

Kyrgyz Republic: 2002 Article IV Consultation, Second Review Under the Poverty Reduction and Growth Facility, and Request for Waiver of Performance Criterion— Staff Report; Staff Supplement; Public Information Notice and Press Release on the Executive Board Discussion; and Statement by the Executive Director of the Kyrgyz Republic

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of a combined discussion of the 2002 Article IV consultation with the Kyrgyz Republic, second review under the Poverty Reduction and Growth Facility, and request for waiver of performance criterion, the following documents have been released and are included in this package:

- the staff report for the combined 2002 Article IV consultation, second review under the Poverty Reduction and Growth Facility, and request for waiver of performance criterion, prepared by a staff team of the IMF, following discussions that ended on **November 5, 2002**, with the officials of the Kyrgyz Republic on economic developments and policies. **Based on information available at the time of these discussions, the staff report was completed on February 5, 2003.** The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.
- a staff supplement of **February 14, 2003** updating information on recent economic developments.
- a Public Information Notice (PIN) and Press Release, **summarizing the views of the Executive Board as expressed during its February 20, 2003, discussion** of the staff report on issues related to the Article IV consultation and the IMF arrangement, respectively.
- a statement by the Executive Director for the Kyrgyz Republic.

The document(s) listed below have been or will be separately released.

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

*May also be included in Staff Report

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

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KYRGYZ REPUBLIC

Staff Report for the 2002 Article IV Consultation, Second Review Under the Poverty Reduction and Growth Facility, and Request for Waiver of Performance Criterion

Prepared by the European II and Policy Development and Review Department
(in consultation with other departments)

Approved by Julian Berengaut and Michael Hadjimichael

February 5, 2003

- Discussions for the 2002 Article IV consultation and the second review under the Poverty Reduction and Growth Facility (PRGF) were held in Bishkek from October 18 to November 5, 2002. The staff team consisted of Mr. Saavalainen (Head), Messrs. Luna, Zeuner, and Medas (EP) (all EU2); Ms. Fernandez (EP, FAD); Messrs. Abrams and Sullivan (all MAE); Mr. Aiyar (EP, PDR), and Mr. Kenjeev (BLS-interpreter). Mr. Mani (FAD) worked closely with the mission on environmental issues. Mr. Odling-Smee joined the mission during October 30–November 3, 2002. Mr. Mukhopadhyay, the Fund's resident representative in Bishkek, assisted the mission.
- The mission held meetings with President Akayev, the Prime Minister, the Deputy Prime Minister, the Ministers of Finance, and Agriculture; the Governor of the National Bank (NBKR), members of the Parliament, and other senior officials. The mission also met with representatives of civil society, private and public enterprises, the banking sector, and the diplomatic community.
- During the last Article IV consultation on November 30, 2001, Executive Directors commended the authorities for good progress in macroeconomic stabilization and the ambitious debt reduction strategy. While recognizing the improved fiscal performance, they underscored the importance of strengthening tax collection and expenditure management. On structural reforms, Directors urged the National Bank to improve bank supervision and take further steps to develop the banking system. Directors expressed concern about weak governance and called for further action in this area. In completing the first review on July 1, 2002, Directors commended the authorities for good policy performance, but were concerned about the output decline. They stressed the need to diversify the economy by strengthening the export potential. For poverty reduction, Directors underscored the need to sustain economic growth.
- The main contributors to this report are Tapio Saavalainen and Francesco Luna, with inputs from Joerg Zeuner, Paulo Medas, Gilda Fernandez, and Shekhar Aiyar.

	Contents	Page
Executive Summary		4
Figures		
1. Performance Under the Program.....		10
2. Baseline and Low-case Scenarios		13
Text Boxes		
1. 2003 Tax Policy Package.....		17
2. Debt Sustainability		19
3. Main Recommendations of the Financial Sector Assessment Program		20
Tables		
1. Quantitative Program Targets		25
2. Prior Action, Structural Performance Criteria and Benchmarks Through end-September 2002.....		26
3. Selected Economic Indicators, 1999–2006.....		27
4. Medium-Term Projections, 1999–2006.....		28
5. General Government Finances.....		29
5.1 State Government Finances		30
5.2 State Government Finances		31
6. Social Fund		32
7. Medium-Term Expenditure Framework for General Budget (excluding PIP), by Functional Classification.....		33
8. National Bank of the Kyrgyz Republic Accounts, 2001–2003.....		34
9. Monetary Survey, 2001–2003.....		35
10. Quarterly Balance of Payments, 2000–2003.....		36
11. External Financing Requirements, 2000–2006.....		37
12. Medium-Term Balance of Payments, 2000–2010.....		38
13. Indicators of Fund Credit, 2000–2006.....		39
14. Prospective Use of Fund Resources, 2001–2006.....		40
15. Reviews and Disbursements Under the Three-Year PRGF Arrangement.....		41
Appendixes		
I. Fund Relations.....		42
II. Relations with the World Bank Group		44
III. Relations with the Asian Development Bank		47
IV. Relations with the European Bank for Reconstruction and Development		48
V. Technical Assistance Provided by the Fund, 1997–2002.....		49
VI. Statistical Issues		52

VII. Safeguards Assessment—Summary of Conclusions..... 55

Attachments

I. Letter of Intent..... 56

Executive Summary

In 2002, price stabilization continued, but growth was disappointing. The 12-month inflation at end-November fell to 2.7 percent from 3.7 percent during 2001, and nominal and real interest rates have declined. Real GDP dropped by 1.7 percent in January-November over the same period a year ago. This decline was due to temporary factors in gold and energy production and growth is expected to rebound in 2003. Monetary aggregates grew rapidly, while the nominal exchange rate appreciated by 3½ percent, indicating strong demand for money.

All performance criteria but one were observed for the period under review (April 1, 2002 through September 30, 2002). The end-September targets on net international reserves (NIR) and net domestic assets (NDA) were met with wide margins. The fiscal deficit was within the program limit, despite the shortfall in revenues owing to the decline in real GDP and the target on tax collection was met thanks to improved tax administration. The continuous performance criterion on the non-accumulation of external arrears was breached, but the underlying obligation was cleared in early January 2003.

The 2002 Article IV discussions focused on policies necessary to achieve the program's medium-term objectives under three constraints: declining gold production, high external debt, and widespread poverty. The staff and the authorities agreed that recent financial policies had been appropriate leading to a successful price stabilization as a necessary condition for sustained growth. Sound productivity growth and wage restraint are essential to preserve the cost competitiveness of Kyrgyz exports and diversify the economy. Strategy discussions also underscored the importance of containing fiscal deficits to achieve external debt sustainability. To keep growth at 5 percent a year, strong structural policies are necessary especially to improve business climate and financial intermediation.

The second-year program aims at a real GDP growth of 5.2 percent in 2003, consolidation of price stabilization, and further structural reforms. The fiscal deficit is programmed to decline to 4.7 percent in 2003 from the projected 5.6 percent in 2002. To increase tax collection, the authorities will extend VAT to large agricultural producers. The growth of monetary aggregates should moderate compared with the pace of 2002 as remonetization slows. The NBKR will maintain a cautious policy stance consistent with the 4.4 percent inflation target. Structural policies will concentrate on two main areas: a banking reform and a new initiative to improve governance. The banking reform should ensure better bank supervision and a further consolidation of the sector. The governance reform will aim at reducing the scope for corruption and state capture.

I. INTRODUCTION

1. On December 6, 2001, the Executive Board approved the Kyrgyz Republic's request for a three-year arrangement under the Poverty Reduction and Growth Facility (PRGF) (IMF C.R. No. 01/223).¹ The first review of the program was completed on July 1, 2002 with a disbursement of SDR 11.72 million (IMF C.R. No. 02/150). On October 31, 2002, the total Fund credit outstanding to the Kyrgyz Republic was SDR 139.2 million, or 157 percent of quota. On completion of the second review, a disbursement of SDR 11.72 million would become available. In the attached Letter of Intent (LOI), the government presents the policies for the period October 1, 2002 to September 30, 2003 and requests a waiver for the nonobservance of the continuous performance criterion on external arrears.

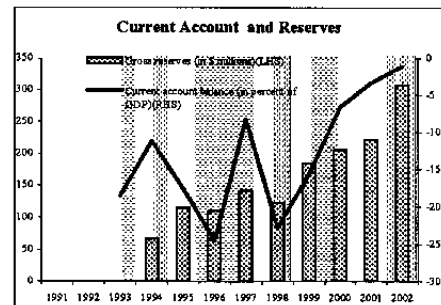
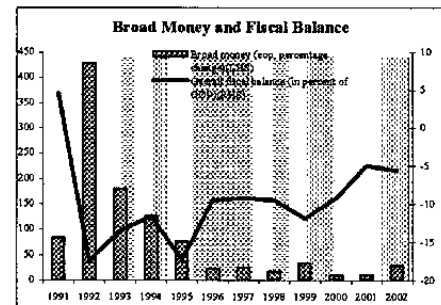
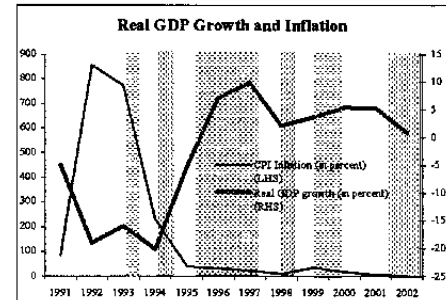
II. ACHIEVEMENTS AND SETBACKS UNDER THE PAST PROGRAMS

2. The Kyrgyz Republic has received financial support from the Fund since 1993.² Over this period, although economic policies have succeeded in stabilizing prices and restoring growth, structural reforms have lagged and external debt has reached unsustainable levels. The authorities identified three different periods during the ten years of transition. The initial period after independence until 1994 was "euphoric" despite the continuous output contraction common to the early stages of transition in other countries as well. Reforms started with great enthusiasm sparked by the new economic and political

¹ Access was granted at 82.6 percent of quota (SDR 73.4 million) for the period October 1, 2001–September 30, 2004.

² After the 1993 stand-by arrangement (SBA), further support was provided under the Enhanced Structural Adjustment Facility (ESAF) in 1994, the Structural Transformation Facility (STF) in 1995, the Poverty Reduction and Growth Facility (PRGF) in 1998 and in 2001.

Macroeconomic Performance, 1991-2002 (proj.) 1/



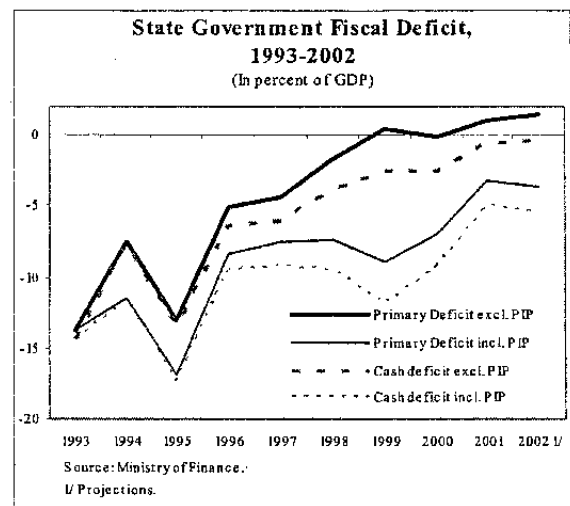
Source: Kyrgyz authorities.

1/ Stand-by Arrangements (May–April 1993), ESAF Trust Fund (July 1994–Mar 1998), PRGF 2 Trust Fund (June 1998–July 2000), PRGF 2 Trust Fund (December 2001–December 2004). Shaded areas represent periods when the program was on-track.

system. The policy climate was favorable at the time of the first of the four IMF-sponsored programs. Foreign reserves improved, inflation fell, exchange rate stabilized, and several first-generation structural reforms were implemented.³ The country was perceived as one of the front-runners in economic transition among the CIS countries. As a result, the government was able to attract significant amounts of donor assistance. However, the first program went offtrack in the first half of 1994 because of large directed credits, inadequate progress in restructuring loss-making public enterprises, and delays in formulating the 1994 budget.

3. A period of “dismay and frustration” (1995–2000) came with the realization that despite the sacrifices of the population, living standards were not improving rapidly.

The 1994–97 ESAF-supported programs went repeatedly offtrack. For example, in 1995, nontax revenue fell significantly short of targets and the central bank monetized the resulting fiscal gap. The pension reform stalled, and external debt arrears increased. The arrangement expired in 1998 after delays in implementation. In 1999, weak expenditure management led to large spending arrears and two reviews under the new PRGF arrangement were not completed because of fiscal slippages. Fiscal deficits remained high, in part, because of the inability to manage effectively the rapidly expanding Public Investment Program (PIP) which peaked at 9.4



percent of GDP in 1999. Although the primary balance (excluding PIP) has recorded a surplus since 1999, the external debt rose to 130 percent of GDP at end-2000 after the sharp nominal depreciation of the som following the Russian financial crisis. Apart from the exchange rate depreciation, the PIP was the main contributor to the external debt but it failed to produce enough growth to avoid the debt problem. In part, this reflected the high share of infrastructure investments in the PIP which take a long time to produce growth. Government debt service increased, thus compressing public savings with a negative contribution to the economy's saving-investment balance.

³ Prices were fully liberalized by 1994 and import tariffs were reduced well below the regional average. After a rapid small-scale privatization, demonopolization and sales of large state-owned enterprises (apart from utilities) started in 1994 under the World Bank sponsored privatization program. Financial reforms started early with a new legislation on the central bank and commercial bank accounting standards. Land reform started in 1992 and the process continued during the first half of the 1990s introducing property rights on land.

4. **Structural reforms in the second half of the 1990s progressed slowly.** The privatization program for medium- and large-enterprises was only partially successful as insiders gained control over much of the former state-owned enterprise block. Also, several program benchmarks on fiscal reforms were not met. In 1998–99, after the Russian crisis, the banking sector faced a major crisis as the largest three commercial banks were bankrupt. A government default on a series of recapitalization bonds and a currency mismatch between assets and liabilities contributed to these bankruptcies. Overall, the implementation rate for structural conditions (i.e., performance criteria and benchmarks) under the Fund-supported programs fell to 63 percent in the period 1998-2000 from over 80 percent in 1994–97.

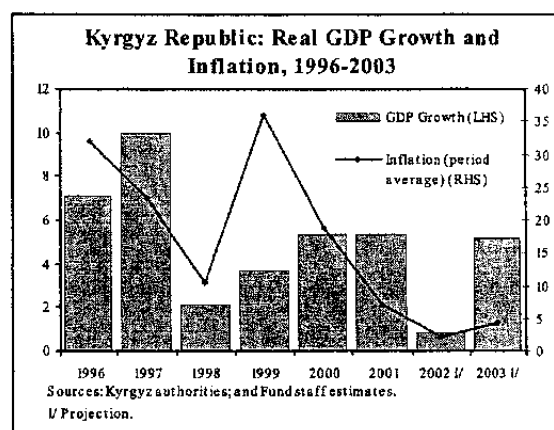
5. **The authorities characterized the period starting in 2001 as the time of “realism and pragmatism.”** Pragmatism came with the acceptance that much work remained to be done, and there were no easy solutions. Constraints imposed by the high external debt and the obvious need to restructure external liabilities also contributed to greater realism. The authorities believe that the program ownership is now stronger as the economy is moving in the right direction with low inflation, a stable exchange rate, and resumed growth. Their confidence was also boosted by the well-appreciated debt rescheduling from the Paris Club providing a temporary relief from the heavy debt burden.⁴ However, the civil society remains critical with regard political reforms and economic results that are late in coming. Although the government has embarked on a comprehensive constitutional reform trying to calm the political climate, tensions are likely to remain high because of the approaching parliamentary and presidential elections in 2005.

6. **The Kyrgyz economy began to grow in 1996 with an average rate of 5 percent in the following five years.** Improving total factor productivity was the main source of growth. A comprehensive land reform was completed in 1996 establishing 72,000 private farms, which boosted yields. With the new Kumtor mine, gold production expanded rapidly improving aggregate industrial productivity, and hydro-power output benefited from high demand of irrigation water in Uzbekistan and Kazakhstan in 2000–01. In 2001–02, nongold, nonenergy industrial production recovered as well. Employment increased in agriculture and services absorbing labor from declining state-owned industries, but the capital stock declined despite extensive investment in infrastructure under the PIP. With economic growth, poverty headcount has decreased by almost 20 percent since 1998, especially in rural areas. Income distribution improved and poverty declined in all regions. Overall, 47 percent of the population were poor at end-2001 down from 57 percent in 1999.

⁴ In March 2002, the Paris Club granted a flow rescheduling of the Kyrgyz debt for 2002–04.

III. PERFORMANCE UNDER THE CURRENT PROGRAM

7. In January–November 2002, real GDP declined by 1.7 percent over the same period a year ago. This reflected a landslide in the Kumtor gold mine and a sharp decline in hydropower production owing to weather conditions.⁵ Excluding gold and energy, real output grew by 3.4 percent. Main contributions came from agriculture, and services, the latter largely reflecting tourism and the spending from the new military base.⁶ With a return of Kumtor's high-grade ore production to the earlier-planned level and normal energy production, real GDP is projected to grow by 5.2 percent in 2003.



8. Prices continued to stabilize as the confidence in local currency increased and the exchange rate vis-à-vis the U.S. dollar and the Russian ruble strengthened. During the first-year program (October 1, 2001–September 30, 2002) the 12-month rate of inflation fell from 5.3 percent to 3.5 percent, and further to 2.3 percent at end-November 2002. The nominal exchange rate appreciated by 3.6 percent vis-à-vis the U.S. dollar, and the nominal and real interest rates declined from 19 and 13 percent to 10 and 7 percent respectively. Narrowing interest rate differentials between domestic and foreign short-term securities and the declining ratio of foreign deposits to broad money suggest that confidence in economic policies improved significantly during the first-year program.

9. The current account improved despite a weaker trade balance. In 2002, the volume of gold exports fell by over 30 percent because of the Kumtor accident, although the impact on the value of exports was mitigated by higher gold prices. Energy exports halved from their 2001 level, mainly because of abundant rainfall in neighboring Uzbekistan and Kazakhstan which reduced water release from the Kyrgyz reservoirs.⁷ On the other hand, expenditures by the new military base generated \$30 million of net exports. This, coupled with stronger tourism and transport receipts and greater official transfers more than compensated the negative effects of gold and energy on the trade balance. As a result, the current account deficit narrowed from 3.3 percent of GDP to 2.8 percent in 2002. With a

⁵ While Kumtor's production continued without interruption, access to high-grade ore was blocked thus reducing the value added of the output.

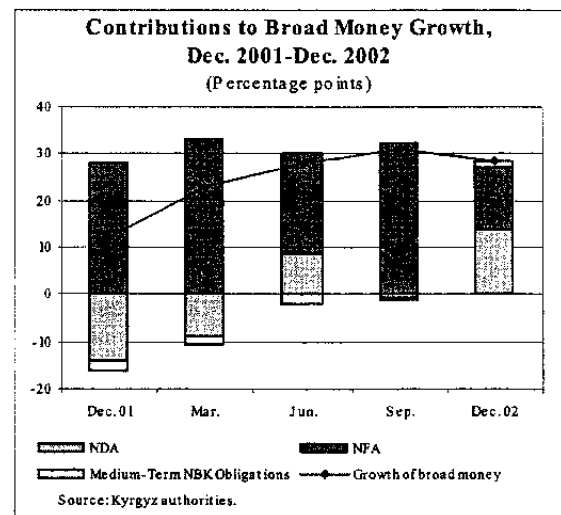
⁶ Manufacturing, excluding gold and electricity, grew by 3.1 percent.

⁷ Water is released for the neighboring countries' irrigation purposes and the generated hydro-power is exported under barter arrangements with Uzbekistan and Kazakhstan.

surplus in the capital account and Paris Club debt restructurings, official gross reserves reached 4.5 months of imports by year-end.

10. **Despite the revenue shortfall from Kumtor, the end-September 2002 fiscal targets were met.** In the first three quarters of 2002, the fiscal deficit was 4.7 percent of GDP—lower than the program ceiling of 5.6 percent of GDP mainly on account of lower-than-projected public investment spending. The tax collection target was met mainly through strong administrative measures. Special task forces were set up both at the central and local government levels to increase tax collection and reduce arrears. In addition, customs collection increased by 39 percent during the first nine months reflecting improved administration. Weaker tax revenue in October and November suggests, however, that the good revenue performance in the third quarter was in part achieved through advance payments. At end-September, there were no outstanding budgetary arrears by the central government on items covered by the performance criteria.⁸ However, the continuous performance criterion on the non-accumulation of external arrears was breached, but the underlying obligation was cleared in late January 2003.⁹

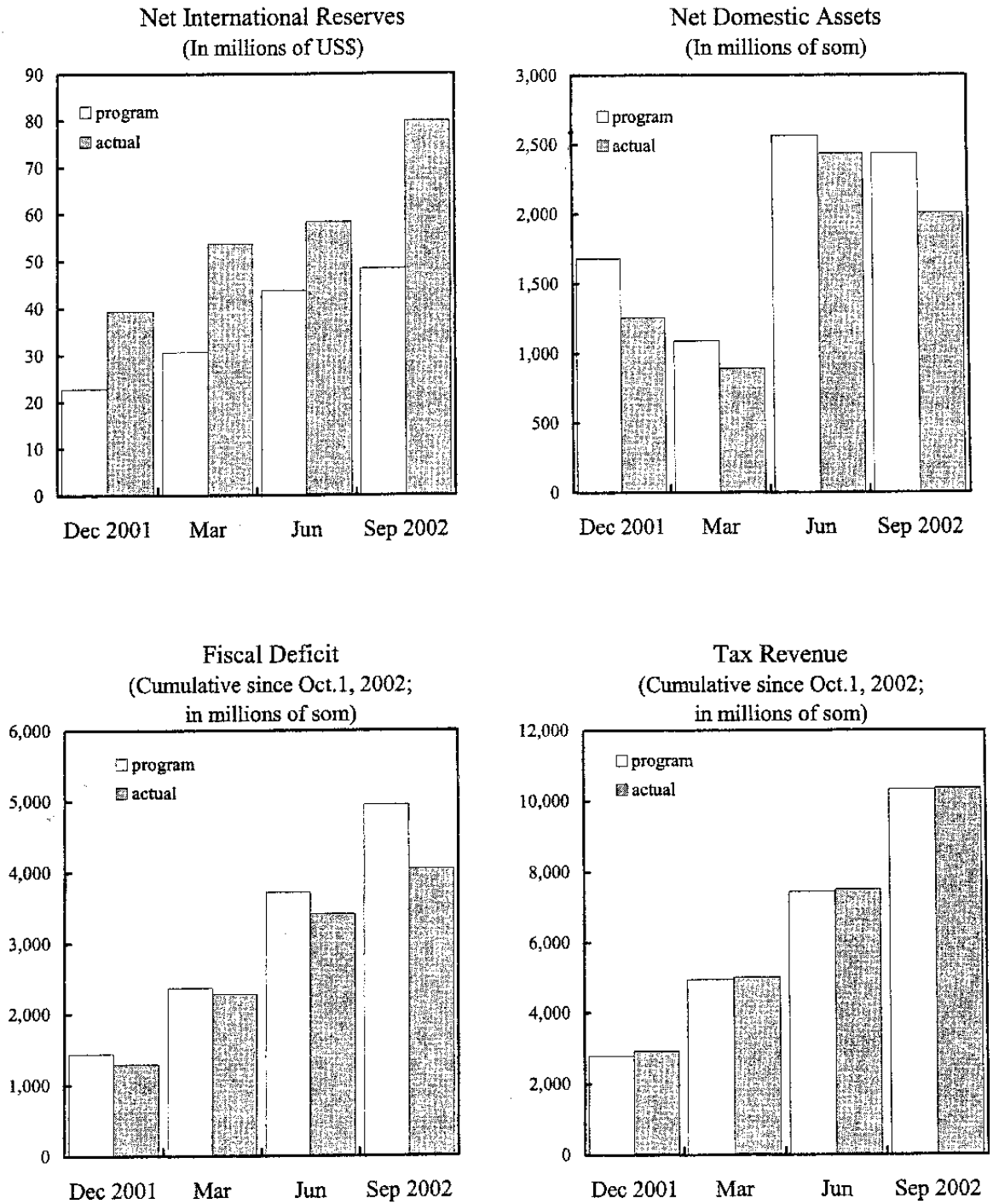
11. **The program targets on net international reserves (NIR), and net domestic assets (NDA) were observed with wide margins (Figure 1).** NIR exceeded the programmed floor by 23 percent of reserve money as the NBKR bought \$ 9.1 million from the foreign exchange market in July-September. The resulting growth in broad money reflected a significant remonetization of the economy. NDA were below the adjusted program ceiling by 6.3 percent of reserve money as part of the foreign exchange inflow was sterilized by increasing government deposits in the central bank. Credit growth to the private sector remained moderate during 2002 (6.7 percent at end-November).



⁸ Other arrears, notably those on VAT refunds and counterpart financing of the PIP, also declined during 2002.

⁹ An international arbitration tribunal in Stockholm, ruling on a commercial dispute related to the failed privatization of KyrgyzTelecom, determined a fee of \$1.5 million to be paid for Raiffeisen Bank by July 12, 2002. This payment remained in arrears until late January 2003.

Figure 1. Kyrgyz: Performance Under the Program
(December 2001–September 2002)



Source: Kyrgyz authorities; and Fund staff estimates.

12. **The end-September 2002 structural performance criteria and benchmarks were observed.** Several amendments to legislation were presented to Parliament. According to these amendments, in liquidation cases, the court should accept only a bank's financial statement confirmed by the NBKR as the factual representation of that bank's financial position (a performance criterion). Amendments to the Law on Licensing (structural benchmark) stipulate that licensing associated with financial institutions will be regulated only by banking laws thus removing an inconsistency with the Law on Licensing. Following discussions with the Fund-World Bank FSAP missions (structural benchmark), the NBKR also introduced stricter supervisory standards and approved a banking sector reform strategy. On the other hand, the NBKR also experienced some setbacks. The liquidation case against Asia Universal Bank, whose asset quality remains dubious, was rejected by a court in the absence of sufficient evidence. In addition, the central bank lost a court case against Krambds Bank last summer, and, in September, was ordered by a court to return the license to Issyk Kul Bank.

13. **Progress was made in fiscal reforms.** The government issued a resolution to increase enforcing and monitoring powers of the Large Taxpayer Unit (performance criterion). The Treasury established a new Financial Division which prepared its first short-term cash flow forecast (structural benchmark). Finally, the government approved the restructuring plan for the Ministry of Finance. It includes a reduction of overstaffing, a reorganization of the departments with emphasis on policy-making and streamlining budgetary processes (structural benchmark). In addition, the NBKR and the Ministry of Finance, with assistance from an MAE mission, concluded the regularization of their financial relations.¹⁰

14. **The privatization of strategic state-owned enterprises is moving ahead.** A tender for KyrgyzTelekom was issued on September 9, and closed on December 10, 2002: 13 offers were received, all from foreigners. In collaboration with the World Bank, the authorities are revising their strategy for energy distribution companies (DISCOs) and are considering giving at least one DISCO in concession to a foreign managing company. In April, 2002, the government also took steps to reduce the quasi-fiscal deficit by cutting the number of privileged users and increasing electricity tariff on households. The World Bank had projected that, as a result of these measures, the quasi-fiscal deficit would decline by two percentage points to 4.1 percent of GDP by end-2002. However, more recent data suggest that the increase in tariffs was in part offset by lower collection rates and increased "technical losses," including theft.

¹⁰ As part of this operation, som 2.7 billion of interest bearing government securities were issued to the NBKR to substitute for noninterest-bearing securities with infinite maturity. Som 350 million were marketable T-bills. The agreement between the Ministry of Finance and the NBKR follows the Fund Safeguard Assessment recommendations (see Appendix VII).

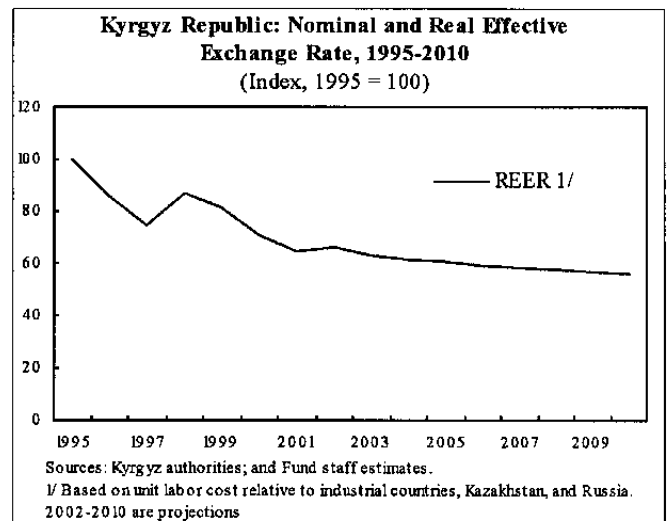
IV. REPORT ON THE DISCUSSIONS

15. **The authorities' draft National Poverty Reduction Strategy (NPRS) provided the basis for discussions on the medium-term strategy.** The NPRS underlines that continuous poverty reduction can be achieved only with sustained economic growth. In 2003-2006 and beyond, real GDP is projected to increase on average by 5 percent a year mainly through productivity gains stemming from structural reforms and more efficient use of capital and labor (Figure 2).¹¹ The authorities argued that this projection, which is the baseline scenario in their NPRS, represents a conservative estimate. The NPRS high-case scenario assumes that GDP could grow by 7 percent a year in the event that the authorities are successful in their efforts to attract more foreign direct investment. However, the effect of the 1998 Russian crisis, volatile energy exports, and the large impact of the recent landslide at the Kumtor gold mine underscore the vulnerability of the Kyrgyz economy and the need for caution in growth projections. Under any scenario, the medium-term strategy needs to aim at diversifying the economy by fostering export-led growth supported by small and medium-size enterprises.

A. Medium-Term Strategy

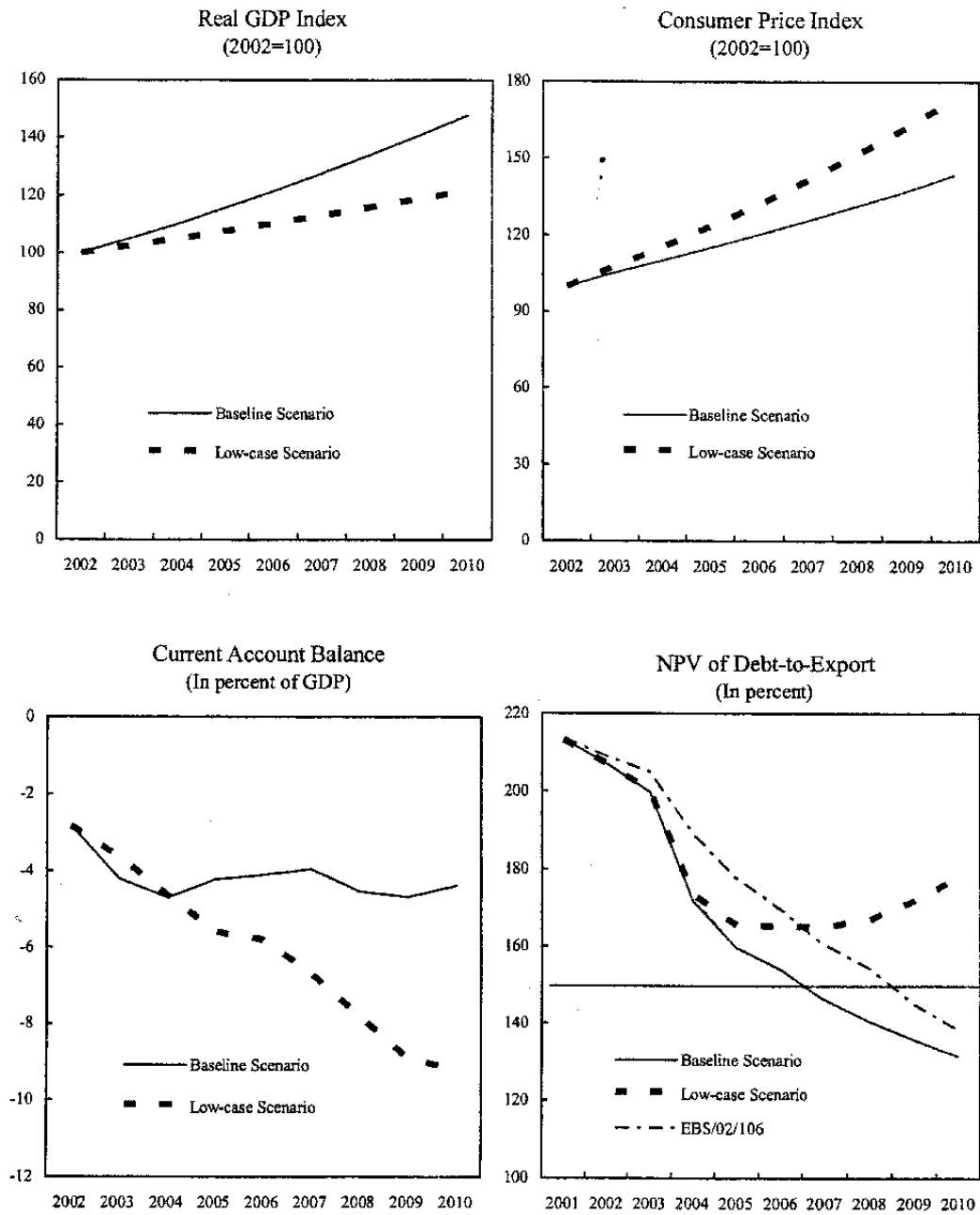
16. **The strategy discussions focused on alternative policies to attain a 5 percent growth path under three constraints: the projected decline in gold production, the need to lower external debt, and low domestic savings because of high poverty.** To achieve the growth objective, export volumes should grow 4.5 percent a year during the remainder of the decade. The negative impact of the declining gold production should be offset by other manufacturing enterprises, agriculture, and tourism. The authorities agreed that inflation should stabilize at 4 percent a year to allow a continued relative price adjustment of public utilities.

Strong productivity growth is critical to preserve cost competitiveness and boost nongold exports. Productivity growth in the tradable goods sector is expected to be about 2-3 percentage points higher than in the nontradable sector and—because of the low starting level—also higher than in competitor countries. This should, in the absence of external and domestic shocks, ensure a



¹¹ Recent and prospective sources of growth are discussed in the Selected Issues paper Chapter II.

Figure 2. Kyrgyz Republic. Baseline and Low-case Scenarios



Source: Kyrgyz authorities; and Fund staff estimates.

competitive real exchange rate.¹² Real wages are expected to grow less than productivity because of high (hidden) unemployment.¹³ However, wage restraint is still necessary because of the current low profitability of the tradable goods sector. The authorities argued that their strategy hinges on open access to foreign markets of Kyrgyz exports. They stressed that tariff and nontariff barriers are currently hindering trade with Uzbekistan, Kazakhstan and Russia.¹⁴ Staff agreed with the need to reduce trade barriers, but noted that a strong cost competitiveness could in part compensate for the extra transport costs, and help Kyrgyz producers gain market shares. Nevertheless, staff advised the authorities to search the cooperation of neighboring countries to remove unofficial constraints in the context of the CIS7 initiative and through WTO.

17. The debt strategy targets reducing the net present value of external debt from 213 percent of exports in 2001 to below 150 percent by 2007. To achieve this target, it will be critical to reduce the fiscal deficit, promote export growth, and be cautious in external borrowing. To lower the public external debt to the targeted level requires decreasing the primary fiscal deficit from an average of 7½ percent in 1996–2000, to below 1 percent by 2006. This could be achieved mainly through streamlining the Public Investment Program and improving tax collection.¹⁵ Such an ambitious fiscal adjustment is consistent with an average current account deficit of about 4.3 percent of GDP in 2003–2006. Assuming an increase in FDI inflows, low interest rates on loans relative to the targeted GDP growth, and some real appreciation of the som, debt dynamics suggest the NPV debt-to-GDP ratio would

¹² The real exchange rate (measured by relative unit labor costs) depreciated by about 40 percent in 1996–2001. As of end-September 2002, the average monthly dollar wage at \$32 is significantly lower than in major trade partner countries (in Kazakhstan \$133; in Russia \$142). Real exchange rate developments are analyzed in detail in the Selected Issues paper Chapter III.

¹³ Some estimates suggest that the true unemployment rate (including the hidden surplus of labor) could be as high as 20 percent compared with the official unemployment rate of about 8 percent in 2002. Although the open employment is expected to increase only slowly, growth will be supported by a declining hidden unemployment which would be reflected in higher total factor productivity.

¹⁴ Trade restrictions against the Kyrgyz Republic are analyzed in the Selected Issues paper Chapter IV.

¹⁵ Tax collection is expected to improve in the medium term as the VAT tax base will be broadened to increasingly include agricultural produce and as the newly-organized Large Taxpayer's Unit will gradually become more effective. These reforms are expected to more than offset the decline in revenue from gold production in the medium term. Revenue from Kumtor is expected to decline from 1.1 percent of GDP in 2003 to 0.6 percent of GDP in 2006. Gold production from Kumtor is expected to cease by 2010 while some new, albeit smaller gold deposits are expected to come on stream (e.g., the Jeeroy mine).

more room for social spending, the authorities aim at improving tax collection and reallocating public resources from nonproductive uses to social purposes. The staff stressed that because of the narrow room for maneuver in macroeconomic policies, the authorities should avoid higher fiscal deficits to finance social spending but instead seek grants to help finance specific poverty reduction programs. At the same time, they should be cautious not to establish unsustainable spending mechanisms with temporary foreign aid.

B. Policy Mix for the Second-Year Program

21. **The key macroeconomic objectives for the second-year program are a return to a higher growth path while continuing with low inflation.** With the recovery of production at the Kuntor gold mine, the staff believes that the authorities' growth projection of 5.2 percent is feasible. The targeted 12-month rate of inflation of 4.4 percent incorporates a onetime increase in prices because of extending VAT¹⁷ to large agricultural producers in April 2003 and implies a 3 percent underlying inflation.

22. **Tax reform was the most difficult topic in program discussions.** The mission pushed strongly for introducing significant but politically sensitive measures to broaden the tax base—the extension of the VAT to large agricultural producers, VAT on utilities and higher electricity tariffs, and higher land tax rates. After difficult and lengthy discussions, the authorities agreed to present to parliament a proposal to extend the VAT to large agricultural producers.¹⁸ This measure is expected to generate 0.3 percentage point of GDP in additional tax revenue in 2003, and more than one percentage point over the medium term. On power tariffs, the authorities requested more time to study the poverty implications and consult with the World Bank staff.¹⁹ The mission also proposed a 20 percent increase in the land tax rate to strengthen local governments' revenue base and increase Social Fund payroll contributions from the agricultural sector.²⁰ The authorities were not, however, in favor of this proposal given the present sensitive political situation.²¹ The mission also discussed the authorities' proposal to reduce excise taxes on gasoline. It pointed out the revenue-reducing impact of such a measure, and the authorities decided to set up a working group to study this matter

¹⁷ For a detailed analysis of this measure, see the Selected Issues Paper, Chapter V.

¹⁸ The Parliament is expected to approve the tax policy package as a prior action before the Board meeting scheduled for February 19, 2003.

¹⁹ Energy sector reform, including the tariff increases, is subject to World Bank conditionality under the program supported by the Consolidated Structural Adjustment Credit.

²⁰ Social security contributions of the agricultural sector are based on the land tax.

²¹ Since the events in the southern part of the country in early 2002, where five people were killed during a violent repression of a demonstration, the political situation has remained tense.

decline to around 50 percent by 2007 from 81 percent in 2001. Assuming a debt stock relief from Paris Club creditors after a successful implementation of the current PRGF-supported program, this ratio would be consistent with the NPV public debt-to-exports ratio of about 145 percent.

18. **The agreed medium-term strategy (2003–2006) is consistent with the original program’s saving-investment analysis (Table 4).** The investment ratio is projected to increase to 23.5 percent in 2006 from 19.4 percent in 2002. This is consistent with a 5 percent growth rate even if the efficiency of investment would decline somewhat from its average 1996-2001 level. Private investment should drive capital accumulation as the externally financed Public Investment Program will be streamlined from 5.1 percent of GDP in 2002 to 3 percent by 2006 and kept at that level from then on. For private investment including FDI, the business climate needs to improve significantly which calls for a comprehensive governance reform to reduce corruption and state capture. The increase in national savings by 2.9 percentage points of GDP over 2002-2006 would reflect the fiscal adjustment and improved enterprise profitability through productivity gains. To promote private savings and improve the efficiency of financial intermediation, the reform of the banking system is important. The use of foreign savings to finance investment could increase by 1.3 percentage point of GDP between 2002 and 2006 as a somewhat higher current account deficit, supported by foreign direct investments,¹⁶ is consistent with the debt sustainability target.

19. **The authorities are aware that poverty reduction objectives and parliamentary and presidential elections in 2005 are likely to increase pressures for higher fiscal spending.** These pressures and the difficult task of reducing corruption and state capture are the main risks for the success of the strategy. Renewed fiscal slippages and a failure to improve business climate could trigger macroeconomic imbalances through rekindling inflation and depreciating nominal exchange rate. Inflation could rise to 7-8 percent and undermine competitiveness. Such policy slippages would lead to the low-case scenario of Figure 2. In this scenario real GDP would grow on average by only 2½ percent a year with export volumes rising only by 2 percent a year in 2003–2010. External debt ratios would start growing rapidly again in 2006 even with the debt stock relief from the Paris Club.

20. **Given the weak financial position of the government, the authorities count mainly on economic growth to reduce poverty.** According to World Bank estimates, for every 1 percent growth in per capita consumption, the headcount index of poverty declines by 0.8 percentage points. Therefore, even without changes in income distribution, the baseline scenario would result in a decline of poverty by 15 percentage points by 2006. To generate

¹⁶ In 2002-2006, FDI flows are projected to increase from 1 percent of GDP to 2.4 percent of GDP, a level significantly lower than the average of 4 percent in the second half of the 1990s. These investments are expected to concentrate in gold mining, light industry, food processing, and tourism.

23. **Several other factors will help raise revenue collection in 2003.** In particular, revenue is expected to increase once the Kumtor gold mine resumes normal operations and as several of its tax holidays expired in the second quarter of 2002.²² In addition, the full-year effect of the recent elimination of various VAT exemptions, the introduction of the excise tax on jet fuel, and the removal of the VAT exemption on PIP imports are expected to improve revenue collection next year. In the 2003 budget proposal, the authorities also introduced a new property tax, a higher excise tax on liquor, and higher presumptive tax rates. Based on the work of the FAD environmental mission, a unified environmental tax will be introduced to replace the existing various fees.²³ Overall, the general government tax-to-GDP ratio is expected to increase to 18.0 percent of GDP in 2003 from the projected 16.9 percent in 2002 (Box 1).

Box 1. 2003 Tax Policy Package	
Items	Revenue Impact (in percent of GDP)
New Measures	0.7
VAT on large agricultural producers	0.3
Higher presumptive tax rates	0.1
New property tax	0.1
Higher excise tax on liquor	0.1
Improved tax administration	0.1
Other Factors	0.5
Elimination of VAT exemptions and excise tax on jet fuel	0.1
Higher Kumtor revenue collection	0.4
Total Impact	1.2

Source: Staff estimates.

24. **Expenditure policy will support the NPRS's poverty alleviation objectives.** As regards government wages, the 2003 budget allows for an average increase of 8 percent. When applied selectively, this would help address the low wage level of key civil servants and support efforts to fight petty corruption. In line with the authorities' poverty reduction objectives, spending on education and health could increase by 5 percent in real terms. To compensate for the likely price impact of introducing the VAT on large agricultural producers, the 2003 budget provides for a 20 percent increase in key social benefits starting from April 2003. In addition, an 8 percent pension increase was tentatively included in the 2003 budget awaiting the results of an updated assessment of the Social Fund's financial position during the February 2003 mission.

²² In the second quarter of 2002, Kumtor started to pay the profit tax, emergency fund tax, and the mineral resource tax.

²³ Macroeconomic aspects of environmental issues in the Kyrgyz Republic are analyzed in the Selected Issues paper, Chapter VI.

compensate for the likely price impact of introducing the VAT on large agricultural producers, the 2003 budget provides for a 20 percent increase in key social benefits starting from April 2003. In addition, an 8 percent pension increase was tentatively included in the 2003 budget awaiting the results of an updated assessment of the Social Fund's financial position during the February 2003 mission.

25. **The economic strategy calls for a cautious monetary policy to keep inflation low and ensure cost competitiveness of Kyrgyz exports.** In 2002, the strong growth of monetary aggregates reflected an increase in the demand for som-denominated assets, mainly for transaction purposes.²⁴ Som broad money would grow less in 2003, by 15 percent, consolidating recent gains in monetization. Demand for som real balances is projected to grow by 6 percent during 2003 compared to a preliminary estimate of a 22 percent increase in 2002. Financial deepening is expected to continue also based on further banking sector reforms supporting the recovery of the private sector. Against this background, the end-March 2003 NIR target aims at increasing foreign reserves by \$24 million from the end-September 2002 level of \$81 million. The program's NDA target for end-March 2003 reflects an increase in government deposits in the central bank to help sterilize the monetary impact of the expected capital inflows.

26. **The authorities shared the staff's concern that the recent rapid money growth could raise inflation expectations.** They assured that any signs of rekindling inflation would prompt them to tighten monetary conditions. The staff pointed out that instead of foreign exchange interventions, this would require more active sales of NBKR or treasury bills. The NBKR's capacity to influence monetary conditions through open market operations has improved as, in addition to its own bills, the stock of T-bills recently doubled with the issuance to the NBKR of interest bearing short-term government securities.

27. **The mission recommended that the NBKR continue its exchange rate policy of managed floating.** The authorities agreed that, in general, the NBKR should intervene in the foreign exchange market only to smooth temporary variations of the nominal exchange rate and strengthen the official reserve position. Leaning against a nominal appreciation, as has been done during 2002, was considered justified because of the need to increase reserves while preserving the tradable good sector's competitiveness. To reduce its operating costs, the NBKR requested Fund support in moving from quarterly to annual audits of its foreign reserves as auditors have not found any weaknesses in reserves management in the past three-year period of quarterly audits.

28. **On trade policy, staff stressed the need to preserve a liberal and low-tariff trade regime.** The authorities should refrain from introducing new seasonal tariffs (such as the

²⁴During January-November 2002, cash in circulation increased by 36 percent compared with a 34 percent growth in som broad money. Deposits increased by 24 percent.

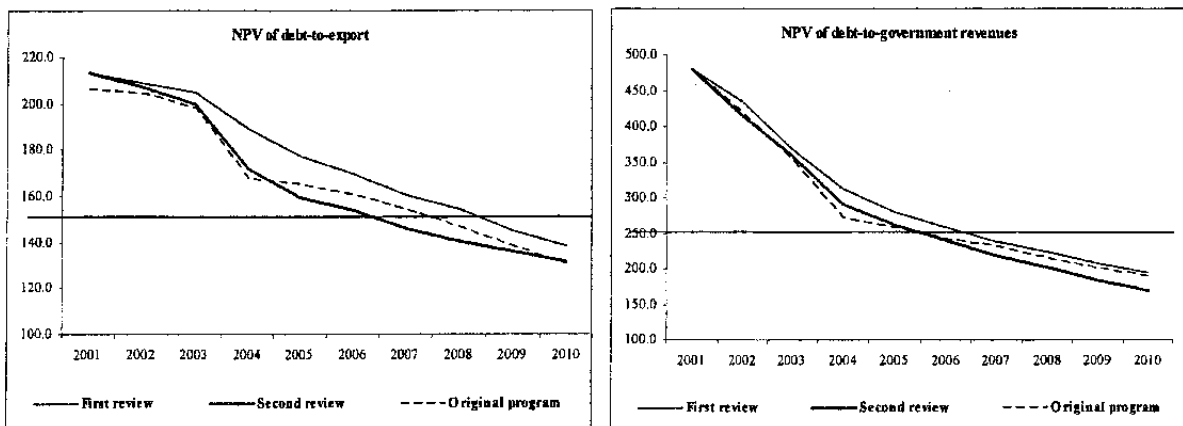
temporary duties imposed on Kazakh wheat this harvest season) or nontariff barriers on agricultural or other imports. The authorities intend to approach neighboring countries with specific proposals to reduce regional trade restrictions, such as transit fees and other nontariff barriers to market access. The exchange regime remains free of restrictions. In accordance with WTO commitments, the tariff structure has been simplified to comprise 4 bands, with an average rate of 5.1 percent.

29. **The staff and the authorities noted that the debt-reduction strategy was on track.** Foreign borrowing has declined and any further contracting of public or publicly-guaranteed debt has been restricted to loans with a grant element of at least 45 percent. Negotiations with Paris club creditors have been completed. Of non-Paris Club creditors, only Uzbekistan, Pakistan, and the Kuwait Fund have not yet rescheduled their claims on comparable terms. An updated debt sustainability analysis suggest that if the PRGF-supported program is implemented successfully, and a stock of debt relief is granted, the Kyrgyz Republic's external debt could reach manageable levels in the second half of the decade (Box 2).

Box 2: Debt Sustainability

The updated debt sustainability analysis is based on the baseline scenario summarized in Figure 2. The weakening of the indicators between the approval of the program and the first review was mainly due to the reduction in the applied discount rate. New simulations suggest that the external debt could become sustainable in 2007 when assessed by the NPV of debt-to-exports and debt service-to-fiscal revenue ratios. In part, the more favorable outcome than projected at the time of the approval of the PRGF arrangement is due to a lower starting level of the external debt reflecting lower-than-expected current account deficit in 2001–2002. In addition, exports of services are projected to be stronger because of increased tourism and higher spending of the international military base. Also, the latest simulations take account of the donors' pledges for increased concessional financial support.

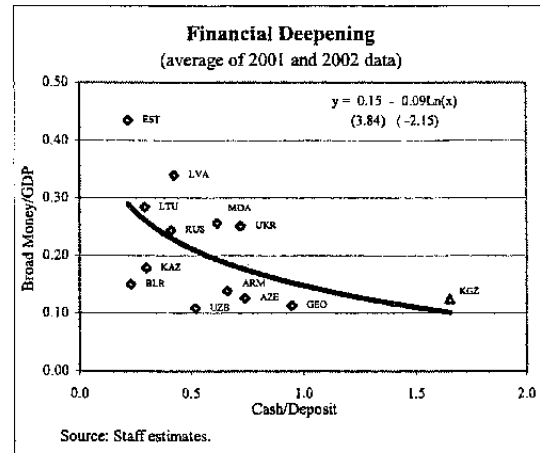
Naturally, the outcome of these simulations is sensitive to several factors. In particular, with lower growth of exports and weaker fiscal adjustment, the debt dynamics would be significantly less favorable. As indicated in the low-case scenario of Figure 2, and discussed in paragraph 20, a 2-3 percentage points lower growth of output and exports would not only keep the external debt at unsustainable levels throughout the decade, but even lead to increasing debt ratios.



Source: Ministry of Finance and staff calculations.

C. Structural Reform Agenda

30. **Discussions on structural reforms focused on two issues: a banking sector reform and governance.** Despite the progress made in recent years towards consolidation and stabilization, the banking sector remains small and financial intermediation is low even by CIS standards. The high proportion of cash to deposits highlights the poor confidence in banks. The authorities recognized the need for strict enforcement of prudential regulations to reduce bank vulnerabilities and improve public trust in banks. Discussions on the banking reform were closely coordinated with the staffs of the World Bank, the Asian Development Bank (AsDB), and the EBRD. Based on the recommendations of the recent FSAP missions (Box 2) a detailed banking sector reform program was designed. It aims at stronger bank supervision, better regulatory framework, divestiture of the state-owned banks, strengthened debt recovery, and improved payments system (see Second-year Memorandum of Economic Policies (SMEP), Box 1). The second year program identifies one performance criterion and three benchmarks that are most critical for the success of the program (see SMEP, Box 3).



Box 3: Main Recommendations of the Financial Sector Assessment Program

Bank governance and the banking system need strengthening. To encourage strategic investors, the government should cancel the 15 percent ownership limit for legal entities. The NBKR should gradually raise Minimum Tier 1 capital, and place increasingly rigorous restrictions on specialized banks. Resolution plans for Kairat and the Savings and Settlement Corporation need to be finalized and implemented.

Banking supervision needs further improvement. The Banking Law should be the sole legal source for bank licensing; moreover accounting practices need to improve as well as the regulatory framework for risk management. Measures that may take longer to carry out include providing legal protection for NBKR employees and third parties doing work for the NBKR; and empowering the NBKR to oppose the appointment of, or require replacing, external auditors.

Weaknesses in the judicial and legal system, which constitute an important barrier to financial sector development, need to be addressed urgently. The government needs to make the judicial system more efficient, effective, independent and accountable. Lawmaking should become more efficient and transparent.

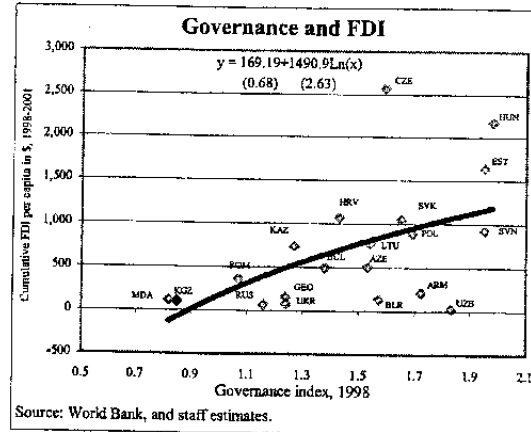
The payment system is slow and inefficient, but it does not pose a systemic risk. The authorities are finalizing plans for modernizing the system to bring it up to international standards. Implementation will, however, require much resources and management time.

Authorities should press ahead with efforts to address the current weak legal framework against money laundering and terrorism financing. The parliament should pass the draft AML/CFT law in the near term, and the NBKR should arrange enough resources and training to ensure effective implementation. Law enforcement bodies should develop an understanding of relevant banking issues and fully implement criminal investigative and prosecutorial measures.

Transparency practices in monetary policy, banking supervision, and payment system oversight are generally good, but could be improved. Changes might include explaining changes in monetary policy on a more systematic and timely basis; regularly reporting on internal governance procedures; and introducing a more formal approach to seeking public comments on proposed changes NBKR policies.

31. **The authorities recognized that a governance reform was necessary for better business climate and foreign investments.**

According to recent surveys, enterprises, households, and public officials perceive basic public institutions as corrupt. The authorities acknowledged that this undermined the legitimacy of the government and helped vested interest capture the state. In particular, they were concerned that mainly small and medium-size enterprises—the engine of growth in transition economies—were negatively affected in this environment. Staff noted that good governance was also necessary to attract foreign direct investment and to boost productivity growth.



32. **The President reiterated his support for a concerted action plan to tackle the governance problem.** The second-year program includes a comprehensive governance reform detailed in Box 2 of the SMEP. This initiative combines the main features of the work under the PRGF-supported program, the AsDB's Corporate Governance and Enterprise Reforms Program, the AsDB's Custom Modernization Project, and the World Bank's forthcoming Governance Structural Adjustment Credit. The focus is on: (i) setting up a stakeholder institution for good governance; (ii) promoting public awareness; (iii) improving efficiency in public administration; (iv) strengthening corporate governance; and (v) reforming the judiciary. Of these measures, the authorities chose one performance criterion and two structural benchmarks for the first half of the second-year program. Further benchmarks will be set out for the midyear review of the second-year program (see SMEP, Box 2).

33. **On privatization, as mentioned before, a tender for KyrgyzTelekom was issued, but the other enterprises will need essential restructuring before privatization.**²⁵ KyrgyzAir's debt restructuring negotiations with the government are underway. Privatizing the distribution companies of the former Kyrgyz Energo and of KyrgyzGas will take more time than envisaged in the original program. The authorities are working with the World Bank staff to review the reform agenda in this area. The World Bank staff is considering concession arrangements and foreign management contracts instead of privatization to

²⁵ Potential proceeds from the sale of KyrgyzTelekom have not been included in the program at this stage. In case of a successful completion of the privatization, the proceeds will be deposited in a special account at the NBKR. The fiscal and monetary implications of this privatization will be incorporated in the program at the time of the third review expected to be completed in June 2003.

improve efficiency in the energy sector. The staff concurred with the authorities that no conditionalities should be introduced on privatizing these companies at this stage.

D. Statistical Issues

34. **The authorities have been working with international financial institutions (IFIs) and bilateral donors to improve national account statistics.** The National Statistics Committee (NSC) is expanding the use of household surveys to improve the quality of the data. The current focus is on discrete quarterly GDP data, and on wages and unemployment. As regards GDP, the particular problems include monthly data for the construction sector and for spending on capital goods, both of which systematically understate true values. The estimates are corrected only in the last quarter of the year, or later. As for prices, the PPI coverage has expanded which improved its reliability but the calculation of the GDP deflator needs improvement. The NSC is preparing a report on the 2002 agriculture census. It will provide a better and much needed review of the largest sector of the economy. The recent data ROSC ascertained the need for training and updating procedures.

E. Program Financing and Monitoring

35. **The second year program is fully financed.** Paris Club debt rescheduling will complement disbursements by the World Bank and the IMF. Gross reserves are expected to be slightly higher—at 4.7 months of imports—by the end of 2003 than in 2002. This level was considered appropriate in view of the Kyrgyz economy's vulnerability to external shocks and high external debt.

36. **Proposed prior actions, quantitative and structural performance criteria, and structural benchmarks are specified in the authorities' SMEP, Table 1 and Box 3.** To better monitor the collection of the social security contributions, a floor on payroll tax collections in cash is now proposed as an additional performance criterion. Another new performance criterion would cover outstanding arrears of Social Fund transfers to the Medical Insurance Fund to help finance the World Bank and USAID sponsored health sector reform. Amendments to the July 2002 TMU clarify the definition of external arrears to encompass claims from overdue commercial obligations. Discussions with staff for the third review are expected to take place in May 2003. The review will focus mainly on progress made in governance reform.

V. STAFF APPRAISAL

37. The authorities' candid assessment of their performance under the previous IMF-supported programs is welcome. The current emphasis on realism and pragmatism bodes well given the challenges ahead. The fact that the fiscal program and debt reduction strategy are on track suggests that the lessons from the past have been learned.

38. Given the ambitious medium-term strategy of the authorities, the need for strict policy discipline is critical. Poverty reduction, the projected decline in gold production, and the high

external debt are constraints that put the economy on a narrow path where slippages could easily lead to a vicious cycle. Expansion of nongold exports is the key to reach the medium growth objective and this requires strong commitment to foster productivity growth and contain inflation. The staff is pleased to note that the authorities share the understanding of the importance of maintaining, or even improving, the current level of cost competitiveness and realize that this calls for a wage policy based on real wages increasing only through productivity growth.

39. Under the current PRGF-supported program, the Kyrgyz authorities are to be commended for their good policy performance. Price stabilization continued in 2002, and the dip in real GDP is expected to be reversed this year. However, the temporary output decline underscores the need to diversify the economy and to work with neighboring countries and the international community to reduce trade restrictions in the region.

40. The observance of all fiscal targets was a commendable achievement in view of the shortfall of revenue from Kumtor. However, the good performance in 2002 is unlikely to be sustained without further reforms in tax administration and broadening the tax base. The government's commitment to extend VAT to large agricultural producers in the current politically sensitive environment deserves appreciation. Staff also welcomes the new action plan for the LTU since it addresses the basic structural weakness in the Kyrgyz tax administration. If fully carried out, this reform would go a long way to reduce the scope for corruption. The impact on prices of the VAT extension has been considered and compensatory measures for the poor are included in the 2003 budget. The staff supports this approach.

41. Monetary policy has been successful in containing inflation while allowing remonetization of the economy. Recent purchases of foreign currency have accommodated the increased demand for local currency, and prevented excessive nominal appreciation, with harmful effects to competitiveness, which is deemed satisfactory at its present level. Against this backdrop, the policy of managed floating of the exchange rate has been appropriate. If there are any signs of accelerating inflation, however, the central bank should react promptly by tightening monetary conditions through open market operations using government securities and its own bills.

42. Staff notes with satisfaction that the external debt strategy is on track. In the coming two years, the authorities must carefully follow this strategy placing emphasis on further fiscal consolidation and avoiding slippages especially prior to the forthcoming elections in 2005. The Ministry of Finance has done a good job in completing all bilateral reschedulings with the Paris Club creditors. It is important that all non-Paris Club creditors also agree on comparable terms.

43. After ten years of transition, the agenda for structural reforms remains to be completed. At the present stage the greatest need is in the areas of governance and banking sector reforms. The civil society's perception of the legitimacy of the government is low and

vested interests and state capture undermine the opportunities of small and medium size enterprises. Strong support from the highest level of the government is essential to guarantee the success of the governance and banking sector reforms. If these reforms are not pursued with vigor, private sector investment and growth will be undermined

44. Looking ahead, the main downside risks are financial instability and, over the medium term, a low-growth trap. The high external debt leaves no room at all for policy failures. Fiscal slippages would be particularly dangerous. In such a scenario, the Paris Club concessional stock rescheduling would be unlikely and the targeted gains in poverty reduction elusive. The staff notes that political factors may cause the authorities to be cautious in introducing strong measures when the 2005 elections approach. The cost of any delays must, however, be also factored in as weak policies would only increase the need for adjustments later on.

45. While the program faces risks, the staff believes that they are manageable. The good track record in 2001–2002 proves that the Kyrgyz authorities have the capacity to succeed in a difficult environment. As the policies are on track, and the breach of the performance criterion was small and has been corrected, the staff supports the authorities request for a waiver and the completion of the second review under the PRGF. Also, the staff supports the NBKR's intention to move to an annual cycle in auditing its foreign reserve management.

46. Is it expected that the next Article IV consultation with the Kyrgyz Republic will be held in accordance with the provisions of the decision on consultation cycles approved on July 15, 2002.

Table 1. Kyrgyz Republic: Quantitative Program Targets 1/
(In millions of soms, unless otherwise indicated, eop)

	2001		2002					
	December	March	March	June	June	September		September
	Actual	March Performance Criteria Adjusted	Actual	June Benchmarks Adjusted	Actual	September Performance Criteria Program	Adjusted	Actual
I. Performance criteria								
1. Floor on net international reserves of the NBKR in convertible currencies (eop stock, in millions of U.S. dollars) 2/	39.3	30.6	53.6	43.7	58.4	57.6	48.4	79.9
2. Ceiling on net domestic assets of the NBKR (eop stock) 3/	1,257	1,090	893	2,566	2,438	1,987	2,436	2,007
3. Ceiling on cumulative fiscal deficit of the state government 4/	1,290 5/	n.a.	2,276	n.a.	3,301	4,948	n.a.	4,047
4. Cumulative floor on state government tax collections in cash 6/	2,929	n.a.	5,008	n.a.	7,508	10,316	n.a.	10,359
5. Ceiling on the stock of central government budget arrears 7/	0	n.a.	0	n.a.	30	0	n.a.	0
6. Ceiling on the stock of Social Fund pension arrears	12	n.a.	0	n.a.	92	0	n.a.	0
7. Floor on payroll collections in cash of the Social Fund 8/	...	...	...	...	...	...	...	...
8. Ceiling on the stock of Social Fund arrears to the Medical Insurance Fund	...	...	...	...	...	...	...	77.1
9. Ceiling on contracting or guaranteeing by the state government or NBKR of new external debt of less than one year (in millions of U.S. dollars) 9/ 10/	0	n.a.	0	n.a.	0	0	n.a.	0
10. Ceiling on contracting or guaranteeing by the state government or NBKR of new nonconcessional external debt (cumulative, in millions of U.S. dollars) 11/	0	n.a.	0	n.a.	0	0	n.a.	0
11. Ceiling on new external payment arrears (in millions of U.S. dollars) 10/	0	n.a.	0	n.a.	0	0	n.a.	1.5
II. Indicative targets								
1. Ceiling on reserve money (NBKR liabilities)	5,359	4,853	5,626	5,602	6,164	5,700	5,700	6,786

Sources: Data provided by the Kyrgyz authorities; and Fund staff estimates and projections.

1/ Until September 2002, foreign exchange components valued at the exchange rate US\$1 = som 49, gold holdings valued at US\$265 per ounce, SDR valued at SDR 1 = US\$1.259. Starting December 2002, foreign exchange components valued at the exchange rate US\$1 = som 47, gold holdings valued at US\$322.4 per ounce, SDR valued at SDR 1 = US\$1.3186. Targets exclude claims and liabilities to BRO countries.

2/ As defined in the Technical Memorandum of Understanding (TMU), excludes, among others, swaps and international reserves of the NBKR that are pledged or blocked.

3/ As defined in the TMU, excludes, among others, the counterpart of the loan by the Eximbank of Turkey and the EBRD/IDA enterprise loan which are channeled through the NBKR.

4/ As defined in the TMU, state government comprises central and local governments. For March 2003, cumulative begins on October 1, 2002. For December 2003, cumulative begins on October 1, 2003.

5/ The deficit for the fourth quarter of 2001 is adjusted for interest payments rescheduled by the Paris Club (som 172 million).

6/ As defined in the TMU, includes, among others, collection of tax arrears but excludes, among others, tax offsets. For March 2003, cumulative begins on October 1, 2002. For December 2003, cumulative begins on October 1, 2003.

7/ As defined in the TMU, central government budget arrears comprise, among others, wages, payroll contributions and mandatory transfers to the Social Fund, categorical grants, payments to KyrgyzEnergO, and allowances to poor families from September 2002 onwards.

8/ For March 2003, cumulative begins on October 1, 2002. For December 2003, cumulative begins on October 1, 2003.

9/ External debt is defined in the TMU as in Executive Board's Decision no. 12274 (00/85) of August 24, 2000. Includes loans, leases, suppliers' credits and other instruments giving rise to external debt.

10/ On a continuous basis.

11/ As defined in the TMU, a debt is classified as concessional if its grant element is at least 45 percent, calculated using a discount rate based on the 10-year average of OECD commercial interest reference rates (CIRR), for debts of maturity greater than 15 years; for debts of maturity 15 years or less, the discount rate should be based on the six month average of the OECD CIRR. The ceilings include loans, leases, supplier's credits and other instruments giving rise to external debt on nonconcessional terms. IMF lending is excluded from the ceiling on new nonconcessional borrowing.

Adjustors

1. The floor on net international reserves of the NBKR will be adjusted: (i) upward/downward by 100 percent for excesses/shortfalls of the use of net foreign financing of the state government budget and cash grants; (ii) upward/downward by 100 percent for excess/shortfall of cash privatization receipts. The adjustment for shortfalls in adjustors (i) and (ii) is limited to US\$ 15 million each, valued at the program exchange rate. In the case of a release of the NBKR's pledged foreign reserves, the NIR floor will be adjusted upward by 100 percent of the net effect of the releases and related amortization payments.

2. The ceiling on net domestic assets of the NBKR will be adjusted: (i) downward/upward by 100 percent for excesses/shortfalls of the use of net foreign financing of the state government budget and cash grants; (ii) downward/upward by 100 percent for excess/shortfall of cash privatization receipts. The adjustment for shortfalls in adjustors (i) and (ii) is limited to US\$ 15 million each, valued at the program exchange rate, excluding the amortization payments for the release of the NBKR's pledged foreign reserves.

**Table 2. Kyrgyz Republic: Prior Action, Structural Performance Criteria, and Benchmarks
Through end-September 2002**

Structural performance criteria	Preliminary assessment and implementation
Submission to parliament of legislative amendments necessary to ensure that the courts accept, as the representation of a bank's financial position, the bank's financial statement as confirmed by the NBKR.	Implemented
Issuance of government resolution to convert the current Large Taxpayer Unit (LTU) into a fully functioning LTU as specified by the recent FAD tax policy mission in Section IV.F of its report on "Further Reform of Tax Policy and Administration."	Implemented
Structural benchmarks	
In consultation with IMF staff and based on the forthcoming FSAP missions' findings, the NBKR will draft a strategy for further banking sector reforms.	Implemented
Establishment of a Financial Planning Division within the Treasury and production of the first cash forecast of revenue and expenditure for the remainder of 2002.	Implemented
Approval of the MoF restructuring plan as described in paragraph 11 of the Supplementary Memorandum of Economic Policies (SMEP) and specified in consultation with IMF staff on the basis of the recent FAD Public Expenditure mission.	Implemented
Submission to parliament of amendments to the Law on Licensing as described in paragraph 14 of the SMEP.	Implemented

Table 3. Kyrgyz Republic: Selected Economic Indicators, 1999-2006

	1999	2000	2001	2002			2003	2004	2005	2006
	Actual	Actual	Actual	Original Prog.	Revised Prog.	New Prog.	New Prog.	Proj.	Proj.	Proj.
GDP										
Nominal GDP (in billions of soms)	48.7	65.4	73.9	80.2	81.5	77.5	85.3	93.3	102.1	111.8
Nominal GDP (in millions of U.S. dollars)	1,243	1,368	1,525	1,637	1,663	1,649	1,815	1,986	2,172	2,379
Real GDP (growth in percent)	3.7	5.4	5.3	4.5	4.4	0.8	5.2	5.0	5.0	5.0
GDP per capita (in U.S. dollars)	255	278	308	324	333	330	359	389	422	457
Prices and wages										
Consumer prices (percent change, eop)	39.9	9.6	3.7	6.0	4.9	3.6	4.4	4.0	4.0	4.0
Consumer prices (percent change, avg)	35.9	18.7	7.0	7.5	4.1	2.3	4.2	4.0	4.0	4.0
Nominal exchange rate (eop)	45.3	48.9	47.7	...	...	...	...	...	...	...
Exchange rate (soms per U.S. dollar, average)	39.1	47.8	48.4	...	...	...	...	...	...	...
Average real wage (1994=100)	118.0	120.8	133.6	135.5	137.8	140.3	144.3	148.2	152.5	156.9
Average monthly wage (in U.S. dollars)	24.7	24.7	28.8	31.2	30.5	31.9	34.2	36.5	39.0	41.7
(In percent of GDP)										
State government finances										
Total revenue and grants	17.7	15.1	17.0	17.3	18.3	18.4	18.5	19.3	20.0	20.6
Tax revenue	12.3	11.7	12.4	13.8	13.8	13.4	14.6	15.2	15.5	16.1
Total expenditure (including net lending)	30.4	24.9	22.2	22.2	23.0	23.7	23.2	23.5	23.7	23.6
Non-interest current expenditure	17.3	14.9	15.9	14.6	15.5	16.4	16.4	16.9	16.9	17.3
Public Investment Program (PIP)	9.4	6.8	4.4	5.5	5.4	5.1	4.5	4.0	3.5	3.0
Overall fiscal balance (cash basis)	-11.9	-9.2	-5.0	-4.9	-5.0	-5.6	-4.7	-4.2	-3.7	-3.0
Primary balance 1/	-9.0	-6.9	-3.3	-2.9	-3.1	-3.7	-2.7	-2.0	-1.1	-0.7
Primary balance (excl. PIP)	0.4	-0.2	1.1	2.6	2.3	1.4	1.9	2.0	2.4	2.3
(Percent change, unless stated otherwise)										
Money and credit 2/										
Reserve money (end-of-period)	23.4	12.3	11.3	8.0	8.1	38.7	6.5	...	...	...
Broad money (end-of-period)	33.9	12.1	11.3	12.4	14.1	29.8	13.3	...	...	...
Velocity of broad money 3/	8.5	10.0	9.4	10.8	8.8	7.6	7.2	...	...	...
Money multiplier	1.6	1.6	1.5	1.6	1.6	1.4	1.5	...	...	...
External sector										
Export growth (goods and services, in U.S. dollars, percent change)	-11.8	8.6	-2.1	2.9	5.1	5.8	12.9	2.5	6.5	7.1
Import growth (goods and services, in U.S. dollars, percent change)	-24.7	-7.2	-13.1	4.9	9.8	15.5	11.6	6.5	5.5	6.4
Current account balance (in percent of GDP)	-15.7	-7.5	-3.3	-6.3	-3.8	-2.8	-4.2	-4.7	-4.2	-4.1
Gross international reserves (months of imports, end-period) 4/	3.4	4.4	4.1	3.7	4.6	4.5	4.7	4.8	4.5	4.5
External debt outstanding in percent of GDP 5/	109.3	111.1	99.7	114.9	107.1	96.1	92.2	81.6	77.7	73.0
Debt service-to-export ratio	21.7	21.7	21.3	29.1	...	18.4	13.0	14.0	25.0	19.8

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

1/ Overall balance less accrued interest payments.

2/ Projections use program exchange rate.

3/ For 1997-2000, annualized quarterly GDP/end-of-period broad money, for 2001-2003, 12-month GDP/average broad money for last two quarters.

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

5/ Excluding Kumtor.

Table 4. Kyrgyz Republic: Medium-Term Projections, 1999-2006

	1999	2000	2001	2002		2003	2004	2005	2006
	Actual	Actual	Actual	Orig. Prog.	New Prog.	Proj.	Proj.	Proj.	Proj.
(Annual percentage change, unless otherwise stated)									
Income									
Nominal GDP (in billions of soms)	48.7	65.4	73.9	80.2	77.5	85.3	93.3	102.1	111.8
Nominal GDP (in millions of U.S. dollars)	1243	1368	1525	1637	1649	1815	1986	2172	2379
GDP per capita (in U.S. dollars)	255	278	308	324	330	359	389	422	457
Real GDP	3.7	5.4	5.3	4.5	0.8	5.2	5.0	5.0	5.0
Prices									
GDP deflator	37.6	27.3	7.3	8.2	4.0	4.6	4.2	4.2	4.2
Consumer prices (average)	35.9	18.7	7.0	7.5	2.3	4.2	4.0	4.0	4.0
Terms of trade	0.9	-7.1	-0.5	...	0.1	0.0	0.0	-0.1	0.4
Wages and employment									
Average monthly wage (in U.S. dollars)	24.7	24.7	28.8	...	31.9	34.2	36.5	39.0	40.7
Real wage growth	-9.0	2.3	10.6	...	5.0	2.8	2.8	2.8	2.9
Employment	3.5	0.2	0.2	...	0.0	0.2	0.2	0.2	0.2
(In percent of GDP)									
Savings and investment balance									
Total Investment	18.0	20.0	18.0	16.1	19.4	20.3	22.3	23.0	23.5
Government	10.5	8.1	5.3	6.3	6.2	5.3	4.9	4.7	4.5
PIP (Public Investment Program)	9.4	6.8	4.4	5.5	5.1	4.5	4.0	3.5	3.0
Other investment (budget)	1.1	1.4	0.9	0.8	1.1	0.8	0.9	1.2	1.5
Non-government	7.6	11.9	12.7	9.8	13.2	15.0	17.4	18.3	19.0
Total domestic savings	2.4	12.5	14.7	9.8	16.5	16.1	17.6	18.7	19.4
Government	-3.2	-2.1	-1.0	0.8	0.1	0.2	0.3	0.5	1.1
Non-government	5.6	14.6	15.7	9.0	16.4	15.9	17.3	18.2	18.4
Foreign savings	15.7	7.5	3.3	6.3	2.8	4.2	4.7	4.2	4.1

Sources: Data provided by the Kyrgyz authorities; and Fund staff estimates and projections.

Table 5. Kyrgyz Republic: General Government Finances

	2001		2002			2003				2004	2005	2006		
	Annual Act.	Annual Orig. Prog.	Annual Rev. Prog.	Q3 Act.	Q4 Prog.	Annual New Prog.	Q1 Prog.	Q2 Proj.	Q3 Prog.	Q4 Proj.	Annual New Proj.	Annual New Proj.	Annual New Proj.	
(In millions of soms)														
Total revenue and grants	15,051	17029	17803	4,696	4,878	16,953	3,518	4,313	5,167	5,722	18,720	21,150	23,787	26,675
Total revenue, of which:	14,429	16634	16919	4,393	4,551	16,068	3,299	4,313	4,949	5,722	18,283	20,713	22,847	25,693
Total tax revenue	11,696	14247	14179	3,619	3,725	13,100	2,907	3,574	4,186	4,700	15,368	17,282	19,164	21,566
State taxes	9,188	11104	11248	2,851	3,025	10,415	2,278	2,937	3,379	3,876	12,470	14,171	15,804	17,952
Social Security Revenue 1/	2,508	3134	2931	768	700	2,685	630	637	807	824	2,898	3,111	3,360	3,614
Grants	622	395	884	304	327	886	218	0	218	0	437	437	940	982
Total expenditure	19,659	21467	22221	5,371	6,538	21,658	4,872	5,408	5,903	6,885	23,068	25,486	28,041	30,557
Current expenditure, of which:	15,744	16395	17101	4,136	4,809	16,886	3,915	4,374	4,550	5,500	18,540	20,913	23,234	25,489
Wages	3,550	3835	3890	949	1,017	3,819	868	1,172	1,043	1,229	4,312	4,847	5,404	6,084
Social fund expenditure	3,928	4472	4549	1,094	1,190	4,484	1,203	1,083	1,226	1,266	4,877	5,388	5,828	6,297
Interest due	1,228	1588	1577	158	544	1,419	168	775	155	603	1,702	2,075	2,622	2,611
Capital expenditure (including PIP)	3,915	5072	5121	1,234	1,669	4,773	957	834	1,353	1,385	4,528	4,573	4,807	5,068
Financial balance	-4,608	-4438	-4419	-674	-1,660	-4,705	-1,354	-1,095	-736	-1,163	-4,348	-4,336	-4,254	-3,882
Net lending	-509	-573	-573	-112	-256	-579	-115	-115	-115	-115	-461	-467	-510	-559
Accrual surplus (+) / deficit (-)	-4,099	-3865	-3846	-562	-1,404	-4,126	-1,239	-980	-621	-1,048	-3,888	-3,869	-3,744	-3,324
Total arrears and rescheduling 2/	304	50	-201	-151	-85	-211	0	0	0	0	-50	-11	-21	-35
Budget expenditure arrears	155	0	-173	-122	-34	-232	0	0	0	0	0	0	0	0
Rescheduling of external interest 2/	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Expenditure arrears of the Social Fund	149	-50	-28	-29	-51	22	-10	-20	-10	-10	-50	-11	-21	-35
Cash surplus (+) / deficit (-)	-3,795	-3915	-4047	-713	-1,489	-4,336	-1,249	-1,000	-631	-1,058	-3,938	-3,880	-3,764	-3,359
Total financing	3,795	3915	4047	713	1,489	4,336	1,249	1,000	631	1,058	3,938	3,880	3,764	3,359
External financing, of which:	4,208	4571	4657	1,040	1,839	4,234	1,105	1,004	1,207	1,410	4,726	6,326	265	303
Principal rescheduling	795	0	809	109	191	801	294	717	279	800	2,091	2,404	0	0
Domestic financing	-712	-2761	-780	-356	-417	-33	120	-28	-600	-376	-883	-2,538	-1,491	-1,686
Privatization proceeds	299	170	170	29	66	135	24	24	24	24	94	90	1,410	940
Financing gap	0	1935	0	0	0	0	0	0	0	0	1	2	3,580	3,580
Memorandum items:														
Primary surplus (+) / deficit (-) (w/o foreign fin. PIP)	672	2051	1940	422	449	1,041	-266	486	675	724	1,618	1,928	2,431	2,605
Primary surplus (+) / deficit (-)	-2,567	-2379	-2470	-554	-945	-2,918	-1,081	-224	-476	-455	-2,236	-1,805	-1,143	-748
Social Expenditure	8,424	8889	9394	...	...	9,017	...	...	...	...	10,144	11,367	12,821	14,315
Augmented Fiscal Deficit 3/	...	...	...	...	...	-5,417	...	...	...	...	...	...	...	...
Bonds issued to the NBKR 4/	...	1,166	...	...	1,081	...	...	...	...	...	...	...	...	...
Domestic quasi-fiscal deficit 5/	4,716	...	3330	...	...	...	...	...	...	...	...	...	...	...
(In percent of GDP)														
Total revenue and grants	20.4	21.2	21.8	6.1	6.3	21.9	4.1	5.1	6.1	6.7	21.9	22.7	23.3	23.9
Total revenue, of which:	19.5	20.7	20.8	5.7	5.9	20.7	3.9	5.1	5.8	6.7	21.4	22.2	22.4	23.0
Total tax revenue	15.8	17.8	17.4	4.7	4.8	16.9	3.4	4.2	4.9	5.5	18.0	18.5	18.8	19.3
State taxes	12.4	13.8	13.8	3.7	3.9	13.4	2.7	3.4	4.0	4.5	14.6	15.2	15.5	16.1
Social Security Revenue 1/	3.4	3.9	3.6	1.0	0.9	3.5	0.7	0.7	0.9	1.0	3.4	3.3	3.3	3.2
Grants	0.8	0.5	1.1	0.4	0.4	1.1	0.3	0.0	0.3	0.0	0.5	0.5	0.9	0.9
Total expenditure	26.6	26.1	27.3	6.9	8.4	27.9	5.7	6.3	6.9	8.1	27.0	27.3	27.5	27.3
Current expenditure, of which:	21.3	20.4	21.0	5.3	6.3	21.8	4.6	5.4	5.3	6.4	21.7	22.4	22.8	22.8
Wages	4.8	4.8	4.8	1.2	1.3	4.9	1.0	1.4	1.2	1.4	5.1	5.2	5.3	5.4
Social fund expenditure	5.3	5.6	5.6	1.4	1.5	5.8	1.4	1.3	1.4	1.6	5.7	5.8	5.7	5.6
Interest due	1.7	2.0	1.9	0.2	0.7	1.8	0.2	0.9	0.2	0.7	2.0	2.2	2.6	2.3
Capital expenditure (including PIP)	5.3	6.3	6.3	1.6	2.2	6.2	1.1	1.0	1.6	1.6	5.3	4.9	4.7	4.5
Financial balance	-6.2	-5.4	-5.4	-0.9	-2.1	-6.1	-1.6	-1.3	-0.9	-1.4	-5.1	-4.6	-4.2	-3.5
Net lending	-0.7	-0.7	-0.7	-0.1	-0.3	-0.7	-0.1	-0.1	-0.1	-0.1	-0.5	-0.5	-0.5	-0.5
Accrual surplus (+) / deficit (-)	-5.5	-4.8	-4.7	-0.7	-1.8	-5.3	-1.5	-1.1	-0.7	-1.2	-4.6	-4.1	-3.7	-3.0
Total arrears and rescheduling 2/	0.4	0.1	-0.2	-0.2	-0.1	-0.3	0.0	0.0	0.0	0.0	-0.1	0.0	0.0	0.0
Budget expenditure arrears	0.2	0.0	-0.2	-0.2	0.0	-0.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Rescheduling of external interest 2/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Expenditure arrears of the Social Fund	0.2	0.1	0.0	0.0	-0.1	0.0	0.0	0.0	0.0	0.0	-0.1	0.0	0.0	0.0
Cash surplus (+) / deficit (-)	-5.1	-4.9	-5.0	-0.9	-1.9	-5.6	-1.5	-1.2	-0.7	-1.2	-4.6	-4.2	-3.7	-3.0
Total financing	5.1	4.9	5.0	0.9	1.9	5.6	1.5	1.2	0.7	1.2	4.6	4.2	3.7	3.0
External financing, of which:	5.7	5.7	5.7	1.3	2.4	5.5	1.3	1.2	1.4	1.7	5.5	6.8	0.3	0.3
Principal rescheduling	1.1	0.0	1.0	0.1	0.2	1.0	0.3	0.8	0.3	0.9	2.5	2.6	0.0	0.0
Domestic financing	-1.0	-3.4	-1.0	-0.5	-0.5	0.0	0.1	0.0	-0.7	-0.4	-1.0	-2.7	-1.5	-1.5
Privatization proceeds	0.4	0.2	0.2	0.0	0.1	0.2	0.0	0.0	0.0	0.0	0.1	0.1	1.4	0.8
Financing gap	0.0	2.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	3.5	3.2
Memorandum items:														
Primary surplus (+) / deficit (-) (w/o foreign fin. PIP)	0.9	2.5	2.4	0.5	0.6	1.3	-0.3	0.6	0.8	0.8	1.9	2.1	2.4	2.3
Primary surplus (+) / deficit (-)	-3.5	-2.9	-3.0	-0.7	-1.2	-3.8	-1.3	-0.3	-0.6	-0.5	-2.6	-1.9	-1.1	-0.7
Augmented Fiscal Deficit 3/	...	...	...	...	...	-7.0	...	...	...	...	...	...	...	...
Social Expenditure	11.4	10.9	11.5	...	...	11.6	...	...	...	...	11.9	12.2	12.6	12.8
Bonds issued to the NBKR 4/	...	1.4	...	...	1.4	1.4	...	...	...	...	...	...	...	...
Domestic quasi-fiscal deficit 5/	6.4	...	4	...	...	4.1	...	...	...	...	...	...	...	...

Source: Ministry of Finance and Fund staff projections.

1/ Excluding government contributions.

2/ It includes interest rescheduled for bilateral loans in 2000. From 2001 onwards, debt rescheduling operations are classified within external financing.

3/ Includes the new bond issuance for the guarantee of the Zhibek Zhulu loan in the amount of US\$23 million dollars.

4/ Refers to the new bond issuance for the guarantee of the Zhibek Zhulu loan.

5/ In the electricity sector.

Table 5.1. Kyrgyz Republic: State Government Finances

In millions of soms	2001		2002				2003					2004		2005		2006
	Annual	Annual	Actual	Q3	Q4	Annual	Q1	Q2	Q3	Q4	MOF	Annual	Annual	Annual	Annual	Annual
	Act.	Orig.	Rev.	Act.	Prog.	Prog.	Prog.	Proj.	Prog.	Proj.	Budget	draft	New Proj.	New Proj.	New Proj.	New Proj.
												w/ authorities				
Total revenue and grants	12,544	13,887	14,872	3,928	4,178	14,268	2,888	3,676	4,360	4,898	16,051	16,055	15,822	18,039	20,427	23,061
Total revenue	11,922	13,492	13,988	3,624	3,851	13,383	2,669	3,676	4,142	4,898	15,595	15,618	15,385	17,602	19,487	22,079
Tax revenue	9,188	11,104	11,248	2,851	3,025	10,415	2,278	2,937	3,379	3,876	12,386	12,470	12,470	14,171	15,804	17,952
Income tax	2,908	2,077	2,182	603	434	1,984	522	494	707	552	2,212	2,275	2,275	2,497	2,800	3,030
VAT	4,221	4,901	5,052	1,338	1,444	4,850	1,027	1,355	1,663	1,796	5,784	5,841	5,841	6,763	7,428	8,649
Excises	1,103	1,211	1,236	278	314	1,072	236	321	328	465	1,282	1,350	1,350	1,516	1,689	1,891
Customs	301	443	372	122	84	380	76	108	136	104	417	425	425	646	723	787
Road and emergency fund tax	990	1,162	1,105	275	322	1,063	204	304	290	447	1,294	1,244	1,244	1,202	1,319	1,440
Other	564	1,311	1,302	236	426	1,066	213	355	255	512	1,397	1,335	1,335	1,548	1,846	2,155
Nontax revenue	2,677	2,387	2,582	761	741	2,805	392	739	763	1,022	3,208	3,148	2,915	3,337	3,580	4,015
Capital revenue	57	1	158	12	84	163	0	0	0	0	1	1	1	93	102	112
Grants	622	395	884	304	327	886	218	0	218	0	456	437	437	437	940	982
Total expenditure	16,880	18,375	19,347	4,663	5,948	18,920	4,168	4,783	5,166	6,143	20,506	20,493	20,260	22,425	24,715	26,973
Current expenditure	12,966	13,303	14,226	3,429	4,279	14,147	3,211	3,949	3,813	4,759	15,226	15,965	15,732	17,852	19,908	21,905
Wages and social fund contributions	4,301	4,547	4,725	1,129	1,389	4,725	1,056	1,430	1,271	1,564	5,438	5,321	5,320	5,984	6,674	7,517
Transfers and subsidies 1/	2,619	2,636	3,061	737	823	3,061	832	942	869	988	3,511	3,631	3,631	3,640	3,850	4,248
Interest due	1,228	1,588	1,577	158	544	1,419	168	775	155	603	1,449	1,722	1,702	2,075	2,622	2,611
Purchases of goods and services	4,818	4,533	4,863	1,405	1,524	4,943	1,155	802	1,518	1,604	4,828	5,292	5,079	5,843	6,423	7,221
Capital expenditure (including PIP)	3,915	5,072	5,121	1,234	1,669	4,773	957	834	1,353	1,385	5,280	4,528	4,528	4,573	4,807	5,068
Domestically financed capital expenditure	676	662	711	258	274	814	142	124	201	206	960	674	674	840	1,233	1,715
of which: domestically financed PIP	232	413	672	114	274	594	105	92	149	152	500	497	497	540	465	436
Foreign financed PIP	3,239	4,410	4,410	977	1,394	3,959	814	710	1,152	1,178	4,320	3,854	3,854	3,733	3,573	3,353
Financial balance	-4,337	-4,488	-4,475	-735	-1,770	-4,652	-1,280	-1,107	-806	-1,245	-4,455	-4,438	-4,438	-4,386	-4,288	-3,912
Net lending	-509	-573	-573	-112	-256	-579	-115	-115	-115	-115	-475	-461	-461	-467	-510	-559
Accrual surplus (+) / deficit (-)	-3,828	-3,915	-3,902	-623	-1,514	-4,073	-1,165	-992	-691	-1,130	-3,980	-3,978	-3,978	-3,920	-3,777	-3,353
Total arrears and rescheduling 2/	155	0	-173	-122	-34	-232	0	0	0	0	0	0	0	0	0	0
Expenditure arrears	155	0	-173	-122	-34	-232	0	0	0	0	0	0	0	0	0	0
Rescheduling of external interests 2/	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Cash surplus (+) / deficit (-)	-5,673	-3,915	-4,075	-745	-1,548	-4,305	-1,165	-992	-691	-1,130	-3,980	-3,978	-3,978	-3,920	-3,777	-3,353
Total financing	3,673	3,915	4,075	745	1,548	4,305	1,165	992	691	1,130	3,980	3,978	3,978	3,920	3,777	3,353
External financing	4,208	4,571	4,637	1,040	1,839	4,234	1,105	1,004	1,207	1,410	4,147	4,773	4,726	6,326	265	303
Public investment program (PIP)	3,239	4,410	4,410	977	1,394	3,959	814	710	1,152	1,178	4,320	3,854	3,854	3,733	3,573	3,353
Disbursements (BOP support)	2,007	1,593	368	0	353	353	235	0	0	288	282	235	1,904	0	0	0
Total amortization	-1,833	-1,432	-930	-46	-99	-878	-423	-224	-224	-568	-1,596	-1,453	-1,453	-1,714	-3,309	-3,050
Debt rescheduling 3/	795	0	809	109	191	801	294	717	279	800	1,135	2,091	2,091	2,404	0	0
Domestic financing 4/	-834	-2,761	-752	-323	-357	-64	36	-35	-540	-304	-267	-890	-843	-2,498	-1,478	-1,692
NBKR	-949	...	...	-393	...	...	...	...	...	...	...	...	...	...	...	...
Provision for Restructured Treasury Bonds 5/	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...
Redemption of NBKR Treasury Bonds 5/	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...
Others	115	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...
Commercial banks	134	...	...	60	...	...	...	...	...	...	...	...	...	...	...	...
Nonbank	-19	...	...	10	...	...	...	...	...	...	...	...	...	...	...	...
Privatization proceeds	299	170	170	29	66	135	24	24	24	24	100	94	94	90	1,410	940
Privatization receipts	27	140	490	66	135	94	...	...	...	...	...	...	...	...	...	...
Noncash privatization receipts	0	0	0	0	0	0	...	...	...	...	...	...	...	...	...	...
Debt write-off from debt-to-equity swaps	0	0	0	0	0	0	...	...	...	...	...	...	...	...	...	...
Valuation adjustments on debt write-offs	0	0	0	0	0	0	...	...	...	...	...	...	...	...	...	...
Other	0	0	0	0	0	0	...	...	...	...	...	...	...	...	...	...
Financing gap 3/	0	1,935	0	0	0	0	0	0	0	0	0	1	1	2	3,580	3,802
Memorandum items:																
Primary surplus (+)/deficit (-) (w/o foreign fin. PIP)	793	2,083	1,912	1,912	390	1,072	-182	493	616	652	1,789	1,598	1,578	1,889	2,418	2,611
Primary surplus (+) / deficit (-)	-2,446	-2,327	-2,498	-2,498	-1,004	-2,886	-997	-216	-536	-527	-2,531	-2,256	-2,276	-1,844	-1,156	-743
Primary surplus (+) / deficit (-) (accrual basis)	-2,600	-2,327	-2,326	-2,326	-970	-2,654	-997	-216	-536	-527	-2,531	-2,256	-2,276	-1,844	-1,156	-743
Social Expenditure 6/	8,424	8,889	9,394	9,394	...	9,017	...	...	...	...	...	10,148	10,144	11,367	12,821	14,315
Subsidies to Public Enterprises	574	380	380	380	82	470	128	163	155	-66	...	380	380	...	...	...
Bonds issued to the NBKR 7/	...	1,166	...	...	1,119	1,119	...	...	...	...	...	...	...	...	...	...
Accumulation of financial regularization escrow account	...	...	...	2,072	...	...	0	0	0	0	...	...	...	-46	-57	-42
of which: NBKR profits	...	...	...	1,262	...	...	0	578	0	0	...	...	...	578	331	298
interest earnings on deposits with NBKR	...	...	...	5,082	...	...	0	36	0	0	...	...	...	36	51	53
interest expense on Zhibek Zholu loans and KSLB	...	...	...	...	...	...	0	-265	0	0	...	...	...	-265	-228	-208
debt redemption	...	...	...	...	...	...	0	-349	0	0	...	...	...	-349	-200	-231
External debt service (accrual basis) 8/	2,797	...	2,072	...	...	1,861	...	...	...	...	...	2,668	2,668	3,068	5,236	4,939
External debt service (cash basis) 8/	2,003	...	1,262	...	...	1,061	...	...	...	...	...	578	578	664	5,236	4,939
PIP	3,471	...	5,082	1,091	1,669	4,552	919	801	1,300	1,300	4,820	4,351	4,351	4,273	4,038	3,789
Tax revenue collection in cash	...	...	...	2,851	3,025	10,415	2,278	2,937	3,379	3,876	12,386	12,470	12,470	14,171	15,804	17,952

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

1/ The following offset transactions were carried out in 2000, but were not included in the budget: in kind grants worth Som 244 million were received, of which Som 160 million were granted as allowances to the poor, and new housing facilities. Som 84 million were granted to the military. These transactions are shown in Q3, 2001. Includes subsidies and transfers to the Social Fund.

2/ It includes interest rescheduled for bilateral loans in 2000. From 2001 onwards, debt rescheduling operations are classified within external financing.

3/ The difference between the financing gap in the BOP and the fiscal tables for 2005-06 reflect potential IMF disbursements.

4/ Includes the social fund until end-June 2002 (when the general government was introduced).

5/ The amount in 2003 refers to the redemption of the Zhibek Zholu bonds. The amounts after 2003 forms part of the NBKR's imputed dividend provision to the budget in the context of the regularization of the financial relationship between the MOF and the NBKR.

6/ Includes the Social Fund.

7/ Refers to the new bond issuance for the guarantee on the Zhibek Zholu loan.

8/ Excluding Kuntor, and debt service by the NBKR and by the state-owned enterprises.

Table 5.2. Kyrgyz Republic: State Government Finances (concluded)

In percent of GDP	2001	2002					2003					2004	2005	2006		
	Annual Act.	Annual Orig. Prog.	Annual Rev. Prog.	Q3 Act.	Q4 Prog.	Annual Prog.	Q1 Prog.	Q2 Prog.	Q3 Prog.	Q4 Prog.	MOF Budget	Annual draft MEP	Annual New Proj.	Annual New Proj.	Annual New Proj.	Annual New Proj.
												w/ authorities				
Total revenue and grants	17.0	17.0	18.3	5.1	5.4	18.4	3.4	4.3	5.1	5.7	18.8	18.8	18.5	19.3	20.0	20.6
Total revenue	16.1	16.6	17.2	4.7	5.0	17.3	3.1	4.3	4.9	5.7	18.3	18.3	18.0	18.9	19.1	19.8
Tax revenue	12.4	13.6	13.8	3.7	3.9	13.4	2.7	3.4	4.0	4.5	14.5	14.6	14.6	15.2	15.5	16.1
Income tax	2.7	2.5	2.7	0.8	0.6	2.6	0.6	0.6	0.8	0.6	2.6	2.7	2.7	2.7	2.7	2.7
VAT	5.7	6.0	6.2	1.7	1.9	6.3	1.2	1.6	1.9	2.1	6.8	6.8	6.8	7.2	7.3	7.7
Excises	1.5	1.5	1.5	0.4	0.4	1.4	0.3	0.4	0.4	0.5	1.5	1.6	1.6	1.6	1.7	1.7
Customs	0.4	0.5	0.5	0.2	0.1	0.5	0.1	0.1	0.2	0.1	0.5	0.5	0.5	0.7	0.7	0.7
Road and emergency fund tax	1.3	1.4	1.4	0.4	0.4	1.4	0.2	0.4	0.3	0.5	1.5	1.5	1.5	1.3	1.3	1.3
Other	0.8	1.6	1.6	0.3	0.6	1.4	0.2	0.4	0.3	0.6	1.6	1.6	1.6	1.7	1.8	1.9
Other revenue	3.7	2.9	3.4	1.0	1.1	3.8	0.5	0.9	0.9	1.2	3.8	3.7	3.4	3.7	3.6	3.7
Grants	0.8	0.5	1.1	0.4	0.4	1.1	0.3	0.0	0.3	0.0	0.5	0.5	0.5	0.5	0.9	0.9
Total expenditure	22.8	22.5	23.7	6.0	7.7	24.4	4.9	5.6	6.1	7.2	24.0	24.0	23.8	24.0	24.2	24.1
Current expenditure	17.5	16.3	17.5	4.4	5.5	18.3	3.8	4.6	4.5	5.6	17.8	18.7	18.4	19.1	19.5	19.6
Wages and social fund contributions	5.8	5.6	5.8	1.5	1.8	6.1	1.2	1.7	1.5	1.8	6.4	6.2	6.2	6.4	6.5	6.7
Transfers and subsidies 1/	3.5	3.2	3.8	1.0	1.1	3.9	1.0	1.1	1.0	1.2	4.1	4.3	4.3	3.9	3.8	3.8
Interest due	1.7	1.9	1.9	0.2	0.7	1.8	0.2	0.9	0.2	0.9	1.7	2.0	2.0	2.2	2.6	2.3
Purchases of goods and services	6.5	5.6	6.0	1.8	2.0	6.2	1.4	0.9	1.8	1.9	5.7	6.2	6.0	6.3	6.3	6.5
Capital expenditure (including PIP)	5.3	6.2	6.3	1.6	2.2	6.2	1.1	1.0	1.6	1.6	6.2	5.3	5.3	4.9	4.7	4.5
Domestically financed capital expenditure	0.9	0.8	0.9	0.3	0.4	1.1	0.2	0.1	0.2	0.2	1.1	0.8	0.8	0.9	1.2	1.5
of which: domestically financed PIP	0.3	0.5	0.8	0.1	0.4	0.8	0.1	0.1	0.1	0.2	0.6	0.6	0.6	0.6	0.5	0.4
Foreign financed PIP	4.4	5.4	5.4	1.3	1.8	5.1	1.0	0.8	1.3	1.4	5.1	4.5	4.5	4.0	3.5	3.0
Financial balance	-5.9	-5.5	-5.5	-0.9	-2.3	-6.0	-1.5	-1.3	-0.9	-1.5	-5.2	-5.2	-5.2	-4.7	-4.2	-3.5
Net lending	-0.7	-0.7	-0.7	-0.1	-0.3	-0.7	-0.1	-0.1	-0.1	-0.1	-0.6	-0.5	-0.5	-0.5	-0.5	-0.5
Accrual surplus (+) / deficit (-)	-5.2	-4.8	-4.8	-0.8	-2.0	-5.3	-1.4	-1.2	-0.8	-1.3	-4.7	-4.7	-4.7	-4.2	-3.7	-3.0
Total arrears and rescheduling 2/	0.2	0.0	-0.2	-0.2	0.0	-0.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Cash surplus (+) / deficit (-)	-5.0	-4.8	-5.0	-1.0	-2.0	-5.6	-1.4	-1.2	-0.8	-1.3	-4.7	-4.7	-4.7	-4.2	-3.7	-3.0
Total financing	5.0	4.8	5.0	1.0	2.0	5.6	1.4	1.2	0.8	1.3	4.7	4.7	4.7	4.2	3.7	3.0
External financing	5.7	5.6	5.7	1.3	2.4	5.5	1.3	1.2	1.4	1.7	4.9	5.6	5.5	6.8	6.3	6.3
Public investment program (PIP)	4.4	5.4	5.4	1.3	1.8	5.1	1.0	0.8	1.3	1.4	5.1	4.5	4.5	4.0	3.5	3.0
Disbursements (BOP support)	2.7	2.0	0.5	0.0	0.5	0.5	0.3	0.0	0.0	0.0	0.3	0.3	0.3	2.0	0.0	0.0
Total amortization	-2.5	-1.8	-1.1	-0.1	-0.1	-1.1	-0.3	-0.5	-0.3	-0.7	-1.9	-1.7	-1.7	-1.8	-3.2	-2.7
Debt rescheduling 3/	1.1	0.0	1.0	0.1	0.2	1.0	0.3	0.8	0.3	0.9	1.3	2.5	2.5	2.6	0.0	0.0
Domestic financing	-1.1	-3.4	-0.9	-0.4	-0.5	-0.1	0.0	0.0	-0.6	-0.4	-0.3	-1.0	-1.0	-2.7	-1.4	-1.5
NBKR	-1.3	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...
Redemption of NBKR Treasury Bonds 4/	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...
Others	0.2	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...
Privatization proceeds	0.4	0.0	0.0	0.0	0.1	0.2	0.0	0.0	0.0	0.0	0.1	0.1	0.1	0.1	1.4	0.8
Financing gap 3/	0.0	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...
Memorandum items:																
Primary surplus (+)/deficit (-) (w/o foreign fin. PIP)	1.1	2.6	2.3	0.5	0.5	1.4	-0.2	0.6	0.7	0.8	2.1	1.9	1.9	2.0	2.4	2.3
Primary surplus (+) / deficit (-)	-3.3	-2.9	-3.1	-0.8	-1.3	-3.7	-1.2	-0.3	-0.6	-0.6	-3.0	-2.6	-2.7	-2.0	-1.1	-0.7
Social Expenditure 5/	11.4	10.9	11.5	...	...	11.6	...	...	...	...	...	11.9	11.9	12.2	12.6	12.8
Subsidies to Public Enterprises	0.8	0.5	0.5	0.2	-0.1	0.6	0.1	0.2	0.2	-0.1	0.2	...	...	...	...	...
Primary surplus (+) / deficit (-) (accrual basis)	-3.5	-2.9	-2.9	-0.6	-1.3	-3.4	-1.2	-0.3	-0.6	-0.6	...	-2.6	-2.7	-2.0	-1.1	-0.7
Bonds issued to the NBKR 6/	...	1.4	...	...	1.4	...	...	...	...	...	...	...	...	...	...	...
Accumulation of financial regularization escrow account	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...
of which: NBKR profits	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...
interest earnings on deposits with NBI	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...
interest expense on Zhibek Zhulu loan	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...
debt redemption	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...
External debt service (accrual basis) 7/	3.8	...	2.5	...	...	2.4	...	...	...	...	...	...	...	...	...	...
External debt service (cash basis) 7/	2.7	...	1.5	...	...	1.4	...	...	...	...	...	3.1	3.1	3.3	5.1	4.4
PIF	4.7	...	6.2	1.4	2.2	5.9	1.1	0.9	1.5	1.6	...	5.1	5.1	4.6	4.0	3.4
VAT/private consumption	8.6	...	...	...	...	9.4	...	...	...	...	...	10.4	10.4	10.9	11.1	11.7

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

1/ The following offset transactions were carried out in 2000, but were not included in the budget: in kind grants worth Som 244 million were received, of which Som 160 million were granted as allowances to the poor, and new housing facilities. Som 84 million were granted to the military. These transactions are shown in Q3, 2001. Includes all transfers and subsidies to the Social Fund.

2/ It includes interest rescheduled for bilateral loans in 2000. From 2001 onwards, debt rescheduling operations are classified within external financing.

3/ The difference between the financing gap in the BOP and the fiscal tables for 2005-06 reflect potential IMF disbursements.

4/ The amount in 2003 refers to the redemption of the Jibek Jolou bonds. The amounts after 2003 forms part of the NBKR's imputed dividend provision to the budget in the context of the regularization of the financial relationship between the MOF and the NBKR.

5/ Includes the Social Fund.

6/ Refers to the new bond issuance for the guarantee on the Zhibek Zhulu loan.

7/ Excluding Komtor, and debt service by the NBKR and by the state-owned enterprises.

Table 6. Kyrgyz Republic: Social Fund

	2001	2002					2003				2004	2005	2006	
	Annual Act.	Annual Orig. Prog.	Annual Rev. Prog.	Q3 Act.	Q4 New Proj.	Annual New Proj.	Q1 New Proj.	Q2 New Proj.	Q3 New Proj.	Q4 New Proj.	Annual New Proj.	Annual New Proj.	Annual New Proj.	Annual New Proj.
(In millions of soms)														
Total revenues	3704	4574	4669	1168	1315	4483	1142	1109	1309	1464	5024	5499	5928	6399
Total contributions received	3218	3843	3765	953	1070	3600	816	894	1033	1160	3903	4247	4632	5052
Total transfers from state budget	398	667	840	207	229	840	311	200	261	289	1061	1190	1232	1280
Other revenue	88	64	64	8	17	43	15	15	15	15	60	62	64	67
Total expenditures	3974	4524	4613	1106	1205	4536	1216	1097	1240	1382	4934	5449	5894	6369
Pension Fund	3504	3996	4124	1068	1087	4111	1148	1037	1193	1214	4592	5054	5475	5933
Transfers to other funds	321	528	517	67	169	403	78	80	57	178	392	405	420	436
Social Insurance Fund	143	168	232	40	39	148	17	30	27	26	99	102	106	110
Employment Fund	97	158	156	21	41	99	20	16	21	41	99	102	106	110
Medical Insurance Fund	81	201	129	6	89	156	40	34	9	111	194	201	208	216
Accrual surplus(+)/deficit (-)	-271	50	56	61	110	-53	-74	12	70	82	90	50	34	30
Net accumulation (+)/repayment (-) of arrears	149	-50	-28	-29	-51	22	-10	-20	-10	-10	-50	-11	-21	-35
Cash surplus(+)/deficit (-)	-121	0	28	33	59	-31	-84	-8	60	72	40	39	13	-5
(In percent of GDP)														
Total revenues	5.0	5.7	5.7	1.5	1.7	5.8	1.3	1.3	1.5	1.7	5.9	5.9	5.8	5.7
Total contributions received	4.4	4.8	4.6	1.2	1.4	4.6	1.0	1.0	1.2	1.4	4.6	4.6	4.5	4.5
Total transfers from State budget	0.5	0.8	1.0	0.3	0.3	1.1	0.4	0.2	0.3	0.3	1.2	1.3	1.2	1.1
Other revenue	0.1	0.1	0.1	0.0	0.0	0.1	0.0	0.0	0.0	0.0	0.1	0.1	0.1	0.1
Total expenditures	5.4	5.6	5.7	1.4	1.6	5.9	1.4	1.3	1.5	1.6	5.8	5.8	5.8	5.7
Pension Fund	4.7	4.9	5.1	1.4	1.4	5.3	1.3	1.2	1.4	1.4	5.4	5.4	5.4	5.3
Transfers to other funds	0.6	0.7	0.6	0.0	0.2	0.5	0.1	0.1	0.1	0.2	0.4	0.4	0.4	0.4
Net accumulation of arrears	0.2	0.0	0.0	0.0	-0.1	0.0	0.0	0.0	0.0	0.0	-0.1	0.0	0.0	0.0
Accrual surplus(+)/deficit (-)	-0.4	0.1	0.1	0.1	0.1	-0.1	-0.1	0.0	0.1	0.1	0.1	0.1	0.0	0.0
Net accumulation (+)/repayment (-) of arrears	0.2	-0.1	0.0	0.0	-0.1	0.0	0.0	0.0	0.0	0.0	-0.1	0.0	0.0	0.0
Cash surplus(+)/deficit (-)	-0.2	0.0	0.0	0.0	0.1	0.0	-0.1	0.0	0.1	0.1	0.0	0.0	0.0	0.0

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

Table 7: Medium Term Expenditure Framework for General Budget (excluding PIP), by Functional Classification

(In percent of GDP)

As percent of GDP		1999	2000	2001	2002	2002	2003	2004	2005	2006
		Actual	Actual	prel.	orig.prog.	rev. prog.	rev. proj.	rev. proj.	rev. proj.	rev. proj.
Total Expenditure of General Government		...	21.7	21.5	20.6	22.1	22.0	22.8	23.5	23.8
I.	General public services	2.6	3.1	2.8	2.7	2.7	2.7	2.6	2.6	2.6
II.	Defense	1.7	1.8	1.3	1.5	1.5	1.5	1.5	1.5	1.5
III.	Public order and safety affairs	0.9	1.1	1.0	0.9	0.9	1.0	1.0	1.0	1.0
Social Spending		8.6	10.8	11.4	13.1	11.6	11.9	12.2	12.6	12.8
IV.	Education	3.9	3.5	3.9	3.7	4.0	4.1	4.2	4.3	4.3
V.	Health	2.3	2.0	1.9	2.1	2.1	2.3	2.4	2.6	2.7
VI.	Social security and welfare affairs	2.5	1.7	1.9	1.8	2.0	2.2	2.3	2.4	2.6
VII.	Social Fund	...	3.6	3.8	5.6	3.5	3.3	3.3	3.3	3.2
VIII.	Housing and community services	1.0	1.0	1.1	0.7	0.7	0.7	0.8	0.9	0.9
IX.	Recreational, cultural and religious activities	0.6	0.5	0.4	0.4	0.4	0.4	0.4	0.4	0.4
X.	Energy complex (electricity production)	0.2	0.0	0.3	0.0	0.0	0.0	0.0	0.0	0.0
XI.	Agriculture, water resources, forestry	0.7	0.7	0.8	0.5	0.5	0.5	0.5	0.6	0.6
XII.	Mining and mineral resources	0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
XIII.	Transportation and communication	1.1	0.7	0.6	0.6	0.6	0.6	0.6	0.7	0.7
XIV.	Other economic affairs and services	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
XV.	Other	0.9	1.4	0.6	...	3.1	2.4	2.9	3.1	3.2
XVI.	Unidentified expenditure	...	0.3	1.0	...	0.0	0.0	0.0	0.0	0.0

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

Table 8. Kyrgyz Republic: NBKR Accounts, 2001-2003

(In millions of soms; end-period stocks) 1/

	2001		2002						2003			
	Dec. Act.	Mar. Act.	Jun. Act.	Sep. Rev. Prog.	Sep. Act.	Dec. Orig. Prog.	Dec. Rev. Prog.	Dec. New Prog.	Mar. Prog.	Jun. Prog.	Sep. Prog.	Dec. Prog.
Net foreign assets	4,947	4,945	3,939	3,914	5,018	2,229	4,236	5,718	6,079	6,083	6,497	6,766
Net international reserves (without foreign assets with high risk)	1,930	2,626	2,863	2,820	3,915	977	3,142	4,517	4,895	4,917	5,347	5,633
Other foreign assets	3,068	2,370	1,128	1,145	1,154	...	1,145	1,252	1,235	1,218	1,201	1,184
Balance with CIS countries	-51	-51	-51	-51	-51	-51	-51	-51	-51	-51	-51	-51
Long-term foreign liabilities	-2,716	-2,709	-2,721	-2,698	-2,742	-2,718	-2,674	-2,607	-2,607	-2,583	-2,583	-2,560
Net domestic assets	3,128	3,390	4,945	4,484	4,511	5,954	4,230	4,321	4,205	4,284	3,961	3,710
Domestic credit (net)	3,424	3,614	4,836	4,223	4,464	...	4,099	4,191	4,063	4,094	3,792	3,503
Claims on government (net), o/w:	2,911	3,133	4,429	3,584	4,036	1,593	3,251	3,570	3,690	3,662	3,062	2,687
Loan to gov in forex (Turkish loan)	2,135	2,135	2,135	2,135	2,135	2,135	2,135	2,048	2,048	2,048	2,048	2,048
Total government deposits	-2,078	-1,861	-1,412	-2,295	-1,808	-3,478	-2,629	-2,187	-2,067	-2,095	-2,695	-3,070
Government restructurization bonds 2/	1,563	1,563	1,286	1,283	1,286	...	1,283	1,286	0	0	0	0
Repos	25	-35	-109	150	-67	...	360	100	-125	-65	240	325
Claims on DMB	488	515	517	488	494	544	488	521	498	497	490	491
Other items net	-296	-223	109	261	47	3,817	132	130	142	190	169	207
including DEBRA liabilities under EBRD	97	97	147	97	97	...	97	93	93	93	93	93
Reserve money	5,359	5,626	6,164	5,700	6,786	5,465	5,793	7,432	7,677	7,784	7,874	7,916
Money outside of the banks	5,022	5,214	5,615	...	6,235	...	...	...	...	...	...	...
Deposits of banks in foreign currency	0	0	0	...	0	...	...	...	...	...	...	...
Cash of commercial banks	153	140	121	...	172	...	...	...	...	...	...	...
Reserves of commercial banks	184	272	428	...	380	...	...	...	...	...	...	...
<i>Memorandum items:</i>												
Reserve money growth (12 month)	11.3	21.9	44.6	13.8	35.5	8.1	8.1	38.7	36.5	26.3	16.0	6.5
Gross reserves (in millions of U.S. dollars)	221.8	231.5	230.9	243.4	262.8	210.0	257.3	270.8	289.1	279.6	296.2	306.7
in months of imports	4.1	3.8	3.8	4.3	4.3	3.6	4.6	4.5	4.5	4.3	4.6	4.7
Net international reserves (in millions of U.S. dollars)	39.4	53.6	58.4	57.6	79.9	19.9	64.1	96.1	104.2	104.6	113.8	119.9
change over previous period (in millions of U.S. dollars)	-34.1	14.2	4.9	7.2	21.5	...	6.6	15.4	8.0	0.5	9.1	6.1
Net domestic assets 3/	631	893	2,438	1,987	2,007	...	1,733	1,920	1,804	1,883	1,560	1,308

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

1/ Until September 2002, actual and programmed foreign exchange assets and liabilities are valued at the program exchange rate of 49 soms per US dollar, 1.259 U.S. dollar per SDR and a gold price of U.S. dollar 265.5 per Troy ounce. Programmed foreign exchange assets and liabilities are otherwise valued at the exchange rate of 47 soms per U.S. dollar, 1.3186 U.S. dollar per SDR and a gold price of U.S. dollar 322.4 per Troy ounce.

2/ As of January 1, 2003, the bonds are restructured as part of the regularization of financial relations between the NBKR and the MOF.

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

Table 9. Kyrgyz Republic: Monetary Survey, 2001-2003

(In millions of soms; end-period stocks) 1/

	2001				2002				2003			
	Dec. Act.	Mar. Act.	Jun. Act.	Sep. Rev. Prog.	Sep. Act.	Dec. Rev. Prog.	Dec. Prog.	Mar. Prog.	Jun. Prog.	Sep. Prog.	Dec. Prog.	
Net foreign assets	6,534	6,468	5,313	5,815	6,805	5,131	6,235	7,619	8,196	8,158	8,764	9,108
NBKR	4,947	4,945	3,939	3,914	5,018	3,229	4,236	5,718	6,079	6,083	6,497	6,766
Commercial Banks	1,587	1,523	1,374	1,901	1,787	1,902	1,999	1,901	2,117	2,075	2,267	2,343
Medium-term NBK obligations	-2,716	-2,709	-2,721	-2,698	-2,742	-2,718	-2,674	-2,607	-2,607	-2,583	-2,583	-2,560
Net domestic assets	4,443	4,980	6,365	5,940	5,960	7,347	5,865	5,596	5,433	5,736	5,462	5,469
Credit to government, net	3,325	3,491	4,829	3,742	4,496	1,946	3,128	4,029	4,149	4,121	3,521	3,146
Credit from the NBKR	2,911	3,133	4,429	3,584	4,036	1,593	3,251	3,570	3,690	3,662	3,062	2,687
Commercial banks	414	358	400	158	460	353	-123	458	458	458	458	458
Government bonds	132	130	126	130	126	...	130	126	126	126	126	126
Treasury bills actual value	323	400	404	400	428	...	400	428	428	428	428	428
Other	-41	-172	-130	-372	-94	0	-653	-95	-95	-95	-95	-95
Credit to rest of the economy	2,831	2,864	2,908	3,431	2,924	4,273	4,101	2,897	2,602	2,884	3,232	3,575
of which: extended in foreign currency	1,965	2,004	2,079	...	2,106	...	...	...	...	...	...	...
Other items, net	-1,713	-1,374	-1,372	-1,233	-1,461	1,128	-1,363	-1,329	-1,317	-1,269	-1,290	-1,252
Broad money	8,260	8,739	8,957	9,057	10,023	8,760	9,427	10,608	11,022	11,311	11,643	12,017
Currency outside banks	5,020	5,211	5,615	...	6,234	5,338	...	...	...	...	...	...
Deposits	3,240	3,528	3,342	...	3,788	3,422	...	...	...	...	...	...
of which: foreign currency deposits	2,071	2,244	2,041	2,273	2,493	2,150	2,296	2,561	2,612	2,612	2,691	2,772
Broad money: som component	6,189	6,495	6,916	6,784	7,530	6,610	7,131	8,047	8,410	8,698	8,952	9,246
<i>Memorandum items:</i>												
Velocity (quarterly) 2/	9.3	8.7	8.4	8.2	7.9	10.8	8.6	7.6	7.3	7.2	7.2	7.2
Som velocity (quarterly) 2/	12.9	11.7	11.1	11.2	10.4	14.3	11.7	10.0	9.5	9.4	9.4	9.4
Broad money growth (12 months)	12.0	22.7	28.1	18.5	31.1	12.4	14.1	29.8	27.4	27.5	17.3	13.3
Som broad money growth (12 months)	17.0	25.4	35.3	17.9	30.9	12.1	15.2	30.0	29.5	25.8	18.9	14.9
Multiplier	1.5	1.6	1.5	1.6	1.5	1.6	1.6	1.4	1.4	1.5	1.5	1.5
Financial Soundness indicators:												
Equity capital to total assets	52.2	...	43.4	...	...	...	...	...	...	...	...	...
Non-performing loans (NPLs) to total loans	13.4	...	13.8	...	...	...	...	...	...	...	...	...
Total provisioning to NPLs	63.5	...	69.2	...	...	...	...	...	...	...	...	...
Return on assets	1.5	...	1.0	...	...	...	...	...	...	...	...	...
Liquid assets to total assets	27.0	...	33.6	...	...	...	...	...	...	...	...	...

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

1/ Until September 2002, actual and programmed foreign exchange assets and liabilities are valued at the program exchange rate of 49 soms per US dollar, 1.259 U.S. dollar per SDR and a gold price of U.S. dollar 265.5 per Troy ounce. Programmed foreign exchange assets and liabilities are otherwise valued at the exchange rate of 47 soms per U.S. dollar, 1.3186 U.S. dollar per SDR and a gold price of U.S. dollar 322.4 per Troy ounce.

2/ 12 month GDP over average quarterly broad money.

Table 10. Kyrgyz Republic: Quarterly Balance of Payments: 2000 - 2003

(in millions of USD)

	2000	2001	2002				2003							
	Year Act.	Year Act.	Q1 Act.	Q2 Act.	Q3 Prel.	Q4 Prog.	Year Orig. Prog.	Year Rev. Prog.	Year New Prog.	Q1 Prog.	Q2 Proj.	Q3 Proj.	Q4 Proj.	Year Prog.
Current account balance	-90.8	-51.0	-16.3	-4.5	-16.2	-9.7	-103.1	-62.7	-46.7	-26.7	-5.7	-33.0	-10.8	-76.2
(excluding official transfers)	-152.4	-85.2	-30.2	-16.2	-34.6	-24.8	-160.0	-109.5	-105.8	-40.1	-20.2	-47.7	-26.4	-134.4
Trade balance	4.0	39.9	-14.8	3.3	-24.1	-17.2	-11.3	5.3	-52.7	-18.6	-1.9	-15.9	6.5	-29.8
Exports, fob	510.9	480.3	117.0	127.7	110.6	121.4	496.2	490.0	476.6	121.9	140.9	135.1	145.1	542.9
CIS countries	213.7	172.2	34.5	37.0	45.9	47.0	203.9	189.7	164.4	41.4	49.4	38.2	45.7	174.7
Energy	82.0	51.5	3.3	2.3	10.6	9.2	48.1	47.6	25.4	9.0	8.0	6.4	6.4	29.9
Other	131.7	120.7	31.1	34.7	35.3	37.8	155.8	142.1	139.0	32.4	41.4	31.8	39.2	144.8
Non-CIS	297.2	308.0	82.5	90.7	64.7	74.3	292.3	300.3	312.2	80.6	91.4	96.8	99.4	368.3
Gold	195.3	224.6	45.3	45.8	27.6	37.6	195.9	212.3	156.3	38.5	43.5	60.0	64.7	206.8
Imports, fob	506.9	440.3	131.7	124.4	134.6	138.5	507.5	484.7	529.3	140.5	142.8	150.9	138.5	572.7
CIS countries	279.7	250.0	80.1	68.9	73.6	84.7	272.7	260.7	307.4	84.1	78.8	83.9	77.1	323.9
Energy	120.4	116.7	48.0	25.7	31.6	43.5	104.1	98.3	148.9	44.8	34.4	32.5	41.4	153.1
Other	159.3	133.4	32.1	43.1	42.1	41.2	168.6	162.4	158.5	39.3	44.4	51.4	35.7	170.7
Non-CIS	227.2	190.3	51.6	55.5	61.0	53.8	234.8	223.9	222.0	56.4	63.9	67.1	61.4	248.8
Services (net)	-170.9	-110.1	-13.7	-17.5	-8.2	-6.9	-125.7	101.5	-46.2	-18.6	-17.9	-26.8	-28.5	-91.8
Non-interest service	-86.9	-44.5	-4.5	-1.5	-0.6	-0.7	-71.0	-38.4	-7.3	-10.0	-2.9	-8.8	-7.9	-29.6
Interest payments (scheduled)	-51.3	-39.4	-3.7	-10.2	-4.2	-10.1	-38.7	-38.8	-28.1	-4.1	-12.6	-3.9	-13.0	-33.6
o/w moratorium interest	0.0	0.0	0.0	0.0	-0.8	-0.9	0.0	-0.7	-1.7	-1.1	-1.1	-1.1	-1.1	-4.4
Other net income	-32.6	-26.2	-5.5	-5.8	-3.4	3.8	-16.0	-24.3	-10.9	-4.5	-2.4	-14.1	-7.5	-28.6
Transfers (net)	76.0	19.1	12.1	9.7	16.0	14.4	33.9	33.5	52.2	10.5	14.0	9.7	11.2	45.4
Official	61.7	34.2	13.8	11.7	18.4	15.1	56.9	46.8	59.1	13.4	14.5	14.7	15.6	58.2
Private	14.4	-15.1	-1.7	-2.0	-2.4	-0.7	-23.0	-13.3	-6.9	-2.9	-0.5	-5.0	-4.4	-12.9
Capital account balance	64.3	-9.5	37.9	-3.2	34.5	13.3	22.4	37.4	82.5	25.0	-8.1	36.3	1.3	54.3
Commercial banks	-1.9	-12.5	-3.8	-0.3	1.7	-4.0	-5.0	-8.4	-6.4	-4.6	0.9	-4.1	-1.6	-9.4
Medium and long-term loans, net	40.6	-23.5	12.4	-27.2	17.6	12.4	-7.5	4.1	15.3	11.7	-15.7	19.2	-2.6	12.5
Disbursement	131.3	73.6	14.2	18.3	19.9	36.6	95.0	95.0	89.0	17.3	15.1	24.5	25.1	82.0
CIS	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Non-CIS	131.3	73.6	14.2	18.3	19.9	36.6	95.0	95.0	89.0	17.3	15.1	24.5	25.1	82.0
Of which PIP	92.3	67.8	14.1	18.3	19.9	29.7	90.0	90.0	82.0	17.3	15.1	24.5	25.1	82.0
Amortization (scheduled)	-90.7	-97.1	-1.8	-45.5	-2.3	-24.1	-102.5	-90.9	-73.7	-5.6	-30.8	-5.3	-27.7	-69.5
CIS	-13.2	-22.5	-0.3	0.0	-0.3	-0.8	-1.4	0.0	-1.5	-0.3	-0.3	-0.4	-0.4	-1.4
Non-CIS	-77.4	-74.6	-1.5	-45.5	-2.0	-23.3	-101.1	-90.9	-72.2	-5.4	-30.5	-4.9	-27.3	-68.1
Of which Kumtor	-49.3	-49.3	0.0	-18.0	0.0	-18.0	-49.3	-49.3	-36.0	0.0	-18.0	0.0	-12.0	-30.0
Foreign direct investment	-6.9	-1.1	11.1	-12.2	11.1	4.3	33.8	25.0	14.3	11.0	2.9	14.4	7.4	30.7
Other assets (including acc. pay. & receiv.)	32.5	27.6	18.3	36.5	4.1	0.5	1.1	16.7	59.4	6.9	3.7	6.7	3.1	20.5
Errors and omissions & short term capital	10.3	19.0	-22.7	4.6	0.0	0.0	0.0	0.0	-18.1	0.0	0.0	0.0	0.0	0.0
Overall balance	-16.2	-41.6	-1.1	-3.1	18.3	3.6	-80.8	-25.3	17.7	-1.7	-13.9	3.3	-9.5	-21.9
Financing	16.2	41.6	1.1	3.2	-18.3	-3.6	36.3	-24.8	-17.6	1.7	13.9	-3.3	9.5	21.8
NIR	-13.9	-18.4	-14.7	-4.9	-22.0	-15.4	3.8	-31.5	-56.9	-8.0	-0.5	-9.2	-6.1	-23.8
Gross official reserves (- increase)1/	-21.2	-16.3	-9.8	0.7	-31.9	-7.9	-2.9	6.7	-49.0	-18.4	9.6	-16.7	-10.5	-36.0
IMF (net)	7.3	-2.1	-4.9	-5.6	9.9	-7.5	6.7	29.4	-8.0	10.4	-10.1	7.5	4.4	12.2
Purchases and disbursements	18.7	14.9	0.0	0.0	14.8	0.0	29.4	-22.7	14.8	15.5	0.0	12.7	12.7	40.8
Repurchases and repayments	-11.4	-17.0	-4.9	-5.6	-4.9	-7.5	-22.7	25.0	-22.8	-5.2	-10.1	-5.2	-8.3	-28.7
Release of pledged reserves 2/	0.0	0.0	13.2	0.0	0.0	0.0	0.0	17.6	13.2	0.0	0.0	0.0	0.0	0.0
Exceptional Financing (including arrears)	30.1	19.1	2.6	8.1	3.7	4.3	32.5	-2.2	18.6	4.7	14.4	5.9	15.6	40.6
Accumulation of arrears (net)	0.8	-14.7	0.9	0.2	1.8	0.2	0.0	19.8	3.0	-1.5	-0.9	-0.1	-1.4	-3.8
Debt rescheduling	29.3	33.8	1.7	7.9	1.9	4.1	0.0	0.0	15.6	6.3	15.3	5.9	17.0	44.5
on arrears	0.0	0.0	0.0	0.0	0.0	0.0	0.0	6.1	0.0	0.0	0.0	0.0	0.0	0.0
on principal	0.0	16.2	0.3	2.2	0.3	1.5	0.0	12.9	4.4	4.5	8.6	4.2	11.1	28.5
on interest	0.0	17.6	1.4	5.7	1.2	2.1	0.0	0.8	10.4	1.1	6.0	1.1	5.2	13.4
on moratorium interest	0.0	0.0	0.0	0.0	0.4	0.4	0.0	7.5	0.8	0.7	0.7	0.7	0.7	2.6
BOP support (ADB) 3/	0.0	33.4	0.0	0.0	0.0	7.5	17.5	0.0	7.5	0.0	0.0	0.0	0.0	0.0
BOP support (WB) 3/	0.0	7.5	0.0	0.0	0.0	0.0	15.0	0.0	0.0	5.0	0.0	0.0	0.0	5.0
Financing gap (-) (after fiscal measures)	0.0	0.0	0.0	0.0	0.0	0.0	-44.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum Items														
Gross reserves in months of imports		4.1	3.8	3.8	4.3	4.5	3.7	4.6	4.5	4.5	4.3	4.6	4.7	4.7

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

1/ Valued at end-year exchange rates. Gross reserves exclude NBKR pledges to secure government-guaranteed loans and blocked deposits.

2/ Paris Club Savings

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

Table 11: Kyrgyz Republic: External Financing Requirements: 2000-2006

(In millions of U.S. dollars)

	2000 Actual	2001 Est.	2002 Orig. Prog.	2002 Proj.	2003 Proj.	2004 Proj.	2005 Proj.	2006 Proj.
1. Gross Financing requirements	274.9	230.3	288.1	248.2	272.4	284.4	284.9	278.0
External current account deficit (excluding official transfers)	152.4	85.2	160.0	105.8	134.4	152.1	151.3	142.9
Debt Amortization	90.7	97.1	102.5	73.7	69.5	80.4	108.0	87.1
Repayment of Arrears	-0.8	14.7	0.0	-3.0	3.8	0.0	0.0	0.0
Gross Reserves	21.2	16.3	2.9	49.0	36.0	23.0	-2.2	23.2
IMF repurchases and repayments	11.4	17.0	22.7	22.8	28.7	28.9	27.8	24.8
2. Available financing	274.9	230.3	243.6	248.3	272.4	284.4	191.5	181.8
Foreign Direct Investment	-6.9	-1.1	33.8	14.3	30.7	30.7	48.9	58.0
Medium and long term loans	131.3	73.6	95.0	89.0	82.0	79.4	82.0	75.3
Balance of payments Support 1/	0.0	40.9	32.5	7.5	5.0	40.5	0.0	0.0
World Bank	0.0	7.5	15.0	0.0	5.0	15.5	0.0	0.0
AsDB	0.0	33.4	17.5	7.5	0.0	25.0	0.0	0.0
IMF purchases	18.7	14.9	29.4	14.8	40.8	25.4	0.0	0.0
Debt Rescheduling	29.3	33.8	0.0	15.6	44.5	51.2	0.0	0.0
Other flows 2/	102.5	68.1	52.9	107.1	69.3	57.1	60.6	48.5
3. Financing gap	0.0	0.0	-44.5	0.0	0.0	0.0	-93.4	-96.2

Source: Kyrgyz authorities and Fund staff estimates and projections.

1/ BOP support loans for 2000 are shown as part of official disbursements.

2/ Includes official transfers, errors and omissions, capital account transactions of commercial banks and other assets.

Table 12. Kyrgyz Republic: Medium-Term Balance of Payments, 2000-2010
(In millions of U.S. dollars)

	2000	2001	2002			2003	2004	2005	2006	2007	2008	2009	2010
	Actual	Actual	Orig.	Prog.	Rev. Prog.	Prel.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
Current account balance 1/	-90.8	-51.0	-103.1	-62.6	-46.7	-76.2	-93.3	-91.8	-97.5	-103.1	-130.0	-147.1	-150.7
Trade balance	4.0	39.9	-11.3	5.3	-52.7	-29.8	-58.9	-67.1	-89.5	-97.6	-138.1	-162.4	-172.2
Exports, fob	510.9	480.3	496.2	490.0	476.6	542.9	548.5	576.6	610.4	653.2	658.8	679.8	726.8
CIS countries	213.7	172.2	203.9	189.7	164.4	174.7	191.0	226.4	251.2	282.7	318.0	357.4	400.8
of which : Energy	82.0	51.5	...	47.6	25.4	29.9	35.5	53.9	57.7	61.7	66.1	70.7	75.6
Other countries	297.2	308.0	292.3	300.3	312.2	368.3	357.5	350.3	359.1	370.5	340.7	322.4	326.0
Of which : Gold	195.3	224.6	195.9	212.3	156.3	206.8	187.1	163.9	157.1	148.9	93.6	55.7	37.9
Imports, fob	506.9	440.3	507.5	484.7	529.3	572.7	607.4	643.8	699.9	750.8	796.8	842.2	899.0
CIS countries	279.7	250.0	272.7	260.7	307.4	323.9	345.6	367.4	400.2	433.8	466.8	502.2	540.4
Other countries	227.2	190.3	234.8	223.9	222.0	248.8	261.7	276.3	299.7	317.0	330.1	340.0	358.6
Services (net)	-170.9	-110.1	-125.7	-101.4	-46.2	-91.8	-81.4	-76.9	-49.5	-38.6	-27.5	-19.2	-9.0
Non-interest service	-86.9	-44.5	-71.0	-38.4	-7.3	-29.6	-30.8	-20.8	1.4	10.0	18.9	26.5	35.3
Receipts	61.8	80.5	68.1	97.4	116.5	126.8	138.1	154.5	173.0	191.9	211.4	230.2	251.7
Payments	-148.8	-125.1	-139.0	-135.9	-123.7	-156.4	-168.8	-175.3	-171.6	-181.9	-192.4	-203.7	-216.5
Interest payments (scheduled)	-51.3	-39.4	-38.7	-38.7	-28.1	-33.6	-37.9	-46.7	-43.3	-41.0	-40.1	-39.4	-38.9
o/w moratorium interest	0.0	0.0	...	-0.7	-1.7	-4.4	-7.1	-7.1	-7.1	-7.1	-7.1	-7.1	-7.1
Other net income	-32.6	-26.2	-16.0	-24.3	-10.9	-28.6	-12.7	-9.4	-7.6	-6.3	-6.3	-6.3	-5.4
Transfers (net)	76.0	19.1	33.9	33.5	52.2	45.4	46.9	52.3	41.6	33.1	35.6	34.6	30.6
Official	61.7	34.2	56.9	...	59.1	58.2	58.8	59.6	43.5	32.6	32.6	30.6	25.6
Private	14.4	-15.1	-23.0	...	-6.9	-12.9	-11.9	-7.3	-3.9	0.5	3.0	4.0	5.0
Capital account balance	64.3	-9.5	22.4	37.4	82.5	54.3	28.0	23.9	49.2	90.8	107.3	125.8	161.0
Commercial banks	-1.9	-12.5	-5.0	-8.4	-6.4	-9.4	-11.7	-10.0	-8.0	-8.0	-8.0	-8.0	-8.0
Medium- and long-term loans, net	40.6	-23.5	-7.5	4.1	15.3	12.5	-1.0	-26.0	-11.8	23.8	29.2	33.1	51.5
Disbursement -Projects	131.3	73.6	95.0	95.0	89.0	82.0	79.4	82.0	75.3	86.3	91.9	105.2	113.3
Amortization (scheduled)	-90.7	-97.1	-102.5	-90.9	-73.7	-69.5	-80.4	-108.0	-87.1	-62.5	-62.7	-72.1	-61.8
Foreign direct investment	-6.9	-1.1	33.8	25.0	14.3	30.7	30.7	48.9	58.0	63.0	73.1	86.7	103.5
Other assets (including accounts payable and receivable)	32.5	27.6	1.1	16.7	59.4	20.5	10.0	11.0	11.0	12.0	13.0	14.0	14.0
Errors and omissions and short term capital	10.3	19.0	0.0	0.0	-18.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	-16.2	-41.6	-80.8	-25.3	17.7	-21.9	-65.2	-67.8	-48.2	-12.3	-22.7	-21.3	10.3
Financing	16.2	41.6	36.3	25.3	-17.6	21.8	65.2	-25.6	-48.0	-53.0	-28.0	-31.0	-49.4
Net international reserves	-13.9	-18.4	3.8	-24.8	-56.9	-23.8	-26.5	-25.6	-48.0	-53.0	-28.0	-31.0	-49.4
Gross official reserves (-: increase)	-21.2	-16.3	-2.9	-38.5	-49.0	-36.0	-23.0	2.2	-23.2	-31.6	-8.5	-12.0	-28.4
IMF (net)	7.3	-2.1	6.7	6.7	-8.0	12.2	-3.5	-27.8	-24.8	-21.4	-19.5	-19.0	-21.0
Purchases and disbursements	18.7	14.9	29.4	29.4	14.8	40.8	25.4	0.0	0.0	0.0	0.0	0.0	0.0
Repurchases and repayments	-11.4	-17.0	-22.7	-22.7	-22.8	-28.7	-28.9	-27.8	-24.8	-21.4	-19.5	-19.0	-21.0
Release of pledged reserves 2/	0.0	0.0	...	25.0	13.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Exceptional Financing (including arrears)	30.1	19.1	32.5	17.6	18.6	40.6	51.2	0.0	0.0	0.0	0.0	0.0	0.0
Accumulation of Arrears (net)	0.8	-14.7	0.0	-2.2	3.0	-3.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Debt rescheduling	0.0	33.8	0.0	19.8	15.6	44.5	51.2	0.0	0.0	0.0	0.0	0.0	0.0
on arrears	0.0	0.0	...	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
on principal	0.0	16.2	...	6.1	4.4	28.5	31.8	0.0	0.0	0.0	0.0	0.0	0.0
on interest	0.0	17.6	...	12.9	10.4	13.4	14.4	0.0	0.0	0.0	0.0	0.0	0.0
on moratorium interest	0.0	0.0	...	0.8	0.8	2.6	5.0	0.0	0.0	0.0	0.0	0.0	0.0
BOP support loans (ADB) 3/	0.0	33.4	17.5	7.5	7.5	0.0	25.0	0.0	0.0	0.0	0.0	0.0	0.0
BOP support loans (WB) 3/	0.0	7.5	15.0	0.0	0.0	5.0	15.5	0.0	0.0	0.0	0.0	0.0	0.0
Financing gap (-)	0.0	0.0	-44.5	0.0	0.0	0.0	0.0	-93.4	-96.2	-65.3	-50.7	-52.3	-39.1
Memorandum items:													
GDP (in millions of U.S. dollars)	1368.0	1526.5	1636.5	1663.0	1597.8	1758.3	1923.6	2104.4	2302.3	2518.7	2755.4	3140.6	3443.1
Current account balance (in percent of GDP)	-6.6	-3.3	-6.3	-3.8	-2.9	-4.3	-4.8	-4.4	-4.2	-4.1	-4.7	-4.7	-4.4
Growth of exports of goods and services (volume)	7.7	-1.4	2.6	4.7	2.2	10.4	1.3	4.3	4.9	5.9	1.3	2.7	5.5
Growth of imports of goods and services (volume)	-14.8	-13.6	3.5	9.4	11.7	9.1	4.9	3.1	4.5	5.0	4.0	3.7	4.6
External Public Debt (US\$ million)	1778.8	1629.4	1879.8	1780.4	1723.2	1774.4	1711.7	1727.3	1769.2	1808.8	1849.6	1893.3	1945.2
as percent of GDP	130.0	106.7	115.0	107.1	104.5	97.8	86.2	79.5	74.4	69.3	64.6	60.3	56.5
External Public Debt (NPV Terms)	1119.2	1180.7	...	...	1191.4	1214.4	1115.9	1111.2	1129.6	1149.1	1169.0	1187.1	1208.9
as percent of GDP	81.8	77.3	...	...	72.2	66.9	56.2	51.2	47.5	44.0	40.8	37.8	35.1
External Public Debt/Exports (NPV Terms)	197.7	213.3	...	...	207.0	199.8	171.7	159.7	154.0	146.1	140.4	135.7	131.5
Debt service-to-exports ratio	21.7	21.3	...	...	18.4	13.0	14.0	25.0	19.8	14.8	14.0	14.3	12.4
Gross reserves 5/	205.5	221.8	213.3	257.3	270.8	306.7	329.7	327.5	350.8	382.4	390.9	402.9	431.3
In months of subsequent year's imports	4.4	4.1	3.7	4.6	4.5	4.7	4.8	4.5	4.5	4.6	4.5	4.3	4.3
Financing gap as percentage of GDP	0.0	0.0	-2.7	0.0	0.0	0.0	0.0	-4.4	-4.2	-2.6	-1.8	-1.7	-1.1

Sources: Kyrgyz authorities and Fund staff estimates and projections.

1/ Including transfers.

2/ Paris Club Savings

3/ BOP support loans for 1998-2000 are shown as part of disbursements under capital account.

5/ Valued at end-year exchange rates. Gross reserves exclude NBKR pledges to secure government-guaranteed loans and blocked deposits.

Table 13. Kyrgyz Republic: Indicators of Fund Credit, 2000-2006

(In percent, unless otherwise indicated)

	2000	2001	2002	2003	2004	2005	2006
Outstanding Fund credit (end-of-period)							
In millions of SDRs	144.3	143.3	136.4	145.6	143.0	122.1	103.5
In millions of U.S. dollars	188.0	181.1	176.4	192.7	189.8	162.6	137.9
In percent of quota	162.5	161.3	153.6	164.0	161.0	137.5	116.5
In percent of GDP	13.7	11.9	10.7	10.6	9.6	7.5	5.8
In percent of total exports	32.8	32.3	29.7	28.8	27.6	22.2	17.6
In percent of external public debt (including Kumtor)	10.6	11.1	10.2	10.9	11.1	9.4	7.8
In percent of external public debt (excluding Kumtor)	12.4	12.6	11.0	11.3	11.3	9.5	7.8
In percent of gross reserves at the beginning of the period	102.0	88.1	79.5	71.2	61.9	49.3	42.1
Debt service due to the Fund							
In millions of SDRs	10.2	13.2	19.1	22.4	22.3	21.3	18.9
In millions of U.S. dollars	13.4	16.7	24.6	29.6	29.6	28.3	25.2
<i>Of which:</i>							
Repurchases and repayments	11.3	16.1	24.0	28.7	28.9	27.8	24.8
Charges/interests	2.0	0.5	0.7	0.9	0.7	0.5	0.4
In percent of quota 1/	11.5	14.9	21.5	25.2	25.1	24.0	21.3
In percent of GDP	1.0	1.1	1.5	1.6	1.5	1.3	1.1
In percent of total exports	2.3	3.0	4.2	4.4	4.3	3.9	3.2
In percent of total debt service (including Kumtor)	8.7	10.9	19.8	22.5	20.1	15.5	16.3
In percent of debt service (excluding Kumtor)	15.7	18.0	29.5	28.1	25.9	17.2	18.2
In percent of gross reserves at the beginning of the period	7.2	8.1	11.1	10.9	9.6	8.6	7.7

Sources: IMF, Treasurer's Department; and Fund staff calculations.

Table 14. Kyrgyz Republic: Prospective Use of Fund Resources, 2001-2006

	<u>Outstanding</u> End-Dec. 2001	2002	2003	2004	2005	2006
SBA transactions	0.00					
Purchases		0.00	0.00	0.00	0.00	0.00
Repurchases		0.00	0.00	0.00	0.00	0.00
STF transactions	9.41					
Purchases		0.00	0.00	0.00	0.00	0.00
Repurchases		5.38	4.03	0.00	0.00	0.00
PRGF transactions	133.85					
Disbursements		11.72	30.84	19.10	0.00	0.00
Repayments		13.18	17.63	21.74	20.87	18.61
Total Fund credit outstanding	143.26	136.42	145.60	142.96	122.09	103.47
		(In percent of quota)				
Total Fund credit outstanding 1/		153.63	163.97	160.99	137.49	116.52
Disbursements under PRGF		13.20	34.73	21.51	0.00	0.00

Sources: IMF, Treasurer's Department; and Fund staff calculations.

1/ Relative to the quota of SDR 88.8 million.

Table 15. Kyrgyz Republic: Reviews and Disbursements
Under the Three-Year PRGF Arrangement

Date	Action	Disbursement
December 6, 2001	Approved three year Arrangement.	SDR 11.72 million
July 1, 2002	First review based on end-March 2002 performance criteria, completed.	SDR 11.72 million
February, 2003	Complete second review based on end-September 2002 performance criteria and establish conditions and disbursements for the second year of the arrangement.	SDR 11.72 million
On or after May 15, 2003	Complete third review based on end-March 2003 performance criteria.	SDR 9.56 million
June 2003	Indicative targets.	
On or after November 15, 2003	Complete fourth review based on end-September 2003 performance criteria and adopt conditions and disbursements for the third year of the arrangement.	SDR 9.56 million
On or after May 15, 2004	Complete fifth review based on end-March 2004 performance criteria.	SDR 9.55 million
June 2004	Indicative targets	
On or after November 15, 2004	Complete sixth review based on end-September 2004 performance criteria.	SDR 9.55 million

KYRGYZ REPUBLIC—FUND RELATIONS
(As of December 31, 2002)

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

II. General Resources Account	SDR Million	Percent of Quota
Quota	88.80	100.0
Fund Holdings of Currency	92.83	104.54
Reserve position in Fund	0.00	0.01

III. SDR Department	SDR Million	Percent of Allocation
Holdings	0.47	N/A

IV. Outstanding Purchases and Loans	SDR Million	Percent of Quota
Systemic Transformation	4.03	4.54
ESAF/PRGF arrangements	132.22	148.90

V. Latest Financial Arrangements

Type	Approval Date	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
PRGF	12/06/2001	12/05/2004	73.40	23.44
ESAF/PRGF	06/26/1998	07/25/2001	73.38	44.69
ESAF	07/20/1994	03/31/1998	88.15	88.15

VI. Projected Payments to Fund

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

	Forthcoming				
	2003	2004	2005	2006	2007
Principal	21.70	21.70	20.90	18.60	16.10
Charges/Interest	0.70	0.50	0.40	0.30	0.20
Total	22.40	22.20	21.30	18.90	16.30

VII. Implementation of HIPC Initiative. Not applicable.

VIII. Safeguards Assessments

Under the Fund's safeguards assessment policy, National Bank of the Kyrgyz Republic (NBKR) is subject to an assessment with respect to the PRGF arrangement, which was approved on December 06, 2001 and is scheduled to expire on December 05, 2004. A safeguards assessment of the NBKR was completed on January 18, 2002. The assessment concluded that high risks may exist in the financial reporting framework and in the system of internal controls. Staff findings, proposed recommendations under program conditionality and other recommendations are reported in Appendix VII. Implementation of the measures by the NBKR needs to be monitored by staff.

IX. Exchange Rate Arrangements

The currency of the Kyrgyz Republic has been the som (100 tyiyn =1 som) since May 15, 1993. The National Bank of Kyrgyz Republic publishes daily the exchange rate of the som in terms of the U.S. dollar, which is determined in the interbank foreign exchange market.

X. Article IV Consultations

The Kyrgyz Republic is on the 24-month consultation cycle. The last Article IV consultation discussions were held in September 2001 and the Article IV consultation was completed by the Executive Board on November 30, 2001.

XI. FSAP Participation and ROSC Assessment

The FSAP missions were held in May and September 2002, and the discussions were concluded during the 2002 Article IV consultation. A ROSC Fiscal Transparency mission was held in March 2001 and the ROSC Fiscal Transparency Module has been submitted to the Board concurrently with 2001 Article IV consultation report. A ROSC Data mission was held in November 2002.

XII. Resident Representative

The fifth resident representative of the Fund in the Kyrgyz Republic, Mr. Bhaswar Mukhopadhyay, has held his post in Bishkek since March 17, 2001.

Kyrgyz Republic—Relations with the World Bank Group
(As of January 8, 2003)

1. On December 6, 2001, the World Bank Boards of Directors endorsed a Country Assistance Strategy (CAS) Progress Report for World Bank Group based on the Government's Interim National Poverty Reduction Strategy Paper and Comprehensive Development Framework, which suggest that fiscal year 2002 will be a year of consolidation and stocktaking. The next CAS, covering the fiscal years 2003-05, is expected to be finalized during Spring 2003. It will be the fourth full CAS and the first to be based on the full Poverty Reduction Strategy Paper, which the authorities finalized in December 9, 2002.
2. International Development Association (IDA). Between 1994 and 2002, IDA has approved 24 projects totaling approximately \$614 million (after cancellations), of which about \$442.5 million has been disbursed. Six structural adjustment credits have already been completed, which provided quick disbursing support for the Government's economic reform programs in privatization, enterprise restructuring, agricultural policy, financial sector, public sector resource management and pension reform. Four investment operations have also been completed supporting reform and rehabilitation of the telecommunication sector, social safety nets, health, and rural finance.
3. The active portfolio includes 14 operations:
 - A balance of payments support operation (Consolidation Structural Adjustment Credit) assisting with reforms in the power and gas sector, and improvements to the business environment (reducing the cost on business from licensing and inspections). The first tranche of the CSAC was disbursed at the end of 2000, and the second at the end of 2001. One additional tranche remains to be disbursed before the closing date of June 2003.
 - Two operations supporting energy sector rehabilitation and reform (Power and District Heating and a Technical Assistance Credit supported the CSAC program)
 - Seven operations supporting provision of key public goods and reform in agriculture (irrigation rehabilitation, flood emergency, on-farm irrigation, rural finance, agricultural support services, sheep and wool development, and land registration—the latter also provides the basis for the introduction of a tax of non-movable property in rural and urban areas)
 - An operation supporting capacity building in the financial sector and a line of credit for private enterprises.
 - A second health sector operation continuing support for sectoral restructuring and reform program

- A rural water supply and sanitation operation (approved together with the CAS Progress Report)
- A urban transport operation

4. The World Bank Group's operational objectives for the next 12 months are to support completion of a full Poverty Reduction Strategy through focused analytical work and technical assistance, the enhancement of portfolio performance, and the ongoing structural reforms in energy, business environment, public expenditure management, health and water and sanitation and agriculture. In this endeavor, the IDA is planning to support the authorities efforts in strengthening the governance framework through a Governance Structural Adjustment Credit (GSAC) and accompanying Governance Technical Adjustment Credit (GTAC)—both are at an advanced stage of preparation. The Bank has also undertaken a Public Expenditure Review, a Pension Note Update, and a Poverty Assessment—the former two studies are at the discussion stage with the authorities and the last one is near finalization. As noted earlier, a full CAS, covering the fiscal years 2003–2005, is expected to be finalized in Spring 2003.

5. IFC has focused on institution building, technical assistance, and strategic investments. Building upon IFC's initial investment in the financial sector, the Demir Kyrgyz International Bank, IFC played an instrumental role in the establishment of the largest bank in the country the Kyrgyz Investment and Credit Bank, with a \$1.4 million equity investment. IFC developed a strategic partnership with FINCA by investing \$1.0 million in a fund to support microenterprises. This investment was accompanied by technical assistance to FINCA to facilitate its transformation and to the government in developing the appropriate regulatory framework. IFC has also provided technical assistance to review and develop the legal and regulatory framework for leasing. Under the Extending IFC's Reach Initiative, IFC has undertaken promotional and business development activities with small and medium-sized enterprises and approved three investments of \$470,000, \$300,000 and \$1.4 million for agribusiness, packaging and pasta production projects respectively. IFC is playing a catalytic role in the development of SEAF-CAESIF, a regional equity fund that will provide equity, quasi-equity and debt financing as well as technical and managerial assistance to growth-oriented SMEs.

6. The primary focus of IFC activities in the period leading up to the next CAS will be to improve the business environment, provide support for SMEs and closely coordinating with the World Bank to create a framework that will facilitate foreign investment in mining, utilities and infrastructure. With financial support from the Swiss Government, IFC draws upon the resources of the Private Enterprise Partnership to advise on improving the business environment, provide training and support services for SMEs, continue past IFC efforts to develop leasing activities, and support agri-business for local and export markets. Technical assistance with a focus on project development is currently being undertaken in the tourism sector. IFC will work with IDA on a possible agricultural marketing and processing project, which could provide the basis and framework for collaboration in agricultural leasing. IFC will investigate opportunities for development of the IT sector. IFC will cooperate with IDA

and the government in developing a legal and regulatory framework that will facilitate new foreign investment in mining in future years.

7. MIGA has supported the development of private sector in Kyrgyz Republic by extending guarantees to foreign direct investments in four projects in the manufacturing, services, and mining sectors. As of June 30, 2000, the total amount of foreign direct investment facilitated, as a result of MIGA guarantees, is over \$360 million. MIGA has also provided capacity building in foreign investment techniques to the State Committee on Foreign Investments and Economic Development, in an initiative supported by the Swiss government. MIGA plans to continue to assist the development of Kyrgyz Republic through its guarantee program and capacity building. Data on the Kyrgyz Republic is also featured in MIGA's Privatization Link service, which connects potential investors to information on companies slated for divestiture via the Internet.

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KYRGYZ REPUBLIC—RELATIONS WITH THE ASIAN DEVELOPMENT BANK (ASDB)
(As of October 31, 2002)

AsDB operations in the Kyrgyz Republic commenced in 1994. To date, AsDB has approved 21 loans, all on concessional terms, totaling \$542.2 million, of which about \$331 had been disbursed by October 31, 2002. Lending for fast disbursing, policy based project has accounted for about a third of total lending. Besides loan operations, AsDB has extended technical assistance (TA) grants totaling about \$29.2 million since 1994. The TA operations follow the sharp sectoral focus of the Country Operational Strategy (COS) and complement the AsDB's loan operations. A high proportion of the TA assistance is for supporting the government's efforts for institution strengthening and capacity building, with a view to supporting sustainable economic development.

The current COS was endorsed by the Board of the Asian Development Bank in November 1996. The strategy confirmed the principal objectives of the Interim Operational Strategy that had guided AsDB's operations in the Kyrgyz Republic since 1994. These objectives are: (i) support for the government's reform through encouraging institutional changes and strengthening institutional capacity, and improving the provision of public services; (ii) encouraging private sector development; and (iii) improving long-term growth potential through investment in both physical infrastructure and human development and preserving the environment. In achieving these objectives, the COS has deliberately adopted a sharp focus on a small number of strategic areas, including (i) improvement in the provision of public services, particularly social services provided by local governments and the management of reform by the central government; (ii) agriculture, including rural finance; (iii) human development, especially education; and (iv) infrastructure rehabilitation. In 1999, in response to the negative effects of the Russian crisis, the AsDB's reach was broadened to include assistance to the financial sector. This selective approach has enabled the AsDB to maintain a strong sector presence and a well-focused policy dialogue. The current COS needs to be revised to reflect ASDB's and the Government's latest priorities. A new country strategy and program (CSP) will be completed in 2003 in close consultation with the Government and other stakeholders.

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

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

**KYRGYZ REPUBLIC—RELATIONS WITH THE EUROPEAN BANK FOR
RECONSTRUCTION AND DEVELOPMENT (EBRD)**
(As of July 31, 2002)

In 2002, the key strategic priorities of the EBRD in Kyrgyzstan include: the development of a dynamic micro, small and medium enterprise sector; the strengthening of the financial sector; the support to the privatization program and assistance with attracting foreign direct investment.

1. Between 1994 and 31 July 2002, the EBRD signed 17 investment projects in Kyrgyzstan with a total commitment of €174 million. Disbursements account for 84 per cent of these commitments. The private sector accounts for 52 percent of the commitments with 91 percent provided as debt and 9 percent—as equity. The public sector accounts for 48 percent of the commitments, all in the form of debt.
2. Thirteen projects are in the private sector, which include two credit lines for micro, small and medium enterprises and a regional trade facilitation program. Five of the private sector investments have been made under the Direct Investment Facility program, established in 1998. The objective of this program is to demonstrate the viability of equity investment with local entrepreneurs in difficult markets by providing equity and limited debt financing to private sector businesses.
3. Four projects are in the public sector, with one project aimed at the modernization of the telecommunications network, two projects focusing on upgrading components of the electricity transmission network, and one project in the agribusiness sector. The total commitment of these projects is €82.4 million (or 43 percent of the total).
4. In terms of sectoral allocation, 22 per cent of commitments are in natural resources, 36 per cent in power and energy, 21 per cent in the financial sector and 20 per cent in general and specialized industries.
5. These projects have been supported by the EBRD's technical cooperation program, which is targeted at the financial sector, natural resource management, agribusiness, and critical infrastructure bottlenecks (such as the modernization of telecommunications, and electricity transmission and distribution).
6. The EBRD objective is to avoid putting pressure on Kyrgyzstan's foreign debt burden. Therefore, the EBRD sets special requirements in terms of their expected impact on the country's systemic transition for any investments involving sovereign obligations.

KYRGYZ REPUBLIC: TECHNICAL ASSISTANCE PROVIDED BY THE FUND, 1997–2002
(As of November 19, 2002)

<i>Dept.</i>	<i>Subject/Identified Need</i>	<i>Timing</i>	<i>Counterpart</i>
FAD	Review status of revenue administration; evaluate need for further technical assistance	June 1997	Ministry of Finance
	Review status of revenue administration; evaluation need for further technical assistance	January 1998	Ministry of Finance
	Tax policy and administration	April 1998–May 1999 (long-term peripatetic advisor)	Ministry of Finance
	Tax Policy and Administration	March 1999	Ministry of Finance
	Expenditure control and Fiscal Transparency	May 1999	Ministry of Finance
	Customs Administration	September 1999	Ministry of Finance
	ROSC Fiscal Transparency Module	March 2–13, 2001	Ministry of Finance
	Tax Policy and Administration	January 28-February 9, 2002	Ministry of Finance
	Treasury Reform and Expenditure Management	February 11-27, 2002	Ministry of Finance
MAE	Foreign exchange operations, monetary operations, government securities market and central bank organization	September 1997	National Bank of the Kyrgyz Republic
	Foreign Exchange Management	June–July 1998	National Bank of the Kyrgyz Republic
	Central bank operations and liquidity management	October 1998	National Bank of the Kyrgyz Republic
	Banking Supervision	March–April 1999	National Bank of the Kyrgyz Republic
	Central Bank operation and liquidity management	December 2–15, 1999	National Bank of the Kyrgyz Republic

KYRGYZ REPUBLIC: TECHNICAL ASSISTANCE PROVIDED BY THE FUND, 1997-2002
(As of November 19, 2002)

<i>Dept.</i>	<i>Subject/Identified Need</i>	<i>Timing</i>	<i>Counterpart</i>
	Banking System Stabilization and Research	January 21-February 3, 2000	National Bank of the Kyrgyz Republic
	Banking and Payment Systems Reform	November 10-23, 2000	National Bank of the Kyrgyz Republic
	Bank Restructuring (short-term expert)	April 9-May 16, 2001	National Bank of the Kyrgyz Republic
	Financial Institutions (short-term expert)	April 23-May 7, 2001	National Bank of the Kyrgyz Republic
	Banking Sector Reform, Central Bank Law, Monetary Operations	July 23-August 4, 2001	National Bank of the Kyrgyz Republic
	Payment Systems	September 21-October 3, 2001	National Bank of the Kyrgyz Republic
	Payment Systems	March 21-April 8, 2002	National Bank of the Kyrgyz Republic
	Regularization of Financial Relations between the NBKR and the Ministry of Finance	April 23-May 3, 2002 & October 31-November 8, 2002	National Bank of the Kyrgyz Republic
	Financial Sector Assessment Program (in cooperation with the World Bank)	May 15-18, 2002 & August 26-September 9, 2002 & October 29-November 6, 2002	National Bank of the Kyrgyz Republic
STA	Balance of Payments Statistics	July 1997	National Statistical Committee
	Review of monetary statistics and finalization of IFS page	February 1998	National Bank of the Kyrgyz Republic
	Review of trade statistics procedures	March 1998	National Statistical Committee
	Money and Banking Statistics	March 1999	National Bank of the Kyrgyz Republic
	Balance of Payments Statistics	October-November, 1999	National Bank of the Kyrgyz Republic

KYRGYZ REPUBLIC: TECHNICAL ASSISTANCE PROVIDED BY THE FUND, 1997-2002
(As of November 19, 2002)

<i>Dept.</i>	<i>Subject/Identified Need</i>	<i>Timing</i>	<i>Counterpart</i>
	Price Statistics	March 1-15, 2000	National Statistical Committee
	National Accounts Statistics	March 2-15, 2000	National Statistical Committee
	GDDS Metadata Preparation	Dec. 14-22, 2000	National Statistical Committee
	ROSC Data Assessment	Nov. 5-21, 2002	National Statistical Committee

List of Resident Advisors

FAD	Establishment of Treasury	Mr. Chaturvedi	Oct. 1994-Aug. 1996
FAD	Tax Administration	Mr. Walker	Oct. 1994-Dec. 1996
FAD	Tax Policy Advisor	Mrs. Guevara	Jun.-Dec. 1999
FAD	Customs Administration Advisor	Mr. Sawyer	Mar.-Jun. 2000 and From Aug.-Nov. 2000
MAE	General Policy	Mr. Aurikko	Sep. 1995-Aug. 1996
MAE	Accounting	Mr. Listman	Oct. 1995-Jun. 1996
MAE	Accounting	Mr. Seng	May 1996-Dec. 1997
MAE	Banking Supervision Advisor	Mr. Franson	Sep. 1999-Feb. 2001
MAE	Banking Supervision/Restructuring Advisor	Mr. Svartsman	Nov. 2001-Jan. 2004
MAE	Public Debt Policy and Management	Mr. Azarbajevani	Dec. 2002-Dec. 2004
PDR	External Debt Advisor	Mr. Azarbajevani	Feb. 2000-May 2001
STA	Balance of Payments	Mr. Hafiz	Jun. 1996-May 1997
STA	Multitopic General Advisor	Mr. Khawaja	Apr. 1996-Apr. 1999

KYRGYZ REPUBLIC—STATISTICAL ISSUES

General framework

1. The NSC maintains a comprehensive and regularly updated data web site largely incorporating Fund dissemination standards metadata structure and format, with good coverage and timeliness (<http://stat-gvc.bishkek.su>). The Kyrgyz Republic is presently participating in the Fund's General Data Dissemination System (GDDS); its dissemination practices more than fully meet the GDDS recommendations, and meet most of the SDDS requirements.

2. A data ROSC mission, which took place in November 2002, carried out a review of the Kyrgyz Republic's data dissemination practices against the GDDS, as well as an in-depth assessment of the quality of national accounts, CPI, PPI, government finance, monetary, and balance of payments statistics.

National accounts

2. In general, data dissemination of national accounts statistics is prompt. Technical assistance has been received from the IMF, EUROSTAT, OECD, World Bank, and bilateral donors. While significant progress has been made in improving the national accounts estimation process, problems persist with respect to the quality of the source data due mainly to excessively tight collection deadlines and efforts are needed to improve the quality of the source data for GDP quarterly estimates. Difficulties also remain in properly estimating the degree of underreporting, especially in the private sector. To improve the coverage and reliability of primary data, work has been undertaken to introduce scientific sampling procedures. Improved sampling procedures have been adopted for household surveys and new report forms are being introduced for the survey of enterprises. The NSC has established a division of sample surveys, which would assist in improving the sampling techniques. However, subannual national accounts statistics are still collected on a cumulative basis rather than by discrete time periods.

Prices, wages, and employment

3. The scope of the new CPI, which has been published since January 1995, is broadly consistent with international standards. The price index covers all urban resident households of all sizes and income levels, although rural households, which comprise the majority of the population, are not covered. A recent ROSC mission recommended that the authorities expand the coverage of the CPI to include rural households.

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

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

5. Problems exist in the compilation of the average wage, especially with respect to the valuation of payments in kind and the coverage of the private sector. Also, the monthly statistics are not comparable with the annual data due to different coverage and classifications.

6. Employment data have similar inconsistencies between annual and monthly data. The coverage of unemployment includes an estimate of unregistered unemployed.

Fiscal accounts

7. The scope of government statistics falls short of international standards in that they exclude data for the Social Fund and the externally financed Public Investment Program, although these data are published separately. Other limitations are that financial transactions exclude transactions with domestic banks and there are discrepancies between the deficit and the financing data. The authorities do not provide any details on the financing data. While revenue and expenditure data are generally set up according to GFS standards, both categories have some items misclassified. There are nontax revenues classified as taxes and specific expenditure items are misclassified in the budget and treasury accounts. .

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

Monetary sector

9. The authorities introduced new charts of accounts for the NBKR and the commercial banks during 1997, with the assistance of a resident MAE advisor and the USAID. A money and banking statistics mission in March 1999 reviewed the compilation of the monetary data and found that the classification of accounts is generally in accordance with the Fund's methodology. However, the information provided by the NBKR's chart of accounts is not sufficiently detailed to support the sectoral breakdown of the monetary statistics compiled and there is a need to improve not only the chart of accounts but also the accompanying instructions. The main findings of the November 2002 ROSC mission were that: (1) the residency criterion is not uniformly applied as the currency denomination is used to classify some transactions with foreign and domestic units, (2) deposits with banks in liquidation are

included in broad money, (3) source data do not provide sufficient information for a more detailed sectoral breakdown (e.g., subsectorization of nonbanks institutions as recommended in the *Monetary and Financial Statistics Manual*), and (4) there are discrepancies among monetary, fiscal and BOP data; consistency checks are not conducted by the monetary statistics and BOP compilers for commercial banks data on foreign assets and liabilities. Monetary data for *IFS* publication have been reported on a regular monthly basis with a lag of about one month. Since December 2002, monetary data are reported electronically to STA.

External sector

10. The compilation of balance of payments statistics has improved with the assistance of a technical assistance mission on balance of payments statistics that visited the NBKR during 1999. A data ROSC mission in November 2002 noted that the compilation of balance of payments statistics in Kyrgyz Republic broadly follows the guidelines of the *Balance of Payments Manual, Fifth Edition (BPM5)*. The NBKR has good arrangements with other agencies to ensure timely flow of data. However, individual records from several sources (particularly the ITRS data and Customs declarations) are not available to the NBKR, which limits its ability to cross-check the accuracy of data. Although the data collection program has been expanded in the recent past, coverage deficiencies remain with respect to trade, services, and foreign direct investment. The NBKR surveys of enterprises lack an up-to-date register and have inadequate coverage of enterprises, particularly those in free economic zones. There is also a need for improving compilation procedures for achieving temporal consistency of data, and investigating and reconciling discrepancies.

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

SAFEGUARDS ASSESSMENT—SUMMARY OF CONCLUSIONS

Safeguards Assessment

An on-site assessment of the NBKR was conducted during August 2001. The assessment received full cooperation from the NBKR, and its management agreed to all the measures proposed by the staff.

Vulnerabilities

The vulnerabilities identified included:

(i) a significant portion of the NBKR's assets was in the form of non-interest bearing government securities with infinite maturity, the actual fair value of these assets being significantly lower than their normal value, therefore, overstating the capital base of the bank, and

(ii) the central bank law does not preclude distribution of net unrealized gains on foreign exchange or securities.

Remedies Under Program Conditionality

The NBKR and the MoF have finalized an agreement to regularize their financial relations. As part of the agreement, the noninterest-bearing securities with infinite maturity held by the NBKR have been converted into short- and medium-term securities that bear a market rate of interest, while the NBKR will pay interest on government deposits. The agreement becomes effective by end-2002.

The NBKR has considered, as recommended in the Safeguard Assessment, modifying the national bank law to specifically state that net unrealized gains on market price fluctuations for domestic and foreign securities, as well as on foreign exchange rate revaluations, will not be distributed to the government. It is, however, not necessary to open parliamentary discussions on amendments to the national bank law, as the arrangement can be confirmed through a formal agreement between the NBKR and the MoF. According to an agreement to signed in June 2002, the NBKR continues to make distributions from realized profits only.

Bishkek, Kyrgyz Republic
January 31, 2003

Mr. Horst Köhler
Managing Director
International Monetary Fund
Washington, D.C. 20431

Dear Mr. Köhler:

The Kyrgyz authorities held discussions with Fund staff in October/November 2002 for the second review under the PRGF arrangement. Based on these discussions, the attached Second-year Memorandum of Economic Policies (SMEP) reviews economic developments and policy implementation through September 2002, updates the macroeconomic framework, and discusses the financial policies and structural reform program for the second-year program (October 1, 2002–September 30, 2003). It supplements the MEP dated November 16, 2002, as well as the supplementary MEP dated June 13, 2002. It also proposes quantitative performance criteria, as well as structural performance criteria and benchmarks, for end-March 2003.

All performance criteria for end-September 2002 were met, except for the continuous performance criterion on the non-accumulation of external payments arrears. The arrear was cleared in early January 2003, and we request a waiver for the non-observance of this performance criterion.

On the basis of the performance up to September 2002 and the policies set out in the attached memorandum, the government also requests the completion of the second review. We expect the third, fourth, fifth, and sixth reviews under the arrangement to be completed after the test dates of end-March 2003, end-September 2003, end-March 2004, and end-September 2004, respectively.

International experts have completed quarterly audits of the reserves of the National Bank of the Kyrgyz Republic (NBKR) following the IMF Board meeting on February 9, 2000, when Executive Directors discussed remedial actions in connection with an earlier misreporting of reserves. The auditors have since confirmed the correctness of the data that has been transmitted to the Fund. We therefore intend to move from a quarterly to annual audits of reserves to reduce the operational costs of the NBKR.

We prepared a National Poverty Reduction Strategy (NPRS), which sets forth the main elements of our approach to poverty reduction and macroeconomic policies and structural reforms supporting it. The NPRS was submitted to the Fund on December 9, 2002.

We believe that the policies and measures set forth in the memorandum are adequate to achieve the objectives of our program. At the same time, we stand ready to take any additional measures that may become necessary for this purpose in consultation with the Fund staff. The government will provide the Fund with such information as the Fund requests in connection with the Kyrgyz Republic's policies and developments under the program.

Yours sincerely,

/s/
Nikolai Tanaev
Prime Minister
Kyrgyz Republic

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

KYRGYZ REPUBLIC

SECOND-YEAR MEMORANDUM OF ECONOMIC POLICIES For the period October 1, 2002-September 30, 2003

I. INTRODUCTION

1. This Second-year Memorandum of Economic Policies (SMEP) supplements our Memorandum of Economic Policies dated November 16, 2001, and the Supplementary Memorandum of Economic Policies dated June 13, 2002. These documents describe the economic policies supported by the International Monetary Fund (IMF) under a three-year Poverty Reduction and Growth Facility arrangement (PRGF). The SMEP reviews our policy performance during the first-year program (October 1, 2001-September 30, 2002) and describes the policies for the period October 1, 2002-September 30, 2003. These policies are consistent with the National Poverty Reduction Strategy (NPRS) we submitted on December 9, 2002 for the IMF and World Bank endorsement.

II. PERFORMANCE UNDER THE PROGRAM

2. Because of a landslide in the Kumtor gold mine, lower energy exports, and a delayed harvest, real GDP declined by 2.6 percent in the first nine months of 2002. Excluding gold production, however, growth was positive (1.1 percent). Stabilization continued with the 12-month inflation falling from 5.3 percent at the beginning of the first-year program to 3.5 percent in September 2002. The nominal exchange rate appreciated by 3.6 percent during this period and nominal and real interest rates declined. Confidence in economic policies improved as indicated by narrower interest rate differentials between domestic and foreign government securities.

3. We also made progress in poverty reduction. A study conducted with the World Bank staff confirms that, since 1998, poverty has decreased by almost 20 percent. Income differentials narrowed and poverty declined in all regions—more in rural than in urban areas. Unfortunately, the poorest region—the mountainous area of Naryn—benefited only a little. Nevertheless, poverty reduction remains our first priority as 47 percent of the population were still poor at end-2001.

4. Despite the drop of fiscal revenue from Kumtor, we have achieved all end-September 2002 quantitative targets under the program (Table 1). The net international reserves (NIR) target was met with a wide margin as confidence in domestic currency improved and currency substitution decreased. Net domestic assets (NDA) of the central bank (NBKR) remained below the program ceiling by 6.3 percent of reserve money. The targets for fiscal deficit and tax collection were also met and there were no budgetary arrears under the program as the earlier small pension arrears were cleared in September. The two structural performance criteria for end-September 2002 were observed as well. Legislative amendments

to ensure that courts use only the NBKR-confirmed financial accounts as a basis for bank liquidation cases were submitted to parliament on September 30 and a government resolution was issued to reform the Large Taxpayer Unit (LTU) to make it fully responsible for tax collection from large enterprises in 2003.

5. Regarding the banking sector, amendments to the Law on Licensing were sent to parliament. With these amendments, the licensing of financial institution has been made the responsibility of the NBKR alone (a structural benchmark for end-September). We have also drafted a banking sector reform program (a structural benchmark for end-September) based on the IMF/World Bank Financial Sector Assessment Program (FSAP) recommendations. In the fiscal area, a government resolution was issued on the restructuring of the Ministry of Finance (a structural benchmark for end-September). This includes introducing permanent secretary posts for the highest level of civil service in the ministry to ensure quality and continuity in administration. A Financial Planning Division within the Treasury was established and it has produced the first cash revenue and expenditure forecast for the remainder of 2002.

6. Because of a commercial dispute related to the failed Kyrgyz Telekom privatization, we temporarily incurred in a small amount of external arrears. An international arbitration tribunal in Stockholm awarded Raiffeisen, our privatization consultant, fees for \$1.5 million on July 12, 2002. We have now cleared these arrears and request a waiver for non-observance of the relevant continuous performance criteria. We also intend to change the schedule of the audits of the NBKR's net international reserves from quarterly to annual audits.

7. We are grateful to our creditors who in March 2002, at the Paris Club, granted a flow rescheduling of our debt for 2002-2004. Since then, we have met with our creditors to finalize the bilateral agreements. We have obtained reschedulings from France, Germany, Denmark, Japan, Turkey, and Russia. Unfortunately, a rescheduling agreement could not be reached with Union Bank of Switzerland (UBS) on a guaranteed debt which we thus repaid in May 2002. Negotiations are being concluded with South Korea and India, while they are still proceeding with the Kuwait Fund and China. By end-2002, Pakistan and Uzbekistan had not responded to our requests for discussions.

III. PROGRAM FOR THE PERIOD OCTOBER 2002-SEPTEMBER 2003

8. The second-year program sets forward policies to achieve our medium term goals under three constraints: the projected decline in gold production, the high external debt, and the need to reduce poverty. To offset the negative impact of the declining gold production on growth and the balance of payments, other industries should fill the gap. This will call for strong cost competitiveness and structural reforms to improve productivity. At the same time, the poverty reduction objectives should not lead to higher fiscal deficits. Excessive deficits could trigger macroeconomic imbalances through rekindling inflation, depreciating nominal

exchange rate, and increasing external debt. It is essential that we devise and preserve a right balance of policies to avoid slow growth, unsustainable external debt, and persisting high poverty levels. The high dependency on a few export commodities calls for diversification of the economy and we need to direct our policies toward this goal already now.

9. We will focus on strengthening structural policies, especially in governance and banking, to increase economic efficiency. Containing the growth of unit labor costs relative to trade partners will be critical for maintaining the competitive edge of Kyrgyz exports. At the same time, financial policies will need to contain consumer price inflation.

10. In view of our currently weak fiscal position, we will mainly rely on economic growth to reduce poverty and avoid higher fiscal deficits to finance social spending. For targeted poverty reduction programs, we will seek grants instead of loans including under the CIS7 Initiative. To generate resources for social spending, we will follow a three-pronged approach. We will expand the tax base, improve tax administration, and reallocate public resources from nonproductive uses to social spending.

11. Private investment should be the driving force of capital accumulation. The externally financed Public Investment Program (PIP) will be streamlined from 5.1 percent of GDP in 2002 to 3.5 percent by 2005 and reduced to 3 percent thereafter. In 2003-2006 the increase in national savings by 3 percentage points of GDP would reflect further fiscal adjustment and improving enterprise profitability through productivity gains. The use of foreign savings to finance investment would increase by 1.3 percentage points in the same period.

12. For the period October 1, 2002-September 30, 2003, we have revised the macroeconomic framework, introduced new quantitative and structural program targets, and specified further our intentions in fiscal, monetary, external, and structural policies. In the latter area, in particular, we will strengthen governance and move to the next stage of the banking sector reform.

13. The landslide at the Kuntor mine and the reduction in energy production has led to a downward revision of real GDP growth from 4.3 percent to 0.8 percent in 2002. Growth will rebound next year as gold production returns to a higher level in the second half of 2003. Year on year, we project real GDP to grow by 5.2 percent in 2003. Building on the recent gains in price stabilization, we expect the 12-month inflation to remain low—at 3.6 percent—in 2002. For 2003, our inflation target is 4.4 percent, somewhat higher than in 2002 reflecting higher administered prices and indirect taxes. With the sustained stability in the foreign exchange market, these developments would lead to an increase in GDP per capita (in U.S. dollar terms) by 17 percent during 2002-2003. The current account deficit for 2002 is now projected at only 2.8 percent of GDP—smaller than projected earlier (3.8 percent). The reduction in gold exports are more than compensated thanks to higher gold prices, lower PIP related imports, and a sharp increase of service revenues including from the international military base. For 2003, the program target is to contain the external current account deficit to 4.2 percent and increase official gross reserves to \$271 million by end-2002 and further to \$307 million, or 4.7 months of imports by end-2003.

Fiscal policies

14. In 2002, the fiscal (cash) deficit is now projected to increase to 5.6 percent of GDP from 5.0 percent in 2001. This weakening of the fiscal balance reflects the lower-than-expected growth and the related revenue shortfall from the Kumtor gold mine. However, for 2003, when output recovers, the program aims at strong fiscal adjustment. The deficit will be reduced to 4.7 percent of GDP. This will be achieved mainly through an increase in state budget revenue from the projected 13.4 percent of GDP in 2002 to 14.6 percent in 2003. We expect that the recovery of revenue from Kumtor and the extension of VAT to large agricultural producers will account for most of it, while the rest will come from the full-year effect of recent eliminations of various VAT exemptions. We intend to reach the NPRS's target of 15 percent central government tax ratio in 2005. This goal can be achieved only by broadening the tax base significantly in the coming years. Since agriculture accounts for 40 percent of GDP but only 5 percent of tax revenue, it is necessary to extend VAT within agriculture to cover large producers' direct sales to the domestic market in the 2003 budget as of April 1, 2003. With respect to other tax measures, we have already submitted to Parliament for approval a new tax on real property. It will improve the financial position of local governments and promote fiscal decentralization. In addition, we will increase the excise tax on liquor from som 15 to som 18 per liter. Mineral resource taxation will be amended by end-June 2003 (as recommended by the World Bank) to make it comparable with international standards. We will introduce a unified environmental tax by end-2003 in lieu of the existing system of fees. Finally, to reduce smuggling, we have exempted medicines from the VAT as of January 1, 2003.

15. On tax rates, no further adjustments will be introduced during the second-year program. Indeed, following the profit tax rate reduction in the beginning of 2002, profit tax collections excluding KyrgyzEnergo remained constant in January-September compared to the same period in the previous year, only thanks to significant efforts in collection. This suggests extreme caution in tax rate reductions. However, by end-March 2003 we will study the possibility of reducing the high payroll tax rate in the medium term provided that we can compensate the potential revenue loss by other means. By end-March, 2003, we will prepare proposals on the taxation of capital gains for discussion with the Fund staff during the third review of the PRGF supported program. We are finalizing our plan to move to a funded pension scheme in close cooperation with the World Bank staff and discuss the short- and medium term fiscal implications with the IMF staff before proposing any adjustments in payroll tax rates. On trade taxes, we raised the custom tariffs on flour and grain from 0 to 20 percent temporarily until end-December 2002 in part for fiscal reasons and in part in response to Kazakhstan's similar measures earlier in 2002. We will not repeat such protective tax measures next year but instead try to involve our neighbors in a mutually beneficial trade liberalization policy consistent with the WTO best practices. An interministerial task force is studying the possibility of reducing the excise tax on gasoline. The results of the analysis will be discussed at the time of the Fund mission next February.

16. Tax administration also needs to be improved. Implementation of the government resolution on reforming the Large Taxpayer Unit (LTU) is our number one priority in this

area. A detailed action plan has been approved (Annex I) and tax collection by the central LTU from the first 60 large enterprises will start in early 2003. We have requested technical assistance from the IMF to ensure effective implementation of this reform. Regarding Free Economic Zones, no new FEZs or similar tax exemption arrangements will be introduced. Of the total stock of som 106 million of claims on VAT refunding accumulated before 2002, we will clear the som 53 million stock of VAT refunding claims to large enterprises by end-March 2003.

17. We will introduce new performance criteria on payroll tax collection in cash and the Social Fund's transfer to the Medical Insurance Fund (MIF). Compliance with the floor on payroll tax collections will require that republican and local government spending agencies are current with their payroll contributions to the Social Fund and that monthly transfers are effected on the 25th day of each month. Meanwhile, post-January 1, 2002 arrears of the Social Fund to the MIF, excluding arrears on medical insurance of the unemployed and pensioners will be reduced from som 77 million at end-September 2002 to som 50 million by year-end, and som 40 million at end-March 2003. All arrears will be cleared by end-2003. No new arrears to the Medical Insurance Fund will be accumulated beginning October 2002 and all current transfers to the MIF and transfers to clear post-January 1, 2002 arrears will be in cash (no offsets or in-kind payments).

18. On the expenditure side, in line with our poverty reduction strategy, we will increase social spending by 0.3 percentage point of GDP, to 11.9 percent in 2003. In compensation for the extension of VAT on large producers' direct sales to domestic market, the 2003 budget incorporates an 8.0 percent average increase in government wages and old-age pensions from April 1, 2003. The specific amount of the increase in old-age pensions will be determined during the February mission depending on the financial position of the Social Fund. At the same time, the Unified Monthly Benefit will be increased on average by 20 percent to compensate poor households for the expansion of the VAT coverage. On public investment, we will continue our work to establish clear guidelines for prioritizing the PIP on the basis of its likely impact on growth, export potential, and poverty reduction. Draft guidelines were submitted for the IMF, World Bank, and ADB staff comments at end-December, 2002. In 2003, we expect that \$82 million donor financing will be disbursed to finance the PIP. We have been able to reduce counterpart financing arrears from som 189 million to som 135 million at end-October 2002 and plan to clear the rest by end-January 2003. Fiscal performance criteria under the program will be cash tax collection, cash deficit, avoidance of arrears in wages, pensions, categorical grants, mandatory transfers to the Social Fund, energy bills to KyrgyzEnergo, allowances to poor families, and the performance criteria on payroll tax collection and the Social Fund's transfers to the Medical Insurance Fund as described above.

19. To improve efficiency in administering public finances, we will complete the Ministry of Finance restructuring according to the time schedule indicated in Annex II. To improve the budgetary process, we will issue a time schedule for the preparation of the 2004 budget by end-January 2003. The Treasury has started quarterly cash forecasting and these forecasts will be shared with the Fund staff on a regular basis. Pending the computerization

of the Treasury, we will develop a temporary commitment control and arrears tracking system on a manual basis. The first such report will be shared with the Fund staff by end-March 2003. Finally, to provide an accurate presentation of overall public finances, we will present to parliament consolidated general government accounts in the context of the 2003 State Budget. A Medium-Term Fiscal Framework for 2004-2006 to be designed to achieve real GDP growth of 5 percent and inflation of not more than 4 percent will be approved and published by the Economic Policy Council by end-March 2003.

Monetary and exchange rate policy

20. Our economic strategy is based on cautious monetary policy to keep inflation low to minimize pressure on the exchange rate and to ensure cost competitiveness of Kyrgyz exports. Broad money has increased substantially since the beginning of the program to accommodate a strong demand for money as evidenced by a stable and slightly appreciating nominal exchange rate. However, the NBKR stands ready to use open market operations to reduce liquidity in case we perceive any sign of rekindling inflation. We expect the demand for real balances to increase by 6 percent during 2003 which implies continuing remonetization of the economy and a further decline in currency substitution. The structural measures on the banking sector reforms detailed below are expected to improve financial intermediation and raise the money multiplier, albeit only slightly in the short term. Consistent with these trends, and with our growth and inflation targets, reserve money is programmed to grow by 6.5 percent during 2003 down from a projected 39 percent increase during 2002. This implies for 2003 a 15 percent growth of some broad money, down from a currently projected 30 percent during 2002. Our new performance criteria on NIR and NDA of the NBKR have been set against the backdrop of the better-than-expected balance of payments outcome and reversed currency substitution. Although the current account deficit is expected to widen somewhat in 2003, the continuing strengthening of confidence in the som and continued BOP support should make an increase of NIR by \$23.4 million feasible during October 1, 2002-March 31, 2003. As we expect a surplus in the primary fiscal balance (excluding the foreign financed component of the PIP), NDA should decline further by some 199 million between October 1, 2002 and March 30, 2003. In daily monetary operations, the NBKR will increasingly rely on using treasury bills as the market gains depth. T-bills issued in December, 2002, as part of the normalization of financial relations between the Ministry of Finance and the NBKR will provide the necessary instruments.

21. The NBKR will continue its exchange rate policy of managed floating. It will intervene on the foreign exchange market to smooth temporary variations of the nominal exchange rate and to strengthen the official foreign reserve position. In our medium term strategy, we believe that the tradable goods sector's competitiveness is better served by containing the growth of unit labor costs rather than by a nominal exchange rate depreciation.

External sector policies

22. We are actively pursuing our debt reduction strategy primarily through further fiscal adjustment. By 2005, we intend to reduce the general government primary fiscal deficit to 1.4 percent of GDP from the projected 3.8 percent in 2002. The streamlining of the PIP is underway and these expenditures will decline to 3.5 percent of GDP by 2005. We have also issued a tender for KyrgyzTelekom and, if successful, 75 percent of those receipts will be deposited in a special account at the NBKR to be used later for external debt reduction. We have limited the contracting of new public or publicly guaranteed debt to loans with grant element of at least 45 percent. Consistent with the Paris Club agreement, we continue pursuing with interested foreign investors debt-for-equity and debt-for-nature swaps.

23. In trade policy, our main problem is regional trade restrictions. As a member of the WTO and in the context of the CIS7 initiative, we plan to approach our neighboring countries with specific proposals to alleviate these restrictions starting with fees imposed on road transportation. On our part, we will maintain a free trade and exchange regime and refrain from introducing new seasonal tariffs or non-tariff barriers on agricultural or other imports. By end-January 2003, we will develop an action plan to help farmers to improve their access to the world market. We will also investigate the feasibility of moving from barter to cash in our energy trade with the neighboring countries in the medium term. A feasibility report will be submitted to the Economic Policy Council by end-March 2003.

24. More generally, we will honor the program's continuous performance criterion on not imposing or intensifying restrictions on payments and transfers for current international transactions, introducing multiple currency practices, concluding bilateral payments agreements that are inconsistent with the IMF's Article VIII, or imposing or intensifying imports restrictions for balance of payments reasons.

Structural policies

25. In the second-year program, the emphasis of our structural policies will be in two areas: governance reform and further restructuring of the banking sector. Reforms in these areas are necessary to improve the business and investment climate, mobilize domestic resources to finance investment, and improve access to credit. On banking reform, we will follow the advice of the recent FSAP mission to reduce commercial banks' vulnerabilities. The reform effort will concentrate on further enhancing bank supervision, improving the regulatory framework, divesting state-owned banks, strengthening DEBRA, and accelerating the computerization of the payment system. The specific measures and implementation schedule are presented in Box 1.

26. The general perception of corruption in public institutions limits the efficiency of the government. We will pursue vigorously our new action plan to tackle the governance problem. This plan combines the main features of the work done under the PRGF-supported program, the ADB's Corporate Governance and Enterprise Reforms Program, the ADB's Custom Modernization Project, and the World Bank's Governance Structural Adjustment

Credit. We will concentrate on five areas: (i) institution building for good governance; (ii) promoting public awareness; (iii) improving efficiency in public administration; (iv) strengthening of corporate governance; and (v) reforming the judiciary. The specific steps toward good governance are presented in Box 2. This box also indicates which measures will be specifically monitored under the IMF, World Bank, and AsDB-supported programs.

IV. PRIOR ACTIONS AND PROGRAM MONITORING

27. We recognize that the adoption by parliament of the 2003 State and Social Fund Budgets as discussed with the Fund staff is a precondition for the IMF Executive Board approval of the second-year program and completion of the second review under the three-year PRGF arrangement.

28. To monitor policy implementation under the second-year program through end-March 2003, we set out several quantitative and structural performance criteria and benchmarks shown in Table 1 and Box 3 of this Memorandum. In particular, we have added two performance criteria for program performance: a floor on payroll tax collections and a ceiling on the stock of Social Fund arrears to the Medical Insurance Fund (MIF). Detailed definitions of the quantitative targets appear in the revised Technical Memorandum of Understanding (TMU, Annex III).

29. The government of the Kyrgyz Republic and the NBKR believe that the policies and measures set forth in this SMEP are adequate to achieve the objectives of the program. However, in consultation with the Fund staff, we will take any further measures that may be needed to ensure the success of the program. These consultations can be initiated by the government or whenever the Managing Director requests them.

Box 1. Banking Sector Reform Program for 2003-2005				
Bank supervision	Regulatory framework	State-owned banks	DEBRA	Payments system
<p>1. A NBKR task force will analyze the financial legislation and develop proposals to eliminate gaps and any inconsistencies with respect to the Basel Principles by end-March 2003;</p> <p>2. Submit to Parliament amendments to Banking Law to ensure the independence of the internal audits function by end-September 2003;</p> <p>3. Submit to Parliament amendments to the law on Audit to empower NBKR to reject, require replacement, and if necessary appoint external auditors and require auditors to disclose and discuss their findings, and working papers, at NBKR request - by end-September 2003;</p> <p>4. Submit to Parliament amendments to the Law on Audit by end-September 2003 to define the qualification requirements of external bank auditors.</p> <p>5. Establish a unit to supervise microfinance institutions - by end-January 2003.</p>	<p>1. Submit to Parliament draft AML/CTF legislation – by end-January 2003.</p> <p>2. Develop and design a deposit insurance scheme (DIS). Implementation is envisaged for 2005, provided the DIS is funded and participating banks meet all eligibility criteria ;</p> <p>3. Raise minimum own capital requirement to som 30 million by end-June, 2003 and to som 60 million by end-2005; 1/</p> <p>4. Eliminate the specialized bank status by end-January 2003;</p> <p>5. Submit to Parliament amendments to legislation to eliminate the 15 percent maximum ownership threshold by end-September 2003;</p>	<p>I. KAIRAT:</p> <p>1. Issue a privatization tender by end-March 2003;</p> <p>2. Actively seek IFI equity participation;</p> <p>3. Select a short list of fit and proper strategic investors and start negotiations by end-December 2003.</p> <p>II. SSC</p> <p>1. Adopt by end-January 2003 a joint Government-NBKR resolution to transfer ownership to the government and complete transfer by end-March 2003;</p> <p>2. By end-September 2003, streamline and increase efficiency of branch network in performing payments services possibly including postal offices (cost benefit study of the appropriate range of activities through the World Bank by end-June 2003);</p> <p>3. Prepare by end-September 2003 a proposal of a development strategy of the SSC, including the potential for microfinancing and equity participation by the IFIs;</p> <p>III. KAFC</p> <p>1. Prepare a concept paper for sustainable financial development in coordination with WB and IMF by end-January 2003.</p>	<p>1. Make it independent legal entity as of February 1, 2003;</p> <p>2. Only liquidation and debt recovery tasks as of February 1, 2003;</p> <p>3. Aim at financing through fees starting July 1, 2003;</p> <p>4. Seek TA from IDA by end-November 2002;</p> <p>5. No write-offs of debts unless specifically authorized by DEBRA's Supervisory Board.</p>	<p>1. Streamline and modernize regulatory and legal framework on electronic payments to reduce the risk in the payments system;</p> <p>2. Finalize and publish Strategic Plan for 2003-2005 by end-January 2003.</p>

1/ Own capital is defined as tier 1 capital less cross-shareholdings in any financial institution.

Box 2. Governance Reform Measures for 2003-2005

Institution building	Public awareness	Efficiency of public administration	Corporate governance	Judiciary
<p>1. Establish a National Integrity Working Group and related organizations within and outside government (IMF);</p> <p>2. Organize a National Integrity Workshop (IMF);</p> <p>3. Submit to parliament a conflict of interest law by end-March 2003 (WB);</p> <p>4. Prepare a restructuring plan of the State Commission for Procurement and amend the public procurement law in line with European Union directives by end-September 2003 (WB);</p>	<p>1. Conduct and publish annual perception surveys of public and corporate governance, starting 2003 (WB);</p> <p>2. Publish annually a list of the 50 largest delinquent tax payers and energy users (IMF);</p> <p>3. Publish a quarterly fiscal bulletin on budget execution (IMF);</p> <p>4. Approve and publish the 2004-2006 medium-term fiscal framework by end-March 2003 (IMF);</p> <p>5. Publish annually the Chamber of Accounts audits of state finances (WB).</p>	<p>1. Based on the functional review of these institutions, consolidate the Ministry of Foreign Trade and Industry, the State Antimonopoly Committee, the State Committee for Standards and Measures, the State Commission for Entrepreneurship, and the Center for Foreign Investment to eliminate functional duplications and inefficiencies (IMF).</p> <p>2. Revise the protocols for tax and customs inspections as recommended by the ADB by end-2003 (ADB);</p> <p>3. Eliminate the backlog in VAT refunds by end-March 2003 and streamline VAT refund regulation (IMF) by end-Sept. 2003;</p> <p>4. Strengthen the role of financial officers in line ministries (WB);</p> <p>5. Adopt a strategy for implementing structural changes in the Ministries of Health, Education, and Agriculture based on the recent functional review (by end-June 2003) (WB);</p> <p>6. Complete functional reviews of the Ministries of Labor, Social Protection, Justice, and Transport and Communications and of the State Property Fund by end-June 2003 (WB);</p> <p>7. Limit the maximum number of annual enterprise inspections (WB).</p> <p>8. Review the charter of the Economic Development Fund in view to consolidate its loan recovery operations with DEBRA (WB).</p>	<p>1. Introduce IAS 2001 for all enterprises listed on the KES by January 2004 (ADB);</p> <p>2. Introduce IAS 2001 for all commercial banks by January 2004 (ADB);</p> <p>3. Train inspectors on IAS 2001 and only accept 2002 financial statements from KES listed enterprises based on IAS 2001 (ADB);</p> <p>4. Approve new law on national standards for asset valuation (ADB);</p> <p>5. Complete a re-evaluation by SPF of physical and financial assets of three large SOEs (ADB);</p> <p>6. Amend relevant regulations on pledges as recommended by the ADB;</p>	<p>1. Reform the development agenda of the Ministry of Justice following the recent functional review by end-March 2003 (WB).</p> <p>2. Issue implementation regulations for extra-judicial arbitration of commercial disputes by end-March 2003 (ADB);</p> <p>3. Require that all decisions be justified in writing and published (IMF);</p> <p>4. Establish an independent anti-corruption unit appointed by the President and approved by Parliament by end-June 2003 (IMF);</p> <p>5. Streamline significantly court proceedings on banking issues starting March 1, 2003 (ADB);</p> <p>6. Improve legal tools to ensure value of collateral by end-March 2003 (ADB);</p> <p>7. Review the court fee system with a view to reduce fees to 3 percent of par value of collateral by end-January 2003 (IMF);</p> <p>8. Streamline significantly appeal system by end-June 2003 (ADB);</p>

Box 3. Prior Action, Structural Performance Criteria, and Benchmarks

Prior Action

Adoption by Parliament of the 2003 State and Social Fund Budgets as discussed with the Fund staff;

Structural performance criteria

By end-March 2003

- Approval by the Economic Policy Council and publishing of the 2004-2006 Medium-Term Fiscal Framework designed to achieve real GDP growth of 5 percent and inflation of not more than 4 percent a year;

By end-June 2003

- Raise minimum own capital requirement for commercial banks to som 30 million.

Structural benchmarks

By end-January 2003

- Submit to Parliament draft AML/CFT¹ legislation.
- Publish the list of the 50 largest delinquent tax payers;
- Eliminate the specialized bank status.

By end-March 2003

- Reduce arrears on VAT refunds as specified in paragraph 16 of the SMEP.
- Issue implementation regulations for extra-judicial arbitration of commercial disputes.
- Develop a commitment control and arrears tracking system on a manual basis.
- Issue a privatization tender for KAIRAT bank.

¹ Anti-Money Laundering and Combating Financing Terrorism.

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

	2001		2002							2003			
	December	March	March	June	June	September		September	December	March	June	September	December
	Actual	Performance Criteria Adjusted	Actual	Benchmarks Adjusted	Actual	Program	Adjusted	Actual	Benchmarks	Performance Criteria	Indicative targets	Indicative targets	Benchmarks
I. Performance criteria													
1. Floor on net international reserves of the NBKR in convertible currencies (eop stock, in millions of U.S. dollars) 2/	39.3	30.6	53.6	43.7	58.4	57.6	48.4	79.9	96.1	104.2	104.6	113.8	119.9
2. Ceiling on net domestic assets of the NBKR (eop stock) 3/	1,257	1,090	893	2,566	2,438	1,987	2,436	2,007	1,920	1,804	1,883	1,560	1,308
3. Ceiling on cumulative fiscal deficit of the state government 4/	1,290 5/	n.a.	2,276	n.a.	3,301	4,948	n.a.	4,047	1,548	2,713	3,705	4,396	1,130
4. Cumulative floor on state government tax collections in cash 6/	2,929	n.a.	5,008	n.a.	7,508	10,316	n.a.	10,359	3,025	5,303	8,240	11,619	3,876
5. Ceiling on the stock of central government budget arrears 7/	0	n.a.	0	n.a.	30	0	n.a.	0	0	0	0	0	0
6. Ceiling on the stock of Social Fund pension arrears	12	n.a.	0	n.a.	92	0	n.a.	0	0	0	0	0	0
7. Floor on payroll collections in cash of the Social Fund 8/	...	...	...	...	...	...	...	...	975	1,715	2,515	3,389	1,102
8. Ceiling on the stock of Social Fund arrears to the Medical Insurance Fund	...	...	...	...	...	...	...	77.1	50	40	20	10	0
9. Ceiling on contracting or guaranteeing by the state government or NBKR of new external debt of less than one year (in millions of U.S. dollars) 9/ 10/	0	n.a.	0	n.a.	0	0	n.a.	0	0	0	0	0	0
10. Ceiling on contracting or guaranteeing by the state government or NBKR of new nonconcessional external debt (cumulative, in millions of U.S. dollars) 11/	0	n.a.	0	n.a.	0	0	n.a.	0	0	0	0	0	0
11. Ceiling on new external payment arrears (in millions of U.S. dollars) 10/	0	n.a.	0	n.a.	0	0	n.a.	1.5	1.5	0	0	0	0
II. Indicative targets													
1. Ceiling on reserve money (NBKR liabilities)	5,359	4,853	5,626	5,602	6,164	5,700	5,700	6,786	7,432	7,677	7,784	7,874	7,916

Sources: Data provided by the Kyrgyz authorities; and Fund staff estimates and projections.

1/ Until September 2002, foreign exchange components valued at the exchange rate US\$1 = som 49, gold holdings valued at US\$265 per ounce, SDR valued at SDR 1 = US\$1.259. Starting December 2002, foreign exchange components valued at the exchange rate US\$1 = som 47, gold holdings valued at US\$322.4 per ounce, SDR valued at SDR 1 = US\$1.3186. Targets exclude claims and liabilities to BRO countries.

2/ As defined in the Technical Memorandum of Understanding (TMU), excludes, among others, swaps and international reserves of the NBKR that are pledged or blocked.

3/ As defined in the TMU, excludes, among others, counterpart of the loan by the Eximbank of Turkey and the EBRD/IDA enterprise loan which are channeled through the NBKR.

4/ As defined in the TMU, state government comprises central government and local governments. For March 2003, cumulative begins on October 1, 2002. For December 2003, cumulative begins on October 1, 2003.

5/ The deficit for the fourth quarter of 2001 is adjusted for interest payments rescheduled by the Paris Club (som 172 million).

6/ As defined in the TMU, includes, among others, collection of tax arrears but excludes, among others, tax offsets. For March 2003, cumulative begins on October 1, 2002. For December 2003, cumulative begins on October 1, 2003.

7/ As defined in the TMU, central government budget arrears comprise, among others, wages, payroll contributions and mandatory transfers to the Social Fund, categorical grants, payments to KyrgyzEnergo, and allowances to poor families from September 2002 onwards.

8/ For March 2003, cumulative begins on October 1, 2002. For December 2003, cumulative begins on October 1, 2003.

9/ External debt is defined in the TMU as in Executive Board's Decision no. 12274 (00/85) of August 24, 2000. Includes loans, leases, suppliers' credits and other instruments giving rise to external debt.

10/ On a continuous basis.

11/ As defined in the TMU, a debt is classified as concessional if its grant element is at least 45 percent, calculated using a discount rate based on the 10-year average of OECD commercial interest reference rates (CIRR), for debts of maturity greater than 15 years; for debts of maturity 15 years or less, the discount rate should be based on the six month average of the OECD CIRR. The ceilings include loans, leases, supplier's credits and other instruments giving rise to external debt on nonconcessional terms. IMF lending is excluded from the ceiling on new nonconcessional borrowing.

Adjustors

1. The floor on net international reserves of the NBKR will be adjusted: (i) upward/downward by 100 percent for excesses/shortfalls of the use of net foreign financing of the state government budget and cash grants; (ii) upward/downward by 100 percent for excess/shortfall of cash privatization receipts. The adjustment for shortfalls in adjustors (i) and (ii) is limited to US\$ 15 million each, valued at the program exchange rate. In the case of a release of the NBKR's pledged foreign reserves, the NIR floor will be adjusted upward by 100 percent of the net effect of the releases and related amortization payments.

2. The ceiling on net domestic assets of the NBKR will be adjusted: (i) downward/upward by 100 percent for excesses/shortfalls of the use of net foreign financing of the state government budget and cash grants; (ii) downward/upward by 100 percent for excess/shortfall of cash privatization receipts. The adjustment for shortfalls in adjustors (i) and (ii) is limited to US\$ 15 million each, valued at the program exchange rate, excluding the amortization payments for the release of the NBKR's pledged foreign reserves.

**Schedule of Basic Actions on Stepwise Establishment of the
Large Taxpayer Unit**

Activity	Begin	End
Establishment of the headquarters of the LTU; selection and appointment of full-time department head and staff	01/11/02	30/12/02
Selection of taxpayers to be controlled	01/01/03	30/01/03
Decision on organizational structure	01/02/03	28/02/03
Preparation and implementation of regulations to support LTU operations	01/02/03	30/03/03
Design of a manual ledger card system for revenue accounting purposes	15/03/03	30/04/03
Notification to the large taxpayers of the new arrangements for filing and paying their taxes with effect from 01/08/03	01/04/03	30/04/03
Decision on the computerized information systems requirements for the LTU	01/05/03	30/06/03
Preparation of procedural manuals for the LTU based on new procedures and use of a new, manual, revenue accounting system	01/05/03	30/06/03
Creation of a special bank account for the deposit of tax payments by large taxpayers	01/06/03	30/07/03
Training of LTU staff on new procedures	01/07/03	30/10/03
Seminars to explain the new system to large taxpayers	01/07/03	30/07/03
Review/update information on name, address, economic activity, tax obligations, settlement accounts, etc., from large taxpayers	01/08/03	30/09/03
Collection by LTU from large taxpayers becomes operational 1/	01/08/03	
Design and implementation of the computerized LTU information system	01/08/03	30/07/04

1/ This timetable envisages that effective control of the large taxpayers will be transferred to the LTU starting August 1, 2003, although the implementation of the self-assessment system may only be possible after the preparation of the manuals, the training of LTU staff, and the seminars for taxpayers have been completed.

2/ This timetable also assumes that by August 1, 2003 only the large taxpayers in the Bishkek area will have been transferred to the LTU. Large taxpayers in the Chui region will be transferred in the 3rd quarter of 2003, and the rest in the 1st quarter of 2004.

3/ This is a tentative timetable that will be revised upon the completion of a comprehensive assessment by an IMF fiscal expert in the first quarter of 2004.

Schedule of the Restructuring of the Ministry of Finance

Actions	Date
Approval of the framework for the reorganization of the office and management of the Ministry of Finance: reduction of its employment by 10 percent, development and approval of the required statutory acts that regulate the activity of the Ministry according to the Concept and the new Staff Organizational Framework Chart	August 1, 2002
Functional reorganization of jurisdictional units of the Ministry of Finance. Elaboration and implementation of basic measures under the Fiscal Reform Strategy observing the dates as set up in the Decree of the President of the Kyrgyz Republic of July 16, 2002, No. 191	October 1, 2002
Improving its analytical and forecasting work, a regulatory legal framework that regulates a budget process, administration and revenue collection.	January 1, 2003

TECHNICAL MEMORANDUM OF UNDERSTANDING

1. The Kyrgyz Republic's performance under the second-year PRGF-supported program will be assessed by the IMF on the basis of the observance of quantitative and structural performance criteria and benchmarks. This annex and the tables attached to the SMEP define the quantitative performance criteria and indicative targets, the structural benchmarks and performance criteria (Box 3 attached to the SMEP), as well as the monitoring requirements.¹

I. QUANTITATIVE TARGETS

2. Quantitative targets are summarized in Table 1 of the SMEP and defined below. This annex sets out the quantitative benchmarks for end-December 2002, quantitative performance criteria for end-March 2003, and indicative targets for end-June and end-September 2003. At the time of the third review, quantitative performance criteria will be set for end-September 2003.

Floor on net international reserves of the NBKR in convertible currency

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

4. Total gross international reserves of the NBKR shall be defined as the NBKR holdings of monetary gold, holdings of SDRs, any reserve position in the IMF, and any holdings of convertible currencies in cash, debt instruments (including accrued interest) or with foreign banks. Amounts pledged as collateral or in swaps or otherwise blocked, capital subscriptions in foreign financial institutions, and non-liquid assets of the NBKR are excluded. Excluded are also net forward positions, defined as the difference between the face value of foreign currency denominated NBKR off-balance sheet claims on non-residents and foreign currency obligations to both residents and non-residents. However, net claims on other BRO countries are excluded from the ceiling. For program monitoring purposes, gross international reserves shall be valued at a fixed program exchange rate of som 47 per U.S. dollar and \$1.3186 per SDR. Official gold holdings shall be valued at \$322.4 per troy ounce. Program cross exchange rates are listed in Table 10.

5. Total international reserve liabilities of the NBKR in convertible currencies shall be defined as outstanding liabilities to the IMF and other convertible currency liabilities of the NBKR to non-residents with an original maturity of up to and including one year. For program monitoring purposes, total international reserve liabilities shall be valued at the

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

program exchange rates. Thus calculated, the stock of net international reserves in convertible currencies amounted to \$80.7 million as of September 30, 2002.

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

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

	(In millions of U.S. dollars)
December 31, 2002 (benchmark)	96.1
March 31, 2003 (performance criterion)	104.2
June 30, 2003 (indicative target)	104.6
September 30, 2003 (indicative target)	113.8
December 31, 2003 (benchmark)	119.9

1/ End-of-period stocks.

7. The floor on net international reserves of the NBKR will be adjusted: (i) upward/downward by 100 percent for any excess/shortfall in net foreign financing and cash grants; and (ii) upward/downward by 100 percent for any excess/shortfall in cash privatization receipts. The adjustment for shortfalls in adjustors (i) and (ii) is to be limited to \$15 million each. In the case of a release of the NBKR's pledged foreign reserves, the NIR floor will be adjusted upward by 100 percent of the net effect of the releases and related amortization payments.

8. Net foreign financing is defined as balance of payment support loans plus cash grants to the state government budget minus amortization payments by the Ministry of Finance and NBKR (excluding repayments to the Fund). This definition applies to the adjustors to NIR and NDA. The cumulative net foreign financing for the program period is as follows:

Table 2. Projected Net Foreign Financing and Cash Grants
Cumulative from October 1, 2002

	(In millions of U.S. dollars)
December 31, 2002	13.1
March 31, 2003	22.3
June 30, 2003	21.4
September 30, 2003	25.5
December 31, 2003	24.1

Ceiling on the net domestic assets of the NBKR

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

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

10. Thus defined, the NBKR's net domestic assets consist of: (a) gross credit to the general government from the NBKR minus deposits of the general government with the NBKR minus the counterpart of the loan by the Eximbank of Turkey; (b) gross credit to domestic banks by the NBKR minus the counterpart of the EBRD and IDA enterprise loans; and (c) all other net assets of the NBKR (other items net). Thus defined, the stock of the NBKR's net domestic assets amounted to som 2,003 million on September 30, 2002.

11. The ceilings on the net domestic assets of the NBKR during the program period are reported in Table 3 below.

Table 3. Ceilings on the Net Domestic Assets of the NBKR 1/

	(In millions of soms)
December 31, 2002 (benchmark)	1,920
March 31, 2003 (performance criterion)	1,804
June 30, 2003 (indicative target)	1,883
September 30, 2003 (indicative target)	1,560
December 31, 2003 (benchmark)	1,308

1/ End-of-period stocks.

12. The ceiling on net domestic assets of the NBKR will be adjusted: (i) downward/upward by 100 percent of the excess/shortfall in net foreign financing and cash grants; and (ii) downward/upward by 100 percent of the excess/shortfall of cash privatization receipts. The adjustment for shortfalls in adjustors (i) and (ii) is to be limited to \$15 million each valued at the program exchange rate excluding the amortization payments for the release of the NBKR's pledged foreign reserves.

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

Ceiling on the cumulative fiscal deficit of the state government

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

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

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

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

	(In millions of soms)
December 31, 2002 (benchmark)	1,548
March 31, 2003 (performance criterion)	2,713
June 30, 2003 (indicative target)	3,705
September 30, 2003 (indicative target)	4,396
December 31, 2003 (benchmark) 2/	1,130

1/ Cumulative beginning from October 1, 2002.

2/ Cumulative beginning from October 1, 2003

Floor on cumulative tax collections in cash by the state government

16. Cumulative tax collections in cash correspond to the line “IV. Tax Receipts” in the Treasury Report and comprise the following categories: 1.0 taxes on income and profits; 4.0 taxes on property; 5.1 VAT on domestic and imported products; 5.1.1.0 retail sales tax; 5.2 excises on domestic and imported products; 5.4 specific taxes on services; 5.5 taxes on use of goods and services; 5.6 taxes on use of natural resources; 6.0 taxes on international trade; 7.0 other taxes. Thus defined, cumulative tax collections in cash since October

amounted to som 10,359 million as of September 30, 2002. Cumulative tax collections in cash include collections of tax arrears but exclude tax offsets.

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

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

	(In millions of soms)
December 31, 2002 (benchmark)	3,025
March 31, 2003 (performance criterion)	5,303
June 30, 2003 (benchmark)	8,240
September 30, 2003 (indicative target)	11,619
December 31, 2003 (benchmark) 2/	3,876

1/ Cumulative from October 1, 2002.

2/ Cumulative from October 1, 2003.

Ceiling on the stock of central government budget arrears

18. For the purposes of the program, central government budget arrears are defined as an overdue payment obligation of the Republican budget related to: (i) wages; (ii) Social Fund payroll contributions; (iii) mandatory transfers to the Social Fund; (iv) categorical grants; (v) payments to Kyrgyz Energo; and (vi) allowances for poor families. A payment is defined to be overdue if it remains unpaid after its due date for (iii) and (iv); for 30 days after its due date for (i) and (ii); 60 days after its due date for (v); and 40 days after its due date for (vi). As of September 30, 2002, the stock of thus defined central government budgetary arrears was zero.

19. The ceilings on the stock of central government budget arrears during the program period are reported in Table 6 below.

Table 6. Stock of Central Government Budget Arrears

	(In millions of soms)
December 31, 2002 (benchmark)	0
March 31, 2003 (performance criterion)	0
June 30, 2003 (indicative target)	0
September 30, 2003 (indicative target)	0
December 31, 2003 (benchmark)	0

Ceiling on the outstanding stock of Social Fund pension arrears

20. A pension payment by the Social Fund is defined as overdue if it remains unpaid for 30 days after its due date. As of September 30, 2002, the stock of pension arrears was zero.

Floor on the payroll tax collections of the Social Fund

21. Cumulative payroll tax collections in cash correspond to the total contributions collected by the Social Fund from both employers and employees for a given period.
22. The floor for the cumulative tax collection in cash during the program period are reported in Table 7 below.

Table 7. Cumulative Floor on Payroll Tax Collections in Cash 1/

	(In millions of soms)
December 31, 2002 (benchmark)	975
March 31, 2003 (performance criterion)	1,715
June 30, 2003 (indicative target)	2,515
September 30, 2003 (indicative target)	3,389
December 31, 2003 (benchmark) 2/	1,102

1/ Cumulative from October 1, 2002.

2/ Cumulative from October 1, 2003.

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

23. Social Fund arrears to the Medical Insurance Fund are defined as overdue transfer obligations of the former to the latter as defined by law and refer only to arrears incurred starting January 1, 2002. A transfer is defined to be overdue if it remains unpaid after its due date.
24. The ceiling on the cumulative stock of Social Fund arrears to the Medical Insurance Fund during the program period are reported in Table 8 below. As of end-September 2002, total arrears of the Social Fund to the Medical Insurance Fund amounted to soms 77.1 million. No new arrears will be accumulated to the Medical Insurance Fund starting October 1, 2002.

Table 8. Cumulative Ceiling on the Stock of Social Fund Arrears to the Medical Insurance Fund

	(In millions of soms)
December 31, 2002 (benchmark)	50
March 31, 2003 (performance criteria)	40
June 30, 2003 (indicative target)	20
September 30, 2003 (indicative target)	10
December 31, 2003 (benchmark)	0

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

25. In connection with the contracting or guaranteeing of external debt by the state government of the Kyrgyz Republic, the NBKR, or any other agency acting on behalf of the state government of the Kyrgyz Republic, 'debt' is understood to have the meaning set out in point 9 of the Guidelines on Performance Criteria with respect to External Debt in Fund arrangements (Decision No. 12274-00/85, dated August 24, 2000).³

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

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

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

Ceiling on new external payments arrears

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

Ceiling on reserve money

29. For the purposes of the program, reserve money consists of currency issued by the NBKR and balances on commercial banks' correspondent accounts with the NBKR. The stock of reserve money amounted to som 6,786 million as of end-September, 2002. The indicative limits for the program periods are reported in Table 9 below.

Table 9. Ceilings on Reserve Money 1/

	(In millions of soms)
December 31, 2002 (benchmark)	7,432
March 30, 2003 (indicative target)	7,677
June 30, 2003 (indicative target)	7,784
September 30, 2003 (indicative target)	7,874
December 31, 2003 (benchmark)	7,916

1/ End-of-period stocks.

II. REPORTING REQUIREMENTS UNDER THE PROGRAM

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

The balance sheet of the NBKR

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

Monetary survey

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

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

International reserves and key financial indicators

34. The NBKR will provide detailed monthly data within 14 days from the end of the month on the composition of both its gross and net international reserves in convertible currencies and holdings of monetary gold. These data will be provided at two alternative sets

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

of the exchange rates and the gold price: first, at those used to derive the NFA position in the NBKR accounts; second, at those specified in the program (Section I). In addition, weekly reports should be sent to the Fund every Monday on: (a) exchange rates (including the official and interbank exchange rates), foreign exchange interbank market turnover, and the volume of NBKR foreign exchange sales and purchases in the interbank market and with other parties; and (b) treasury bill yields and the amount of treasury bill sales and redemptions. On the 25th day of the month following the reference month, the NBKR will provide data on bank deposit and lending rates by maturity.

Banking system data

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

External debt

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

Budgetary and extrabudgetary data

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

Balance of payments data

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

Other general economic information

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

Table 10. Program Cross Exchange Rates

	Currency Names	National Currency/US\$	US\$/National Currency
GBP	UK pound sterling	0.6429	1.555399518
DKK	Danish krone	7.5922	0.131714072
EUR	Euro	1.0222	0.978300189
INR	Indian rupee	48.3655	0.020675907
CAD	Canadian dollar	1.5760	0.634518395
CNY	Chinese yuan	8.2772	0.120814167
KRW	South Korean won	1,226.6773	0.000815210
NOK	Norwegian krone	7.4841	0.133616229
TRL	Turkish lira	1,660,664.2599	0.000000602
SEK	Swedish krona	9.3470	0.106986026
CHF	Swiss franc	1.4999	0.666733333
JPY	Japanese yen	122.4359	0.008167538
AZM	Azerbaijani manat	4,897.9844	0.000204166
AMD	Armenian dram	557.9864	0.001792158
BYR	Belarusian rubel	1,864.0246	0.000536474
KZT	Kazakh tenge	154.4674	0.006473857
LVL	Latvian lats	0.6070	1.647446544
LTL	Lithuanian litas	4.0000	0.250000000
MDL	Moldavian lei	13.5746	0.073666751
RUR	Russian ruble	31.6350	0.031610595
TJS	Tajik somoni	2.8730	0.348068712
UZS	Uzbek sum	808.4429	0.001236946
UAH	Ukrainian hryvnia	5.3295	0.187635325
EEK	Estonian kroon	15.9935	0.062525543

INTERNATIONAL MONETARY FUND

KYRGYZ REPUBLIC

**Staff Report for the 2002 Article IV Consultation, Second Review Under the
Poverty Reduction and Growth Facility, and Request for Waiver of Performance
Criterion
Supplementary Information**

Prepared by European II and Policy Development and Review Departments
(In consultation with other departments)

Approved by Oleh Havrylyshyn and Michael Hadjimichael

February 14, 2003

1. This supplement reports on developments since the staff report was issued and on implementing the prior action for completing the second program review. It also reviews compliance with end-December 2002 and end-January 2003 program benchmarks.

Recent Developments

2. **The referendum on the new constitution was held on February 2, 2003.** Voter turnout reached 86 percent and the approval rate was 77 percent. The referendum included a vote of confidence in President Akayev which confirms his stay in office until the end of the term in 2005.

3. **Preliminary data indicate that real GDP declined by 0.5 percent in 2002 while the program was based on a 0.8 percent increase.**¹ The difference reflects a larger-than-expected contraction in energy production and lower growth in agriculture. Excluding gold and energy production, real GDP increased by 3.5 percent. The 12-month rate of inflation was 2.3 percent at end-December 2002, compared with the targeted 3.6 percent under the program.² As a result of the lower starting level, the tax base in 2003 could be 3 percent

¹ Preliminary data for end-January 2003 suggest 4.6 percent real GDP growth over January 2002, while the program is based on an unchanged real output in the first quarter of 2003.

² The 12-month rate of inflation was 2.5 percent in January 2003.

smaller than projected earlier. Because of the recent improvement in tax collection, however, the program's fiscal targets for end-March 2003 remain feasible.³

Prior Action

4. **The general government budget for 2003—excluding the three related tax laws—has been approved by Parliament.** In late December 2002, both houses approved the spending limits, the tax collection targets, and the fiscal deficit as programmed. The approval of the related tax legislation was delayed, however. While the increase in the excise tax on liquors has been imposed, extending VAT on large agricultural producers' direct sales to the domestic market has been approved only by the lower house of the parliament. In addition, the new property tax has yet to be passed by both the lower and upper house.

5. **The government has requested that the measures still to be completed under the prior action be identified as performance criteria under the program for end-March 2003 (Attachment I).** Accordingly, the upper house would approve the VAT extension in its next session beginning on March 17 and both houses would approve the property tax. In addition, the President would enact these laws by end-March. Reasons for the delays include the politically difficult referendum process, extra time needed to seek support from parliamentarians for the sensitive VAT legislation, and the winter recess of the upper house. These delays have not significantly affected the fiscal program because the VAT extension was to become effective only on April 1, 2003 and the impact of the delay in imposing the real property tax is 0.03 percent of GDP in 2003.

Performance under the Program

6. **The program is on track although the Social Fund did not quite meet the benchmark on payroll tax collection at end-December 2002 (Table 1).** The target was missed by 5.7 percent of total cash collections in the fourth quarter of 2002. The authorities report that this reflected a weaker-than-expected collection from local governments, but a correction is expected in the first quarter of 2003. The end-December 2002 benchmark for the state fiscal deficit has reportedly been met, mainly because of better revenue performance.

7. **The benchmarks of the monetary program for end-December 2002 were observed.** Reflecting strong demand for local currency, the NBKR bought \$12 million from the market in October-December. As a result, its net international reserves (NIR) exceeded the program floor by 5.6 percent of reserve money. Net domestic assets (NDA) remained below the ceiling by 1.8 percent of reserve money as part of the foreign exchange inflow was sterilized by increasing government deposits in the central bank.

³ The gross tax ratio improved by 1.4 percentage point of GDP in 2002, significantly more than projected (1 percentage point), suggesting that the strengthening of collection efforts in the second half of 2002 contributed 0.4 percent of GDP to tax performance.

8. The three end-January 2003 structural benchmarks have been implemented.

First, the government submitted to parliament a draft AMC/CFT⁴ law drafted in line with the recommendation of the Financial Sector Assessment Program (FSAP). Second, the list of the 50 largest delinquent taxpayers was published. Third, the NBKR eliminated the specialized bank status.⁵

Staff Appraisal

9. As the program is on track and the delay in enacting the tax laws does not undermine the fiscal program, the staff supports the authorities' request to modify the end-March 2003 performance criteria and to complete the second review under the PRGF arrangement.

⁴ Anti-Money Laundering and Combating Financing Terrorism.

⁵ Three banks had been assigned the specialized status allowing them to operate under restrictions imposed by the central bank despite not meeting the minimum capital requirement.

Bishkek, Kyrgyz Republic
February 14, 2003

Mr. Horst Köhler
Managing Director
International Monetary Fund
Washington, D.C. 20431

Dear Mr. Köhler:

This Supplementary Letter of Intent seeks the IMF Executive Board approval for a modification of our Second-Year Memorandum of Economic Policies (SYMEP) presented to you on January 31, 2003. In the SYMEP, we recognized that the adoption by parliament of the 2003 State and Social Fund Budgets was a precondition for the IMF Executive Board completion of the second review under the three-year PRGF arrangement.

So far, however, we have not been able to carry out fully this prior action. While the 2003 budget expenditures and revenue estimates were approved by both the lower and upper houses of the parliament in late December 2002, the work is not yet completed on the supporting tax legislation. Specifically, two tax laws remain to be enacted. First, on February 8, the Lower House of the parliament approved to extend the VAT on large agricultural producers but the upper house has not yet confirmed it because of the winter recess. Second, while we have presented the new property tax law to parliament, it is expected to be discussed in the lower house only on February 19 and requires the upper house confirmation after that.

There are three reasons for the delay. First, the referendum of our new constitution took more time than initially expected as the process was subject to high political tensions. Therefore, the parliament was able to consider the tax legislation only after the February 2 referendum. Second, our constitution requires a sequential approval of tax legislation by both chambers of parliament. Since the next session of the upper house starts only in mid-March 2003, we were not able to pass these two tax laws as committed in the SYMEP. Third, it took more time than envisaged to convince the parliamentarians about the necessity of the politically sensitive extension of the VAT within agriculture.

Because of these difficulties, we request the IMF Executive Board to approve a modification of our SYMEP regarding these two tax laws. We propose that the Executive Board approve our second-year program with the following performance criteria to be applied for end-March 2003:

- approval by the upper house of the parliament, and enactment, of the VAT extension on the direct sales of large agricultural producers referred to in paragraph 14 of the SYMEP; and

- approval by the lower and upper houses of parliament, and enactment, of a new tax on real property with a combination of tax rates and coverage providing at least the same estimated revenue impact as the draft submitted to parliament on February 12, 2003, and referred to in paragraph 14 of the SYMEP.

With these measures, our 2003 budget will be completed, including the tax legislation as envisaged in the SYMEP. This delay in decision making does not have any significant impact on our fiscal program. The VAT extension was initially expected to become effective on April 1, 2003, and we estimated the revenue impact of the real property tax conservatively for 2003. Overall, however, we recognize that these delays in the budgetary process should not be repeated. Therefore, we intend to review our budgetary mechanisms to ensure that parliament can approve our future budgets before the beginning of each fiscal year.

Yours sincerely,

/s/
Nikolai Tanaev
Prime Minister
Kyrgyz Republic

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

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

	2001		2002								
	December	March	March	June	June	September	September	December	December		
	% Actual	Performance Criteria Adjusted	Actual	Benchmarks Adjusted	Actual	Performance Criteria Program	Actual	Benchmarks Program	Adjusted	Preliminary	
I. Performance criteria											
1. Floor on net international reserves of the NBKR in convertible currencies (eop stock, in millions of U.S. dollars) 2/	39.3	30.6	53.6	43.7	58.4	57.6	48.4	79.9	96.1	95.4	105.2
2. Ceiling on net domestic assets of the NBKR (eop stock) 3/	1,257	1,090	893	2,566	2,438	1,987	2,436	2,007	1,920	1,955	1,780
3. Ceiling on cumulative fiscal deficit of the state government 4/	1,290 5/	n.a.	2,276	n.a.	3,301	4,948	n.a.	4,047	1,548	n.a.	1,469
4. Cumulative floor on state government tax collections in cash 6/	2,929	n.a.	5,008	n.a.	7,508	10,316	n.a.	10,359	3,025	n.a.	3,062
5. Ceiling on the stock of central government budget arrears 7/	0	n.a.	0	n.a.	30	0	n.a.	0	0	n.a.	0
6. Ceiling on the stock of Social Fund pension arrears	12	n.a.	0	n.a.	92	0	n.a.	0	0	n.a.	0
7. Floor on payroll collections in cash of the Social Fund 8/	...	...	...	...	...	...	...	...	975	n.a.	920
8. Ceiling on the stock of Social Fund arrears to the Medical Insurance Fund	...	...	...	...	...	...	...	77.1	50	n.a.	48
9. Ceiling on contracting or guaranteeing by the state government or NBKR of new external debt of less than one year (in millions of U.S. dollars) 9/ 10/	0	n.a.	0	n.a.	0	0	n.a.	0	0	n.a.	0
10. Ceiling on contracting or guaranteeing by the state government or NBKR of new nonconcessional external debt (cumulative, in millions of U.S. dollars) 11/	0	n.a.	0	n.a.	0	0	n.a.	0	0	n.a.	0
11. Ceiling on new external payment arrears (in millions of U.S. dollars) 10/	0	n.a.	0	n.a.	0	0	n.a.	1.5	1.5	n.a.	1.5
II. Indicative targets											
1. Ceiling on reserve money (NBKR liabilities)	5,359	4,853	5,626	5,602	6,164	5,700	5,700	6,786	7,432	7,432	7,639

Sources: Data provided by the Kyrgyz authorities; and Fund staff estimates and projections.

1/ Until September 2002, foreign exchange components valued at the exchange rate US\$1 = som 49, gold holdings valued at US\$265 per ounce, SDR valued at SDR 1 = US\$1.259. Starting December 2002, foreign exchange components valued at the exchange rate US\$1 = som 47, gold holdings valued at US\$322.4 per ounce, SDR valued at SDR 1 = US\$1.3186. Targets exclude claims and liabilities to BRO countries.

2/ As defined in the Technical Memorandum of Understanding (TMU), excludes, among others, swaps and international reserves of the NBKR that are pledged or blocked.

3/ As defined in the TMU, excludes, among others, counterpart of the loan by the Eximbank of Turkey and the EBRD/IDA enterprise loan which are channeled through the NBKR.

4/ As defined in the TMU, state government comprises central government and local governments. For March 2003, cumulative begins on October 1, 2002. For December 2003, cumulative begins on October 1, 2003.

5/ The deficit for the fourth quarter of 2001 is adjusted for interest payments rescheduled by the Paris Club (som 172 million).

6/ As defined in the TMU, includes, among others, collection of tax arrears but excludes, among others, tax offsets. For March 2003, cumulative begins on October 1, 2002. For December 2003, cumulative begins on October 1, 2003.

7/ As defined in the TMU, central government budget arrears comprise, among others, wages, payroll contributions and mandatory transfers to the Social Fund, categorical grants, payments to KyrgyzEnerg, and allowances to poor families from September 2002 onwards.

8/ For March 2003, cumulative begins on October 1, 2002. For December 2003, cumulative begins on October 1, 2003.

9/ External debt is defined in the TMU as in Executive Board's Decision no. 12274 (00/85) of August 24, 2000. Includes loans, leases, suppliers' credits and other instruments giving rise to external debt.

10/ On a continuous basis.

11/ As defined in the TMU, a debt is classified as concessional if its grant element is at least 45 percent, calculated using a discount rate based on the 10-year average of OECD commercial interest reference rates (CIRR), for debts of maturity greater than 15 years; for debts of maturity 15 years or less, the discount rate should be based on the six month average of the OECD CIRR. The ceilings include loans, leases, supplier's credits and other instruments giving rise to external debt on nonconcessional terms. IMF lending is excluded from the ceiling on new nonconcessional borrowing.

Adjustors

1. The floor on net international reserves of the NBKR will be adjusted: (i) upward/downward by 100 percent for excesses/shortfalls of the use of net foreign financing of the state government budget and cash grants; (ii) upward/downward by 100 percent for excess/shortfall of cash privatization receipts. The adjustment for shortfalls in adjustors (i) and (ii) is limited to US\$ 15 million each, valued at the program exchange rate. In the case of a release of the NBKR's pledged foreign reserves, the NIR floor will be adjusted upward by 100 percent of the net effect of the releases and related amortization payments.

2. The ceiling on net domestic assets of the NBKR will be adjusted: (i) downward/upward by 100 percent for excesses/shortfalls of the use of net foreign financing of the state government budget and cash grants; (ii) downward/upward by 100 percent for excess/shortfall of cash privatization receipts. The adjustment for shortfalls in adjustors (i) and (ii) is limited to US\$ 15 million each, valued at the program exchange rate, excluding the amortization payments for the release of the NBKR's pledged foreign reserves.



INTERNATIONAL MONETARY FUND

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FOR IMMEDIATE RELEASE
March 7, 2003

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Concludes 2002 Article IV Consultation with the Kyrgyz Republic

On February 19, 2003, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with the Kyrgyz Republic.¹

Background

Program summary

After two years of real GDP growth above 5 percent, output stagnated in 2002. It was adversely affected by a large landslide at the Kumtor gold mine—the country's major exporter—and weather-related contraction in hydro-electric energy production. On the other hand, real GDP excluding gold and energy recorded a 3.5 percent growth rate. Price stabilization has continued: the 12-month inflation fell to a lowest level during independence to 2.3 percent.

The proposed program is consistent with the country's National Poverty Reduction Strategy (NPRS) presented to the IMF and the World Bank on December 9, 2002. It projects a real GDP growth of 5 percent a year in 2003-2006 supported by productivity gains through structural reforms and more efficient use of capital and labor. The key policies include a continuous fiscal adjustment and a modest growth of some broad money of 15 percent in 2003

¹ Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities.

after rapid remonetization of the economy observed recently. The National Bank will continue its exchange rate policy of a managed float, which has served the country well. It will intervene in the foreign exchange market to smooth temporary market fluctuations and to accumulate reserves as appropriate. The program aims at a 4 percent inflation in 2003 and the medium term.

Total factor productivity is expected to be the main source of growth resulting from structural reforms, including in the areas of governance and the banking sector. As gold production is expected to start declining in the medium term, other industries will need to offset its negative growth impact which calls for strong cost competitiveness of exports. Export volumes are projected to grow 4.5 percent per year.

The continuation of fiscal adjustment is necessary for the success of the foreign debt reduction strategy launched in 2001. To strengthen the tax base, the government has introduced the 2003 budget with several new tax measures including an extension of VAT to cover large agricultural producers' sales in the domestic market. Overall, the general government tax-to-GDP ratio is expected to increase to 18 percent in 2003 from 17 percent in 2002. The authorities intend to streamline the Public Investment Program to 4.5 percent of GDP in 2003 so that the overall cash deficit will decline to 4.6 percent of GDP down from 5.6 percent of GDP in 2002. In the medium term, the fiscal deficit is targeted to fall to 3 percent of GDP. The proposed second-year program is fully financed through a combination of debt reschedulings from the Paris Club and balance of payment support from multilateral institutions.

The need to reduce trade restrictions in Central Asia is crucial to reap the benefits of foreign trade. The Kyrgyz authorities already maintain a liberal and low tariff trade regime. Recently, in line with World Trade Organization recommendations, the top import tariff has been further reduced and the number of tariff bands cut from six to four. The authorities also agreed to refrain from introducing new tariffs or nontariff barriers on agricultural or other imports.

Progress in improving governance to reduce corruption and state capture and reforms in the banking sector are critical for the success of the program. The new governance initiative aims at increasing the efficiency of public administration, the effectiveness of corporate governance, and the transparency of the judiciary. The banking reform, drawing on the recommendations of the recent Financial Sector Assessment Program (FSAP), aims at strengthening bank supervision, divesting state-owned banks, and computerize the payments system. The Kyrgyz Republic joined the IMF on August 5, 1992. Its quota² is SDR 88.8 million (about US\$120 million). The Kyrgyz Republic's outstanding use of IMF credits at end-November 2002 totaled SDR 137.9 (about US\$186.4 million).

² A member's quota in the IMF determines, in particular, the amount of its subscription, its voting weight, its access to IMF financing, and its allocation of SDRs.

Executive Board Assessment

Directors commended the Kyrgyz authorities for their prudent monetary and fiscal policies. While real GDP contracted somewhat in 2002, partly owing to one-time factors, it was set to grow again in 2003 at about the strong pace of the preceding five years. Inflation has fallen significantly over the same period and remains well contained, and international reserves are growing, supported by broad exchange rate stability for the som. Importantly, economic growth has reduced poverty, especially in the rural areas, and income distribution has improved.

Directors emphasized that, despite the encouraging progress seen in those areas, many challenges remain. The level of external debt remains high, more needs to be done to reduce poverty and improve social conditions, and in light of the decline in gold resources, greater diversification of the economy is needed, built on stronger small- and medium-scale enterprises. More progress in reducing corruption and state capture and improving governance is also essential to encourage private sector investment and economic diversification, and to instill greater public faith in state institutions. Directors welcomed the authorities' determination not to repeat the uneven policy implementation of previous Fund-supported programs, and to move ahead with a realistic and pragmatic policy and reform agenda.

Directors commended the authorities for meeting the current Poverty Reduction Growth Facility-supported program's fiscal targets despite the shortfall of revenue from the Kumtor gold mine. At the same time, they stressed that achieving a sustainable fiscal position over the medium term will depend crucially on further reforms in tax administration and broadening the tax base. In this context, Directors welcomed the submission to parliament of legislation to extend the VAT to large agricultural producers, while also having included in the budget measures to protect the poor from potentially higher food prices. On the expenditure side, Directors supported the authorities' intention to use the scope created by a further streamlining of the Public Investment Program and cuts in spending on less essential items to increase spending on social and poverty reduction programs.

Directors noted that the central bank's monetary policy has contained inflation while allowing for a remonetization of the economy. In view of the strong growth of the monetary aggregates, they urged the authorities to react quickly to any sign of rekindling inflation by tightening monetary conditions through open market operations. The recent issuance of marketable government securities by the Ministry of Finance to the central bank provides room for maneuver in this respect.

Directors considered that the exchange rate policy of managed floating has been successful in preventing excessive appreciation of the nominal exchange rate and thereby supporting competitiveness. They commended the authorities for their liberal trade and foreign exchange regimes.

Directors emphasized that, in light of steadily declining gold resources, diversifying the export base will be essential if the authorities' medium-term growth and poverty reduction objectives are to be attained. Improved cost competitiveness in the non-gold sector through increases in productivity, along with continued low inflation, would be important in that regard. At the same time, Directors noted that the trade restrictions and other non-tariff barriers constrain Kyrgyz export prospects in the region, and hamper the realization of the country's comparative advantage and export potential. They emphasized the importance of addressing these restrictions in the context of intensified regional cooperation.

Directors agreed that the implementation of the external debt strategy was on track, and they encouraged the government to adhere strictly to its objectives, in particular by further fiscal consolidation and by avoiding fiscal slippages in the run-up to the 2005 parliamentary and presidential elections. Directors welcomed the completion of all bilateral debt reschedulings with Paris Club creditors, and encouraged the authorities to pursue agreements with all remaining non-Paris Club creditors on comparable terms. Strong implementation of the PRGF-supported program would be the best way to encourage Paris Club creditors to exercise their goodwill clause for a debt stock relief in 2004.

Directors believed that more should be done to push forward the structural reform agenda. They stressed that strengthening governance, the legal system, and the banking sector is crucial to improving the business climate, attracting foreign direct investment, and boosting productivity. The authorities should take a firm stance against corruption and state capture, which undermine private investment and the opportunities of small and medium-size enterprises. Directors underscored the need to continue developing the still small banking sector, and address bank vulnerabilities. They urged the authorities to apply strictly the prudential regulations in order to improve public trust in banks. They welcomed the submission to parliament of a draft law on anti-money laundering and combating the financing of terrorism, in line with the recommendations of the Financial Sector Assessment Program. Directors stressed the importance of restructuring and privatizing public enterprises.

Directors commended the authorities for the broad participatory process employed in preparing the National Poverty Reduction Strategy (NPRS), which provides a comprehensive approach to poverty reduction and medium-term macroeconomic strategy. However, Directors underscored the need to strengthen costing, prioritization, and sequencing of policy measures in the NPRS, and to finalize implementation plans and monitoring and evaluation mechanisms in the NPRS Secretariat.

Public Information Notices (PINs) are issued, (i) at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies; and (ii) following policy discussions in the Executive Board at the decision of the Board.

Kyrgyz Republic: Selected Economic Indicators, 1999-2003

	1999	2000	2001	2002
				Prel.
GDP				
Nominal GDP (in billions of soms)	48.7	65.4	73.9	75.2
Nominal GDP (in millions of U.S. dollars)	1,243	1,368	1,525	1,600
Real GDP (growth in percent)	3.7	5.4	5.3	-0.5
GDP per capita (in U.S. dollars)	255	278	308	320
Prices and wages				
Consumer prices (percent change, eop)	39.9	9.6	3.7	2.3
Consumer prices (percent change, avg)	35.9	18.7	7.0	2.1
Nominal exchange rate (eop)	45.3	48.9	47.7	...
Exchange rate (soms per U.S. dollar, average)	39.1	47.8	48.4	...
Average real wage (1994=100)	118.0	120.8	133.6	...
Average monthly wage (in U.S. dollars)	24.7	24.7	28.8	...
				(In percent of GDP)
State government finances				
Total revenue and grants	17.7	15.1	17.0	19.0
Tax revenue	12.3	11.7	12.4	13.8
Total expenditure (including net lending)	30.4	24.9	22.2	24.4
Non-interest current expenditure	17.3	14.9	15.9	16.9
Public Investment Program (PIP)	9.4	6.8	4.4	5.3
Overall fiscal balance (cash basis)	-11.9	-9.2	-5.0	-5.7
Primary balance 1/	-9.0	-6.9	-3.3	-3.8
Primary balance (excl. PIP)	0.4	-0.2	1.1	1.4
				(Percent change, unless stated otherwise)
Money and credit 2/				
Reserve money (end-of-period)	23.4	12.3	11.3	42.9
Broad money (end-of-period)	33.9	12.1	11.3	35.1
Velocity of broad money 3/	8.5	10.0	9.4	7.2
Velocity of som broad money 3/	...	14.3	12.9	9.5
Money multiplier	1.6	1.6	1.5	1.4
External sector				
Export growth (goods and services, in U.S. dollars, percent change)	-11.8	8.6	-2.1	...
Import growth (goods and services, in U.S. dollars, percent change)	-24.7	-7.2	-13.8	...
Current account balance (in percent of GDP)	-15.7	-7.5	-3.3	...
Gross international reserves (months of imports, end-period) 4/	3.4	4.4	4.1	...
External debt outstanding in percent of GDP 5/	109.3	111.1	94.4	...
Debt service-to-export ratio	21.7	21.7	21.3	...

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

1/ Overall balance less accrued interest payments.

2/ Projections use program exchange rate.

3/ For 1997-2000, annualized quarterly GDP/end-of-period broad money, for 2001-2003, 12-month GDP/average broad money for last two quarters.

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

5/ Excluding Kumtor.



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FOR IMMEDIATE RELEASE
February 21, 2003

International Monetary Fund
Washington, D.C. 20431 USA

IMF Completes in Principle Second Review Under the Three-Year Poverty Reduction and Growth Facility Arrangement and Approves Request for Waiver of Performance Criterion for the Kyrgyz Republic

The Executive Board of the International Monetary Fund (IMF) today completed the second review of the Kyrgyz Republic's economic performance under the three-year Poverty Reduction and Growth Facility Arrangement (PRGF) and approved a request for a waiver for the nonobservance of the continuous performance criterion on external payments arrears. A final decision by the Executive Board is pending discussion of the Kyrgyz Republic's Poverty Reduction Strategy Paper, entitled National Poverty Reduction Strategy, by the World Bank's Executive Board. The final decision will enable the IMF to disburse an amount equivalent to SDR 11.72 million (about US\$16 million) under the arrangement.

The IMF's Executive Board approved the three-year arrangement effective on December 6, 2001 (see [Press Release No. 01/49](#)) for a total of SDR 73.4 million (about US\$100 million).

The PRGF is the IMF's concessional facility for low-income countries. It is intended that PRGF-supported programs will in time be based on country-owned poverty reduction strategies adopted in a participatory process involving civil society and development partners, and articulated in a Poverty Reduction Strategy Paper (PRSP). This is intended to ensure that each PRGF-supported program is consistent with a comprehensive framework for macroeconomic, structural, and social policies to foster growth and reduce poverty.

Following the discussion of the Executive Board, Eduardo Aninat, Deputy Managing Director, and Acting Chairman, said:

"The Kyrgyz Republic has made good progress in macroeconomic stabilization, which provides a promising base for the government's ambitious medium-term economic strategy. Prudent fiscal and monetary policies have brought down inflation and helped to stabilize the foreign exchange markets. Real GDP, which declined in 2002, is projected to return to growth in 2003. Important structural reforms to sustain growth and reduce poverty are underway.

"The medium-term challenges are demanding, however. These include the need to further reduce poverty and the external debt level, and to diversify the economy in light of the prospect of declining gold production and exports. Strong structural policies to support productivity growth and improve cost competitiveness are crucial in order to strengthen non-gold exports. The

authorities will need to devote special attention to further reforms in the areas of governance and banking, which will be particularly important to support private investment and economic diversification.

“Fiscal consolidation, together with the support of international creditors and donors, will be important to bring the external debt to more sustainable levels. Raising revenues through better tax administration and a broadening of the tax base is needed, as the room for spending cuts is limited. On the expenditure side, the streamlining of the Public Investment Program will free resources that can be devoted to social spending and poverty reduction efforts.

“Monetary policy has been successful in containing inflation while allowing remonetization of the economy, and the exchange rate policy of managed floating has prevented excessive nominal appreciation. The central bank stands ready to react promptly to any signs of accelerating inflation.

“The authorities are to be commended for completing the rescheduling agreements with all Paris Club creditors. It is to be hoped that the remaining negotiations with non-Paris Club creditors will be finalized soon and on comparable terms.

“The comprehensive approach to poverty reduction contained in the Kyrgyz Republic’s National Poverty Reduction Strategy (NPRS) document supports well the ambitious medium- term macroeconomic strategy. The NPRS will be updated, with a focus on refining costing and prioritization policies and improving the monitoring and evaluation mechanisms,” Mr. Aninat said.

**Statement by Fritz Zurbrügg, Executive Director for Kyrgyz Republic and
Narynbek Davletov, Assistant to Executive Director
February 20, 2003**

Our authorities are very grateful to the staff and management for their continuous support of the Kyrgyz Republic's economic reform effort. This contributed to achieving the status of one of the most advanced CIS countries in terms of the progress in implementing market reforms. The recent macroeconomic results, with average GDP growth close to five percent since 1997 and with end-2002 inflation declining to only 2.3 percent, also point to the benefits of pursuing sound economic policies. However, despite all the recent progress, the economic and social conditions in the Kyrgyz Republic remain very difficult. Poverty is still afflicting almost half of the population, the GDP per capita is still much below the pre-transition level and the external public debt has reached an unsustainable level. As noted by the staff, our authorities have frankly admitted that slippages and uneven speed of implementing the reform agenda, in particular in the structural area, contributed to such less than favorable results. However, given that the IMF, the World Bank and other development partners played a very active part in shaping the Kyrgyz Republic's reform program, it is important to also assess their respective roles in contributing to the final outcomes.

Implementation of the PRGF program

The staff report and the other interesting documents prepared for today's discussion provide a wealth of information on recent economic developments, progress in structural reforms and future plans for the Kyrgyz economy. Our authorities highly appreciate this comprehensive documentation, including in particular the very helpful FSSA report, and broadly share the staff assessment. They welcome the constructive attitude of the staff, which seems to be more focused on finding solutions to existing problems than on simply exposing all weaknesses and risks.

The implementation of the PRGF program approved in December 2001 has been broadly satisfactory and fully justifies the completion of the second review. All but one end-September 2002 quantitative performance criteria have been observed, in some cases with a significant margin. All structural performance criteria and benchmarks have also been fully implemented. This includes the three end-January 2003 structural benchmarks providing for the submission of the draft AML/CFT legislation, the publication of the list of 50 largest delinquent tax payers and the elimination of the specialized bank status. According to preliminary data, also most of the end-December 2002 program targets (benchmarks) have been met. Our authorities regret the temporary failure to observe the continuous performance criterion on the external debt arrears and request a waiver for the nonobservance of this program condition. The temporary and minor breach of this criterion resulted from a long-standing dispute with a European bank that provided advice of doubtful quality on one of the failed privatization deals, but was ultimately awarded compensation by an international arbitration tribunal.

As explained in the supplemental letter of intent of February 14, 2003 our authorities have also requested a slight modification of program conditionality for end-March 2003 because of an unexpected delay in fully implementing the prior action envisaged for the completion of the second review. While the 2003 budget has been approved in accordance with the program last December and includes all the agreed fiscal targets, the parliamentary approval of some of the accompanying tax legislation has been delayed. This concerns in particular the extension of VAT to large agricultural producers, which still awaits the formal decision of the upper chamber, and the legislation introducing a new property tax, which has yet to be approved by the parliament. Our authorities are fully committed to ensuring the passage of the relevant legislation by end-March 2003 and propose to make it a formal condition for the completion of the next program review. As explained by the staff, the revenue losses resulting from the delays in approving the new tax legislation are expected to be minimal and do not present any significant threat to the fiscal program. Our authorities warmly welcome staff's recommendation to complete the review despite the delay in formally adopting the new tax legislation given that the implementation of the whole program remains on track and should not be undermined by this slippage.

Fiscal Policy

The observance of the fiscal performance criteria despite the unexpected contraction in GDP is both a testimony to the authorities' commitment to the program and a clear indication that the Kyrgyz tax system has become more robust. The good revenue performance observed in 2002 despite the reductions in corporate and personal income tax rates was mainly the result of improved tax collection efforts. Improved administration also contributed to raising the customs revenue by almost 40 percent in the first three quarters of last year. With the additional tax policy measures proposed for the 2003 budget, our authorities believe that they are well on track to reaching both this year's target of 14.6 percent as well as the 15.2 percent tax revenue to GDP ratio projected for 2004. The assumed increase in tax revenue should result, among others, from the planned extension of VAT to large agricultural producers (to be implemented from April 1, 2003) and from the full recovery of production in the Kumtor gold mine. The implementation of the recently adopted resolution on reforming the Large Taxpayers Unit should also help in further improving tax collection.

Efforts to raise revenue have been accompanied by a disciplined expenditure policy. In view of the unsustainable increase in the external public debt, the state budget expenditure has been reduced from 30.4 percent of GDP in 1999 to 22.8 percent in 2001. As such a depressed level of spending could not be maintained without negatively affecting growth prospects and poverty reduction efforts, the program for 2002 envisaged a moderate increase in public spending, including on social programs. The official medium term projections assume a virtual stabilization of the expenditure to GDP ratio and a very modest and gradual increase in social spending to be made possible by a further streamlining of the public investment program (PIP) and by cuts in spending on other less essential items. In accordance with the agreed program, our authorities intend to work out and publish by end-March 2003 a Medium-Term Fiscal Framework for 2004-2006 that will aim at achieving an

average real GDP growth of 5 percent and an inflation rate of no more than 4 percent. In order to improve fiscal transparency, starting from this year the parliament is to be provided with a consolidated presentation of general government accounts.

Monetary and Exchange Rate Policies

The reduction in inflation from almost 40 percent in 1999 to 2.3 percent at the end of 2002, the relative stability of the exchange rate and the gradually growing confidence in the national currency (som) provide a clear proof that the monetary policy implemented by the National Bank of the Kyrgyz Republic (NBKR) has been successful in supporting the government's objective of establishing stable macroeconomic environment as a basis for future growth. The larger than programmed decline in inflation in 2002 occurred despite a significant acceleration in broad money growth that reflected an increased demand for money. The net international reserves (NIR) level has been maintained well above the program floor, as the NBKR continued purchasing significant amounts of foreign exchange on the market. The net domestic assets target was also reached without difficulty, in part thanks to increased government deposits in the central bank. The projections for 2003 envisage a substantial deceleration in broad and reserve money growth and a slight increase in inflation, mainly on account of the envisaged broadening of the VAT base. The NBKR intends to closely monitor the price developments and stands ready to tighten its policies in case of any risk of a more significant acceleration of inflation. The recently concluded agreement regularizing the financial relations between the Ministry of Finance and the NBKR should improve the effectiveness of the central bank's open market operations as it envisages a gradual conversion of government's obligations into marketable securities. The first phase of this operation has already been completed in December last year with the issuance of a significant amount of new treasury bills. The NBKR also intends to carefully consider the FSAP mission's recommendation to introduce a lombard facility.

In the area of the exchange rate, the NBKR intends to maintain its policy of managed floating, with interventions limited to smoothing temporary fluctuations and ensuring an adequate level of official foreign exchange reserves. Our authorities firmly believe that their overarching objective of preserving external competitiveness is better served by containing the unit labor costs increases than by allowing the exchange rate to depreciate.

Structural Reforms

The uneven implementation of structural reforms has been identified by the staff as one of the key factors explaining the Kyrgyz Republic's slower than expected transition to a fully-fledged market economy. Our authorities are fully committed to strengthening and consolidating their structural reform agenda as they recognize that further progress in this area holds the key to achieving their medium-term growth and poverty reduction targets. The crucial importance of increasing the total factor productivity has been clearly shown by the results of the staff's interesting study on the sources of growth. The full observance of all structural performance criteria and benchmarks during the first year of the PRGF program should be seen as a manifestation of our authorities' renewed commitment to advancing

structural reform. This should serve the long-term objective of increasing the efficiency and competitiveness of the Kyrgyz economy.

During the second year of implementing the PRGF program our authorities intend to focus their structural reform efforts on strengthening governance and advancing the restructuring of the banking sector. The measures envisaged in the latter area aim at reducing the vulnerabilities identified in the FSSA report by further increasing banks' capital base, improving the efficiency of banking supervision and strengthening the Debt Restructuring Agency (DEBRA). Our authorities will also develop specific plans to restructure and/or privatize the two remaining state-owned banks (Kairat and SSC).

The efforts in the area of governance will mainly aim at improving the business and investment climate and will focus on such areas as building institutions for good governance, improving efficiency of public administration, strengthening corporate governance and reforming judiciary system. Special attention will be given to addressing the problem of corruption and eliminating all barriers to private domestic and foreign investment.

Our authorities intend to continue their privatization program and expand it to include some strategic sectors. The first significant step has been made in September with the announcement of the tender for KyrgyzTelecom. Our authorities are cooperating with the World Bank in elaborating various options for the privatization of the energy sector. Given the complexity of this undertaking and the currently uncertain market conditions, our authorities welcome the staff's pragmatic approach to setting the program conditionality in this area.

External Sector Policies

Last year's improvement in the external current account position, despite large declines in exports of gold and energy, can be seen as an important achievement and as proof of the potential to develop non-traditional sources of foreign exchange earnings. However, the declining trend in exports revenue and the continuing large dependence on a small number of potentially unstable export items remain a source of concern. Our authorities intend to address this problem by actively promoting the diversification of production and exports structures and by maintaining an adequate level of external competitiveness. They also intend to preserve the Kyrgyz Republic's liberal trade regime, make fuller use of the WTO membership and promote regional cooperation. As documented by the staff's helpful background studies, the recent unsatisfactory export performance cannot be explained by developments in competitiveness but can, to some extent, be attributed to various restrictions on transit and bilateral trade imposed by the neighboring countries. Our authorities plan to seek a solution to this problem by intensifying bilateral dialog and by trying to make broader use of the already existing regional free trade arrangements but they also count on the support of the international community, including through the CIS-7 process.

The rescheduling agreement with the Paris Club has significantly alleviated the current debt servicing burden and facilitated the financing of the PRGF program. Our authorities have already concluded all bilateral agreements with Paris Club members and are

actively seeking similar understandings with remaining bilateral creditors. However, the unsustainable external debt can still be seen as a Damocles sword threatening the achievement of the Kyrgyz Republic's long-term development goals. Our authorities multi-pronged strategy to address this problem envisages, among others, the continuation of fiscal adjustment and significant restrictions on new external borrowing, including a ban on contracting new loans on commercial terms and a requirement to secure at least 45 percent of grant element in concessional loans. Also, 75 percent of receipts from future large privatizations should be set aside and used for debt reduction. However, all these internal efforts will not be sufficient to achieve a sustainable debt position and further international support through the contemplated Paris Club debt stock reduction will be necessary to complement these domestic efforts and provide a comprehensive and lasting solution of the Kyrgyz debt problem.

National Poverty Reduction Strategy

The recently achieved tangible progress in reducing poverty (from 55.3 percent in 1999 to 47.6 percent in 2001) and the further improvement in income distribution belong to the most encouraging developments during the latest phase of the Kyrgyz Republic's economic and social transformation. The comprehensive National Poverty Reduction Strategy (NPRS) developed by our authorities through an open and participatory process intends to build on this progress and achieve a further improvement in several social indicators, including reduction in the incidence of poverty to 39 percent in 2005. A special feature of the Kyrgyz NPRS is its strong link with the all-encompassing long-term development vision provided by the Comprehensive Development Framework. An attempt has also been made to link the NPRS objectives to the achievement of the Multilateral Development Goals. The Consultative Group Meeting held in Bishkek in October 2002 helped to shape the final version of the NPRS and proved that the adopted targets enjoy the support of the international community. The three main pillars of the NPRS encompass fostering economic growth and creating employment opportunities, improving efficiency and equity of social protection and human development, and improving governance and efficiency of the public sector.

Our authorities agree that the targets set out in the NPRS are ambitious but they can also be considered indispensable and realistic. The attainment of the envisaged reduction in poverty by about 3 percentage points annually presupposes the maintenance of an average GDP growth rate of about 5 percent. With the planned intensification of the structural reform effort, the achievement of such growth rates could be considered feasible. However, our authorities are fully aware that in view of the Kyrgyz Republic's large vulnerability to external shocks and natural disasters there is a need to strengthen the economy's resilience and to avoid any slippages in the implementation of the economic reform agenda. Our authorities also hope that the international community will continue offering its strong support to the implementation of the NPRS, including through an increased provision of grant resources. The requested completion of the second PRGF review would also contribute to promoting macroeconomic stability and thereby facilitating the achievement of our authorities' poverty reduction targets.