will be possible if the state and society will focus on the following three prerequisites in the course of implementing the Roadmap:

- relying on its own capabilities;
- enforcement of the rule of law; and
- achievement of unity.

Main goal of the National Strategy for 2013-2017 is to build a stable society, improve living standards, reduce poverty through accelerated economic growth, improved business climate and the rule of law, and establish an efficient management system. Achieving our goals will require building a well-functioning social market economy driven by a productive private sector, while the task of the state should primarily be focused on creation of enabling environment for private sector activities.

Macroeconomic stability will be the key target benchmark. The cornerstone of economic stability in the medium term will include fiscal and monetary policies that aim to achieve sustainable economic growth, well-balanced budget, predictable inflation and keeping within means, not at the cost of "future generations".

Public investment (Public Investment Program) should be aimed at development of such sectors of the economy, the growth of which contributes most to the economic development of remote areas, and which have significant multiplier effect on development of related industries.

We are confident that the implementation of the reforms in our strategy will allow us to meet our ambitious goals, including the following key quantitative parameters:

Table 1. Key Quantitative Parameters of Macroeconomic Stability in 2013-2017

Parameter:	Target:
Average annual real GDP growth	Not less than 7%
Inflation	Interval of 5-7% (from 2015)
Fiscal deficit	Not more than 5% of GDP
Public external debt	Up to 60% of GDP

The rest of this document outlines specific policies and reforms in number of areas, including those supported by the Development Policy Operation 2.

Public Financial Management and Fiscal Policy

Fiscal policy in 2013 was aimed at the full and timely financing of all social obligations of the state and creation of favorable conditions for economic growth. Similar principles guide our medium-term fiscal framework which envisages a slight increase in the fiscal deficit in 2014 (to account for the closure of the Manas Transit Center) followed by reduction in the deficit to less than 3 percent of GDP in 2016.

At the same time, we are actively implementing the Medium Term Action Plan to reform the public financial management system of the Kyrgyz Republic for 2012-2015 (approved by resolution of the Government of the Kyrgyz Republic No.675 dated October 3, 2012).

Budget Process

In order to improve the budgetary legislation to bring it closer to the international standards and adapt to progressive innovations in the budget process, a draft of the Budget Code of the Kyrgyz Republic has been prepared and introduced to the Parliament of the Kyrgyz Republic in accordance with the established procedure.

On 7 February 2014, the Ministry of Finance of the Kyrgyz Republic received the comments from the World Bank on the draft law. The comments will be considered in the process of further work with the Jogorku Kenesh (Parliament) of the Kyrgyz Republic on the draft law. On 28 February 2014 the extensive public hearings on the draft Budget Code of the Kyrgyz Republic were held with participation of the government agencies, the parliamentarians, and the civil society. Comments are also expected to be provided by the International Monetary Fund (IMF) and other stakeholders following the conducted parliamentary hearings. We are actively working with the representatives of the Parliament and the World Bank to ensure that the law that is finally enacted remains in line with good international practices.

We are also increasing the transparency of the budget process. Information on the budget is posted on the official website of the Ministry of Finance on a regular basis, including the Medium-Term Budget Framework for 2014-2016, draft and approved annual budgets, Civilian Budget, detailed monthly budget execution report and other budgetary information. Public budget hearings continue to be one of the channels to ensure transparency and citizens' engagement in the annual budget preparation process.

Continued progress is being made on gradual introduction of program-based results-oriented budgeting. Extensive training was provided to budget specialists in line ministries and the 2014 budget presented draft program-based budgets for 28 pilot institutions in addition to their budgets in the traditional format. We are also completing the introduction of GFS2001 standards in budget preparation and reporting.

Treasury

We are committed to implement a well-functioning treasury information system for the public sector in the Kyrgyz Republic. Unfortunately, our earlier efforts to implement a fully integrated TMIS did not come to fruition due to objective reasons; however, we are committed to the process and are exploring options with the World Bank and other partners to advance the process further.

Internal Audit

In order to achieve internal audit objectives of the Medium Term Action Plan to reform the PFM system of the Kyrgyz Republic we amended the Internal Audit Law and adopted the following regulations to ensure efficient internal audit:

- a) Regulation on the Board of Internal Audit was approved by resolution of the Government of the Kyrgyz Republic No.498 dated 09.09.2013.
- b) Resolution of the Government of the Kyrgyz Republic No.721 dated 12.31.2013 approved ethical standards of internal auditors of state bodies and institutions of the Kyrgyz Republic.
- c) Regulation on financial management and control in budget institutions was approved by resolution of the Government of the Kyrgyz Republic No.722 dated 12.31.2013.

Still, the agenda ahead is significant. Development of financial management and control requires establishment of the legal and regulatory framework, methodology, as well as arrangement for retraining of public institutions in the area of financial management and control. Also, improved quality of internal audit requires introduction of a system of certification of internal auditors.

Public Procurement

We are making significant efforts to establish a more transparent and accountable public procurement process in the country. We are strengthening the role of the regulatory body for public procurement. With the resolution of the Government of the Kyrgyz Republic No.68 dated February 3, 2014, the Public Procurement Department was established at the Ministry of Finance of the Kyrgyz Republic as a separate agency to pursue the public procurement policy of the Kyrgyz Republic. We are also committed to ensuring that the Department is able to recruit and retain high quality staff and are exploring various options to provide adequate remuneration to its staff.

Further to this, the Ministry of Finance of the Kyrgyz Republic drafted a new Public Procurement Law that aims primarily at eliminating corruption schemes in public procurement and reducing the room for maneuvering (discrete action) for those responsible for public procurement. The Public Procurement Law of the Kyrgyz Republic has been adopted by the Government of the Kyrgyz Republic, and will be considered by the Parliament of the Kyrgyz Republic. In view of improving and enhancing the appeals and protests redress mechanism the draft secondary legislation, providing for establishment of an independent appeals mechanism, has been drafted and will be adopted upon enactment of the Public Procurement Law.

In an effort to improve the transparency of the public procurement system, the Ministry of Finance launched the e-procurement portal (www.zakupki.okmot.kg) on April 9, 2012 and has since considerably

improved its coverage and functionality. Since the beginning of 2012, all procurements of public authorities of the Kyrgyz Republic are published on the public procurement portal.

Going forward, we plan to further advance the public procurement portal including developing modules for online e-procurement and use of electronic digital signatures. Implementation of the new system will require extensive training for the regulator, the implementing agencies, the independent appeals commission as well as the private sector.

Anti-corruption

Anti-corruption remains a key priority of our agenda. Following the adoption of the Anti-corruption Action Plan in 2012, we are taking steps for its effective implementation. We adopted resolution No.44-p dated February 12, 2014 (on approval of the Methodology of design and implementation of departmental anti-corruption program and action plan and the Methodology of anti-corruption monitoring and evaluation) mandates the use of the monitoring and evaluation methodology by the public sector institutions. An approved Methodology of design and implementation of departmental anti-corruption program and action plan and the Methodology of anti-corruption monitoring and evaluation are consistent with the international standards used by FATF, IMF and the World Bank. Adoption of the above resolution will help streamline the form of submitting reports on execution and implementation of anti-corruption measures by the Government of the Kyrgyz Republic and provide us with a valuable tool to monitor the impact of our anti-corruption efforts.

The State Personnel Service also recently completed the first round of verifications of asset declarations of civil servants in high-risk positions. This has been a very important experience for our institutions as it enabled a number of different agencies to cooperate and exchange data and information. This activity will considerably improve the usefulness of asset declarations in the fight against corruption. We plan to expand the number of civil servants covered in the future once we establish an automated Human Resources Information Management System.

We are strengthening provisions to prevent Conflict of Interest (CoI). Conflict of Interest is regulated with Article 9 of the Civil Service Law of the Kyrgyz Republic No.114 dated August 11, 2004, as well as in other sectoral legislation. However, findings of the monitoring of the practice of dealing with conflicts of interest in public service conducted by the State Personnel Service of the Kyrgyz Republic in 2012 show that such situations continue to exist. In order to establish a mechanism for resolving conflicts of interest in state and municipal service of the Kyrgyz Republic, the Government of the Kyrgyz Republic adopted the resolution "On approval of the Interim Guidelines on conflict of interest in state and municipal service of the Kyrgyz Republic" No.90 dated February 13, 2014 developed on the basis of the

OECD's Model Guidance. This is expected to be an intermediary step until the enactment of a separate Law on Conflict of Interest which we expect to take place in the second half of 2014.

Energy Sector

The energy sector of the Kyrgyz Republic has significant growth prospects. The country has a rich and relatively inexpensive hydropower potential that may lead to profitable export of electricity. However, this potential remains largely untapped. The sector is facing serious problems, such as lack of financial viability and weakened reliability of power supply. The main reason is a low tariff level, which is significantly lower than the cost recovery level. Performance indicators of the sector are also low. In particular, commercial and technical losses remain high (about 16 percent), despite the reduction of losses in recent years. Due to the outdated energy infrastructure and an insufficient level of maintenance and repair, the sector requires substantial investment to prevent fatal crashes and prolonged outages.

In order to address these problems, the Government of the Kyrgyz Republic has issued resolution No.299 dated 07.24.2013 that approved the Energy Sector Reform Action Plan for 2013-2014. Main goals and objectives of this Action Plan are as follows: reform and improvements in the energy sector regulation; modernization of management and maintenance of financial sustainability; providing sufficient income for the reconstruction and modernization of the power grid in order to restore uninterrupted power supply to consumers; reconstruction and modernization of the energy sector facilities; reduction of electricity losses; improved quality of service and public confidence.

As part of implementation of the action plan, we have increased investments in the sector's infrastructure, including: US\$208 million for construction of the 500 kV Datka substation and 220 kV power lines to increase the power supply in the southern regions; US\$45 million for modern metering and data acquisition system in transmission networks; US\$390 million for 500 kV transmission line Datka - Kemin and 500 kV Kemin substation to supply electricity for the northern part of the country, regardless of the networks of neighboring countries; US\$55 million for rehabilitation of the Toktogul hydropower plant, US\$23 million for renovation of substations in Bishkek and Osh, the two largest cities in the country, and US\$5 million for 110 kV double circuit overhead line and 110/10 kV substation in Ak-Ordo community of Bishkek.

In addition, a number of projects have been launched recently to meet winter energy shortages and increase export potential - Upper Naryn cascade HPP (US\$728 million); Kambarata-1 HPP; Bishkek CHP Modernization (US\$386 million); At-Bashi HPP Reconstruction. The World Bank's "Electricity Supply Reliability and Improvement Project" (US\$25 million) is at its initial stage to increase transparency and accountability in JSC Severelectro, the largest distribution company. Activities are

under way on the Kyrgyzstan-China pipeline construction (US\$1.2-1.4 billion) and CASA-1000 is also entering the implementation stage (US\$200 million).

We are also improving the governance of the system. The Ministry of Energy and Industry of the Kyrgyz Republic has issued an order on posting information on balances of special accounts and transit accounts of the energy companies, key operational and technical performance indicators, as well as financial statements on web-sites of power companies and the Ministry on a regular basis. As part of this, and with the support from the World Bank, in April 2014, we revised the key efficiency and performance indicators for the companies in the sector. This will considerably improve the transparency of the energy companies.

Another accomplishment is the introduction of the Fuel and Energy Sector Transparency Initiative (FESTI) aimed at improving transparency and control in the industry and ensuring greater public participation and transparency. According to the Initiative (FESTI), a supervisory board with the participation of civil society has been created and is currently operational.

Revisions to the legal framework for the energy sector (Law on Energy, law on Electric Energy and Law on Natural and Allowed Monopolies) expected to be submitted to the Parliament in the second quarter of 2014 will clarify the authorities and responsibilities in the sector and establish an independent settlement center in order to ensure transparent accounting and monitoring of electricity and financial flows in the sector. Going forward, we plan to establish an independent regulator and introduce a long-term contract for the management of distribution companies with a private operator that has intensive international managerial experience, to re-evaluate the assets of entire energy sector companies including heat and power companies in order to fully reflect the true costs of replacing those assets in the tariffs, and to conduct comprehensive financial and technical audits of the power companies. We also intend to adopt a new tariff policy for power and heat supply to gradually reach full cost recovery level, as well as adopt a modern tariff methodology that will allow for accurate and unequivocally calculation of tariffs. We are aware that higher energy prices will affect the population, especially the most vulnerable, and will introduce measures to mitigate these risks. Initially, this may be done by providing a lifeline tariff (i.e. social norm tariff) and, gradually, as we strengthen our social protection systems, we plan to move to a more targeted system of supporting the most vulnerable.

Judicial System Reform

At all times impartial and fair trial has been a measure of development of the state, not only as a democratic and legal state, but also as a state that is successful in the economic and social areas. Confidence of our citizens in their rights not being violated and, if violated, being restored, depends on performance of our judicial system. All of these challenge public authorities, especially the judiciary,

with objectives of building an independent and autonomous judicial system that meets the calls of the time and protects rights, freedoms and dignity of a citizen.

As of today, there are three priorities in this area: i) selection of judges; ii) development of an updated procedural law and other laws aimed at improving the administration of justice and iii) future development of the judicial system in Kyrgyzstan until 2017.

Within the first priority, the Judicial Selection Council of the Kyrgyz Republic has selected judges in accordance with the established procedures; the Supreme Court of the Kyrgyz Republic, Constitutional Chamber of the Supreme Court of the Kyrgyz Republic, all regional and the overwhelming majority of military courts have been formed and perform to the utmost with involvement of the President of the Kyrgyz Republic and the Parliament of the Kyrgyz Republic. We are currently revising the judge's selection process to reduce the scope for subjectivism in the process and to ensure the best candidates are awarded the job.

Within the second priority, recommendations for further reform of the judicial system of the Kyrgyz Republic elaborated on the basis of social dialogue have been accepted as a basis for concerted actions of public authorities in the country; the Council for Judicial Sector Reforms under the President of the Kyrgyz Republic has been established and operates within this reform. Seven expert working groups for drafting relevant procedural and other laws have been established and operate.

Within the third priority, the Judicial Council of the Kyrgyz Republic, acting on behalf of the judicial system, has prepared and submitted to the Government of the Kyrgyz Republic draft State Targeted Program "Development of the Judicial System of the Kyrgyz Republic for 2014-2017". This is a significant accomplishment as it sets the stage for an independent judicial budget and envisages gradual, but significant, increase in the resources available to the sector. Namely, further stepwise increase in the financing of the judicial system by 10 percent (of the financing in the previous period, 2014) per annum will start from 2015 on, until it gradually reaches the level of 1 percent of the national budget expenditures.

We are also increasing the salaries of the staff in the judicial sector to improve motivation and reduce incentives for corrupt practices. Resolution on conditions of remuneration of public and municipal employees of the Kyrgyz Republic No.384 dated June 28, 2013 and Resolution on conditions of remuneration of judges of the Kyrgyz Republic, civil servants of the Supreme Court of the Kyrgyz Republic, Office of the Constitutional Chamber of the Supreme Court of the Kyrgyz Republic No.560 (restricted circulation) dated October 18, 2013 were adopted (both effective from October 1, 2013). Thus, as compared to 2013, in 2014 efforts to reform the judicial system take into account the 51.9 percent increase in wages.

We have taken steps to increasing the transparency of the judicial sector. The Judicial Department of the Supreme Court of the Kyrgyz Republic prepared a report on statistics of performance of the judicial sector, which is posted on the websites of the Judicial Council (www.sskr.kg) and the Supreme Court (sudsistem.kg). Later on, these statistics will be published in the Bulletin of the Supreme Court of the Kyrgyz Republic and can also be used to assess the impact of our reforms over the functioning of the judiciary.

Private Sector Development

The Government of the Kyrgyz Republic continues to focus on supporting and developing the private sector, which is to become the engine of the national economy. Following efforts are made to facilitate and ensure predictability of the private sector.

We are reforming the inspection process, which until now was a big burden for the private sector. The Ministry of Economy of the Kyrgyz Republic launched an official web portal for inspections of businesses conducted by state regulatory agencies (proverka.kg) on August 21, 2012 providing information for inspections with pilot state control bodies. We also amended the legal framework to reduce the number of inspectorates and introduce risk-based inspections. Most recently, we developed and launched Kontr-Pro-3 module in inspection agencies in the Bishkek region which facilitates the actual implementation of risk-based supervision. The process of introducing the database in central and regional offices of state control bodies will be phased and completed once the technical constraints are addressed. The database, managed by the Ministry of Economy, is the first interagency electronic workflow in the Kyrgyz Republic, which unifies the databases of inspections of 12 state control bodies into a single database with the risk profile of businesses.

For the authorities, use of Kontr-Pro3 simplifies audits and allows:

- reducing unwarranted and unnecessary inspections by state control bodies;
- accelerating the process of harmonization of orders to conduct inspections;
- analyzing efficiency of audits and application of risk criteria during inspections;
- checking and eliminating duplicate inspections;
- raising awareness of entrepreneurs regarding inspections.

On the side of businesses, any business may now access the site and obtain information about when and which inspector plans to visit it; which risk group it belongs to; how often it will be inspected. There is an online forum for communication and complaints of entrepreneurs on illegal inspections. Together with IFC, we are working on also revising the checklists for inspections which will further reduce the burden of inspections for businesses.

Kontr-Pro3 was implemented in the next 6 pilot state control bodies: State Inspectorate for environmental and technical safety under the Government of the Kyrgyz Republic, State Veterinary Inspectorate for phytosanitary security under the Government of the Kyrgyz Republic, Social Fund of the Kyrgyz Republic, Department of Drug Supply and Medical Equipment under the Ministry of Health of the Kyrgyz Republic, Department of Precious Metals at the Ministry of Finance, and State Service for Financial Market Regulation and Supervision under the Government of the Kyrgyz Republic.

Financial Sector

The banking system grew steadily in 2013, maintaining stability and the potential for increasing the level of cooperation and efficiency. This also reflects the efforts of the NBKR to improve quality and effectiveness of banking supervision, including through: i) strengthening the oversight function of the NBKR, ii) expanding capacity of the NBKR in supervision and regulation of the banking sector; iii) remedying situations with troubled, as well as iv) improving the regulatory and supervisory framework in line with international standards of the Basel Committee.

The National Bank of the Kyrgyz Republic recently completed the development of its credit registry. This registry will enable it to have timely information on exposure of banks and greatly facilitate the supervision process, thus contributing to stability of the financial sector. This is only an initial step in the developing of a broader integrated information system within the NBKR that is expected to greatly improve effectiveness of financial sector regulation and supervision.

Adoption of the new Banking Code, currently in Parliament approval procedure, will help improve quality and efficiency of standards of the banking legislation through a systematic approach and use of the latest international practices; consolidate good practice of the well-established banking system and identify ways for further improvements; harmonize all parts of the banking legislation in order to avoid inconsistencies, conflicts and contradictions; clarify legal status of members of banking relationships, determine their relationships, as well as the fundamental relationships both within and outside of the banking system.

We are taking efforts to increase confidence in the financial sector and strengthen the deposit protection system. We drafted amendments to the Law on protection of bank deposits (resolution of the Government of the Kyrgyz Republic No.528 of September 27, 2013) which, among other things: extends the coverage of the deposit protection system to private entrepreneurs; reduces the compensation time from 60 to 30 days and streamlines the procedures for timely payment of compensations; expands the scope of information shared and strengthens cooperation with the central bank; advances the role of the Deposit Protection Agency to issue methodologies and recommendations on deposit protection system

for banks and improves the governance arrangements in the Deposit Protection Agency. We are actively working with the Parliament to ensure successful promotion of the proposed amendments.

The proposed amendments will improve the legislation of the Kyrgyz Republic in the area of deposit protection and allow for preliminary preparation for transition from the "paybox" mandate to the "paybox with additional, yet limited powers" mandate which is also envisaged in the draft Banking Code which is currently in Parliamentary approval stage. Over the medium term, we expect to reach the third stage, and final stage, and transit to the "risk minimizer" mandate for the deposit protection system, in line with recommendations of the FSAP 2013.

Corporate Governance

We are aware that an efficient private sector requires corporate governance arrangements that promote accountability and transparency to stakeholders and we are taking steps in this direction. We recently prepared the draft Law of the Kyrgyz Republic "On amendments to the Law on joint stock companies" aimed at increasing responsibility of the board of directors of joint-stock companies in making decisions on consummation of transactions by such companies, as well as facilitating procedures and clarifying the process of obtaining dividends by shareholders and streamlining the procedure for termination of office of members of the board of directors in joint-stock companies.

Furthermore, the SSFMRS is in the process of designing a program of securities market development in the Kyrgyz Republic for 2014-17 which will include a number of measures to improve corporate governance in Kyrgyz enterprises, including through: i) improving effectiveness of corporate governance in joint-stock companies and issuers of publicly offered securities; ii) revising of requirements for the listing of securities of joint-stock companies; iii) ensuring reliability of the securities registration system; and iv) strengthening and building capacity of the authorized state authority for regulation of the securities market.

In conclusion, we are convinced that implementation of the priorities of the NSSD are of prime importance to ensure sustainable and successful future of our country and that the reforms outlined above represent a coherent program that will contribute to achieving stronger economic growth and poverty reduction over the medium-term. We trust that this request for World Bank support in the amount of US\$25 million for the implementation of this reform program will receive your endorsement.

Sincerely yours,

Dj. Otorbaev

Prime Minister of the Kyrgyz Republic



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Президенту Группы
Всемирного Банка
г-ну Джиму Йонг Киму

Уважаемый господин Ким,

Правительство Кыргызской Республики (далее - Правительство) свидетельствует свое почтение Всемирному банку и благодарит за постоянное содействие в социально-экономическом развитии Кыргызской Республики.

От имени Правительства прошу Вас выделить 25 млн долл. США на Операцию в поддержку политики развития, направленную на укрепление управления в государственном секторе и улучшения среды для развития частного сектора.

Последние экономические события

Последний год был успешным для Кыргызской Республики. Усилия Правительства по преодолению экономического кризиса и восстановлению положительного роста экономики демонстрируют значительный рост. Согласно данным Национального статистического комитета Кыргызской Республики за 2013 год, рост реального ВВП достиг 10.5 %, по сравнению со снижением до 0.1 % в 2012 году, а номинальный ВВП достиг 350.0 млрд сомов (7.2 млрд долл. США). Рост достигнут благодаря устойчивому восстановлению производства на главном золоторудном месторождении страны, вклад которого составил 5.1 процентного пункта в общий темп роста. Отрадно, что секторы экономики, не связанные с производством золота продолжили расти в течение трех последних лет и объемы производства выросли на 5.8 %, отражая увеличение темпов роста промышленного производства (без учета Кумтора) (3.5 %), сельского хозяйства (2.9 %), услуг (5.4 %) и строительства (12.4 %).

Что касается расходной части бюджета, то удалось удерживать высокие объемы инвестиций, с увеличением на 2.9 % в 2013 году, наряду с ростом объема денежных переводов, улучшением доступа к кредитам и умеренным улучшением ситуации на рынке труда, которые способствовали росту

потребления. Несмотря на восстановление уровня экспорта золота, остальные экспортные операции снизились. С ростом импорта, обусловленным высоким внутренним спросом, выросли объемы торговли по сравнению с аналогичным периодом 2012 года.

Макроэкономическая политика и благоприятные изменения глобальных цен на продовольствие и энергоресурсы в результате привели к низкой инфляции. Так, годовые темпы инфляции снизились до 4.0 % в декабре 2013 года (в годовом исчислении) с 7.5 % в декабре 2012 года. Обменный курс сома к доллару США обесценился на 3.9 % в 2013 году, т.к. республика продолжала следовать политике обменного курса с лимитированными интервенциями, нацеленными на сохранение конкурентоспособности реального обменного курса.

Согласно предварительным данным Национального статистического комитета Кыргызской Республики, уровень экономической активности снизился, но остается устойчивым в 2014 году. Рост реального ВВП в январе-марте 2014 года достиг 5.6 %, без учета Кумтора, рост составил 4,9 %, а также по итогам 2014 года ожидается рост на уровне 6,9 %. При этом, возникли новые вызовы, в том числе девальвация валюты основных торговых партнеров, а также снижение прогнозируемых темпов роста в Российской Федерации. Национальная валюта (сом) также обесценилась в определенной степени; при условии сохранения конкурентоспособности на традиционных экспортных рынках это может привести к более высокой инфляции и отразится на темпах роста.

Настоящее письмо о политике развития устанавливает ключевые меры, которые предпринимаются Правительством для поддержания макрофискальной стабильности и укрепления управления государственным сектором, а также среды для развития частного сектора. Программа реформ интегрирована в Национальную стратегию устойчивого развития Кыргызской Республики на период 2013-2017 годы (далее - НСУР), утвержденную Указом Президента Кыргызской Республики от 21 января 2013 года № 11, и является продолжением программы, которая была поддержана в рамках Первой операции в поддержку политики развития (ОППР1) в 2013 году. Программа предполагает позицию в фискальной политике, которая поддерживает макроэкономическую стабильность, обеспечивающую расходы на защищенные социальные статьи, а также реформы, направленные на повышение прозрачности и подотчетности государственного сектора, укрепление судебной системы, сокращение проверок бизнеса и снижение рисков для финансового сектора.

Цели и индикаторы развития страны

Более широкие приоритеты и задачи в области развития установлены в соответствии с НСУР, которая отражает стратегические направления для устойчивого развития страны, основные приоритеты и главные инвестиционные проекты в этот период. Основная задача на следующие пять лет заключается в создании государства с сильными демократическими принципами и построении фундамента для успешного развития Кыргызской Республики. Это станет возможно, если государство и общество будут фокусировать внимание на следующих трех предпосылках для реализации НСУР:

- использование собственных возможностей;
- усиление верховенства закона;
- достижение единства.

Основная цель НСУР заключается в построении стабильного общества, повышении уровня жизни, снижении уровня бедности через ускорение экономического роста, улучшении деловой среды и укреплении верховенства закона, создании эффективной системы управления. Достижение целей потребует построения нормально функционирующей социальной рыночной экономики, движимой продуктивным частным сектором, при этом задача государства должна быть сконцентрирована на создании благоприятной среды для деятельности частного сектора.

Макроэкономическая стабильность является основной целевой задачей. Основа экономической стабильности в среднесрочной перспективе включает фискальную и монетарную политики, нацеленные на достижение устойчивого экономического роста, сбалансированного бюджета, предсказуемой инфляции и жизни по средствам, а не за счет «будущих поколений».

Государственные инвестиции (Программа государственных инвестиций) нацелены на развитие таких секторов, рост которых обеспечит экономическое развитие отдаленных регионов, и значительный мультипликативный эффект от развития смежных отраслей. Реализация реформ, заложенных в НСУР позволит достичь стратегических целей, в том числе следующих количественных параметров:

Таблица 1. Основные количественные параметры макроэкономической стабильности в 2013-2017 годах

Параметр:	Целевой показатель:
Среднегодовой рост реального ВВП	Не менее 7 %
Инфляция	Интервал от 5 до 7 % (с 2015 г.)
Фискальный дефицит	Не более 5 % ВВП
Внешний государственный долг	До 60 % ВВП

Остальные разделы настоящего документа устанавливают конкретные программы и реформы в ряде областей, в том числе те, которые осуществляются при поддержке Операции по политике развития - 2.

Управление государственными финансами и фискальная политика

Фискальная политика в 2013 году была направлена на полное и своевременное финансирование всех расходов на социальные статьи государства и создание благоприятных условий для экономического роста. Аналогичные принципы заложены в основу среднесрочной фискальной политики государства, которая предусматривает небольшое увеличение бюджетного дефицита в 2014 году (с учетом закрытия Транзитного центра «Манас»), за которым последует снижение дефицита размером менее 3 % к ВВП в 2016 году.

В то же время, активно реализуется Среднесрочный план действий по реформированию системы государственных финансов Кыргызской Республики на 2012-2015 годы, утвержденный постановлением Правительства Кыргызской Республики от 3 октября 2012 года № 675.

Бюджетный процесс

В целях совершенствования бюджетного законодательства и приведения его к международным стандартам, а также внедрения прогрессивных инновационных решений в бюджетный процесс, был разработан проект Бюджетного кодекса Кыргызской Республики и представлен в Жогорку Кенеш Кыргызской Республики (Парламент) в соответствии с установленными процедурами. 7 февраля 2014 года Министерством финансов Кыргызской Республики получены комментарии Всемирного банка к законопроекту, которые будут проработаны Министерством в ходе дальнейшей работы с Жогорку Кенешем Кыргызской Республики над законопроектом. 28 февраля 2014 года проведены

расширенные Парламентские слушания с участием представителей государственных органов, депутатов Жогорку Кенеша Кыргызской Республики, представителей гражданского сектора по проекту Бюджетного кодекса Кыргызской Республики. Кроме того, ожидаются комментарии Международного валютного фонда (МВФ) и других заинтересованных сторон по итогам проведенных Парламентских слушаний. Правительство активно работает с представителями Жогорку Кенеша Кыргызской Республики и Всемирного банка по обеспечению принятия Закона в соответствии с передовым международным опытом.

Правительством также обеспечивается повышение уровня прозрачности бюджетного процесса. Информация о бюджете публикуется на веб-сайте Министерства финансов Кыргызской Республики на регулярной основе, включая среднесрочный бюджет на 2014-2016 годы, проекты бюджетов и принятые годовые бюджеты, гражданский бюджет, детальный ежемесячный отчет об исполнении бюджета и другая информация по бюджету. Общественные слушания по бюджету продолжают оставаться одним из каналов обеспечения прозрачности и вовлечения граждан к процессу разработки бюджета.

Отмечается прогресс в постепенном переходе к программному, ориентированному на результат, бюджетированию. Проведен расширенный тренинг для бюджетных специалистов в профильных министерствах, в бюджете на 2014 год представлен проект программного бюджета для 28 пилотных ведомств в дополнение к их бюджету, составленному в традиционном формате. Завершается процесс внедрения стандартов GFS2001 в подготовке бюджета и отчетности по нему.

Казначейство

Предпринимается меры по внедрению полноценно функционирующей информационной системы казначейства для государственного сектора Кыргызской Республики. Прежние попытки внедрить полностью интегрированную TMIS (информационную систему казначейства) не были плодотворными по объективным причинам. Однако, работа в данном направлении продолжается, в частности производится поиск альтернатив совместно с Всемирным банком и другими партнерами по развитию для продвижения данного вопроса.

Внутренний аудит

В целях обеспечения достижения задач по внутреннему аудиту в соответствии со Среднесрочным планом действий по реформированию

системы управления государственными финансами Кыргызской Республики, внесены изменения в закон о внутреннем аудите и утверждены следующие положения для обеспечения эффективного внутреннего аудита:

- Положение о Совете по внутреннему аудиту, утвержденное постановлением Правительства Кыргызской Республики от 9 сентября 2013 года № 498;

- Этические стандарты внутренних аудиторов государственных органов и учреждений Кыргызской Республики, утвержденное постановлением Правительства Кыргызской Республики от 31 декабря 2013 года № 721;

- Положение о финансовом управлении и контроле в бюджетных учреждениях, утвержденное постановлением Правительства Кыргызской Республики от 31 декабря 2013 года № 722.

Развитие финансового менеджмента и контроля требует создания правовой и регулятивной среды, методологии, а также переобучения служащих государственных органов, задействованных в сфере финансового менеджмента и контроля. Кроме того, улучшение качества внутреннего аудита требует внедрения системы сертификации внутренних аудиторов.

Государственные закупки

Прилагаются значительные усилия по созданию более прозрачного и подотчетного процесса государственных закупок. Усилена роль органа, регулирующего государственные закупки. Постановлением Правительства Кыргызской Республики от 3 февраля 2014 года № 68 создан Департамент по государственным закупкам при Министерстве финансов Кыргызской Республики, в качестве отдельного ведомства в сфере государственных закупок Кыргызской Республики. Департамент будет укомплектован на долгосрочной основе высококвалифицированными специалистами, а также рассматриваются различные варианты достойной оплаты труда сотрудников Департамента.

Кроме того, Министерством финансов Кыргызской Республики разработан проект закона о государственных закупках, направленный, главным образом, на устранение коррупционных элементов в сфере государственных закупок и возможностей для коррупционных проявлений (злоупотреблений должностным положением) теми, на кого возложена ответственность за государственные закупки. Закон о государственных закупках Кыргызской Республики был одобрен Правительством и будет утвержден Жогорку Кенешем Кыргызской Республики. В целях улучшения и совершенствования процедур рассмотрения жалоб и протестов, договорных обязательств были разработаны проекты подзаконных актов, предусматривающие создание независимого механизма по рассмотрению

жалоб и протестов. Данные подзаконные акты будут приняты сразу после принятия новой редакции Закона Кыргызской Республики «О государственных закупках»

В целях повышения прозрачности системы государственных закупок, с 9 апреля 2012 года Министерством финансов запущен в работу портал электронных закупок (www.zakupki.okmot.kg). С момента запуска в значительной мере улучшились охват и функциональность портала. С начала 2012 года информация о всех закупках государственных органов Кыргызской Республики публикуется на портале государственных закупок.

Планируется и далее развивать портал государственных закупок, в том числе разработку модулей для он-лайн закупок и использование электронных цифровых подписей. Реализация новой системы потребует обучения регулятора, представителей закупающих организаций, комиссий по рассмотрению жалоб и частного сектора.

Антикоррупционные меры

Борьба с коррупцией остается основным приоритетом Правительства. После принятия Антикоррупционного плана действий в 2012 году, предпринимаются шаги по эффективной его реализации. Правительством принято распоряжение об утверждении Методики разработки и реализации ведомственной программы и плана мероприятий по противодействию коррупции, а также Методологии антикоррупционного мониторинга и оценки от 12 февраля 2014 года № 44-р, которое обязывает государственные органы применять методологию мониторинга и оценки. Утвержденные Методика и Методология соответствуют международным стандартам, применяемым FATF, МВФ и Всемирным банком. Принятие вышеназванного постановления гармонизирует форму представления отчетов об исполнении и реализации антикоррупционных мер Правительством и станет ценным инструментом мониторинга воздействия антикоррупционных действий.

Кроме того, Государственной кадровой службой Кыргызской Республики недавно завершён первый раунд верификации деклараций о доходах госслужащих, занимающих должности с высокой категорией риска. Данная работа позволила наладить обмен данными и информацией между различными государственными институтами, а также в значительной мере повысить полезность механизма в борьбе против коррупции. Планируется увеличить охват госслужащих в будущем, после создания автоматизированной информационной системы управления человеческими ресурсами.

Предпринимаются меры по совершенствованию процедур и положений, предотвращающих конфликт интересов, регулируемый статьей 9

Закона Кыргызской Республики «О государственной службе Кыргызской Республики», а также другими законами. Однако выводы, сделанные в результате мониторинга практики работы с конфликтом интересов на государственной службе, проведенного Государственной кадровой службой Кыргызской Республики в 2012 году показали, что такие ситуации продолжают существовать. В целях создания механизма по разрешению конфликта интересов на государственной и муниципальной службе Кыргызской Республики, Правительством было принято постановление «Об утверждении временного руководства по конфликту интересов на государственной и муниципальной службе Кыргызской Республики» от 13 февраля 2014 года № 90, разработанного на основе Модели руководства ОЭСР. Предполагается, что оно станет промежуточной мерой до принятия отдельного закона о конфликте интересов, предположительно, во второй половине 2014 года.

Энергетика

Энергетический сектор Кыргызской Республики обладает значительными ресурсами. В стране есть богатый и относительно недорогой гидроэнергетический потенциал, что может привести к выгодному экспорту электроэнергии. Однако этот потенциал остается в значительной степени нереализованным. Сектор сталкивается с серьезными проблемами, такими как отсутствие надлежащего финансирования и ослабление надежности электроснабжения. Основной причиной этого является низкий уровень тарифов, который значительно ниже уровня возмещения затрат. Эксплуатационные показатели сектора также низкие. В частности, коммерческие и технические потери продолжают оставаться высокими (около 16 процентов), несмотря на снижение потерь в последние годы. Из-за устаревшей инфраструктуры энергетического сектора и недостаточного уровня технического обслуживания и ремонта сектор требует значительных инвестиций для предотвращения сбоев и длительных отключений.

Для решения вышеуказанных проблем, распоряжением Правительства от 24 июля 2013 года № 299-р утвержден План действий по реформированию энергетического сектора на 2013-2014 годы. Основными целями и задачами данного Плана действий является реформирование и улучшение регулирования энергосектора; модернизация управления и обеспечение финансовой устойчивости; обеспечение достаточного объема доходов для реконструкции и модернизации энергосистемы в целях восстановления бесперебойного электроснабжения потребителей; реконструкция и модернизация объектов энергосектора; снижение потерь электроэнергии; повышение качества обслуживания и общественного доверия.

Во исполнение Плана действий, увеличены инвестиции в инфраструктуру сектора, включая строительство подстанции 500 кВ Датка и линии электропередачи 220 кВ для увеличения объемов подачи электроэнергии в южные регионы, на сумму 208 млн долл. США; внедряется современная система учета и сбора данных в передающих сетях на сумму 44,8 млн долл. США; идет строительство линии электропередачи 500 кВ Датка – Кемин и подстанции 500 кВ Кемин на сумму 390 млн долл. США для обеспечения электроснабжения северной части республики, вне зависимости от сетей соседних стран; реализуется проект реабилитации Токтогульской ГЭС на сумму 55 млн долл. США, проект реконструкции подстанций городов Бишкек и Ош, самых крупных городов страны, на сумму 23,08 млн долл. США и на стадии завершения проект «Строительство двухцепной ВЛ 110 кВ и ПС 110/10 кВ в жилмассиве Ак-Ордо г. Бишкек» (5 млн долл. США);

Кроме того, в последнее время для покрытия зимнего дефицита энергии и повышения экспортного потенциала начаты проект «Строительство Верхне-Нарынского каскада ГЭС» (728 млн долл. США); проект «Строительство Камбаратинской ГЭС-1»; проект «Модернизация ТЭЦ г. Бишкек» (386 млн долл. США); проект «Реконструкция Ат-Башинской ГЭС»; на стадии начала реализации проект Всемирного Банка «Повышение подотчетности и надежности системы электроснабжения» (25 млн долл. США) с тем, чтобы повысить прозрачность и подотчетность в самой крупной распределительной компании ОАО «Северэлектро»; проект «Строительство газопровода «Кыргызстан-Китай» (1,2-1,4 млрд долл. США); также входит в стадию реализации проект «CASA-1000» (200 млн долл. США) на территории Кыргызской Республики.

Также улучшается управление энергетической системой. Министерством энергетики и промышленности Кыргызской Республики издан приказ, в соответствии с которым на интернет-сайтах энергокомпаний и министерства регулярно размещается информация об остатках на специальных и транзитных счетах; операционных и технических показателях деятельности; финансовых отчетах. В этом направлении, в сотрудничестве со Всемирным Банком, пересмотрены ключевые показатели эффективности и деятельности для энергокомпаний в апреле 2014 года.

Другой реализованной мерой является введение Инициативы прозрачности топливно-энергетического комплекса (ИПТЭК или FESTA), направленной на улучшение прозрачности и управления отрасли, обеспечение более широкого участия общественности и прозрачности. Согласно этой Инициативе (ИПТЭК или FESTA), создан и в настоящее время действует наблюдательный совет с участием гражданского общества.

Во втором квартале 2014 года будут направлены проекты законов о внесении изменений в законодательство (Закон КР «Об энергетике», Закон

КР «Об электроэнергетике» и Закон КР «О естественных и разрешенных монополиях») на рассмотрение Жогорку Кенеша Кыргызской Республики, предусматривающие более четкое разграничение полномочий и ответственности между государственными ведомствами, участвующими в секторе, и создание Расчетного центра для обеспечения прозрачного учета, мониторинга энергии и денежных потоков в секторе. Правительство намерено придать статус независимости регулятору; внедрить долгосрочный контракт на управление распределительными компаниями с частным оператором, имеющим длительный международный опыт успешного управления электроэнергетической компанией; осуществить переоценку активов всех энергокомпаний, включая электрические и теплоснабжающие предприятия, для полного отражения в тарифах реальных расходов на замещение этих активов, а также провести полный финансовый и технический аудит деятельности электрических компаний. Также предполагается внедрение новой тарифной политики в сфере электро- и теплоэнергетики, предусматривающей доведение тарифов на электро- и теплоэнергию до уровня полного возмещения затрат, а также принятие современной тарифной методологии, позволяющей правильно высчитывать тарифы. Увеличение тарифов окажет влияние на население, особенно на уязвимые слои населения, в связи с чем будут предприняты меры для смягчения рисков. На первоначальном этапе увеличение тарифов может быть осуществлено через введение lifeline тарифов (тариф социальной нормы), и постепенно, с улучшением системы социальной поддержки, планируется перейти на более целевую поддержку уязвимых слоев населения.

Реформа судебной системы

Во все времена беспристрастный и справедливый суд являлся показателем развития государства не только как демократического и правового, но и успешного в экономической и социальной сферах. И от того, как будет работать судебная система, зависит уверенность граждан страны в том, что их права не будут нарушены, а если они нарушены, то будут восстановлены. Все это ставит перед государственными органами, и особенно судебными, задачи формирования независимой и самостоятельной судебной системы, отвечающей требованиям времени и ставящей во главу угла защиту прав, свобод и достоинства гражданина.

На сегодня в этом направлении можно выделить три приоритета. Первый - это отбор судей, второй - это разработка обновленного процессуального законодательства и иных законов, направленных на совершенствование отправления правосудия. И третий - это предстоящее развитие судебной системы Кыргызской Республики до 2017 года.

В рамках первого приоритета, согласно установленным процедурам, Советом по отбору судей Кыргызской Республики проведен отбор на должности судей; с участием Президента Кыргызской Республики и Жогорку Кенеша Кыргызской Республики сформированы и полноценно функционируют Верховный суд Кыргызской Республики, Конституционная палата Верховного суда Кыргызской Республики, все областные и большинство военных судов. В настоящее время вносятся изменения в процессе отбора судей с целью снижения уровня субъективизма и обеспечения принятия на работу наилучших кандидатов.

В рамках второго приоритета, приняты за основу выработанные на основе общественного диалога рекомендации по дальнейшему реформированию судебной системы Кыргызской Республики, для обеспечения согласованных действий государственных органов страны; в рамках реформирования образован и действует Совет по судебной реформе при Президенте Кыргызской Республики. Сформированы и работают 7 экспертных рабочих групп по разработке соответствующих проектов процессуальных и иных законов.

В рамках третьего приоритета, постановлением Правительства от 19 марта 2013 года № 174 одобрен и направлен в Жогорку Кенеш Кыргызской Республики проект Государственной целевой программы «Развитие судебной системы Кыргызской Республики на 2014-2017 годы». Это является значительным достижением, устанавливающим платформу для независимого бюджета судебной системы и предусматривающим постепенное, но существенное увеличение объема ресурсов, выделяемого для данного сектора. С 2015 года начнется дальнейшее поэтапное увеличение размеров финансирования судебной системы на 10 % ежегодно от предыдущего периода (2014 год) и постепенно достигнет планки - в размере 1 % от расходов республиканского бюджета.

Правительством также предпринимаются меры по повышению заработной платы работников судебной системы с целью повышения мотивации и снижения коррупционных проявлений. Приняты постановления «Об условиях оплаты труда государственных и муниципальных служащих Кыргызской Республики» от 28 июня 2013 года № 384 и «Об условиях оплаты труда судей Кыргызской Республики, государственных служащих аппарата Верховного суда Кыргызской Республики, аппарата Конституционной палаты Верховного суда Кыргызской Республики» от 18 октября 2013 года № 560 (введены в действие с 1 октября 2013 года). Так, по сравнению с 2013 годом, в 2014 году работа по реформированию судебной системы проводится с учетом повышения оплаты труда на 51,9 %.

Предприняты шаги по повышению прозрачности судебной системы. Судебным департаментом при Верховном суде Кыргызской Республики

подготовлен отчет по статистическим данным, который выложен на интернет-сайте Совета судей (www.sskr.kg) и на интернет-сайте Верховного суда (sudsistem.kg). Позже, эти статистические данные будут опубликованы в бюллетене Верховного суда Кыргызской Республики и могут применяться для оценки воздействия государственных реформ на функционирование судебной системы.

Развитие частного сектора

Правительство, по-прежнему, ориентировано на поддержку и развитие частного сектора, который должен стать локомотивом национальной экономики. В целях облегчения и обеспечения предсказуемости функционирования частного сектора ведется следующая работа.

Правительством осуществляется реформирование процесса проверок, которые до сегодняшнего дня являлись тяжелым бременем для частного сектора. Министерством экономики Кыргызской Республики 21 августа 2012 года запущен официальный портал по проверкам деятельности субъектов предпринимательства, осуществляемым государственными контролирующими органами (proverka.kg), который представляет собой сочетание Автоматизированной системы управления процессами по проведению проверок субъектов предпринимательства и Информационного портала по вопросам проверок с пилотными государственными контролирующими органами. Правительством также инициировано внесение дополнений в законодательство с целью снижения количества инспекций и внедрения проверок, основанных на рисках. Разработана и внедрена программа «Контр-Про-3» в государственных контролирующих органах Бишкека, предусматривающая фактическую реализацию надзора, основанного на рисках. Процесс формирования базы данных в центральных и региональных отделениях государственных контролирующих органов будет поэтапно осуществлен по мере устранения ограничений технического характера. База данных, управляемая Министерством экономики Кыргызской Республики, является первым проектом межведомственного электронного документооборота в Кыргызской Республике, объединяющим базы данных по проверкам 12 государственных контролирующих органов в единую базу данных, с указанием профиля риска компаний.

Для контролирующих органов и Министерства экономики Кыргызской Республики ведение базы данных упрощает проведение проверок и позволяет:

- сократить необоснованные и излишние проверки государственными контролирующими органами;
- ускорить процесс согласования предписаний на проведение проверок;

- вести аналитическую работу по эффективности проводимых проверок, применению критериев рисков при проведении проверок;
- проверять и исключать дублирующие проверки;
- повысить информированность предпринимателей о проводимых проверках.

Любой предприниматель может на сайте получить информацию о том, когда и какой инспектор планирует прийти на проверку, к какой степени риска относится субъект предпринимательства, как часто его будут проверять. Имеется форум в режиме он-лайн для общения и жалоб предпринимателей на незаконные проверки. Совместно с Международной финансовой корпорацией (МФК – IFC), Правительство работает над внесением изменений в проверочные листы, что снизит бремя проверок на предпринимательство.

Программа «Контр-Про-3» внедрена в следующих 6-ти пилотных государственных контролирующих органах: Государственная инспекция по экологической и технической безопасности при Правительстве Кыргызской Республики, Государственная инспекция по ветеринарной и фитосанитарной безопасности при Правительстве Кыргызской Республики, Социальный фонд Кыргызской Республики, Департамент лекарственного обеспечения и медицинской техники при Министерстве здравоохранения Кыргызской Республики, Департамент драгоценных металлов при Министерстве финансов Кыргызской Республики и Государственная служба регулирования и надзора за финансовым рынком при Правительстве Кыргызской Республики.

Финансовый сектор

В 2013 году банковская система развивалась поступательно, сохраняя устойчивость и потенциал для повышения уровня посредничества и эффективности функционирования. Продолжена работа по совершенствованию качества и эффективности банковского надзора, в том числе посредством: а) усиления надзорной функции Национального банка Кыргызской Республики (НБКР); б) расширения потенциала НБКР в осуществлении надзора и регулирования банковского сектора; в) повышения эффективности своевременного реагирования на ухудшение ситуации и урегулирования ситуаций с проблемными банками; а также г) улучшения регулирующей и надзорной структуры в соответствии с Международными стандартами Базельского комитета.

Национальным банком Кыргызской Республики недавно завершена разработка кредитного регистра. Кредитный регистр позволит НБКР своевременно получать информацию о рисках банков и в значительной мере

будет способствовать оптимизации надзорного процесса, тем самым обеспечивая стабильность финансового сектора. Это лишь первые шаги в создании более широкой интегрированной информационной системы внутри НБКР, которая в значительной мере повысит эффективность регулирования и надзора в финансовом секторе.

Проект Банковского кодекса Кыргызской Республики в настоящее время находится на рассмотрении Жогорку Кенеша Кыргызской Республики. Принятие Банковского кодекса позволит: повысить качество и эффективность норм банковского законодательства на основе системного подхода и использования новейшей мировой практики; закрепить положительную практику сформировавшейся банковской системы и определить пути дальнейшего совершенствования; гармонизировать все составляющие банковского законодательства, в целях исключения разночтений, коллизий и противоречий; уточнить правовой статус участников банковских правоотношений, определить их взаимоотношения, а также основополагающие отношения как внутри банковской системы, так и внешние.

Предпринимаются меры по повышению доверия к финансовому сектору и укреплению системы защиты депозитов. Разработан проект Закона Кыргызской Республики «О внесении изменений и дополнений в Закон Кыргызской Республики «О защите банковских вкладов (депозитов)» (постановление Правительства Кыргызской Республики от 27 сентября 2013 года № 528), который предусматривает: расширение охвата системой защиты депозитов частных предпринимателей; сокращение периода компенсации с 60 до 30 дней и оптимизацию процедур по своевременной выплате компенсаций; расширение объема предоставляемой информации и укрепление сотрудничества с центральным банком; повышение роли Агентства по защите депозитов в издании методологии и рекомендаций по системе защиты депозитов для банков, а также совершенствование механизмов управления в Агентстве по защите депозитов. Правительство активно сотрудничает с Жогорку Кенешем Кыргызской Республики по обеспечению успешного принятия предложенных изменений.

Предлагаемые изменения предусматривают совершенствование законодательства Кыргызской Республики в сфере защиты депозитов и обеспечивают предварительную подготовку к переходу от мандата «Денежной корзины» к мандату «Денежной корзины с дополнительными, но ограниченными полномочиями», который также предусмотрен в проекте Банковского кодекса, находящегося на стадии принятия Жогорку Кенешем. В среднесрочном периоде, предполагается переход системы защиты депозитов к третьему финальному этапу - мандат «Минимизатора рисков», в соответствии с рекомендациями ФСАП-2013.

Корпоративное управление

Эффективный частный сектор требует таких механизмов корпоративного управления, которые продвигают подотчетность и прозрачность для игроков в связи с чем предпринимаются меры в этом направлении. Разработан проект Закона Кыргызской Республики «О внесении изменений и дополнений в Закон Кыргызской Республики «Об акционерных обществах», направленный на повышение ответственности совета директоров акционерных обществ при принятии решений о совершении обществом заинтересованных сделок, а также облегчение процедуры и внесение ясности в процесс получения акционерами дивидендов, и упорядочение процедуры прекращения полномочий членов совета директоров в акционерных обществах.

Кроме того, Государственной службой регулирования и надзора за финансовым рынком при Правительстве Кыргызской Республики в настоящее время разрабатывается проект Программы развития рынка ценных бумаг в Кыргызской Республике на 2014-2017 годы, предусматривающей реализацию мер по совершенствованию корпоративного управления на предприятиях страны, в том числе посредством: а) повышения эффективности корпоративного управления в акционерных обществах и эмитентов публично размещенных/размещаемых ценных бумаг; б) совершенствования требований к листингу ценных бумаг акционерных обществ; в) обеспечения надежности системы регистрации прав на ценные бумаги; и г) укрепления и развития потенциала уполномоченного государственного органа по регулированию рынка ценных бумаг.

Реализация приоритетов Национальной стратегии устойчивого развития Кыргызской Республики на период 2013-2017 годы является делом первостепенной важности для обеспечения устойчивого и успешного будущего страны и реформы, обозначенные в ней, представляют собой последовательную программу, предусматривающую устойчивый экономический рост и снижение уровня бедности в среднесрочной перспективе.

Выражаем надежду, что вопрос о выделении 25 млн долл. США на поддержку программы реформ будет решен в возможно кратчайшие сроки.

С уважением,

Премьер-министр



Дж.К. Оторбаев

ANNEX 3: FUND RELATIONS ANNEX



INTERNATIONAL MONETARY FUND

EXTERNAL
RELATIONS
DEPARTMENT

IMF Executive Board Completes the Fifth Review under the ECF Arrangement for the Kyrgyz Republic and Approves US\$14.6 Million Disbursement

Press Release No. 13/490

December 4, 2013

The Executive Board of the International Monetary Fund (IMF) today completed the fifth review of Kyrgyz Republic's economic performance under the program supported by the Extended Credit Facility (ECF). The Executive Board's decision enables the immediate disbursement of an amount equivalent to SDR 9.514 million (about US\$14.6 million) to the Kyrgyz Republic, bringing total disbursements under the arrangement to SDR 57.08 million (about US\$87.6 million). The Executive Board also considered the Report on the 2013 Financial System Stability Assessment (FSSA).

The Kyrgyz Republic's Extended Credit Facility arrangement was approved by the IMF's Executive Board on June 20, 2011 (see [Press Release No. 11/245](#)) with total access equivalent to SDR 66 million (about US\$102.2 million).

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

“The Kyrgyz economy is recovering strongly after a contraction related to disruptions in gold production in 2012. Fiscal policy has remained prudent despite declining gold prices. Imports for large infrastructure projects are putting pressure on the current account. The medium-term outlook is broadly favorable, but not without challenges, including from gold price volatility and the slowdown in the region.

“The loss of nontax revenues related to the closure of the Manas Transit Center in 2014 will create headwinds for the fiscal consolidation that is needed to reduce vulnerabilities, rebuild policy buffers, and ensure macroeconomic stability and debt sustainability. In the near term, the revenue loss will be offset by grants, revenues from the new oil refinery, and expenditure restraint. Over the medium term, tax system reforms are expected to offset the loss and build a more stable and predictable revenue base. In addition, public financial management reforms will strengthen fiscal governance and transparency, and help to control expenditures.

“Proper implementation of the new operational framework for monetary policy will be instrumental in improving monetary transmission. It will be important for the National Bank to maintain a tight monetary policy stance to mitigate potential inflationary pressures stemming from the strong recovery and rapid credit growth.

“Creating a well-functioning financial sector is key to supporting private sector-led growth. The new banking code, once enacted, will be instrumental to strengthen the bank intervention and resolution process and bolster confidence in the banking system. Developing a strategic plan to strengthen bank supervision and a crisis management framework are important elements to increase stability and resilience of the financial sector. To strengthen the Anti-Money Laundering/Combating the Financing of Terrorism framework, the authorities should adopt the remaining legislative changes.

“Diversification of the economy would help reduce the volatility in growth stemming from potential disruptions in gold production and reduce the persistently high current account deficit. Good governance and sound institutions remain critical to create a level playing field, improve investor confidence, and lay the foundation for strong private sector-led growth.”

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