

INTERNATIONAL MONETARY FUND
AND THE INTERNATIONAL DEVELOPMENT ASSOCIATION

KYRGYZ REPUBLIC

Joint Staff Assessment of the Poverty Reduction Strategy Paper

Prepared by Staffs of the International Development Association
and the International Monetary Fund

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I. OVERVIEW

1. The National Poverty Reduction Strategy (NPRS) of the Government of the Kyrgyz Republic builds on the Interim National Poverty Reduction Strategy (I-NPRS) presented to the Boards of the International Monetary Fund (IMF) and the International Development Association (IDA) in November 2001 and December 2001, respectively. It represents an important milestone in the Kyrgyz Republic's ongoing efforts to elaborate a comprehensive, home grown strategy for poverty alleviation. The strategy was prepared in close collaboration with all key stakeholders.
2. **The NPRS builds on the strengths of the I-NPRS, particularly the inclusive nature of its formulation process.** The NPRS represents a joint effort between the Government and civil society in the country. It also benefited from discussions with and comments from the donor community during both the preparation process and Consultative Group Meeting held in Bishkek during October 2002. Thus, the wide participatory process that characterized the I-NPRS, has been continued in the preparation of the NPRS. The NPRS is also closely linked to the country's ten-year development vision that was laid out in its Comprehensive Development Framework (CDF). The development of a quality dataset for poverty analysis was a strong feature of the I-NPRS, and further improvements in that area characterizes the NPRS. The elaboration of a comprehensive governance reform strategy and strong focus on equity and efficiency of public policies for effective poverty reduction, including at Oblast level, as well as its candid recognition of human right issues are additional strengths of the NPRS.
3. **There remain areas where progress needs to be made during the implementation and subsequent updates of the NPRS.** Although improved relative to I-NPRS, the poverty diagnosis needs to be sharpened further, and the link between the poverty diagnosis, poverty

reduction strategy objectives, and priority actions strengthened. Significant progress is also needed in the areas of costing and prioritization of policy actions presented in the Appendix V for future updates to enable the authorities exercise leadership in the fight against poverty. In this regard, financing requirements for priority NPRS actions need to be clearly defined and linked with annual budgets within the recently introduced Medium Term Expenditure Framework (MTEF). Similarly, efforts must be undertaken to ensure that continued strong civil society participation in further policy development does not detract from the need to prioritize key policy actions. Successful implementation of the NPRS also calls for continued institutional capacity building within the government for strategy formulation, implementation, monitoring and evaluation, and resource management, including aid mobilization and coordination on the basis of the NPRS.

II. THE PARTICIPATORY PROCESS

4. **The NPRS describes in detail the participatory process that characterized the development of the strategy.** This process—involving all branches of government, parliament civil society, the private sector and donors—was launched in 1999 in connection with the preparation of the CDF and the I-NPRS. It consisted of a large number of well-attended seminars, conferences and workshops, regular *kurultai* (people’s conventions) between government officials and civil society across the country, extensive discussion with NGO groups, with private sector (in particular private sector representatives from Chambers of Commerce and Industry) and frequent consultation with donors. The participatory process created substantial public interest in the NPRS. The government emphasizes that their approach helped stakeholders participate both in the identification of objectives and in the formulation of policies to achieve them.

5. **The NPRS emphasizes that the participatory process, which promotes a broad-based ownership, will be central to its implementation, monitoring, and evaluation and future updates.** Accordingly, it wishes to institutionalize the lines of communication already established for ensuring that the public is fully informed about the NPRS’s implementation progress, for seeking their feedback on modifications and updates of the strategy, and for engaging them, on an equal partnership basis, in the monitoring and evaluation of the strategy. In this effort, a key role is envisaged for NGOs, including through developing mechanisms to allow NGOs to participate in the formation of local budgets and in the implementation of some economic and social NPRS programs, and by providing them with training in project planning and management. Nevertheless, these efforts, while commendable, may need to be phased-in in parallel with improvements in implementation capacity.

6. **Active dissemination of information has characterized the NPRS process and efforts in this area should continue to be strengthened.** In addition to the frequent contacts with civil society, the government has striven to make relevant information pertaining to the NPRS readily available to the public. A CDF/NPRS website has been established, and preliminary versions of the document, working and methodological materials, information on strategy discussions, and analytical materials are regularly posted on the website. The government has also announced its intention to regularly publish NPRS updates in the local

media, and to conduct information campaigns on the most successful aspects of the NPRS process.

7. **The authorities have actively involved Kyrgyz Republic's development partners in the preparation of the NPRS.** Donors have provided significant technical and financial support from the outset.¹ This was crucial in supporting preparation of a number of analytical studies that helped in formulation of the NPRS, including a poverty assessment prepared jointly by the World Bank and the Government. There were regular consultations with development partners, including representatives of the international financial institutions (IFIs), through the preparation process. The draft NPRS was also discussed extensively and benefited from the recent Consultative Group meeting. However, a number of bilateral donors have indicated the need for more frequent consultation with their representatives in the implementation phase of the NPRS.

8. **The participatory process will need to be better managed toward prioritization of policy actions.** The wide consultations of the NPRS objectives in the country generated a very large number of suggestions and ideas. In an effort to build broad-based ownership, the government included most of these reform objectives in the NPRS, with limited success in their prioritization and sequencing. In the future, the staffs believe that greater ownership would be fostered, if the government were to effectively facilitate evolution of a well-focused and realistic action plan directly out of the participatory process. However, the role of the Ministry of Finance will be essential in the costing process and in coordinating the various initiatives. In particular, it is critical that the NPRS be directly linked to the annual budget and the recently introduced MTEF.

III. POVERTY DIAGNOSIS

9. **The NPRS poverty diagnosis is based on reliable and representative data.** Poverty data in the Kyrgyz Republic come from three sources: (i) the Kyrgyz Poverty Monitoring Survey, which consists of multi-purpose data from nationally representative cross-section samples of individuals, households, and communities collected in October-November of 1993, 1997 and 1998; (ii) a multi-purpose survey of 3,000 households in the fall of 1999, with a focus on energy; and (iii) the Household Budget Survey, which consists of panel data on monthly household expenditures covering a whole year. The I-NPRS had pointed out the need to study the poverty data to better understand linkages between growth and poverty alleviation in Kyrgyz Republic. The joint World Bank-Kyrgyz Poverty Assessment, drawing trends from the above noted surveys for different years (despite their differing survey instruments and sampling coverage), demonstrates that economic reforms, including the equitable land reform, have led to significant growth and significant poverty reduction in the past 4 years. Thus, the

¹ In addition to the Fund and the World Bank, The Asian Development Bank (AsDB) has been closely involved in supporting the NPRS. Major technical and financial support for the CDF/NPRS has also been provided by the UNDP and other United Nations specialized agencies, the European Union, the European Bank for Reconstruction and Development and the governments of Japan, the United States, and Switzerland and other agencies.

NPRS poverty reduction targets for 2005, underlined by expected broad-based economic growth, are justified. However, the specific target of reducing poverty to about 39 percent by the year 2005 is derived from projected 5 percent annual growth from 2001 onward. The staffs view this target as optimistic given the negative 0.5 percent growth estimate for 2002 (reflecting the land-slide in Kumtor gold mine), notwithstanding an expected return to the 5 percent growth from 2003 onward. A key challenge for achieving the poverty reduction target is to sustain and broaden the sources of economic growth through accelerated economic and governance reforms, as described in para.13 and para.16 below.

10. **Further improvements would strengthen the analytical basis of the poverty diagnosis.** One area where the NPRS analysis is particularly weak concerns the relationship between employment generation and poverty reduction objectives. This largely stems from reliance on administrative data for the registered unemployed, which do not adequately capture the full unemployment picture. The NPRS diagnosis would have been stronger if household survey data on unemployment and labor market conditions were collected and analyzed on a regular basis. More generally, the absence of analyses of the impact of macroeconomic policies, sectoral policies and social policies on the evolution of poverty are important gaps in the NPRS's poverty diagnosis. The staffs commend the National Statistical Committee (Natstatcom) for its continued efforts to correct these problems by planning to adopt an integrated budget and manpower household survey starting in 2003, which include establishing a new benchmark and a more systematic monitoring of poverty, labor market and unemployment trends, and other dimensions of household welfare such as health, education, and access to network services, and allow for improved monitoring of the links between these policy dimensions. The staffs also commend the rich gender dimensions of the NPRS, including several adequate gender specific actions.

IV. PRIORITY PUBLIC ACTIONS

11. **The broad policy priorities of the NPRS are appropriate.** The three pillars of the NPRS, aiming at (i) fostering economic growth and creating employment opportunities; (ii) improving efficiency and equity of social protection and human development; and (iii) improving governance, public sector efficiency and institutional and human capacity, are consistent with the multi-dimensional nature of poverty alleviation. The policy action plan set forth in the NPRS is generally consistent with these three pillars.

12. **Significant weaknesses in costing, prioritizing and sequencing the NPRS measures mar an appropriate agenda.** These had been identified as weaknesses of the I-NPRS as well. For the NPRS, the authorities made an attempt to cost most measures and programs under consideration. However, the basis of these estimates is not clear and there is a significant need to improve the quality of cost estimates. As regards prioritizing and sequencing measures, this has proven to be a challenge that the authorities have found difficult to overcome. The staffs see this as a serious shortcoming of the NPRS, particularly in light of the weak implementation capacity in the country. For the future, there is a need for tangible progress in this area. An appropriate tool for better costing, prioritisation and sequencing of the plan is the recently introduced MTEF, which should be published. The recently prepared Public Expenditure

Review by the World Bank should also assist. These documents will also help communicate a coherent and feasible reform agenda to civil society.

A. Macroeconomic Framework, Fiscal Choices, and Financing Plan

13. **The medium-term macroeconomic framework is conducive to macroeconomic stability and poverty reduction.** The macroeconomic framework targets real GDP growth of about 5 percent per annum over the period 2002-05, which is consistent both with the average over the period 1999-01 and the NPRS reform objectives, but could be considered challenging due to below-noted fragility of growth prospects. However, this rate of growth is a pre-requisite for any significant reduction of poverty in the country. The stance of monetary policy outlined in the NPRS is suitably tight to contain annual inflation in the medium-term to under 4-5 percent, which is also consistent with the desired stability in the foreign exchange market. The NPRS clearly recognizes the severe external debt problem and thus the need for fiscal adjustment, including through limits on the Public Investment Program. In light of these constraints, the NPRS appropriately recognizes the critical role that exports and private sector investment will have to play for stimulating broad-based growth and for achieving the growth target. It is commendable that the NPRS recognizes that the feasibility of this strategy requires the Kyrgyz Republic to improve its international competitiveness through productivity gains resulting from the implementation of bold structural and governance reforms. However, NPRS could have benefited from alternative scenarios and policy considerations to deal with risks of exogenous shocks because the country is very vulnerable to volatility of world market prices, weather conditions and shocks in the neighboring countries.

14. **The fiscal choices inherent in the NPRS are consistent with the policy objectives, but mechanisms to allocate expenditures are still at an early stage of development.** The NPRS targets an increase in the central government tax revenue to GDP ratio to at least 15 percent by 2005, mainly through a broadening of the tax base and an improvement in tax administration. The staffs believe that the measures proposed are sufficient to achieve the revenue target but they need to be better specified. Better revenue collection is necessary, since it cushions the expenditure compression required to achieve the fiscal adjustment consistent with debt sustainability. However, the NPRS should specify the necessary arrangements in support of the fiscal decentralization and clarify whether these arrangements were taken into account in the medium-term framework. The medium-term path of budgetary spending, which encompasses all external loan-financed project expenditure, targets a steady increase in social spending, consistent with the poverty reduction objectives of the NPRS. However, as noted earlier, the cost estimates need refining and conversion to resource envelopes at an individual ministry level. With progress over time, the MTEF should help translate NPRS priorities into expenditure allocations.

15. **The NPRS's assessment of the availability of domestic and external financing is reasonable.** External financing to cover budgetary financing gaps are either already available or likely to be committed, as several key donors have negotiated or are in the process of negotiating multi-year packages with the Kyrgyz Republic. At the recent Consultative Group meeting, donors broadly endorsed the poverty alleviation plan contained in the draft NPRS and expressed their desire to align their own support with the priorities and objectives outlined in

the document. At the meeting, amounts pledged to be committed over the next three years, though disbursed over a longer time frame could be sufficient to meet the country's critical budgetary financing requirements in the period ahead. At the same time, more work needs to be done to establish mechanisms to ensure the alignment of these resources with the NPRS priorities, which are not directly linked with the annual budgets and the MTEF, as noted earlier.

B. Structural and Sectoral Policies

16. **The NPRS recognizes the central importance of good governance and public resource management for poverty reduction.** The proposed reforms aim to enhance the transparency and accountability of the State; increase voice and participation of citizens in public affairs; improve budget formulation and execution; rationalize roles and responsibilities of government entities; empower local governments; improve service delivery, including at the local level; improve the quality and professionalism of the civil service; introduce modern management systems and technology in public sector operations; strengthen investor confidence in businesses; and reduce corruption. Overall, the discussion and diagnosis of problems in the NPRS is comprehensive and candid. However, looking ahead, following important areas will need to be better emphasized both during implementation and in the first NPRS progress report. First, in addition to acknowledging the existence of corruption in various government agencies and the judiciary, the NPRS needs to recognize state capture by vested interests as the root cause of many governance problems for addressing them adequately. Second, the NPRS needs to address significant deficiencies in implementation of existing procurement law, which is sound in itself. Third, the NPRS needs to focus on ways of increasing the independence and effectiveness of the Chamber of Accounts, which is the main external control agency of the State, and it needs to address significant weaknesses in the internal controls within the government. Fourth, to achieve tangible progress in planned decentralization of service provision and greater community involvement, the NPRS needs to focus on strengthening accountability and financial management at the local government and the community levels as a matter of priority. More broadly, the NPRS needs to recognize better that proper sequencing and prioritizing of governance reforms are essential to build grassroots support for their continued implementation.

17. **A comprehensive plan to strengthen the financial sector is a key component of the NPRS.** The plan identifies measures to be undertaken to strengthen bank supervision, and improve the regulatory framework and the debt collection capacity. It also identifies near-term actions to resolve the status of remaining state-owned banks, and to strengthen the payments system, although with some gaps in describing the strategies concerning Saving and Settlement Company and Kairat Bank. The staffs believe that, with proper implementation, these concrete actions should help significantly in allowing the banking system to play its proper role in facilitating financial intermediation. In this context again, the staffs note that proper sequencing of reforms is essential for success. By contrast, the NPRS's extensive discussion on the situation in the non-bank financial sector offers fewer concrete proposals for action. In this area, microfinance institutions have been very successful, and with recent improvements in their legal framework, should continue to grow. Leasing and land securitization also offer good opportunities that should be elaborated on in the NPRS progress reports.

18. **The NPRS recognizes the private sector as the driving force behind sustainable growth and poverty reduction.** To this end, it acknowledges the need for continued transformation of economic activity from public to private sector; sound legal and regulatory framework (particularly reducing administrative barriers to private investment and SME development); good corporate governance principles (particularly introduction of international standards for accounting and auditing and effective commercial dispute resolution mechanisms); and intensive export promotion (particularly through increasing the role of processing industries, further improving the customs and tax policies and exploring the new production lines). In this context, the staffs encourage the authorities to examine the implications for the Kyrgyz economy of the various trade barriers imposed by its neighbors. Furthermore, the authorities should consider whether the Kyrgyz own trade policy and its significant variations of tariff protection across industries could be revised to promote diversification. Additional efforts are needed in ensuring enforcement of legislative reforms; in specifying concrete policy actions and timetable for elimination of administrative barriers; and in enhancing partnership with business community for articulating specific actions and programs geared to increase quality and consistency of production for export markets. Special attention is also needed to improve the consistency of overall reform objectives across sectors, particularly concerning agriculture. Similarly, the strategy proposed for export promotion designs in some cases a too dirigist role for the state. Instead export promotion should use tools that are market based and aim at improving the general business environment.

19. **Sustaining agricultural growth is critical for the country's poverty reduction efforts in the medium term.** The NPRS clearly recognizes this fact and correctly identifies the need for stimulating outward oriented agricultural production, but it devotes insufficient attention to the still incomplete transformation to a market based mode of production. This is reflected in interventionist elements of the strategy, such as the role envisaged for the farmers as primarily suppliers of raw materials for the public-sector dominated processing industry. Unlike in the other sections of the NPRS, measures needed for creating an enabling environment for greater private sector participation are largely missing. The staffs would encourage the authorities to shift their attention to articulating the government's role in providing an adequate regulatory framework and enabling environment for the further development of private initiatives, which have already been proven to bring tangible benefits to the sector. In addition, prioritization, sequencing, and costing of irrigation efforts are also largely missing. These modifications, and the enunciation of more clearly monitorable steps would be desirable in forthcoming NPRS updates.

20. **The NPRS discusses comprehensively the needs in the education and health sectors.** The overview of both the health and the education sectors provides a sound assessment of progress with reforms to date, the need for additional budgetary allocations, especially for health sector, and the major challenges ahead. However, the action plans outlined for both sectors would benefit from greater attention to prioritization, and sequencing. The staffs believe that the first priority should be to provide education of acceptable quality in the compulsory cycle of the education. Likewise, in order to improve educational performance of children from educationally deprived households; preschool education would need to be targeted to these vulnerable groups, as coverage improves. In staffs view, improved efficiency of education spending (e.g. by financing educational outputs, like students, rather than inputs,

like teachers and classrooms) and better targeting of rural education needs require greater attention during the NPRS implementation.

21. **Health care financing reforms are central to realizing the gains made so far in improving the financial strength and sustainability of the sector.** Therefore, the staffs believe that vigorous attention to timely resource transfers in cash to the Health Insurance Fund should be a priority during NPRS implementation. In addition, the staffs believe that implementation of already identified measures for improving equity in resource allocation across the oblasts along with finalization and implementation of the strategy on TB/AIDS are equally important priorities in the health sector. The staffs also believe that before embarking on promotion of privatization in health care, authorities should consider introducing an adequate regulatory framework for private health care and tackle the issue of streamlining the public health facilities.

22. **The NPRS recognizes well the challenges of devising an effective, equitable and affordable social protection strategy.** It provides a concise and generally well-balanced assessment of the present dilemma of reconciling the paucity of resources with the need to offer social protection in the face of widespread household poverty. Its proposal to ensure benefits payments in cash is appropriate, but the staffs believe that the financial implications and incentive compatibility of some other measures need to be reconsidered. In particular, it may not be realistic to aim at guaranteeing a minimum consumption level well above the poverty line. The staffs also have concerns about the NPRS proposals for pension reform, particularly the feasibility of creating a fully funded second-pillar pension component during the NPRS implementation timetable. The focus on enhancing the collection performance and improving the efficiency of the Social Fund is desirable. This could include developing an internally balanced pension income adequacy and earnings replacement policy. The NPRS would also benefit from a discussion of specific policy actions to strengthen the sustainability of the pension system in view of a targeted improvement of the living standards of pensioners. In line with the poverty diagnosis, the NPRS identifies the need for expanding residential care to assist disadvantaged children, but the staffs believe that greater focus on community based efforts to foster more productive lives for children and families would deliver the needed benefits in a more cost effective manner.

23. **The NPRS correctly identifies the energy sector as critical for the country's development prospects, but priorities within the sector need to be clearly defined and re-focused.** The NPRS recognizes that the losses in the energy sector (in both electricity and gas) are high. Accordingly, the NPRS rightly proposes the need to reduce technical and commercial losses in the sector and eliminate payments in barter and offsets, albeit with no specific measures are presented to this end. More broadly, the NPRS should address the crucial need for investments in rehabilitating distribution networks both for electricity and gas. Furthermore, the NPRS should recognize that there is no alternative to private sector participation in the distribution of electricity and gas. Given the difficult global environment for energy privatization, the use of alternative models for private sector participation such as concessions or, as a second best alternative, management contracts could be the only feasible approaches during the NPRS implementation.

24. **The long-term financial health of the power sector depends critically on full cost recovery by companies.** To this end, the NPRS correctly identifies the need for a medium-term tariff policy, but the absence of any parameters for continued tariffs adjustments is a key shortcoming of the strategy. The staffs are aware that electricity tariff increase in particular is a highly sensitive issue both socially and politically, and believe that this could only be addressed with a well functioning social protection system for the poor against tariff increases. These issues require a careful assessment and policy-action plan within the above-noted broader set of reform challenges in power sector, as part of the priority activities supporting the NPRS implementation.

25. **Plans to maintain and improve infrastructure need to be balanced against severe resource constraints.** The NPRS correctly identifies infrastructural improvements, notably in transport and the utilities sector, as urgent tasks. However, the staffs have concerns about some of the plans outlined in the NPRS. For instance, significant private sector investment in the roads or railroad sector is unlikely and, thus, focus needs to be shifted to identification of means to prevent deterioration of the existing infrastructure during implementation and future updates of the NPRS. For planned greater involvement of the local communities in priority infrastructure development, the staffs believe that the future NPRS updates should elaborate on measures needed for avoiding large disparities in regional financing capacities from being translated into disparities in infrastructure development and service delivery. For plans that are closely tied to the privatization of strategic enterprises, the staffs believe that some key elements of the strategies remain to be developed. The rehabilitation of Kyrgyzair is closely tied to its planned privatization, but this faces uncertain prospects, and fallback plans are not discussed in the NPRS. As regards telecommunications, a majority holding in Kyrgyztelecom has recently been tendered and its rehabilitation plans will also be developed in that context. However, the NPRS proposes no solutions for the smaller telecommunications firms and does not focus on need for a regulatory framework that will promote fair competition.

26. **The mining sector strategy of the NPRS calls attention to general problems of the sector but future updates should refine the strategy.** The NPRS identifies well the need for sustaining the sector's economic and social performance and creating competitive legal conditions conducive to attracting private investments. However, the NPRS could have more substantively built upon the mining sector strategy studies that have already been undertaken² and spell out clearly specific policy proposals based on more systematic evaluation of past policies. The staffs recommend such a fuller strategy to be developed on a priority basis and reflected in the first NPRS progress report. In this context, the authorities should re-assess the ambiguous and sometimes too interventionist role that the government is envisaged to play in the future development of the sector. Future updates should also evaluate implications of political obstacles and/or vested interests undermining the development objectives of the mining sector through promoting imperfect competition.

² The problems of the mining industry have been identified by the World Bank Mining sector study in a close collaboration with the Kyrgyz counterparts (see The Kyrgyz Republic Mining Sector Review, 1994 and The Kyrgyz Republic Mining Sector Review Update, The World Bank, 2002).

27. **The identification and analysis of the poverty-linked environmental protection is appropriate.** The NPRS sets out goals to improve land and water resources management, notably with regard to access to drinking water, municipal sewage treatment and waste collection, reversal of land degradation, increase forest cover and increase areas under special protection. In staffs view, the goals are appropriate but ambitious relative to the NPRS's time frame and the budgetary allocations for environmental management. The planned activities are largely in the public sector, with little or no attention to incentives for community based improvements in natural resources management that are being piloted by various international donors. In addition, the investment plan contains little to address the uranium mine tailings problems, apart from additional surveys, and a financing plan for rural/urban water supply is absent.

V. TARGETS, INDICATORS AND MONITORING

28. **The NPRS provides medium-term targets for poverty reduction and sets out a framework for expanding these indicators over time.** The NPRS includes sixteen targets for 2005, which are selected on the basis of the poverty diagnosis, existing sectoral policies and technical consultations. Although there are some gaps in the proposed core set, the staffs believe that they generally provide an initial working baseline and are consistent with the present monitoring and evaluation capacity. Likewise, the selected core indicators—e.g. income poverty, maternal and child mortality, access to primary education and health care services—constitute a good attempt to utilize the Millennium Development Goals (MDGs) framework. The staffs welcome the government's intention, as presented in Appendix XI, to gradually expand the core set of indicators. Overall, although the document still lacks a clear distinction between inputs, outcomes and impact, and their corresponding monitoring frequency, the current range of selected core indicators should capture progress on a broad range of issues.

29. **There are, however, some weaknesses in the proposed system of indicators.** The core indicators focus mainly on social sphere, although a few productive sector indicators are included such as private sector share in GDP and access to telecommunications. Looking ahead, these could be supplemented with indicators such as access to electricity, and wage levels. In some cases, indicators could be better chosen to reflect the objectives and key constraints. For example, macroeconomic indicators could be broadened to include private investment and domestic saving rates; education indicators could cover special problem areas such as extremely low levels of pre-school education and low levels of secondary education. Also more quality indicators on human capital would be desirable.³ Labor market indicators could be enhanced to provide reliable estimate of unemployment. Governance indicators could also be broadened based on the recently completed Governance and Service Delivery Survey by the World Bank. In some other cases, the indicators could benefit from taking account of

³ Good quality quantitative data is not available for monitoring universal primary education, which needs to be supplemented by the qualitative analysis to understand, for example, learning outcomes.

available sources of data for setting a representative baseline⁴ (e.g. mortality rates, education enrolment rates, access to safe drinking water). In addition, the indicators would greatly benefit from greater disaggregation to capture rural urban inequities, regional differences, income disparities and gender imbalance.

30. A closer link between policy actions and final targets along with better understanding of implications of lower than expected economic performance remain a task to be pursued. In the staff's judgment, the poverty reduction targets are broadly consistent with the macroeconomic framework of a stable macroeconomic environment and a GDP growth of about 5 percent. As agriculture is expected to be one of the main contributors to growth, income distribution is not expected to worsen, which is consistent with the targeted pro-poor growth process. The staffs believe, however, that given the vulnerability of country's economic performance to external and natural shocks, it will be necessary to undertake a sensitivity analysis to simulate the impact of lower than expected economic growth on poverty reduction. On that basis, a contingency priority action plan could be developed. The development of long-term output targets would also help to ensure linkage between planned medium-term actions and long-term goals. These efforts should also focus on clearly spelling out linkages among key policy actions and the NPRS targets for important sectoral policies (education, health, social protection, rural development and infrastructure). The staffs encourage the authorities to include multiple scenarios in the context of future NPRS progress reports. In addition, a recurrent debt sustainability analysis will help monitor the progress on the foreign debt reduction effort.

31. The implementation of plans for monitoring and evaluation remains a challenging task. The staffs welcome the emphasis the NPRS puts on a monitoring system that is based on sample surveys, participatory assessments, as well as statistical reporting systems. The public expenditure management reform will also contribute to improve the timeliness and quality of expenditure data. The existing public expenditure reporting systems provide an incomplete basis for monitoring poverty-related expenditure, in part because the classification of expenditure does not cover all categories of pro-poor spending with particular difficulties in measuring implicit subsidies provided through the utility pricing and payment systems. However, the staffs note with concern that the action matrix presented in Appendix V does not lay out specific steps in this regard. The staffs suggest these gaps to be addressed in future NPRS updates along with specific capacity building and co-ordination challenges for Natstatcom and the line ministries/agencies in utilizing the new, integrated budget and manpower household survey for effective monitoring and evaluation. The staffs also stress the importance of developing simple and cost effective monitoring and coordination mechanisms with a focus on improving effectiveness of the process rather than control.

⁴ For example, the NPRS baseline year core indicators differ from those reported by the United Nations Statistical Databases (UNSD) concerning maternal mortality (at 42.3 per 100, 000 live births in 1999 in NPRS compared to very high rate of 80 percent in 1995 in UNSD), universal primary education (at 89.5 percent in 1999 in NPRS, compared to at 85 percent or below in 1998 in UNSD) and proportion of the population with access to safe drinking water (at 85.6 percent in 1999 in NPRS compared to only 77 percent in 2000 in the UNSD).

VI. RISKS TO THE STRATEGY

32. **The Kyrgyz economy is highly indebted, landlocked, and vulnerable to external shocks.** The country's macroeconomic strategy faces the challenge of achieving real GDP and export growth in a setting of high external indebtedness that necessitates adjustments in the external current and the fiscal accounts. Thus, raising private investment is of critical importance to maintaining the momentum of growth. However, even with good policies, adverse economic shocks can lead to a severe deterioration of the macroeconomic environment, including a depreciation of the exchange rate and sluggish investment activity. Agriculture, hydropower and mining sectors are of great importance in the Kyrgyz economy, and all of them have proven vulnerable to weather related developments and natural disasters. Finally, as a landlocked country, the Kyrgyz Republic's export promotion potential depends significantly on the easing of trade barriers in the region, particularly by its neighbors, over whom it has little leverage. Improved regional cooperation will, therefore, be critical to achieving NPRS objectives.

33. **In a fragile political environment urgent reforms may become increasingly difficult to undertake.** The political environment in the Kyrgyz Republic has become more complex in recent years. An increasingly vocal opposition, and the impending Presidential elections in 2005, may inhibit the government's ability and willingness to pursue the difficult reforms needed to improve the investment climate, notably combating state capture by vested interests, i.e. reforms critical to stimulating the supply side of the economy. In the same vein, delays in the rehabilitation of the strategic sectors of the economy (such as infrastructure and energy) and in creation of conditions for private capital inflow to these sectors would weaken the prospects for successful fiscal and external debt strategies. As mentioned above (para. 23 and para.24), this will lead to increased fiscal pressures and to a forced economic adjustment with negative impact on growth and poverty reduction prospects.

34. **Weak capacity is also a risk to the successful implementation of the NPRS.** Severe institutional constraints challenge the implementation of the NPRS. The NPRS objective of increased reliance on local service delivery increases these challenges. New monitoring and evaluation functions will further strain government capacity. This underscores the need to not only embark urgently on the civil service and capacity-building reforms but also identify critical stepping-stones on the path to achieving broader NPRS objectives, as one of the priority tasks over the next few months. Kyrgyz Republic will need to benefit from better coordinated external support to meet the challenge of implementing and monitoring the NPRS.

VII. CONCLUSIONS

35. **The NPRS represents a significant achievement.** In light of the risks described above, however, the path to success is narrow. Policy slippages could easily lead to a low-growth trap with a deteriorating external debt position and macroeconomic imbalances. Under those circumstances, the government's poverty reduction target could become unattainable. On the NPRS process itself, weaknesses still remain, notably in definition of the public sector's role in the country's development strategy, and in costing and prioritizing measures and in their monitoring and evaluation. However, the staffs acknowledge that, in the absence of prior

experience, preparation of the NPRS document represents a credible and inclusive effort on the part of the Kyrgyz authorities. The staffs commend the authorities for recognizing in the NPRS some of its shortcomings, and believe that with experience and continued development and refinement of strategies these can be overcome.

36. **The staffs of the IDA and the IMF consider that the authorities' poverty reduction strategy provides a suitable basis for Bank and Fund concessional assistance.** The staffs recommend that the respective Executive Directors of the World Bank and the IMF reach the same conclusion.