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IMPLEMENTATION COMPLETION REPORT

KYRGYZ REPUBLIC
REHABILITATION CREDIT
(Credit 2491-KG)

May 30, 1997

Country Operations Division 1
Country Department III
Europe and Central Asia Region

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CURRENCY EQUIVALENTS

After May 10, 1993 -- Currency Unit = Som, 1 Som = 100 Tying

EXCHANGE RATES

Som per US\$1

		End of Period	Average
1995	1st Quarter	10.89	10.84
	2nd Quarter	10.72	10.88
	3rd Quarter	10.72	10.64
	4th Quarter	11.26	11.07
1996	1st Quarter	11.31	11.30
	2nd Quarter	12.26	11.80
	3rd Quarter	12.68	12.31
	4th Quarter	16.90	15.70

WEIGHTS AND MEASURES

Metric System

KYRGYZ REPUBLIC - FISCAL YEAR

January 1 to December 31

ABBREVIATIONS AND ACRONYMS

APEAC	-	Agricultural Privatization and Enterprise Adjustment Credit
DEBRA	-	Debt Resolution Agency
ERRA	-	Enterprise Reform and Resolution Agency
ESAF	-	Enhanced Structural Adjustment Facility
FINSAC	-	Financial Sector Adjustment Credit
FSU	-	Former Soviet Union
FXC	-	Foreign Exchange Component of the Rehabilitation Credit
GDP	-	Gross Domestic Product
IBRD	-	International Bank for Reconstruction and Development
IDA	-	International Development Association
IFC	-	International Finance Corporation
IMF	-	International Monetary Fund
MOF	-	Ministry of Finance
NBK	-	National Bank of Kyrgyzstan
PESAC	-	Privatization and Enterprise Sector Adjustment Credit
PIA	-	Project Implementation Assessment
PIC	-	Pre-identified Imports Component of the Rehabilitation Credit
PIU	-	Project Implementation Unit
SDR	-	Special Drawing Right
SPF	-	State Property Fund
STF	-	Systemic Transformation Facility of the IMF
TA	-	Technical Assistance
TAC	-	Technical Assistance Component of the Rehabilitation Credit
TACIS	-	Technical Assistance for the Commonwealth of Independent States (EU)
UCB	-	Unified Cash Benefit

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IMPLEMENTATION COMPLETION REPORT

KYRGYZ REPUBLIC

REHABILITATION CREDIT (2491-KG)

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IMPLEMENTATION COMPLETION REPORT

KYRGYZ REPUBLIC

REHABILITATION CREDIT (Credit 2491-KG)

Evaluation Summary

Introduction

1. The Rehabilitation Credit of SDR 43.3 million (US\$ 62.3 million equivalent), the first Credit to the Kyrgyz Republic, was approved on May 13, 1993 and declared effective on July 7, 1993. Credit objectives were to support the design and initial implementation of the reform program and to provide foreign exchange for vital imports in order to help arrest the decline of the economy, and thus improve the chances of success of the Government's stabilization effort and the transition to a market-based economy. The Credit also provided funds for technical assistance for formulating and implementing these reforms and building institutional capacity within the Government .

2. The program was designed to serve as a bridge to future structural adjustment operations and in fact, has been succeeded by four adjustment operations. Two of these have been successfully completed (Privatization and Enterprise Sector Adjustment Credit (Cr. 2639-KG) and Agricultural Privatization and Enterprise Adjustment Credit (Cr. 2750-KG). The third operation, the Financial Sector Adjustment Credit (Cr. 2890-KG) is expected to be completed shortly. A Public Sector Resource Management Adjustment Credit was approved on April 16, 1997. Seven investment and technical assistance operations are also currently under implementation (Social Safety Net, Telecommunications, Private Enterprise Support, Health, Sheep and Wool, Power and District Heat, and Financial Sector Technical Assistance).

Project Origin and Objectives

3. The Kyrgyz Republic experienced an unprecedented decline in real incomes from 1991 to 1993 triggered by the breakdown of inter republican trade and payments arrangements associated with the breakup of the FSU. The Kyrgyz Republic was more affected than many of the other republics owing to its dependence on imported oil and gas, geographical isolation and lack of immediately exploitable resources. Markets for specialized Kyrgyz products were lost, transfers from the Soviet budget ceased and formerly subsidized prices for imported energy were adjusted upward toward world prices. The rapid rise in energy prices had led to a terms of trade loss of over 40% in 1993. Output and trade contracted sharply and many enterprises, cut off from their customary markets, were on the verge of collapse. Real GDP declined by about 45% between 1991 and 1993 and inflation soared, reaching four digit levels in 1992 and 1993. The Kyrgyz authorities responded to the economic crisis by embarking on an ambitious program of macroeconomic stabilization to reduce inflation, and systemic reforms designed to bring about the transition to a market economy. IDA supported the initiation of a dialogue on the reform agenda through the preparation of a comprehensive Country Economic Report in 1992.

4. The exigencies and uncertainties of the times demanded a quick, flexible response. The Rehabilitation Credit represents the effort of the International Development Association (IDA), with strong bilateral support, to respond rapidly and positively to the Government's efforts. The

Rehabilitation Credit was also designed in conjunction with the first Systemic Transformation Facility (STF) supported by the IMF. The Credit had three components: pre-identified imports (PIC), reimbursement of foreign exchange payments for other qualified imports (FXC); and technical assistance (TAC). It was intended that the PIC would be used for a limited number of large orders in critical areas, and a third of the foreign exchange provided would be auctioned by the central bank (NBK) to help develop an inter-bank market for convertible currency. The Government's Memorandum of Economic Reform Policies (MERP) did not contain a comprehensive set of time-bound actions. Rather, it set forth a framework outlining the Government's initial economic policy orientation and intentions. The Rehabilitation Credit was therefore designed as an umbrella operation for the design and continuation of the overall reform program.

Implementation Experience and Results

5. The Project successfully achieved its objectives and proved to be a flexible, positive instrument of support for the Kyrgyz reform program initiation. The policy program (outlined in the Project Implementation Assessment --PIA, Table 5) has proven highly satisfactory and results are beginning to be felt. There has been progress toward closing the fiscal gap (PIA, paras. 8-10), restraining monetary expansion and reducing inflation (PIA, para. 11), and achieving a sustainable balance of payments situation (PIA, para 12). The ultimate test of these stabilization and adjustment efforts however, is its effect on output and incomes. In this regard, recent performance is encouraging: after three years of sharply declining production, the economy began to recover in 1996. Preliminary data suggest that GDP grew by 5.6% in 1996, as a result of good weather, a turnaround in industrial production and growing public and private investment. It is clear, however, that poverty has increased substantially and further measures are needed to improve targeting, undertake selective interventions and bolster the social safety net (PIA, para. 21).

6. During the three and a half years the Project was under implementation, the structural reform program articulated initially under the Rehabilitation Credit was expanded, deepened and closely monitored under succeeding IDA-financed credits. Key achievements (outlined in PIA, Table 5) include: by February 1997, of the approximately 1,300 state-owned medium to large-scale enterprises included in the mass privatization program, 993 had gone through coupon auction; of these 804 were fully or majority privatized. Most of the remaining enterprises are scheduled for privatization under the 1996/97 privatization plan. Under the Enterprise Reform and Resolution Agency (ERRA), of the 29 large loss making state owned enterprises, ultimately four were liquidated, four left the program, fifteen were sold and the sales process is continuing for six (PIA, paras. 14-17). Substantial progress has been made toward modernizing Kyrgyz commercial laws to meet the demands of private investors.

7. The Kyrgyz Republic has made substantial progress toward dismantling state control over agriculture. Prices for all agricultural commodities have been liberalized, the system of state orders has been dismantled, and by February 1996 all export taxes on agricultural commodities had been eliminated. Ownership shares and land use rights in most state farms and collectives have been distributed to their workers. Restrictions on maximum farm size were abolished and land use rights were increased to 99 years. Most state and collective farms have been transferred into joint stock companies and about one third of the land under cultivation has been converted into numerous small private farms. The state monopoly on grain purchase and bread production and distribution has been ended, and privatization of the state bread complex is almost complete. (PIA, paras. 18-19). In the financial sector, real interest rates have reached positive levels, capital requirements and prudential regulations have been adjusted, and the NBK has effectively strengthened its supervisory capacity. A comprehensive financial sector reform, comprising downsizing, financial restructuring of insolvent state-owned banks, the

establishment of a temporary debt resolution agency and the creation of a regulatory and supervisory framework for non-bank financial institutions is under implementation (PIA, paras. 20-21). Prospects for the sustainability of reform effort are strong. However, much remains to be done in strengthening the fiscal system, building the legal, administrative and institutional framework required by a dynamic market economy and, building or rehabilitating vital physical infrastructure.

8. Implementation of the PIC component was fully satisfactory. As project preparation progressed, country conditions and needs were changing rapidly. The need to have a program in place as early as possible meant that some of the detailed implementation arrangements had to be worked out during implementation rather than during the design phase. Both IDA and the Government managed the mesh of evolving program needs and development objectives in a positive, pragmatic manner and the resultant project impact was strong. Among the practical problems encountered were the unfamiliarity of sectoral officials with the principles of competitive international procurement and limited technical knowledge which slightly delayed the preparation of bidding documents. Procedures governing how goods would be passed on to or paid for by end-users were developed during implementation rather than in the design phase, posing some initial confusion among beneficiaries. Frequent IDA staff turnover and multiple sub-task management responsibilities also added additional complexity to supervision arrangements. Nevertheless, the component successfully achieved its objectives. Virtually all of the participating ministries and agencies have indicated that the goods received were timely and vital to maintaining the momentum of the reform program in the early years. However, in retrospect the design of the PIC component proved more complex and time intensive than originally envisaged (PIA, paras. 25-27).

9. The broad goals of the TAC were achieved -- the provision of quality policy and technical advice critical to the reform process. Of particular importance was the advisory support for the enterprise restructuring effort. The studies and analytical work financed was in general of good quality. TA requirements evolved considerably during project and the final consultancy services financed reflected these changing circumstances. These changes resulted from three primary factors: first, the international donor community proved highly responsive to needs of the country's fast paced reform program, leading to a heavy influx of grant funding for TA. This additional grant assistance in some cases paralleled or duplicated the needs envisaged under the Rehabilitation Credit, thus TAC activities were modified. Second, for some of the proposed work, the timing of the assistance was premature. Involved ministries and agencies had not had time to develop sufficient understanding of the problems or ownership of the task. Finally, as the reform agenda deepened, new and more specific technical assistance needs emerged and the TAC proved to be a highly effective vehicle for meeting these needs.

10. Institutional capacity gains were substantial. The experience under the TAC prompted the Government to take steps to improve overall planning and management of TA (PIA, paras. 30-31). Further, the country gained considerable expertise in international procurement policies and practices through TAC implementation, as Project Implementation Unit staff assumed new levels of responsibility within the Government and internationally. Ultimately, a semi-autonomous Consultative Agency for International Procurement was created, building directly on Rehabilitation Credit implementation experience. TAC activities and impact are described in the PIA, Table 7.

11. The FXC provided resources to pay for public and private sector imports at an exchange rate determined through auction sale in the interbank market. Some received from sale of the foreign exchange were used as a source of non-inflationary finance of the budget. A number of reallocations to the FXC were made throughout project implementation. The provision of foreign exchange at the critical period surrounding the introduction of the new currency was of major assistance to the

stabilization effort. The rapid injection of foreign exchange helped to establish public confidence and brake inflationary expectations (PIA, para. 29).

12. Prospects for the sustainability remain strong. Expanding incomes and employment will make it easier to complete enterprise restructuring and to raise fiscal revenues needed to expand social and economic infrastructure and strengthen the social safety net. Commitment to reform has not wavered even when GDP decline was in double digits, as evidenced by successful implementation of successor adjustment operations focusing on privatization, agricultural and financial sector and budgetary reforms. However, much remains to be done in strengthening the fiscal system and fostering the legal, administrative and institutional framework required by a dynamic market economy.

Summary of Findings, Future Operations and Key Lessons Learned

13. The strategy of using the Rehabilitation Credit as an umbrella operation for initiating a comprehensive reform program to be followed by subsequent adjustment operations worked well, as evidenced by the approval of four follow-on operations. The preparation of a Social Sector Adjustment operation is now underway. Other operations in various stages of preparation and discussion emphasize further support for agriculture and rural development (Rural Finance, Agriculture Support Services, Irrigation, Real Estate Registration, Water Supply and Sanitation and a People's Initiative Fund). Among the key lessons learned under the Rehabilitation Credit are:

14. Government ownership and commitment is the key to success. The rapid progress of reform in the case of the Kyrgyz Republic is in no small measure due to the fact that the Government understood the process of adjustment and had made a rapid beginning, even prior to project approval. Further, the authorities have understood that a successful reform demands far more than "stroke of the pen" measures, and they have stayed the course over time, under difficult circumstances. In the instances where the potential benefits of TA were not well understood or embraced at the outset, its utilization and management were less effective. The role of Goskominvest in overseeing the policy program and project implementation was of particular importance.

15. Project design and implementation arrangements should be simple and clear at the outset, however, flexibility is critical. While the goals of this project were clear, institutional and implementation arrangements were less well-defined, owing to the urgent need to have a program in place as early as possible. This meant that many of the details of implementation had to be worked out as the program evolved. The flexible and pragmatic approach adopted by the Kyrgyz and IDA worked well and, despite a number of practical obstacles, enabled the project to achieve its stated objectives.

16. Managerial responsibility and lines of communication within IDA and with the Borrower should be clear and continuity stressed. To the extent feasible, task managers should remain with a project from design through implementation and assignment of sub-task manager authority should be minimized. For the future, complex multi-sectoral operations of this nature should be managed from the field, both to reduce confused signals and to accelerate problem solving.

IMPLEMENTATION COMPLETION REPORT

KYRGYZ REPUBLIC: REHABILITATION CREDIT (CR 2491-KG)

Project Implementation Assessment

1. The Rehabilitation Credit of SDR 43.3 million (US\$ 62.3 million equivalent) was approved on May 13, 1993 and declared effective on July 7, 1993. The project closed December 31, 1996 and final disbursements were effected in April 1997. Parallel financing was provided by the Government of the Netherlands, which provided a grant of US\$5 million to finance agricultural inputs and veterinary medicines. The Government of the Swiss Confederation provided a grant of Sfr 14 million for critical inputs in the energy sector and the Japanese Government made parallel financing equivalent to US\$ 60 million available for pre-identified imports, technical assistance and foreign exchange (Table 8B).

A. Project Origin and Objectives

2. Macroeconomic Context. The Kyrgyz Republic experienced an unprecedented decline in real incomes from 1991 to 1993 triggered by the breakdown of inter republican trade and payments arrangements associated with the breakup of the FSU. The Kyrgyz Republic was more affected than many other republics of the FSU owing to its dependence on imported oil and gas, geographical isolation and lack of immediately exploitable resources. Markets for specialized Kyrgyz products were lost, transfers from the Soviet budget ceased and formerly subsidized prices for imported energy were adjusted upward toward world prices. The rapid rise in energy prices had led to a terms of trade loss of over 40% in 1993. Output and trade contracted sharply and many enterprises, cut off from their customary markets, were on the verge of collapse. Real GDP declined by about 45% between 1991 and 1993 and inflation soared, reaching four digit levels in 1992 and 1993.

3. The Kyrgyz authorities responded to the economic crisis by embarking on a program of macroeconomic stabilization to reduce inflation, and systemic reforms designed to bring about the transition to a market economy. Despite the difficult circumstances, the Kyrgyz Republic began the process of stabilization and reform in 1992, becoming the first republic of the FSU to introduce reforms designed to reduce the role of the state and decontrol prices. It introduced revenue and expenditure measures to reduce fiscal imbalance and stabilize the economy. A VAT was enacted and personal and corporate income taxes and excises were revised, eliminating most tax privileges and exemptions. (This VAT was essentially a turnover tax that has little relation to a modern invoice-based, input crediting VAT.) The monetary system was strengthened by adopting new central and commercial banking laws, and establishing a two tier banking system with the National Bank holding enhanced supervisory powers at the apex. The Government also began to adopt a legal framework appropriate to a market economy; and to set the stage for privatization. By the end of 1992 the Parliament had adopted a Concept Note outlining modalities for divestiture of state assets. Rents had been liberalized on private housing, barriers to entry into agricultural processing and marketing lifted, and the drafting of a new Constitution was in progress.

4. Project Origin. The exigencies and uncertainties of the times demanded a quick, flexible response. As a first step, IDA prepared a comprehensive Country Economic Memorandum in 1992 which provided the underpinning for dialogue on the reform effort. The Rehabilitation Credit represents the effort of the International Development Association (IDA), with strong bilateral support, to respond rapidly and positively to the Government's efforts. The framework for the economic reform program is

12. Achieving a Sustainable Balance of Payments Situation. As part of the stabilization program, the Government established a foreign exchange auction market, a floating exchange rate and a fully liberalized foreign exchange regime with no restrictions on capital or current transactions. The trade regime has been liberalized; non-tariff barriers were removed and export taxes have been eliminated on all goods. Kyrgyzstan's external accounts reflect encouraging signs associated with renewed economic growth. After stagnating in 1993-94, external trade expanded rapidly in 1995 and 1996. Exports rose by about 20% in 1995, led by export of machinery and food products to the CIS, scrap metal, wool and cotton to China. Imports rose by almost 50%, partly as a result of US\$ 110 million in imports for the Kumtor gold project. Both imports and exports rose by almost 30% in 1996. The current account deficit has risen steadily, reaching US\$ 361 million in 1996. A good part of the deficit was financed by disbursements of official loans which (excluding the ESAF) reached US\$ 166 million in 1996. The bulk of this was on concessional terms, mostly from IDA, ADB, EBRD and OECF.

13. Reviving Economic Growth. The ultimate test of the success of stabilization and adjustment efforts is its effect on output and incomes. In this regard, recent performance is encouraging: after three years of sharply declining production, the economy began to recover in 1996. Preliminary data suggest that GDP grew by 5.6% in 1996, as a result of good weather, a turnaround in industrial production and growing public and private investment. It is clear, however, that poverty has increased: preliminary results of a 1996 survey indicate that the percentage of households in poverty may have risen from about a third in 1993 to just under half in 1996.

Implementing Structural Reform

14. Progress in Privatization and Enterprise Reform. The Government is implementing a multi-year privatization program aimed at divesting all its commercially-oriented enterprises. The privatization program began with the transfer of the housing stock to the occupants in 1991-93 and the cash sale of small businesses. Initially, the majority of shares in some enterprises were transferred without charge to workers' collectives. As part of the privatization process, the remaining state owned enterprises are divesting all social assets. A study to assess the fiscal implications of divestiture and limit the disruption of social services has been carried out. By the end of 1994, the Government had essentially completed privatization 4,000 small (less than 100 employees) shops and services through a series of cash auctions administered by the State Property Fund.

15. In December 1993, a Privatization Law was adopted aimed at divesting all productive and social assets through a "mass privatization" scheme aimed at ensuring a wider distribution of ownership of medium and large scale enterprises (100 or more employees) through use of coupon and cash auctions. Under this law, the new divestiture strategy involved: (i) cash auction of small enterprises; (ii) sale of state owned shares in partially-privatized enterprise through coupon and cash auctions; and (iii) privatization of medium and large scale enterprises through free distribution of 5% of their shares to workers and managers, sale of 25% through coupon auctions, and the cash sale of up to 70% to investors on the basis of competing privatization proposals. All commercially viable small-scale enterprises have been privatized. By February 1997, of the approximately 1,300 state-owned medium- to large-scale enterprises included in the mass privatization program, 993 had gone through coupon auction; of these 804 were fully or majority privatized. Most of the remaining enterprises are scheduled for privatization under the 1996/97 privatization plan.

As a first step, they will be put through coupon auction during the year. The disposition of the State's remaining shares would be governed by each enterprise's individual privatization program.

17. The Government established an Enterprise Reform and Resolution Agency, ERRA, in May 1994, to deal with restructuring or liquidating 29 large loss-making state-owned enterprises. These 29 enterprises were placed in a care and management program (subsequently four were removed from the program). Their access to credit and budget subsidies were cut off and most employees were placed on administrative leave at reduced salaries. Diagnostic studies were undertaken (assisted by consultants financed out of TAC funds). Final disposition of these enterprises is being supported by succeeding Bank adjustment operations. Following diagnosis of their prospects, four of the enterprises were liquidated and the others have been downsized and restructured financially. Fifteen of the companies have been sold and the sales process is continuing for six others.

18. Accelerating Development of Market Agriculture. The Government is establishing an enabling environment for private agriculture by: (i) developing land markets as the basis for agrarian reform; (ii) demonopolizing and privatizing the large state-owned conglomerates that dominated agricultural marketing and processing; and, (iii) completely eliminating remaining price and trade restrictions and local government interference in commercial decisions. The challenges facing the sector are however, formidable. While market pricing and incentives were introduced early in the reform program, supporting services and infrastructure (an efficient rural credit delivery system, privatized distribution and marketing systems and extension services) are still being developed.

19. The Kyrgyz Republic has, nonetheless, made substantial progress toward dismantling state control over agriculture and reforming the sector along market economy lines. Prices for all agricultural commodities have been liberalized, the system of state orders has been dismantled, and by February 1996 all export taxes on agricultural commodities had been eliminated. Ownership shares and land use rights in most state farms and collectives have been distributed to their workers. Restrictions on maximum farm size were abolished, land use rights were increased to 99 years, and a Land Registration Act establishing a unified system is being considered by Parliament. Most state and collective farms have been transferred into joint stock companies and about one third of the land under cultivation has been converted into numerous small private farms. The state monopoly on grain purchase and on bread production and distribution has been ended, and privatization of the state bread complex is almost complete.

20. Strengthening the Financial Sector. The Government has begun to take steps to strengthen the legal and institutional framework of the financial system. New central bank and commercial bank laws were approved in 1992. A new national currency, the Som, was introduced in May 1993. The foreign exchange market has been fully liberalized and a number of market-based policy instruments have been introduced.

21. Prompted by concerns about the solvency of the banking system, the national Bank of Kyrgyzstan (NBK) commissioned an external audit of four big specialized banks, and undertook a comprehensive review of other commercial banks. The review found that more than half of the commercial banks had negative net worth and that two thirds of loans were non performing at the end of 1995. Therefore in late 1995, NBK began a comprehensive financial sector reform and restructuring program. It adopted regulations requiring that provision be made for bad loans, conducted on-sight inspections of all banks and significantly strengthened its banking supervision department. It closed the worst performing banks and put other weak banks under direct supervision. In 1996, as part of the FINSAC credit, the NBK closed the two largest commercial banks (the only remaining state banks), and created a temporary Debt Resolution Agency (DEBRA) to expedite collection or write-off of non

performing loans in the portfolios of the liquidated banks. NBK initiated a program to recapitalize other large banks and strengthen bank supervision and prudential regulation. The National Bank also established a savings institution to preserve a payments mechanism after the closure of bank branches in rural areas. As part of the reform program, a new set of financial legislation is being prepared or enacted while existing laws are being reviewed and revised. As a result of these Government efforts, a small core of sound banks has emerged and public confidence in banks is growing.

Rationalizing the Social Safety Net

22. In an effort to strengthen the social safety net and make it more effective, the Government consolidated the former family allowance, bread compensation, and other special payments into a uniform cash benefit for families with incomes below the minimum wage (UCB). Three types of cash transfers are now provided by the current social safety net: (i) social insurance, including pensions, short-term illness and unemployment; (ii) universal benefits, including military pensions and family benefits and; (iii) means-tested benefits covering the very poor. The Social Fund is the key administrative unit for the social safety net, collecting revenues and making payments. The Social Fund has been in deficit since 1994. Revenue collections have consistently fallen short of estimates given the financial disarray of state owned enterprises. Compliance from new, and newly privatized enterprises has been weak. However, the Government has made a strong effort and recent payments on pensions and social benefits arrears have been reduced to one month. The Government intends to adopt a pension reform plan in 1997, rationalizing pension benefits. A baseline household survey was undertaken in 1993. Two poverty monitoring surveys have been undertaken since 1996 and two more are planned.

C. Implementation Record and Major Factors Affecting the Project

23. Implementation of the policy program was very strong, as discussed above. Implementation of the pre-identified imports (PIC) and technical assistance (TAC) components was fully satisfactory, despite complex institutional arrangements. On the Kyrgyz side, responsibility for project management resided in the newly formed Project Implementation Unit (PIU), located in Goskominvest, the State Committee for Foreign Investments and Economic Assistance. For IDA's part, the Country Operation Department held overall responsibility for project management with sector specialists serving as sub-task managers for PIC and TAC components. Effective coordination was hampered somewhat by frequent IDA staff turnover and multiple managerial responsibilities. There were at least five IDA task managers and numerous sub-task managers throughout the course of project implementation. Similarly, the PIU directorship changed hands four times and some staff turnover was experienced. Communications between Bank task and sub-task managers, consultants, the PIU, line ministries and end-users were frequently confusing.

24. The implementation schedule for the pre-identified imports component was unrealistic -- anticipated procurement deliveries were expected within six months of effectiveness. This scheduling did not take into account the potential difficulties in reaching agreement on import requirements, preparing technical specifications and bidding documents and designing delivery arrangements. Implementation of both the PIC and TAC components thus proved far more difficult and time consuming than anticipated. In the end, considerably fewer project proceeds were used for pre-identified imports than had been planned. Expenditures under the TAC were in approximately the amount foreseen, however, the composition was quite different reflecting the evolving needs of the reform program. Nevertheless, despite the problems and delays that arose in implementation, project closing was delayed only six months, until end-December 1996, to accommodate the completion of long term advisory services. Final payments were effected within four months of Credit Closing.

Rehabilitation Credit: Allocated and Actual Use of Funds

Category	(expressed in million US\$)	
	Allocated	Actual
Pre-identified import component (PIC)	33.0	14.4
Foreign exchange component (FMC)	20.0	41.0
Technical assistance component (TAC)	7.0	6.9
Total	60.0	62.3

Note: The differences in the totals reflect changes in the dollar / SDR rate

25. Implementation Experience under the Pre-identified Imports Component. The PIC component successfully achieved its objectives of providing priority imports necessary to maintain production and services. Implementation proved more complex than envisaged as this was the first experience for Kyrgyz officials in dealing with IDA and country conditions and needs were changing rapidly. Lists of goods to be imported under the PIC were initially determined by discussions between Bank staff, potential end-user agencies and the procurement advisors hired under the Credit. The quality and thoroughness of these discussions varied from sector to sector, with infrastructure units faring best and agriculture, the most complex. Proposed lists were negotiated between end-user ministries and the PIU, with dollar amounts allocated among end-user ministries and agencies.

26. Preparation of bidding documents proved difficult because of limited technical knowledge within sectoral ministries and agencies reflecting past centralized procurement practices in which goods were ordered by source name and number. Translating equipment lists and technical specifications into English, refining them and then retranslating them into Russian proved difficult and time consuming.

Rehabilitation Credit: Allocated and Actual Use of Pre-identified Imports Component, by sector

Sector	Amount (million US\$)	
	Proposed	Actual
Agriculture	9.5	2.4
Irrigation	1.0	1.1
Communications	5.5	0.6
Energy	9.5	4.2
Transport	4.5	0.7
Health	1.5	0.1
Environment	1.5	0.0
Other	0.0	5.3
Total	33.0	14.4

Note: Other consists of US\$ 0.345 million for computer equipment for the Legal Department of the President's Office, Treasury Department and Ministry of Finance and US\$ 5.001 million for natural gas imports by Kyrgyzgas.

27. There was also confusion about costs as end-users had become used to paying non-market prices and some did not realize that they would have to pay for the goods when they became available. As procedures were clarified, expressed priorities began to change. Mechanisms had to be developed for budgetary credit to ministries and credits from ministries to end users so they had resources to purchase goods. Agreements were reached between the Ministry of Finance and sectoral ministries/end users (these agreements were subsequently renegotiated in some instances with newly privatized joint stock companies) for repayments to the budget. Repayments are just beginning. In the agricultural sector

farmers experienced difficulties in paying market prices and agreements were reached to allow a 50 percent subsidy and provision of credit in kind. Throughout the PIC procurement process, beneficiary ministries/end-users sometimes decided the goods were no longer of highest priority, did not match their current needs or they simply did not want the particular items recommended under the bidding exercises. Again, the agricultural sector proved most complex, as demand did not always match cropping patterns which had begun to respond to market signals. Of the 82 multi-sector procurement exercises initiated at project launch, only 50 proceeded to contract award.

28. In retrospect, it appears that the PIC component, although well designed to respond to the exigencies of the times, proved complex to administer and is unlikely to have ultimately affected the overall composition of imports. Moreover, the component design risked sending the wrong signals to the Government about the allocation of foreign exchange for specific imports. This ultimately provided impetus for accelerating the development of the auctions under the foreign exchange component.

29. Foreign Exchange Component. This component achieved its objectives. It provided foreign exchange to pay for imports by the public and private sectors at an exchange rate determined through auction sale in the interbank market. Som received from sale of the foreign exchange were used as a source of non-inflationary finance of the budget. Sale of foreign exchange helped underpin the Som shortly after its adoption as the domestic currency, helping to establish public confidence. About three fourths of the funds were received in 1993-94. Ultimately, approximately US\$41 million was auctioned, as a result of transfer of funds from the PIC reflecting need for sustained financial flows.

30. Technical Assistance Component. The broad goals of the TAC were achieved, that is, providing timely policy and technical advice critical to the reform process. The studies were in general of good quality and most were produced on time. The flexible approach to TA within the project enabled many activities to be financed that might not otherwise have been possible and facilitated advancing the sequenced program of reforms. As implementation progressed, the Government internalized the experiences garnered under the component and recognized the importance of well planned and managed TA. On its own initiative, Goskominvest prepared a paper on the effective utilization of technical assistance which was the subject of a meeting of international donors in Bishkek in November 1995.

31. The TAC component was originally intended to finance advisory services for deepening the reform program in a number of key areas, particularly: enterprise restructuring/liquidation and privatization; agriculture sector revitalization; mining sector development; financial sector reform; the development of a legal framework and enabling environment for private sector investment; and health and pharmaceutical sector policies. TA requirements evolved considerably during project and the final consultancy services provided reflected these changes (Table 7). These changes resulted from three primary factors: first, as the project took shape, the international donor community proved highly responsive to needs of the country's fast paced reform program, leading to a heavy influx of grant funding for TA. This additional assistance in some cases paralleled or duplicated the needs envisaged under the Rehabilitation Credit, thus TAC activities were modified to allow the Government to optimize use of grant financing. Second, for some of the proposed work, the timing of the assistance was premature. Involved ministries and agencies had not had time to develop sufficient understanding of the problems and ownership of the task. Finally, as the Government refined and deepened its own reform agenda, new and more specific technical assistance needs emerged. Policymakers developed a better sense of timing and sequencing of reforms and the TAC component proved a flexible vehicle for meeting some of these needs. Ultimately, the majority of the technical assistance funds were redirected into consultancies on the enterprise restructuring and privatization program and diagnostic studies of the ERRA enterprises. The component also funded some critical technology requirements for core economic

ministries, consultancy services to manage the procurement of this Credit and other internationally financed projects and selected training and auditing services.

D. Project Sustainability

32. Prospects for the sustainability of reform are strong. Expanding incomes and employment will make it easier to complete enterprise restructuring and to raise fiscal revenues needed to expand social and economic infrastructure and strengthen the social safety net. The Kyrgyz Government's commitment to reform was strong even when GDP decline was in double digits and has remained firm, as evidenced by successful implementation of successor adjustment operations. The prognosis is good: inflation is abating and national product is increasing. The Government's popular mandate has been renewed and its commitment to reform has been maintained. Successor projects for enterprise, agricultural and financial sector adjustment are being implemented satisfactorily, and the IMF has provided continuing support. However, much remains to be done in strengthening the fiscal system, building the legal, administrative and institutional framework required by a dynamic market economy, and building or rehabilitating vital physical infrastructure. IDA and other donors remain committed to assisting the Government in these efforts.

E. IDA Performance

33. IDA's performance proved responsive, flexible and pragmatic as the needs of the time dictated. IDA, through this project, played a vital role in supporting the critical early phase of stabilization and adjustment through the provision of foreign exchange, which facilitated successful introduction of the new currency and helped stem the decline of domestic product. The policy advice surrounding the design and implementation of this and subsequent operations helped to crystallize Government thinking and the conversion of principles into programs and actions. This program served as the underpinning for discussions among the newly formed Consultative Group and acted as catalyst for attracting additional resources (Table 8B). In recognition of the rapidly evolving country situation, IDA and the Government worked collaboratively throughout implementation to ensure that program development objectives were met, while pragmatic solutions to implementation problems were found. The project was supervised at regular intervals but consistency in supervision suffered from frequent changes in task/sub-task management responsibilities. Earlier establishment of a Resident Mission presence and delegation of primary responsibility to the field might have facilitated implementation.

F. Borrower Performance

34. The Borrower's performance was fully satisfactory, particularly with respect to the implementation of the policy program which was overseen by Goskominvest. Procurement arrangements were well handled by the PIU, which acquired considerable institutional expertise, leading to the eventual creation of a semi-autonomous Consultative Agency on International Procurement. Many PIU staff have acquired managerial, technical, financial and procurement skills that have been deployed both within the Government and internationally. While implementation of the overall reform program progressed well, inter-ministerial coordination of the PIC activities and the technical assistance program also proved challenging for the PIU staff. In the later years of implementation, the PIU was also affected by several changes in unit leadership and overall organizational changes within the government.

G. Assessment of Outcome

35. The Kyrgyz Rehabilitation Credit was a pioneer operation, the first of its kind in the FSU. The experience gained through its design and implementation has been applied in the development of similar

operations. The policy program initiated under the project has proven highly satisfactory. Implementation of the Government's stabilization and reform program has been strong, and positive results are beginning to be seen. The project contributed to the successful outcome by providing foreign exchange at a critical time, helping the Government to formulate its program, and providing technical assistance in critical areas. Implementation of the program has contributed to a decline of inflationary pressures and a renewal of growth. Although the PIC and TAC components proved more difficult to administer and took longer than anticipated, these problems did not seriously affect the substantial, positive impact of the project itself. The project has had a strong institutional building impact, through the expertise gained in management of technical assistance and aid coordination, generally, and in international procurement, specifically.

H. Future Operations

36. The strategy of using the Rehabilitation Credit as an umbrella operation for initiating a comprehensive reform program to be followed by subsequent adjustment operations worked well. This Credit was followed by four adjustment operation: PESAC (Cr. 2639-KG, SDR 42.5 million) approved in June 1994; APEAC (Cr. 2750-KG, SDR 28.6 million), approved in June 1995; and FINSAC (Cr 2890-KG, SDR 31.2 million) approved in May 1996, nearing completion. The PESAC and APEAC operations were concluded successfully in June 1994 and June 1995. The FINSAC operation is nearing completion. A Public Sector Resource Management Adjustment Credit was approved in April 1997 and preparation of a Social Sector Adjustment operation is now underway. Many sector reforms initiated under the Rehabilitation program have received support through the seven ongoing investment/TA operations.

I. Key Lessons Learned

37. **Government ownership and commitment is the key to success.** The rapid progress of reform in the case of Kyrgyzstan is in no small measure due to the fact that the Government understood the process of adjustment and had made a rapid beginning, even before approval of the project. In the instances where the potential benefits of TA were not well understood or embraced at the outset, its utilization and management were less effective. The role of Goskominvest as a central, influential and capable coordinating body was critical to project success.

38. **Project design and implementation arrangements should be simple and clear at the outset but flexibility is critical.** While the goals of this project were clear, the urgencies of timing were such that institutional and implementation arrangements were not fully defined at project launch. The operation comprised three very different components, each with its own objectives and requisites for successful implementation. The project implementation schedule underestimated the time needed to implement the PIC, particularly given the inexperience of the Borrower, complexity of the task, and multiple participants in the process. Inclusion of a technical assistance component also increased the complexity of supervision. In this case, it would probably would have been more efficient to have made a separate credit for technical assistance limited to enterprise privatization and governance with a single task manager. Nevertheless, the flexibility of the design and pragmatism during implementation resulted in a successful operation.

39. **Managerial responsibility and lines of communication within IDA and with the Borrower should be clear and continuity stressed.** To the extent feasible, task managers should remain with a project from design through implementation and assignation of sub-task manager authority should be minimized. For the future, complex multi-sectoral operations of this nature should be managed from the field, both to reduce confused signals and to accelerate problem solving.

Statistical Tables

Table 1:	Summary of Assessments
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* Tables 6 and 9 are not included because they are not applicable to the Rehabilitation Credit. Table 11 is not included because there have been no reported instances of non-compliance with Operational Manual Statements.

Table 1: Summary of Assessments

<u>A. Achievement of Objectives</u>	<u>Substantial</u>	<u>Partial</u>	<u>Negligible</u>	<u>Not applicable</u>
Macro Policies	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Sector Policies	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Financial Objectives	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Institutional Development	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Physical Objectives	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Poverty Reduction	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Gender Issues	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Other Social Objectives	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Environmental Objectives	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Public Sector Management	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Private Sector Development	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Other (specify)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
<u>B. Project Sustainability</u>	<u>Likely</u>		<u>Unlikely</u>	<u>Uncertain</u>
	<input checked="" type="checkbox"/>		<input type="checkbox"/>	<input type="checkbox"/>
<u>C. Bank Performance</u>	<u>Highly satisfactory</u>		<u>Satisfactory</u>	<u>Deficient</u>
Identification	<input type="checkbox"/>		<input checked="" type="checkbox"/>	<input type="checkbox"/>
Preparation Assistance	<input type="checkbox"/>		<input checked="" type="checkbox"/>	<input type="checkbox"/>
Appraisal	<input type="checkbox"/>		<input checked="" type="checkbox"/>	<input type="checkbox"/>
Supervision	<input type="checkbox"/>		<input checked="" type="checkbox"/> *	<input type="checkbox"/>

<u>D. Borrower Performance</u>	<u>Highly satisfactory</u>	<u>Satisfactory</u>	<u>Deficient</u>
Preparation	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>
Implementation	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>
Covenant Compliance	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>
Operation (if applicable)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

<u>E. Assessment of Outcome</u>	<u>Highly satisfactory</u>	<u>Satisfactory</u>	<u>Unsatisfactory</u>	<u>Highly unsatisfactory</u>
Policy	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
PIC/TAC	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

* The high turnover of Bank task managers during preparation and implementation and multiple sub-task managers resulted in a lack of continuity. The arrangements on the Government side were also complicated by the large number of sectoral ministries/agencies involved and managerial and staff turnover in the PIU.

Table 2: Related Bank Credits

Credit title	Purpose	Year of approval	Status
Following operations:			
1. PESAC Enterprise Reform & Privatization	Support for enterprise restructuring and the 1994-95 privatization program	FY94	completed 6/95
2. APEAC Continuation of Privatization Program and Agricultural Sector Restructuring	Support for restructuring/privatization of the agricultural sector parastatals and continuation of the 1995-96 privatization program	FY95	completed 6/96
3. FINSAC Financial Sector Reform & Continuation of Privatization Program	Financial sector reform and 1996-97 privatization program	FY96	2nd tranche review anticipated mid 1997
4. PSRMAC Reform of Budget Preparation & Intergovernmental Fiscal Affairs	Reform of intergovernmental finances and budgeting systems	FY97	approved 4/97, under implementation
5. SOSAC Social Sector Adjustment	Reforms in pensions, social assistance and sectoral financing (details to be discussed)	FY98	under preparation

Table 3: Project Timetable

Steps in Project Cycle	Date Planned	Actual Date/ Latest Estimate
Identification (Executive Project Summary)	04/92	04/92
Preparation	06/92	06/92
Appraisal	10/92	10/92
Negotiations	04/93	04/93
Board Presentation	05/93	05/93
Signing	06/93	05/93
Effectiveness	06/93	07/93
Project Completion	06/96	12/96
Loan Closing	06/96	12/96

Table 4: Loan/Credit Disbursements: Estimated, Actual and Cumulative
(US\$ million equivalent)

	FY93	FY94	FY95	FY96	FY97
Appraisal estimate	10.00	45.00	3.00	2.00	0.00
Actual	0.00	39.29	5.65	14.50	2.86
Actual as % of estimate	0.00	87.30	188.30	725.00	--
Date of final disbursement	April 28, 1997				
Cumulative		39.29	59.44	62.30	--

Table 5: Key Policy Achievements

I. Enterprise Reform and Privatization

The program signalled Government intentions to act quickly on small scale privatization and develop a plan for medium and large scale enterprises; improve corporate governance; and eliminate state interference in commercial decisions of enterprises. These goals have been achieved with support under the Rehabilitation Credit and successor adjustment operations. Privatization of state enterprises is the backbone of the Government's strategy for attaining adjustment in the real sectors and stimulating growth. Since 1994 the Government has carried out mass privatization under its 1994-95 and 1996-97 privatization programs (supported under IDA's PESAC, APEAC and currently FINSAC operations). By February 1997, of the approximately 1,300 state-owned medium to large-scale enterprises included in the mass privatization program, 993 had gone through coupon auction; of these 804 were fully or majority privatized. Most of the remaining enterprises are scheduled for privatization under the 1996/97 privatization plan.

In May 1994, the Government established the Enterprise Reform and Resolution Agency (ERRA) to deal with restructuring or liquidating 29 large loss-making state-owned enterprises. These 29 enterprises were placed in a care and management program (four were subsequently removed from the program). Their access to credit and budget subsidies were cut off and most employees were placed on administrative leave at reduced salaries. Diagnostic studies were undertaken (assisted by consultants financed out of TAC funds). Final disposition of these enterprises were supported under successor operations. Following diagnosis of their prospects, four of the enterprises were liquidated and the others have been downsized and restructured financially. Fifteen of the companies have been sold and the sales process is continuing for six others.

II. Legal Basis for a Market Economy, Competition and Private Sector Development

The Government pledged to promote competition in production and distribution to support private sector development including the legislation focusing inter alia on ownership and property rights and commercial and contract law and laws on foreign investment. Substantial progress has been made toward modernizing Kyrgyz commercial laws to meet the demands of private investors. Among the laws recently enacted are a National Procurement Law; revised Civil Code (part 1), and the Tax Code. Other laws in final stages of preparation include: Laws on Pledge (Collateral), a new Banking Law, Insurance Companies, Securities Market, Investment Funds and Leasing, Foreign Investment, Mining Code, Bankruptcy legislation and the Land Code. The State Property Fund is being strengthened to serve the needs of potential foreign investors and to facilitate improved governance, management and monitoring of those enterprises remaining in the state sector with support from an IDF grant.

III. Agricultural Sector Reform

The Government undertook to develop a medium term strategy featuring continued privatization, transformation of state and collective farms into private corporate entities or farms, the development of an appropriate structure for crop and livestock production, reduction of state intervention in the sector, appropriate irrigation charges and an inventory of proposed public investment projects. Kyrgyzstan has made substantial progress toward dismantling state control over agriculture and reforming the sector along market economy lines with support from APEAC and complementary sectoral investments. Prices for all agricultural commodities have been liberalized, the system of state orders has been dismantled, and by February 1996 all export taxes on agricultural commodities had been eliminated. Ownership shares and land use rights in most state farms and collectives have been distributed to their workers. Restrictions on maximum farm size were abolished, land use rights were increased to 99 years, and a Land Registration Act establishing a unified system is being considered by Parliament. Most state and collective farms have been transferred into joint stock companies and about one third of the land under cultivation has been converted into numerous small private farms. The state monopoly on grain purchase and on bread production and distribution has been ended, and privatization of the state bread complex is almost complete. Work on the irrigation sector is underway with IDA support and the Government has prepared, and updated annually for the Consultative Group, a three year rolling public investment plan for all sectors.

IV. Financial Sector Reform

The Government announced its intentions to develop a solid and efficient financial system. The program would focus, inter alia, on the development of appropriate financial sector legislation, interest rates, enhanced foreign exchange operations and measures to address enterprise arrears. Real interest rates have reached positive levels, capital requirements and prudential regulations have been adjusted, and the NBK has effectively strengthened its supervisory capacity. A comprehensive financial sector reform, comprising downsizing, financial restructuring of insolvent state-owned banks, the establishment of a temporary debt resolution agency and the creation of a regulatory and supervisory framework for non-bank financial institutions is under implementation with support under the FINSAC and FINSAC TA operations.

V. Social Protection

The Government stated its intentions to, inter alia, focus on the development of a poverty line, review social investment and expenditure planning, and to begin to address family allowances, pensions and unemployment issues. A baseline household survey was completed in 1993. Poverty monitoring surveys were conducted in March 1996 and December 1996/January 1997 and surveys are planned for September 1997 and 1998. Progress has been made in streamlining transfers to economically vulnerable groups through the unified cash benefit, paid through the budget to families with per capita incomes below the minimum wage. (The UCB reflects the consolidation of former family allowances, bread compensation, child allowances, and social payments.) Main beneficiaries include children under 16, students, non-working pensioners, the disabled and the unemployed. Under the Social Safety Net project the Government is addressing targeting social assistance benefits and improving the capacity of the Employment Services. Discussions on a proposed social sector adjustment operation have been initiated with the Government.

VI. Macroeconomic Policies

The Government assumed full control over macroeconomic policies with the introduction of the Som in May 1993. During 1994 deposit and credit interest rates were liberalized, directed credits were discontinued and domestic bank financing of the budget deficit was curtailed sharply. A tight monetary stance in 1994 succeeded in bringing inflation down to 32 percent in 1995 and 35 percent in 1996. Interest rates have followed a similar path, with the central bank discount rate declining from over 100 percent in January 1995 to 55 percent in December 1996. A foreign exchange auction market, floating exchange rate and a fully liberalized exchange rate with no restrictions on current or capital account transactions have been established. A major liberalization of the trade regime also occurred over the past three years. Non-tariff barriers were removed and export taxes have been eliminated on all goods. Both imports and exports expanded rapidly in both 1995 and 1996. The current account deficit, including official transfers, rose from 18 to 22 percent of GDP in 1996.

Table 7: Technical Assistance Included in Project¹

Study	Purpose as defined at appraisal/redefined	Status	Impact of study
1. Enterprise Reform, Privatization and Private Sector Development	Long term advisory services were provided for the restructuring/liquidation of large loss-making companies under the newly created Enterprise reform and Resolution Agency (ERRA). Viability assessments to determine economic and financial viability of 29 enterprises.	completed	The Privatization Advisors assisted in the conceptualization and implementation of the ERRA program and the privatization exercise under the auspices of the State Property Fund (whose implementation was/is supported under the PESAC/APEAC and FINSAC operations). 4 enterprises were liquidated, 4 were dropped from the program, 15 were sold and 6 are under offer.
2. Legal Reform	Development of a legal reform program, legal drafting and assistance in coordination and institutional strengthening of the office of the President's Legal Advisor's Office (long term advisory services).	completed	Development of legislation related to commercial and civil law (approximately 19 laws benefited from advisory services; seminars and workshops offered and legal advisory services.
3. Mining Code	Support for the development of mining code and regulations and model agreement. Policy advice.	completed	Initiated dialogue on sectoral policies; elaborated draft code and regulations; final bill pending reconciliation within Parliament.
4. Government Restructuring	To assist the Kyrgyz authorities in designing policies and structures to make the Government more flexible, effective, efficient, based on the social and economic transformation experiences of other countries.	completed	Interactive report opened a dialogue on effective governance. Report discussed by the Executive Branch and Cabinet.
5. Commercial Bank Audits	To provide financial background on two banks critical to financial sector restructuring program	completed	Procurement arrangements and implementation of audits of AKB and Agroprombank were delayed. Findings provide NBK/DEBRA with input for addressing issues related to asset disposition and restructuring.
6. Audits/Commercial Bank Training	(i) Project audits of PESAC, and Dutch Grant for Rehabilitation Credit	completed	Two audits fulfilled compliance with Credit/Grant Agreements
	(ii) Technical assistance for banks dealing with foreign exchange	completed	Two seminars presented to equip banking staff to increase efficiency of import/export operations and currency reserves and build stronger relations with correspondent banks.

¹ Many of the originally programmed studies were cancelled at the request of the Government as grant financing from other donors became available. These included: studies on agricultural privatization and pricing and irrigation is being covered through EU-TACIS and project preparation and sector work done by the ADB and IDA; reform promotion activities were covered by a bilateral donor; health and pharmaceuticals were covered through the Manas program financed by a variety of donors; and financial sector assistance was provided initially from bilateral donors and currently through the FINSAC TA operation.

**7. Procurement Policies
Procedures and Practice**

**Procurement agents would be
contracted to facilitate project
implementation and provide training
for Goskominvest's PIU staff**

completed

Agents provided services for PIC/TAC procurement; provided a country assessment of laws and regulations governing procurement provided a training needs analysis and informal and formal training to staff in country and in the UK. A semi-autonomous Consultative Agency on International Procurement was established to provide advisory services to public and private sector. Calibre of PIU staff sufficient to attract international recruitment by multilateral organization.

Table 8A: Project Costs

Category	Appraisal estimate (US\$ million)			Actual/latest estimates (US\$ million)		
	Local costs	Foreign costs	Total	Local costs	Foreign costs	Total
1. Pre Identified import component (PIC)	-	33.0	33.0	-	14.40	14.40
2. Foreign exchange component (FMC)	-	20.0	20.0	-	41.00	41.00
3. Technical assistance component (TAC)	-	7.0	7.0	-	6.65	6.65
4. Project Implementation Unit (PIU)	0.25		0.25	0.25		0.25
Total	0.25	60.0	60.25	0.25	62.05	62.30 ¹⁾

1) Final amount reflects exchange rate fluctuations.

Table 8B: Project Financing²⁾

	Appraisal estimate (US\$ million)			Actual/latest estimates (US\$ million)		
	Local costs	Foreign costs	Total	Local costs	Foreign costs	Total
IDA	-	60.0	60.0	-	62.05	62.05
Domestic Contribution	0.25	-	0.25	0.25	-	0.25
Total	0.25	60.0	60.25	0.25	62.05	62.30 ¹⁾

1) Final amount reflects exchange rate fluctuations.

2) Parallel financing for the program was provided by the Governments of Switzerland, Netherlands and Japan. The Swiss Government provided Swf 14 million on May 18, 1994 to finance critical imports in the energy sector of the Kyrgyz Republic. Under the grant, the design, manufacturing, transport, erection management, testing and commissioning of three substations Orok, Tokmak and Ljermontovo were carried out. All equipment has been supplied and installed and the substations are in operation. The Grant is scheduled to close on December 31, 1998. The Government of the Netherlands provided a grant in the amount of NLG 9 million in May 1993 for the procurement of agrochemicals and veterinary medicines through Kyrgyzvetzoonab (veterinary medicines) and Kyrgyzselkhozkhimia (agricultural chemicals). Following privatization, distribution has been handled through the joint newly formed stock companies. The grant closed on June 30, 1995 and the financial audit was completed in December 1996. The Overseas Economic Corporation Fund (OECF) made a loan of Japanese Yen 6,500,000,000 in support of the Government's Reform Program on October 14, 1993. The loan financed Yen 4.0 M of pre-identified imports, Yen 2.1 M of other imports and Yen 0.2 M of consulting services. The program was completed on October 24, 1996 and the completion report issued in October 1996.

Table 10: Status of Legal Covenants
Kyrgyz Republic
Rehabilitation Credit

Agreement	Section	Covenant Type	Present Status	Original Fulfillment Date	Revised Fulfillment Date	Description of Covenant	Comments
Text Reference:	2.01	03	C	09/01/93	09/01/93	Government to open and maintain in dollars a special deposit account in a commercial bank on terms and conditions satisfactory to the Association.	completed
Text Reference:	3.04 (a)	03	C	07/01/93	07/01/93	Government to submit the agreement between the Ministry of Economy and Finance and the National Bank acceptable to the Association pursuant to which a certain amount of the funds reimbursed of the proceeds of the credit allocated to category (2) shall be used for interventions in the inter-bank foreign exchange auction.	completed
Text Reference:	3.04 (b)	09	C			The National Bank of Kyrgyzstan to submit monthly reports on the total volume of the inter-bank foreign exchange auctions and its interventions financed out of the funds reimbursed by the Association to the Government.	PIU maintained during initial period; as auctions were institutionalized NBK maintains own records open for review.
Text Reference:	3.05(b)	01	C			Furnish the Association as soon as available, but in any case not later than six months after the end of each such year, a certified copy of the report of such audit by said auditors, of such details as necessary.	First audit completed Nov. 1995; final audit in progress.

Covenant types:

1. = Accounts/audits
2. = Financial performance/revenue generation from beneficiaries
3. = Flow and utilization of project funds
4. = Counterpart funding
5. = Management aspects of the project or executing agency
6. = Environmental covenants
7. = Involuntary resettlement

8. = Indigenous people
9. = Monitoring, review, and reporting
10. = Project implementation not covered by categories 1-9
11. = Sectoral or cross-sectoral budgetary or other resource allocation
12. = Sectoral or cross-sectoral policy/regulatory/institutional action
13. = Other

Present Status:

- C = covenant complied with
 CD = complied with after delay
 CP = complied with partially
 NC = not complied with

Table 12: Bank Resources: Missions

Stage of project cycle	Month/ Year	No. of Persons	Days in Field	Specialization ¹	Performance Rating ²		Types of Problems ³
					Implementation status	Development objectives	
Through appraisal	(1) 04/92	21	15	E, R, P, F, A, G, N, I, M, L, S, O, H, C, B, K			
	(2) 06/92	15	17	E, B, D, A, L, F, P, L, T, C, H, I			
	(3) 10/92	4	7	E, L, C			
	(4) 01/93	5	14	E, C			
Appraisal through Board approval	10/92	5	11	E, L, B, F			
Supervision	11/93	4	7	X, B, F	S	S	F, T
	06/94	2	10	X, F	S	S	F, T
	02/95	3	10	X, M, B	S	S	F, M
	07/95	2	3	X, B	S	S	F, M
	11/95	2	10	X, RX	S	S	F
	04/96	4	5	X, B, R, RX, L	S	S	F
	11/96	2	6	X, RX	S	S	
Completion	03/97	2	9	X, E, RX	S	S	
Total							

Note: Some specialists (e.g., the lawyer, and PESAC Task Manager, etc.) reviewed components related to their scope of work during other operational missions.

1 - Key to Specialized staff skills:

E = Economist/Macroeconomic
 B = Disbursement Specialist
 D = Debt Specialist
 A = Agriculturist
 L = Lawyer
 F = Financial Sector Specialist
 P = Private Sector Development Specialist
 L = Telecommunications
 T = Transport Sector Specialist
 C = Procurement

H = Health Sector Specialist
 I = Irrigation
 X = Country/Operations Officer
 K = Accountant
 O = Labor Markets
 S = Social Safety Net Specialist
 M = Mining Specialist
 R = Research Analyst
 G = Energy Specialist
 N = Industry
 RX = Resident Mission Operations Officer

2 - Key to Performance Ratings:

S - Satisfactory
 U - Unsatisfactory

3 - Key to Types of Problems

F - Financial
 T - Technical
 M - Managerial

Table 13: Bank Resources: Staff Inputs

Stage of project cycle	Planned		Revised		Actual	
	Weeks	US\$	Weeks	US\$	Weeks	US\$
Preparation to appraisal*	49.0	142.2	48.0	142.2	48.0	142.2
Appraisal*	58.3	188.4	58.3	188.4	58.3	188.4
Negotiations through Board approval*	4.3	12.8	4.3	12.8	4.3	12.8
Supervision	125.6	449.1	122.5	366.7	113.8	319.8
Completion	-	-	11.0	48.8	1.6	18.0 ^{1]}
Total	236.2	792.5	244.1	758.9	178.0	681.2

* Planned and Revised data unavailable. Actual data used instead.

1] As of end March 1997.

Aide Memoire
Implementation Completion Report (ICR): Rehabilitation Credit (2491-KG)

1. The Rehabilitation Credit (Cr. 2491-KG) was closed on December 31, 1996. Final disbursements are in progress and Goskominvest is making arrangements for the final project audit, due June 30, 1997. A Mission comprised of Ms. Nancy Cooke, Sr. Country Officer, Ms. Sarina Turgunaliyeva, Operations Officer, Resident Mission, Bishkek and Mr. David Greene, visited Bishkek in March 1997 to prepare an Implementation Completion Report. Ms. F. Aynur Sumer participated in some Mission meetings. Mr. Almaz Janaliev, of the Project Implementation Unit of Goskominvest, worked with the Mission throughout its stay. The Mission met with representatives of the Ministries of Finance/Economy, Agriculture, Industry, Health, Transport and Communications, NBK, Kyrgyz Energy Holding Company, and the State Property Fund. The Mission thanks the Kyrgyz authorities for their cooperation and for the many courtesies extended to it. It also appreciates the excellent Final Evaluation Report prepared by GOSKOMINVEST which will be included in the Implementation Completion Report.

2. The purpose of this note is to preview the principal findings of the mission and the proposed content of the ICR. The major conclusions are: (1) the project successfully achieved its major objectives, notably, supporting the initiation of the Government's Economic Reform Program and providing the foundation for a continued policy dialogue; (2) the project had a very strong institution/capacity building impact; (3) although the project provided timely finance for critical imports, the design of the pre-identified imports component (PIC) proved difficult to administer and future adjustment projects should avoid using this mechanism; (4) technical assistance needs evolved during project implementation. While the final technical assistance supported under the project ultimately proved well suited to the emerging needs of the Program, experience suggests that free standing technical assistance projects allow more flexibility.

3. Although problems arose in the implementation of PIC and TAC components, modifications were made as needed and these problems did not detract from the overall success of the project. Moreover, a number of involved sectoral ministries and agencies have noted that the experiences gained in the implementation of the Rehabilitation Credit have served them well in the course of design and implementation of subsequent investment operations. Finally, the reform program initiated under the Rehabilitation Credit served as the underpinning for three subsequent adjustment operations. The Privatization and Enterprise Sector Adjustment Credit and the Agricultural Privatization and Enterprise Adjustment Credit were completed successfully in 1994 and 1995 respectively. A Financial Sector Adjustment Credit, approved in June 1996 is under implementation and a Public Sector Resource Management Adjustment Credit was negotiated in February 1997.

4. The success of the project was in no small measure due to commitment of the **Kyrgyz Government** both to implementing the reform program and to building a

constructive relationship with the World Bank. Success on the economic front can be seen in gradual stabilization of the economy, virtual completion of market liberalization, continuing progress in privatization, improvement of enterprise governance, building of a legal and institution framework for a market economy and in signs of recovery of economic activity. Considerable progress has also been made on land reform and distribution, the introduction of a social safety net, and the development of a viable financial system.

5. In retrospect, the expectations under which the PIC was designed proved unrealistic. The list of critical imports was prepared early in project design. Procurement (preparation of technical specifications and bidding documents, payments arrangements and logistics) turned out to be more complex than anticipated and changes in circumstances during implementation dictated modifications in the list. The process took substantially longer than anticipated, impeding delivery and sometimes resulted in an imperfect match of end-user needs and demand. Reallocation of a significant amount of funds from the PIC to the foreign exchange component (FXC) permitted timely disbursement of credit funds. Nevertheless, despite these complications, most recipient ministries/agencies confirmed that the project-financed imports were essential and assisted them in maintaining production and services. Further, Kyrgyz officials proved to be rapid learners and substantial procurement expertise was built up in the process.

6. Experience under this operation suggests that free standing technical assistance projects work better than technical assistance components of adjustment operations. The TAC experienced significant modification during implementation as Program requirements evolved during the adjustment process. Much of the TAC was reallocated to support ERRA and privatization program activities required by continuing reform efforts supported under the PESAC and APEAC programs. Although the process of procuring consultants and consultancy firms proved very time consuming and delayed project completion, the overall performance of the consultants was satisfactory. The technical assistance provided under the project made a solid contribution to the formulation and implementation of the Kyrgyz adjustment program.

7. In conclusion, the timely provision of Bank Group financial assistance and policy advice in the formulation and implementation of the Rehabilitation Credit, combined with Government determination to carry out reform, even under difficult circumstances to the reform process, resulted in accelerated economic stabilization and restructuring. The success of the Rehabilitation program proved to be the foundation upon which broad support of the international community could be built and substantial capital flows mobilized. In this regard, the project may be considered very successful.

Bishkek, Kyrgyzstan
March 10, 1997

**STATE COMMISSION
ON FOREIGN INVESTMENTS AND ECONOMIC ASSISTANCE
(GOSCOMINVEST)
PROJECT IMPLEMENTATION UNIT**

**FINAL EVALUATION REPORT
THE REHABILITATION CREDIT (2491-KG)**

REHABILITATION CREDIT (2491-KG) THE KYRGYZ REPUBLIC

INTRODUCTION.

In 1991 Kyrgyzstan faced a great number of difficulties caused by USSR's collapse. The economy of the Republic almost completely depended on centralised command administration. Until the Soviet Union's dissolution Kyrgyzstan has received substantial subsidies accounting for between 11 and 12 per cent of GDP from central budget. The industrial and agricultural sectors of the Kyrgyz Soviet Socialist Republic were integral part of united economic complex which has been managed by means of planning. The breach of the co-operation ties and business relations between former soviet republics have been caused with the gradual build-up of customs and exchange barriers. This resulted in loss of markets for goods, produced by the Kyrgyz manufacturers, and losses of customary suppliers. The economic crisis was deepened by the cessation of centralised subsidiary financing.

In view of these negative factors Kyrgyzstan have found difficulties in preservation of economy against breakdown. Output fell across the entire Kyrgyz economy. GDP fell down by an estimated 10 per cent in 1991, by 16.5 per cent in 1993, and by over 20 per cent in 1994. The industrial sector experienced the sharpest loss in output, with annual declines in 1992, 1993, and 1994 of approximately 25 percent.

In these circumstances preparation of comprehensive reform program became extremely critical for the Kyrgyz Republic. The Government of Kyrgyzstan elaborated the program determining principles, instrumentation and objectives of country development. The key objectives of the reform program are: (i) to stabilise the economy; and (ii) to effect structural reform to create the conditions for growth in an economy and integration with the world economy. For these purposes the Government determined the most important directions of development. There are (I) enterprise reform, (ii) agricultural sector reform, (iii) financial sector reform, and (iv) creation of modern infrastructure and market economy environment. To achieve the objectives of economic reforms the industrial and agricultural policies had been adopted. In accordance with its principles and because of lack of funds it was decided to concentrate recourses on support of priorities. The Government determined that such priorities are the agriculture and food industry, energy sector, mining industry, textile and sewing industry. These branches should serve as "boosters" for the development of the whole national economy. However, even in spite of limitation of fields for primary financing Kyrgyzstan was not in a position to provide sufficient funds out of internal recourses. In view of this, the Government emphasised the foreign investments as essential condition of successful transition to market-oriented economy. On July, 1992 the State Commission on Foreign Investments and Economic Assistance (GOSCOMINVEST) was established for the co-ordination of foreign assistance. On April 19, 1993 the Government of the Kyrgyz Republic officially applied to the International Development Association (IDA) requesting financial

assistance in support of Economic Reform Program. The IDA agreed to provide the Rehabilitation Credit for the purposes of maintenance of the Kyrgyz economy in transition period. On May 20, 1993 the IDA and the Kyrgyz Republic signed the Credit Agreement for the total amount of 43,000,000SDR (60,000,000USD equivalent).

In order to co-ordinate all activities Project Implementation Unit (PIU) has been established under GOSCOMINVEST. PIU was responsible for the overall implementation, procurement and disbursement of the Rehabilitation Credit and the related reporting and accounting activities.

IMPLEMENTATION.

In Kyrgyzstan the Rehabilitation Credit was the first big lending operation of international financial institution. By this Credit the IDA provided concrete and overall support for the reform process. The IDA's funding allowed to (i) import goods extremely needed for the Kyrgyz economy in transition, (ii) hire qualified consultants for advising of local staff in different activities, (iii) stimulate foreign exchange markets and enhance private sector access to foreign exchange. The initial allocation of the Rehabilitation Credit was made to the following categories:

Category	Allocated amount (expressed in SDR)	Allocated amount (expressed in USD)
(1) Pre-identified imports component (PIC)	23,800,000	33,000,000
(2) Foreign exchange component (FXC)	14,000,000	20,000,000
(3) Technical assistance component (TAC)	5,100,000	7,000,000
TOTAL	43,300,000	60,000,000

During implementation a number of reallocations have been effected to meet project needs. The schedule of all reallocations is attached.

Upon completion of the Rehabilitation Credit project the final undisbursed amounts under PIC and TAC components were transferred to FXC.

PRE-IDENTIFIED CRITICAL IMPORT COMPONENT.

1.2. Under this component critical goods were procured for key sectors of economy of Kyrgyzstan. Total number of the contracts concluded by the PIU is 40. The total amount paid against the placed contracts is USD14,439,996.75.

1.1 At the early stage of the implementation process local PIU staff was not adequately experienced in international procurement procedures. By this reason contracting of procurement agent was provided to assist the Government in the management of procurement, and training of the PIU staff. The procurement agent was chosen through an international tender. As the result of this tender Crown Agents was assigned as a procurement agent for Rehabilitation Credit.

1.3. In close co-operation PIU and Crown Agents' consultants carried out procurement exercises under the Rehabilitation Credit. The goods have been procured via ICB, LIB and International Shopping procedures in strict accordance with the World Bank's Guidelines for Procurement.

1.4 The list of procurement under PIC is as follows:

Sector	End-User	Goods supplied	Number of placed contracts	Total amount of placed contracts (USD)
Agriculture	Ministry of Agriculture: Kyrgyzzoovetsnab Kyrgyzselhozhimia	veterinary medicines, pesticides, herbicides	9	2,433,983.80
Irrigation	Ministry of Irrigation	pump equipment, non-return valves, concrete mixers	4	1,074,486.00
Communications	Ministry of Communications	splicing materials, computer equipment, exchange spares, test equipment	3	641,551.23
Energy Sector	Kyrgyz State Energy Holding Company (KSEHC)	electrical cables, electrical substations, pump equipment, air compressors, steel pipes, welding electrodes, rubber hose	13	4,173,779.91
Transport	Ministry of Transport	bus spare parts	5	685,764.73
Health sector	Ministry of Health: "Kyrgyzfarmacy"	pharmaceuticals	2	95,610.00
Government of the Kyrgyz Republic	Legal Department of President Office	computer equipment	1	31,456.50
	Treasury Department	computer equipment	1	86,129.00
	Ministry of Finance	computer equipment	1	225,766.73
	"Kyrgyzgas"	gas	1	5,001,600.00

1.4 All equipment, spare parts and materials were procured on the basis of formal requests provided by the end-users and technical specifications approved by them. Upon delivery to Kyrgyzstan the related government agencies have distributed the goods among inferior branches in accordance with their interior schedule.

1.5 The ministries confirmed that all objectives of critical goods' procurement were achieved. All supplied goods are in use strictly according to the purposes which they are intended.

1.6 To make the above statement more sound some exemplification are needed to be made.

- (i) The irrigation sector was considered as one of the fields which is in urgent need of financing. The essential part of the Rehabilitation Credit proceeds was granted to this sector. The Ministry of Irrigation requested pump equipment, non-return valves and concrete mixers to be procured out of the Credit funds. PIU concluded the contracts on supply of the above totalling USD1,074,486. Upon delivery the Ministry of Irrigation distributed these goods among the regional departments in Osh, Naryn, Djalal-Abad, Talas, Chui. Besides, the small primary reserve of non-return valves and mixers was also made. All supplied equipment and spare parts have been used for the purposes of replacement of outdated ones. Presently they are in operation by users. The procurement of the above goods allowed to replace outworn pumps and non-return valves on pipes of pump stations. New concrete mixers are currently being used for repair of hydrotechnical installations and coating of canals. These measures resulted in rehabilitation of capacities of pump stations, hydrous constructions and meliorate channels supplying water for sewage-farms.
- (ii) In Kyrgyzstan a great number of energy installations supplying electricity to users were in bad order because of lack of financing. In many cases the terms of use of equipment expired long ago. Very often it conducted to malfunctions in supply of power to private consumers and enterprises as well. In these circumstances it was critical to find the funds if only for first technical aid. The Rehabilitation Credit became the substantial source for procurement of spare parts. The Kyrgyz State Energy Holding Company (KSEHC) made requests for procurement of spare parts most needed for maintenance and reconstruction of energy installations all over the territory of the country. In consequence of competitive bidding 13 contracts for a total amount of USD4,173,779.91 have been concluded with foreign suppliers.

The transformers purchased under the Rehabilitation Credit have been used by KSEHC for renewal of existing capabilities of energy system. All received goods are distributed among regional electric network's outfits. The rehabilitation allowed to improve the supply of electricity. It is very important because the consumption of electric power sharply increased for the reason of reduction of use of expensive coal, gas and oil fuel by local consumers. The procurement of the above mentioned goods consists with the Government general policy in energy sector which is oriented on gain of energy independence on foreign imports. In accordance with this policy a major part of the Kyrgyz economy should be shifted to electric delivery from local sources. The purchase of the cables, transformers,

electrodes, compressors and other products allows peak periods consumption to be maintained.

- (iii) The public transport of Bishkek is in a difficult situation caused by lack of financing. The failure to purchase new buses and spare parts for needs of municipal transport resulted in wear of buses' fleet. The great number of buses was inoperational because of absence of spare parts. In view of that the public transport is an important part of capital infrastructure and taking into consideration the annual increase of urban population, an essential part of the Credit proceeds was allocated for procurement in transport sector. The Ministry of Transport applied for the purchase of buses spare parts to be made. PIU carried out tenders and concluded 5 contracts for a total amount of USD685,764.73. During 1995-1996 Bishkek Municipal Transport Department utilised all supplied spares for repair of buses. These measures resulted in an increase of operational buses in the capital of Kyrgyzstan and materially reduced the extent of the problem.

1.7 In view of the above said, positively, a conclusion can be drawn that key objectives of the Rehabilitation Credit have been achieved. The implementation of the Credit has met the originally posed goals and fully answered the name of "rehabilitation" of the Kyrgyz economy. In absence of sufficient financing out of the republican budget the funds of the Rehabilitation Credit allowed to support the basic sectors during initial stage of transition period.

TECHNICAL ASSISTANCE COMPONENT.

2.1 The TAC provided financing for technical assistance in structural reform areas such as enterprise reform, privatisation and private sector development, policy and legislation development in agriculture, mining, procurement. The original allocation for the Technical Assistance Component of USD7,000,000 and remained unchanged throughout the project. The PIU concluded 35 contracts and the total paid amount is USD6,912,463.31. The table attached as Annex A shows the contracts concluded under the TAC.

2.2 Procurement Agent. The assistance to the Government in procurement procedures was an issue of primary importance under the TAC. Originally the local PIU staff did not have a satisfactory experience in international procurement practices. In view of this, the Government of the Kyrgyzstan and the IDA agreed that a Procurement Agent be hired to initially carry out a procurement under the Rehabilitation Credit while simultaneously training a local staff. In a process of international competitive bidding 4 proposals from foreign firms were received. As the result of the bids evaluation "Crown Agents" was assigned as a Procurement Agent. During the implementation of the Rehabilitation Credit the PIU and Crown Agents jointly conducted procurement and other related functions in accordance with the IDA Guidelines and the Credit Agreement. The Consultants carried out training of local staff by means of in-country courses, training in Crown Agents'

Training Centre in UK. On-the-job training was the most important and useful for PIU because the PIU staff gained a practical experience and familiarised itself with the bidding procedures. Consequently, the PIU's staff-members are in a position to conduct all procurement procedures independently. Moreover, PIU provided expertise to all other ministries and government agencies on tender issues. In order to preserve all gained expertise and knowledge, it was decided by the Government to restructure PIU into Consultative Agency on International Procurement responsibilities of which would be provision ministries and agencies with expertise, consultation on procurement related issues and further development of state procurement system in the Kyrgyz Republic.

2.3 Government Restructuring. Since the Kyrgyz Republic's independence it was necessary to streamline the structure of management for social and economic development. For this purpose the three-person team of foreign advisors was hired. They were requested to review the conditions of successful governance and propose ways to enhance the efficiency of Ministries and other governmental organisations, basing their recommendations on the experience in other countries. After reviewing background documents, including the Regulations of different economic ministries, examples of the major economic legislation of recent years, sector studies and task reports, and a series of meetings with the President of Kyrgyzstan and his staff, the advisory team prepared the recommendations to make the Government more effective, efficient and flexible. The ways of transformation proposed by the advisors were carefully considered and adopted by the Government.

2.4 Legal Reform. The transition from a command to a market-oriented economy required substantial changes in the legal and institutional framework governing economic activities in the Kyrgyz Republic. In order to strengthen the Government's capacity to carry out a comprehensive legal reform program the allocation of USD450,000 was made in the Rehabilitation Credit. Basing the results of limited competitive bidding, Checchi & Co. in association with Paterson, Webb, Belknab & Tyler was invited to contract negotiations. The amount of concluded contract was USD410,500. The sum of USD39,500 from initial allocated amount was earmarked for the purchase of computer equipment for Legal Department of the President Office (LDPO). The consultants rendered services in elaboration of new legislation which would meet the requirements of the emerged economic activity; drafting comments to the existing Kyrgyz legislature; preparation of analytical reports on the strategy of legal reforms; the delivery of public lectures on topics dealing with legal reform; the conduct of in-country training seminars for the Kyrgyz Government lawyers; and consultation on the establishment of a data bank at the LDPO in the general area of business law of selected CIS countries. In close co-operation with the foreign consultants the LDPO, prepared the drafts of different commercial laws and submitted them for consideration to the Jogorku Kenesh (the Parliament), participated in various seminars and work-shops for their introduction, identified and made a planning for elaboration of new laws (required by the present situation), revision and amendment of existing legislature which is currently under implementation. The area covered by their work was commercial and civil legislation, which would regulate activities and establish norms of its application for enterprises

(state and private), law on banks and its activities, investment activities, ownership, civil code, judicial code, arbitration, etc. The starting point and the achieved goals have given an impulse for further development of legal reforms and the work initiated by the consultants was undertaken by the different agencies under co-ordination of LDPO.

2.5 Seminar on Foreign Exchange Operations. During the transition to market economy the National Bank of Kyrgyzstan (NBK) used foreign exchange transactions as one of several instruments to implement its monetary policy. At the early stage it was vital that all staff working in the foreign exchange departments of banks gained an adequate knowledge of this instrument. It was, therefore, proposed to organise a phased training in international operations in order to gradually develop experience through classroom lectures, case studies, bookkeeping and accounting exercises. As the result of competitive tendering process AIB International Consultants and the Centre Pour la Formation de la Profession Bancaire were retained to present two seminars in Bishkek. The total amount of the contract was USD350,000. The delivered training programme gave to the banks' staff a solid knowledge of how to (i) build sound relations with corresponding banks, (ii) increase the efficiency and volume of import/export operations, and (iii) improve the management of the country's foreign exchange earnings and hard currency reserves. The consultants transferred and developed the skills and understanding of banks' staff a knowledge of the international rules and practices of documentary credit operations, as established by the International Chamber of Commerce (advanced letter of credit operations including bank guarantees and standby letters of credit), accounting for international operations (including IAS and BIS requirements), currency dealing with Reuters and Telerate, SWIFT operations, risk management, liquidity management, asset/liability committees, internal and external audits. It was expected that in the obtained knowledge would form a basis which could help the Kyrgyzstan overcome and adapt to a constant change of international banking world.

2.6 Audit of Agroprombank and AKB Kyrgyzstan. The improvement of bank supervision was critical to restructuring and sound development of the commercial banking sector. In this regard the amount of USD400,000 out of the Rehabilitation Credit's funds was allocated for the audit of two large commercial banks in the Kyrgyz Republic. Agroprombank and AKB Kyrgyzstan were selected for those pilot audits. The bidding exercise resulted in first-ranked firm being invited to contract negotiations. However, in view of unacceptable changes were made to their original proposal the second highest-evaluated bidder was invited to negotiations. During this process the original TOR was changed. The amount of concluded contract was USD393,600. The purposes of assignment were (i) to establish true financial position of the above banks in accordance with the international accounting standards, (ii) to evaluate their branch network. During the implementation of this project the PIU met with the difficulties caused by inadequate performance of the services by auditors. The initial reports submitted for consideration to the National Bank and the IDA were not satisfactory because they did not provide the analysis of banks' branches as it was required in the TOR. These concerns became the matter of the enduring discussions held between the National Bank of Kyrgyzstan, the IDA, the PIU GOSCOMINVEST and the audit firm.

Finally it was agreed that auditors' team visits all necessary branches and conducts the needed audit. The auditors carried out this work and prepared the reports on branches network. From the first these reports were not accepted by the National Bank. The matter was that these documents were issued later than planned initially. At this moment the NBK already annulled the Agroprombank's license hence substantial part of initial objectives were not met. Besides the NBK was not fully satisfied with the quality of performance of services. In excuse of this the auditors appealed to the fact of lack of co-operation from side of banks' officials. The PIU was informed that all negative comments sent to the auditors were carefully considered. In spite of the above said the number of the important objectives of the project have been met. Presently the information obtained during the audit of two banks are in use of the NBK for determination of future activities in banks' restructuring under FINSAC project.

2.7 Mining Legislation. The aims of TA in mining sector were to assist in establishing the internationally competitive legal, regulatory and fiscal environment necessary to promote private sector development and to provide assistance in strengthening of relevant government institutions, including training of officials in administering of regulations. As the result of the limited international bidding International Mining Consultants Limited (IMCL) of UK was selected for carrying out of this assignment. The PIU concluded the contract with the above mentioned firm for a total amount of USD429,875. The consultants rendered advisory services in two main components: (i) a dialogue on mineral policies required to attract investment; (ii) design and drafting the mining code, regulations and model investment agreement. During the implementation of the project IMCL have reviewed existing mineral recourse base and mining law. The collected and summarised information was used for organisation of seminars and workshops for the officials from the State Committee on Geology, Kyrgyzalyn, the Ministry of Industries, the Ministry of Finance, the Committee on Technical Inspection. The work of consultants resulted in formulation of policy statement covering taxation of mining and mineral development, institutional reform, licensing procedures, state involvement in mining, royalty. IMCL team provided essential assistance to the working group established by the Government for drafting of detailed legislation. During preparation of draft law on sub-soil this group incorporated the features of the draft which was elaborated by the IMCL consultants. Upon completion of the project the end-users found the technical assistance provided by the consultants useful and quite efficient.

2.8 Enterprise Reform and Resolution. The objectives of TA provided in this area were drafting and reviewing relevant legislation, designing strategies and implementation mechanisms, carrying out pilot transactions, and strengthening institutions and skills. To facilitate the liquidation/restructuring of large loss-making enterprises (LLME) the Government established a new high-level entity, the Enterprise Reform and Resolution Agency (ERRA). For the purposes of rendering of technical assistance to this agency the PIU conducted a tender exercise and concluded the contract with BMB (Netherlands) for an amount of 2,184,163.70USD equivalent. The team of hired advisers assisted ERRA in the following activities: (i) orderly liquidation of the non-viable enterprises or their components, (ii) rearrangement of the remaining components into commercial entities,

and (iii) the provision of the resulting entities with a reasonable chance of success by resolving their indebtedness, strengthening their management and giving them clear and realistic operating programs. During the implementation of the above program the PIU in close consultation with ERRA and the BMB advisers concluded 15 contracts with the firms which were assigned as the short-term consultants. These consultants carried out the diagnostic studies in respect of 29 state enterprises according to the priorities set by ERRA. The results of such studies served as the basis for determination of further development for the LLMEs within the PESAC program. In general, this TA was required to give a support to the complex program designed for the large state enterprises belonged to the key sectors of the Kyrgyz economy.

2.9 Privatisation Adviser. In order to provide a conceptual guidance in matters of enterprise privatisation activity to the State Property Fund, the PIU concluded contract with a foreign consultant. The adviser rendered consultancy services in different areas of privatisation. This work included assistance in (i) regulation of investment funds, (ii) sale of state-owned shares in privatised joint-stock companies and in fully state-owned enterprises, (iii) demonopolization and privatisation of enterprises in wholesale trade and in transport sector, and other matters related to privatisation.

2.10 Audit of the Rehabilitation Credit. The PIU arranged the competitive bidding exercise for the audit of the Credit accounts which was required under the conditions of the Credit Agreement. As the result of tender Ernst & Young Kazakhstan was assigned to carry out the audit services. The total amount of the contract was USD25,000. The auditors prepared the audit report which was considered and approved by the Government and the IDA.

2.11 Audit of Dutch Grant. During the implementation of the Rehabilitation Credit the IDA agreed the audit of Dutch Grant to be financed out of Credit's funds. In order to hire auditors, the PIU invited a number of firms, however, all of them refused to submit their proposals in view of lack of available staff. The PIU concluded the contract with Coopers & Lybrand Kazakhstan for the amount of USD9,375. The C&L's team conducted audit and prepared the Audit Report which then was approved by the IDA.

2.12 Computers for GOSCOMINVEST and ERRA. Under the TA component some procurement of goods has been made. In view of the large scope of work to be made by the above entities it was decided to furnish GOSCOMINVEST and ERRA with the computer equipment extremely needed to carry out the activities. As the result of international competitive tender two separate contracts for supply of the above goods were signed. The purchase of this equipment allowed to essentially improve and facilitate the work of the above entities.

2.13 Audit of PESAC. It was agreed that the Rehabilitation Credit. The purpose of this assignment was to carry out the audit of PESAC credit as it is provided in Credit Agreement for PESAC. The audit firm selected for this assignment have visited Bishkek and reviewed the documents in the Ministry of Finance. Unfortunately, further

implementation was essentially delayed because of different objective and subjective reasons. The auditors required the VAT to be paid out of the Kyrgyz Government's funds. This issue was solved by GOSCOMINVEST and the Ministry of Finance approved the payment of the VAT to be effected. However, further performance of the obligations by the auditors was unsatisfactory. In view of the delay in submission of the Audit Report the payments under the Rehabilitation Credit were not completed by the closing date. Even after approval of the draft reports by the IDA and the Ministry of Finance it took a long time to lead the auditors to submit the full set of documents forming the Audit Report. Finally the Report was provided but the quality of services rendered by the auditors can not be considered satisfactory.

2.14 Summarising all above said, the Government considers that despite the different issues raised during implementation of TAC the objectives of this component have been achieved. All end-user agencies are satisfied of quality and scope of consultancy services rendered under the Rehabilitation Credit. The assistance provided by the advisers facilitated implementation of projects in different areas of economy. During the process of joint work with expatriate consultants local staff gained a solid knowledge and experience.

FOREIGN EXCHANGE COMPONENT.

3.1 The amount under the FXC was the biggest one in comparison with other components of the Rehabilitation Credit. Initially the amount of USD20,000,000 was allocated for the FXC. During implementation the portion of this component have been essentially increased to meet the project features.

3.2 The FXC was used for the following main purposes. The National Bank of Kyrgyzstan carried out the financing of the expansion of the auction market. The local currency received from the sale of this foreign exchange provided non-inflatory financing of the state budget.

3.3 Due to the FXC the Kyrgyz commercial banks expanded their activities in foreign exchange transactions.

PERFORMANCE OF THE BANK.

1. The Bank's overall performance in respect of Rehabilitation Credit was completely satisfactory. The World Bank's assistance clinched the successful implementation of the whole project. Generally the Bank's staff involved in implementation of the Credit has been fulfilling its obligations with the high level of professional competence. The Bank's officials carried out their scope of work with due diligence and efficiency.

2. The joint work of the Bank, the WB Resident Mission, the PIU and the relevant Government agencies resulted in achievement of planned objectives. Such close co-

operation was very fruitful and useful. This allowed to establish the necessary policy dialogue between the Bank and the Kyrgyz Republic that was one of the important goals of the project. Necessary interaction have been arranged in different ways such as regular communication with the WB, reporting, the review missions and periodic meetings in the Resident Mission. All main activities were carried out in close consultation and co-ordination with the World Bank. Bureaucracy and verbalism which could impede implementation did not arise during the period of the project. Almost all issues have been solved by the WB in due course and form. Some cases of insignificant delays can not be considered essential because these did not affect on the further progress.

3. The Rehabilitation Credit was the first financial assistance of such value and importance for the Kyrgyz Republic that the experience gained through the dialogue and co-operation are in use for implementation of sequential financial assistance provided by the World Bank and other international institutions.

4. The implementation, especially, procurement and disbursement activities were carried out successfully with the assistance of the World Bank through a provision of necessary documentation such as a sample documents, handbooks, manuals and directories.

5. In the process of project implementation, the qualified specialists of the Bank provided necessary support with the recommendations and advice on different issues.

6. The Bank promptly conducted disbursement activities upon formal requests of the PIU and in accordance with the current requirements of the different projects under the Rehabilitation Credit. All reallocations among the components were effected by the Bank in time.

7. The World Bank fulfilled its obligations and responsibilities under the Credit Agreement in due form that resulted in achievement of all objectives under the project.

PERFORMANCE OF THE BORROWER

1. In order to implement the Rehabilitation Credit, which was an important base for realisation of the Economy Reform Program, the Government of the Kyrgyz Republic endeavoured to perform its duties in due manner. During the implementation process the relevant Government entities and the PIU did their best efforts to achieve goals of each particular project.

2. The Credit covered the several sectors of the Kyrgyz economy, an assistance to which was determined as most significant for the future development of Kyrgyzstan. Realisation of all projects was under the supervision of senior Government officials. The periodic sessions of Board of GOSCOMINVEST constantly kept reviewing the status of projects' implementation.

3. The PIU GOSCOMINVEST was established to execute activities needed for fulfilment of the Borrower's obligations. At the early stage of implementation the PIU

staff had not adequate skills and knowledge in procurement and disbursement. However, after short period of joint work with the foreign consultants the PIU staff members gained a necessary expertise and were able to carry out procedures independently.

4. In process of co-operative work with the PIU and foreign advisers, the end-user agencies got their first practice in dealing with the projects funded by the international financial organisations. Now many of them use the obtained experience for implementation of other projects.

6. To fulfil the conditions of repayment of the funds the Ministry of Finance elaborated the form of debt agreements to be concluded with recipient agencies. This form are currently in use of the Ministry of Finance for different credits provided by foreign investors.

7. In order to facilitate implementation of projects under the Rehabilitation Credit the Government lend necessary support to the PIU.

LESSONS LEARNED DURING IMPLEMENTATION

1. At the early stage after the Credit became effective the PIU staff was inexperienced in procedures needed to implement the Project. However, the substantial and rapid progress was made in this respect as the result of the delivered training, especially, on-the-job training and own practice. In short time the local staff became capable to carry out all scope of procurement and disbursement activities in accordance with WB's guidelines independently. The factors which could influence in rapid development of PIU's qualification are as follows: adequate knowledge of foreign languages, intensive (short-term) theoretical training, comprehensive on-the-job training under supervision of qualified consultants.

2. The lack of comprehension of the World Bank rules and procedures by the end-users caused the delays during implementation of some Projects. There were two main reasons of these delays such as lack of sufficient co-operation from the part of the end-user agencies and limitless interference into the procurement process. Unfortunately, there were the cases when such agencies tried to affect the procurement activities in a way which was not allowed. Sometimes it took a long time to get formal responses from the beneficiaries in respect of approval of bidding documents, comments on reports, answers on submitted questions and opinion on different issues. In some cases the end-users had changed their initial decisions and reconsidered their opinion and comments on the documents approved by them before. Mainly, that was due to problem with the knowledge of English language and, of course, difference in systems and standards of technologies existed in the Kyrgyz Republic.

3. In addition to the above said, the delays in implementation of the projects were caused by inadequate performance of the contracted firms, mainly consultancy firms.

Some of them did not fulfil their obligations in accordance with the required Terms of Reference and time period. The Government intends to take a more active part in management of procurement in general, and technical assistance, specifically. This would include more input into the design of terms of reference, selection of consultants and management of assignments. Further, there would be substantial strengthening of the Government's capacity to evaluate contractor/supplier performance.

4. Also the additional training is required to all PIUs in the sphere of arbitrage, termination of the contracts and consequent activities in this connection. None of the PIUs has such experience in order to remedy a situation in case of default by the consultants.

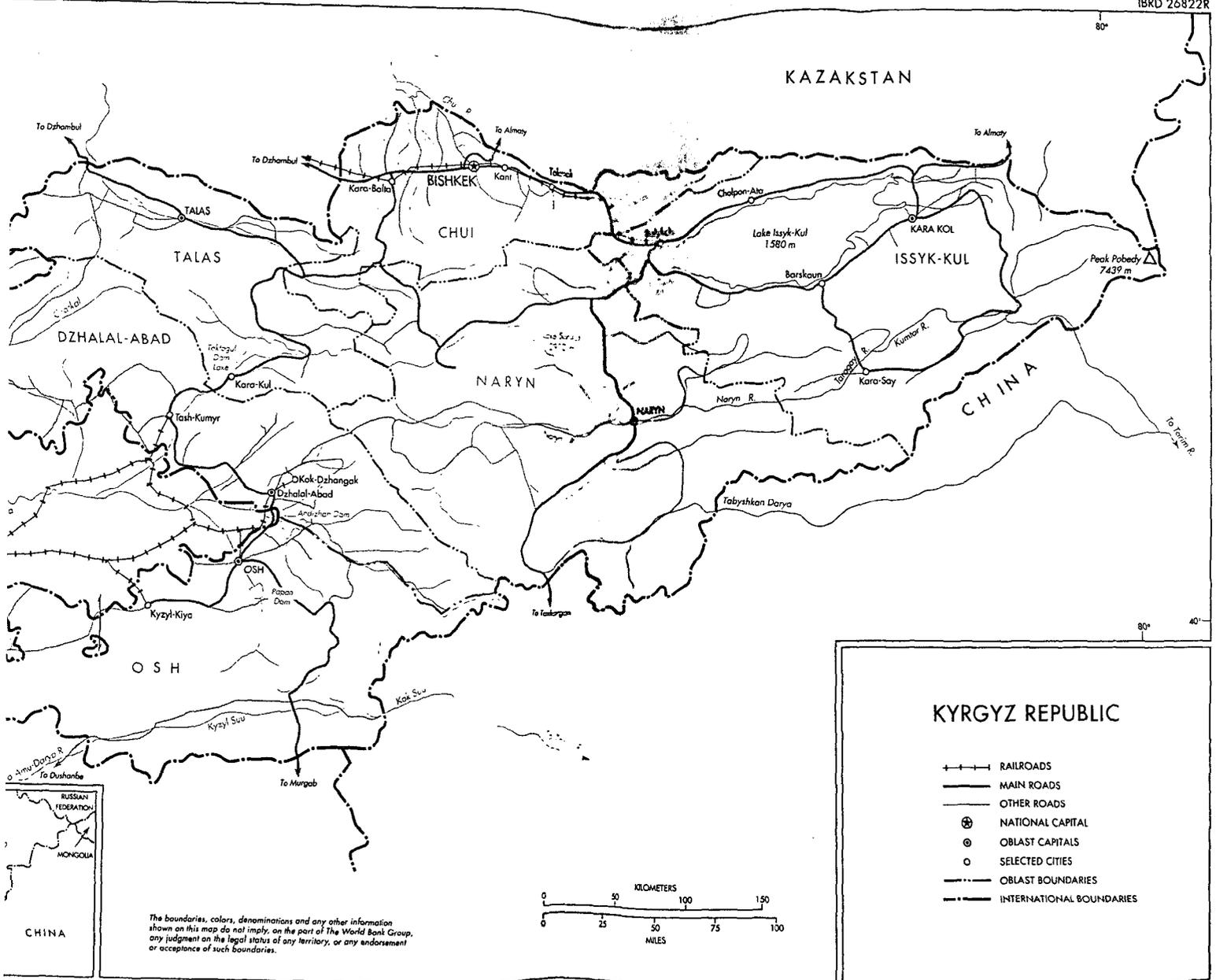
5. In case of procurement of pesticides, herbicides and veterinary medicines the Ministry of Agriculture was not in a position to distribute the purchased goods. The matter of such situation is the inability of farmers to pay for the imported products, procured at a market price through ICB, because of cessation of centralised financial support. But it does not mean that agriculture does not need these goods. Taking into consideration this reason, the Government of the Kyrgyz Republic issued a special decree to remedy the situation. In accordance with this decree the Ministry of Finance provided the credit "in form of goods" to allow the farmers to receive the pesticides, herbicides and veterinary medicines and be ready for the harvest or other seasons. This measure essentially facilitated the sale of these products to users. In this respect, it is very important to analyse carefully the current situation (market price, availability of goods in stocks, warehouses, ability of goods to compete in a local market and be in need by the end-user after procurement at market price) prior to ratification of the list of goods to be procured.

6. The involvement of domestic manufactures, suppliers, consultancy firms and individuals is also a sensitive theme. In our opinion, the domestic market should not be limited in participation in supply of equipment, provision of services etc. In some cases, the domestic qualification and knowledge, intellectual capability surpassed the foreign consultant expertise.

OVERALL REVIEW

1. The objectives of all three components of the Rehabilitation Credit were achieved. The amount of the Credit was fully disbursed. The inputs provided under the Credit in forms of critical imports in key sectors were made to limit its rapid decline and rehabilitate the Kyrgyz economy in transition period. Technical assistance to a number of the Government agencies was provided in form of consultancy services in different fields such as legislation, financing, privatisation thus reinforcing the implementation of the Government Economic Reform Program, restructuring of the Government and improving its institutional capacity in order to meet the requirements of the market economy. The foreign exchange component was used in providing support to the newly introduced national currency, contribution to an inter-bank market in convertible currency and improving an accessibility of private sector to foreign exchange.

2. Mutual assistance and close co-operation with the World Bank, Resident Mission of the World Bank and the Kyrgyz Republic was established during the implementation process. The objective of establishment of policy dialogue was successfully achieved. This allowed to set up all current and future issues in further assistance in Economic Reform Program. The background for future co-operation between the World Bank and the Kyrgyz Republic was established and strengthened. The gained experience and practice are very useful for further relationship development.



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