



Kyrgyz Republic

2007 JOINT COUNTRY PORTFOLIO REVIEW

IDB Portfolio

Background Paper

*Regional Office in Almaty
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I. INTRODUCTION

1. Islamic Development Bank (IDB) participated in the joint country portfolio reviews (JCPR) that were conducted by Asian Development Bank (ADB), KfW and the World Bank (WB) in November 2004 and March 2006. This year IDB will also join the portfolio review with ADB, KfW and the World Bank so that the common problems affecting the portfolios of the institutions could be taken up more effectively with the Government. The following issues will be taken up jointly with ADB, KfW and WB: donor coordination, counterpart funding, prioritization of public investment program (PIP), harmonization of procedures, taxation of donor projects etc. Project-specific issues will be taken up by respective financing institution separately with the Government.

2. The overall objective of the JCPR is to assess the performance of the country portfolio based on the analysis of key performance indicators using information gathered during the review of individual projects. The Mission will present its findings to the Government and agree on an action plan to mitigate the implementation hurdles to improve portfolio performance. In doing so, the JCPR will work jointly with the Government as required to:

- (i) review procedures and policies that cause implementation delays and underperformance, and
- (ii) identify the major generic and cross sector issues in project implementation.

II. OVERALL PORTFOLIO DESCRIPTION AND PERFORMANCE

A. Portfolio Description

1. Lending

3. **Size.** The Kyrgyz Republic became a member of IDB in November 1993. However, it already had started receiving assistance in 1992 under Special Assistance Operations (they will be discussed further in this report under Technical Assistance). As of 28 February 2007, the country's portfolio comprises 7 loans with a total amount of US\$ 60.91 million equivalent and 2 installment sale operations for the amount of US\$ 18.50 million. Of the total loan and installment sale¹ financing, five projects were completed, two were cancelled, and two are ongoing. IDB does not provide financing in a form of program loans. Ongoing loan have an un-disbursed balance of ID 1.688² million (equivalent of US\$ 2.4 million) as of 28 February 2007 (Taraz-Talas-Suusamyrd Road Project). This number can be further increased with the approval of Osh - Irkeshtam Road project and anticipated approval of 110-kv transmission line in mid 2007 up to ID 24.00 million (equivalent of US\$ 34.6 million). **Figures 1 and 2** show the volume of annual lending of IDB to the Kyrgyz Republic and the number of operations approved annually for the period 1994 to 2007. The list of approved lending operations by sector for the period 1994-2007 is provided in **Appendix 1**.

4. After a period of six years of no loan financing, the IDB has approved a US\$17.3 million loan for the reconstruction of Osh-Irkeshtam Road Project in February 2007. The non-activity of the IDB for the last 6 years was due to the understanding of current debt servicing and absorbing capacity problems that necessitated Government's policy of restrained borrowings as part of its debt reduction strategy. This strategy envisages a reduction in the size of

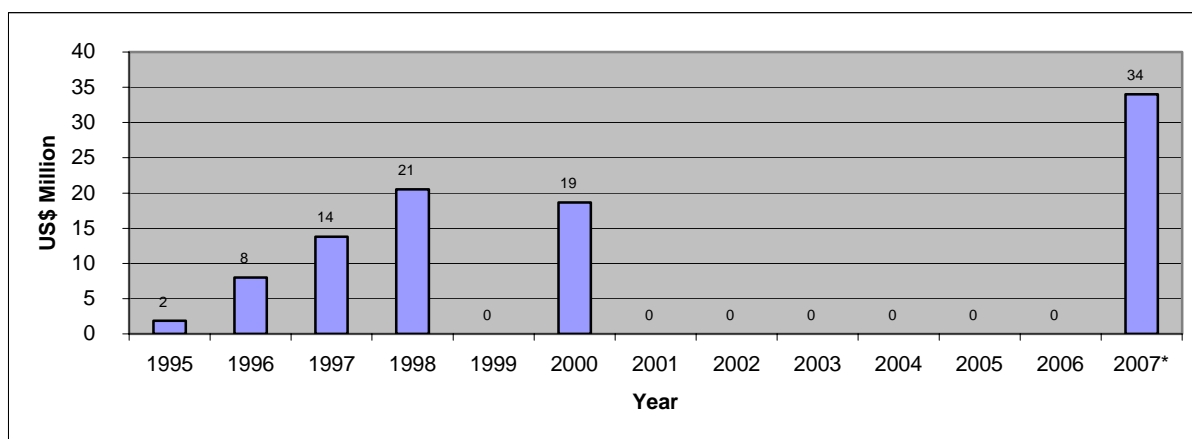
¹ *Loan* provides long-term financing for the implementation of development projects. Current size of loan is usually limited to ID 7.00 million per project. Loan bears administrative fee not exceeding 2.5 % p.a. Repayment is made in semi-annual installments over a period of 25 years including gestation period of 3 to 7 years. *Installment sale* is a medium-term mode of financing introduced by IDB in 1984. It calls for a contract between IDB and beneficiary for whom the Bank procures tangible assets and sells it at a mark-up allowing the beneficiary to make the payment on a deferred basis. Current size of IS is usually limited to ID 35.00 million per project. Current mark-up is fixed at 6% with a rebate of 15% for prompt repayment. Repayment is made in semi-annual installments over a period of 15 years including gestation period of up to 3 years

² *ID* = Islamic Dinar which equivalent to Special Drawing Right (SDR) of the IMF.

largely externally funded PIP from about 6% of GDP in 2001 to about 3% of GDP by 2005. IDB's annual lending level began with US\$ 1.88 million in 1995. It reached the peak level of US\$20.5 million in 1998. Since 1998, the IDB's financial assistance was in the form of concessional financing only. Other modes of financing, such as Installment Sale, Leasing, and Istisna³, cannot be applied to Kyrgyz Republic due to IMF conditionalities.

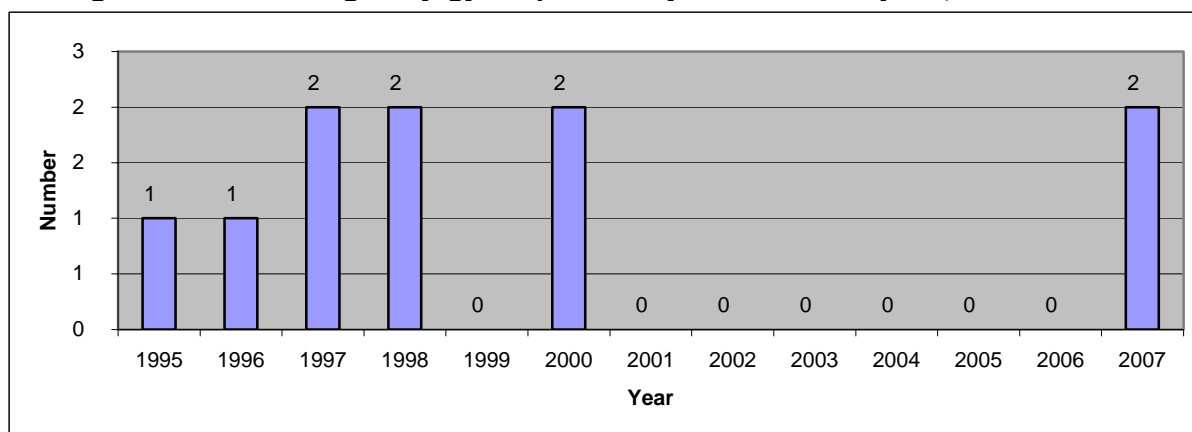
5. It is hoped that IDB lending program will reach about US\$34 million in 2007 which covers two projects, i.e. Osh-Irkeshtam Road and 110 kv Transmission Line projects. In accordance with MOU signed with the Government, for 2006-2008 a US\$ 51.40 million loan program was prepared. However, future lending levels could be further increased depending on the ability of the Government to borrow.

Figure 1. IDB Lending to Kyrgyz Republic – by Amount, 1995-2007⁴



* estimated

Figure 2. IDB Lending to Kyrgyz Republic – by Number of Projects, 1995-2007



6. **Composition.** *Appendix 1* provides the list of IDB projects approved from 1995-2007, while their sectoral composition is in *Figure 3*. The transport and communications sector continues to be the most important sector with a 58% share in IDB project portfolio. Four loans were provided to the transport and communications sector in the amount of US\$ 45.95 million for rehabilitating the strategically and economically important Bishkek-Osh road, Taraz-Talas-Suusamyр Road, Osh-Irkeshtam Road and expansion and upgrading of Osh Airport

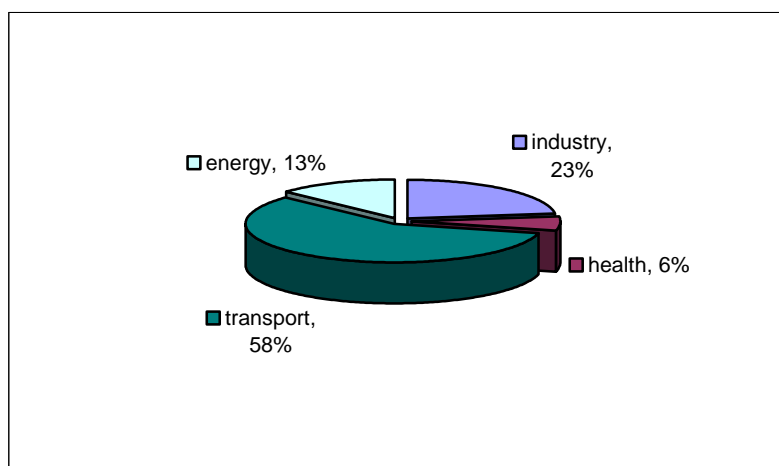
³ Leasing (ijara) is a medium-term mode of financing which refers to renting arrangements for the financing of capital equipment and other fixed assets to be leased for a fixed period of time against payment of fixed or floating semiannual rentals. Istisna is a contract whereby a party undertakes to produce a specific thing which is possible to be made according to certain agreed-upon specifications at a determined price and for a fixed delivery date. Current size of leasing and instisna financing is usually limited to ID 35.00 million per project. Current repayment period can go up to 15 years, and fixed mark up is at the level of 6% p.a. with availability of 15% rebate in case of prompt repayments.

⁴ As of 28 February 2007

(cancelled). Energy sector is expected to be the second largest sector with one approved project (220-kV transmission line) and one planned (110-kV transmission line) to be approved in 2007. Industry and mining is the third largest sector and includes two approved operations for Manufacture of distribution transformers and substations and Electroterm refrigerator (cancelled). Social infrastructure comprises education, health, water supply, and sanitation; however, it is only represented by two projects in health sector (Specialized maternity hospital and National cardiology center).

7. For promotion of private sector, IDB has established Islamic Corporation for the Development of Private Sector (ICD) to which Kyrgyz Republic is a member. One small operation amounting for US\$ 400,000 was approved in favor of Kyrgyz Company in 2004 under a US\$ 5.00 million credit facility extended to Small Enterprise Assistance Fund (SEAF). In 2006, ICD extended three credit lines to three commercial banks amounting to US\$ 4.00 million. Development of private sector remains one of the main priorities of the Bank's strategy in Kyrgyz Republic.

Figure 3. Sectoral Distribution of Lending by Amount (as of 28 February 2007)



**Table 1. Disbursements and Net Resource Transfers
1999-2006**

Year	Amount in US\$ Million		
	Lending Disbursement	Repayment	Net Transfer of Resources
	A	B	(A-B)
1999	5,0	0,2	4,8
2000	5,8	0,6	5,2
2001	4,4	0,5	3,9
2002	2,1	0,8	1,3
2003	4,7	1,3	3,4
2004	6,36	1,86	3,5
2005	1,7	2,11	-0,4
2006	4,41	2,85	1,56
2007	0,02	-	0,02

8. The disbursements in 2005 equaled ID 1.2 million (equivalent of US\$1.7 million), lower than total disbursements in 2004 by more than 70 %. As of 31 December 2006, the cumulative disbursement to the Kyrgyz Republic had reached ID 25.4 million (equivalent of US\$ 34.49 million), or about 80 % of the total lending approved (excluding cancellations and cancelled savings). As of the same date, the un-disbursed lending balance of ongoing operations amounts to ID 1.688 million (equivalent of US\$2.4 million), which is coming mainly from Taraz-Talas-Suusamyr Road project.

9. The net inflow of resources to the country falls modestly in the medium term for two reasons: the expiry of grace period of the loans taken before 1995, and a decline in the level of assistance from IDB during 2001-2006 which is expected to increase in medium-term.

2. Grant Assistance

10. **Size.** As of 28 February 2007, IDB provided 8 technical assistance (TA) projects amounting to US\$ 1,896 million and 4 Special Assistance (SA) projects amounting to US\$1,665 million. Therefore, total grant financing for the country equals to US\$3,561 million. Of these grant projects, 3 are project preparatory TAs amounting to US\$ 0.828 million, 5 TAs for US\$1.068 million are advisory TAs for capacity building, institutional strengthening and training. SA operations were provided for support of Islamic institutions (US\$ 0.325 million) and emergency assistance (US\$ 1.340 million)⁵. The list of all approved TAs by sector is provided in **Appendix 2**. Eight of the TAs and SAs projects were completed as of 31 December 2006.

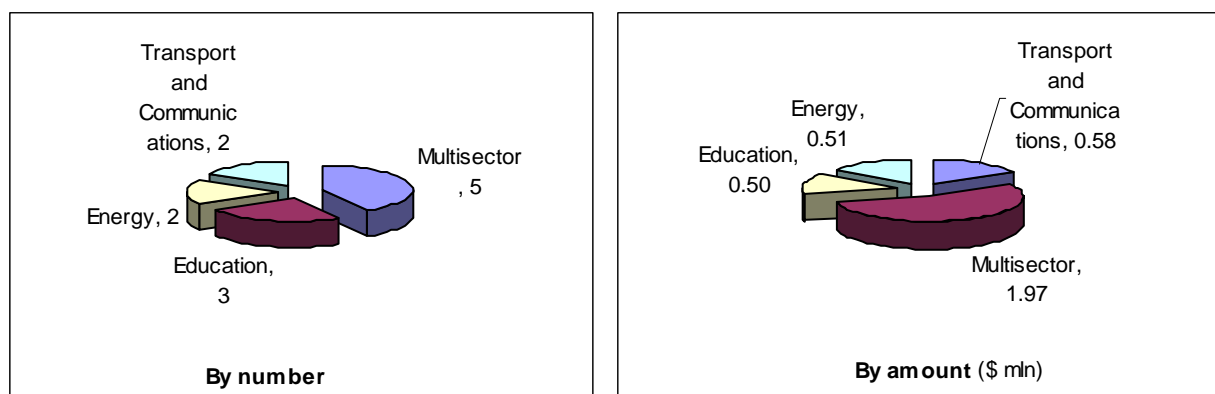
11. **Composition.** The sectoral composition of the approved grant portfolio is shown in **Figure 4** and **Table 2**. Multisector is the recipient of the largest amount of grant financing, US\$ 1.972 M (55%), including: Assistance to Earthquake Victims of Toktogul region for US\$ 1.140M, Capacity Building of Charitable Foundation of Maternity for US\$ 0.130M, Strengthening Capacity of Ministry of Economy and Finance and Introduction of Islamic Banking and Finance. Grants were provided for 2 TA projects for preparation of feasibility studies in transport sector, and for energy sectors, i.e. Improvement of Production Capacity of Transformers and Substations manufacturing plant and for Feasibility Study for Export of Power. Grants were also allocated for three education projects. Advisory TA was provided for OREMI JSC, Meerim Fund and State Property Committee to support policy reform and assist in project implementation through capacity building. IDB's advisory TAs provides high quality consultancy inputs, purchase of equipment and training to assist the Government's policy and institutional reforms.

**Table 2. Sectoral Distribution of Approved TAs by Amount and Number
(as of 28 February 2007)**

Sector	No. of		Amount	
	TAs	%	US\$ Million	%
Education	3	25	0.499	14
Energy	2	17	0.512	14
Transport & Communication	2	17	0.578	16
Multisector	5	41	1.972	56
Total	12	100	3.561	100.0

⁵ Financing in the form of Special Assistance is usually provided only to non-member countries of the Bank.

**Figure 4. Sectoral Distribution of TAs by Number and Amount
(as of 28 February 2007)**



B. Portfolio Performance

1. Lending

12. As of 28 February 2007, 1 lending project is under implementation with an un-disbursed amount of ID 1.688 million (equivalent of US\$ 2.4 million). A number of other indicators are used to assess portfolio performance such as time taken from loan approval to signing of financing agreement, for loan effectiveness from signing, etc. The time taken for approval to loan effectiveness for the ongoing Kyrgyz portfolio of 1 lending project was 34.6 months, and 29.8 months for loan signing after approval. In overall, average time from approval to signing, and from signing to effectiveness for all lending operations approved for Kyrgyz Republic (excluding cancellations) was 6.9 and 5.8 months, respectively. Disbursement performance continued to be poor and needs closer monitoring in 2007. It is hoped that action will be taken by the authorities to facilitate signing the loan agreement for Osh-Irkeshtam Road Project. The IDB has in fact approved the list of consulting companies to undertake detailed design and supervision of the project.

2. Grant Assistance

13. Of the total 12 approved TAs and SAs, eight are completed. Three of the active TAs are for the Ministry of Finance, State Property and Direct Investment and Introduction of Islamic Banking. One TA (Oremi Productive Capacity) was cancelled in 2006.

14. TA for Improvement of Production Capacity of OREMI Transformers and Substation Manufacturer. The management of the company changed hand several times. The status of the company was also not clear. In view of long delay the IDB cancelled the TA on the understanding that it is ready to provide another TA with revised scope of work.

15. TA for Capacity Building for State Property and Direct Investment Committee. In spite of the fact that the project was approved, signed and became effective in 2002, the implementation progress is very slow. The implementation schedule must be revised considering current delay and should be implemented accordingly. Further delay will lead to cancellation.

16. TA for Capacity Building of the International Charitable Foundation of MEERIM. The TA is completed. Project completion report was submitted in December 2006.

17. TA for Strengthening the Capacity of the Ministry of Economy and Finance. The project was approved in August 2005 and financing agreement was signed in November 2005 and currently the selection of consultants is in progress. Schedule of implementation should be prepared so that it will be implemented accordingly.

18. TA Introduction of Islamic Banking: Approved in December 2006. Agreement signed and EcoBank is the implementing agency. The TA is under active implementation.

3. Work program for 2007

19. Osh-Irkeshtam Road Rehabilitation Project (Loan). This Project includes rehabilitation of about 40 km section of the Osh-Sarytash-Irkeshtam road. The project was approved and presented to the Board of Executive Directors in February 2007.

20. 110-kV Transmission line (Loan). This project was appraised in 2004 and ready for submission to Board of Executive Directors. The Government of Kyrgyzstan confirms the readiness to proceed with this project. A re-appraisal mission is expected in February 2007.

21. TA (grant) for FS for Issy-kul ring road. The updated project documents were submitted to IDB Head Quarter for consideration and need to be followed up.

22. TA (grant) Investment Conference. The IDB in principle agreed to undertake Investment Conference in Bishkek in 2007.

III. PORTFOLIO PERFORMANCE AND MAJOR ISSUES

22. Considering a relatively small size of current IDB portfolio in the country, this section will be limited to a list of major issues concerning implementation of current portfolio of IDB operations approved for the Kyrgyz Republic. However, beginning 2007, the IDB is expected to enhance its activities in Kyrgyz Republic with the approval of two projects and several TA including holding of investment conference. The salient features of IDB operation in 2006 and the coming years are as following:

- (i) In 2006 the implementation of Taraz-Talas-Suusamyр Road was progressing very well and full completion is expected in 2007. This will coincide with government continuing to implement another road projects with the approval of Osh-Irkeshtam road project.
- (ii) Implementation of TA projects continued to be rather slow in 2006. One TA for OREMI was cancelled by the IDB in view of inability of the company's management to come up with concrete plan of action. The IDB is willing to consider a new TA with a new scope of work. TA for MEERIM NGO was completed in 2006. No progress is seeing in the TA for State Property and Direct Investment, while Capacity building for the Ministry of Finance is progressing reasonably well. TA Introduction of Islamic Banking in Kyrgyz will provide the opportunity for the authorities and the public the prospect for Islamic banking and finance industry in the country, thus gives alternate solutions to certain sectors of the economy.
- (iii) IDB work program until 2008 is attached hereto as **Appendix 3** and will be further discussed with the Government.
- (vi) In case of loans, PMUs report three problems: (i) difficulties in obtaining VAT exemption, (ii) ambiguity in the computation of Government co-financing which is usually provided in the form of tax exemption, and (iii) ambiguities in the procedure for taxation of consultants and contractors (local as well as foreign) hired under loan projects. JCPR will reiterate the issue of taxation of consultants/contractors with the Government and seek its assistance to put in place interim measures to mitigate the problem until MOF will develop procedure for taxation of the entities under investment projects funded by IFIs.
- (vii) Loan effectiveness is one of the major constraints. Effectiveness of one project was delayed for more than 4 years, and the Bank finally had to cancel the project.
- (viii) Portfolio disbursement performance could be improved if the Government could show

some flexibility in PIP spending, and expeditiously resolves the problem of taxation of project purchases.

- (ix) The Bank faced delays with implementation of approved TAs. Despite the fact that assistance was provided on a grant basis, delays were observed in all major project components, including selection of consultants, procurement of equipment, and training visits. One of the reasons brought to the attention of the Bank was high turnover of staff of executing agencies, lack of continuity and consequential lack of knowledge of IDB policies and procedures.

APPENDIX 1

LIST OF APPROVED PROJECTS

Mode	Code	Project name	Approved	Signed	Effective	Total cost (US\$M)	ID	US\$
Loan	KYR0014	Reconstruction of Taraz-Talas-Suusamyр road (under completion)	04.11.2000	27.04.2003	22.09.2003	10,954	7,000	9,150
Loan	KYR0013	Expansion and upgrading of Osh airport* (cancelled)	03.04.2000	15.05.2000	-	23,924	7,000	9,500
Loan	KYR0027	Reconstruction of Osh-Irkeshtam Road (under implementation)	25.02.07	-	-	19.8	14.00	17.3
IS	KYR0012	Electroterm refrigerator* (cancelled)	19.07.1998	-	-	16,180	7,800	10,500
Loan	KYR0010	Construction of Bishkek-Osh road (completed)	20.04.1998	22.10.1998	20.12.1998	12,700	7,300	10,000
Loan	KYR0009	National center of cardiology therapeutics and (completed)	19.10.1997	16.11.1997	01.02.1998	4,466	2,190	3,000
Loan	KYR0007	220 kv transmission line (completed)	06.07.1997	16.11.1997	01.02.1998	26,480	7,000	10,080
IS	KYR0006	Manufacture of distribution transformers and substations (completed)	28.01.1996	17.06.1996	01.03.1997	22,000	5,370	8,000
Loan	KYR0003	Specialized maternity hospital (completed)	23.01.1995	15.04.1995	20.11.1995	6,360	1,350	1,880
TOTAL APPROVED PROJECTS (incl. cancellations)			9	7	6	123,064	59.61	79.41

APPENDIX 2

LIST OF APPROVED GRANT PROJECTS

Mode	Code	Project name	Approved	Signed	Effective	Total cost (US\$M)	ID	US\$
TAG	KYR0021	CB. Introduction of Islamic Banking (under implementation)	08.01.07	09.01.07	09.01.07	0,285	0,170	0,255
TAG	KYR0019	CB for Meerim NGO (completed)	25.08.2003	03.09.2003	03-09.2003	0,174	0,100	0,130
TAG	KYR0017	CB for State Property and Direct Investment (under implementation)	11.08.2002	08.10.2002	08.10.2002	0,218	0,139	0,174
TAG	KYR0016	OREMI production capacity (cancelled)	05.10.2002	14.04.2003	14.04.2003	0,318	0,199	0,262
TAG	KYR0008	FS/DD for Taraz-Talas-Suusamyr road (completed)	21.09.1997	16.11.1997	16.11.1997	0,331	0,200	0,280
TAG	KYR0004	FS/TD for Bishkek-Torugart road (completed)	22.05.1995	29.11.1995	29.11.1995	0,341	0,200	0,298
TAG	KYR0002	FS for export of power (completed)	06.09.1993	03.11.1993	03.11.1993	0,285	0,180	0,250
TAG	KYR0020	Strengthening the capacity of the Ministry of Economy and Finance (under implementation)	10.08.2005	25.11.2005	25.11.2005	0,284	0,170	0,247
SAO	KYR0018	Urgent relief for flood victims (completed)	02.09.2003	02.09.2003	02.09.2003	0,200	0,146	0,200
SAO	KYR0011	Arabic script program (completed)	29.10.1991	01.02.1994	01,02.1994	0,020	0,016	0,020
SAO	KYR0001	Islamic institute and 4 Quranic schools (completed)	25.05.1992	15.05.1995	15.05.1995	0,305	0,219	0,305
SAO	KYR0001	Assistance to earthquake victims (completed)	09.11.1992	18.06.1993	18.06.1993	1,140	0,812	1,140
TOTAL APPROVALS (incl. cancellations)			12	12	12	3,332	2,551	3,561

APPENDIX 3**TENTATIVE WORK PROGRAM, 2007-2009****1428H (2006-2007)**

Osh-Irkeshtam Road (Loan)
110-kV Transmission line (Loan)
TA (grant) for FS for Issy-kul ring road
TA for Investment Conference

1429H 1 (2007-2008)

Taraz-Talas-Suusamyr road (phase 2) (Loan)
Microfinancing credit (Loan)
Global line of financing (IS/Leasing/Istisna)
TA (grant) for Capacity building of Ministry of Industry, Trade and Tourism

1430H (2008-2009)

Issy-kul ring road (Loan)
Health Sector Project (Loan)
TA (grant) for Capacity building of Kyrgyzpost