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Kyrgyz Republic: Fourth Review Under the Three-Year Arrangement Under the Poverty Reduction and Growth Facility and Request for Modification of Quantitative Performance Criteria—Staff Report; Staff Statement; Press Release on the Executive Board Discussion; and Statement by the Executive Director for the Kyrgyz Republic

In the context of the fourth review under the three-year arrangement under the Poverty Reduction and Growth Facility and request for a modification of quantitative performance criteria, the following documents have been released and are included in this package:

- the staff report for the Fourth Review Under the Three-Year Arrangement Under the Poverty Reduction and Growth Facility and Request for Modification of Quantitative Performance Criteria, prepared by a staff team of the IMF, following discussions that ended on February 28, 2007, 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 May 2, 2007. 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 statement of May 18, 2007 updating information on recent developments;
- a Press Release summarizing the views of the Executive Board as expressed during its May 18, 2007 discussion of the staff report that completed the review; and
- a statement by the Executive Director for the Kyrgyz Republic.

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

Joint Staff Advisory Note of the Poverty Reduction Strategy Paper
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*
Poverty Reduction Strategy Paper—Country Development Strategy
Technical Memorandum of Understanding*
*Also included in Staff Report

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

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INTERNATIONAL MONETARY FUND

KYRGYZ REPUBLIC

Fourth Review Under the Three-Year Arrangement Under the Poverty Reduction and Growth Facility and Request for Modification of Quantitative Performance Criteria

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

Approved by David Owen (MCD) and Scott Brown (PDR)

May 2, 2007

EXECUTIVE SUMMARY

The authorities have maintained fiscal discipline and met all end-December 2006 quantitative PCs. Output is rebounding and inflation remains subdued. However, most end-December 2006 and end-March 2007 structural benchmarks have been missed, partly because of political tensions that slowed the legislature.

The 2007 program, which targets 6½ percent output growth and 5 percent inflation, caps the fiscal deficit at 3.1 percent of GDP and maintains a prudent monetary policy. The government plans to implement delayed structural measures under the program, deepen financial sector and public financial management reforms, and strengthen external debt management. Steadfast implementation (with donor assistance) of other reforms to improve the business climate, stamp out corruption, rehabilitate the energy sector, and enhance social services would facilitate the achievement of rapid sustained growth and ease the external debt burden, despite the country's decision to forego HIPC/MDRI debt relief.

Risks in the outlook would be mitigated by reducing political tensions, forging internal support for reform, and reducing the vulnerability to external shocks. On balance, staff considers these risks manageable and recommends completion of the fourth review under the PRGF arrangement.

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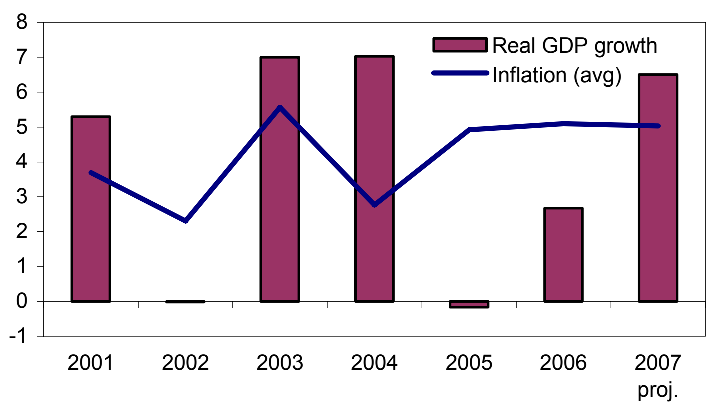
Attachments

I. Recent Developments and Performance Under the Program

1. **The authorities have continued to maintain macroeconomic discipline and the PRGF-supported program remains on track.** All end-December 2006 quantitative performance criteria (PCs) were met, in most cases by wide margins (Table 1). However, as tensions between the government and parliament delayed passage of important legislation, most structural benchmarks for end-December 2006 and end-March 2007 were missed (including, those on enhancing the NBKR's autonomy, preparing for privatization of the Kyrgyz Agricultural Finance Corporation (KAFC), and securing passage of a new tax code) (Table 2).

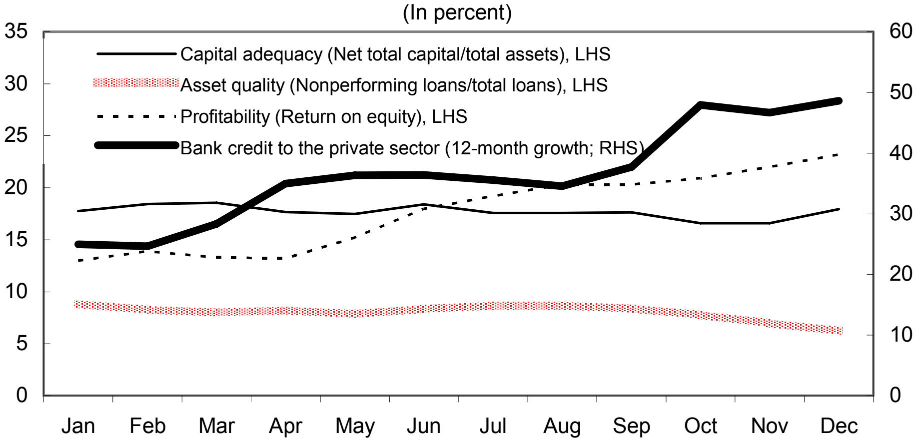
2. **Activity started to rebound in 2006, after a slight contraction in 2005,** with nongold output growth of 5.1 percent. Total output only grew by 2.7 percent, dampened by a gold mine accident. Despite a rapid increase in monetary aggregates stemming from large NBKR unsterilized intervention, inflation has remained subdued due to continued remonetization—with a rise in consumer prices by 5.1 percent during 2006 (compared with the program's 5.7 percent target) and by 4 percent during the 12 months to March 2007 (Figure 1). Reserve money grew by 47.5 percent in 2006 and 44.5 percent in the 12 months to March 2007. Credit to the private sector has also been rising rapidly (56 percent year-on-year in February 2007), albeit from a low base, thus far without a significant worsening in the quality of loan portfolios (Figure 2).

Figure 1. Real GDP Growth and CPI Inflation, 2001–07



Source: Kyrgyz authorities; and Fund staff projections.

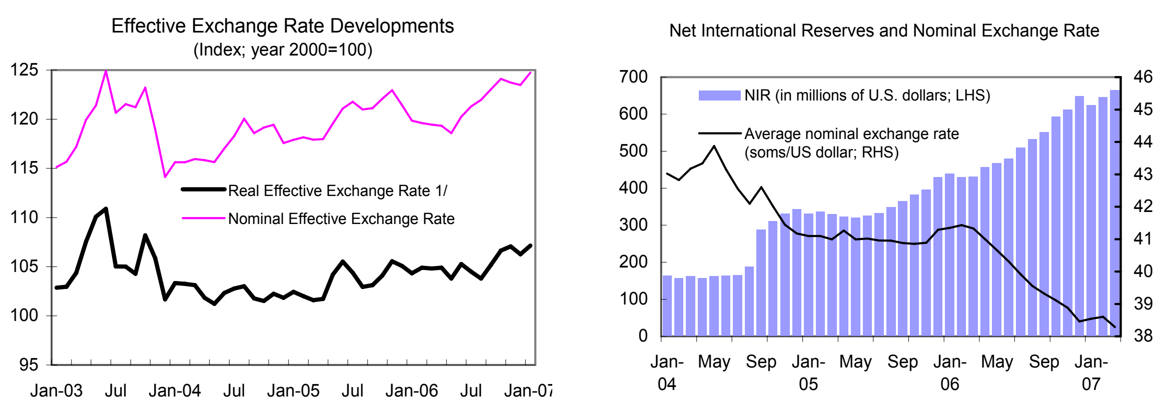
Figure 2. Credit Growth and Bank Performance, 2006
(In percent)



Source: Kyrgyz authorities.

3. **Despite the NBKR's intervention, the som appreciated by 8 percent against the U.S. dollar during the year, but the real effective appreciation has been modest,** partly because of a strengthening of the currencies of major trading partners, such as Kazakhstan and Russia (Figure 3). Owing to rising imports and an accident-related shortfall in gold exports, the external current account deficit widened to 16¾ percent of GDP in 2006. Nevertheless, sizable short-term capital inflows (including errors & omissions that partly reflect unrecorded remittances and shuttle trade re-exports) led to a faster-than-expected buildup in foreign reserves. At end-March 2007, gross reserves amounted to $816 million, or 3.5 months of projected 2008 imports of goods and services.

Figure 3. Exchange Rate Developments



Source: INS database.
1/ Against 20 major trading partners. Increase indicates appreciation.

Source: Kyrgyz authorities.

4. **The overall general government deficit (2.3 percent of GDP) and the primary balance before grants (2.2 percent) were lower than projected in 2006.** This reflected strong revenue gains despite a 2 percentage-point cut in the rate of social security contributions during the year. The strong revenue performance and shortfalls in capital expenditure more than offset overruns in current outlays in 2006, and tax receipts during the first quarter of 2007 have remained buoyant. The indicative limit on the electricity sector's quasi-fiscal deficit (QFD) in 2006 was also met.

5. **Political tensions over the past several months have distracted the authorities, delayed passage of key legislation and prompted the government's decision to forego HIPC/MDRI debt relief.** Moreover, recent changes in the structure of government, including a shift of some Finance Ministry responsibilities to a new Ministry of Economy and Trade, have complicated policy coordination. The country has undergone two constitutional reforms, and tensions between the government and parliament have sparked demonstrations by the opposition and two cabinet reshuffles, the latest one involving the appointment in March 2007 of a new cabinet led by Prime Minister Almaz Atambaev. After the mission's departure, parliament reduced the retirement age (overturning an earlier presidential veto) and introduced a bill proposing nationalization of the mining industry.

II. Report on the Discussions

A. Overview

6. **Policy discussions took place in the wake of the country's decision to forego HIPC/MDRI debt relief.** The government has updated the Country Development Strategy (CDS) to address the diminished longer-term resource envelope, while seeking to spur private sector-led growth through new initiatives (e.g., fostering SME development; expediting privatization; and attracting FDI and loans from regional creditors to develop manufacturing and natural resource-based projects).[1] Moreover, the authorities sent to parliament a capital amnesty bill, hoping to foster capital repatriation and a one-off spike in tax receipts.

7. **The economic program for 2007 targets 6½ percent output growth, driven by the industrial and construction sectors and a rebound in gold production.** The program seeks to keep inflation around 5 percent and secure a foreign reserve gain to maintain end-year reserve coverage at 4 months of projected 2008 imports. The external current account deficit would narrow to 12½ percent of GDP from 16¾ percent in 2006, on the back of a recovery in gold exports and buoyant nongold exports and remittances. Fiscal and monetary

[1] For details, see the JSAN of the CDS (Kyrgyz Republic—Poverty Reduction Strategy Paper—Joint Staff Advisory Note, April 27, 2007 (www.imf.org)).

prudence will continue to underpin macroeconomic stability, and the government is committed to implementing further reforms to foster financial deepening and enhance public financial management (Box 1).

Box 1. Public Financial Management (PFM) Reforms

The authorities recognize the need for improvements in PFM to facilitate economic growth and poverty reduction. In particular, frequent and nontransparent budget revisions make budget execution at the sectoral level unpredictable, while accountability for use of resources is weakened by lack of robust internal controls and a modern accounting framework.

The authorities are implementing a PFM reform action plan supported by major donors, which includes (i) government ownership; (ii) coordinated donor support; and (iii) benchmarking and measurement of progress based on the Public Expenditure and Financial Accountability (PEFA) indicators. The priority is to address basic obstacles to the implementation of budgets in a predictable way and with a solid internal control framework. Progress will depend on the ability to reinforce ownership, retain qualified Finance Ministry staff, and upgrade managerial and technical capacity.

Going forward, the focus within the PFM action plan will be to (i) enhance tracking and reporting of poverty related expenditure; (ii) submit to parliament amendments to the basic budget law, to clearly define and limit changes to the budget during execution, and to ensure prior parliamentary approval of all supplementary budgets; (iii) introduce a chart of accounts and accounting standards for all public agencies consistent with international public sector accounting standards; and (iv) develop general standards, methodology and an appropriate institutional framework for internal controls, consistent with international internal audit standards. The authorities plan to issue an updated Medium-Term Budgetary framework in May 2007 that will include economic, functional and administrative summaries of expenditures, and will be better aligned with the annual budget process and PRSP priorities.

B. Fiscal and Quasi-Fiscal Issues

8. **The overall government deficit will be capped at 3.1 percent of GDP in 2007,** and will be financed mostly from external sources and privatization receipts (Table 4)**.** The budget is premised on further revenue gains to keep the tax-to-GDP ratio broadly unchanged, despite an additional 2 percentage-point reduction in the rate of social fund contributions, to 27 percent. The medium-term revenue effort will be underpinned by introduction of a new tax code and further improvements in tax and customs administration. The authorities plan to phase out gradually the cascading and distortionary Road and Emergency Fund taxes from 2008, but they may advance this if revenue performance significantly exceeds expectations.

9. **On the expenditure side, the budget envisages no general wage increase,** but includes wage hikes of 50 percent for Interior Ministry and corrections personnel and 30 percent for cultural and social sector employees. The increases would raise the wage bill to 7.6 percent of GDP—a relatively high level compared to other CIS countries in the region. The authorities plan to launch a civil service reform (CSR) that could check the wage bill drift over time, although allowing further selective increases to senior staff and specialized professionals. However, they have yet to develop their CSR strategy and indicated that no

significant retrenchments are expected in the immediate future, owing to the increase in positions associated with the recent creation of new ministries and agencies.

Wage Bill in CIS Countries, 2007
(General Government; in percent of GDP)

Armenia	4.3
Azerbaijan	4.9
Georgia	3.5
Kazakhstan	3.4
Kyrgyz Republic	**7.6**
Tajikistan	4.4
Turkmenistan	6.5
Uzbekistan	8.9

Source: Country authorities and Fund staff estimates.

10. **The budget also includes a 15 percent increase in pensions,** bringing the cumulative increase over the past three years to 44 percent by year's-end (a 24 percent increase in real terms, albeit from a low base). After the mission's departure, parliament reduced the retirement age by three years, to 60 years for males and 55 years for females, reversing an earlier presidential veto. The authorities have indicated that this measure will be phased in over a three-year period and could cost 0.3 percent of GDP in 2007, with additional longer-term costs yet to be clarified. They noted that they are reviewing possible short-term offsetting measures, such as an effort to raise the remuneration of social fund deposits; sale of social fund assets; and intensification of the fund's revenue effort. The authorities also plan to secure minor savings in transportation outlays for senior officials and other non-essential current spending. Staff encouraged the authorities to formulate a comprehensive blueprint for pension reform (with World Bank assistance) to put the social fund finances on a sound footing and foster development of domestic capital markets, possibly by creating voluntary private pension funds. The fiscal cost of transitioning to this mixed system and offsetting measures to safeguard overall fiscal stability should be incorporated into the Medium-Term Budgetary Framework (MTBF).

11. **In line with the fiscal decentralization mandated by parliament, the 2007 budget introduces a two-tier system comprising the center and municipalities** (Box 2). The authorities are taking precautionary steps to forestall a loss of fiscal control, but recognize that effective fiscal decentralization hinges on capacity building and clear demarcation of each tier's fiscal competencies. Meanwhile, they are introducing reforms in public financial management and refining the fledgling MTBF (MEP, ¶ 9).

Box 2. Fiscal Decentralization

Parliament passed a law in 2003 mandating far-reaching fiscal decentralization, which the government is starting to implement. Under the new system, comprising the center and municipalities, resources available to the latter will comprise their actual own revenues, as well as *categorical grants* earmarked to education and formula-based *equalization grants.* By contrast, under the previous four-tier system the central government, together with provincial (*oblast*) and regional (*rayon*) administrations, essentially framed municipal budgets. After the new system is fully developed, municipalities should be able to prepare their own budgets and transparently execute them, subject to a few basic rules, and the size of each municipality's equalization grant will be determined through a transparent formula.

The authorities have indicated that extensive capacity building will be required at the center and municipal levels (external donors have provided limited training to municipalities in generic budget issues), and that conceptual and operational issues remain to be clarified before the system becomes fully operational. In particular, they need to specify (i) the scope and criteria for municipal requests for unforeseen changes in quarterly equalization grant allocations; (ii) sanctions on the Finance Ministry untimely or incomplete allocation of equalization grants; (iii) accountability for the use of funds and safeguards to forestall the accumulation of local government arrears; and (iv) each tier's responsibilities for service delivery. To maintain macro economic stability, some of the local government economic and financial bodies will remain under the Finance Ministry's supervision until local capacity is built.

12. **The government is contemplating creation of a Development Fund (DF) that would on-lend resources to the financial system and be fully integrated into the budget** (MEP, ¶ 6). Loanable resources could include the public sector's shares in the Centerra mining conglomerate (which operates Kumtor, the principal gold mine), and other privatization receipts. Staff advised the authorities to carefully weigh the risks of directed credits, and to minimize them by introducing appropriate fiduciary safeguards and fully integrating the DF (if passed by parliament) into the annual macroeconomic programs. Meanwhile, the status of this proposal is uncertain, in light of differences of views within the cabinet and the recent tabling of a bill by an opposition MP that would effectively nationalize the country's gold mines.

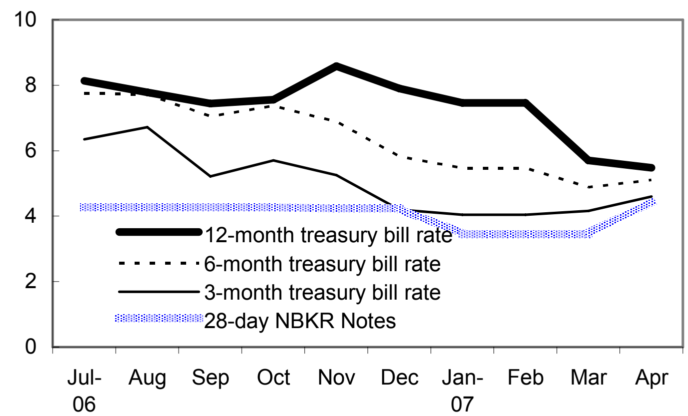
13. **The government has discussed an energy sector action plan with World Bank staff,** which envisages phased power tariff hikes to cost-recovery levels by 2010 (after a de facto tariff freeze since 2002), accompanied by social safety nets (MEP, ¶ 10). Meanwhile, pending final government approval of the plan, the authorities have targeted a decline in the electricity sector's quasi-fiscal deficit (an indicative program target) to under 5½ percent of GDP in 2007.

C. Monetary and Financial Sector Issues

14. **The monetary program, premised on further remonetization of the economy, sets limits on the NBKR's net domestic assets consistent with reserve money growth of 25 percent and broad money growth of 30 percent.** To strengthen liquidity management, the NBKR will further enhance its current indirect monetary control instruments (repos, deposit auctions and central bank notes), drawing on the recommendations of an upcoming

MCM TA mission. The authorities also plan to maintain the managed exchange rate float regime—essentially smoothing exchange rate fluctuations and reducing recourse to unsterilized intervention. Staff also advised the authorities to stand ready to raise policy interest rates (which have declined somewhat since end-2006) as needed, to keep liquidity expansion in check (Figure 4).

Figure 4. Policy Interest Rates, 2006–07



Source: Kyrgyz authorities.

15. **The authorities plan to deepen financial sector reforms.**[2] They will step up supervision; introduce a mandatory deposit insurance scheme for small depositors in 2008; enhance the payment system; and create a sound framework to foster term lending and capital market development (Box 3 and MEP, ¶ 12–14). The authorities reiterated their intention to eventually privatize the former KAFC, but they are now reviewing the company's privatization strategy in consultation with the World Bank and the EBRD. The NBKR expected the independent review of its internal audit function to be completed shortly (MEP, ¶ 11). Staff underlined the importance of securing passage of pending legislation to strengthen the central bank's autonomy, although the authorities noted that parliamentary support for this bill was weak.

[2] For details, see the Financial System Stability Assessment Update (Kyrgyz Republic—Financial System Stability Assessment—Update, May 3, 2007 (www.imf.org)).

Box 3. Financial Sector Reforms

I. Strengthening the legal framework and central bank independence

- A bill before parliament would amend the central bank's charter to enhance its autonomy.
- To underpin finality of bank resolution, the NBKR has proposed further amendments to the bank bankruptcy law. The authorities have also amended the civil code and the collateral law to facilitate use and seizure of collateral.
- Following passage of new AML/CFT legislation, the NBKR, the Service for Supervision and Regulation of Financial Market (SSRFM) and the Financial Intelligence Unit have developed regulations for bank reporting under the law and enabling amendments to the criminal code.

II. Stepping up financial sector supervision

- The NBKR and the SSRFM continue to strengthen supervision. The NBKR has introduced regulations for consolidated supervision in line with Basel Core Principles for Effective Banking Supervision, and tightened on- and off-site assessments of prudential requirements. It has also developed a framework for assessing market, country and transfer risks of banks, and instructed banks to closely track these risks and maintain adequate capital to cover them.
- The NBKR increased minimum capital requirements on existing banks to som 60 million ($1.5 million) in 2006, to be further increased to som 100 million in 2008. The floor for new banks remains at som 300 million.
- The NBKR has started to develop a supervision framework for Islamic banking.

III. Bolstering indirect monetary control instruments and enhancing the payment system

- The NBKR introduced deposit auctions as a new monetary control instrument (besides repos and central bank notes) in 2006. It plans to take further steps to enhance liquidity management, drawing on recommendations of the upcoming MCM TA mission and the ongoing MCM regional TA on debt management and securities market development.
- The NBKR has maintained a trading platform and acted as a depository for government securities, and initiated payment of salaries and utilities through the banks. It will launch a Real-Time Gross Settlement system in 2008.
- The NBKR is poised to introduce mandatory deposit insurance for small depositors in 2008.
- The NBKR will sponsor legislation to facilitate the use of bank accounts (including demand deposits) for settlement purposes by legal entities and individuals.

D. Other Issues

16. **The authorities hope to lessen the external debt burden in the coming years by maintaining prudent macroeconomic policies, promoting rapid economic growth, and further strengthening external debt management.** They pointed to the latest joint Fund/Bank debt sustainability analysis (LIC DSA) presented last fall (Country Report No. 07/135), which suggests that these mutually reinforcing policies would gradually put the debt ratios on a downward and more sustainable path. They hoped that, by end-2007, all the critical NPV of debt ratios would already show a significant decline, as a result of the economic recovery and further tax revenue gains. Furthermore, they noted that their updated external debt management strategy (which is expected to be implemented shortly) would maintain the 45 percent minimum grant element on any new public borrowing, strengthen risk assessment of external loans, and tighten supervision of external borrowing by public enterprises. While commending the authorities for their commitment to prudent policies and

enhanced debt management, staff cautioned that the country would remain at a high risk of debt distress, unless the vulnerability to exogenous shocks and policy reversals was lessened by economic diversification and broader internal political support for economic reform.

17. **The authorities are requesting small modifications to the end-June 2007 program limits on the central bank's NIR and NDA and the floor on tax collections**, as well as to the indicative limit on reserve money. To better align the fiscal stance with the goal of securing debt sustainability, they also wish to treat the overall general government deficit (instead of the general government primary deficit before grants) as the fiscal indicator to be monitored henceforth as a performance criterion under the program.

III. Staff Appraisal

18. **Macroeconomic performance under the PRGF-supported program in 2006 and the year-to-date has been good.** Real GDP growth last year was dampened by an accident in a major gold mine, but the recovery in other sectors has gained momentum. Moreover, despite a turbulent political environment, the authorities have maintained fiscal discipline and kept inflation subdued. All end-December 2006 quantitative PCs have been met comfortably, and preliminary data suggest that the end-March 2007 indicative targets have also been met.

19. **Nevertheless, tense government relations with parliament and civil society have hampered the implementation of the reform agenda,** as evidenced by nonobservance of six structural benchmarks. Moreover, the government backed off under political pressure from its earlier decision to request HIPC and MDRI debt relief, which would have helped secure debt sustainability and create fiscal space for pro-poor spending. Some initiatives with potentially serious economic downsides have recently been passed or tabled in parliament, including a reduction in the retirement age.

20. **Against this backdrop, the authorities' updated economic program for 2007 seeks to underpin macroeconomic stability by continued fiscal and monetary prudence.** Inflation is targeted at 5 percent and real GDP growth at 6½ percent, and a further reserve gain would keep gross reserve coverage at a comfortable level. To achieve these goals, the overall fiscal deficit will be capped at 3.1 percent of GDP.

21. **In the fiscal area, the government needs to forestall an upward drift in current spending by refraining from further wage and pension hikes and retrenching redundant personnel.** There is also a need to bolster expenditure controls and the Medium-Term Budgetary Framework, and to deepen other public financial management reforms. In the face of expenditure pressures, it will be particularly important to further strengthen tax administration, especially by securing prompt passage of the new tax code and resisting pressures to dismantle the Large Taxpayers Unit.

22. **Safeguarding fiscal stability also hinges on limiting the fallout from the recent reduction in the retirement age.** The authorities' decision to phase in the provisions of the

new law over a three-year period is a welcome first step, which needs to be accompanied by offsetting actions to keep the programmed fiscal path on course. Moreover, the government should rally broad support for a comprehensive pension reform geared at securing long-term financial viability of the pension system.

23. **To keep inflation in check, the central bank needs to moderate the increase in monetary aggregates,** by largely refraining from unsterilized intervention, continuing to enhance indirect monetary control instruments, and raising policy interest rates. Staff commends the authorities for the important steps taken thus far to bolster supervision and modernize the financial system. Going forward, staff advised the authorities to consolidate these reforms and to implement expeditiously the delayed measures envisaged in the program—especially enhancing the NBKR's autonomy and privatizing KAFC.

24. **While the administration has an impressive record of macroeconomic discipline, much remains to be done to achieve the rapid sustained growth required to raise living standards and ease the debt burden.** These challenges are compounded by the diminished resource envelope as a result of the decision taken early this year to forego HIPC/MDRI debt relief. In these circumstances, the reform blueprint discussed with donors in late 2006 (as possible HIPC conditionality) continues to serve as a solid springboard for action. The authorities would now be advised to fully develop their reform agenda in advance of a Development Forum (including senior government officials, parliamentarians, donors and NGOs), which they plan to host in Bishkek at end-May. In particular, the authorities should focus on enhancing the business climate (including by resisting pressures to nationalize the mining industry); fostering good governance and transparency in public sector operations; rehabilitating the energy sector and implementing the long delayed increases in electricity tariffs; and improving the targeting and delivery of social services. In addition, the authorities need to refine the external debt management framework and persevere in building central and local government capacity.

25. **Periodic clashes between the government and the opposition, which have distracted the authorities' attention, highlight the urgency of resolving these tensions and rallying internal support for reforms.** The country's vulnerability to external shocks also poses a risk that could be further exacerbated by populist initiatives to increase state intervention in the economy—including in the key mining sector. In the staff's views, these risks remain manageable and will be mitigated by continued engagement of the Fund and other donors in support of the government's adjustment effort. On this basis, staff recommends completion of the fourth review under the PRGF arrangement.

Table 1. Kyrgyz Republic: Quantitative Program Targets for 2005–07 1/

(In millions of soms, unless otherwise indicated; eop)

	2005	2006			2007	
	December	December			June	Dec.
	Actual	IMF/CR/06/235 2nd Review	IMF/CR/07/135 3rd Review	Act.	Rev. Prog.	Prog.
I. **Performance criteria**						
1. Floor on net international reserves of the NBKR in convertible currencies (eop stock, in millions of U.S. dollars)	416	457	518	606	658	787
2. Ceiling on net domestic assets of the NBKR (eop stock)	-1,943	-1,469	-2,034	-2,559	-1,094	-1,769
3. Ceiling on cumulative primary deficit of the general government	3,229	3,701	3,221	2,459	...	...
4. Ceiling on cumulative overall deficit of the general government	...	...	...	...	1,665	3,937
5. Cumulative floor on state government tax collections in cash	16,361	17,650	18,431	19,981	10,246	23,141
6. Ceiling on the stock of central government budget arrears	0	0	0	0	0	0
7. Ceiling on the stock of Social Fund pension arrears	0	0	0	0	0	0
8. Cumulative floor on payroll collections in cash of the Social Fund	4,912	4,823	4,945	5,528	2,864	5,738
9. Ceiling on the stock of Social Fund arrears to the Medical Insurance Fund	0	0	0	0	0	0
10. Ceiling on contracting or guaranteeing by the state government, NBKR or any other agency acting on behalf of the state government, of new nonconcessional external debt with maturity of less than one year (continuous, in millions of U.S. dollars)	0	0	0	0	0	0
11. Ceiling on contracting or guaranteeing by the state government, NBKR or any other agency acting on behalf of the state government, of new nonconcessional external debt with maturity of one year or more (millions of U.S. dollars)	0	0	0	0	0	0
12. Ceiling on accumulation of new external payment arrears (continuous, in millions of U.S. dollars)	0	0	0	0	0	0
II. **Indicative targets**						
1. Ceiling on reserve money (eop stock)	15,466	17,708	19,642	22,806	24,177	28,499
2. Ceiling on the cumulative quasi-fiscal deficit of the electricity sector (in millions of soms)	7,609	6,509	6,509	6,127	3,822	6,633
3. Ceiling on contracting or guaranteeing by the state government or NBKR of new concessional external debt (in millions of U.S. dollars) 2/		(as specified in the TMU)				

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

1/ Definitions are provided in the TMU.
2/ New concessional loans during the year.

Table 2. Kyrgyz Republic: Structural Conditionality

I. September–December 2006

Structural benchmarks for end-September 2006

- Prepare an action plan to reduce the energy sector's quasi-fiscal deficit in close cooperation with World Bank staff, addressing problems of transmission and distribution losses, payment indiscipline, and tariff adjustment. [Observed]

- Expand the operation of the Large Taxpayers Unit to cover at least 60 percent of tax revenues. [Observed]

Structural benchmarks for end-December 2006

- Conduct an independent review of the NBKR's internal audit function. The review could be performed by the internal audit department of another central bank, and should include a review of the capacity of the NBKR's internal audit division, as recommended by the Safeguards Assessment Report conducted by Finance Department in 2005. [Not observed]

- Bring KAFC to the point of sale and issue a privatization tender for the company. [Not observed]

- Submit to IMF staff a report prepared by the ministry of labor and social protection recommending measures to improve labor market flexibility. [Observed]

- Secure approval of legislation that has been already sent to parliament to enhance the NBKR's legal independence and ensure legal protection of its employees in performing official duties. [Not observed]

II. March–December 2007

Structural benchmarks for end-March 2007

- The government will submit to parliament amendments (drafted by the NBKR) to the civil, housing and land codes, as well as to all the laws governing collateral, in order to harmonize provisions on collateralized lending by financial institutions and facilitate collateral seizure in cases of default. [Not observed]

- Approval of the tax code bill that is before parliament. [Not observed]

- The government will adopt a new medium-term external debt management strategy aimed at ensuring external debt sustainability as described in paragraph 24 of the MEP for the third review under the arrangement. [Not observed]

Structural benchmarks for end-June 2007

- The NBKR will implement regulations for consolidated supervision to monitor risks faced by financial institutions, in line with the recommendations of the 2005 Basel Core Principles for Effective Banking Supervision Assessment.

- The government will introduce a new and detailed budget classification, based on the best practice reporting of government finances (GFS 2001), which will permit monitoring of poverty reducing expenditures in the monthly budget execution reports.

Table 2 (Concluded). Kyrgyz Republic: Structural Conditionality

Structural benchmarks for end-September 2007

- Submit to IMF staff a written Memorandum of Understanding agreed between the NBKR and the Service for Supervision and Regulation of Financial Market (SSRFM), delineating the specific supervisory responsibilities of the SSRFM and establishing modalities for information-sharing between them, as recommended by the FSAP update mission.

- Submit to parliament an internal audit law for government agencies in line with best international audit practices, in order to establish an appropriate framework for internal public sector controls.

Structural benchmarks for end-December 2007

- To ensure finality of bank resolution, the government and the NBKR will secure parliamentary approval of further amendments to the bank bankruptcy law modifying the provisions introduced in September 2006, which allowed reinstatement of banks that are insolvent and in the process of liquidation.

- Submit to IMF staff a best-practice, time-bound action plan to modernize customs administration, including greater selectivity of customs control based on risk criteria and expanding post-clearance audits.

- Submit to parliament enabling legislation to enhance flexibility in the use of bank accounts (including demand deposits) for settlement purposes by legal entities and physical persons.

Table 3. Kyrgyz Republic: Selected Economic Indicators, 2004–08

	2004	2005	2006		2007	2008
	Actual		IMF/CR/06/235 2nd Review	Prel.	Projections	
Nominal GDP (in billions of soms)	94.4	100.9	111.1	113.2	126.6	140.4
Nominal GDP (in millions of U.S. dollars)	2,215	2,460	2,646	2,822	3,287	3,646
Real GDP (growth in percent)	7.0	-0.2	5.0	2.7	6.5	6.6
GDP per capita (in U.S. dollars)	435	477	508	542	624	685
Consumer prices (percent change, eop)	2.8	4.9	5.7	5.1	5.0	4.0
Consumer prices (percent change, average)	4.1	4.3	5.7	5.6	5.0	4.0
Producer prices (percent change, eop)	4.3	6.0	...	10.4	…	5.0
Producer prices (percent change, average)	9.0	2.6	...	15.3	…	5.0
Unemployment rate	9.0	9.7	...	...	...	...
Poverty rate (consumption approach)	46	44.0	...	...	...	...
Investment and savings (in percent of GDP)						
Investment	20.8	21.6	22.6	23.4	23.6	24.6
Public	4.9	4.8	4.4	4.5	5.6	5.8
Private	16.0	16.8	18.2	18.9	18.0	18.8
Savings	17.4	19.3	15.8	6.6	11.0	13.8
Public	-0.1	0.6	0.9	2.0	2.1	2.8
Private	17.5	18.7	14.9	4.6	8.9	11.0
Savings/Investment balance	3.5	2.3	6.8	16.8	12.6	10.8
General government finances (in percent of GDP) 1/						
Total revenue and grants	23.3	24.7	24.0	26.6	27.6	28.2
of which: Tax revenue	18.3	20.0	19.2	21.5	21.6	21.5
Total expenditure (including net lending)	27.7	28.4	27.1	28.8	30.7	30.6
of which: Current expenditure	23.3	24.1	23.1	24.6	25.6	25.3
Capital expenditure	4.9	4.8	4.4	4.5	5.6	5.8
Overall fiscal balance	-4.4	-3.7	-3.1	-2.3	-3.1	-2.5
Primary balance	-3.1	-2.2	-4.3	-1.4	-2.1	-4.0
Banking sector 2/						
Net foreign assets (percent change, eop)	108.7	20.1	12.5	50.6	28.0	3.6
Net domestic assets (percent change, eop)	-52.3	54.5	35.4	68.7	37.6	112.8
Credit to private sector (in percent of GDP)	7.0	8.0	8.6	11.0	11.8	16.6
Broad money (percent change, eop)	33.6	25.5	17.0	54.1	30.0	28.2
Velocity of broad money 3/	5.6	4.7	4.4	3.8	3.0	2.6
Interest rate 4/	24.3	25.7	...	23.5	...	...
External sector						
Current account balance (in percent of GDP)	-3.5	-2.3	-6.8	-16.8	-12.6	-10.8
Export of goods and services (million USD)	943	942	1,072	1,158	1,419	1,636
Export growth (percent change)	26.0	-0.1	13.8	22.9	22.5	15.3
Import of goods and services (million USD)	1,127	1,397	1,607	2,223	2,535	2,823
Import growth (percent change)	27.6	23.9	13.1	59.1	14.0	11.4
Gross official reserves (million USD) 5/	544	609	627	817	937	1,067
Gross reserves (months of imports, eop)	4.7	3.3	4.4	3.9	4.0	4.2
External public debt outstanding (in percent of GDP) 6/	88	78	78	69	61	56
Debt service-to-export ratio (in percent) 6/	6.4	7.3	5.6	5.5	5.2	4.4
Memorandum items						
Exchange rate (soms per U.S. dollar, average)	42.6	41.0	...	40.1	...	...
Real effective exchange rate						
Index (1995=100)	72.0	72.8	...	73.6	...	...

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

1/ General government comprises state government and Social Fund finances. State government comprises central and local governments.
2/ Projections are based on program exchange rates specified in the Technical Memorandum of Understanding (TMU).
3/ 12-month GDP over end-period broad money.
4/ Weighted average interest rate on som-denominated loans.
5/ Gross reserves exclude international reserves of the NBKR that are pledged or blocked.
6/ Excludes obligations of Kumtor gold mine.

Table 4. Kyrgyz Republic: Summary of General Government Fiscal Operations, 2005–07

	2005		2006				2007			
	Act.		IMF/CR/06/235, 2nd Revie		Prel.		IMF/CR/07/135, 3rd Review		Revised Projections	
	Million of soms	Percent of GDP	Million of soms	Percent of GDP	Million of soms	Percent of GDP	Million of soms	Percent of GDP	Million of soms	Percent of GDP
Total revenue and grants	24,913	24.7	26,672	24.0	30,062	26.6	30,149	24.9	34,971	27.6
Total revenue	23,883	23.7	25,517	23.0	29,174	25.8	29,209	24.1	32,170	25.4
Current revenue	23,750	23.5	25,366	22.8	28,955	25.6	29,088	24.0	31,930	25.2
Tax revenue 1/	20,182	20.0	21,352	19	24,317	21.5	24,914	20.5	27,386	21.6
Of which:										
Income tax	3,516	3.5	3,065	2.8	3,506	3.1	3,517	2.9	3,657	2.9
VAT	7,089	7.0	7,721	6.9	9,151	8.1	9,545	7.9	10,177	8.0
Customs	1,664	1.6	1,978	1.8	2,803	2.5	2,544	2.1	4,000	3.2
Social Fund revenue (excluding government contribution)	3,821	3.8	3,703	3.3	4,336	3.8	4,243	3.5	4,245	3.4
Nontax revenue	3,568	3.5	4,014	3.6	4,637	4.1	4,174	3.4	4,544	3.6
Capital revenue	133	0.1	151	0.1	220	0.2	120	0.1	240	0.2
Grants	1,031	1.0	1,155	1.0	888	0.8	940	0.8	2,801	2.2
Program grants	393	0.4	…	…	266	0.2	…	…	953	0.8
PIP grants	637	0.6	…	…	622	0.5	…	…	1,848	1.5
Total expenditure	29,127	28.9	30,500	27.4	32,863	29.0	34,499	28.4	39,499	31.2
Current expenditure	24,304	24.1	25,650	23.1	27,786	24.6	29,054	24.0	32,362	25.6
Wages	6,329	6.3	6,981	6.3	7,451	6.6	7,593	6.3	9,679	7.6
Transfers and subsidies 2/	3,401	3.4	4,173	3.8	4,201	3.7	4,620	3.8	4,995	3.9
Social Fund expenditures	5,664	5.6	6,062	5.5	6,421	5.7	6,765	5.6	7,202	5.7
Interest 3/	1,564	1.6	928	0.8	1,002	0.9	1,239	1.0	1,219	1.0
Purchases of other goods and services	7,347	7.3	7,506	6.8	8,711	7.7	8,836	7.3	9,268	7.3
Capital expenditure (including PIP)	4,823	4.8	4,850	4.4	5,077	4.5	5,445	4.5	7,137	5.6
Domestically financed capital expenditure	961	1.0	1,393	1.3	1,287	1.1	1,528	1.3	1,929	1.5
Foreign loan financed PIP	3,240	3.2	3,457	3.1	3,195	2.8	3,917	3.2	3,360	2.7
Foreign financed PIP grants	622	0.6	…	…	594	0.5	…	…	1,848	1.5
Financial balance	-4,214	-4.2	-3,828	-3.4	-2,800	-2.5	-4,350	-3.6	-4,528	-3.6
Net lending	-451	-0.4	-354	-0.3	-227	-0.2	-590	-0.5	-591	-0.5
Overall balance (accrual)	-3,763	-3.7	-3,473	-3.1	-2,573	-2.3	-3,760	-3.1	-3,937	-3.1
Primary balance	-2,199	-2.2	-2,463	-2.2	-1,571	-1.4	-2,521	-2.1	-2,718	-2.1
Primary balance excluding grants	-3,229	-3.2	-3,701	-3.3	-2,459	-2.2	-3,461	-2.9	-5,518	-4.4
Total financing	3,763	3.7	3,473	3.1	2,573	2.3	3,760	3.1	3,937	3.1
External financing	3,526	3.5	3,681	3.3	2,998	2.6	3,510	2.9	3,154	2.5
Public investment program (PIP)	3,240	3.2	3,457	3.1	3,195	2.8	3,917	3.2	3,360	2.7
Disbursements (BOP support)	0	0.0	748	0.7	301	0.3	395	0.3	578	0.5
Total amortization	-1,803	-1.8	-523	-0.5	-677	-0.6	-741	-0.6	-724	-0.6
Arrears and debt relief	2,088	2.1	0	0.0	178	0.2	-61	-0.1	-59	0.0
Domestic financing	76	0.1	-495	-0.4	-445	-0.4	30	0.0	501	0.4
Exceptional Financing 4/	161	0.2	287	0.3	21	0.0	220	0.2	282	0.2
Memorandum items:										
Social spending	14,646	14.5	16,689	15.0	18,078	16.0	19,189	15.8	21,243	16.8
Health and education	7,201	7.1	8,325	7.5	9,373	8.3	9,574	7.9	11,241	8.9
Social security benefits and pensions	7,445	7.4	8,364	7.5	8,704	7.7	9,615	7.9	10,002	7.9

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

1/ Includes payroll tax revenue (contributions to the Social Fund), net of the government contribution to the Social Fund.
2/ Excludes transfers to the Social Fund.
3/ Starting in 2006, interest and amortization reflect bilateral agreements signed following the March 2005 Paris Club agreement.
4/ Mainly privatization proceeds.

Table 5. Kyrgyz Republic: General Government Finances, 2005–07

	2005	2006		2007				
	Year	Year		Q1	Q2	Q3	Q4	Year
	Act.	Prog.	Prel.	Projections				
				(In millions of soms)				
Total revenue and grants	24,913	26,672	30,062	6,989	8,560	9,205	10,217	34,971
Total revenue	23,883	25,517	29,174	6,551	7,960	8,300	9,359	32,170
Of which: tax revenue 1/	20,182	21,352	24,317	5,691	6,673	7,116	7,905	27,386
Grants	1,031	1,155	888	439	600	905	858	2,801
Program grants	393	…	266	131	100	327	396	953
PIP grants	637	…	622	308	501	578	462	1,848
Total expenditure (including net lending)	28,676	30,500	32,635	7,698	9,516	10,311	11,382	38,908
Current expenditure	24,304	25,650	27,786	6,696	7,813	8,081	9,772	32,362
Wages	6,329	6,981	7,451	1,884	2,496	2,559	2,739	9,679
Transfers and subsidies 2/	3,401	4,173	4,201	1,013	1,200	1,165	1,617	4,995
Social Fund expenditures	5,664	6,062	6,421	1,716	1,759	1,823	1,904	7,202
Interest	1,564	928	1,002	195	570	150	304	1,219
Purchases of other goods and services	7,347	7,506	8,711	1,888	1,788	2,384	3,209	9,268
Capital expenditure (including PIP)	4,823	4,850	5,077	1,170	1,963	2,333	1,671	7,137
Domestically financed capital expenditure	961	…	1,287	400	500	600	429	1,929
Foreign financed PIP loans	3,240	…	3,195	462	963	1,155	780	3,360
Foreign financed PIP grants	622	…	594	308	501	578	462	1,848
Financial balance	-4,214	-3,828	-2,800	-876	-1,216	-1,209	-1,226	-4,528
Net lending	-451	-354	-227	-168	-261	-102	-61	-591
Overall balance (accrual)	-3,763	-3,473	-2,573	-709	-956	-1,107	-1,165	-3,937
Primary balance	-2,199	-2,545	-1,571	-514	-385	-956	-862	-2,718
Primary balance excluding grant	-3,229	-3,701	-2,459	-953	-986	-1,861	-1,719	-5,518
Total financing	3,763	3,473	2,573	709	956	1,107	1,165	3,937
External financing	3,526	3,681	2,998	494	649	1,458	553	3,154
Domestic financing	76	-495	-445	154	105	-362	604	501
Exceptional Financing 3/	161	287	21	61	203	10	9	282
				(In percent of GDP)				
Total revenue and grants	24.7	24.0	26.6	5.5	6.8	7.3	8.1	27.6
Total revenue	23.7	23.0	25.8	5.2	6.3	6.6	7.4	25.4
Of which: tax revenue 1/	20.0	19.2	21.5	4.5	5.3	5.6	6.2	21.6
Grants	1.0	1.0	0.8	0.3	0.5	0.7	0.7	2.2
Program grants	0.4	…	0.2	0.1	0.1	0.3	0.3	0.8
PIP grants	0.6	…	0.5	0.2	0.4	0.5	0.4	1.5
Total expenditure (including net lending)	28.4	27.4	28.8	6.1	7.5	8.1	9.0	30.7
Total expenditure	28.9		29.0	6.2	7.7	8.2	9.0	31.2
Current expenditure	24.1	23.1	24.6	5.3	6.2	6.4	7.7	25.6
Capital expenditure (including PIP)	4.8	4.4	4.5	0.9	1.6	1.8	1.3	5.6
Domestically financed capital expenditure	1.0	…	1.1	0.3	0.4	0.5	0.3	1.5
Foreign loan financed PIP	3.2	…	2.8	0.4	0.8	0.9	0.6	2.7
Foreign grant financed PIP	0.6	…	0.5	0.2	0.4	0.5	0.4	1.5
Financial balance	-4.2	-3.4	-2.5	-0.7	-1.0	-1.0	-1.0	-3.6
Net lending	-0.4	-0.3	-0.2	-0.1	-0.2	-0.1	0.0	-0.5
Overall balance (accrual)	-3.7	-3.1	-2.3	-0.6	-0.8	-0.9	-0.9	-3.1
Overall balance (cash)	-3.7	-3.1	-2.3	-0.6	-0.8	-0.9	-0.9	-3.1
Primary balance	-2.2	-4.3	-1.4	-0.4	-0.3	-0.8	-0.7	-2.1
Primary balance excluding grant	-3.2	-3.3	-2.2	-0.8	-0.8	-1.5	-1.4	-4.4
Total financing	3.7	3.1	2.3	0.6	0.8	0.9	0.9	3.1
External financing	3.5	3.3	2.6	0.4	0.5	1.2	0.4	2.5
Domestic financing	0.1		-0.4	0.1	0.1	-0.3	0.5	0.4
Exceptional Financing 3/	0.2	0.3	0.0	0.0	0.2	0.0	0.0	0.2
Memorandum item:								
Social spending	14.5	15.0	16.0	3.4	4.0	4.2	5.0	16.8

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

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

2/ Excludes transfers to the Social Fund.

3/ Mainly privatization proceeds.

Table 6. Kyrgyz Republic: State Government Finances, 2005–07

(In millions of soms)

	2005	2006		2007				
	Year	Year		Q1	Q2	Q3	Q4	Year
	Actual	Prog.	Prel.	Projections				
Total revenue and grants	21,006	22,886	25,644	5,914	7,477	8,116	9,139	30,646
Total revenue	19,975	21,731	24,756	5,476	6,877	7,211	8,282	27,845
Current revenue	19,929	21,663	24,618	5,450	6,851	7,172	8,212	27,685
Tax revenue	16,361	17,650	19,981	4,636	5,610	6,047	6,848	23,141
Income tax	3,516	3,065	3,506	911	831	879	1,036	3,657
VAT 1/	7,089	7,721	9,151	1,904	2,502	2,624	3,147	10,177
Excises	1,150	1,379	1,205	319	362	372	384	1,437
Customs	1,664	1,978	2,803	723	991	1,073	1,213	4,000
Land tax	319	559	412	93	91	161	222	567
Road tax and Emergency Fund	1,410	1,550	1,534	330	433	464	459	1,686
Retail sales tax	605	675	772	190	216	236	243	885
Other 2/	610	724	599	166	183	239	144	732
Nontax revenue	3,568	4,014	4,637	813	1,241	1,125	1,364	4,544
Capital revenue	46	68	138	26	25	39	70	160
Grants	1,031	1,155	888	439	600	905	858	2,801
Program grants	393	…	266	131	100	327	396	953
PIP grants	637	…	622	308	501	578	462	1,848
Total expenditure (excluding net lending)	25,601	26,645	28,947	6,879	8,750	9,294	10,301	35,224
Current expenditure	20,778	21,795	23,871	5,709	6,787	6,961	8,630	28,087
Wages and Social Fund contributions	7,484	8,150	8,699	2,270	2,885	2,918	3,157	11,230
Transfers and subsidies 3/	3,401	4,173	4,201	1,013	1,200	1,165	1,617	4,995
Transfers to Social Fund	982	1,038	1,257	344	344	344	344	1,375
Interest	1,564	928	1,002	195	570	150	304	1,219
Purchases of other goods and services 4/	7,347	7,506	8,711	1,888	1,788	2,384	3,209	9,268
Capital expenditure (including PIP)	4,823	4,850	5,077	1,170	1,963	2,333	1,671	7,137
Domestically financed capital expenditure	961	1,393	1,287	400	500	600	429	1,929
Foreign-financed PIP	3,240	3,457	3,195	462	963	1,155	780	3,360
Foreign grant financed PIP	622		594	308	501	578	462	1,848
Financial balance	-4,595	-3,759	-3,303	-965	-1,273	-1,178	-1,162	-4,578
Net lending	-451	-354	-227	-168	-261	-102	-61	-591
Primary balance excluding grants	-3,610	-3,632	-2,962	-1,012	-1,437	-1,394	-1,374	-5,568
Primary balance	-2,580	-2,477	-2,074	-829	-1,388	-1,224	-1,168	-2,767
Accrual surplus (+) / deficit (-)	-4,144	-3,404	-3,076	-797	-1,012	-1,076	-1,101	-3,987
Total financing	4,144	3,404	3,076	797	1,012	1,076	1,101	3,987
External financing	3,526	3,681	2,998	494	649	1,458	553	3,154
Public investment program (PIP)	3,240	3,457	3,195	462	963	1,155	780	3,360
Disbursements (BOP support)	0	748	301	193	0	385	0	578
Total amortization	-1,803	-523	-677	-91	-257	-101	-274	-724
Arrears and rescheduling	2,088	0	178	-70	-57	20	47	-59
Domestic financing	457	-564	58	243	161	-393	539	551
Exceptional Financing 5/	161	287	21	61	203	10	9	282

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

1/ In 2005, the VAT and customs revenues were reclassified, leading to lower VAT and higher customs duty collections.
2/ Mainly mineral resource tax and motor vehicle tax.
3/ Excludes transfers to Social Fund (columns for original program include transfer to Social Fund).
4/ Includes carry-forward expenditure from previous fiscal year (som 994 million in 2004, som 945 million in 2005, and som 480 million in 2006).
5/ Mainly privatization proceeds.

Table 7. Kyrgyz Republic: Social Fund Operations, 2005–07

	2005	2006		2007				
	Year	Year		Q1	Q2	Q3	Q4	Year
	Actual	Prog.	Prel.	Projections				
	(In millions of soms)							
Total revenue	5,063	4,955	5,667	1,461	1,472	1,448	1,496	5,876
Total contribution	4,976	4,872	5,585	1,441	1,452	1,428	1,476	5,796
Contribution from government	1,156	1,169	1,249	386	388	359	418	1,551
Contribution from nongovernment	3,821	3,703	4,336	1,055	1,063	1,069	1,058	4,245
Other revenue	87	83	82	20	20	20	20	80
Total expenditure	5,664	6,062	6,421	1,716	1,759	1,823	1,904	7,202
Pension fund (cash)	5,330	5,794	6,100	1,636	1,669	1,733	1,798	6,836
Social insurance fund (cash)	79	0	0	0	0	0	0	0
Medical insurance fund (cash)	254	268	321	80	90	90	106	366
Financial balance	-601	-1,107	-754	-255	-287	-375	-408	-1,326
Budgetary transfer	982	1,038	1,257	344	344	344	344	1,375
Overall balance	381	-69	503	88	57	-31	-64	50
	(Percent of GDP)							
Total revenue	5.0	4.5	5.0	1.3	1.3	1.3	1.3	4.6
Total contribution	4.9	4.4	4.9	1.3	1.3	1.3	1.3	4.6
Contribution from government	1.1	1.1	1.1	0.3	0.3	0.3	0.4	1.2
Contribution from nongovernment	3.8	3.3	3.8	0.9	0.9	0.9	0.9	3.4
Other revenue	0.1	0.1	0.1	0.0	0.0	0.0	0.0	0.1
Total expenditure	5.6	5.5	5.7	1.5	1.6	1.6	1.7	5.7
Pension fund (cash)	5.3	5.2	5.4	1.4	1.5	1.5	1.6	5.4
Social insurance fund (cash)	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Medical insurance fund (cash)	0.3	0.2	0.3	0.1	0.1	0.1	0.1	0.3
Overall balance	-0.6	-1.0	-0.7	-0.2	-0.3	-0.3	-0.4	-1.0
Budgetary transfer	1.0	0.9	1.1	0.3	0.3	0.3	0.3	1.1
Cash balance	0.4	-0.1	0.4	0.1	0.1	0.0	-0.1	0.0
Memorandum items:								
Average monthly pension (in som; end of period) 1/	796	876	906	982	1,000	1,037	1,037	1,037
Payroll tax rate	31.0	29.0	29.0	29.0	27.0	27.0	27.0	27.0
Revenue collection in cash	4,912	4,823	5,528	1,426	1,437	1,414	1,461	5,738
Cash collection ratio (in percent)	98.7	99.0	99.0	99.0	99.0	99.0	99.0	99.0

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

1/ Includes payments to compensate vulnerable households for electricity tariff increases introduced in June 2002.
GDP

Table 8. Kyrgyz Republic: Medium-Term Expenditure Framework for General Government by Functional Classification, 2005–09

(In percent of GDP)

		2005	2006		2007	2008	2009
		Act.	Prog.	Prel.	Projections		
	Total expenditure 1/	28.4	26.6	28.8	30.7	30.6	30.1
I.	General public services	3.0	2.0	3.0	3.2	3.1	3.0
II.	Defense	1.4	1.1	1.5	1.6	1.5	1.5
III.	Public order and safety affairs	1.7	0.9	1.7	1.9	1.8	1.7
	Social spending	14.5	15.5	16.0	16.8	17.1	17.2
IV.	Education	4.9	4.7	5.6	5.9	6.0	6.0
V.	Health	2.3	2.5	2.7	3.0	3.2	3.3
VI.	Social security and welfare affairs 2/	2.1	3.1	2.3	2.5	2.6	2.7
VII.	Pension fund 3/	5.3	5.2	5.4	5.4	5.3	5.2
VIII.	Housing and community services	1.0	1.1	1.3	1.4	1.3	1.3
IX.	Recreational, cultural and religious activities	0.6	0.4	0.7	0.8	0.8	0.7
X	Energy complex (electricity production)	0.3	0.4	0.2	0.2	0.2	0.2
XI.	Agriculture, water resources, forestry	2.3	1.9	2.2	2.4	2.4	2.2
XII.	Mining and mineral resources	0.3	0.2	0.3	0.3	0.3	0.3
XIII.	Transportation and communication	2.0	1.8	2.0	2.2	2.1	2.0
XIV.	Other economic affairs and services	0.8	0.6	0.7	0.8	0.8	0.7
XV.	Other (including net lending)	0.4	0.6	-0.7	-0.7	-0.7	-0.7

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

1/ Including PIP and net lending.
2/ Excluding net transfers to the Social Fund, but including the contingency item for social compensation in case of electricity tariff increases.
3/ Social Fund operations net of transfers to other funds.

Table 9. Kyrgyz Republic: NBKR Accounts, 2005–07

	2005	2006				2007			
	Dec.	June	Dec.			Mar.	Jun.	Sep.	Dec.
	Act.	Act.	Prog.	Act.	Act. 1/	Projections 1/			
	(Annual percent change)								
Net foreign assets	24.2	36.7	11.4	51.7	49.4	52.9	40.4	30.4	23.9
Net domestic assets	108.9	-37.6	217.6	-233.9	-85.8	152.0	125.1	407.4	798.0
Of which:									
Net claims on general government	182.6	18.8	-25.1	34.3	28.7	70.3	44.2	18.7	14.1
Claims on rest of the economy	-27.3	-59.1	80.1	-157.1	-163.1	27.9	63.0	-456.2	88.1
Reserve money	24.9	32.9	14.5	47.5	47.4	54.9	42.5	34.2	25.0
Currency in circulation	20.5	28.9	15.0	48.4	48.4	60.3	40.1	34.2	23.8
Commercial banks' reserves and other balances	114.9	73.4	11.0	41.1	40.8	25.8	32.9	21.7	13.6
	(Contribution to reserve money growth, in percent) 2/								
Net foreign assets	24.0	28.8	11.3	50.9	48.7	34.8	29.2	29.4	23.9
Net domestic assets	1.0	-1.6	3.2	-3.5	-1.3	2.1	2.5	-0.4	1.1
Of which: net claims on general government	6.2	1.3	-1.9	2.6	2.5	2.7	2.0	1.2	0.9
Reserve money	24.9	27.2	14.5	47.5	47.4	37.0	31.6	29.0	25.0
Of which: currency in circulation	16.1	21.7	13.0	42.0	48.4	32.7	26.3	25.1	20.8
	(In millions of soms)								
Net foreign assets	15,236	16,554	16,977	23,114	22,767	22,993	23,208	25,187	28,205
Net international reserves	17,477	18,984	19,176	25,445	24,908	25,134	25,329	27,308	30,308
Long-term foreign liabilities	-2,353	-2,332	-2,311	-2,401	-2,201	-2,201	-2,181	-2,181	-2,162
Other foreign assets	164	-46	163	121	111	111	111	111	111
Balances with CIS countries	-51	-51	-51	-51	-51	-51	-51	-51	-51
Net domestic assets	230	410	731	-308	33	782	970	732	294
Net claims on general government	1,188	1,316	890	1,596	1,530	1,656	1,773	1,481	1,745
Loans to government in forex (Turkish loan)	1,943	1,943	1,981	2,033	1,864	1,864	1,864	1,864	1,864
Total government deposits (-)	-5,202	-4,801	-4,792	-4,617	-4,513	-4,371	-4,117	-4,410	-3,913
Treasury bonds 3/	3,897	3,523	3,151	3,529	3,529	3,513	3,476	3,476	3,244
Treasury bills	550	650	550	650	650	650	550	550	550
Repos	-50	-198	200	-504	-504	0	-100	0	-663
Claims on commercial banks	351	344	342	332	314	310	309	306	305
Other items (net)	-1,259	-1,052	-701	-1,732	-1,307	-1,185	-1,013	-1,055	-1,093
Reserve money	15,466	16,965	17,708	22,806	22,800	23,775	24,177	25,918	28,499
Currency in circulation	13,414	14,971	15,430	19,910	19,910	20,776	20,969	22,470	24,648
Commercial banks' reserves and other balances	2,052	1,994	2,278	2,896	2,890	2,999	3,208	3,449	3,852
Of which: required reserves	1,160	1,372	1,411	1,529	1,522	1,837	1,928	2,105	2,510
Memorandum items:									
Reserve money growth (in percent, relative to end of previous year)	24.9	27.2	14.5	47.5	47.4	37.0	31.6	29.0	25.0
Net international reserves (in millions of dollars) 4/	416	452	457	606	647	653	658	709	787
Net domestic assets (in millions of soms) 4/	-1,943	-1,756	-1,469	-2,559	-2,031	-1,282	-1,094	-1,332	-1,769

Sources: Kyrgyz authorities; and Fund staff estimates.

1/ Based on new program exchange rates (including 38.5 soms/dollar) specified in the TMU.
2/ Contribution is defined as annual change of asset stock relative to previous year's reserve money stock (in percent).
3/ Includes government securities issued in December 2002 to replace restructured bonds, as well as those issued for revaluation losses, lost capital in the Asian Development Bank, and capitalized past interest arrears on bonds.
4/ Non-adjusted.

Table 10. Kyrgyz Republic: Monetary Survey, 2005–07

	2005	2006				2007			
	Dec.	Jun.	Dec.			Mar.	Jun.	Sep.	Dec.
	Act.	Act.	Prog.	Act.	Act. 1/	Projections 1/			
					(Annual percent change)				
Net foreign assets	20.1	27.0	12.5	50.6	47.6	60.3	50.1	37.4	28.0
Net domestic assets	54.5	64.6	35.4	68.7	65.0	35.5	14.7	20.3	37.6
Of which:									
Net claims on general government	24.2	0.4	-47.8	-14.4	-16.5	14.2	37.2	23.2	46.9
Credit to the rest of the economy	32.0	49.0	19.9	56.8	47.5	52.3	40.0	35.7	26.8
Broad money (M2X)	25.5	34.9	17.0	54.1	51.7	55.3	41.4	33.6	30.0
Of which:									
Broad money, excluding forex deposits (M2)	43.5	62.3	20.0	51.1	84.5	56.7	40.5	31.0	30.6
Currency held by the public	17.5	29.1	14.5	48.6	48.6	52.0	36.7	28.3	24.0
Total deposit liabilities	40.6	44.6	20.9	47.8	54.8	60.4	48.9	41.9	39.0
					(Contribution to broad money growth, in percent) 2/				
Net foreign assets	16.9	18.0	10.1	40.7	38.3	30.9	27.5	27.5	22.0
Net domestic assets	8.6	11.3	6.9	13.4	12.7	3.9	1.6	0.5	8.0
Domestic credit	13.0	15.1	4.3	20.3	16.7	12.2	11.0	8.8	9.1
Net claims on general government	1.6	0.0	-3.1	-0.9	-1.1	0.4	1.3	0.4	1.7
Credit to the rest of the economy	11.4	15.0	7.4	21.2	17.8	11.8	9.7	8.4	7.5
Other items (net)	-4.4	-3.7	2.6	-6.9	-4.0	-1.5	-2.7	-1.5	5.1
Broad money (M2X)	25.5	29.3	17.0	54.1	51.0	34.8	29.1	28.0	30.0
Of which:									
Broad money, excluding forex deposits (M2)	28.4	41.2	14.9	38.1	64.8	28.2	22.9	21.2	22.9
Currency held by the public	11.4	15.3	8.9	29.6	29.6	20.9	16.5	16.8	14.4
Total deposit liabilities	14.1	14.0	8.1	24.5	21.3	13.9	12.5	11.2	15.6
					(In millions of soms)				
Net foreign assets	17,232	18,096	19,393	25,946	25,433	27,011	26,976	29,111	32,544
Of which: long-term foreign liabilities (-)	-2,353	-2,332	-2,311	-2,401	-2,201	-2,201	-2,181	-2,181	-2,162
Net domestic assets	4,170	6,167	5,647	7,033	6,879	5,809	6,677	7,247	9,462
Domestic credit	9,416	11,124	10,335	13,761	12,989	13,998	14,675	15,287	16,704
Net claims on general government	1,406	1,350	734	1,203	1,174	1,417	1,770	1,378	1,725
Credit to the rest of the economy	8,010	9,774	9,601	12,558	11,816	12,581	12,905	13,909	14,979
Of which: in forex	5,813	6,799	6,721	9,001	8,259	8,530	8,711	9,389	10,036
Other items net	-5,246	-4,957	-4,688	-6,728	-6,110	-5,988	-5,816	-5,858	-5,079
Broad money (M2X)	21,402	24,264	25,040	32,979	32,312	32,820	33,653	36,358	42,006
Of which:									
Broad money, excluding forex deposits (M2)	15,959	18,286	19,156	24,108	24,108	25,159	25,686	27,455	31,492
Currency held by the public	13,065	14,545	14,961	19,410	19,410	19,700	19,883	21,325	24,078
Total domestic currency deposit liabilities	2,894	3,742	4,196	4,698	4,698	5,460	5,803	6,130	7,414
Memorandum items:									
Broad money (M2X) growth (in percent,									
relative to end of previous year)	25.5	29.3	17.0	54.1	51.0	34.8	29.1	28.0	30.0
Credit to the rest of the economy (in percent of GDP)	8.0	9.4	8.6	11.0	10.4	10.9	10.9	11.5	11.8
M2X velocity 3/	4.7	4.3	4.4	3.8	3.5	3.5	3.5	3.3	3.0
M2X multiplier	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.5
Dollarization indicators (in percent) 4/									
Asset dollarization	72.6	69.6	70.0	71.7	69.9	67.8	67.5	67.5	67.0
Liability dollarization	25.4	24.6	23.5	26.9	25.4	23.3	23.7	24.5	25.0

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

1/ Based on new program exchange rates (including 38.5 soms/dollar) specified in the TMU.

2/ Contribution is defined as annual change of asset stock relative to previous year's broad money stock (in percent).

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

4/ Asset dollarization is measured as the ratio of credit extended in foreign exchange to total banking system credit to the private sector, and liability dollarization as the share of foreign exchange deposits in broad money.

Table 11. Kyrgyz Republic: Balance of Payments, 2005–09

(In millions of U.S. dollars)

	2005	2005	2006		2007		2008	2009
			IMF/CR/06/235		IMF/CR/07/135			
	EBS/05/145	Actual	2nd Review	Prel.	3rd Review	Rev. Proj.	Projections	
Current account balance	-197	-57	-179	-473	-302	-416	-394	-382
excluding transfers	-560	-531	-601	-1,107	-824	-1,172	-1,240	-1,288
Trade balance	-435	-419	-474	-988	-723	-1,038	-1,073	-1,080
Exports, fob	686	687	786	811	901	1,011	1,185	1,353
CIS countries	305	305	347	381	405	426	448	472
Of which: energy	33	33	38	43	44	47	52	58
Non-CIS countries	382	382	439	430	496	585	738	881
Of which: gold	231	231	268	206	289	340	478	614
Imports, fob	1121	1,106	1,260	1,799	1,624	2,049	2,259	2,433
CIS countries	648	641	747	940	1,004	1,034	1,153	1,237
Of which : energy	295	289	353	473	512	492	559	589
Non-CIS countries	473	465	513	859	621	1,015	1,105	1,196
Services	-45	-36	-61	-76	-20	-78	-114	-138
Receipts	256	256	285	347	398	408	451	491
Payments	-300	-291	-347	-424	-418	-486	-565	-630
Income	-80	-76	-65	-42	-81	-57	-53	-70
Interest payments 1/	-41	-37	-19	-23	-24	-25	-27	-37
Other net income	-39	-39	-46	-20	-58	-32	-26	-33
Current Transfers (net)	363	474	422	634	522	757	846	906
Official	28	23	37	12	43	41	45	41
Private	335	451	385	622	479	715	801	865
Capital Account	-6	-13	-6	-39	-9	-34	-29	-22
Official	52	50	41	34	49	43	51	50
Private	-58	-63	-46	-74	-58	-77	-80	-72
Financial account (including errors and omissions)	252	119	208	694	413	576	565	566
Commercial banks	48	-29	-12	-39	40	25	30	35
Medium-and long-term loans, net	-9	10	73	55	78	66	84	98
Disbursement	109	90	112	96	115	107	121	141
Of which: loan financed PIP	79	79	82	76	98	87	99	111
Amortization 1/	-99	-60	-39	-41	-37	-42	-36	-43
FDI and portfolio investment (net)	101	45	95	107	110	109	127	146
Derivatives and net short-term flows (incl. errors & omissions)	126	93	52	577	173	375	344	323
Overall balance	49	49	23	181	102	127	143	162
Financing	-49	-49	-23	-181	-102	-127	-143	-162
Net international reserves	-93	-93	-41	-193	-110	-140	-150	-162
Gross official reserves (- increase)	-81	-81	-18	-170	-90	-120	-130	-140
IMF (net)	-13	-12	-23	-24	-20	-20	-20	-22
Exceptional Financing (including arrears)	44	44	0	4	-2	-2	0	0
BOP support loans (ADB)	0	0	8	8	0	0	8	0
BOP support loans (WB)	0	0	10	0	10	15	0	0
Memorandum items:								
GDP (in millions of U.S. dollars)	2,441	2,460	2,646	2,820	3,071	3,287	3,661	4,050
Current account balance (in percent of GDP)	-8.1	-2.3	-6.8	-16.8	-9.8	-12.6	-10.8	-9.4
Growth of exports of goods and services (volume, percent)	-8.2	-8.2	2.2	4.6	12.9	16.7	12.7	10.5
Growth of imports of goods and services (volume, percent)	14.4	13.3	6.7	34.0	8.8	11.4	7.6	6.6
External public debt (US$ million) 2/	2,010	1,910	2,068	1,948	2,037	2,005	2,062	2,115
as percent of GDP	82	77.6	78.2	69.1	66.3	61.0	56.3	52.2
External public debt (NPV US$ million) 2/	1106	1,145	1,153	1,179	1,221	1,222	1,265	1,307
as percent of GDP	45	46.5	43.6	41.8	39.8	37.2	34.6	32.3
as percent of exports	117	121.5	107.6	101.8	94.0	86.1	77.3	70.9
Public debt service-to-exports ratio 2/ 3/	7.1	7.3	5.6	5.5	5.3	5.2	4.4	4.6
Gross reserves 4/	609	609	627	817	811	937	1,067	1,207
in months of subsequent year's imports	4.5	3.3	4.4	3.9	4.3	4.0	4.2	4.4

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

1/ Starting 2006, interest and amortization reflect bilateral agreements signed following the March 2005 Paris Club agreement to grant debt relief on London terms.
2/ Public and publicly guaranteed debt.
3/ Net of rescheduling.
4/ Valued at end-period exchange rates.

Table 12. Kyrgyz Republic: Indicators of Fund Credit, 2005–11

(In percent, unless otherwise indicated)

	2005	2006	2007	2008	2009	2010	2011
	Actual	Prel.	Projections				
Outstanding Fund credit (end-of-period)							
In millions of SDRs	124.5	108.4	94.8	81.3	66.5	50.3	35.2
In millions of U.S. dollars	183.8	159.5	141.7	121.9	100.1	75.9	53.4
In percent of quota 1/	140.2	122.1	106.8	91.5	74.9	56.6	39.7
In percent of GDP	7.5	5.7	4.3	3.3	2.5	1.7	1.1
In percent of total exports	19.5	13.8	10.0	7.5	5.4	3.8	2.4
In percent of external public debt	9.6	8.2	7.1	5.9	4.7	3.5	2.4
In percent of gross reserves (beginning of period)	33.8	26.2	17.3	13.0	9.4	6.3	4.2
Debt service due to the Fund							
In millions of SDRs	21.5	19.2	16.6	15.2	15.1	16.5	15.3
In millions of U.S. dollars	31.8	28.3	24.9	22.8	22.7	24.9	23.2
Of which:							
Charges/interests	1.0	0.9	0.7	0.6	0.5	0.4	0.3
Repurchases and repayments	30.8	27.4	24.1	22.2	22.2	24.5	22.8
In percent of quota 1/	24.3	21.6	18.7	17.1	17.0	18.6	17.2
In percent of GDP	1.3	1.0	0.8	0.6	0.6	0.6	0.5
In percent of total exports	3.4	2.4	1.8	1.4	1.2	1.3	1.1
In percent of total debt service	37.9	32.9	27.1	26.6	22.2	15.9	20.1
In percent of total public debt service	46.2	44.7	33.8	31.9	27.0	28.5	25.7
In percent of gross reserves (beginning of period)	5.9	4.6	3.0	2.4	2.1	2.1	1.8

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

1/ Kyrgyz Republic quota: SDR 88.8 million.

Table 13. Kyrgyz Republic: Prospective Use of Fund Resources, 2006–11

(in millions of SDR, unless otherwise stated)

	Outstanding End-Dec. 2006	2007	2008	2009	2010	2011
		Projections				
PRGF transactions	108.4					
Disbursements	2.5	2.5	1.3	0.0	0.0	0.0
Repayments	18.6	16.1	14.8	14.7	16.2	15.1
Total Fund credit outstanding	108.4	94.8	81.3	66.5	50.3	35.2
Total Fund credit outstanding 1/	122.1	106.8	91.5	74.9	56.6	39.7
Disbursements under PRGF 1/	2.9	2.9	1.4	0.0	0.0	0.0

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

1/ In percent of the country's quota (SDR 88.8 million).

Table 14. Kyrgyz Republic: Reviews and Disbursements Under the Three-Year PRGF Arrangement

Date	Action	Associated Disbursement
February 23, 2005	Approved three-year arrangement.	SDR 1.26 million
October 24, 2005	Completed first review based on end-June 2005 performance criteria.	SDR 1.27 million
May 5, 2006	Completed second review based on end-December 2005 performance criteria.	SDR 1.27 million
November 3, 2006	Completed third review based on end-June 2006 performance criteria.	SDR 1.27 million
May 18, 2007	Complete fourth review based on end-December 2006 performance criteria, and set conditions and disbursements for the third year of the arrangement.	SDR 1.27 million
On or after August 15, 2007	Complete fifth review based on end-June 2007 performance criteria.	SDR 1.27 million
On or after February 15, 2008	Complete sixth review based on end-December 2007 performance criteria.	SDR 1.27 million

ATTACHMENT I

April 24, 2007

Mr. Rodrigo de Rato
Managing Director
International Monetary Fund
700 19th Street, N.W.
Washington, D.C. 20431

Dear Mr. de Rato:

The attached Memorandum of Economic Policies (MEP) describes program implementation to date, sets out the government's economic strategy for the remainder of the program period, and includes program understandings reached with the IMF. Further to our letter of October 17, 2006, reviewing our performance under the program supported by the Poverty Reduction and Growth Facility (PRGF) arrangement approved in February 2005, we are pleased to inform you that all quantitative performance criteria for end-December 2006 were met, some with comfortable margins (Table 1). As indicated in Table 2, the implementation of some of the end-December 2006 and end-March 2007 structural benchmarks under the program has been delayed, owing in part to tensions between the government and parliament that have since been resolved. We are now seeking to expedite the passage of pending economic legislation and to add momentum to financial sector and public financial management reforms.

The Executive Board concluded the third review under the PRGF arrangement on November 3, 2006, and the fourth review is expected to be completed by May 2007. We hereby request disbursement of the SDR 1.27 million tranche upon Board completion of the fourth review.

We believe that the policies specified in the MEP provide a strong basis for sustaining growth in a low-inflation environment and alleviating poverty. We stand ready, nevertheless, to take any additional measures necessary to achieve the program's objectives. The government will continue to provide the Fund with the necessary information for assessing progress in implementing our program, as specified in the Technical Memorandum of Understanding (TMU), and will consult with Fund staff and management on any measures that may be appropriate at the initiative of the government or whenever the Fund requests a consultation.

The government intends to make public this letter and the staff report for the fourth review under the PRGF arrangement. Accordingly, it authorizes the IMF to arrange to post these documents on the Fund's website once the Executive Board completes its review.

Sincerely yours,

/s/	/s/
Almaz Atambaev	Marat Alapaev
Prime Minister	Chairman
Kyrgyz Republic	National Bank of the Kyrgyz Republic

ATTACHMENT II. MEMORANDUM OF ECONOMIC POLICIES FOR THE KYRGYZ REPUBLIC

I. RECENT ECONOMIC PERFORMANCE

1. This Memorandum reviews the implementation of the government's economic program supported by the PRGF arrangement approved in February 2005. The government has continued to maintain macroeconomic discipline and adhere to the PRGF-supported program, as evidenced by the observance of all end-December 2006 quantitative performance criteria, in some cases with ample margins (Table 1). However, as tensions with parliament delayed the passage of important legislation, some of the program's structural benchmarks have been missed (Table 2). After a slight contraction in 2005, real GDP grew at 2.7 percent in 2006, dampened by a gold mine accident. Excluding gold, however, output growth rebounded to 5.1 percent, driven by industry, construction and services. Consumer prices increased by 5.1 percent during the year (versus the program's 5.7 percent target), and by 4.3 percent during the 12 months ended February 2007. Owing to a sharp increase in imports and an accident-related shortfall in gold exports, the external current account deficit widened to 16¾ percent of GDP in 2006. Nevertheless, sizable short-term capital inflows (including errors and omissions that partly reflect unrecorded remittances and shuttle trade re-exports) led to a faster-than-expected buildup in gross reserves, to 3.9 months of projected 2007 imports of goods and services by year's-end.

2. The general government primary deficit before grants, at 2.2 percent of GDP in 2006, was well below expectations, owing to strong revenue gains (particularly from customs duties and VAT on imports).The quasi-fiscal deficit of the electricity sector (measured under the old cost-recovery tariff methodology) declined as planned to 5½ percent of GDP, owing to improved bill collection and a reduction in technical losses and theft.

3. The NBKR conducted sizable unsterilized intervention in the foreign exchange market in 2006 to mitigate the appreciation of the som. As a result, reserve money growth was faster than planned, but due to continued remonetization of the economy, inflation has remained subdued. Despite the foreign exchange intervention, the som appreciated by 8 percent against the U.S. dollar during the year, but in real effective terms the appreciation was only 1.3 percent, due to the strengthening of the currencies of key trading partners (especially Russia and Kazakhstan). Broad money and credit to the private sector have also increased rapidly, but loan portfolios have remained healthy and bank profitability indicators have improved.

II. PROGRAM OBJECTIVES AND ECONOMIC POLICIES FOR 2007

4. The government's economic strategy through 2010, based on the Country Development Strategy (CDS) and the Development Program that is being prepared by the new cabinet, focuses on poverty alleviation and private sector-led growth in a low- inflation environment. To that end, the government will continue to maintain macroeconomic stability and deepen financial sector and public financial management reforms. It will also reform the energy and mining sectors and take measures to enhance the business climate, improve the delivery and targeting of social services, and fight corruption. A specific reform agenda, drawing on the CDS and the Joint Country Support Strategy of the World Bank and other donors, will be discussed at a Consultative Group meeting in Bishkek this spring.

5. More specifically, our economic program for 2007 targets real GDP growth of 6½ percent, inflation at 5 percent, and a further gain in net international reserves that would keep end-year reserve coverage at 4 months of projected 2008 imports of goods and services. The external current account deficit would narrow to 12½ percent of GDP (on the back of a recovery in gold exports and continued buoyancy in workers' remittances) and be financed by FDI, other private inflows, and concessional external assistance. To achieve these goals, the overall deficit of the general government will be capped at 3.1 percent of GDP, mostly financed from external sources (Table 1). This will be accompanied by a firm monetary policy and a reduction in the quasi-fiscal losses of the electricity sector. We have also established structural benchmarks on critical financial sector and public financial management reforms through end-2007 (Table 2), and will strive to meet the program benchmarks missed thus far, as discussed below.

6. The government has initiated discussions with the Centerra mining company regarding its current and future operations in the Kyrgyz Republic, including the Kumtor gold mine, and it is counting on a significant increase in receipts. As indicated in Memorandum of Economic Policies for the third review under the PRGF arrangement, we are determined to harness these resources for productive uses in a manner consistent with macroeconomic stability. More specifically, we are seeking passage of a bill before parliament creating a Development Fund that would be sourced mainly from a portion of these additional receipts and possibly by future asset sales. We also reiterate that the utilization of these receipts (either through the public sector investment program or as net lending to the financial sector under the proposed Development Fund) will be fully and transparently reflected in the annual general government budgets approved by parliament and in the Medium-Term Budgetary Framework. As such, they will be fully integrated into the macroeconomic program supported by the PRGF arrangement, so as to safeguard short-term macroeconomic stability and longer-term external viability.

A. Fiscal and Quasi-Fiscal Issues

7. Fiscal discipline will remain the linchpin of macroeconomic stability. The 2007 budget passed in April is premised on further significant revenue gains, despite a 2 percentage-point reduction in the rate of social fund contributions in April, to 27 percent. The revenue effort will be underpinned by passage of the new tax code and further improvements in tax and customs administration—including further strengthening the Large Taxpayer Unit under the aegis of the State Tax Inspectorate. We are planning to gradually reduce the cascading and distortionary Road and Emergency Fund taxes from 2008, and may advance these cuts if revenue performance significantly exceeds expectations during 2007.

8. The budget also features a sizable increase in public salaries for certain categories (namely, 50 percent for the Interior Ministry and corrections personnel, and 30 percent for social sector employees) that will raise the general government wage bill to 7½ percent of GDP. Moreover, public pensions will be increased by 15 percent in 2007. To forestall an upward drift in the wage bill over the medium-term, while making room for differentiated increases in the remuneration of specialized professionals and senior officials from 2008, the government is launching a civil service reform in 2007 aimed at reducing the civilian workforce. The government will also start designing a pension reform with World Bank assistance, geared at

securing the system's longer term viability and encouraging the development of the domestic capital market.

9. In keeping with the fiscal decentralization mandated by parliament, the 2007 budget is framed in two-tiers (the central and local governments). To maintain overall fiscal discipline, the government will continue to help local authorities build capacity and it will clearly demarcate revenue and expenditure competencies at both tiers. In particular, the government will take measures to transfer the financial and economic bodies of the local governments under the jurisdiction of the ministry of finance, in order to maintain economic stability. Moreover, the government will continue to enhance public financial management with assistance from the World Bank, the IMF and the UK Department for International Development (DfID). In particular, it will track pro-poor spending in the monthly budget report from mid-2007 (in accordance with a new state-of-the-art (GFS 2001) budget classification); submit to parliament an internal audit law consistent with best international practice; and ensure that the State Agency on Public Procurement and Material Reserves does not participate directly in the procurement process. Further, the government will refine the Medium-Term Budgetary Framework (MTBF) to yield sectoral MTBF ceilings directly and transparently linked to annual budgets, and it will strengthen the annual budget process by including functional, economic and administrative summaries in the budget bill. The government will foster transparency in public sector operations, and to better equip the Ministry of Finance to take the lead in implementing this broad reform agenda, it is considering measures to strengthen the role of the Ministry of Finance.

10. To help deliver reliable and sustainable long-term energy supply for domestic use and exports, the government has developed a rehabilitation plan for the energy sector with support from the World Bank. The plan includes a medium-term tariff policy framework (MTTF) featuring phased adjustments in electricity tariffs under a pre-announced calendar to cost recovery levels by 2010, accompanied by social safety nets to cushion the effect of the adjustment on the poor. The MTTF also envisages actions to boost utility bill collections and to reduce technical losses and theft. In this vein, and consistent with the MTTF and the new cost-recovery methodology agreed with the World Bank, the electricity sector's quasi-fiscal deficit (an indicative program target) is slated to decline to 5½ percent of GDP in 2007, from an estimated deficit of 7½ percent in 2006 under the same methodology. The government will also encourage private participation in the energy sector, and will continue to provide professional management of electricity companies, including transparency in appointing senior managers, improved financial reporting, and performance contracts between these companies' management and executive boards. The Ministry of Industry, Energy and Fuel Resources is tasked with formulating and reviewing energy sector policy and enhancing the sector's regulatory framework.

B. Monetary and Financial Sector Policies

11. Price stability remains the overarching goal of monetary policy. The NBKR will seek to contain inflation at 5 percent during the year and, premised on further remonetization, the monetary program sets limits on the expansion of its net domestic assets consistent with reserve money growth of 25 percent and broad money growth of 30 percent. To keep liquidity expansion in check, the NBKR will further enhance its indirect monetary control instruments, price these

instruments flexibly, and maintain the managed exchange rate float that has served the country well. The NBKR will limit foreign exchange intervention to smoothing exchange rate fluctuations and securing the programmed buildup in international reserves. To enhance the credibility of macroeconomic policy, thereby bolstering investor confidence, every effort will be made to secure passage of pending legislation to strengthen the NBKR's autonomy. Meanwhile, we expect the independent review of the NBKR's internal audit function (a pending end-December 2006 structural benchmark) to be completed shortly with assistance from the Swiss National Bank, as part of the ongoing efforts to enhance the accountability of the NBKR.

12. Several measures have been introduced in recent years to strengthen the financial system, especially regarding supervision, the payment system, and curtailment of money laundering and the financing of terrorism. The authorities will introduce further measures to strengthen financial intermediation and pave the way for introduction of a mandatory deposit protection system for small depositors in 2008. In anticipation of a further rapid credit expansion, they will step up supervision (including through strict enforcement of procedures for tracking market, operational and country risks), and clearly delineate the supervisory responsibilities of the Service for Supervision and Regulation of Financial Market (SSRFM), while establishing a framework to share information between the SSRFM and the NBKR. Meanwhile, the SSRFM will strengthen supervision of insurance companies and financial institutions operating in the stock exchange. To enhance the payments system, the NBKR will make the real-time gross settlement (RTGS) system fully operational by end-2007, and the government will submit to the parliament enabling legislation to enhance flexibility in the use of bank accounts (including demand deposits) for settlement purposes by legal entities and physical persons. Furthermore, to ensure finality of bank resolution, the government will secure passage of amendments to the bank bankruptcy law modifying provisions introduced last September that allowed reinstatement of insolvent and liquidated banks.

13. The government remains committed to the privatization of the Kyrgyz Agricultural Finance Corporation, which has since been transformed into a Rural ("Ayil") Bank to enhance its growth potential. The government is studying two options for privatizing the Ayil Bank, namely (a) issuing a privatization tender under the current paid up capital, or (b) inviting private investors to raise the banks' capital and formulate a business plan conducive to subsequent disposal of the government's shares on more attractive terms. The government will decide on the preferred route by end-April 2007, in consultation with the World Bank, the Asian Development Bank (AsDB) and the European Bank for Reconstruction and Development (EBRD).

14. To help mobilize the significant domestic savings needed to underpin rapid growth, the government will foster development of the capital market and ensure its effective supervision. In this connection, and to encourage mortgage and other term lending, it will submit to parliament amendments to the civil, housing and land codes, and to the laws governing collateral, strengthening the legal foundations for using and seizing collateral in cases of default. We will continue the phased redemption of government bonds against a similar amount of government deposits at the central bank, redeeming som 200 million in 2007 for reissue to banks, and will simplify the nomenclature of public debt instruments. The authorities will ensure that any restructuring of government liabilities to the NBKR will not adversely impact the balance sheet of the NBKR.

C. Other Structural Reforms

15. As part of our ongoing agenda to improve the business climate and strengthen the legal foundation for private property, we reaffirm our commitment to the blueprint outlined in the CDS to boost private sector-led growth. In particular, we will promote transparency and efficiency in public administration, and in order to enhance the business environment, we will continue to simplify licensing procedures, streamline regulatory bodies, improve the autonomy and efficacy of the judiciary, and propose legal steps to strengthen property rights. These reforms will be supported by technical (and possibly financial) assistance from multilateral and bilateral donors involved in these areas.

D. Program Monitoring

16. The program will continue to be monitored through semi-annual reviews. For that purpose, we have set quantitative performance criteria (PCs) for end-December 2007 (along with proposed modifications to the end-June PCs established during the third review), and semi-annual indicative targets for reserve money and the electricity sector's quasi-fiscal deficit. We will make every effort to comply with the missed structural benchmarks for end-December 2006, and have set benchmarks for end-September and end-December 2007 (see Table 2). To better align the fiscal stance with the overarching goal of securing debt sustainability, we will henceforth treat the overall deficit of the general government as the key fiscal indicator that will be treated as a PC under the program. Completion of the fifth review later this year will, hinge on observance of the end-June 2007 quantitative PCs outlined in Table 2. Detailed definitions and reporting requirements for all quantitative PCs and data sources are presented in the attached Technical Memorandum of Understanding.

Table 1. Kyrgyz Republic: Quantitative Program Targets for 2005–07 1/

(In millions of soms, unless otherwise indicated; eop)

	2005	2006			2007	
	December	December			June	Dec.
	Actual	IMF/CR/06/235 2nd Review	IMF/CR/07/135 3rd Review	Act.	Rev. Prog.	Prog.
I. **Performance criteria**						
1. Floor on net international reserves of the NBKR in convertible currencies (eop stock, in millions of U.S. dollars)	416	457	518	606	658	787
2. Ceiling on net domestic assets of the NBKR (eop stock)	-1,943	-1,469	-2,034	-2,559	-1,094	-1,769
3. Ceiling on cumulative primary deficit of the general government	3,229	3,701	3,221	2,459	…	…
4. Ceiling on cumulative overall deficit of the general government	…	…	…	…	1,665	3,937
5. Cumulative floor on state government tax collections in cash	16,361	17,650	18,431	19,981	10,246	23,141
6. Ceiling on the stock of central government budget arrears	0	0	0	0	0	0
7. Ceiling on the stock of Social Fund pension arrears	0	0	0	0	0	0
8. Cumulative floor on payroll collections in cash of the Social Fund	4,912	4,823	4,945	5,528	2,864	5,738
9. Ceiling on the stock of Social Fund arrears to the Medical Insurance Fund	0	0	0	0	0	0
10. Ceiling on contracting or guaranteeing by the state government, NBKR or any other agency acting on behalf of the state government, of new nonconcessional external debt with maturity of less than one year (continuous, in millions of U.S. dollars)	0	0	0	0	0	0
11. Ceiling on contracting or guaranteeing by the state government, NBKR or any other agency acting on behalf of the state government, of new nonconcessional external debt with maturity of one year or more (millions of U.S. dollars)	0	0	0	0	0	0
12. Ceiling on accumulation of new external payment arrears (continuous, in millions of U.S. dollars)	0	0	0	0	0	0
II. **Indicative targets**						
1. Ceiling on reserve money (eop stock)	15,466	17,708	19,642	22,806	24,177	28,499
2. Ceiling on the cumulative quasi-fiscal deficit of the electricity sector (in millions of soms)	7,609	6,509	6,509	6,127	3,822	6,633
3. Ceiling on contracting or guaranteeing by the state government or NBKR of new concessional external debt (in millions of U.S. dollars) 2/			(as specified in the TMU)			

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

1/ Definitions are provided in the TMU.

2/ New concessional loans during the year.

Table 2. Kyrgyz Republic: Structural Conditionality

I. September–December 2006

Structural benchmarks for end-September 2006

- Prepare an action plan to reduce the energy sector's quasi-fiscal deficit in close cooperation with World Bank staff, addressing problems of transmission and distribution losses, payment indiscipline, and tariff adjustment. [Observed]

- Expand the operation of the Large Taxpayers Unit to cover at least 60 percent of tax revenues. [Observed]

Structural benchmarks for end-December 2006

- Conduct an independent review of the NBKR's internal audit function. The review could be performed by the internal audit department of another central bank, and should include a review of the capacity of the NBKR's internal audit division, as recommended by the Safeguards Assessment Report conducted by Finance Department in 2005. [Not observed]

- Bring KAFC to the point of sale and issue a privatization tender for the company. [Not observed]

- Submit to IMF staff a report prepared by the ministry of labor and social protection recommending measures to improve labor market flexibility. [Observed]

- Secure approval of legislation that has been already sent to parliament to enhance the NBKR's legal independence and ensure legal protection of its employees in performing official duties. [Not observed]

II. March–December 2007

Structural benchmarks for end-March 2007

- The government will submit to parliament amendments (drafted by the NBKR) to the civil, housing and land codes, as well as to all the laws governing collateral, in order to harmonize provisions on collateralized lending by financial institutions and facilitate collateral seizure in cases of default. [Not observed]

- Approval of the tax code bill that is before parliament. [Not observed]

- The government will adopt a new medium-term external debt management strategy aimed at ensuring external debt sustainability as described in paragraph 24 of the MEP for the third review under the arrangement. [Not observed]

Structural benchmarks for end-June 2007

- The NBKR will implement regulations for consolidated supervision to monitor risks faced by financial institutions, in line with the recommendations of the 2005 Basel Core Principles for Effective Banking Supervision Assessment.

- The government will introduce a new and detailed budget classification, based on the best practice reporting of government finances (GFS 2001), which will permit monitoring of poverty reducing expenditures in the monthly budget execution reports.

Table 2 (Concluded). Kyrgyz Republic: Structural Conditionality

Structural benchmarks for end-September 2007

- Submit to IMF staff a written Memorandum of Understanding agreed between the NBKR and the Service for Supervision and Regulation of Financial Market (SSRFM), delineating the specific supervisory responsibilities of the SSRFM and establishing modalities for information-sharing between them, as recommended by the FSAP update mission.

- Submit to parliament an internal audit law for government agencies in line with best international audit practices, in order to establish an appropriate framework for internal public sector controls.

Structural benchmarks for end-December 2007

- To ensure finality of bank resolution, the government and the NBKR will secure parliamentary approval of further amendments to the bank bankruptcy law modifying the provisions introduced in September 2006, which allowed reinstatement of banks that are insolvent and in the process of liquidation.

- Submit to IMF staff a best-practice, time-bound action plan to modernize customs administration, including greater selectivity of customs control based on risk criteria and expanding post-clearance audits.

- Submit to parliament enabling legislation to enhance flexibility in the use of bank accounts (including demand deposits) for settlement purposes by legal entities and physical persons.

Attachment III. Kyrgyz Republic: Technical Memorandum of Understanding

III. Introduction

1. The Kyrgyz Republic's performance during the period January 1, 2005–December 31, 2007 under the three-year PRGF-supported program will be assessed by the IMF on the basis of the observance of quantitative performance criteria and structural benchmarks. This updated memorandum and its attached tables define the quantitative performance criteria and indicative targets under program supported by the Poverty Reduction and Growth facility (PRGF) arrangement.[3] This update reflects the changes made to the program as specified in the Memorandum of Economic Policies (MEP) for the fourth review under the arrangement.

2. The program exchange rate of the Kyrgyz som to the U.S. dollar is set at som 38.5 = $1. The corresponding cross exchange rates and program gold price for 2007 are provided in Table 11.

IV. Quantitative Performance Criteria

3. The quantitative targets (i.e., quantitative benchmarks for end-March and end-September 2007, and quantitative performance criteria for end-June and end-December 2007) presented in Table 1 and 2 of the MEP are defined below.

Floor on net international reserves of the National Bank of the Kyrgyz Republic (NBKR) in convertible currencies

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

5. 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 or with foreign banks, and debt instruments (including accrued interest). Amounts pledged as collateral or in swaps or otherwise blocked, capital subscriptions in foreign financial institutions, and illiquid assets of the NBKR are excluded. Also excluded are net forward positions, defined as the difference between the face value of foreign currency denominated NBKR off-balance sheet claims on nonresidents and foreign currency obligations to both residents and nonresidents. In addition, net claims on other Commonwealth of Independent States (CIS) countries are excluded from the floor. For program monitoring purposes, gross international reserves shall be valued at program exchange rates and gold prices.

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[3] Central government and republican government are synonymous in this memorandum. The State government comprises central and local governments. The general government comprises the state government, the Social Fund, and the Development Fund that was established on [date].

6. Total international reserve liabilities of the NBKR in convertible currencies shall be defined as outstanding liabilities to the IMF and other convertible currency liabilities to nonresidents with an original maturity of up to and including one year. For program monitoring purposes, total international reserve liabilities shall be valued at the program exchange rates as described in paragraph 2 above. Thus calculated, the stock of net international reserves in convertible currencies amounted to $605.8 million as of December 31, 2006.

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

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

(In millions of U.S. dollars)

September 30, 2006 (benchmark)	413
December 31, 2006 (performance criterion)	457
March 31, 2007 (benchmark)	572
June 30, 2007 (performance criterion)	658
September 30, 2007 (benchmark)	709
December 31, 2007 (performance criterion)	787

1/ End-of-period stocks.

8. The floor on net international reserves of the NBKR will be adjusted:
(a) upward/downward by 100 percent for any excess/shortfall in net foreign financing defined in paragraph 9 below; (b) upward by 30 percent for any nonprogrammed cash grants; and (c) upward/downward by 100 percent for any excess/shortfall in cash privatization receipts in foreign exchange. Valued at the program exchange rate, the program cash privatization receipts are equivalent to $5 million in 2007. The total adjustment in respect of adjustors (a) and (c) is to be limited to $25 million, valued at the program exchange rate.

9. ‘Net foreign financing and cash grants’ is defined as balance of payment support loans, plus cash grants to the state government budget, plus any changes in the balance of unused PIP funds held at the NBKR, minus amortization (excluding repayments to the Fund) and interest payments on external debt made by the Ministry of Finance, and the NBKR. This definition applies to the adjustors to both the NIR and the NDA. The program cumulative net foreign financing is given in Table 2. The balance of unused PIP funds was equivalent to $36.16 thousands as of December 31, 2006.

Table 2. Projected Net Foreign Financing and Cash Grants 1/

(In millions of U.S. dollars)

September 30, 2006	1.6
December 31, 2006	18.4
March 31, 2007	0.8
June 30, 2007	-11.6
September 30, 2007	13.6
December 31, 2007	-1.4

1/ Cumulative from the beginning of the calendar year.

Ceiling on the net domestic assets of the NBKR

10. Net domestic assets of the NBKR are defined as reserve money of the NBKR (defined below), minus the NBKR's net foreign assets,[4] 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 (Equation 1).

(1) NDA=RM–NFA–MLT–Turkish Loan–EBRD-IDA Enterprise Loan

11. 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 minus som 2,559 million on December 31, 2006.

[4] The NBKR's net foreign assets consist of net international reserves, as defined in this TMU, plus other foreign assets, plus the net claims on other CIS countries.

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

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

(In millions of soms)

September 30, 2006 (benchmark)	-1,413
December 31, 2006 (performance criterion)	-1,469
March 31, 2007 (benchmark)	-1,958
June 30, 2007 (performance criterion)	-1,094
September 30, 2007 (benchmark)	-1,332
December 31, 2007 (performance criterion)	-1,769

1/ End-of-period stocks.

13. The ceiling on net domestic assets of the NBKR will be adjusted: (a) downward/upward by 100 percent of the excess/shortfall in net foreign financing of the state government budget; (b) downward by 30 percent for any nonprogrammed cash grants; and (c) downward/upward by 100 percent of the excess/shortfall of cash privatization receipts. The total adjustment for shortfalls in adjustors (a) and (c) is to be limited to $25 million, valued at the program exchange rate.

Ceiling on the cumulative overall deficit of the general government

14. The overall deficit of the general government is defined as the sum of: (a) 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 general government; (b) the change in the stock of net claims of the foreign banking system and nonfinancial institutions and households on the general government; (c) net privatization receipts including from Centerra share sales; (d) net foreign loans disbursed to the state government for budgetary support; and (e) net foreign loans disbursed to the general government for project financing. The fiscal balance will be measured at the program exchange rates, unless foreign currency-denominated assets or liabilities are converted into domestic currency upon receipt or accrual.

15. The change in the stock of net claims of the domestic banking system on the general government is defined as the change in the stock of the banking system claims on the general government, less the change in the stock of all deposits of the general government with the banking system. The claims of the banking system on the general government include: (a) bank loans to the general government; (b) securities or bills issued by the general government held by banks, with the exception of those issued in relation with bank rescue operations; and (c) overdrafts on the current accounts of the general government with banks.

16. The program ceilings on the cumulative overall deficit of the general government are reported in Table 4 below.

Table 4. Ceilings on the Operations of the General Government 1/

(In millions of soms)

	Primary Deficit (before grants)	Overall Deficit
September 30, 2006 (benchmark)	2,541	...
December 31, 2006 (performance criteria)	2,541	...
March 31, 2007 (benchmark)	589	...
June 30, 2007 (performance criteria)	...	1,666
September 30, 2007 (benchmark)	...	2,773
December 31, 2007 (performance criteria)	...	3,937

1/ Cumulative beginning from the beginning of the calendar year.

Cumulative floor on state government tax collections in cash

17. Tax collections in cash correspond to the line "IV. Tax Receipts" in the Treasury Report and comprise the following categories: 1.0 tax on income and profits; 2.0 taxes on goods and services; 3.0 specific taxes on services; 4.0 taxes on property; and 5.0 taxes on international trade. Cumulative tax collections in cash include collections of tax arrears but exclude tax offsets.

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

Table 5. Floors on State Government Cash Tax Collections 1/

(In millions of soms)

September 30, 2006 (benchmark)	12,512
December 31, 2006 (performance criterion)	17,650
March 31, 2007 (benchmark)	4,236
June 30, 2007 (performance criterion)	10,246
September 30, 2007 (benchmark)	16,293
December 31, 2007 (performance criterion)	23,141

1/ Cumulative from the beginning of the calendar year.

Ceiling on the stock of central government budget arrears

19. For the purposes of the program, central government budget arrears are defined as an overdue payment obligation of the republican budget arising since the start of the three-year program period (January 1, 2005) and related to: (a) wages; (b) Social Fund payroll contributions; (c) mandatory transfers to the Social Fund; (d) categorical grants; (e) payments of electricity bills; and (f) allowances to poor families. A payment is defined to be overdue if it remains unpaid after its due date for (c) and (d); for 30 days after its due date for (a) and (b); for 60 days after its due date for (e); and for 40 days after its due date for (f). The program ceilings on the stock of central government budget arrears are zero at each test date.

Ceiling on the stock of Social Fund pension arrears

20. A pension payment by the Social Fund is defined as overdue if it has come due since the start of the three-year program period (January 1, 2005) and remains unpaid for 30 days or more after its due date. The program ceilings on the stock of Social Fund pension arrears are zero at each test date. No new pension arrears will be accumulated.

Floor on the Social Fund payroll tax collections in cash

21. Payroll tax collections in cash correspond to the total cash contributions collected by the Social Fund from both employers and employees for a given period.

22. The program floors for the Social Fund tax collections in cash are reported in Table 6 below.

Table 6. Floor on Social Fund Cash Payroll Tax Collections 1/

(In millions of soms)

September 30, 2006 (benchmark)	3,430
December 31, 2006 (performance criterion)	4,823
March 31, 2007 (benchmark)	1,372
June 30, 2007 (performance criterion)	2,863
September 30, 2007 (benchmark)	4,276
December 31, 2007 (performance criterion)	5,736

1/ Cumulative from the beginning of the calendar year.

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 to arrears incurred starting January 1, 2005. A transfer is defined to be overdue if the value date of any transfer obligation is more than five business days after the due date. The program ceilings on the stock of Social Fund pension arrears to the Medical Insurance Fund are zero at each test date.

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

24. 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).[5]

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[5] 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. Debt can take a number of forms, the primary ones being as follows: (a) 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); (b) 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 (c) 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

(continued…)

25. External debt ceilings apply to (a) 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 (b) 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 nonconcessional external debt is zero as specified in Table 2 of the MEP.

26. For the purposes of the ceiling on contracting and guaranteeing new external debt, any other agency acting on behalf of the state government will in particular include all nonfinancial public enterprises with share capitals of not less than Kyrgyz som 100 million in which the state government holds at least 51 percent of the share capital (The public enterprises listed in Table 12 currently meet the foregoing criteria) and the Development Fund.

Ceiling on new external payments arrears

27. For the purposes of the program, external payment arrears will consist of all debt-service obligations (i.e., payments of principal or interest) arising in respect of any debt contracted or guaranteed or assumed by the state government of the Kyrgyz Republic, or the NBKR, or any agency acting on behalf of the state government of the Kyrgyz Republic since the Kyrgyz Republic's independence, including, without limitations, unpaid penalties, interest charges or judicially awarded damages associated with these arrears owed by the state government of the Kyrgyz Republic, or the NBKR, or any agency acting on behalf of the state government of the Kyrgyz Republic, on imports received subsequent to independence. The ceiling on new external payment arrears shall apply on a continuous basis throughout the period of the PRGF arrangement.

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expected service life of the property, while the lessor retains the title to the property. For the purpose of the guideline, the debt is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement excluding those payments that cover the operation, repair or maintenance of the property.

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

III. INDICATIVE TARGETS

Ceiling on reserve money

28. 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 indicative program limits are reported in Table 7 below.

Table 7. Ceilings on Reserve Money 1/

(In millions of soms)

September 30, 2006	15,905
December 31, 2006	17,708
March 31, 2007	20,617
June 30, 2007	24,177
September 30, 2007	25,918
December 31, 2007	28,499

1/ End-of-period stocks.

Ceiling on the quasi-fiscal deficit of the electricity sector

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

(1) $QFD = Q*MC - R$;

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

(3) $R = (\sum Ci) * T * Ccash$,

where:

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

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

R is the total cash revenue;

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

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

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

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

30. For the purposes of the program, the marginal cost of production is equal to 2.3 U.S. cents per kilowatt hour for 2006 and 2.8 U.S. cents for 2007, and normative losses (including own-use) are defined as 15 percent of domestic supply. Total billing of end-users is defined as consumption times the posted nominal tariff. The cash collection component is the amount of bills paid in cash to the energy companies, and excludes any form of cash-to-cash settlements, off-sets, barters, or other noncash payments. The indicative ceiling on the quasi-fiscal deficit in the electricity sector is as follows (Table 8).

Table 8. Ceiling on Quasi-Fiscal Deficit of the Electricity Sector 1/

(In millions of soms)

June 30, 2006	3,745
December 31, 2006	6,509
June 30, 2007 2/	3,822
December 31, 2007 2/	6,633

1/ Cumulative from the beginning of the calendar year.
2/ At new cost recovery rate.

Ceiling on contracting or guaranteeing of concessional external debt

31. The annual ceiling on the contracting or guaranteeing of new concessional external debt by the state government of the Kyrgyz Republic or the NBKR or any other agency working on behalf of the state government is set by the U.S. dollar nominal sum of project loan agreements yet to be signed and agreed, plus balance of payments support loans required to fill the external financing gap, as programmed. Pursuant to monitoring this indicative target ceiling, the Ministry of Finance will provide quarterly information on the total nominal U.S. dollar value of: (a) new project and program loans signed and agreed during the previous three-month period; and (b) new project and program loans planned, but yet to be signed and agreed, during the previous three-month period. The annual indicative ceilings on the contracting or guaranteeing of new medium- and long-term concessional external loans for 2007 are specified in Table 9.

Table 9. Annual Indicative Ceiling on Contracting and Guaranteeing of New Concessional Loans in 2007 1/

With disbursements beginning in	In millions of U.S. dollars
2007	106
2008	11

1/ New concessional loans signed in 2006, excluding contingency amounts.

These ceilings are nominal debt lumped by the year in which their disbursements commenced. For 2007, the limit implies contracting loans of which $106 million will start disbursing in 2007 and $11 million in 2008.

32. 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. The average of the CIRRs over the last 10 years will be used for debts with maturity of at least 15 years and the average CIRR of the preceding six months will be used for shorter maturities.

IV. Reporting Requirements Under the Program

33. The government and the NBKR will provide the Fund with the necessary economic and financial statistical data to monitor economic developments and the quantitative targets. In particular, the government and the NBKR will provide the following specific information:[6]

The balance sheet of the NBKR

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

Monetary survey

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

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

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

International reserves and key financial indicators

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

Banking system data

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

External debt

39. The Ministry of Finance, together with the NBKR, will provide monthly information on the disbursements, principal and interest payment—both actual and falling due; on contracting and guaranteeing of medium- and long-term external loans by the state government and the NBKR; and any stock of outstanding arrears on external debt service payments within 21 days of the end of each month. In addition, the Ministry of Finance will 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 extra budgetary data

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

41. The Ministry of Industry, Energy and Fuel Resources, in consultation with the Ministry of Finance, and the World Bank, will submit to Fund staff each March and September a semi-annual report on the electricity sector QFD according to the format specified in Table 10 below.

Balance of payments data

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

Other general economic information

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

Table 10. Kyrgyz Republic: Electricity Quasi-Fiscal Deficit

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

1/ Generation plus imports minus exports minus normative losses.
2/ Excess technical and commercial losses as percent of production.
3/ Average posted tariff, calculated as quotient of total bill and consumption volume.
4/ Nominal tariff times cash collection rate
5/ Marginal costs, derived from marginal incremental capital cost.

Table 11. Program Cross Exchange Rates

	Currency Names	National Currency/US$	US$/National Currency
SDR		0.6653	1.5032
GBP	UK pound sterling	0.5099	1.9611
DKK	Danish krone	5.6646	0.1765
EUR	Euro	0.7597	1.3163
INR	Indian rupee	44.2580	0.0226
CAD	Canadian dollar	0.8616	1.1606
CNY	Chinese yuan	7.8065	0.1281
KRW	South Korean won	929.8488	0.0011
NOK	Norwegian krone	6.2800	0.1592
TRL	Turkish lira (new)	0.7080	1.4125
SEK	Swedish krona	6.8770	0.1454
CHF	Swiss franc	0.8193	1.2206
JPY	Japanese yen	118.8954	0.0084
AZM	Azerbaijani new manat	1.1474	0.8715
AMD	Armenian dram	363.4299	0.0028
BYR	Belarusian rubel	2139.9832	0.0005
KZT	Kazakh tenge	126.9947	0.0079
LVL	Latvian lats	0.5360	1.8657
LTL	Lithuanian litas	2.6304	0.3802
MDL	Moldovan lei	12.9049	0.0775
RUR	Russian ruble	26.3796	0.0379
TJS	Tajik somoni	3.4265	0.2918
UZS	Uzbek sum	1237.7857	0.0008
UAH	Ukrainian hryvnia	5.0500	0.1980
EEK	Estonian kroon	11.8873	0.0841
AUD	Australian dollar	0.7907	1.2641
	Gold ($/troy ounce)		635.0000

Table 12. List of Public Enterprises Covered under Performance Criteria on Contracting and Guaranteeing New External Debt (¶26 of the TMU).

JSC Electrical Stations
JSC National Electrical Grid of Kyrgyzstan
JSC Kyrgyzaltyn
JSC Kyrgyztelecom
JSC International Airport Manas
JSC Severelectro
JSC National Air Company
JSC Jibek Jolu
JSC Bishkek Teploset
JSC Kyrgyzneftegas
JSC Bishkek Machinery Plant
JSC Kadamjai Antimony Plant
JSC Jalal-Abadelectro
JSC Kyrgyzgas
JSC Kara Balta Mining Plant
JSC Vostokelectro
JSC Oshelectro
State JSC Kyrgyzgasmunaizat

INTERNATIONAL MONETARY FUND

KYRGYZ REPUBLIC

Fourth Review Under the Three-Year Arrangement Under the Poverty Reduction and Growth Facility and Request for Modification of Quantitative Performance Criteria—Informational Annex

May 2, 2007

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ANNEX I. KYRGYZ REPUBLIC—RELATIONS WITH THE FUND
(As of March 31, 2007)

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

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

III. SDR Department	**SDR Million**	**Percent of Allocation**
Holdings	17.87	N/A

IV. Outstanding Purchases and Loans	**SDR Million**	**Percent of Quota**
PRGF Arrangements	103.92	117.03

V. Latest Financial Arrangements

Type	**Approval Date**	**Expiration Date**	**Amount Approved (SDR Million)**	**Amount Drawn (SDR Million)**
PRGF	03/15/2005	03/14/2008	8.88	5.07
PRGF	12/06/2001	03/14/2005	73.40	73.40
PRGF	06/26/1998	07/25/2001	73.38	44.69

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

	Forthcoming				
	2007	2008	2009	2010	2011
Principal	11.65	14.80	14.73	16.24	15.31
Charges/Interest	0.50	0.42	0.34	0.27	0.19
Total	12.15	15.22	15.07	16.50	15.50

VII. Status of HIPC and MDRI Assistance

The Executive Board considered the preliminary HIPC document on October 13, 2006. However, following a cabinet change earlier this year, the authorities have decided not to avail themselves of HIPC and MDRI assistance.

VIII. Safeguards Assessments

Under the Fund's safeguards assessment policy, the National Bank of the Kyrgyz Republic (NBKR) is subject to an assessment with respect to the PRGF arrangement, which was approved on March 15, 2005. An updated safeguards assessment of the NBKR was completed on October 14, 2005. The assessment found that the NBKR's safeguards framework has been strengthened since the previous assessment completed in 2002. However, a number of areas were identified where further steps would solidify the progress achieved, which include improving oversight of the audit processes and the internal control systems by establishing an audit committee, strengthening the legal framework for NBKR's autonomy, and enhancing the NBKR's internal audit function.

IX. Exchange Rate Arrangements

The currency of the Kyrgyz Republic has been the som (100 tyiyn =1 som) since May 15, 1993. The Kyrgyz Republic's exchange regime is classified as a managed float with no preannounced path for the exchange rate. The NBKR publishes daily the exchange rate of the som in terms of the U.S. dollar, which is determined in the interbank foreign exchange market. The Kyrgyz Republic maintains an exchange system that is free of restrictions on the making of payments and transfers for current international transactions, except for exchange restrictions maintained for security reasons relating to the restriction of financial transactions and the freeze of accounts of certain individuals or organizations associated with terrorism pursuant to (i) relevant UN Security Council resolutions and (ii) the list of current terrorist organizations designated by the U.S. Secretary of State. The authorities are in the process of notifying these measures to the Fund pursuant to Executive Board decision No. 144-(52/51).

X. Article IV Consultations

The Kyrgyz Republic is on the 24-month consultation cycle. The last Article IV consultation discussions were held in August 2006 and were completed by the Executive Board in November 2006.

XI. FSAP Participation and ROSC Assessment

An FSAP update mission in October 2006 reviewed progress since the 2002 assessment, and the Board is scheduled to consider the Financial System Stability Assessment (FSSA) along with the 4th PRGF review. A fiscal ROSC mission was held in March 2001 and the ROSC Fiscal Transparency Module was published on March 13, 2002. A data ROSC mission was held in November 2002 and the ROSC Data Module was published on November 10, 2003. A new fiscal ROSC assessment mission is tentatively scheduled for early May 2007.

XII. Resident Representative

The seventh resident representative of the Fund in the Kyrgyz Republic, Mr. McHugh, took up his post in Bishkek in late September 2006.

ANNEX II. KYRGYZ REPUBLIC—RELATIONS WITH THE WORLD BANK GROUP
(As of April 12, 2007)

1. The last CAS covering FY03–06 has been completed in July 1, 2006. Currently the WB Country team jointly with four development partners (ADB, DFID, SWISS, and UN Agencies) is on final stage of developing new joint Country Support Strategy (JCSS) covering the period of FY 07-10. The proposed JCSS is based on the government's Country Development Strategy (equivalent of PRSP) which sought to capitalize on major reforms to date while maintaining a reform and growth course that will reduce poverty and enhance prospects for debt sustainability. The JCSS 2007-2010 Board discussion is planned for June 19, 2007.

2. Until the new JCSS is approved, the World Bank Group's operational objective for the next four months is to continue supporting the ongoing government's efforts to improve governance, energy sector performance, the business environment, the banking sector, public expenditure management, intergovernmental finance, the pension system, social protection, health, water and sanitation, and agriculture, and to enhance the portfolio performance. It will continue assisting the government with economic sector work and capacity building.

3. **International Development Association (IDA)**. Since the Kyrgyz Republic joined the World Bank in September 1992, it has received commitments of $776.3 million for 38 IDA-funded projects, out of which $607.1 million have already been disbursed. Out of 19 operations totaling $481 million completed so far, seven structural adjustment credits provided quick disbursing support for the government's economic reform programs in privatization, enterprise restructuring, agricultural policy, financial sector, public sector resource management, pension reform and energy reform. Twelve investment operations supported reform and rehabilitation of the telecommunications sector, social safety nets, health, rural finance, private enterprises and livestock development.

4. The active Bank portfolio in the Kyrgyz Republic comprises 19 operations with total commitments of $254.3 million, of which $138.2 million (54 percent) remains to be disbursed. Four new projects: Avian Influenza Control, Water Management Improvement, Second Village Investment Project, and Reducing Technical Barriers for Entrepreneurship and Trade have been approved by Board and became effective in FY07. In addition to the country portfolio, the Kyrgyz Republic also benefits from the regional HIV/AIDS project.

5. There are currently five projects under preparation: (i) The repeater On- Farm Irrigation (second phase of On-Farm Irrigation project), (ii) Strengthening the National Statistical System, (iii) Bishkek-Osh Infrastructure, (iv) Agricultural Investment and Know How (ASSP- 2), and (v) Tien Shan Biodiversity Project (second phase of regional Biodiversity project). The second On-Farm Irrigation project is planned to go the Board this fiscal year, meanwhile other projects undergoing various stages of preparation process

6. **International Finance Corporation (IFC).** The IFC strategy in Kyrgyz Republic is focused on institution and capacity building through investment and technical assistance to promote private sector development, especially small and medium-size enterprises (SMEs), and support the transformation into a market-based economy. IFC's investments grew steadily to $57 million, since 1996. The committed IFC portfolio as of April 1, 2007 stands at $15 million, with

$14 million disbursed (77% in financial markets, 9% in general manufacturing and 14% in agribusiness).

7. The largest investment in the existing portfolio was the Kumtor Gold Mine, with further investments in a packaging plant “Altyn-Ajydar”, pasta plant “Akun”, four financial sector projects Demirbank, KICB, FINCA and Bai-Tushum. Under the framework of MSEF joint project with EBRD, IFC has provided credit lines to local banks as AKB Kyrgyzstan, Ineximbank and Kazcommertsbank.

8. IFC has completed 14 technical assistance projects in the areas of: (i) institutional and capacity building in the financial sectors including leasing, microfinance, (ii) creating favorable business environment for SMEs, (iii) improvement of investment climate, and (iv) developing capacity building for tourism. In 2005, IFC launched two technical assistance projects to improve legal, regulatory and tax framework for housing finance and leasing. It started the second stage of IFC Central Asian Primary Market Development Project in 2007, and will continue the second phase of IFC Central Asian Regional Leasing project. It will also start a regional technical assistance project to improve corporate governance in enterprises of Central Asia including Kyrgyzstan.

Multilateral Investment Guarantee Agency (MIGA). MIGA has supported private sector development in the Kyrgyz Republic by extending guarantees to foreign direct investments in four projects in the manufacturing, services, and mining sectors. MIGA’s current portfolio in the Kyrgyz Republic consists of two projects, financed by Austrian and Italian investors, in support of the country’s services sector. The combined gross exposure from these projects is US$14.8 million. Two claims have been filed relating to projects guaranteed by MIGA. One of them is the Kyrgyz Airlines project in which the Government of the Kyrgyz Republic cancelled the airline's license to operate, alleging that the investor breached material obligations under the license agreement. The case is in arbitration in London. The second dispute relates to the Manas Management Company project which handles the catering and cargo operations of the Manas International Airport in Bishkek. MIGA is seeking to settle the dispute through mediation, and is in close contact with both the Kyrgyz authorities and the investors for this purpose. . Recently, a draft settlement agreement was discussed in detail by the two parties at a mediation facilitated by the Agency. At present, the Government is reviewing some terms relating to the settlement and the investors are awaiting outcome. Due to the recent changes in the Government the process is taking much longer than anticipated. The total amount of foreign direct investment facilitated by MIGA guarantees is over $360 million. At present, there are no projects involving the Kyrgyz Republic in MIGA’s FY07 pipeline.

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ANNEX III. KYRGYZ REPUBLIC—RELATIONS WITH THE ASIAN DEVELOPMENT BANK (ADB)

(As of March 31, 2007)

1. The Kyrgyz Republic became a member of ADB in 1994 and began receiving assistance in the same year. The country has received 26 loans and 3 grants for a total amount of $634 million. Seven out of the 26 loans are program loans totaling $199.5 million provided to support policy reforms to facilitate the transition to a market economy. The remaining 19 are project loans and three project grants totaling $434.5 million provided to support various investment activities. At present, eight loans with approved loan amount of $183.3 million are ongoing and one loan in amount of $15 million is awaiting effectiveness. These loans have an un-disbursed balance of $106 million as of March 31, 2007. All these loans were provided on concessional terms from the Bank's special fund resources—Asian Development Fund (ADF). In addition, ADB had provided 65 technical assistance (TA) projects amounting to $38 million as of today. Of these, 18 are project preparatory TAs amounting to $11.7 million and the remaining 47 TAs for $26.2 million are advisory TAs for capacity building, policy advice, institutional strengthening and training. The Kyrgyz Republic has also received six JFPR Grants amounting to $6 million.

2. The transport and communications sectors accounted for the largest share of ADB assistance, followed by the multisector, and law, economics and public policy. The current Country Strategy and Program Update (CSPU) for 2006–2008 (approved in November 2005), confirms ADB priorities of (i) investing in agriculture, which is key to pro-poor growth; (ii) reforming the financial sector to stimulate domestic savings and investment; (iii) improving trade and road linkages with regional markets; and (iv) selectively supporting human development, particularly basic education and early childhood development.

3. ADB's annual lending began with $40 million in 1994 and reached the peak level of $89.2 million by 1997. Thereafter, lending levels fell slightly and hovered between $65 million and $75 million through 2001. ADB's average annual lending level during 2002 and 2003 was $15.25 million. This was much lower than the lending levels in the past, largely due to the government's policy of restrained borrowings as part of its debt management strategy which envisaged a reduction in the size of the largely externally funded PIP from about 6 percent of GDP in 2001 to about 3.1 percent of GDP by 2006. The level of assistance for the block of two year 2005–06 was $60.8 million. The allocation for the block of two years 2007–08 is determined at $55 million. This program will be reviewed, based on the availability of ADF funds and the rules governing grants, to make it consistent with the Government's debt reduction strategy and the limits on the PIP.

4. The performance of ADB's portfolio is generally satisfactory, although one loan is rated at risk. The scarcity of budgetary resources, and ceilings on the externally funded PIP constituted the biggest risks to the country portfolio. ADB and the World Bank have thus

sought the removal of quarterly disbursement ceilings, which delay project implementation. In August 2005, IMF agreed to be more flexible in determining annual targets for the PIP, which is expected to improve portfolio performance.

5. The allocation of ADF resources to the country is based on the government's attainment of performance targets (triggers) in five areas: (a) making steady progress in macroeconomic management and structural reforms in the financial sector, and customs administration; (b) making progress in prioritizing on-going PIP projects; (c) adhering to the national debt reduction strategy; (d) finalizing the Country Development Strategy 2007-2010 (formerly called the NPRS); and (e) implementing a package of legal and judicial reforms for improving the investment climate for the private sector. Since 2005, up to 50 percent of ADF assistance to the country come in the form of grants.

6. The Kyrgyz Republic is one of the pilot countries selected for harmonization and alignment of donor procedures at the Rome Conference on harmonization held in February 2002. ADB coordinates its activities closely with the EBRD, IMF, IsDB, World Bank, the UN System, and bilateral donors at all levels of development cooperation. There have been significant strides forward in aid coordination since the last CG meeting held in Bishkek in November 2002, when both the Government and the donors agreed to focus on improving significantly coordination efforts. Since then efforts are being made to share sectoral and operational information and better coordinate lending and technical assistance activities. Since 2003, ADB and World Bank, which together account for over 75 percent of the PIP, conducts a joint portfolio review.

7. Kyrgyz Resident Mission participated actively in the harmonization working group and contributed to the development of the National Action Plan for Harmonization which was approved by the Government in February 2005. The areas identified for harmonization in the immediate future are: (a) procedures for procurement of goods and services; (b) financial management and monitoring of projects; and (c) project implementation units. World Bank and ADB procurement documentation has been harmonized in these areas.

8. Starting from September 2005, ADB together with other major bilateral and multilateral agencies (DFID, SDC/seco, UN, and WB) providing assistance to the Kyrgyz Republic is developing a Joint Country Support Strategy (JCSS) for the period 2007–10 to improve donor harmonization and alignment, and ensure more consolidated donor assistance to the country. The priority areas for JCSS are identified as its main pillars: (i) promoting private sector and economic growth, (ii) good governance and reducing corruption, and (iii) improving health, education and other social services.

Annex IV. Kyrgyz Republic—Relations with the European Bank for Reconstruction and Development (EBRD)

(As of March 31, 2007)

1. The EBRD facilitates the transition to a market-based economy through its direct support for private sector investment and key infrastructure, and targeted technical assistance. Under the Early Transition Countries' Initiative (ETCI) introduced in 2005, the Bank is able to more innovative respond to the Kyrgyz economic requirements. Therefore, the Bank is considering smaller, "more difficult" projects. The ETCI also foresees technical cooperation (TC) to support investment development.

2. According to the Strategy for the Kyrgyz Republic approved in November 2004, the Bank's priorities are to: (a) foster the private sector; (b) strengthen the financial sector; (c) provide support for essential infrastructure; and (d) strengthen the policy dialogue to improve the investment climate and support reform efforts. A new Strategy should be approved in the first 3-4 months of 2007; although the main activities are expected to remain the key focus.

3. As of April 2007, the Bank had approved 42 projects (including restructurings) bring around EUR 800 million of investment. The Bank has provided more then EUR 300 million of this amount.

4. During the past three years, the Bank expanded its activities in the financial sector to include:

- The Kyrgyz Micro and Small Enterprises Financing Facility (MSEFF). As of 28 February 2007, USD 184,995,454 (cumulative) had been disbursed in 76,915 loans to small and medium-size enterprises. Up to date MSEFF has helped to create or sustain 113 953 jobs. The Bank works with seven participating commercial banks and also with non banking institutions - Bai-Tushum, Aiyl Bank and FINCA.
- In 2006, the Bank signed a USD 1 million Guarantee in favour of Bai-Tushum to a local bank in Kyrgyz Republic which will provide local currency funds for on-lending to MSEs and solidarity groups.
- Equity investments in Ineximbank, Demir Bank, and KICB.
- Expansion of Trade Facilitation Program (TFP). Five banks are participants in the TFP.
- In 2004, the Bank signed a co-financing facility of USD 4 million to KICB. This new ETC product is provided to meet financing needs of emerging medium-sized private companies. The first sub loan agreement has been signed on December 26, 2005 for EUR 450,000.

Other major investments by the Bank during its operations in KR include:

- USD 20 million loan and USD 10 million sub debt, since converted into USD 17 m equity participation in Centerra Gold (the Bank's senior loan have been fully repaid).
- Loan to Hyatt-Regency Hotel, USD 6.3 million in 1997.
- Loan to Interglass plant, USD 6 million in 2004.

- Loan to Limatex (cotton-processing plant in Djalal-Abad), USD 1 million in 2005.
- Loan to Raduga Invest (resort on Issyk-Kul lake), USD 6 million in 2005.
- Loan to Karven Four Seasons (resort on Issyk-Kul lake), USD 3.8 million in 2006.

Although the Bank is currently unable to provide loans with sovereign guarantee the Bank continues to monitor public sector projects:

- Modernization of the telecommunications network (USD 7.9 million).
- Two projects to upgrade electricity transmission networks in Issyk-Kul and Talas regions (USD 63 million combined).

The Bank is working with the Government to consider non-sovereign financing of infrastructure – roads, telecoms and other infrastructure.

5. The Bank also implements grant-funded TC to support its investment portfolio, including the financial sector (including MSFF consultants among others), natural resources/environment, agribusiness and infrastructure. Recent TCs include:

- In telecoms, to advise on key reforms, including inter-capacity access arrangements;
- Training for judges in commercial law;
- Investor protection reform initiative;
- Roll out of the Business Advisory Service and Turn Around Management programs, providing consulting services to viable businesses.

6. Finally, the Bank maintains an active dialogue with the government. For example, the Bank was instrumental in founding the International Business Council, which is devoted to working with the government on improving the investment climate. The Bank is planning to help fund a new Investors Council under the President to address business concerns. The Bank also has provided guidance on legal reforms, such as the newly revised Law on Pledge.

ANNEX V. KYRGYZ REPUBLIC—TECHNICAL ASSISTANCE PROVIDED BY THE FUND
February 2003–December 2006

Dept.	Subject/Identified Need	Timing	Counterpart
FAD	Improving the Effectiveness of the Large Taxpayer Unit	February 24–March 7, 2003	Ministry of finance
	Treasury Management Information System	July 21–29, 2003	Ministry of finance
	VAT on agriculture	November 3–11, 2003	Ministry of finance
	Priorities for Tax Administration Reform	July 22–August 5, 2004	Ministry of finance
	Supporting Tax Administration Reform and installing new Expert Advisor	January 16–28, 2006	Prime minister's office
MFD	Review of the Capital Adequacy and Dividend Arrangements for the National Bank of the Kyrgyz Republic	August 18–28, 2003	National Bank of the Kyrgyz Republic
	Review of Debt Restructuring Operation and 2003 Financial Reporting	October 28–November 10, 2003	National Bank of the Kyrgyz Republic
	Monetary Operations, Banking System Development, and Central Bank Autonomy	September 13–23, 2004	National Bank of the Kyrgyz Republic
	Review of NBKR Debt Restructuring Arrangements, Options for Deepening Financial Markets and Amendments to the NBKR Law	December 7–18, 2004	National Bank of the Kyrgyz Republic
	Payments System	January 25–February 7, 2005, April 12–25, 2005, and October 18–27, 2005, February 20–March 5, 2006	National Bank of the Kyrgyz Republic
	Bank Supervision and Regulation	February 23–March 8, 2005, May 18–28, 2005, July 17–28, 2005, October 02–13, 2005, January 15–26, 2006, February 12–23, 2006, March 20–30, 2006	National Bank of the Kyrgyz Republic
	FSAP update	September 4–15, 2005	National Bank of the Kyrgyz Republic
	AML/CFT	April 19–25, 2006	National Bank of the Kyrgyz Republic
	Government Securities/Money Markets	August 25–30, 2006	National Bank of the Kyrgyz Republic

Annex V. (Concluded) Kyrgyz Republic—Technical Assistance Provided by the Fund
February 2003–December 2006

Dept.	Subject/Identified Need	Timing	Counterpart
LEG	Update of the AML/CFT Legislation (jointly with MFD)	February 5–11, 2004	National Bank of the Kyrgyz Republic
	Review of Bank Legislation	March 1–4, 2004 April 26–May 6, 2004	National Bank of the Kyrgyz Republic
	Review of Tax Legislation	July 27–August 5, 2004	Ministry of finance
	Assisting in drafting Tax Code	December 4–10, 2005	Prime minister's office
STA	SDDS Subscription	January 28–February 5, 2004	National Statistical Committee
	Balance of Payments Statistics	March 15–29, 2004	National Bank of the Kyrgyz Republic
	Monetary and Financial Statistics	April 27–May 11, 2004	National Bank of the Kyrgyz Republic

List of Resident Advisors

MFD	Banking Supervision/Restructuring Advisor	Mr. Svartsman	January 2004–January 2005
MFD	Public Debt Policy and Management	Mr. Azarbayejani	December 2002–December 2004
MCM	Debt Management and Development of Government Securities Management	Mr. Riecke	August 2006–August 2009

ANNEX VI. KYRGYZ REPUBLIC—STATISTICAL ISSUES

General framework

1. Data provision is adequate for surveillance. The three institutions responsible for collecting, compiling and disseminating macroeconomic statistics—the National Statistics Committee (NSC), the ministry of economy and finance (MOF), and the National Bank of Kyrgyz Republic (NBKR)—have legal and institutional environments that support statistical quality, and their respective staff are well versed in current methodologies. Unlike staff resources, however, computer and financial resources are generally not commensurate with current needs and therefore constrain statistical development, especially for the NSC.

2. The NSC maintains a comprehensive and regularly updated web site with data that largely incorporate international methodological recommendations and adequate coverage and timeliness (http://www.stat.kg). In February 2004, following improvements in compilation and dissemination of the reserves template and external debt data, the Kyrgyz Republic subscribed to the SDDS.

3. A data ROSC mission in November 2002 assessed the data dissemination practices against the GDDS and undertook an in-depth assessment of the quality of national accounts, prices, government finance, monetary, and balance of payments statistics. The mission concluded that the quality of the macroeconomic statistics had improved significantly in the last few years. The authorities had established a good track record of implementing recommendations of past technical assistance and had demonstrated commitment to pursue plans and programs to further improve their statistics. The mission recommended that a program of regular intersectoral consistency checks be introduced to reduce the sometimes significant, unexplained discrepancies between the government finance, monetary, and balance of payments datasets. The authorities' response to the data ROSC (posted on the IMF website (www.imf.org/external/np/rosc) includes an update on the status of implementation of the ROSC mission's recommendations.

National accounts

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

Prices, wages, and employment

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

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

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

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

Fiscal accounts

9. The scope of central government statistics falls short of international standards because it excludes data for the Social Fund and the externally financed Public Investment Program (these data are published separately). Other limitations involve the exclusion of financial transactions with domestic banks and the discrepancies between the deficit and financing data. While revenue and expenditure data generally accord with the *GFSM 1986*, there are misclassifications in both categories (for example, some nontax revenues are classified as taxes, and certain expenditure items are misclassified in the budget and treasury accounts). Monthly GFS data for *IFS* publication have been reported up to October 2006. Annual GFS data however, were not reported for the *GFS Yearbook.,* The latest data for the *GFS Yearbook* were for 2001, covering budgetary central government and local government operations.

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

Monetary sector

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

12. An STA mission on monetary and financial statistics visited Bishkek during April 27–May 11, 2004 to (a) follow up on the implementation of the ROSC recommendations; (b) expand the institutional coverage of the broad money survey; and (c) assist the NBKR in implementing the methodology in the *MFSM*. It found that the NBKR had made substantial progress in implementing ROSC recommendations pertaining to monetary statistics. To address the outstanding issues, the mission further recommended that the NBKR (a) improve the basic source data to allow for proper classification of the transactions with foreign and domestic units; (b) fully implement the *MFSM*'s methodology concerning accrual accounting; (c) exclude deposits with banks in liquidation from monetary aggregates and classify them as restricted deposits; and (d) set up a working group to follow up on consistency between monetary and balance of payments statistics. The mission also recommended expanding the current broad money survey to include the accounts of credit unions and microfinance companies.

13. Monthly monetary data for IFS publication are reported on a regular and timely basis. Since December 2002, monetary data have been reported electronically to STA. In 2005, the NBKR began reporting its monetary data to STA using Standardized Report Forms, which are designed in accordance with the *MFSM*'s methodology.

External sector

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

15. 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. The State Customs Inspectorate has introduced the customs receipt order for shuttle traders that simplifies and improves recording of imports of goods by shuttle

traders. However, the high value limits applied for free import of goods by individuals have fostered a large shuttle trade, which has complicated estimation of this activity.

16. An STA mission on balance of payments statistics was in Bishkek during March15–29, 2004 to address compilation issues, and to assess training needs. The mission noted that while progress has been made in several areas, further improvements were needed in the international transactions reporting system; data sampling methods; and data validation and coverage, particularly on trade, services, private sector external debt, and foreign direct investment. The mission developed a questionnaire for collecting data on foreign direct investments and provided guidelines on the collection of data on external debt.

Kyrgyz Republic: Table of Common Indicators Required for Surveillance
(As of April 10, 2007)

	Date of latest observation	Date received	Frequency of Data[6]	Frequency of Reporting[6]	Frequency of publication[6]	Memo Items:	
						Data Quality – Methodological soundness[7]	Data Quality – Accuracy and reliability[8]
Exchange Rates	3/30/07	4/02/07	D	D	W		
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	2/28/07	3/30/07	M	M	M		
Reserve/Base Money	3/30/07	4/02/07	D	D	M	LO, O, LO, LO	LO, O, O, LO, LO
Broad Money	2/28/07	3/22/07	M	M	M		
Central Bank Balance Sheet	3/30/07	4/02/07	D	D	M		
Consolidated Balance Sheet of the Banking System	2/28/07	3/22/07	M	M	M		
Interest Rates[2]	3/23/07	4/02/07	W	W	W		
Consumer Price Index	2/28/07	3/09/07	M	M	M	O, LO, O, O	LO, LO, O, O, O
Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4]	2/28/07	3/22/07	M	M	Y	O, LNO, LO, O	LO, O, O, LO, LO
Revenue, Expenditure, Balance and Composition of Financing[3]– Central Government	2/28/07	3/22/07	M	M	M		
Stocks of Central Government and Central Government-Guaranteed Debt[5]	9/30/06	11/11/06	M	M	Y		
External Current Account Balance	12/31/06	1/28/07	Q	Q	Q	LO, LO, LO, LO	O, LO, LO, LO, LO
Exports and Imports of Goods and Services	12/31/06	1/26/07	Q	Q	Q		
GDP/GNP	2/28/07	3/09/07	M	M	M	O, O, LO, O	LO, LO, LO, O, O
Gross External Debt	9/30/06	12/30/06	M	M	Y		

[1] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[2] Both market-based and officially determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[3] Foreign and domestic financing only.
[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.
[5] Including currency and maturity composition.
[6] Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Annually (A), Irregular (I); Not Available (NA).
[7] Reflects the assessment provided in the data ROSC (published on November 2003, and based on the findings of the mission that took place during November 2002) for the dataset corresponding to the variable in each row. The assessment indicates whether international standards concerning concepts and definitions, scope, classification/sectorization, and basis for recording are fully observed (O), largely observed (LO), largely not observed (LNO), or not observed (NO).
[8] Same as footnote 7, except referring to international standards concerning source data, statistical techniques, assessment and validation of source data, assessment and validation of intermediate data and statistical outputs, and revision studies.

Statement by the IMF Staff Representative
May 18, 2007

The following information has become available since the staff report was issued. It does not change the thrust of the staff appraisal.

1. **Political situation.** After a series of demonstrations by the opposition in April, political tensions have eased. The immediate focus of the political debate has shifted to a new constitution (the third one since late 2006) that is being drafted by a task force for submission to parliament in the coming weeks. The new draft is expected to demarcate more clearly the responsibilities of the president, the prime minister and parliament. Some opposition groups have, nonetheless, announced plans to organize new demonstrations later this year.

2. **Output and prices.** The economic recovery has accelerated, with real GDP growth of 4.4 percent in the 12 months ended April, driven by the construction and manufacturing sectors. CPI inflation during the same period fell to 3.7 percent, despite stepped up foreign exchange intervention by the NBKR that helped raise the annual growth rate of reserve money to 45.3 percent. As a result, gross international reserves in early May stood at $850 million, or 3.6 months of projected 2008 imports of goods and services. The authorities attribute the easing of price pressures in recent months to increasing remonetization of the economy. Staff has cautioned them to be ready to tighten the monetary stance if inflationary pressures reemerge over the coming months.

3. **Fiscal issues.** Preliminary Q1 2007 data suggest that the overall general government deficit was 0.5 percent of GDP lower than programmed, owing to continued revenue buoyancy and under-execution of capital outlays. Tax collections, in particular, exceeded the program's indicative floor, increasing by 28.6 percent year-on-year on the back of strong performance of VAT, customs duties and land taxes. The authorities have indicated that the reduction in the retirement age enacted by parliament (overriding an earlier presidential veto) will create an unexpected fiscal gap in the order of 0.5 percent of GDP, which they expect to cover during the year by intensifying their tax effort and possibly foregoing certain outlays. Staff plans to discuss the authorities' evolving fiscal strategy in greater detail at the time of the 5th PRGF review in summer 2007.

4. **Structural benchmarks.** The authorities are working toward fulfillment of the missed end-December 2006 and end-March 2007 structural benchmarks under the program. They said that *the review of the NBKR's internal audit function* will begin shortly (with assistance from the Swiss National Bank), and noted that parliament has included *the former Kyrgyz Agricultural Finance Corporation (KAFC)* in the list of strategic companies requiring legislative approval for privatization. A decree outlining *the new medium-term external debt strategy* is awaiting government approval. The *new tax code bill* has already undergone its first reading and is expected to be considered by parliament in the coming weeks. Regarding the envisaged *amendments to the civil, housing and land codes and to laws governing collateral, aimed at harmonizing provisions on collateralized lending by financial*

institutions, parliament has already passed the amendments to the civil code and the authorities are working on the requisite amendments to the land and housing codes.

5. **Mining sector bill.** The government has publicly distanced itself from a bill introduced by parliament proposing nationalization of the mining industry, which has since undergone a first reading. Moreover, the government has offered to restart negotiations with the Canadian Cameco/Centerra mining group (which had been initiated by the previous cabinet) to revise the 1994 investment contract guiding the operations of the key Kumtor mine.

6. **Electricity sector issues.** The authorities have indicated that they remain broadly committed to the energy sector action plan, which they had designed last year with World Bank assistance with a view to improving the sector's financial and physical performance. The officials are still contemplating two increases in power tariffs later this year, as part of the phased adjustments to reach cost-recovery tariffs by 2010, but details remain to be worked out by the top political leadership.

7. **Development Fund.** A draft bill sent to parliament proposing creation of a Development Fund is awaiting its first reading. The new cabinet has not yet decided whether to champion the bill.

8. **HIPC/MDRI.** Prime Minister Atambaev has just written to the Managing Director and the President of the World Bank acknowledging that the country's earlier decision to forego HIPC/MDRI debt relief was mainly conditioned by pressures from parliament and civil society. He stressed that the government remains committed to the implementation of the structural reforms drawn from the CDS that had been agreed, ad referendum, in late 2006 as floating Completion Point triggers under the HIPC Initiative. Against this backdrop, the Prime Minister appealed to the Fund and World Bank to consider whether the Kyrgyz Republic could still qualify for debt relief under the MDRI. Under the existing guidelines, the country exceeds the per capita income threshold of $380 for income-based MDRI from the Fund. The Bank does not provide income-based MDRI relief, but both institutions would grant MDRI relief to highly indebted poor countries that reach the completion point under the HIPC Initiative. However, recently released 2006 data suggest that the Kyrgyz Republic would be highly unlikely to meet the HIPC eligibility thresholds at this point because of amortization payments and gains in government revenue that have significantly reduced the ratio of net present value of debt to government revenue.

INTERNATIONAL MONETARY FUND
EXTERNAL RELATIONS DEPARTMENT

Press Release No. 07/104
FOR IMMEDIATE RELEASE
May 21, 2007

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Completes Fourth Review Under the PRGF Arrangement with the Kyrgyz Republic and Approves US$1.9 Million Disbursement

The Executive Board of the International Monetary Fund (IMF) has completed the fourth review of the Kyrgyz Republic's economic performance under the three-year Poverty Reduction and Growth Facility (PRGF) arrangement. The completion of the review enables the release of an amount equivalent to SDR 1.27 million (about US$1.9 million). This brings total disbursements under the arrangement to SDR 6.34 million (about US$9.6 million).

The PRGF arrangement was approved on February 23, 2005 (see Press Release No. 05/40) for an amount equivalent to SDR 8.88 million (about US$13.5 million).

Following the Executive Board discussion of the Kyrgyz Republic's economic performance, Murilo Portugal, Deputy Managing Director and Acting Chair, said:

"The Kyrgyz authorities have maintained macroeconomic discipline, comfortably meeting the end-2006 quantitative targets under the PRGF-support program despite a challenging political environment. The economic program for 2007 aims at preserving economic stability and advancing structural reform to improve living standards in a low-inflation environment.

"The *Country Development Strategy* (CDS) for 2007–10 offers a comprehensive blueprint for stepping up economic and social development and achieving the Millennium Development Goals. The CDS appropriately prioritizes good governance and reduction of corruption; creation of a friendly business climate; and removal of deep-seated impediments to sustained and rapid private sector-led growth. Successful implementation of the CDS hinges on rallying broad domestic support for reform and carefully costing and prioritizing poverty reducing spending, especially given the limited resource envelope following the decision to forego further debt relief.

"Fiscal prudence must remain the linchpin of macro-economic stability and debt sustainability. It will be essential to check the upward drift in current spending observed in recent years and improve the targeting of spending. Measures are also needed to offset the immediate fiscal impact of the recent reduction in the retirement age, and to reform the pension system, setting it on a sound financial footing.

“Passage of the new tax code would create a sound basis for further improvements in tax administration. The authorities recognize the importance of managing carefully the fiscal decentralization process to forestall a short-term loss of fiscal control, and the need to build capacity and define clearly the competencies and responsibilities of each government tier.

“A firm monetary policy will be essential to keep inflation in check. The monetary authorities are encouraged to largely refrain from large unsterilized intervention in the foreign exchange market, while continuing to enhance indirect instruments of monetary control, and being ready to adjust policy interest rates if needed.

“The updated Financial System Stability Assessment highlights the progress made in modernizing the financial sector, but there is scope for further strengthening financial sector supervision—especially in advance of the introduction of a deposit insurance scheme for small depositors in 2008. It will be important to take well-sequenced steps to bolster financial intermediation and capital market development, as well as to increase the central bank’s autonomy,” Mr. Portugal said.

Statement by Thomas Moser, Executive Director for Kyrgyz Republic and Sadriddin Djienbekov, Advisor to Executive Director
May 18, 2007

1. On behalf of our Kyrgyz authorities, we would like to thank the staff for the constructive discussions and the useful reports. As the staff points out, the authorities have managed to maintain macroeconomic discipline and stability, despite lingering political tensions. All quantitative performance criteria under the PRGF-supported program have been met comfortably, with both the fiscal deficit and inflation lower than projected. Delays in implementing structural reforms were mostly due to the difficult relations between the executive and the legislative powers. The legislative process was dominated by discussions on constitutional reform, which put other legislative issues on hold.

2. In February 2007, after a difficult debate in the Kyrgyz Republic, the authorities decided to renounce their participation in the HIPC Initiative. The Kyrgyz parliament confirmed the government's decision in March. The authorities are nevertheless committed to implement the reforms that had been considered as possible Completion Point triggers, which are an integral part of the new Country Development Strategy (CDS) for 2007–10. The authorities are also aware of the need to maintain a prudent fiscal stance and to promote economic growth in order to secure debt sustainability. They also plan to further strengthen external debt management, for which they intend to implement the newly designed framework, with continued technical assistance from donors.

3. As noted in the staff update, the authorities are working toward fulfillment of the missed structural benchmarks, while continuing with the implementation of prudent macroeconomic policies. The macroeconomic outlook remains favorable. Economic recovery has accelerated in the first quarter of 2007, with strong growth in the industrial and construction sectors. External trade has picked up as well, while at the same time inflation declined further.

Fiscal policy

4. Fiscal performance has exceeded expectations, mainly thanks to strong revenue performance, with tax revenue now over 20 percent of GDP. The introduction of a new tax code and improvements in tax and customs administration will further underpin the authorities' efforts to strengthen revenue. Preliminary data for the first quarter of 2007 suggests a continuation of fiscal overperformance.

5. The 2007 budget passed in April features a salary increase for specific public sector categories. In order to make room for differentiated increases in the remuneration of specialized professionals and senior officials, the government is planning to launch as soon

as feasible a civil service reform aimed at reducing the civilian workforce. As to the reduction in the retirement age enacted by parliament, the government has decided to phase in the provisions of the new law over a three-year period, and it intends to cover fiscal costs with both growing revenue and expenditure measures if needed. In this connection, the government is also considering a pension reform with World Bank assistance, geared at securing the system's longer term viability and encouraging the development of the domestic capital market.

Monetary and Financial Sector Policies

6. The National Bank (NBKR) is committed to price stability. It will seek to contain inflation at 5 percent this year, against a background of continued remonetization. To keep liquidity expansion in check, the NBKR will further enhance its indirect monetary control instruments (drawing on the findings of an upcoming MCM technical assistance mission), price these instruments flexibly, and maintain a managed exchange rate float. To enhance the payments system, the NBKR will make a new real-time gross settlement (RTGS) system operational by end-2007 or early 2008.

7. To enhance the credibility of macroeconomic policy, every effort will be made to secure passage of pending legislation to strengthen the NBKR's autonomy. The NBKR is also advancing the external review of its internal audit function. The NBKR has invited and received offers from three international auditing firms, but it needs to negotiate some improvements in order to ensure a well-targeted review that meets international standards. This has led to a delay, but the review is expected to be carried out in June.

8. The Financial System Stability Assessment update attests to the substantial progress that the authorities have made in several areas since the 2002 assessment. The authorities very much appreciate the report, which provides a useful road map for further improvements. The authorities also welcome the findings that solvency and profitability ratios of the banking system are at comfortable levels, that prudential ratios are generally being observed, that the loan portfolio of banks has improved substantially since 2002, that the level of dollarization is declining, and that the NBKR has further enhanced the transparency of its practices and procedures.

9. Given rapid credit expansion, the authorities intend to step up supervision and further improve the legal and supervisory framework. Amendments to the civil, housing and land codes, and to the laws governing collateral in order to strengthen the legal foundations for using and seizing collateral in cases of default, has been submitted (structural benchmark for end-March) and already approved by parliament. The government also remains committed to the privatization of the Kyrgyz Agricultural Finance Corporation.

Other Structural reforms

10. The Kyrgyz authorities' CDS underscores the importance of a new development strategy focused on boosting economic efficiency, improving governance and service delivery, eradicating corruption, and better targeting social assistance. It thereby builds on the experience from the National Poverty Reduction Strategy, which was presented to the Executive Boards of the Fund and IDA in January 2003, and on extensive consultations with a broad range of stakeholders. A specific reform agenda, drawing on this Strategy and the Joint Country Support Strategy of the World Bank and other donors, will be discussed at a Development Forum meeting in Bishkek at the end of this month.

11. The CDS places high priority on the energy sector as an engine of growth, with private participation being a key element. With support from the World Bank, the authorities have developed a rehabilitation plan for the energy sector to help deliver reliable and sustainable long-term energy supply for domestic use and exports. The plan includes a medium-term tariff policy framework featuring phased adjustments in electricity tariffs under a pre-announced calendar to cost recovery levels by 2010, accompanied by social safety nets to cushion the effect of the adjustment on the poor.

12. The President has created an Investment Board with the objective of protecting investors' rights. The authorities reaffirm their commitment to the blueprint outlined in the CDS to boost private sector-led growth by improving the business climate and strengthening the legal foundation for private property. The government does not support any actions toward a nationalization of the mining industry. In particular, it will propose legal steps to strengthen property rights, improve the autonomy and efficacy of the judiciary, continue to simplify licensing procedures, streamline regulatory bodies, and promote transparency and efficiency in public administration. These reforms will be supported by technical (and possibly financial) assistance from multilateral and bilateral donors involved in these areas.