



# Report and Recommendation of the President to the Board of Directors

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Project Number: 52225-003  
August 2021

## Proposed Policy-Based Loan and Grant for Subprogram 2 Kyrgyz Republic: Promoting Economic Diversification Program

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Asian Development Bank

## **CURRENCY EQUIVALENTS**

(as of 11 August 2021)

Currency unit	–	som (Som)
Som1.00	=	\$0.0118
\$1.00	=	Som84.7016

## **ABBREVIATIONS**

ADB	–	Asian Development Bank
ADF	–	Asian Development Fund
COVID-19	–	coronavirus disease
DPCC	–	Development Partners Coordination Council
EU	–	European Union
GDP	–	gross domestic product
IED	–	Independent Evaluation Department
IMF	–	International Monetary Fund
MLSD	–	Ministry of Labor and Social Development
MOE	–	Ministry of Economy
MOES	–	Ministry of Education and Science
MOF	–	Ministry of Finance
NBKR	–	National Bank of the Kyrgyz Republic
NDS 2040	–	National Development Strategy of the Kyrgyz Republic for 2018–2040
OJSC	–	open joint stock company
PCF	–	per capita financing
PPEF	–	post-program engagement framework
PPP	–	public–private partnership
REX	–	Registration of Export System
SMEs	–	small and medium-sized enterprises
TA	–	technical assistance
TVET	–	technical and vocational education and training
UN	–	United Nations

## **NOTE**

In this report, “\$” refers to United States dollars.

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## CONTENTS

	Page
PROGRAM AT A GLANCE	
I. THE PROPOSAL	1
II. PROGRAM AND RATIONALE	1
A. Background and Development Constraints	1
B. Policy Reform, ADB's Value Addition, and Sustainability	6
C. Expected Outcome of the Reforms	12
D. Development Financing Needs and Budget Support	13
E. Implementation Arrangements	13
III. DUE DILIGENCE	14
IV. ASSURANCES	15
V. RECOMMENDATION	15
APPENDIXES	
1. Policy Design and Monitoring Framework	16
2. List of Linked Documents	48
3. Development Policy Letter	49

## PROGRAM AT A GLANCE

1. Basic Data		Project Number: 52225-003	
Project Name	Promoting Economic Diversification Program (Subprogram 2)	Department/Division	CWRD/CWPF
Country	Kyrgyz Republic	Executing Agency	Ministry of Finance
Borrower	Kyrgyz Republic		
Country Economic Indicators	<a href="https://www.adb.org/Documents/LinkedDocs/?id=52225-003-CEI">https://www.adb.org/Documents/LinkedDocs/?id=52225-003-CEI</a>		
Portfolio at a Glance	<a href="https://www.adb.org/Documents/LinkedDocs/?id=52225-003-PortAtaGlance">https://www.adb.org/Documents/LinkedDocs/?id=52225-003-PortAtaGlance</a>		
2. Sector		ADB Financing (\$ million)	
✓ Public sector management	Economic affairs management		26.67
	Public expenditure and fiscal management		26.67
	Social protection initiatives		26.66
		Total	80.00
3. Operational Priorities		Climate Change Information	
✓ Addressing remaining poverty and reducing inequalities		GHG reductions (tons per annum)	0.000
✓ Accelerating progress in gender equality		Climate Change impact on the Project	Low
✓ Strengthening governance and institutional capacity			
		ADB Financing	
		Adaptation (\$ million)	0.00
		Mitigation (\$ million)	0.00
		Cofinancing	
		Adaptation (\$ million)	0.00
		Mitigation (\$ million)	0.00
Sustainable Development Goals		Gender Equity and Mainstreaming	
SDG 1.3, 1.5, 1.b		Effective gender mainstreaming (EGM)	✓
SDG 2.3			
SDG 4.3			
SDG 5.a, 5.c			
SDG 8.3			
SDG 9.1			
SDG 10.3, 10.4			
SDG 16.6			
SDG 17.17, 17.4			
4. Risk Categorization:		Complex	
5. Safeguard Categorization		Environment: C Involuntary Resettlement: C Indigenous Peoples: C	
6. Financing			
Modality and Sources		Amount (\$ million)	
ADB		80.00	
Sovereign Programmatic Approach Policy-Based Lending (Grant): Asian Development Fund		10.70	
Sovereign Programmatic Approach Policy-Based Lending (Concessional Loan): Ordinary capital resources		69.30	
Cofinancing		0.00	
None		0.00	
Counterpart		0.00	
None		0.00	
Total		80.00	
Currency of ADB Financing: US Dollar			

## I. THE PROPOSAL

1. I submit for your approval the following report and recommendation on (i) a proposed policy-based loan and (ii) proposed grant, both to the Kyrgyz Republic, for subprogram 2 of the Promoting Economic Diversification Program (PEDP), and (iii) the inclusion of proposed subprogram 3 in the programmatic approach.

2. The program continues to support the implementation of reforms in the *National Development Strategy of the Kyrgyz Republic for 2018–2040* (NDS 2040) and its overarching objective of gradually diversifying the Kyrgyz economy away from an over-reliance on gold production and exports (about 6%–10% of gross domestic product [GDP] each year) and remittance-led consumption (about 30% of GDP).<sup>1</sup> The program is a milestone in the NDS 2040 connecting past reform support from the Asian Development Bank (ADB) to the Government of Kyrgyz Republic on trade and investment competitiveness, small and medium-sized enterprise (SME) development, infrastructure development (including through public–private partnerships [PPPs]), and industry-based skills development. The Kyrgyz Republic is recovering from the impact of the coronavirus disease (COVID-19) pandemic outbreak that began in March 2020, which has led to severe economic and employment contraction and fiscal difficulties. This program has been enhanced to support the government stay on the reform course in spite of these challenges, by (i) insulating the originally planned and needed medium-term reform efforts from the crisis effects, (ii) while adding urgent reforms to improve the governance, fiscal management (and buffers) and social protection mechanisms that have now been agreed to be crucial enablers of the original medium-term reform agenda.<sup>2</sup>

## II. PROGRAM AND RATIONALE

### A. Background and Development Constraints

3. **Development constraints.**<sup>3</sup> The current crisis in the Kyrgyz Republic is the worst since the fall of the Soviet Union (para. 4) but it is also just one more of a long series of frequent economic recession episodes that have conflated hardship-inducing external shocks, serious social and political instability, and disruptions to medium-term reform and institutional development plans.<sup>4</sup> This boom-bust pattern explains the lack of income per capita convergence of the country with advanced economies in the last few decades. Even though it is urgent for economic policy to focus on stabilizing the current COVID-19 related health, macroeconomic, and social crises, the government also recognizes that keeping on track efforts to diversify its economy must remain its crucial reform priority. The Kyrgyz Republic's lack of economic diversification remains both (i) at the core of its significant structural vulnerability to external shocks, including an overreliance on commodities sales and migrant labor remittance, and which the lack of fiscal buffers and effective social protection systems exacerbates (including a lack of women's access to social protection, employment, and finance); and (ii) a drag on medium-term economic growth and debt sustainability. Addressing some of its key binding constraints has been a focus of ADB's

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<sup>1</sup> Government of the Kyrgyz Republic. 2018. [National Development Strategy: 2018–2040](#). Bishkek.

<sup>2</sup> Independent Evaluation Department. 2018. [Country Partnership Strategy Final Review Validation: Kyrgyz Republic, 2013–2017](#). Manila: ADB; and Independent Evaluation Department. 2018. [Corporate Evaluation: Policy-Based Lending, 2008–2017: Performance, Results, and Issues of Design](#). Manila: ADB.

<sup>3</sup> Sector assessments (accessible from the list of linked documents in Appendix 2).

<sup>4</sup> ADB. 2019. *Kyrgyz Republic: Improving Growth Potential*. Manila. In the last two decades, the Kyrgyz economy recorded recessionary episodes in 2002, 2005, 2010, 2012, 2016, 2018 and 2020.

support since 2007.<sup>5</sup> There has been incremental progress and important lessons from experience for the design of the proposed programmatic assistance. But major binding constraints remain:

- (i) **Weak trade and investment competitiveness.** Exports are concentrated on a few products (mainly precious metals and mineral commodities and three major markets [Kazakhstan, the Russian Federation, and Switzerland]). This is not only a symptom of the underlying lack of product diversification and weak business environment, it also constitutes a drag on future growth and export potential.<sup>6</sup> Several agricultural products have considerable export potential, but lack the enabling policy and institutional support that could help diversify and expand export penetration, reduce transaction costs associated with customs, and improve farmer knowledge about disease prevention, control, and other required non-price competitiveness enablers.<sup>7</sup> Women represent 44% of the total agricultural workforce, and play an important role in agri-food value chains. In addition, despite a relatively open foreign direct investment (FDI) regime, the sources of FDI inflows remain dependent on a few sources and focused on very few sectors (mineral processing, and finance and insurance). This eliminates a crucial avenue for knowledge and technology transfer from abroad to the Kyrgyz economy. Reforms are also needed to (i) improve the policy, legal, and institutional environment for trade and investment and reflect ongoing Government commitment to improving public sector governance; (ii) strengthen the capacity of small businesses to comply with international market access requirements; and (iii) improve exporter access to market intelligence.<sup>8</sup>
- (ii) **Limited small and medium-sized enterprise development.** The SME share of employment and GDP are low by regional standards.<sup>9</sup> Although formal credit to SMEs has been rising steadily since 2009, banks continue to treat SMEs as high risk-high transaction cost ventures. Collateral requirements can reach between 120%–200% of the total loan amount, making it almost impossible for SMEs to leverage debt to grow their businesses, with greater gender-differentiated effect on women.<sup>10</sup> Most SMEs lack the knowledge, skills and experience to tap into export markets, and graduate into higher value-added activities as businesses mature.<sup>11</sup> SMEs, particularly those in tourism and hospitality, but also small manufacturing, construction, transport and trade sectors, have been particularly vulnerable to the current crisis, as consumer demand has plummeted and economic activity has decreased by 80%. Due to their concentration in these sectors and high incidence of informality, women-headed enterprises, representing over 50% of firms in tourism, hospitality and trade, were disproportionately affected. In terms of social ramifications, there is evidence of rising gender-based violence

<sup>5</sup> ADB. [Kyrgyz Republic: Vocational Education and Skills Development Project](#); ADB. [Kyrgyz Republic: Investment Climate Improvement Program](#). ADB; and [Kyrgyz Republic: Second Investment Climate Improvement Program](#).

<sup>6</sup> ADB. 2020. [Structural Transformation in the Kyrgyz Republic: Engineering Future Paths of Capability Accumulation](#). Manila.

<sup>7</sup> Significant scope in this regard also exists to improve the country's utilization rate under the European Union (EU) Generalised Scheme of Preferences Plus (GSP+) to provide preferential market access to the EU markets.

<sup>8</sup> International Institute for Applied Systems Analysis. 2018. [Industrial Development of Kyrgyzstan: Trade Opportunities, Export Potential and the Role of Economic Integration Processes](#). Laxenburg, Austria

<sup>9</sup> United Nations Conference on Trade and Development. 2017. *The State of Micro and Small and Medium-Sized Enterprise Development in Kyrgyzstan*. Geneva.

<sup>10</sup> Women are less likely to own and control key productive assets (and collateral). The available limited data on number of bank borrowers indicates that women make between 9%–30% of bank borrowers. This might explain why women tend to use unsecured lending from microfinance institutions rather than borrowing from commercial banks. The National Statistic Committee collects and reports on “women-headed businesses”, based on the information collected from business registers (according to the Government Decree dated 23 April 2008 #182).

<sup>11</sup> S. Hasanova. 2018. *Financial Inclusion, Financial Regulation, Financial Literacy and Financial Education in the Kyrgyz Republic*. ADBI Working Paper Series. No. 850. Manila: Asian Development Bank.

following loss of jobs and reductions in income.<sup>12</sup>

- (iii) **Lack of infrastructure development.** The quality of infrastructure in the Kyrgyz Republic is among the lowest in the world—the country ranks 107 out of 140 countries with regard to overall infrastructure quality.<sup>13</sup> Absent or poorly maintained infrastructure significantly increases business costs for air and road transportation and energy, which affects cost competitiveness in energy and transport-intensive sectors. Similar challenges also effect social sector infrastructure.<sup>14</sup> Public investment through the three-year rolling Public Investment Program has traditionally addressed infrastructure development needs in the country, however, needs have outpaced current levels of investment. Public infrastructure investment is characterized by weak infrastructure governance encompassing weak institutional capacity for project preparation, contract management, financial forecasting and budgeting, and monitoring and evaluation.<sup>15</sup> PPPs can be a very efficient procurement avenue to address infrastructure development needs in the country. With ADB support, the government has made significant progress in developing an enabling policy, legal and institutional framework for PPPs. In 2018, the Economist Intelligence Unit ranked the Kyrgyz Republic 9th out of 19 Asian countries for level of PPP readiness,<sup>16</sup> but it also noted slow implementation of PPP projects. The main constraints to effective implementation of PPP projects are: (i) limited PPP understanding, sensitization and awareness within sector ministries; (ii) ineffective gateway review processes within the Ministry of Finance (MOF) to ensure fiscally-responsible PPPs; and (iii) limited access to non-recourse finance for viable PPP projects.
- (iv) **Weak links between skills development and industry needs.** The labor market of the Kyrgyz Republic is characterized by skilled workers and technicians from the Soviet era who are approaching retirement. The current technical and vocational education (TVET) system is not able to meet the labor force replacement rate, which is up to five times higher than the number of skilled workers entering the workforce.<sup>17</sup> The government recognizes that workers who are unprepared for the changing skills requirements are less likely to find employment and more likely to be in volatile low wage jobs. In the absence of a national qualifications system and framework, unstructured TVET system variations have sprung up. Innovative TVET finance reforms such as the introduction of per capita financing (PCF) and incentive funds to improve administration and operations, are needed to accompany the increased use of TVET to modernize the labor force.<sup>18</sup> This lack of policy framework has resulted in (i) insufficient support for employment generation, (ii) migration-led and remittance dependency, and (iii) large shares of low-productivity agricultural employment. There is also a strong gender divide in vocational education, with less than 10% female students in engineering,

<sup>12</sup> During January–March 2020, for example, the number of reported domestic violence cases rose by 65% compared with same period in 2019. ADB–UNDP. 2020. *COVID-19 in the Kyrgyz Republic: Socioeconomic and Vulnerability Impact Assessment and Policy Response*. This was prepared during April–July 2020, under ADB’s technical assistance (TA). ADB. 2018. TA 9624: [Supporting Knowledge Solutions in Central and West Asian Countries](#). Manila.

<sup>13</sup> World Economic Forum. 2018. [The Global Competitiveness Report, 2017–2018](#). Geneva.

<sup>14</sup> For example, expansion of early pre-school education and childcare (only 25% of children aged 3–6 years were enrolled in preschool education in 2020) and safe schools in the country is a Government priority. In addition, improved access to childcare leads to increased labor force participation of women.

<sup>15</sup> Government of the Kyrgyz Republic. 2018. *Report on Results of the Joint Review of Implementation of Public Investment Projects financed by the Asian Development Bank and the World Bank for 2017*, April. Bishkek.

<sup>16</sup> The Economist Intelligence Unit. 2018. [Evaluating the environment for public–private partnerships in Asia: The 2018 Infrascopes](#). London.

<sup>17</sup> ADB. *Unpublished. Technical and Vocational Education and Training—System Rationalization: Strategies and Implementation Plans*. TVET in the Kyrgyz Republic comprises of two levels: primary vocational education (PVE) and secondary vocational education.

<sup>18</sup> PCF is a new form of education finance that is considered international good practice. Funding is based on student numbers rather than the continuation of lump-sum projections (largely based on historic budgeting).

construction and agriculture subjects.<sup>19</sup> Gender segregation in education has effects on the labor market, where women dominate in often lower-paid sectors. For example, in 2019, the gender pay gap—the average difference in earnings between men and women—was 23%.<sup>20</sup>

- (v) **Weak fiscal management and social protection system coverage and targeting.** The lack of fiscal buffers and effective social protection systems exacerbates the vulnerability of the Kyrgyz Republic to external shocks, including the COVID-19 pandemic. This could be attributed to the inherent fiscal procyclicality and liquidity-constrained consumer behavior responses that amplify the shocks through the economy. This procyclicality in both public and private expenditure in crises does not only increase permanent impact on potential growth in general (through, for example, the destruction of franchise value in the private sector that bankruptcies create or asset quality hangover effects in the financial system),<sup>21</sup> but it has also very often brought social instability in the Kyrgyz Republic and political upheaval. Sustained reform efforts and institutional development planning over the last few decades in the Kyrgyz Republic have often fallen prey to the frequent political transitions that external shocks result in. Establishing social protection systems to become more shock-responsive and countercyclical has been a key strategic mechanism in successful development cases. Besides creating political constituencies for reform, such social protection mechanisms help countries navigate through increased trade openness and its adjustment shocks.<sup>22</sup> The COVID-19 pandemic has illustrated again the perils that the Kyrgyz Republic faces in this particular regard. The socio-economic risk to households has been heightened due to low coverage and the inadequacy of its existing social protection transfers.<sup>23</sup> It is also crucial to establish fiscal buffers and debt management options to help address liquidity issues in the immediate aftermath of crises. Methodologies to ensure fiscal oversight of PPPs and ensure they are fiscally responsible, as well as fiscal rules to help regain fiscal space and improve public debt sustainability in the medium-term, are central as well as improving targeting mechanisms to maximize impact and minimize costs of social protection.<sup>24</sup>

4. **Macroeconomic impact of COVID-19 Crisis.** Immediately prior to the crisis, the International Monetary Fund (IMF) assessed the Kyrgyz economy and concluded that macroeconomic and financial sector performance in 2019 was broadly sound. Real GDP growth had increased to 4.6% in 2019 due to a pickup of both gold and non-gold output. The budget deficit had decreased to 0.1% of GDP in 2019, and, as a result, public debt decreased to 51.6% of GDP.<sup>25</sup> But the widespread loss of income and jobs and increase in poverty and income inequality resulting from the COVID-19 pandemic crisis knocked the Kyrgyz economy off from its trajectory. While the government's immediate priority has been to minimize the spread of the contagion, responding to its socio-economic consequences has become crucial. The economy contracted by 8.6% in 2020, the worst recession since the collapse of the Soviet Union in the

<sup>19</sup> Representation of women among vocational managers and technical subject teachers is about 25%.

<sup>20</sup> National Statistics Committee of the Kyrgyz Republic. 2019. *Women and Men of the Kyrgyz Republic*. Bishkek.

<sup>21</sup> A growing body of empirical evidence shows that demand slumps do lead to permanent impacts on potential growth through well-defined mechanisms. [1] Girardi, D., W. Paternesi Meloni and A. Stirati. 2020. *Reverse Hysteresis? Persistent Effects of Autonomous Demand Expansions*. Cambridge Journal of Economics, 44(4), 835–869; [2] Fontanari, C., A. Palumbo and C. Salvatori. 2020. *Potential Output in Theory and Practice: A Revision and Update of Okun's Original Method*. Structural Change and Economic Dynamics, 54, 247–266.

<sup>22</sup> Rodrik, D. 1998. *Why Do More Open Economies Have Bigger Governments?* Journal of Political Economy, 106(5), 997–1032. doi:10.1086/250038.

<sup>23</sup> While they were effective in terms of distributing top-ups to existing beneficiaries, they were less effective in identifying and expanding coverage to the new vulnerable).

<sup>24</sup> The fiscal impact of 2021–2022 will be significant in the Kyrgyz Republic, and fiscal management efficiency reforms will be crucial to create necessary fiscal space and efficiencies, and equip the government with fiscal options that can enable it to pursue renewed and more sustained reform and institutional development efforts.

<sup>25</sup> IMF. 2019. [Kyrgyz Republic: 2019 Article IV Consultation—Press Release; and Staff Report](#). Washington, DC.

1990s. Remittances declined by 25% in early 2020, reflecting the large number of returning migrant workers (mainly from Russian Federation) and the depreciation of the Russian ruble. The fiscal deficit widened to around 3.3% of GDP in 2020 with tax revenues declining by 2.1% of GDP.<sup>26</sup>

5. Growth is expected to rebound in 2021–2022, but uncertainty remains high. Barring a resurgence of the pandemic, the economy is projected to grow by 3.8% in 2021 and by 6.4% in 2022, underpinned by the more favorable global outlook, recovery of domestic activity, higher gold production, and a gradual rebound in tourism, transportation and related services. A budget deficit of 4.2% of GDP is projected for 2021 (Table 1) subject to the availability of financing. This deficit will reduce public debt by about 1.0% of GDP, while maintaining the fiscal stimulus. The budget reflects a cyclical recovery in tax revenue and the observed improvement in tax compliance, a moderate decline in the public sector wage bill, and higher spending on goods and services and investment. However, if sufficient financing cannot be mobilized, further cuts to non-priority expenditure will be needed (for example, goods and services, subsidies and lower priority investment) while preserving health and social spending.<sup>27</sup> The government plans to bring the deficit below 3.0% of GDP and cap public debt at 60% of GDP by 2025, in line with the *Main Directions of Fiscal Policy for 2020–2023*, the government's main fiscal policy statement, and the IMF's policy advice.<sup>28</sup>

**Table 1: Selected Macro-Fiscal Aggregates, 2018–2021 (as of 28 February 2021)**

Item	2018	2019	2020 (e)	2020 (rev.) <sup>a</sup>	2021 (f)
Real GDP (% change)	3.5	4.6	3.4	-8.6	3.8
Inflation (% change, 12-month ave.)	1.5	1.1	4.9	6.3	9.4
Total revenue and grants (% of GDP)	32.5	32.4	32.5	31.0	31.1
<i>Tax revenues</i>	20.2	19.6	21.8	17.5	18.9
Total expenditure and net lending (% of GDP)	33.1	32.5	30.9	34.3	35.3
Overall balance (% of GDP)	-0.6	-0.1	-1.6	-3.3	-4.2
Total public debt (% of GDP)	54.8	51.6	55.5	68.0	67.1
<i>External debt</i>	47.0	43.3	46.7	58.3	56.8
Current account balance (% of GDP)	-12.1	-12.1	-7.7	4.5	-5.8
Nominal GDP (\$ million)	8,271	8,872	8,781	7,747	8,027

e = estimate, f = forecast, GDP = gross domestic product, rev = revised.

<sup>a</sup> Pre-budget support from IMF, ADB, Eurasian Fund for Stabilization and Development and EU.

Sources: Government of Kyrgyz Republic and IMF staff estimates.

6. **Impact of COVID-19 Crisis on government reform agenda.** The government is maintaining its committed course and continues to implement reforms with development partner support. However, the fiscal and social emergencies that became the focus of the Ministries of Agriculture, Economy, Education and Science, Finance, and Labor and Social Development had negative consequences on the general reform momentum of early-2020. The normal functioning of government institutions could not be maintained for large periods of time due to quarantines. Public sector bureaucracies' capacity to keep the most fundamental levels of public services and public policy at work was challenged for most of 2020. It was not only the specific policy dialogue and technical assistance (TA) to reform activities that slowed, but also the inter-ministerial and

<sup>26</sup> The deficit was reduced to 3.3% of GDP through general grant budget support from IMF (\$242 million), ADB (\$50 million through the COVID-19 Active Response and Expenditure Support (CARES) Program), the Eurasian Fund for Stabilization and Development (\$100 million), and the EU (\$34 million).

<sup>27</sup> IMF. 2021. *Kyrgyz Republic—Assessment Letter for the Asian Development Bank*. Washington, DC. (accessible from the list of linked documents in Appendix 2).

<sup>28</sup> Government of Kyrgyz Republic. 2020. *Main Directions of Fiscal Policy for 2020–2023*. Bishkek.

coordination focus that reform challenges entail and require. The reforms originally envisioned for subprogram 2 were delayed.

## **B. Policy Reform, ADB's Value Addition, and Sustainability**

7. In addition to being developed on the basis of the NDS 2040, the proposed program is aligned with ADB's *Strategy 2030*, including operational priorities on addressing remaining poverty and reducing inequalities, accelerating progress in gender equality and strengthening governance and institutional capacity,<sup>29</sup> and with ADB's Country Partnership Strategy for 2018–2022.<sup>30</sup> The program has been prepared with ADB TA and support from the IMF on the policy dialogue with government on debt sustainability and on the preparation of fiscal management reforms.<sup>31</sup> The transition to a dynamic, globally oriented, market-based economy requires consideration for a number of issues that the COVID-19 has illustrated as key: (i) importance of social safety nets to help cushion the impact of the pandemic and structural adjustment costs on the populace, (ii) fiscal buffers to allow an immediate crises response and to create fiscal room to safeguard public expenditures related to the reform effort (paras. 10–18), and (iii) constituency building through policy measures to safeguard public expenditure on social protection while addressing the low coverage and inadequacy of the existing safety net. ADB's programmatic assistance helps incorporate this emerging consensus.

8. **The programmatic approach.** In September 2019, ADB's Board of Directors approved the programmatic approach and a \$50 million grant for subprogram 1.<sup>32</sup> Through 12 policy actions, subprogram 1 helped the government to build the foundation for policy and institutional reforms in agriculture, trade and investment competitiveness, SME development, PPP development and industry-linked skills development. The program was originally designed with two subprograms. Subprogram 2's originally expected implementation was August 2019–July 2021. The COVID-19 pandemic crisis fundamentally disrupted reform timelines and the implementation of the reform preparatory activities under subprogram 2 (para. 6). This was more prevalent in reform areas 1 and 2, and less of a factor in reform areas 3 and 4. But, overall, the original timeline for subprogram 2 implementation suffered, and besides a significant increase in the fiscal needs and fiscal difficulties described in paras. 4–5, the crisis reality and the policy dialogue that ensued has produced a clear awareness for (i) urgent institutional development needs to address emerging problems in the private sector (para. 7), (ii) the key complementary reform needs discussed in para. 3 v, and (iii) particular attention paid to reforms that extend the economic diversification agenda but also reflect Government commitment to advancing specific governance reforms such as improving investor protection and making state-owned enterprises more transparent and accountable. These three items now benefit from a clear policy acknowledgement of urgency from the government.

9. Considering the importance of providing more space to the Government for reform implementation given the complexity of reforms amidst an ongoing pandemic, introducing fiscal management and social protection reforms (paras. 3–4 and 6) and to help Government meet its

<sup>29</sup> ADB. 2018. [\*Strategy 2030: Achieving a Prosperous, Inclusive, Resilient, and Sustainable Asia and the Pacific\*](#). Manila.

<sup>30</sup> ADB. 2018. [\*Country Partnership Strategy. Kyrgyz Republic 2018–2022—Supporting Sustainable Growth, Inclusion, and Regional Cooperation\*](#). Manila.

<sup>31</sup> ADB. 2018. [\*Technical Assistance to the Kyrgyz Republic for Preparing the Promoting Economic Diversification Program\*](#). Manila.

<sup>32</sup> ADB. 2019. [\*Report and Recommendation of the President to the Board of Directors: Proposed Programmatic Approach and Policy-Based Grant for Subprogram 1 to the Kyrgyz Republic for the Promoting Economic Diversification Program\*](#). Manila.

urgent financing needs in 2021 and 2022 (estimated at 4.2% of GDP [or around \$337 million in 2021] and 4.0% of GDP [or around \$349 million] in 2022), the government requested financing for subprogram 2 to be increased to \$80 million (from \$50 million originally planned).<sup>33</sup> The program was also restructured to add a proposed subprogram 3 (amounting to \$50 million and scheduled for Board approval in the third quarter of 2022) and a new reform area that is deemed to be a crucial enabler of the program's objectives (*fiscal and social protection resilience improved to enable post-COVID-19 stabilization and recovery*). These changes meant that some restructuring and re-sequencing of policy actions (17 in total) and sub-policy actions (19) from the original subprogram 2 were needed. Of this number, 7 actions were completed, 9 actions were pushed back to subprogram 3, and 3 were merged to allow better focus.<sup>34</sup> In addition, 8 new actions were added to strengthen the focus on agriculture and food security, and as part of the emerging agreement on fiscal management and social protection reforms. These changes remain fully aligned with the original program outcome, that is, increased broad-based economic growth, and the original logical framework for the program as outlined in the design and monitoring framework for subprogram 1. Overall, the proposed program builds on effective engagement in the Development Partners Coordination Council (DPCC) comprising government and major development partners such as ADB, and the IMF.<sup>35</sup>

**10. Reform area 1: Trade and investment competitiveness to develop non-mineral sector and diversify exports and investments improved.** The actions under this reform area aim to promote the overall enabling environment for investment and export competitiveness and food and agriculture, while addressing some of the scarring effects left by the COVID-19 crisis. Under *subprogram 2*, the government adopted several reform measures to unlock production and supply chains beginning with the Resolution of the “*8th Financing of Agriculture Program*” to provide preferential credits for agricultural producers to accelerate animal husbandry, crop production, processing of agricultural products, and implementation of spring farm work in 2020. This will help change the focus of agricultural policy priorities towards increased agricultural production and food security. All actions have been completed and verified. Under (indicative) *subprogram 3*, Parliament will approve the Law “*On Organic Agricultural Production*” to improve alignment of national organic certification with international standards and improve competitiveness of organic product exports into the EU, Eurasian Economic Union and other international markets. In line with the *Program for the Creation and Development of Trade and Logistics Centers for Agricultural Products in the Kyrgyz Republic for 2019–2023*, the government will (i) complete a feasibility study on the construction of a modern wholesale agricultural market, the first such market in the country, and (ii) establish at least 2 trade and logistics centers for storage, distribution and transportation of agricultural products. The Ministry of Economy (MOE) will roll out the Registration of Export System (REX) for exporting to the EU within the framework of the Generalised System of Preferences Plus (GSP+) preferential market access program.<sup>36</sup>

<sup>33</sup> ADB. 2020. [Country Operations Business Plan: Kyrgyz Republic \(2020–2022\)](#). Manila.

<sup>34</sup> Further elaboration on the modified actions and additional actions taken by the government as compared to the original subprogram 2 indicative reforms is provided in Comparison of Original and Revised Reforms under Subprogram 2 (accessible from the list of linked documents in Appendix 2).

<sup>35</sup> ADB, in particular, has been helping with reforms to improve the investment climate and competitiveness since 2008, but it has also witnessed the negative effects of frequent political transitions on the continuity of reform efforts in general. The analytical basis for this program is supplemented by the ADB–United Nations Development Programme (UNDP) assessments of the socio-economic impact of COVID-19 in the Kyrgyz Republic (footnote 12), findings from ADB's previous and ongoing engagement, and various sector assessments.

<sup>36</sup> The REX will help increase exports to the EU and ensure improved uptake of the program by (i) registering at least 80% of exporters to the EU market, (ii) adopting an Order of the Investment Promotion and Protection Agency (IPPA) on REX system procedures, and (iii) training of IPPA staff to administer REX (with at least 40% women participants). The government will approve and operationalize the Center for Halal Development under MOE (with at least 45%

Finally, an overarching National Investment Strategy for 2021–2025 will be adopted and implementation commenced through, amongst other things, the development of an investment incentives package to attract FDI into key sectors such as clothing and textiles and food processing and targeted geographical locations outside Bishkek and Osh, as well as the operationalization of an investor grievance mechanism.

**11. Reform area 2: Small and medium-sized enterprise development to broaden the economic base and promote entrepreneurship improved.** The actions under this reform area aim to broaden the economic base and promote entrepreneurship and the participation of women in economic activities. While these actions will have critical medium- to long-term impact on job creation, there was also some urgency to implement them to mitigate the adverse impact of the COVID-19 crisis on job opportunities for the poor and vulnerable groups, including women. Under *subprogram 2*, the government established its direct financing policy by executing the Som14 billion “*Financing of Business Entities Program*” in 2020 and provided a direct credit line to all SMEs (at least 30% of which were women-headed SMEs), increased risk pricing efficiency and transparency in credit markets through the full operationalization of an integrated online credit history and scoring system for banks and financial institutions, and increased the use of non-productive agricultural land for, inter alia, collateralization in external finance by submitting the Government Resolution “*On the opinion of the Government of the Kyrgyz Republic on the draft Law of the Kyrgyz Republic On amendments to certain legislative acts of the Kyrgyz Republic on investment support*” to Parliament. The National Bank of Kyrgyz Republic (NBKR) issued regulations for financial institutions to report on guarantees issued to SME’s that are women-headed. This measure will help stabilize collateral requirements, particularly where real estate is used (real estate is the main form of collateral in rural areas, is mainly owned by men and tends to fluctuate in value). The Board of the Open Joint Stock Company (OJSC) Guarantee Fund directed that 30% of the loans guaranteed be reserved for women-headed SMEs. To reduce barriers to entry in markets and tax rules that give birth to rent-seeking and additional informal costs to regulatory compliance, government (i) submitted the draft Law of the Kyrgyz Republic “*On State Registration of Legal Entities, Branches (Representative Offices)*” to Parliament, allowing submission of registration documents in electronic form and automation of legal entity registration processes, and (ii) adopted the Resolution “*Amendments to some decisions of the Government of Kyrgyz Republic*” to ease and improve tax administration and reduce compliance costs to the private sector, enabling consolidated reporting of income tax and social insurance contributions. All actions have been completed and verified.

**12.** Under (indicative) *subprogram 3*, the government will execute the Som16 billion “*Financing of Business Entities Program*” in 2021 to consolidate the policy direction initiated in 2020 for direct financial support to SMEs (at least 35% of beneficiaries must be women-headed SMEs). Sustaining this program on an annual basis will send a strong signal of government support for SME development and entrepreneurship. To expand the range of affordable financial products to SMEs, the government will (i) introduce (with NBKR) warehouse receipt finance to e.g., enable farmers to use their stored produce as financial collateral, (ii) abolish tax reporting for small businesses (applying a simplified taxation system based on retail sales tax to reduce [formal and informal] compliance costs),<sup>37</sup> and (iii) provide a digital platform to improve SME operations,

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female technical staff trained) with an annual budget allocation in 2021 in order to unlock opportunities for exporting to this \$739.5 billion global market.

<sup>37</sup> These different forms of financial assistance will be complemented by Business Service Centers in Bishkek and Osh (staffing them with at least 40% women, and 30% of women at decision making positions) so that businesses are able to (i) obtain permits, licenses, and all other regulatory compliance documentation in one office, and (ii) have access to business planning, skills and technical training, market information and financial resources. There will be periodic reporting on services provided by the Business Centers, disaggregated by type, sex, sector and region.

and expand national and international markets by submitting a draft e-Commerce Bill to Parliament for approval.

**13. Reform Area 3: Public-private partnership to develop social and economic infrastructure improved.** The actions under this reform area aim to develop critical social and economic infrastructure through PPP investments in a fiscally-sustainable manner. This will in turn help reduce the costs of doing business and of delivering public services. Under subprogram 2, the government (i) increased the budget allocation for the Center for Public-Private Partnership from Som7.0 million in 2019 to Som11.1 million in 2020 to allow recruitment of PPP experts, this is crucial to establish key legal and financial expertise in Government, and in turn, allow the Centre to be more effective in the further development of PPPs; (ii) MOE submitted to Cabinet a draft decree for a 5-year strategic framework for PPP development in Kyrgyz Republic called *PPP Development Program 2021–2026*, which sets standards and principles for project development and support and to strengthen fiscal risk management; and (iii) in accordance with the Law of Kyrgyz Republic “*On Public-Private Partnership*”, the Government approved (a) methodological guidelines for assessing fiscal exposure for direct and contingent liabilities of PPP agreements, (b) utilization of a fiscal exposure assessment tool that estimates direct and contingent liabilities for awarded PPP agreements, (c) operational guidelines and model documents to develop financially viable PPP projects in accordance with international good practice; and (d) certified at least 30 Government officials (of which at least 40% were women) in 2020 for Level 1 of the PPP Certification Program by APM Group (APMG) International as part of a comprehensive capacity development plan). All actions have been completed and verified.

**14.** Under (indicative) *subprogram 3*, the government will (i) increase the Center’s budget from Som11.1 million in 2020 to Som14.8 million in 2021, and (ii) ensure certification of another 20 Government officials (with at least 40% female officials trained) in the APMG International PPP Certification Program in order to ensure continued build-up of expertise and effective implementation of the government’s PPP agenda. This action is continued in the post-program engagement framework (PPEF). In line with the *PPP Development Program 2021–2026*, Government will implement the Financial Support Framework for PPPs commencing with submission to Parliament of (i) amendments and regulations to the Law of Kyrgyz Republic “*On Public-Private Partnership*” to identify, approve and monitor all contingent liabilities arising from any PPP agreement irrespective of the value of the PPP project; (ii) regulations to provide for adequate budget allocation to meet any direct or contingent liabilities should they materialize through the establishment of a Guarantee Fund or any other mechanism that meets the purpose of budgeting for direct and contingent liabilities arising from PPP; and (iii) annual reports on the aggregated amount of fiscal spending and future commitments in terms of direct and contingent liabilities arising from all awarded PPP agreements and the related value for money.<sup>38</sup>

**15. Reform area 4: Industry-linked skills development through enhanced internal efficiency and qualifications structure improved.** The actions under this reform area aim to improve the quality, funding and relevance of TVET by modernizing the curricula and teaching and learning materials, improving quality assurance mechanisms, strengthening cooperation with industry, and ensuring adequate TVET financing. Under *subprogram 2*, in order to complete the transition from historical lump-sum budget allocations to annual performance-based budget allocations and ensure better alignment between the TVET curricula and the needs of the labor market, the government (i) piloted PCF in 8 national Centers of Excellence in secondary

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<sup>38</sup> The government will allocate Som254 million through the Project Development Support Fund to at least 7 PPP projects, and will award at least 4 PPP contracts that have been appraised and structured in line with international standards.

vocational education institutions (SVET); (ii) approved the methodology for Sectoral Qualifications Frameworks (SQF), which will match the TVET curricula with sector-and industry-needs; and (iii) approved an Action Plan for a National Qualifications System (NQS). In addition, the Ministry of Education and Science (MOES) legally established and made operational 4 model centers (MCs) in the form of independent entities with 20% of teacher and staff positions filled by women and issued a Ministerial Order to legally establish 8 additional MCs (7 outside Bishkek) with 20% of female teachers and staff, and at least 30% of women in decision making positions in MCs. To promote pre-employment training and on-the-job upskilling, the government established a *Skills Development Fund* (SDF) with an agreed budget allocation of \$250,000 for 2021. All actions have been completed and verified.

16. Under (indicative) *subprogram 3*, the government will (i) complete the roll-out of PCF, with PVET institutions spending not less than 95% of their approved 2020 budget allocation; (ii) evaluate the SVET PCF pilot program before determining whether to complete the nationwide roll out; and (iii) approve the National Qualifications Framework and implement at least 95% of all actions in the NQS Action Plan. The government will establish and operationalize 12 additional MCs (3 outside Bishkek) with 20% of female teachers and staff, and at least 30% of women in decision making positions, and ensure 4 out of 8 additional MCs are fully operational (with 20% of female teachers and staff, and at least 30% of women in decision making positions) in accordance with the approved MOES guidelines and action plan. The government will approve an allocation of \$250,000 for the SDF in 2022 with women comprising at least 30% of participants in the training provided. In the medium-term, budget allocations will be complemented and increasingly substituted by the introduction of a training levy or other private sector cost-share mechanisms.

17. **Reform area 5: Fiscal and social protection resilience to enable post-COVID-19 stabilization and recovery improved.** This reform area aims to strengthen fiscal management and improve resilience to macroeconomic shocks in the future by also expanding the number of social protection beneficiaries in a transparent, evidence-based and targeted manner. This reform area is critical to build the foundation of a more inclusive and sustainable recovery post COVID-19 (para. 3 v).<sup>39</sup> Under *subprogram 2*, to ensure all future emergency support is provided on-budget and to improve consolidated control, monitoring, recording and management reporting, MOF approved an Order to report on all expenses related to COVID-19 (incorporating all financial assistance provided for COVID-19 into the consolidated report of the treasury management information system and mandatory completion of ex-post audits and disclosure of the results on MOF's website). The government approved a new *Strategy for Public Debt Management, 2020–2023* setting targets to deepen the domestic debt market, improve public debt management and ensure COVID-19 emergency response support remains within prudent debt limits.<sup>40</sup> To further enhance Government's ability to rapidly respond to shocks in the future, MOF (i) approved the *Medium-Term Action Plan for Development of Public Finance Management, 2020–2022* to chart key emerging reform objectives in budget planning, medium-term budget forecasting, public

<sup>39</sup> In addition, 3 policy actions that have been developed and agreed with the government will also be considered within the implementation of the World Bank's International Development Association (IDA) Sustainable Development Finance Policy (SDFP) to which ADB will be aligned during the ADF13 period. The objective of the SDFP is to incentivize countries to borrow sustainably and promote coordination between IDA and other creditors. The relevant policy actions are PA 3.14 and PA 3.15 in the PDMF.

<sup>40</sup> Key measures from the new Strategy include medium-term indicators for debt sustainability and a medium-term target for domestic debt. The government commenced implementation through (i) issuance of an order mandating the periodic preparation and approval of the next Medium-Term Debt Strategies and their annual review, (ii) adoption of medium-term indicators jointly prepared with IMF to reduce the fiscal deficit to 3.0% of GDP and overall public debt to 60% of GDP by 2024 as reflected in the Main Directions of Fiscal Policy for 2022–2024 (footnote 28), (iii) adoption of a medium-term domestic debt target of 16% of GDP by 2025 to reduce vulnerability to currency risks.

procurement, improving accounting and reporting standards, and improving internal audit and control procedures; and (ii) established a fiscal buffer, known as the State Budget Reserve, within the level of 1.0% of total budget expenditure, and fully funded it in the 2020 national budget. Finally, Cabinet submitted to Parliament fiscal rules to remove Government discretion to change the annual debt ceiling and to embed a rule-based fiscal framework for determining the debt ceiling and, amongst other things, determine corrective measures and sanctions to be applied if the debt ceiling is breached (defining special circumstances in which the debt ceiling may be breached as well as the path for fiscal adjustment). Recognizing that it would need to accommodate increasing pressure on its social protection program, the government established a “single window”, a national hotline and informational portal, for citizens that need social protection due to the COVID-19 pandemic. This single window enabled vulnerable groups, especially those that have been greatly affected by the pandemic such as the recently unemployed and poor families that have lost their main source of income, and victims of domestic violence, to request social assistance through the hotline.<sup>41</sup> The government also improved the Ministry of Labor and Social Development (MLSD) database structure and data collection by imposing sex, age, and regional-disaggregated information collection of social protection beneficiaries when they apply for assistance (allocating resources for rapid validation).<sup>42</sup> All actions have been completed and verified.

18. Under (indicative) *subprogram 3*, the MOF will introduce legal amendments to the Law on the Budget and the Budget Code to enable mandatory annual publishing of (i) the government’s annual borrowing plans and fiscal risk statement as reflected in the budget, and (ii) the annual list of borrowings of the seven largest state-owned enterprises and ensure that their international financial reporting standards (IFRS)-based annual audited financial statements and the accompanying notes are publicly disclosed. To strengthen fiscal transparency and resilience, the government will prepare and publish a detailed annual fiscal risk assessment. The government will also amend the eligibility criteria and reconfigure business processes of the *Monthly Benefit for Poor Families with Children (MBPFC)* and unemployment benefits to increase coverage of social protection and ensure high uptake rates by newly vulnerable groups. Finally, the government will legislate the provision of a guaranteed but sustainable minimum level of social services for vulnerable groups.

19. **ADB’s value addition.** ADB is a longstanding partner in each of the reform areas proposed. *Subprogram 2* builds on this strong base of country knowledge and more than a decade of close collaboration, policy dialogue and reform effort (footnote 5), which has survived several political cycles due to strong bipartisan support. This strong relationship has enabled ADB to significantly contribute to the government’s economic diversification efforts, as well as, (i) promote gender empowerment and ensure its formalization in government’s policy agenda, (ii) rapidly restructure the program to support immediate challenges of the Government during a period of public health and macroeconomic crises, (iii) introduce and promote other enabling policy reforms that have not received high priority in the past such as fiscal and debt management and social protection, and (iv) rapidly repurpose and provide additional TA to support reform preparation, implementation and monitoring and evaluation.

20. **Lessons Learned.** Key lessons from past interventions and ADB’s experience with policy-

<sup>41</sup> More than 471,000 people (around 7% of the population) have applied for support.

<sup>42</sup> This disaggregated data will help improve the overall social protection system by improving transparency, targeting and alignment of social protection programs in the future. To establish a new targeting framework for social protection of vulnerable groups, and immediate integration of the unemployed due to the COVID-19 pandemic and the victims of domestic violence, the Government approved updating of the MLSD social protection database to include data disaggregated by sex, age and region.

based lending in Kyrgyz Republic and Central Asia have been incorporated into program design:<sup>43</sup>

- (i) **ADB should help develop blueprints for institutional reforms, since these are critical for successful implementation of policy-based loans along with development partner coordination.** Implementation of institutional reforms are more effective and efficient when there is an adequate and detailed blueprint with clear and measurable results indicators.
- (ii) **ADB should continue to support business and investment climate reforms.** The use of long-term and adaptable/flexible programmatic assistance and TA is recommended to support a medium-to long-term reform path, and necessary for sustainability of reforms.
- (iii) **Phasing of technical and vocational education and training reform.** Project interventions demonstrated that TVET reform takes time to be effective, and that the engagement of stakeholders, particularly industry, is slow. Engagement over 10–15 years, involving three or four project cycles and links to related programs for policy reform is likely to provide the most effective and sustainable results.

21. **Development partner coordination.** The program was prepared in close consultation with other development partners, including through the DPCC.<sup>44</sup> Trade and investment competitiveness, SME and gender empowerment reforms have been coordinated with the World Bank (WB), the European Bank for Reconstruction and Development, the United Kingdom Foreign Commonwealth and Development Office, the EU, and the United Nations (UN) agencies; PPP reforms with the WB and International Finance Corporation; Food security reforms with the UN agencies and the Food and Agriculture Organization; Governance and fiscal management with the IMF, the EU and the WB; and Social protection with the UN agencies. The government has requested budget support from other development partners for the years to come through the DPCC, and has sought debt restructuring where possible. In 2021, only ADB is providing policy-based lending. The IMF confirmed in its assessment letter of 19 May 2021 that its updated Debt Sustainability Analysis, which includes the proposed ADB financing of \$80 million, indicates that the Kyrgyz Republic's debt remains sustainable and at moderate risk of debt distress for both external public debt and total public debt (footnote 27).

### C. Expected Outcome of the Reforms

22. The overarching objective of the program is the *"creation of decent jobs, providing decent employment and stable income for people" (NDS 2040)*. As outcome, the program aims to have broad-based economic growth increased.<sup>45</sup> There are no revisions to the outcome or output indicators under the original programmatic approach, as these remain fully aligned with the current reform proposals. Links between the reform proposals and the outcome can be illustrated as follows: (i) *for reform area 1*, for example, improved compliance with export market regulations can help increase utilization of preferential market access into the EU from 60% to 80% by 2023; (ii) *for reform area 2*, for example, key reforms can help ensure that by 2023 the OJSC Guarantee Fund lends 30% of its portfolio to its women-headed SME clients, which will be a substantial improvement over the current situation; (iii) *for reform area 3*, for example, an international best practice PPP policy, legal and institutional framework can ensure that the government is able to meet its significant infrastructure needs in a fiscally responsible way; (iv) *for reform area 4*, for example, improvements in the match between the education system curricula and sector- and industry-needs will be demonstrated by the percentage of firms that identify an inadequately educated workforce as a major constraint to business development declining from 33% in 2014

<sup>43</sup> Independent Evaluation Department (IED). [Validation Report: Investment Climate Improvement Program](#). ADB; IED. [Validation Report: Second Investment Climate Improvement Program](#). ADB; and IED. [Validation Report: Vocational Education and Skills Development Project](#). ADB. All programs were rated successful overall.

<sup>44</sup> Development Coordination (accessible from the list of linked documents in Appendix 2).

<sup>45</sup> The policy design and monitoring framework is in Appendix 1.

to 30% by 2023;<sup>46</sup> and (v) *for reform area 5*, for example, the establishment of fiscal buffers and effective social protection systems can mitigate the inherent fiscal procyclicality and liquidity-constrained consumer behavior responses to macroeconomic shocks. This will be demonstrated by the reduction of overall public debt to 60% by 2024 while also improving social assistance and protection.<sup>47</sup>

## **D. Development Financing Needs and Budget Support**

23. The government's overall financing needs amount to around \$337 million (or 4.2% of GDP) in 2021 and \$349 million (or 4.0% of GDP) in 2022. The budget deficit in 2021 will be partially supported by the proposed loan and grant totaling \$80 million. As per the government's financing strategy, the balance will be financed through further cuts in non-priority expenditure (para. 5). As Government securities currently account for only 8.0% of banking sector assets, there is room for absorption in the domestic financial market. However, if sufficient financing cannot be mobilized, the government will identify non-priority expenditure cuts and renew efforts to engage with international partners to mobilize more concessional resources rather than higher domestic financing, which may increase borrowing costs and crowd out private credit (footnote 27). For *subprogram 2*, the government has requested (i) a concessional loan of \$69.3 million from ADB's ordinary capital resources, and (ii) a grant not exceeding \$10.7 million from ADB's Special Funds resources (Asian Development Fund). The loan will have a 24-year term, including a grace period of 8 years; an interest rate of 1.0% per year during the grace period and 1.5% per year thereafter; and such other terms and conditions set forth in the draft loan agreement. ADB determined the proposed loan and grant size considering the government's commitment to economic diversification reforms and the country's development financing needs.

## **E. Implementation Arrangements**

24. MOF will be the executing agency for subprogram 2 following the government's decision to prioritize high-level administrative attention to the implementation of the restructured program in order to secure much needed policy financing. MOF, MOE, MOES and MLSD will be the implementing agencies. MOF, Prime Minister's Office, and MOE will monitor and evaluate the overall effectiveness of the program through the program completion report process. These three agencies have extensive experience with implementing ADB-financed policy-based lending programs and are responsible for supporting and monitoring the implementation of the policy matrix and leading inter-agency coordination of the PPEF, the latter of which is being included to highlight the trajectory and conclusion of the reform path. Support for reform implementation was provided through ongoing TA (footnote 30). The implementation period is August 2019–March 2021 for *subprogram 2*. *Subprogram 3* is expected to be implemented from April 2021–June 2022. The PPEF is expected to be implemented in 2022 and 2023. The proceeds of the policy-based loan and grant will be withdrawn following ADB's Loan Disbursement Handbook (2017, as amended from time to time).<sup>48</sup>

<sup>46</sup> World Bank. 2019. *Kyrgyz Republic—Enterprise Surveys*. World Bank Group. Washington, DC.

<sup>47</sup> The registry of beneficiaries will show (i) disaggregated data by sex, regions, and type of receiver (family or individuals), and (ii) validation and extension of eligibility certificates. The reform will also include the launch of the information portal and a national toll-free hot line to apply for social assistance, including for victims of domestic violence. Program Impact Assessment (accessible from the list of linked documents in Appendix 2).

<sup>48</sup> List of Ineligible Items (accessible from the list of linked documents in Appendix 2).

### III. DUE DILIGENCE

25. **Safeguards.** Following ADB's *Safeguard Policy Statement* (2009), the program is classified category C for the environment, involuntary resettlement, and indigenous peoples. Program activities will be confined to policy and institutional reforms. No activity will result in or lead to involuntary resettlement, or negatively affect indigenous peoples or the environment. Program proceeds will not be used for any activities resulting in physical or economic displacement, as defined by ADB's *Safeguard Policy Statement*.<sup>49</sup>

26. **Poverty and social.** Until the crisis, the country had registered good progress in poverty reduction, as the general poverty rate (by national definition) fell from 31.7% of total population in 2008–2009 to 22.4% (some 1,429,621 people) in 2018. A large proportion of the population remains vulnerable: in 2015, 35% of the population had income between the national poverty line and 1.5 times that level (footnote 12). A large section of the population is thus either poor or vulnerable to poverty, at risk of a minor income shock that push them into destitution. The COVID-19 pandemic has swelled the numbers of those who are either in self-employment or in precarious employment, and do not have access to meaningful support in times of crisis through the national social protection system. While the impact of the crisis is being picked up in the official poverty data and analyzed, information from the World Food Programme (WFP) May 2020 survey points to growing food security concerns (footnote 12).

27. **Gender.** The program's gender categorization is "*effective gender mainstreaming*". Key policy actions aim to ensure that women are represented as beneficiaries, agents of change and decision makers, and that women are considered in the reform areas of the program. For example, in adopting and implementing measures to increase access to finance for women-headed SMEs, such as the 30% quotas offered under the "*Financing of Business Entities Program*" and by the OJSC Guarantee Fund, the program mitigates the loss of income of women entrepreneurs (who head 35% of SMEs) and women workers who make up around 33% of the SME workforce and who have been disproportionately affected by the pandemic.<sup>50</sup> Other measures as targets for female staff in capacity building activities for IAs, the number of teaching staff and senior management positions in the MCs reserved for women, will help ensure gender empowerment measures are mainstreamed into formal government policy and operations. Domestic violence is widespread and on the rise, and affects women of all social strata. The collection of sex-disaggregated data has been prioritized throughout the program.

28. **Governance.** ADB completed a *Governance Risk Assessment* in 2018 in line with the implementation guidelines of its *Second Governance and Anticorruption Action Plan*.<sup>51</sup> The assessment found that the country's PFM, public procurement and anticorruption systems were functioning well. However, there were also significant weaknesses across all three areas that required strong political will and joint development partner support to address. In the PFM area, for example, poor revenue forecasting, budget credibility, investment planning, off-budget fund reporting and reconciliation, financial management information system use and interoperability, and internal and external auditing, need to be prioritized. In public procurement, procuring entities cannot undertake two-stage bidding and strategic procurement planning is not undertaken due to

<sup>49</sup> Summary Poverty Reduction and Social Strategy (accessible from the list of linked documents in Appendix 2).

<sup>50</sup> In TVET system female teacher are less represented in technical subjects (transport, energy, construction, metal processing) and prevail in subjects like accounting, sewing, and cooking. Gender segregation in education continues in the labor market, where women dominate in often lower-paid sectors. Measures such as quotas for teaching, staff and senior management positions in the MCs reserved for women will help ensure gender empowerment is mainstreamed into formal government policy and operations.

<sup>51</sup> ADB. 2006. [Second Governance and Anticorruption Action Plan \(GACAPII\)](#). Manila.

weaknesses in the legal framework and capacity limitations.<sup>52</sup> The government, with support from development partners including ADB, the IMF, the World Bank, the EU, the UK Foreign, Commonwealth and Development Department, the Swiss Agency for Development and Cooperation and the United States Agency for International Development, are making a concerted effort to overcome weaknesses in these areas through iterative reform strategies, action plans and TA.<sup>53</sup>

29. **Risks and mitigating measures.** Major risks and mitigating measures are highlighted in the policy design and monitoring framework and described in detail in the risk assessment and risk management plan.<sup>54</sup> The risk that the volatile political situation and changes in leadership lead to weakening reform momentum is mitigated by the following: (i) the new Government has formally requested and agreed to the proposed subprogram (subprogram 1 was approved by the previous Government), and (ii) the economic diversification agenda has widespread political and bureaucratic support (para. 19). It is the overall objective of the NDS 2040, the “Unity, Trust and Prosperity, 2018–2022” program (the medium-term development plan of the previous Government) and the “Real Targets, New Perspectives, 2021–2025” program (the plan of the new Government).

30. ADB’s Anticorruption Policy (1998, as amended to date) was explained to and discussed with MOF.

#### IV. ASSURANCES

31. The government has assured ADB that implementation of the program shall conform to all applicable ADB policies including those concerning anticorruption measures, safeguards, gender, procurement, consulting services, and disbursement as described in detail in the loan and grant agreements. All policy actions completed by the government as specified in the policy matrix relating to the program will have to continue to be in effect.

#### V. RECOMMENDATION

32. I am satisfied that the proposed policy-based loan and grant would comply with the Articles of Agreement of the Asian Development Bank (ADB) and recommend that the Board approve:

- (i) the loan of \$69,300,000 to the Kyrgyz Republic for subprogram 2 of the Promoting Economic Diversification Program from ADB’s ordinary capital resources, in concessional terms, with an interest charge at the rate of 1.0% per year during the grace period and 1.5% per year thereafter; for a term of 24 years, including a grace period of 8 years; and such other terms and conditions as are substantially in accordance with those set forth in the draft loan agreement presented to the Board; and
- (ii) the grant not exceeding \$10,700,000 to the Kyrgyz Republic for the subprogram 2 of the Promoting Economic Diversification Program, from ADB’s Special Funds resources (Asian Development Fund) on terms and conditions that are substantially in accordance with those set forth in the draft grant agreement presented to the Board; and the inclusion of subprogram 3 in the programmatic approach (para. 9).

31 August 2021

Masatsugu Asakawa  
President

<sup>52</sup> Although corruption is perceived to be high, the prosecution of several former ministers and senior civil servants has increased since 2018 demonstrating government’s commitment to reducing corruption.

<sup>53</sup> ADB. 2018. *Kyrgyz Republic: Country Governance Risk Assessment*. Manila.

<sup>54</sup> Risk Assessment and Risk Management Plan (accessible from the list of linked documents in Appendix 2).

## POLICY DESIGN AND MONITORING FRAMEWORK

<b>Country's Overarching Development Objective:</b> Creation of decent jobs, providing decent employment and stable income for people. (National Development Strategy) <sup>a</sup>				
<b>Outcome</b> Broad-based economic growth increased.		<b>Risks and Critical Assumptions</b> R: Volatile political situation and changes in leadership lead to weakening reform momentum. Negative economic impacts of COVID-19 pandemic are more severe than projected. Weak administrative capacity of implementing agencies because of a lack of skilled staff, limited resources, and other competing priorities. Lack of internal audit units and insufficient internal controls in line ministries weakens expenditure management and could lead to diversion and mismanagement of funds.		
<b>Prior Actions:</b> <b>Subprogram 1</b> <b>(Completed: August 2018–July 2019)</b>	<b>Prior Actions:</b> <b>Subprogram 2</b> <b>(Completed: August 2019–March 2021)</b>	<b>Policy Actions:</b> <b>Subprogram 3</b> <b>(April 2021–June 2022)</b>	<b>Outcome Indicators</b>	<b>Post-Program Engagement Framework (2022–2023)</b>
Reform Area 1: Trade and investment competitiveness to develop non-mineral sector and diversify exports and investments improved.				
1.1 Government has approved the Kyrgyz Republic Food Security and Nutrition Program 2019–2023 to improve Kyrgyz Republic's nutritional status with sections addressing the specific food and nutrition needs of women, men and children and their role in food and nutrition security, ensure	2.1 To enable the change in agricultural policy priorities towards increased agricultural production and food security, the Government adopted the Resolution of the "8th Financing of Agriculture Program" – a priority action in the <i>Food Security and Nutrition Program 2019–2023</i> which provides preferential credits for agricultural	3.1 The Law "On Organic Agricultural Production" will be submitted to Parliament for approval in order to improve alignment of national organic certification with international standards and improve competitiveness of organic products from Kyrgyz Republic in the EU	a. Kyrgyz Republic's utilization rate under the EU GSP+ preferential trade access increases to 80% by 2023 (2018 baseline: 60%). Source: MOE annual reports.	<ul style="list-style-type: none"> <li>• Government continues to provide exporters with market information and export assistance to diversify export products and markets.</li> <li>• Government continues to build trade and logistics centers in strategic locations to improve market access for farmers and improve export opportunities.</li> <li>• Government continues the implementation of the Food Security and Nutrition Action Plan 2019–2023, with specific attention to the following:</li> </ul>

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consistency of food supplies to the domestic market and compliance with export market consumer protection standards.	producers to accelerate animal husbandry, crop production, processing of agricultural products, and implementation of spring farm work in 2020.	and other international markets.		(i) Government assesses unmet demand for agricultural and agribusiness credit (including demand for women farmers and women rural entrepreneurs) with the aim to expand the resource envelope for targeted concessional finance programs by 2022.
1.2 Government has approved the <i>Program for the Creation and Development of Trade and Logistics Centers for Agricultural Products in the Kyrgyz Republic for 2019–2023</i> to reduce storage, distribution and transportation costs for agricultural producers.		3.2 As part of implementation of the <i>“Program for the Creation and Development of Trade and Logistics Centers for Agricultural Products in the Kyrgyz Republic for 2019–2023”</i> , Government will: (i) complete a feasibility study on the construction of a modern wholesale agricultural market for Kyrgyz Republic; and (ii) establish at least		(ii) Ministry of Agriculture in cooperation with the State Agency for Water Resources reviews and develops policies and programs for increasing irrigated and dryland wheat productivity by 30% over 10 years and seek resources for its implementation.  <ul style="list-style-type: none"> <li>• Government completes construction of a modern wholesale agricultural market.</li> <li>• Government develops matching grant programs for farmers and farmer groups</li> </ul>

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		2 trade and logistics centers.		(including women farmers and women cooperatives) accompanied with training program (with at least 30% women participants) to improve product storage capacity and initial packaging and processing.
1.3 Government has approved the <i>Export Development Program (EDP) 2019–2023</i> which outlines the export strategy and actions to develop the country's export sector, and has commenced implementation of the EDP by: (i) designating a dedicated body within the Government to administer the REX for exporting to the markets of the European Union (EU) countries within the framework of GSP+ trade privileges;		3.3 MOE will roll out the REX, which will help increase exports to the EU under the GSP+ trade privileges program and ensure improved uptake of the program by: (i) registering in REX at least 80% of exporters to the EU market; <sup>b</sup> (ii) adopting an Order of the Investment Promotion and Protection Agency (IPPA) on REX system procedures; and (iii) training of IPPA staff to administer		<ul style="list-style-type: none"> <li>• Government develops a program to overcome barriers and constraints to agricultural trade and work with EA, EU members to develop the concept of a green channel aiming to minimize disruption to agricultural products and food trade.</li> <li>• Government approves the Program for the Development of Pastures and Livestock Breeding in the Kyrgyz Republic for 2020–2024.</li> <li>• Government introduces factoring by commercial banks and other innovative financial instruments for exporters.</li> </ul>

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<p>(ii) obtained the International Laboratory Accreditation Cooperation (ILAC) for the Kyrgyz Center of Accreditation (KCA) through ILAC Mutual Recognition Arrangement (ILAC MRA) to enhance product standardization and harmonization with EU and Eurasian Economic Union access conditions;</p> <p>(iii) signing an agreement with the Islamic Development Bank on preparation of feasibility study to establish the</p>		<p>REX (with at least 40% women participants).</p> <p>3.4 Government will approve and operationalize the “<i>Center for Halal Development</i>” under MOE (with at least 45% female technical staff trained) with an annual budget allocation of \$1.0 million in 2021.</p>		<ul style="list-style-type: none"> <li>• Government continues to increase funding of the Civil Aviation Agency to ensure there are sufficient trained employees to inspect aircraft and equipment based on international standards.</li> </ul>

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<p>integrated supply chain park for Halal product development and export; and</p> <p>(iv) KCA obtaining the status of a full member of the International Forum on Halal Accreditation.</p>				
<p>1.4 Enabling environment to promote diversified foreign investments has been developed through:</p>		<p>3.5 Government will adopt a National Investment Strategy for 2021–2025 and will commence implementation of the strategy through:</p> <p>(i) upgrade of the Investment Promotion Agency to a Ministry of Investment to enable ministerial-level attention to</p>		

<p>(i) Government adopted an Annual Action Plan to improve country ranking in World Bank's rating on Doing Business and have commenced implementation of the following measures:</p> <ul style="list-style-type: none"> <li>• starting a business including amending the Law of the Kyrgyz Republic "On State Registration of Legal Entities, Branches (Representative Offices)" to allow filing of documents in electronic form;</li> <li>• getting electricity including improving power supply</li> </ul>		<p>investment issues;</p> <p>(ii) introduction of an investment incentives regime in targeted sectors and specified geographical locations; and</p> <p>(iii) operationalization of an investor grievance mechanism.</p>		
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<p>reliability and transparency by publishing the average duration and frequency of power outages, as well as the average time to restore power to consumers, on the power utility's website;</p> <ul style="list-style-type: none"> <li>• registering property including publishing real estate data on the government website;</li> <li>• getting credit including introducing a credit rating system and credit scores for borrowers;</li> <li>• paying taxes including introducing consolidated reporting on</li> </ul>				

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<p>income tax and social contributions;</p> <ul style="list-style-type: none"> <li>• trading across borders including risk-based customs control;</li> <li>• enforcing contracts including addressing creditors' claims by consolidating all relevant information in an electronic database; and</li> <li>• resolving insolvency including promoting transparent orderly disposition of assets for distressed companies;</li> </ul>				

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(ii) liberalizing the regulations of the aviation industry through the introduction of the 5th Level of Freedom of Air, which will allow airlines to carry international revenue traffic to help develop tourism, trade and transport logistics industries.				
<b>Reform Area 2: Small and medium-sized enterprise development to broaden the economic base and promote entrepreneurship improved.</b>				
1.5 SME including women-entrepreneurs' access to finance and services is improved through: (i) Jogorku Kenesh (Parliament) approval of a new version of the Law on Guarantee Funds to authorize	2.2 To promote SMEs access to finance and entrepreneurship, the Government and relevant authorities have taken the following reform and policy measures: (i) enabled direct financial support for SME, through the	3.6 To demonstrate its ongoing commitment to SME development and entrepreneurship to the private sector: (i) Government executes a budget allocation of	b. Of the total number of clients of the OJSC Guarantee Fund, at least 30% women-headed received financial loans by 2023 (2020	<ul style="list-style-type: none"> <li>• Government and NBKR continue to implement financial literacy programs and introduce digital financial services and technology platforms for entrepreneurs, especially women.</li> <li>• Government opens more business centers in different oblasts or regions of Kyrgyz</li> </ul>

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<p>the NBKR to regulate and supervise the Guarantee Fund;</p> <p>(ii) NBKR approval of a capital increase for the Guarantee Fund by up to 49%; and</p> <p>(iii) NBKR approval of changes to its regulatory requirements to increase access to financing through:</p> <p>a) Optimization of collateral requirements for the provision of loans;</p> <p>b) Establishment of a credit rating system; and</p> <p>c) Introduction of electronic signatures for online lending to improve financial intermediation.</p>	<p>execution of the Som14 billion “<i>Financing of Business Entities Program</i>” in 2020 which provided a credit line to all SMEs, of which 30% of beneficiaries were women-headed;</p> <p>(ii) increased risk pricing efficiency and transparency in credit markets through the full operationalization of an integrated online credit history and credit scoring system for banks and financial institutions; and</p> <p>(iii) submitted the Government Resolution “On the opinion of the Government of the Kyrgyz Republic on the draft Law of the Kyrgyz Republic “On amendments to certain legislative</p>	<p>Som16 billion in 2021 for the <i>Financing of Business Entities Program</i> and assigns at least 35% of the credit line to women-headed SMEs;</p> <p>(ii) Government and NBKR will introduce warehouse receipt finance, which will enable farmers to use their stored produce as collateral, in order to expand the range of affordable lending to SMEs;</p> <p>(iii) abolish tax reporting for small businesses</p>	<p>Baseline: Zero). Source: OJSC Guarantee Fund annual reports.</p>	<p>Republic (with at least 40% female technical staff).</p> <ul style="list-style-type: none"> <li>• Government funds private equity and venture capital firms to expand the range of non-collateral financing for SMEs.</li> </ul>

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	<p>acts of the Kyrgyz Republic on investment support" to Parliament to increase the use of non-productive agricultural land for, inter alia, collateralization in external finance.</p> <p>2.3 To strengthen the regulatory governance and targeting framework for SME lending:</p> <p>(i) NBKR issued requirements for monthly reporting of guarantee funds by all financial institutions on issued guarantees for women-headed SMEs; and</p> <p>(ii) the board of OJSC Guarantee Fund resolved to ensure that 30% of guaranteed loans are reserved for</p>	<p>and apply a simplified taxation system based on retail sales tax; and</p> <p>(iv) submit the draft e-Commerce Bill to Parliament for approval in order to provide a digital platform to improve SME operations, expand national and international markets, and increase growth potential.</p>		

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	women-headed SMEs. <sup>c</sup>			
1.6 Government has approved the <i>Concept for Development of Business Service Centers for 2019–2022</i> , to provide a range of services including obtaining regulatory approvals to start a business and capacity building and training for SMEs and entrepreneurs.	2.4 To reduce barriers to entry in markets, tax compliance and other transactions costs to SMEs that give birth to rent-seeking and additional informal costs of regulatory compliance, Government: (i) submitted the draft Law of the Kyrgyz Republic “ <i>On State Registration of Legal Entities, Branches (Representative Offices)</i> ” to Parliament, allowing submission of registration documents in electronic form and automation of legal entity registration processes. This will improve	3.7 To improve business start-up and regulatory compliance and expand the range of support services available, MOE will operationalize the Bishkek and Osh Business Service Centers (staffing with at least 40% women, and 30% of women at decision making positions) so that businesses are able to obtain permits, licenses, and all other government requirements in one office as well as have access to business planning, skills and technical training, and financial resources with periodic reporting on		

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	<p>transparency and promote good corporate governance in business formalization, and reduce transaction costs of starting a business; and</p> <p>(ii) adopted the Resolution “<i>On Amendments to some decisions of the Government of Kyrgyz Republic</i>” to ease and improve tax administration, enabling consolidated reporting of income tax and social insurance contributions.</p>	<p>services provided and disaggregated by type, sex, sector and region.</p>		
<b>Reform Area 3: Public–private partnership development to develop social and economic infrastructure improved.</b>				
1.7 MOE has adopted a PPP Manual including model tender documents and gender-sensitive operational	2.5 To upgrade the effectiveness and technical competence of the Center for PPP, the Government increased the	3.8 To ensure continued expert support for the operations of the Center for PPP, Government will: (i) increase the	c. The Kyrgyz Republic’s ranking (1st) in Central Asia in The Economist Intelligence Unit Infrascopes	<ul style="list-style-type: none"> <li>• Government ensures adaptation of the proposed amendments by Parliament and continues to manage the fiscal exposure arising from PPP to ensure fiscal sustainability.</li> </ul>

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<p>guidelines on identification, preparation and implementation of priority socially-oriented PPP projects.</p>	<p>Center's budget allocation from Som7.0 million in 2019 to Som11.1 million in 2020 to allow recruitment of PPP experts.</p>	<p>Center's budget from Som11.1 million to Som14.8 million in 2021 and (ii) MOE will ensure certification of another 20 Government officials (with at least 40% female officials trained) in the APM Group (APMG) International PPP Certification Program.<sup>d</sup></p>	<p>report for level of PPP readiness is maintained. (2019 baseline: 1st in Central Asia). Source: Economist Intelligence Unit.</p>	<ul style="list-style-type: none"> <li>• Government provides for continued CP3P certification for staff of the PPP Center.</li> <li>• Government reviews the framework for gender-responsive identification, preparation, tendering and implementation of PPP projects in order to increase the efficiency and effectiveness of PPP projects.</li> <li>• Government continuously undertakes review and enhancement of operational guidelines and model document to further improve the efficiency and effectiveness of, and integrating gender considerations<sup>e</sup> in project preparation and implementation.</li> <li>• Government continues to raise awareness through expanded outreach activities by the PPP Center and understanding of PPPs through proactive promotion and communication</li> </ul>

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				<p>in order to further sensitize and inform relevant stakeholders in particular line ministries.</p> <ul style="list-style-type: none"> <li>• The PPP Center maintains an appropriate level of staff (with at least 40% female staff) in terms of quantity and quality to coordinate, promote and support the development of PPP.</li> <li>• Government continues to allocate and spend the necessary budget resources for PPP project development to ensure adequate project preparation and reducing the risk of project failure.</li> <li>• Government continues to tender PPP projects in order to improve the quality of public service delivery and reduce the infrastructure gap.</li> </ul>
1.8 Government has approved the establishment of the Center for Public–Private	2.6 To eliminate past ad-hoc, uncoordinated and harmful practices and ensure a fiscally-responsible	3.9 In line with the <i>PPP Development Program 2021–2026</i> , the Government will		

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Partnership with budgetary allocation of \$88,000 for 2019 in order to support and accelerate development of PPP projects.	PPP approach, the MOE submitted to Cabinet a draft decree for a 5-year strategic framework for PPP development in Kyrgyz Republic entitled <i>PPP Development Program 2021–2026</i> to set standards and principles for project development and support and to strengthen fiscal risk management.	implement the <i>Financial Support Framework for PPPs</i> commencing with submission to Parliament of: (i) amendments and regulations to the Law of Kyrgyz Republic “ <i>On Public–Private Partnership</i> ” to identify, approve and monitor all contingent liabilities arising from any PPP agreement irrespective of the value of the PPP project; (ii) regulations to provide for adequate budget to meet any direct or		

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		<p>contingent liabilities should they materialize through the establishment of a Guarantee Fund or any other mechanism that meets the purpose of budgeting for direct and contingent liabilities arising from PPP; and</p> <p>(iii) annual reports on the aggregated amount of fiscal spending and future commitments in terms of direct and contingent liabilities arising from all awarded PPP</p>		

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		agreements and the related value for money.		
1.9 Five tenders for consulting services for preparing public–private partnership (PPP), of which 2 are gender and socially-oriented projects, including feasibility studies and tender documents, have been published, and 2 ongoing feasibility studies have, been completed and approved.	2.7 In accordance with the Law of Kyrgyz Republic “ <i>On Public–Private Partnership</i> ”, the Government approved: (i) methodological guidelines for assessing fiscal exposure for direct and contingent liabilities of PPP agreements; (ii) utilization of a fiscal exposure assessment tool that estimates direct and contingent liabilities for awarded PPP agreements; (iii) operational guidelines and model documents to develop	3.10 In order to improve the quality of the PPP pipeline, Government: (i) will allocate Som254 million through the Project Development Support Fund to at least 7 different PPP projects; and (ii) will award at least 4 PPP contracts that have been appraised and structured in line with international standards. <sup>f</sup>		

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	financially viable PPP projects in accordance with international good practice; <sup>g</sup> and (iv) certified at least 30 Government officials (of which at least 40% were women) in 2020 for Level 1 Foundation certification as per the PPP Certification Program by APMG International. <sup>h</sup>			
<b>Reform Area 4: Industry-linked skills development through enhanced internal efficiency and qualifications structure improved.</b>				
1.11 PCF has been introduced in the primary vocational education institutions (PVET) sub-sector to improve the strategic allocation of funds	2.8 In order to complete the transition from historical lump-sum budget allocations to annual performance-based budget allocations and ensure better alignment between the TVET curricula and the needs of the	3.11 Government: (i) will complete the roll-out of PCF in PVET, with PVET institutions spending not less than 95% of their approved	d. Percentage of firms that identify an inadequately educated workforce as a major constraint to business development declines to	<ul style="list-style-type: none"> <li>• MOES continuously implements PCF: (i) PVET institutions are spending not less than 95% of approved 2022 budget allocation, (ii) 100% incentive funds established, and (iii) PCF has been introduced in not less than 16 SVET institutions.</li> </ul>

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<p>to the sub-sector through:</p> <p>(i) Government approval of transition of PVET to PCF (i.e., money following the individual student and is occupation specific rather than lump-sum allocation per PVET institution); and</p> <p>(ii) Government approval of the creation of incentive funds in PVET institutions under PCF (allowing for flexible and performance-related remuneration of PVET staff and improved consumables and supplies).</p>	<p>labor market, the Government:</p> <p>(i) piloted PCF in at least 8 national Centers of Excellence (7 outside of Bishkek) and in secondary vocational education institutions (SVET);<sup>i</sup></p> <p>(ii) approved the methodology for Sectoral Qualifications Frameworks (SQF), which will match the TVET curricula with sectoral and industry needs; and</p> <p>(iii) approved an Action Plan for an NQS.</p>	<p>2020 budget allocation;</p> <p>(ii) evaluate the SVET PCF pilot program for further roll-out by MOES; and</p> <p>(iii) approve the National Qualification Framework (NQF) and implement not less than 95% of the actions of the NQS Action Plan.</p>	<p>30% by 2023 (2014 baseline: 33%). Sources: Data from surveys conducted post-program by MOES. AVE annual reports.</p>	<ul style="list-style-type: none"> <li>• MOES requires no less than 95% of PVET PCF covered by the national budget and PCF has become the standard financing method of PVET and respective budget approvals by MOF.</li> <li>• Government institutionalizes a coherent process of how occupational standards and labor market needs at large are mirrored into the TVET system, and are referenceable in an NQF.</li> <li>• The Parliament amends the Budget Code and Education Law to encourage entrepreneurial activities in all professional education institutions.</li> <li>• Government and the private sector operate a cofinanced SDF as an independent legal entity and with a public–private governance mechanism (no less than 30% of SDF beneficiaries should be female).</li> </ul>

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				<ul style="list-style-type: none"> <li>• Government allocates \$250,000 in the approved 2023 national budget to SDF or has introduced another sustainable financing mechanism such as a levy.</li> </ul>
1.11 Legislative foundation is provided for an NQS, including an NQF, to match qualifications' supply and demand sides.				
1.12 AVE has developed and approved Model Center (MC) guidelines and action plan that provides for MCs to be established in the form of legal entities (with due registration, articles of association, and bank accounts, with 20% of female teachers and staff) to	2.9 To promote industry-relevant work-based learning and entrepreneurial activities, the MOES issued a Ministerial Order to legally establish 8 additional model centers (MC), of which 7 are outside of the main urban center of Bishkek) with 20% of female teachers and staff, and at least 30% of women in decision making positions in MCs. <sup>j</sup>	3.12 Government will: (i) establish and operationalize 12 additional MCs (3 outside Bishkek) with 20% of female teachers and staff, and at least 30% of women in decision making positions; <sup>k</sup> and (ii) ensure 4 out of 8 additional MCs are fully		

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provide work-based learning opportunities and gradually carry out entrepreneurial activities to generate and retain income.		operational (with 20% of female teachers and staff, and at least 30% of women in decision making positions) in accordance with the approved MOES guidelines and action plan.		
	2.10 To promote pre-employment training and on-the-job upskilling, the Government legally established a SDF with an annual budget allocation of \$250,000 in 2021.	3.13 To continue promotion of pre-employment training and on-the-job upskilling, the Government approves a budget allocation of \$250,000 in 2022 for the SDF.		
<b>Reform Area 5: Fiscal and social protection resilience to enable post-COVID stabilization and recovery improved.<sup>1</sup></b>				
	2.11 To ensure all future emergency support is provided on-budget and to improve		e. Overall public debt level for Kyrgyz Republic reduced to	<ul style="list-style-type: none"> <li>MOF upgrades the functionalities in its public procurement information technology system and update its public</li> </ul>

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	<p>consolidated control, monitoring, recording and management reporting, the MOF approved an Order:</p> <p>(i) incorporating all financial assistance provided for COVID-19 into the consolidated report of the Treasury Management Information System; and</p> <p>(ii) requiring mandatory completion of ex-post audits of COVID-19 emergency funds and disclosing the results on the MOF's website.</p>		<p>60% of GDP target ceiling by 2024 (2020 baseline: 69% of GDP). Source: International Monetary Fund Article IV Staff Reports. MOF annual national budget documents and reports.</p> <p>f. MLSD list of vulnerable households includes sex and age-disaggregated data and number of households by 2023 (2020 baseline: disaggregated data not available). Source: MLSD progress reports. ADB</p>	<p>procurement portal to improve its e-procurement system.</p> <ul style="list-style-type: none"> <li>To improve its revenue forecasting capacity, Government: (i) upgrades its revenue forecasting information technology system; and (ii) introduces a fiscal management model that allows MOF to simulate the impact of Government's fiscal policy decisions on the overall debt position.</li> <li>Government will develop and install a new debt management information technology system that will allow the Public Debt Department to, amongst other things, (i) securely record and maintain all debt-related transactions such as commitments, disbursements and debt service payments; (ii) produce payment projections of principal, interest, and other fees; and (iii) generate reports at</li> </ul>

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			COVID-19 crises support monitoring and evaluation reports.	<p>individual instrument and portfolio levels.</p> <ul style="list-style-type: none"> <li>• Government will adopt a fiscal plan to reduce tax exemptions, energy sector subsidies, and the wage bill as shares of the national budget.</li> <li>• Government approves a new <i>Public Investment Management Assessment</i> and develops a Public Investment Management Strategy to enable efficient public investment planning, comprehensive, unified and targeted resource allocation, and timely and cost-effective implementation.</li> <li>• Government approves the next <i>Strategy for Public Debt Management, 2023–2025</i>.</li> <li>• Government introduces the universal infant benefit as part of state benefit reform by establishing a three-component state benefit for families with children,</li> </ul>

Prior Actions: Subprogram 1 (Completed: August 2018–July 2019)	Prior Actions: Subprogram 2 (Completed: August 2019–March 2021)	Policy Actions: Subprogram 3 (April 2021–June 2022)	Outcome Indicators	Post-Program Engagement Framework (2022–2023)
				incorporating universal grants for newborns and infants and a poverty-targeted grant for older children.
	2.12 In order to deepen the domestic debt market, improve the enabling environment for public debt management, and ensure COVID-19 emergency response support is within prudent debt limits, the Government approved a new <i>Strategy for Public Debt Management for 2020–2023</i> and commenced implementation through: (i) issuance of an Order mandating the periodic preparation and approval <i>Medium-Term</i>	3.14 In order to significantly improve fiscal accountability and transparency, the Ministry of Finance publishes on its website the <i>Strategy for Public Debt Management, 2020–2023</i> and introduces legal amendments to the Law on the Budget and the Budget Code to enable mandatory annual publishing of: (i) the government's annual borrowing plans and fiscal risk statement as		

Prior Actions: Subprogram 1 (Completed: August 2018–July 2019)	Prior Actions: Subprogram 2 (Completed: August 2019–March 2021)	Policy Actions: Subprogram 3 (April 2021–June 2022)	Outcome Indicators	Post-Program Engagement Framework (2022–2023)
	<p><i>Debt Strategy</i> and its annual review;</p> <p>(ii) adoption of medium-term indicators to reduce the fiscal deficit to 3.0% of GDP by 2022, and overall public debt to 60% of GDP by 2022;<sup>m</sup> and</p> <p>(iii) adoption of a medium-term domestic debt target of 16% of GDP by 2024 in order to start reducing vulnerability of the general government to exchange rate risks.<sup>n</sup></p>	<p>reflected in the budget; and</p> <p>(ii) the annual list of borrowings of the seven largest SOEs and ensure that their IFRS-based annual audited financial statements and the accompanying notes are publicly disclosed.<sup>o</sup></p>		
	2.13 To eliminate the current financial fragility and enhance the Government's ability to rapidly respond to			

Prior Actions: Subprogram 1 (Completed: August 2018–July 2019)	Prior Actions: Subprogram 2 (Completed: August 2019–March 2021)	Policy Actions: Subprogram 3 (April 2021–June 2022)	Outcome Indicators	Post-Program Engagement Framework (2022–2023)
	<p>exogenous shocks in the future, the MOF:</p> <p>(i) approved the <i>Medium-Term Action Plan for Development of Public Finance Management, 2020–2022</i> to chart key emerging reform objectives in budget planning, medium-term budget forecasting, public procurement, improving accounting and reporting standards, and improving internal audit and control procedures; and</p> <p>(ii) established a fiscal buffer, known as the State Budget Reserve, within the level of 1.0%</p>			

Prior Actions: Subprogram 1 (Completed: August 2018–July 2019)	Prior Actions: Subprogram 2 (Completed: August 2019–March 2021)	Policy Actions: Subprogram 3 (April 2021–June 2022)	Outcome Indicators	Post-Program Engagement Framework (2022–2023)
	of total budget expenditure, and fully funded it in the 2020 national budget.			
	2.14 To strengthen public financial management and ensure fiscal headroom for coping with unanticipated shocks, Cabinet submitted to Parliament fiscal rules to remove Government discretion to change the annual debt ceiling and to embed a rules-based fiscal framework for determining the debt ceiling and, amongst other things, corrective measures to be taken and sanctions to be applied if the debt ceiling is breached, and	3.15 To help strengthen fiscal sustainability, the Government will prepare and publish a detailed annual fiscal risk assessment.		

Prior Actions: Subprogram 1 (Completed: August 2018–July 2019)	Prior Actions: Subprogram 2 (Completed: August 2019–March 2021)	Policy Actions: Subprogram 3 (April 2021–June 2022)	Outcome Indicators	Post-Program Engagement Framework (2022–2023)
	special circumstances in which the debt ceiling may be breached and the path of fiscal adjustment to be followed afterward.			
	2.15 To establish a new targeting framework for social protection of vulnerable groups, and immediate integration of the unemployed due to the COVID-19 pandemic, and the victims of domestic violence, the Government approved: (i) updating of the MLSD social protection database to include data disaggregated by sex, age and region;	3.16 Government will amend the eligibility criteria and reconfigure business processes of the Monthly Benefit for Poor Families with Children (MBPFC), Uiy-Bologo Komok (UBK) and unemployment benefits to increase coverage of social protection and ensure high uptake rates by newly vulnerable groups in the informal urban and disadvantaged rural households. The data on beneficiaries will		

Prior Actions: Subprogram 1 (Completed: August 2018–July 2019)	Prior Actions: Subprogram 2 (Completed: August 2019–March 2021)	Policy Actions: Subprogram 3 (April 2021–June 2022)	Outcome Indicators	Post-Program Engagement Framework (2022–2023)
	(ii) introduction of a national hotline and website for self-registration; and  (iii) rapid validation of the registered candidates.	be centralized and disaggregated by sex.		
		3.17 Government will formulate a legislative framework for the provision of social services according to a guaranteed minimum level of services for specified vulnerable groups to reinforce their protection and sustainably extend it.		

**Budget Support****Subprogram 1:**

ADB: \$50 million (ADF grant)

**Subprogram 2:**

ADB: \$80 million (Concessional OCR and ADF grant)

**Subprogram 3:**

ADB: \$50 million (Concessional OCR and ADF grant)

**Technical Assistance:**

ADB: \$1.5 million (TASF-6)

ADB = Asian Development Bank, ADF = Asian Development Fund, AVE = Agency for Vocational Education, COVID-19 = coronavirus disease, CP3P = APMG Certified Public-Private Partnership Professional Program, EA = executing agency, EU = European Union, GDP = gross domestic product, GSP+ = Generalised System of Preferences Plus, IFRS = international financial reporting standards, IMF = International Monetary Fund, MLSD = Ministry of Labor and Social Development, MOE = Ministry of Economy, MOES = Ministry of Education and Science, MOF = Ministry of Finance, NA = not applicable, NBKR = National Bank of the Kyrgyz Republic, NQF = national qualifications framework, NQS = national qualifications system, OCR = ordinary capital resources, OJSC = Open Joint Stock Company, PCF = per capita financing, PFM = public financial management, PPP = public-private partnership, PVET = primary vocational and technical education, REX = Registration of Export System, SDF = skills development fund, SME = small and medium-sized enterprise, SOE = state-owned enterprises, SVET = secondary vocational and technical education, TASF = Technical Assistance Special Fund.

<sup>a</sup> Government of the Kyrgyz Republic. 2018. National Development Strategy of the Kyrgyz Republic for 2018–2040. Bishkek.

<sup>b</sup> Zero is the baseline, that is, there were no exporters to the EU registered in REX prior to this action being implemented. 80% of exporters to the EU being registered was assessed to be an ambitious but achievable target.

<sup>c</sup> Around 30% of total bank lending is to women-headed SMES.

<sup>d</sup> Already the government has enrolled some 35 public officials in the APMG CP3P program which is internationally recognized as the standard for PPP capacity building. To continue the necessary capacity building and ensure that at least all officials of the Center for PPP have been trained in the principles of PPP, the government needs to ensure enrollment of 50 officials and successful conclusion of Level 1 in the APMG CP3P program.

<sup>e</sup> To achieve a gender-responsive institutional framework the following measures can be considered: (i) ensuring representation of men and women in institutions and teams involved in ppp process; (ii) providing specific gender training to all relevant government officials involved in the ppp process; and (iii) capacity building measures, such as training, awareness raising or advisory services for the private sector (including women-headed local companies).

<sup>f</sup> International experience has demonstrated that countries of similar size and income level as Kyrgyz Republic can comfortably accommodate up to 4 PPP contracts in a 12-month period.

<sup>g</sup> Guiding materials for the identification, preparation and tender processes for PPP projects in the Kyrgyz Republic in accordance with PPP legislation, including the Law of the Kyrgyz Republic "On Public-Private Partnership" adopted in 2019. The Guidelines contain samples and examples of documents, methodological approaches and instructions required for various stages of preparation and implementation of PPP projects. This will also involve: (i) analysis of gender aspects during the preparation and appraisal stage, e.g. by collecting sex-disaggregated data, including women and men at an early stage in the consultations, and by incorporating gender aspects into the various analyses and assessments; (ii) translation of the analysis and assessment results into the design of projects and programs, e.g. by designing gender-responsive policies, bidding documents and contracts; and (iii) utilizing meaningful performance indicators to monitor and evaluate actions designed to narrow gender gaps.

<sup>h</sup> Already the government has enrolled some 35 public officials in the APMG CP3P program which is internationally recognized as the standard for PPP capacity building. To continue the necessary capacity building and ensure that at least all officials of the Center for PPP have been trained in the principles of PPP, the government needs to ensure enrollment of 50 officials and successful conclusion of Level 1 in the APMG CP3P program.

<sup>i</sup> The targeting was chosen by the Government to promote rural and inclusive development and with regards to establishing MCs which were most likely to successfully establish entrepreneurial activities and work-based learning.

- <sup>j</sup> Gender segregation in education continues in the labor market, where women dominate in often lower-paid sectors. Measures such as quotas for teaching, staff and senior management positions in the MCs reserved for women will help ensure gender empowerment is mainstreamed into formal government policy and operations.
- <sup>k</sup> The targeting was chosen by the Government in alignment with the Kyrgyz Republic's regional development policy 2018–2022, which indicates that each region/oblast should focus on certain key economic sectors it has been developing. In alignment with regional development policy and depending on existing SVET institutions in the country, their development potential and actual enrolment, competence and profiles, 8 SVET institutions were competitively selected throughout the country which are being developed into Centers of Excellence.
- <sup>l</sup> Three policy actions have been developed and agreed with the government as part of the implementation of the World Bank's International Development Association (IDA) Sustainable Development Finance Policy (SDFP) to which ADB will be aligned during the ADF13 period. The objective of the SDFP will be to incentivize countries to borrow sustainably and promote coordination between IDA and other creditors in support of countries' efforts. The relevant policy actions are PA 3.14 and PA 3.15.
- <sup>m</sup> In 2020, the fiscal deficit was estimated to be 8.8% of GDP and overall public debt 69% of GDP.
- <sup>n</sup> In 2020, domestic debt was estimated to be 9.8% of GDP.
- <sup>o</sup> The seven largest state-owned enterprises in the Kyrgyz Republic are: (1) OJSC Kyrgyzalтын; (2) OJSC Severelectro; (3) OJSC Electric Power Plans; (4) OJSC National Electrical Grid of Kyrgyzstan; (5) JSC Oshelectro; (6) OJSC Manas International Airport; and (7) OJSC Bishkekteploset.

**Contribution to Strategy 2030 Operational Priorities:** Operational priority indicators to which this operation will contribute results are detailed in Contribution to Strategy 2030 Operational Priorities (accessible from the list of linked documents in Appendix 2).

Source: Asian Development Bank.

## LIST OF LINKED DOCUMENTS

<http://www.adb.org/documents/rpps/?id=52225-003-3>

1. Loan Agreement
2. Grant Agreement
3. Sector Assessment (Summary): Trade and Investment Competitiveness
4. Contribution to Strategy 2030 Operational Priorities
5. Development Coordination
6. International Monetary Fund Assessment Letter
7. Summary Poverty Reduction and Social Strategy
8. Program Impact Assessment
9. Risk Assessment and Risk Management Plan
10. List of Ineligible Items
11. Safeguards Assessment Matrix
12. Management-Approved Concept Paper: Proposed Programmatic Approach, Policy-Based Grant for Subprogram 1, and Technical Assistance Grant for Kyrgyz Republic: Promoting Economic Diversification Program
13. Approved Report and Recommendation of the President to the Board of Directors: Proposed Programmatic Approach and Policy-Based Grant for Subprogram 1 Promoting Economic Diversification Program

## Supplementary Documents

14. Sector Assessment (Summary): Agriculture, Natural Resources, and Rural Development
15. Sector Assessment (Summary): Finance, and Industry and Trade—Small and Medium Enterprise Development
16. Sector Assessment (Summary): Private Sector Development—Public–Private Partnership Development
17. Sector Assessment (Summary): Skills Development—Technical and Vocational Education and Training
18. Sector Assessment (Summary): Public Sector Management—Public Expenditure and Fiscal Management
19. Sector Assessment (Summary): Public Sector Management—Social Protection Initiatives
20. Comparison of Original and Revised Reforms under Subprogram 2

## DEVELOPMENT POLICY LETTER

**КЫРГЫЗ  
РЕСПУБЛИКАСЫНЫН  
ВИЦЕ-ПРЕМЬЕР-  
МИНИСТРИ**



**ВИЦЕ-ПРЕМЬЕР-  
МИНИСТР  
КЫРГЫЗСКОЙ  
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## DEVELOPMENT POLICY LETTER

**Masatsugu Asakawa,  
President  
Asian Development Bank  
Manila, Philippines**

**Dear President Asakawa,**

**Subject: Promoting Economic Diversification Program, Subprogram 2**

On behalf of the Government of the Kyrgyz Republic, let me express our gratitude to the Asian Development Bank (ADB) for being a longstanding friend and trusted partner and for your continued support economic diversification reform, especially in these very challenging times. The outbreak of the coronavirus disease (COVID-19) pandemic has had a significant health, social and economic impact and, as we did with the difficulties in 2010 and 2020, we look to ADB to help us overcome it.

I am taking this opportunity to brief you on the current macroeconomic situation, as well as Government's efforts to address binding constraints to broad-based, inclusive and sustained economic development in 2021 in order to build a more resilient economy for the future. Although we recognize that it is urgent for economic policy to focus on stabilizing the current crises, the government also recognizes that keeping on track efforts to diversify its economy must remain its crucial reform priority.

The pandemic has added another layer of difficulty to the government's efforts to achieve economic diversification. Real GDP growth increased to 4.5% in 2019 due to a pickup of both gold and non-gold output. The output gap was closed but both headline and core inflation remained well below the inflation target range (5–7%). The current account deficit narrowed to 9.3% of GDP in 2019 (compared to 12.3% in 2018), driven by both higher gold exports and lower imports. Gross official reserves stabilized at 3.9 months of imports of goods and services, reflecting the net impact of purchases of locally produced gold offset partly by foreign exchange sales. The budget deficit decreased to 0.1% of GDP in 2019, and, as a result, public debt decreased to 54% of GDP. The widespread loss of income and jobs and rapid

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increase in poverty and income inequality resulting from efforts to contain the COVID-19 pandemic has heightened the need to accelerate efforts to diversify the economy and make it more resilient to shocks in the future. Our small and medium-sized enterprises (SMEs), for example, many of which were able to create jobs without any substantial support from the budget, face enormous difficulties to keep operating and economic activity has decreased by 80%. There is also an increasing trend of internal migration into rural areas, which is placing significant pressure on public services. Furthermore, since the social protection system does not cover informal workers and a considerable part of the unemployed, many more citizens are falling into poverty.

While the government's immediate priorities have been minimizing the spread of the contagion, responding to its socio-economic consequences has become more urgent—the economy contracted by 8.3% in 2020. Average inflation accelerated to 7.0% in 2020 following border closures and resulting food supply chain disruptions alongside the depreciation of the Kyrgyz som. The current account deficit widened from 7.7% in 2019 to 13.1% in 2020 due to declining trade, in particular, non-gold exports and imports that were affected by falling demand and border closures. Remittances declined by 25% in 2020 reflecting the large number of returning migrant workers and the depreciation of the Russian ruble. The fiscal deficit widened from 0.1% in 2019 to around 8.8% of GDP in 2020 with increased public expenditure to contain the pandemic and declining tax revenue due to lower economic activity and weak consumer demand. Although an economic rebound of 5.0% is forecast for 2021, we agree with the International Monetary Fund (IMF) and ADB that the downside risks are significant. If the outbreak worsens due to new strains of COVID-19 and inadequate vaccination efforts and border closures are prolonged, growth could slow down further in 2021. A budget deficit of 1.3% of GDP (or \$100 million) is projected for 2021, however, we will need to monitor our fiscal performance carefully over the next few months and make adjustments if necessary. The recently completed IMF Article IV consultations should also help us get a better grip of the fiscal position.

Economic diversification will continue to be front and center of our macroeconomic policy agenda as outlined in the *National Development Strategy of the Kyrgyz Republic for 2018-2040* (NDS 2040) and the Government's "*Realistic Goals, New Perspectives*" *National Development Program*. We understand that achieving complete economic diversification will be a gradual process and that, in the short-term, our development will continue to rely on gold and remittances. However, we believe in our strong partnership with ADB, which since 2008 has helped to produce significant improvements in the policy, legal and institutional environment for trade and investment competitiveness, SME development, financial sector development, business regulation public-private partnerships (PPP) development and industry-linked skills development. This is why even though it is urgent for macroeconomic policy to focus on stabilizing the current COVID-19 related health, macroeconomic, and social crises, we have learnt from previous

shocks the importance of keeping on track efforts to diversify the economy and recognize that it must remain a crucial reform priority.

Subprogram 2 of the Promoting Economic Diversification Program (PEDP) is helping to sustain economic diversification reform efforts. Reforms under this subprogram can be summarized as follows.

- (i) in order to improve trade and investment competitiveness, we adopted several reform measures to unlock production and supply chains beginning with the Resolution of the *"8th Financing of Agriculture Program"* to provide preferential credits for agricultural producers to accelerate animal husbandry, crop production, processing of agricultural products, and implementation of spring farm work in 2020. This will help change the focus of agricultural policy priorities towards increased agricultural production and food security;
- (ii) in order to improve SME development, we executed the 14 billion Kyrgyz som *"Financing of Business Entities Program"* in 2020 and provided a direct credit line to all SMEs, of which 33% were women-headed SMEs. We increased risk pricing efficiency and transparency in credit markets through the full operationalization of an integrated online credit history and scoring system for banks and financial institutions. We increased the use of non-productive agricultural land for, inter alia, collateralization in external finance by submitting the Government Resolution *"On the opinion of the Government of the Kyrgyz Republic on the draft Law of the Kyrgyz Republic On amendments to certain legislative acts of the Kyrgyz Republic on investment support"* to Parliament. The National Bank of Kyrgyz Republic (NBKR) issued requirements for regulatory reporting of guarantee funds on issued guarantees by all financial institutions for women-headed SMEs. They issued regulations for financial institutions to report on guarantees issued to SME's that are women-headed, which will help stabilize collateral requirements, particularly where real estate is used. The Board of the Open Joint Stock Company (OJSC) Guarantee Fund directed that 30% of the loans guaranteed be reserved for women-headed SMEs. Finally, to reduce barriers to entry in markets and tax compliance that give birth to rent-seeking and additional informal costs to regulatory compliance, Government (i) submitted the draft Law of the Kyrgyz Republic *"On State Registration of Legal Entities, Branches (Representative Offices)"* to Parliament, allowing submission of registration documents in electronic form and automation of legal entity registration processes, and (ii) adopted the Resolution *"Amendments to some decisions of the Government of Kyrgyz Republic"* to ease and improve tax administration and reduce compliance costs to the private sector, enabling consolidated reporting of income tax and social insurance contributions;
- (iii) in order to improve PPP development, we increased the budget allocation for the Center for Public-Private Partnership from 7.0 million Kyrgyz som in 2019 to 11.1 million Kyrgyz som in 2020 to allow

recruitment of PPP experts. This is crucial to establish key legal and financial expertise in Government, and in turn, allow the Centre to be more effective in the further development of PPPs. MOE submitted to Cabinet a draft decree for a 5-year strategic framework for PPP development in Kyrgyz Republic called *PPP Development Program 2021–2026*, which sets standards and principles for project development and support and to strengthen fiscal risk management. In accordance with the Law of Kyrgyz Republic “*On Public-Private Partnership*”, the Government approved (i) methodological guidelines for assessing fiscal exposure for direct and contingent liabilities of PPP agreements, (ii) utilization of a fiscal exposure assessment tool that estimates direct and contingent liabilities for awarded PPP agreements, (iii) operational guidelines and model documents to develop financially viable PPP projects in accordance with international good practice; and (iv) certified at least 30 Government officials (of which at least 40% were women) in 2020 for Level 1 of the PPP Certification Program by APMG International as part of a comprehensive capacity development plan);

- (iv) in order to complete the transition from historical lump-sum budget allocations to annual performance-based budget allocations and ensure better alignment between the technical and vocational education (TVET) curricula and the needs of the labor market, we: (i) piloted per capital financing in 8 national Centers of Excellence in secondary vocational education institutions (SVET), (ii) approved the methodology for Sectoral Qualifications Frameworks (SQF), which will match the TVET curricula with sector-and industry-needs, and (iii) approved an Action Plan for a National Qualifications System (NQS). In addition, the Ministry of Education and Science (MOES) legally established and made operational 4 model centers (MCs) in the form of independent entities with 20% of teacher and staff positions filled by women and issued a Ministerial Order to legally establish 8 additional MCs (7 that will be located outside the main urban center of Bishkek) with 20% of female teachers and staff, and at least 30% of women in decision making positions in MCs. To promote pre-employment training and on-the-job upskilling, the government established a *Skills Development Fund* (SDF) with an agreed budget allocation of \$250,000 for 2021; and
- (v) finally, under reforms to improve fiscal and social protection resilience to enable post-COVID stabilization and recovery to ensure all future emergency support is provided on-budget and to improve consolidated control, monitoring, recording and management reporting, MOF approved an Order to report on all expenses related to COVID-19 (incorporating all financial assistance provided for COVID-19 into the consolidated report of the TMIS and mandatory completion of ex-post audits and disclosure of the results on MOF’s website). The government approved a new *Strategy for Public Debt Management, 2020–2023* setting targets to deepen the domestic debt market, improve public debt management and ensure COVID-19 emergency response support remains within prudent debt limits. To further

enhance Government's ability to rapidly respond to shocks in the future, MOF (i) approved the *Medium-Term Action Plan for Development of Public Finance Management, 2020-2022* to chart key emerging reform objectives in budget planning, medium-term budget forecasting, public procurement, improving accounting and reporting standards, and improving internal audit and control procedures, and (ii) established a fiscal buffer, known as the State Budget Reserve, within the level of 1.0% of total budget expenditure, and fully funded it in the 2020 national budget. Finally, Cabinet submitted to Parliament fiscal rules to remove Government discretion to change the annual debt ceiling, to embed a rules-based fiscal framework for determining the debt ceiling and, amongst other things, determine corrective measures and sanctions to be applied if the debt ceiling is breached (defining special circumstances in which the debt ceiling may be breached and the path of fiscal adjustment). Recognizing that it would need to accommodate increasing pressure on its social protection program, the government established a "single window" (that is, a national hotline and informational portal) for citizens that need social protection due to the COVID-19 pandemic. This single window enabled vulnerable groups, especially those that have been greatly affected by the pandemic such as the recently unemployed and poor families that have lost their main source of income, and victims of domestic violence, to request social assistance through the hotline. The government also improved the MLSD database structure and data collection by imposing sex, age, and regional-disaggregated information collection of social protection beneficiaries when they apply for assistance (allocating resources for rapid validation).

As you can see, we have been able to accomplish many high impact reforms in spite of the ongoing crises. I therefore seek ADB's favorable consideration of our request to receive US\$69.3 million loan and \$10.7 million grant, totaling US\$80 million, under subprogram 2 of the PEDP. The policy design and monitoring framework, agreed between the Government and ADB (attached), is in line with the policy reforms contained in the NDS 2040 and it pleases me to confirm that we have accomplished all the policy actions in subprogram 2. I have also tasked senior officials from the Ministry of Economy and Finance to maintain a regular policy dialogue with ADB while stepping up efforts to implement policy reforms under subprogram 3 of the PEDP, which will be implemented between April 2021–March 2022.

I am confident that the Government's strong leadership and ownership of the reforms, supported by financial and technical assistance from ADB, will help us to sustain efforts to achieve inclusive, broad-based, and sustainable economic growth in the future.

We look forward to the prompt consideration and approval of subprogram 2 of the PEDP. Please extend my deep gratitude and appreciation to your management and staff for their hard work, dedication and help in these difficult times.

Sincerely Yours,



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**Ulukbek Karmyshakov,  
Governor ADB -  
Vice Prime Minister –  
Minister of Economy and Finance**