

**DOCUMENT OF THE EUROPEAN BANK
FOR RECONSTRUCTION AND DEVELOPMENT**

STRATEGY FOR THE KYRGYZ REPUBLIC

As approved by the Board of Directors at its Meeting on 25 February 2015

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EXECUTIVE SUMMARY

The Kyrgyz Republic is committed to the principles outlined in Article 1 of the Agreement Establishing the Bank and is making good progress towards implementation of the principles of multiparty democracy and pluralism through the introduction of a parliamentary system of government and election of a multiparty parliament. However, many challenges remain.

The country went through a period of political upheaval in 2010-2011, but has emerged with a more democratically-oriented political system. A parliamentary coalition was formed in early April 2014 and the new government is headed by a prime minister who has an established track record of supporting reforms in the country. The government has an ambitious agenda focusing in particular on fighting corruption and improving investment climate. A great deal has been achieved in recent years but the country is still confronted with a number of challenges in upholding the rule of law, respecting human rights and promoting inter-ethnic reconciliation.

GDP growth in the Kyrgyz Republic remains highly dependent on output of the Kumtor gold mine. Taking into account the impact of the current slowdown in Russia on remittances, and to a lesser degree on exports, as well as softer growth of gold mining after a significant increase in 2013, and the fragilities of the banking sector, GDP growth is expected to moderate to 4.5 per cent in 2014 and somewhat recover to 4.8 per cent in 2015. For the remainder of the strategy period, growth is likely to be around 5.0 – 5.5 per cent.

In the regional context, the Kyrgyz Republic remains heavily dependent on cooperation with neighbouring countries. Located at an important trade crossroads and being a transshipment point, the country both benefits from and depends on extensive trade flows and investment from China, Kazakhstan and Russia, as well as other partners. The Kyrgyz Republic seeks to join the Customs Union with Russia, Kazakhstan and Belarus in a process which is expected to be finalised by 2015. The accession represents both opportunities and risks for Kyrgyz Republic in terms of pace and direction of structural reforms.

Structural challenges remain significant in many sectors, especially with respect to establishing sound market-supporting institutions. In spite of some positive steps taken by the authorities, such as the establishment of the Business Development and Investment Council, where EBRD has been playing an active role, the business environment is still challenging. The mining and quarrying sector remains both a significant driver and potential downside risk for economic growth in the country, accounting for 10 per cent of GDP and 50 per cent of industrial output. Establishing a stable framework for Kumtor's operations remains one of the key challenges for the country and the outcome of the dispute between the government and Centerra, Kumtor's operator, will be determinant for the country's attractiveness to FDIs. The country's economy outside the extractive sector is dominated by small, family-run companies, whose growth is impeded by inadequate skills and management practices, weak operating models, and lack of access to finance, in addition to the constraining factor of a small domestic market. The Kyrgyz Republic needs to continue to improve the businesses' access to infrastructure and the population's access to basic municipal services. The Kyrgyz Republic is also a country of significant regional disparities, compounded by the often complex relations between the country's ethnic groups. In this context, the following strategic orientations are proposed to form the core of EBRD's engagement in the Kyrgyz Republic in the forthcoming strategy period:

- **Foster sustainable growth by strengthening regional cross-border linkages:** As a landlocked economy with a limited domestic market, the Kyrgyz Republic would benefit greatly from deeper regional integration, given its important energy export potential, as well as good regional trade and transit position. The country is engaged in several regional integration processes, which create opportunities in terms of export markets and potential inwards investments. In that context, the Bank will aim to help facilitate economic and trade cooperation and integration with the region, by supporting rehabilitation of critical infrastructure, strengthening the exporting sector including through access to finance and advisory, as well as supporting cross-border investments and regional cooperation projects.
- **Enable SMEs to scale-up and bolster competitiveness:** Outside the extractive sector, the economy is dominated by fragile, ‘cottage-industry’-type SMEs, with few mid-sized corporates in existence. While deeper regional trade links create opportunities for the best local firms both in terms of export markets and inward investment, stronger operating models and core competencies will be needed to better compete. The Bank will thus support competitiveness and sustainable growth of SMEs with viable business models through investment and advisory, promoting in particular skills transfer and operational efficiency improvements, and seek to strengthen the financial sector to facilitate access to finance for SMEs, in particular in local currency. The Bank will also step up its efforts of improving the business environment through policy dialogue.
- **Promote sustainability of public utilities through commercialisation and private sector participation:** Municipal and energy infrastructure has suffered from years of underinvestment, deficient regulatory environment, and weak core competencies. Most public utilities and power companies have poor financial and operational performance. The power sector is unbundled but remains state owned. Only a few small hydro power plants are private. Below cost tariffs, high losses, obsolete fixed assets, lack of meters and independent regulator make this sector unattractive for the private sector. Water and wastewater services are under municipal control and are operated inefficiently, in particular in smaller cities. To address those issues, the Bank will continue to support municipal utilities, where it has a recognized expertise and delivery model in improving operators’ financial condition, operating practices and governance, and seek to support sustainability of power sector by rehabilitating assets and developing a more attractive institutional framework for private investment.

In addition, the Bank will seek to support through the above priorities the reduction of regional economic disparities, by increasing its outreach to less developed rural areas, in particular in the southern regions, and addressing inclusion gaps in relation to gender and youth across sectors.

Achieving those objectives will require close coordination with other IFIs active in the Kyrgyz Republic and an increase in donor funding, to support investments, SME advisory services and business environment improvement initiatives. To support reforms and transition, the Bank will also enhance its policy advice activities, including developing wider sector policies, in close consultation with key donors.

1 OVERVIEW OF THE BANK'S ACTIVITIES TO DATE

1.1 The Bank's current portfolio

Private Sector ratio: 77%, as of 31 December 2014

Sector	Portfolio				
	Number of projects	Portfolio	% of Portfolio	Operating Assets	% of Operating Assets
Energy	1	123	47%	63	38%
Natural Resources	1	123	47%	63	38%
Power and Energy	0	-	0%	0	0%
Financial Institutions	24	41	16%	33	20%
Depository Credit (banks)	16	31	12%	24	15%
Non-depository Credit (non-bank)	8	10.0	4%	9	5%
ICA	18	36	14%	35	22%
Agribusiness	8	12	5%	12	7%
Equity Funds	1	1	0%	0	0%
ICT ¹	0	-	0%	0	0%
Manufacturing & Services	5	19	7%	19	11%
Property & Tourism	4	4	2%	4	3%
Infrastructure	11	62	23%	33	20%
MEI ²	10	36	14%	10	6%
Transport	1	26	10%	23	14%
TOTAL	54	262	100%	164	100%

Source: EBRD Business Performance Navigator

1.2 Implementation of the previous strategy

In the previous strategy period, the Bank's main priorities in the Kyrgyz Republic were to support the development of local private enterprises, stabilize and develop the financial sector, strengthen critical infrastructure and conduct policy dialogue focused around improving investment climate, promoting energy efficiency, supporting financial system stability and developing local currency and local capital market.

The EBRD has strongly responded to the 2010 crisis in close partnership with key donors and Multilateral Development Banks (MDBs) and managed to significantly increase and accelerate financing and technical assistance across all sectors to support the country's economic and political recovery. In the course of the last strategy period, the Bank signed 56 projects for a total value of €207 million. In the private sector, the majority of the projects were with local SMEs, where the Bank supported 13 clients in the agribusiness, manufacturing, wholesale and retail, hotel management, fuel supply and logistics sectors. All beneficiary companies introduced annual audit of accounts, whenever appropriate simplification of shareholding structure and corporate governance improvements were agreed to improve transparency and efficiency. In addition to financing, the Bank continued offering business advice to SMEs with particular focus on management skills, information communication technology and export promotion. Clients demonstrated a 43% increase in net income and those export oriented reported a 150% increase in exports within a year of the

¹ Information and Communication Technology

² Municipal and Environmental Infrastructure

project. Integration of both teams in the same office helped to further increase the synergy providing business advice and financing to private companies as well as promoting new products, projects, including policy dialogue initiatives, and marketing the EBRD services.

In the larger corporate segment the Bank continued providing financial support to the Canadian mining company Centerra in operating Kumtor, the largest gold mine in The Kyrgyz Republic representing 5.5% of GDP, and float glass producer Interglass in refurbishing and re-launching its production. As both companies faced challenges, the Bank's support was of particular importance. Acknowledging the high importance of the mining sector for the economy and investment attractiveness of the country, as well as the significant challenges in the sector, the Bank initiated support to capacity building of the State Agency for Geology and Natural Resources to facilitate implementation of legal and regulatory reforms.

In the infrastructure sector, the Bank has developed a good portfolio and pipeline of municipal infrastructure and transport projects, covering water, waste water and solid waste management and public transport, with a special focus on the south of the country, as part of the 2010 post-crisis response. Given the country's debt constraints and IMF requirements towards concessionality of external borrowings, as well as affordability issues, the EBRD mobilised substantial capital grants from its own funds, from the Swiss Government, as well as from the EU through Investment Facility for Central Asia (IFCA) and Global Environmental Fund (GEF), in order to supply blended financing packages supported by technical assistance for project preparation and clients' capacity building. This financing and delivery model coupled with a close coordination of policy dialogue with other International Financial Institutions (IFIs) and donor partners, proved to be successful and effective in the conditions of Kyrgyz Republic and enabled the Bank to play a leading role in helping local municipalities and utility companies to start paving the way towards operational and financial sustainability. All municipal utility clients (water, solid waste and transport) introduced IFRS accounts, collection rates improved to above 90%, and cost recovery programs were successfully put in place.

Private sector's access to finance remained one of the strategic priorities for the Bank and in the post-crisis environment the EBRD was virtually the only lender to the domestic financial sector. EBRD continued developing local currency financing mechanisms supported by donor-funded risk sharing grants, which through reduced interest rate allowed making US\$50 million available to the Kyrgyz financial sector in local currency, enabling partner financial institutions to significantly increase their SME portfolio (50% over 2013). In 2013 the Bank completed the first pilot local currency corporate bond issue for one of the top banks where the EBRD (i) provided technical cooperation component, and (ii) acted as an anchor investor. The improvements in corporate bond market documentation and settlement process introduced by the project are likely to become market standards and are already encouraging future issuers to consider local currency bonds as a reliable source of funding.

In 2012 the Bank approved the US\$20 million Kyrgyz Sustainable Energy Financing Facility (KyrSEFF) to provide financing for energy efficiency improvements in the residential, service, agribusiness, SME and industry sectors, supported by EU IFCA grant and technical assistance financing, which has proved highly successful. By the end of August 2014, 90 per cent of the facility has been committed through signed loan agreements with four partners. KyrSEFF success builds on a previous policy dialogue aimed at developing and implementing energy efficiency related legislation and regulations, which has resulted in the

Kyrgyz Republic being the first post-Soviet country to implement an energy efficiency law for buildings fully compliant with EU Directive. This policy dialogue also strengthened institutional and operational capacity of the State Agency for Architecture and Construction required for implementation of the new legislation, as well as provision of energy efficiency certificates and expertise.

The Bank continued to finance and promote the Secretariat of the Business Development and Investment Council, a public-private dialogue platform which facilitated important changes and improvements into investment, fiscal and business related laws and regulations aimed at improving business climate and decreasing corruption. The Council contributed to adoption and amendment of 24 critical laws and regulations over the period. The Bank has also provided support to the government to improve public procurement policies and develop a modern e-Procurement system under the EBRD–UNCITRAL Initiative, in cooperation with the Asian Development Bank.

1.3 Key lessons

The majority of businesses in the Kyrgyz Republic are small and medium sized. Therefore, a key lesson for the Bank's future engagement with SMEs has been the importance of deploying instruments specifically designed for early transition countries (e.g., direct lending facilities, medium-sized co-financing facilities through partner banks), and dedicated donor-funded programs (e.g., capacity building, advisory, studies), as well as leveraging synergies between financial investment and advice for small businesses. Under the newly launched EBRD Small Business Initiative, the Bank should seek to further widen the range of SME products and services tailored to the needs of local companies, in order to improve response speed and increase flexibility of support. This should allow EBRD to strengthen its competitive position and attractiveness for other donors to channel their funds through the Bank, thanks to a more effective and efficient delivery, and increased regional reach.

In addition, to scale-up operations in the country in order to increase transition impact during the next strategy period, the Bank will need to confront objective constraints, in particular the country's small banking sector and the small universe of eligible financial partners resulting from compliance and credit risks of majority of banks, that limit the amount of financing EBRD can provide to and through the sector. Addressing these challenges will require exploring additional opportunities for risk-sharing and other ways to increase exposure.

In recent years, concessional funding coming from Russian and Chinese governments and institutions has intensified in the infrastructure sector, and is expected to continue to ramp-up during the next strategy period. This may have an impact on the Bank's future activities in the sector, in particular in regard to large infrastructure projects. Given the scarce grant financing, for which in many cases the Bank has to compete with other institutions, the role of the EBRD in large infrastructure projects should be realistically viewed as co-financier, joining IFIs such as the World Bank or Asian Development Bank whose annual country envelopes could leave financing gaps. However, in case of small infrastructure projects such as municipal infrastructure, where the Bank's financing and delivery model proved very successful, EBRD should sustain its leading role.

Lastly, a scale up in activities will need to be complemented by an increase in donor funding, to support investments (in particular in municipal projects and local currency lending where the Bank has been playing a leading role), SME advisory services and business environment

improvement initiatives. Although the Bank's activities ultimately aim at fostering sustainability and market mechanisms, donor funding at this stage is still required to pave the way, given affordability constraints and sovereign debt constraints. To support reforms and transition, the Bank will also need to enhance its policy advice activities, including developing wider sector policies, in close consultation with key donors.

2 OPERATIONAL ENVIRONMENT

2.1 Political Context

The Kyrgyz Republic went through a period of political upheaval in 2010-2011, but has emerged with a more democratically-oriented political system that seeks to adhere to the rule of law. The presidential election of 30 October 2011 brought a clear victory to Almazbek Atambayev. A parliamentary coalition, comprising the Social Democratic Party, Ata Meken, and Ar Namys, was formed in early April 2014 and the new government is headed by Prime Minister Djoomart Otorbaev, who has a track record of supporting reforms in the country. The government has an ambitious agenda, which is contained in the 2013-2017 national programme for sustainable development, focusing in particular on fighting corruption and improving investment climate. The next parliamentary elections are due to be held in 2015.

A great deal has been achieved in recent years but the country is still confronted with a number of challenges. The parliamentary model of government is still relatively new and in development, which continues to affect the smooth functioning of different branches of power. The speed of formation of the last parliamentary coalition in 2014 is a positive factor adding to the maturity of the political system of the country. However, the politics in the Kyrgyz Republic have been characterised by high volatility. Within a relatively short period of time the country went through two revolutions (in 2005 and 2010), frequent government changes and four parliamentary coalitions since the introduction of the parliamentary form of government in 2010.

Last year saw frequent protests, including road blocks, notably related to Kumtor gold mine, the country's strategic asset. Going forward, the governance system, particularly at the local level, needs to be significantly improved, as acknowledged by the authorities. The root causes of social instability and inter-ethnic tensions in the southern regions, including poverty and unemployment, are yet to be fully addressed. Corruption remains a problem and poses a threat to the political, economic and social development of the country.

In the regional context, the Kyrgyz Republic stands out due to the progress it has made on the path of democratic transition. At the same time, the country is heavily dependent on cooperation with its neighbours. Located at an important trade crossroads and being a transshipment point, the country both benefits from and depends on extensive regional trade flows and investment, mainly from China, Kazakhstan and Russia. The country seeks to join the Customs Union with Russia, Kazakhstan and Belarus in a process which is expected to be finalised by 2015.

2.2 Macroeconomic context

GDP growth in the Kyrgyz Republic remains highly dependent on output of the Kumtor gold mine. As a result of strike- and weather-related disruptions at the Kumtor mine in the first quarter of 2012, GDP in 2012 contracted by 0.9 per cent. GDP growth rebounded in 2013, on

the back of stronger output of the mining sector, reaching 10.5 per cent. The non-Kumtor GDP preserved its stable growth rate of 5-6 per cent.

Inflation remains highly volatile. It peaked at over 20 per cent year-on-year in early 2011 and decelerated to zero in mid-2012, but averaged 6.6 per cent in 2013, owing to higher food prices. The current account deficit deteriorated significantly from 10 per cent in 2011 to 25.9 per cent of GDP in 2012 and to 23.4 per cent in 2013. The Kyrgyz som remained relatively stable in 2013, however, it depreciated significantly in 1Q2014, following weakening of the Russian Rouble and 20% devaluation of Kazakh Tenge in February 2014. The reliance on remittances, predominantly from Russia, remained very significant, with remittances to GDP reaching around 31% in 2013.

Growth in 2014 is expected to slow down significantly. Taking into account the impact of the current slowdown in Russia on remittances, and to a lesser degree on exports, as well as softer growth of gold mining after a significant increase in 2013, and the fragilities of the banking sector, GDP growth is expected to moderate to 4.5 per cent in 2014 and somewhat recover to 4.8 per cent in 2015. For the remainder of the strategy period, growth is likely to be around 5.0 – 5.5 per cent.

However, several factors may impact this growth trajectory in the strategy period. Expected membership in the Customs Union, combined with deeper regional cooperation and integration outside of the Union countries, could provide a positive impetus for growth. The accession to the Union, which will reduce trade barriers with the Customs Union countries, may improve access of Kyrgyz exporters to the Union markets and increase cross-border trade, as well as potentially facilitate inward investments. More broadly, the accession can also reduce the risk of disruption to remittances flow from Russia, as the Union membership will reinforce free labour movement and protection of Kyrgyz workers' rights in the other Union countries. At the same time, the accession can negatively affect trade of Kyrgyz Republic with non-Customs Union countries, create risks for less competitive domestic industries and render non-economic some of the currently profitable activities of Kyrgyz companies (such as re-exports of goods, which currently is an important sector of the Kyrgyz economy). Uncertainty around the levels of the Kumtor production and the growth in Russia, which has a strong impact on remittances inflows and to a lesser extent on exports, may also impact growth projections.

2.3 Structural reform context

Structural challenges remain significant in many sectors, especially with respect to establishing sound market-supporting institutions. In spite of some positive steps taken by the authorities, such as the establishment of the Business Development and Investment Council, where EBRD has been playing an active role, the business environment is still challenging.

The mining and quarrying sector remains both a significant driver and potential downside risk for economic growth in the country, accounting for 10 per cent of GDP and 50 per cent of industrial output. The transparency of revenues in the sector has improved since Kumtor Gold became compliant with the Extractive Industries Transparency Initiative in March 2011. Establishing a stable framework for Kumtor's operations remains one of the key challenges for the country. The dispute between the government then seeking to nationalise the mine and Centerra, the mine's operator, led to spontaneous protests, which resulted in temporary disruption to production and a state of emergency being briefly imposed in 2012. By

September 2013, Centerra and the government signed a non-binding memorandum of understanding outlining the parameters of the restructuring of the Kumtor deal. In February 2014, the Parliament approved a resolution on Kumtor based on the previously negotiated non-binding Heads of Agreement between the Government and Canadian investor. While the Parliament approval is a positive step towards resolving the dispute, further negotiations and endorsement by both parties of legal agreements are needed. The outcome of the dispute will be determinant for the country's attractiveness to Foreign Direct Investments (FDIs) and will have an important impact on the Bank's activities and ability to attract financial sponsors in the next strategy period.

The Kyrgyz Government has approved the Sustainable Development Program (SDP) in December 2013, as an administrative tool to implement the National Sustainable Development Strategy. The program emphasizes that improving the business environment, reforming the public sector, strengthening the financial system, and addressing infrastructure development needs are essential for achieving high, broad-based, and inclusive growth and reducing poverty. It also highlights the need for additional financing from donors in order to fully implement programs.

In addition to its impact on cross-border trade and investment described above, the Customs Union accession represents both opportunities and risks for Kyrgyz Republic in terms of pace and direction of structural reforms. In the short-run, there is an impetus, as well as dedicated financing provided by the other Customs Union's members, for investment and reforms in areas such as customs infrastructure, sanitary testing and certification facilities, to help prepare the Kyrgyz Republic for operating in a single customs space. For reference, the lack of sanitary testing and certification facilities was one of the factors holding back Kazakhstan companies' ability to take full advantage of the larger economic space, following establishment of the Customs Union.

In a longer-term perspective, however, joining the Customs Union may reduce domestic reform impetus in Kyrgyz Republic, as some of the key structural reforms will be anchored at the Union level where economic institutions are rather weak, and the momentum will be dependent on the pace of reforms in larger members of the Union. In addition, the risk of reduced impetus would be increased if Kyrgyz Republic joins the Eurasian Economic Union, strengthening further the integration of its economic institutions with the Union countries.

2.4 Access to finance

Private sources of capital

The Kyrgyz banking system is small, with an assets-to-GDP ratio of 32 per cent as of end 2013, of which only half represent credit to the economy (16 per cent of GDP). There are currently 24 banks in the Kyrgyz Republic, 12 of which are majority foreign-owned. Russian and Kazakh banks have been showing interest lately in entering the Kyrgyz market. The sector is still recovering from the 2010 crisis. At the time, seven banks were placed under temporary administration. Currently three banks remain in temporary administration and two are in the regime of 'director oversight', under which the National Bank maintains hands-on control over activities of these banks. While the reported levels of non-performing loans (NPLs) have remained relatively low (5.9%), the true quality of assets is uncertain. These vulnerabilities, aggravated by weak corporate governance and a general lack of confidence towards the banking sector, continue to constrain the ability of the sector to provide credit to

the economy. The non-banking financial sector remains small as well, with assets representing 7% of GDP and credit portfolios 5% of GDP.

In that context, access to finance is a challenge, particularly for SMEs. The financial crisis and political developments have affected growth of lending to SMEs, as international microfinance institutions have refrained from providing finance, although now this is recovering. Commercial banks and other institutions have also increased their SME lending in recent years. SME lending is estimated between 30-50 per cent of total lending.

Capital markets in Kyrgyz Republic remain underdeveloped with low level of liquidity, weak implementation of rules and limited investor base. Securities legislation is relatively advanced, although the effectiveness of implementation of rules and regulations is poor. The institutional investor base needed to develop capital markets remains very limited and there is little likelihood that this might change without a government plan in place.

Multilateral development banks and donor finance

Multilateral development and bilateral donors have been active in the Kyrgyz Republic since the 1990s, providing mainly long term funding for infrastructure and private sector development and working with the authorities on legal and regulatory issues to support investment climate improvement. The largest stakeholders have been focusing on the following areas:

- The Asian Development Bank (ADB) is supporting mostly investments in the power, water and road sectors, and assisting the authorities with PPP legislation and e-procurement. As CAREC secretariat, ADB continues to lead and coordinate work on improving respective regional cooperation in trade policy, transit and customs transit.
- Both through investments and policy advice, the World Bank is active in infrastructure investment (power, water, waste water and irrigation, roads) as well as in the financial sector together with IFC, providing long term funding to the banking and microfinance sector, for SMEs and energy efficiency finance.
- The EU is financing mainly rural development (water, solid waste together with EBRD) as well as energy efficiency projects (including through support to KyrSEFF).
- Among bilateral donors, USAID has focused on power and mining sector reforms and institutional capacity building as well as agribusiness and textile sectors. SDC and SECO (Swiss) finance mainly rural development, including water and waste water, agriculture, SME (funding EBRD's Small Business Support) and energy efficiency. DFID has supported rural water systems, tariff and utility reforms. KfW and GIZ are concentrating their efforts on the financial sector, in particular micro- and housing finance, agriculture, mining sector and cross border water management.

In recent years, the Kyrgyz Republic has benefited from increasing bilateral concessional funding from Russia and China. To support accession to the Custom Union (borders and customs laboratories modernisation, infrastructure and economy development), Russia pledged to extend a USD 1.2 billion financing package to the Kyrgyz Republic through a mix of grant and loans. China has also been offering very attractive terms through the China Development Bank and China ExIm Bank, mostly for infrastructure and energy projects. The magnitude and highly concessional nature of these investments could crowd out EBRD and other IFIs' from certain sectors and potentially reduce their leverage on reforms. To address these risks the Bank would continue working in partnership with traditional IFIs and donors to leverage policy dialogue activities and promote reforms in key sectors.

2.5 Business environment and legal context

Business environment

The business environment is still challenging in the Kyrgyz Republic, despite some effective steps taken by the government in recent years. The 2014 Doing Business ranking improved slightly to the 68th rank, but implementation of laws and regulations remains weak. In the areas such as starting business and registering property the Kyrgyz Republic ranks in top 15, but the overall standing of the country is driven by relatively weak performance (ranking outside top 100) in areas such as paying taxes, resolving insolvency, getting electricity and trading across borders.

The EBRD and World Bank's 2013 Business Environment and Enterprise Performance Survey (BEEPS) results show that, whilst there has been improvement in the business environment since 2008, significant obstacles to doing business remain. According to the firms that were surveyed, political instability, corruption, informal sector, tax rates and access to electricity are the main obstacles that they face. In spite of the creation of free market zones, uncertainties in the local legislation and political instability are seen as the major factors that discourage foreign investment in those free zones, as shown by recent research published by the Bishkek Business Club.

The majority of SMEs are concentrated in sectors such as trading which do not generate significant value added and there is a "missing middle" of medium-sized enterprises contributing to GDP. The ability of SMEs to innovate, improve their competitiveness and grow remains hampered by the lack of skills, inadequate management practices and limited access to know-how. The consulting sector has developed dynamically in the last strategy period however services have not yet become an integral part of local business practice. Many SMEs are still either unaware of the services available or do not trust consultants, therefore association with the EBRD is still a key factor in decision-making. Services remain limited to areas such as information communication technology and supply is poor outside main cities. Further professionalisation of the consulting industry is needed, and although the local association of consultants has made progress its long term sustainability cannot yet be guaranteed.

The lack of permanent solution to the Kumtor mine situation remains one of the most important issues affecting attractiveness of Kyrgyz Republic as an investment destination, particularly for foreign investors. The government is continuing to actively seek a solution that could hopefully reduce uncertainty and therefore improve investment climate.

Legal context

Some positive steps were taken recently to bolster competitiveness of SMEs. A draft law designed to simplify and improve accounting requirements for small enterprises with respect to tax and social contributions was submitted to the public for comment. The aim of the law is to reduce the administrative burden on SMEs. However, further improvements to the judicial system and the enforcement of court judgments are required to foster the SME sector.

In the past two years the Kyrgyz Republic has entered into a number of agreements with a

view to establishing closer cooperation and removing existing barriers with other countries in the region. In April 2013 the Kyrgyz Republic and Turkey signed cooperation agreements in the areas of air communication, tourism, and investment. Tajikistan, Kazakhstan and the Kyrgyz Republic are considering restoring a unified energy system to provide a stable and uninterrupted power supply to the countries of the region. Also, in July 2014 the Kyrgyz Republic, Kazakhstan, Tajikistan, Turkmenistan, Uzbekistan and Japan signed a 10-year cooperation agreement as part of the Central Asia and Japan Dialogue (a platform for cooperation between the Central Asian countries with Japan on issues of sustainable development, the expansion of trade and economic relations). The agreement between the Kyrgyz Republic and Russia signed in May 2014 for the development of economic cooperation in the context of the Eurasian economic integration is a further example of the efforts made towards closer integration with other countries in the region.

See Annex 4 for a more detailed assessment of the legal environment.

2.6 Social context

The 2010 revolution, coupled with the global financial crisis, has reversed the trend of improvement in living standards and social conditions observed in the last decade. After hitting a low at 32 per cent in 2009, the overall poverty rate has increased to 38 per cent in 2012. In addition, significant regional disparities remain. Access to health, water and sanitation services as well as employment tends to be more difficult in rural areas, exacerbating differences in living standards across the country. Furthermore, internal migration to Bishkek creates significant challenges. Migrants tend to live in informal settlements, without the provision of public services, and their lack of adequate documentation affects their access to health services and employment. A large gender gap persists in relation to access to health, with high maternal mortality rates and low contraceptive prevalence.

Unemployment remains a concern, in particular among youth and women, with important consequences for the country's long term growth potential. In spite of a slight decrease over the last 5 years, total unemployment remains at 7.6 percent in 2013. Women experience higher unemployment rates than men (10 percent vs. 8 percent) and are over-represented in occupations with lower wages. Similar to other countries in Central Asia, female labour force participation is low, at 53 percent, compared to 77 percent for men, a situation entrenched by the substantial earnings gap between women and men, lack of career progression opportunities, limited access to child care and a return of more traditional values.

Young labour market entrants are particularly affected by a lack of economic opportunities, with 21 percent of 15 – 24 year olds not engaged in education, employment or training and just over 17 percent unemployed. Female youth unemployment is even higher, with only 38 percent of 15-28 year olds active in the labour market, as compared to 64 per cent of male youth of a similar age. One of the drivers of youth unemployment is the comparatively rigid labour market structure, in particular related to hiring and firing flexibility, which tends to benefit existing employees over new entrants. Another factor is the low quality of the education system. In the last Program for International Student Assessment (PISA) survey the Kyrgyz Republic participated in, the country ranked last, performing poorly in all subjects tested (reading, math and science) with a large performance gap between urban students and those in rural schools. Combined with a lack of adequate career guidance and a persistent skills-mismatch between the educational output and the demands of the labour market,

progression routes from education into employment remain weak. This results in a comparatively large proportion of youth being employed in the informal sector, estimated to amount to 26 percent of GDP in the Kyrgyz Republic.

2.7 Energy efficiency and climate change context

Energy intensity in the Kyrgyz Republic remains significantly higher than in developed economies and is almost 4 times greater than the EU average. In addition, the dependency on fossil fuels and the risk associated with security of energy supplies remains a challenge for the next period.

Coal and hydro are the main natural resources of the country and cover half of the Kyrgyz Republic's energy needs. The country possesses the third largest hydropower resources in CIS after Russia and Tajikistan, and has a strong untapped potential in wind, solar, and biogas. However, it remains largely dependent on imports from Uzbekistan and Kazakhstan for fossil fuels, creating energy security concerns.

The limited capacity and obsolete condition of the existing energy infrastructure is an increasing problem, especially as the demand of the end use sector is continuously growing. The power sector is highly subsidised and tariffs for electricity are substantially lower than cost recovery levels (average electricity tariff is almost 10 times lower than the EU-28 average). Low tariffs, together with a high level of technical and commercial losses, strongly affect the ability of generation and distribution companies to undertake the needed capital expenditure, beyond emergency repairs. This has led to a decline in the reliability of the network and a subsequent increase in technical losses. The issue is compounded by inefficient metering and billing procedures, as well as a general lack of financial transparency in the sector.

In that context, energy efficiency improvements across the sectors are crucial to mitigate the increasing electricity demand and support a more sustainable economic development. The building sector is the largest energy end-user (over 40% of the final energy consumption). In order to improve energy efficiency in the sector, the government adopted in 2011 the Law on Energy Performance of Buildings (EPB), effectively transposing the EU Directive on EPB. The Law was developed with the EBRD technical assistance and supported financial products such as the KyrSEFF to be implemented. Going forward, the regulatory framework for energy efficiency and heat supply regulations are areas that would benefit from EBRD support through its policy dialogue.

The country faces significant challenges related to the efficient use of water resources. Although water-rich in principle, poor infrastructure and poor management practices translate into inefficient water use, compounding spatial and seasonal limitations on water access, and affecting crucial economic sectors such as agriculture and hydropower, as well as drinking water supplies. Furthermore, decline in water resources have been identified as one of the most severe climate change risks facing the Kyrgyz Republic, with glacial melting projected to significantly reduce available water resources in the longer-term.

3 STRATEGIC ORIENTATIONS

3.1 Strategic Directions

Although the Kyrgyz Republic is in the forefront of the reform process in Central Asia, transition challenges in the country are still significant, and the business environment remains difficult. While rich in mineral wealth, the Kyrgyz Republic is a landlocked country, whose domestic market is too small to generate sufficient interest from investors outside the extractive sector on its own merit. The country's economy outside the extractive sector is dominated by small, family-run companies, whose growth is impeded by inadequate skills and management practices, weak operating models, and lack of access to finance, in addition to the constraining factor of a small domestic market. The Kyrgyz Republic needs to continue to improve the businesses' access to infrastructure and the population's access to basic municipal services. The economy is energy-intensive, due to a high rate of energy losses, out-of-date energy infrastructure, shortages of energy supply during winter peaks and inefficient equipment. The Kyrgyz Republic is also a country of significant regional disparities, compounded by the often complex relations between the country's ethnic groups. In the aftermath of the political and social unrest of 2010, internal re-integration of the country has been a priority of the parliament and the government, as well as donors. In this context, the following strategic orientations are proposed to form the core of EBRD's engagement in the Kyrgyz Republic in the forthcoming strategy period:

- **Foster sustainable growth by strengthening regional cross-border linkages:** As a landlocked economy with a limited domestic market, the Kyrgyz Republic would benefit greatly from deeper regional integration, given its important energy export potential, as well as good regional trade and transit position. Border disruptions with Kazakhstan in 2010 have highlighted the dependence of the country on cross-border trade. The country is engaged in several regional integration processes (WTO, Eurasian Economic/Customs Union, Shanghai Cooperation Organization, Cooperation Council of Turkic-Speaking States, CAREC), which create opportunities in terms of export markets and potential inwards investments. In that context, the Bank will aim to help facilitate economic and trade cooperation and integration with the region, by supporting rehabilitation of critical infrastructure, strengthening the exporting sector including through access to finance and advisory, as well as supporting cross-border investments and regional cooperation projects.
- **Enable SMEs to scale-up and bolster competitiveness:** Outside the extractive sector, the economy is dominated by fragile, 'cottage-industry'-type SMEs, with few mid-sized corporates in existence. While deeper regional trade links create opportunities for the best local firms both in terms of export markets and inward investment, stronger operating models and core competencies will be needed to better compete. SMEs ability to develop in a more competitive environment is hampered by the lack of skills and inadequate management practices, as well as by the business environment that is not conducive to growth, including limited access to finance, weak property rights, corruption and complex bureaucratic procedures. Leveraging its recently reinforced SME finance and development capabilities, the Bank will thus support competitiveness and sustainable growth of SMEs with viable business models through investment and business advice, promoting in particular skills transfer and operational efficiency improvements, and seek to strengthen the financial sector to facilitate access to finance for SMEs, in particular in local currency. The Bank will also step up its efforts of improving the business environment through policy dialogue.

- **Promote sustainability of public utilities through commercialisation and private sector participation:** Municipal and energy infrastructure has suffered from years of underinvestment, deficient regulatory environment, and weak core competencies. Most public utilities and power companies have poor financial and operational performance. The power sector is unbundled but remains state owned. Only a few small hydro power plants are private. Below cost tariffs, high losses, obsolete fixed assets, lack of meters and independent regulator make this sector unattractive for the private sector. Water and wastewater services are under municipal control and are operated inefficiently, in particular in smaller cities. To address those issues, the Bank will continue to support municipal utilities, where it has a recognized expertise and delivery model in improving operators' financial condition, operating practices and governance, and seek to support sustainability of power sector by rehabilitating assets and developing a more attractive institutional framework for private investment.

In addition, the Bank will seek to support through the above priorities the reduction of regional economic disparities, by increasing its outreach to less developed rural areas, in particular in the southern regions, and addressing inclusion gaps in relation to gender and youth across sectors.

3.2 Key challenges and Bank activities

Theme 1: Foster sustainable growth by strengthening regional cross-border linkages

Transition challenges

- Critical (road, rail, cross-border logistics) infrastructure needs to be enhanced to facilitate cross-border trade and lower transport costs, a key impediment for Kyrgyz exporters. The road sector remains largely unreformed in most aspects (institutions, road user charges, private sector participation). Regional road maintenance units carry out routine maintenance works, but they have not been properly corporatised and there is no competition in place. A comprehensive road sector strategy has been prepared but very little progress has been made in its implementation.
- Regional power transmission bottlenecks translate into electricity rationing in the winter, exacerbated by the excessive dependence on hydro resources, the use of which is driven by regional water sharing arrangements.
- Upgrading inefficient operating assets and shift to higher-value specialised products that conform to international quality standards remain a major challenge among Kyrgyz exporters. Sanitary standards of export products are also often below international and regional benchmarks.
- Exporters' access to finance is constrained by the limited capacity of the financial sector (small asset base, inadequate trade finance products and skills) and limited financial literacy and management skills among export oriented companies.
- In extractive industries, which represent more than 50% of exports, uncertainty remains regarding the legislative and regulatory reform process, while state interference in the sector and insufficient private-sector participation across the value chain endures.
- Significant trade barriers remain, such as tariff and non-tariff barriers, corruption and inefficient policies for trade within the Central Asia region, as well as with Russia and China.

Operational response³

- The Bank will be actively supporting FDI bringing skills, technology, and increased competition and standards into the country, with a particular focus on investments from the extended region. Subject to a stabilisation of the regulatory framework related to mining operations, the Bank will stand ready to support further private operators in the sector to promote responsible operations and highest business and environmental standards, as well as to decrease dependence on a single operating mine.
- The Bank will continue facilitating exports by assisting companies, in sectors such as agribusiness, light industry, construction materials and information technology (IT), using a combination of instruments, including Trade Finance Programme (TFP) lines through banks and business advice to improve export readiness.

³ Due to debt sustainability concerns, public infrastructure projects will be financed with co-financing grants or concessional loans from other IFIs or bilateral donors.

- The Bank will consider opportunities to finance regional logistics, property and tourism projects primarily in Bishkek, Osh, on Issyk-Kul to support regional cooperation and make the country more attractive to business visitors and tourists.
- Financing key regional road corridors to strengthen linkages with neighbouring countries while promoting internal regional inclusion will be considered. To that end, the Bank will target supporting rehabilitation of key regional transport links for the Fergana valley and will consider involvement in other key regional road projects, subject to mobilisation of blended concessional financing in partnership with other development partners. In view of significant funding to infrastructure projects coming from countries like China and Russia, as well as high amounts of concessional financing by traditional IFIs, the Bank sees its role as a co-financier with these IFIs in projects where their country envelopes would leave financing gaps and where projects could deliver acceptable transition results.
- The Bank will consider the possibility of financing regional transmission infrastructure and the development of intra-regional power exchange and optimization of energy and water use in the Central Asia region.

Policy dialogue

- The Bank will continue working with the Ministry of Transport and Communications to support the implementation of road maintenance reform and financing, establishment and strengthening institutional capacity of a Road Agency.
- In order to support procurement efforts required for the provision of critical regional infrastructure, meet the WTO standards, improve process transparency and facilitate private sector participation, the Bank will continue providing TC, in cooperation with the ADB and other partners, to support the government's efforts to improve and upgrade the national public procurement legislation and policies under the EBRD–UNCITRAL Initiative, including introduction of a modern e-Procurement system.
- The Bank will explore opportunities to assist with further strengthening of mining sector governance, regulatory framework, employment of women and practical implementation of Extractive Industries Transparency Initiative (EITI). Efforts aimed at strengthening institutional capacity of key agencies involved in the sector (State Agency for Geology and Natural Resources, Inspection for Environmental and Technical Safety, Department for Technical Inspection, EITI Secretariat) and promoting inclusion in the mining sector will be continued.

Results Framework for Theme 1: Foster sustainable growth by strengthening regional cross-border linkages

CHALLENGES		OBJECTIVES	ACTIVITIES	TRACKING INDICATORS
1.1	Exports are constrained by lack of access to finance, weak sanitary and quality standards	Support Kyrgyz exporters, by facilitating access to finance and improving standards	<ul style="list-style-type: none"> • TFP lines through banks to facilitate exports • Debt and equity investment for export related projects • Advice for small business, including export promotion and quality standards 	<ul style="list-style-type: none"> • Volume of clean (i.e. new) trade finance lines opened by partner banks (<i>Baseline – 0</i>) • Δ in share of exports in total turnover of export-oriented companies supported through direct investments and business advice (<i>Baseline - established at projects approval</i>)
1.2	Foreign investments coming into Kyrgyz Republic have limited technology and skills transfer components	Promote FDIs bringing skills, technology, and increased competition and standards into the country	<ul style="list-style-type: none"> • Debt and equity investment with quality foreign sponsors, with a focus on investment from the extended region 	<ul style="list-style-type: none"> • Δ in volume of FDIs and evidence of foreign investments supported achieving their transition objectives (<i>Baseline - at projects approval; FDI volume (2013) - \$993.2 mln</i>)
1.3	Critical regional transport and energy infrastructure remain insufficiently developed	Jointly with other IFIs, support where possible development of key regional infrastructure in conjunction with promoting road sector reforms	<ul style="list-style-type: none"> • Selectively complement other IFIs finance for regional infrastructure projects (e.g., Fergana valley), using blended concessional financing with reform-oriented conditionalities • Policy dialogue on road sector reforms 	<ul style="list-style-type: none"> • Evidence of projects supporting expansion of regional cross-border physical infrastructure and successfully achieving their transition objectives (<i>Baseline - established at projects approval</i>) • Demonstrated progress in implementation of road reform (e.g., successful implementation of the road maintenance strategy, establishment of the Road Agency) (<i>Baseline –N/A</i>)
<p>Context indicator: Change in the perception about the obstacles related to transport and custom/trade regulations in BEEPS (<i>Baseline 2013 – Transport: 50%; Customs and trade regulations: 65%</i>)</p>				

Theme 2: Enable SMEs to scale-up and bolster competitiveness

Transition challenges

- Competitiveness of SMEs is constrained by their sub-optimal scale, weak management expertise and business standards, as well as low overall productivity, efficiency and value-added. Inadequate skills and emigration of educated workforce remains a key challenge to developing a resilient fabric of growing SMEs moving up in the value chain.
- MSMEs access to finance is a key challenge for growth and achieving the scale needed for more efficient operations and better competitiveness. This is due to both fragilities of the financial sector (narrow asset base, poor corporate governance in banks, high dollarization, security based lending) and lack of sufficient collateral and low financial literacy among borrowers. Moreover integrity profile and excessive credit risks of many local banks and MFIs limit significantly the universe of partners that could be used by the Bank for on-lending to SMEs.
- Significant differences in access to credit exist between SMEs from Bishkek and the regions, a situation exacerbated by substantial regional disparities in relation to the quality and availability of education. In addition, gender inequalities in firm management, ownership and education remain important. Those material inclusion gaps are a key source of vulnerability.
- SMEs are suffering from a challenging business environment, due to inter alia a lack of well-defined property rights, and stable and transparent tax regime. Ensuring a fair and competitive market environment is also a major challenge and a constraint to developing firms that are more competitive on domestic and external markets, given the history of predatory behaviour by enterprises affiliated with politically exposed persons.

Operational response

- The Bank will support SMEs working in the sectors with the highest comparative advantage, such as agribusiness, tourism and competitive segments of the manufacturing and services sectors, through direct lending facilities, risk sharing with local banks, and technical cooperation for project support and capacity building, to facilitate growth, technology transfer, improvements in productivity and business standards.
- The Bank will scale-up its advice for small businesses through local consultants and international industry experts, with a focus on value added sectors. Linkages and complementarity with other products (credit lines through financial intermediaries, Medium Sized Co-financing Facility (MCFF) and Direct Lending Facility (DLF)) will be increased to improve access to finance. In addition the Bank will continue to strengthen the market for advisory services including supporting the professionalisation of the local consulting industry. These activities will play a leading role in increasing the Bank's outreach to less developed rural areas.
- Improvement of access to finance and better quality banking services for MSMEs will remain one of the key priorities for the Bank. The Bank will continue providing eligible banks and micro-financial institutions (MFIs) with targeted loans, where possible in local currency. The Bank will also consider providing dedicated credit lines to support development of leasing and value chain financing in key sectors such as agribusiness; and evaluate opportunities to provide equity investments and larger

debt packages to support MFIs transformation into banks. Given high levels of exposure to the few eligible financial partners and limited additional headroom, the Bank will have to develop instruments enabling it to take higher exposure to the sector if it wants to scale-up its activities. These instruments could include use of the risk-sharing facilities to overcome internal exposure limits, mobilising external partners through A/B structures or parallel financing, and developing portfolio risk sharing for the best quality banks.

- Development of local currency financing at acceptable pricing levels, which is crucial for non-exporter SMEs, will be continued by working with the Currency Exchange Fund (TCX) to raise the available limit for Som lending, increasing donor supported risk-sharing, and exploring alternative sources of raising local currency including a possible issue of Som-denominated bonds by the Bank and entering into swap agreement with the Central Bank.
- Energy- and resource-efficiency contributes to SMEs competitiveness, and the Bank will promote these across the whole economy. The Kyrgyz Republic Sustainable Energy Financing Facility (KyrSEFF) will be expanded in terms of volume, scope (to include water efficiency and waste minimization), local financial partners and regional coverage. In addition, the Finance and Technology Transfer Centre for Climate Change (FINTECC) and similar initiatives will be marketed to support effective resource utilisation, and promote modern technologies and international best practices with strong demonstration effects.
- In order to address the barriers faced by women entrepreneurs, EBRD will seek to offer its integrated ‘Women in Business’ programme to build the capacity and product range of partner financial institutions and offer technical assistance including in accessing finance, developing business skills and networking. This will depend on donor funding and readiness of FI partner banks to engage.

Policy dialogue

- The Bank will step up its support to the Secretariat of the Business Development and Investment Council to maintain active public-private dialogue and continue facilitating improvements and changes in the legal and regulatory framework encouraging a more stable and supportive business environment.
- The Bank will continue its efforts in support of financial sector development by facilitating introduction of new products including mobile banking, possibly supporting financial education and literacy, as well as strengthening regulations.

Results Framework for Theme 2: Enable SMEs to scale-up and bolster competitiveness

	CHALLENGES	OBJECTIVES	ACTIVITIES	TRACKING INDICATORS
2.1	SME competitiveness is constrained by sub-optimal scale, weak management expertise and business standards, as well as low overall productivity	Strengthen SME competitiveness through assets upgrade, skills and technology transfers, as well as advice on business practices and standards	<ul style="list-style-type: none"> ▪ Direct / indirect financing, supported by TC on corporate governance and operating practices ▪ Business advice in areas such as strategy, improving management practices, productivity and quality standards ▪ KyrSEFF and FinTECC implementation 	<ul style="list-style-type: none"> ▪ Small Business Support / TIMS indicators on number of client firms that reported growth, increased productivity and introduce standards (<i>Baseline - established at projects approval</i>) ▪ SEFF and FinTECC SME sub-projects implemented (number / volume) (<i>Baseline - 0</i>)
2.2	Financial sector ability to provide credit to SMEs is hampered by narrow asset base, high cost of local currency and poor corporate governance	Support financial sector development, in particular local currency lending	<ul style="list-style-type: none"> ▪ Targeted credit lines (e.g., SME, resource efficiency, leasing, value chain financing, gender) to financial institutions, when possible in local currency, with capacity building TC ▪ Policy dialogue on new banking products (e.g., mobile banking, water efficiency loans) 	<ul style="list-style-type: none"> ▪ Total number / volume of SME loans, local currency loans and loans outside Bishkek and loans to women-led companies extended by PFIs (<i>Baseline – established at projects approval</i>) ▪ Successful introduction of new banking products, as a result of the Bank’s facility offering and policy dialogue (e.g., mobile banking, water efficiency loans) (<i>Baseline – N/A</i>)
2.3	The business environment remains challenging, in particular with regards to property rights, tax regime and competition	Support improvements in the legal and regulatory framework encouraging a more stable and supportive business environment	<ul style="list-style-type: none"> ▪ Support to Secretariat of the Business Development and Investment Council 	<ul style="list-style-type: none"> ▪ Key achievements of the Business Council (e.g., number and qualitative account of laws and regulatory acts approved/amended as a result of BC activities, number and qualitative account of agenda issues generated by business community and addressed by the Council with a positive decision taken) (<i>Baseline – N/A</i>)
<p>Context indicator: Δ MSME ATC score (<i>Baseline 2014 – Overall 2- (Large) : Market Structure: 1.98 (Large); Market Institutions: 3.64 (Large)</i>)</p>				

Theme 3: Promote sustainability of public utilities through commercialisation and private sector participation

Transition challenges

- Water and wastewater services are separated from the central administration and remain under municipal control but are operated inefficiently; financial and operational performances are generally poor particularly in the smaller cities. Legal and regulatory framework (including lack of independent regulators) and approach to tariff setting (resulting in tariffs that are not cost reflective) remain significant challenges and constrain establishment of sustainable operators in the sector.
- The power sector is unbundled but remains largely state owned; only limited progress has been made towards commercialising operators in the sector and there are limited incentives to support private operations and investors.
- Energy tariffs – currently not costs reflective and not including environmental costs – do not provide incentives for efficient use of energy. Secondary regulations and institutions are not adequately developed and there are insufficient economic incentives to support market penetration of renewable projects, and insufficient capacity for carbon finance projects.
- Significant differences in quality and access to utility services in the South and North remain, reflecting material regional gaps.
- Low collection rates, lack of meter billing, and ineffective contractual arrangements between owners, operators and regulator/government also constrain the development of sustainable utilities sectors.

Operational response

- The Bank will continue expanding its engagement in the municipal infrastructure sector where EBRD's financing and delivery model proved very successful, including water, solid waste and urban transport. In the latter, EBRD will focus on rehabilitation of the public transport fleet and related infrastructure, as well as transportation services, in route optimisation planning and e-ticketing in Bishkek and Osh. Where possible, projects will be co-financed with EIB, IFCA, SECO, and others, including private corporates, with the view to advance commercialisation and private sector participation.
- Institutional reform and commercialisation of the participating utility companies will be supported through corporate development programmes to improve commercial standing, implementation of IFRS, project implementation support, and stakeholder participation programmes to enhance public ownership. As relevant, projects will put emphasis on improving resource efficiency, climate resilience, and inclusion impact.
- To contribute to the reduction of disparities in provision of municipal services across different regions of the country, particular attention will be given to projects in smaller cities, including in the southern regions and around Issyk-Kul and facilitating the participation of women and vulnerable groups in their design and implementation to the extent possible as well as employment opportunities where feasible and appropriate.
- To improve energy security and demonstrate viable financing and project structures, the Bank will encourage and support private sector involvement in construction and operation of small scale renewable energy projects. The Bank will also explore rehabilitation opportunities of existing HPPs, i.e. Toktogul HPP. Through its

activities, the Bank will seek to build resilience to the impacts of climate change on hydropower and pay due care to the regional water and power system requirements of downstream countries.

Policy dialogue

- The Bank will seek to engage in developing a modern water and waste water tariff methodology, setting clear relationship between the local authorities and utility companies, and developing a nation-wide Action Plan to increase individual metering coverage.
- The Bank will support improvements in water sector governance to ensure the sustainability of water sector investments and build resilience to climate change.
- The Bank will continue working with the Bishkek Municipality on the livelihood restoration and resettlement plan in relation to the solid waste management project to improve implementation and communication capacity of the municipality.
- Building on the Bank's successful track record in supporting energy efficiency, legal support for developing regulatory framework for district heating will be considered.
- The Bank will continue policy dialogue with the authorities to improve employment opportunities and HR practices affecting women, youth and regional populations in utility and public transport.

Results Framework for Theme 3: Promote sustainability of public utilities through commercialisation and private sector participation

	CHALLENGES	OBJECTIVES	ACTIVITIES	TRACKING INDICATORS
3.1	Municipal enterprises are operated inefficiently, particularly in smaller cities. Regulatory framework, approach to tariff setting and collection issues constrain sustainability of operators	Improve financial condition, operating practices, sustainability and governance of municipal utilities, with the view to advance commercialisation and private sector participation	<ul style="list-style-type: none"> ▪ Investment in water, district heating, solid waste management and urban transport, where possible in cooperation with other IFIs, donors and/or private sector ▪ TC supporting utility financial and operational performance improvement ▪ Policy dialogue on water and waste water tariff methodology; gender HR practices in municipalities 	<ul style="list-style-type: none"> ▪ Improvements in operational practices and cost performance of municipal operators (<i>Baseline – established at projects approval</i>) ▪ Number of target groups households (outside Bishkek) connected to new or substantially improved municipal and other infrastructure services (water, waste water, heat, roads) (<i>Baseline – 0</i>) ▪ Introduction of improved water and waste water tariff methodology in line with cost recovery principles, as a result of the Bank’s policy dialogue and technical assistance (<i>Baseline – N/A</i>)
3.2	The power sector remains largely state owned and inefficient, only limited progress has been made towards private sector participation, and energy tariffs do not reflect operating and environmental costs	Support sustainability of power sector by rehabilitating assets, and developing a more attractive institutional framework for private investment	<ul style="list-style-type: none"> ▪ Rehabilitation of HPP and TPP and investment alongside private investors in small scale renewables, taking account of climate resilience ▪ Policy dialogue on regulatory framework facilitating investments in energy efficiency projects 	<ul style="list-style-type: none"> ▪ Share of private ownership in power generation (<i>Baseline 2013 – 2%</i>) ▪ HPP capacity refurbished and / or made more climate-resilient (<i>Baseline – 0</i>) ▪ Number of renewable and energy efficiency investments reaching commercial operation with the Bank’s support (<i>Baseline – 0</i>)
<p>Context indicator: Δ in MEI and Power ATC scores (<i>Baseline 2014 – Water & Wastewater: 2 (Large); Urban Transport: 2 (Large); Power: 2+ (Large)</i>)</p>				

3.3 Potential risks to Country Strategy implementation

The ability of the Bank to deliver on its strategy in the Kyrgyz Republic and achieve expected outcome may be affected by a number of factors beyond the Bank's influence and control.

- While the political decision of the Kyrgyz Republic to join the Eurasian Customs Union is expected to create opportunities for economic development and trade, it poses also several risks to local businesses that are not yet adequately and accurately assessed by the authorities. For example, viability of SMEs in the light industry, trade and services might be significantly affected by the new customs duties to be introduced as a result of Customs Union accession. In the agriculture and food processing sectors, companies may find it difficult to meet Customs Union internal norms and standards, in terms of veterinary and quality requirements, and availability of adequately accredited laboratories and quality certificates. This may limit the universe of bankable clients in the corporate and SME sector, but also provide opportunities for the Bank to support companies in meeting these challenges.
- EBRD's ability to support FDIs will depend on the overall investment climate in the country. The final outcome of the negotiations with Centerra over Kumtor project will send a signal to foreign investors and could affect their appetite to invest in the Kyrgyz Republic.
- The strong presence of other IFIs and donors with large concessional financing and grant resources, as well as the acceleration of investments by Russia and China could potentially significantly reduce investment opportunities for the Bank. Scaling up investments and ability to finance infrastructure and power and energy sectors is highly dependent on the ability of the Bank to mobilise substantial capital grants and TC, and will represent a continued challenge from the transition and sound banking principles point of view.
- The Bank's ability to provide local currency finance is dependent on the access to the local currency funding. Existing limits in TCX for the Som funding, as well as immature capital market and lack of market based instruments create risks to the implementation of the Bank's projects in support of access to local currency finance by both financial partners and SMEs.
- The small size of the financial sector and the very limited number of potential partners may restrict the possibility for the Bank to increase outreach to SMEs. If no consolidation happens, the Bank may struggle to find ways to increase exposure to the financial sector, which will also limit its ability to develop new products.

3.4 Environmental and Social Implications of Bank Proposed Activities

The Bank's Environmental and Social Policy and Performance Requirements will apply to all projects carried out in the Kyrgyz Republic. The Bank will work closely with clients in developing Environmental and Social Action Plans with the objective of mitigating potential negative impacts and ensuring compliance with Kyrgyz national standards and the applicable EBRD Performance Requirements. EBRD's approach to managing the environmental and social risks associated with the projects that it supports continues to be complementary to that of other IFIs (e.g. World Bank, IFC, ADB and the EIB); however, given the recent revisions to the Bank's Environmental and Social Policy, it is envisioned that environmental and social capacity building, with both public and private sector clients, will play an important role in the overall success of the Kyrgyz Republic country strategy.

One of the most pressing environmental issues facing the Kyrgyz Republic is the continued decline of the country's sensitive biodiversity. Although only 0.13 percent of the world's landmass (199,951 sq. km) falls within its territory, the Kyrgyz Republic is home to approximately 1 percent of the world's known flora and fauna. The country also falls within Conservation International's *Mountains of Central Asia Hotspot*, recognising the Kyrgyz Republic as a high priority for global biodiversity conservation. To help address this issue, the Bank will continue promote biodiversity conservation and management practices through the projects that it supports, particularly in its investments related to rural infrastructure development, energy, extractive industries and agribusiness.

EBRD will also work closely with its clients to maximise benefits in terms of access to employment and/or services, especially for those who are considered to be vulnerable. This includes groups of people who are trying to urbanise, who lack appropriate documentation and/or who establish themselves in informal settlements, without legal title, that often lack adequate infrastructure and related services. Whilst this presents a very real challenge to EBRD and its clients, the Bank's environmental and social due diligence will be designed to ensure that vulnerable groups, who might be disproportionately affected by a project, are identified. This will enable both adequate mitigation measures to be put in place as part of the project design as well as interventions that will enhance these groups' ability to benefit from the Project's activities. Moreover, stakeholder engagement will be carried out in a culturally sensitive manner that is aimed at including the participation of both men and women and/or those groups who might otherwise not have a voice.

Many priorities that the Bank has currently set for the Kyrgyz Republic are anticipated to provide environmental and social benefits, such as water and wastewater treatment, improvements to urban infrastructure and energy efficiency projects. These projects, along with environmental and social capacity building initiatives and specific measures to support both water and biodiversity conservation will be targeted for Technical Cooperation support. EBRD will also continue to invest in, and provide training to, local banks to ensure that they are capable of implementing environmental and social due diligence procedures in accordance with the Bank's own stringent requirements, thus promoting sound development practices within the SME sector.

Protection of the environment and the health of the population are at the heart of a new nuclear safety fund which will be established by the EBRD to address the extensive legacy of Soviet era uranium mining and processing in the Kyrgyz Republic and other Central Asian countries. Multiple sites with large amounts of radioactive and toxic waste have been left behind which are largely unprotected or badly maintained and are in urgent need of remediation. It has been widely acknowledged in the international community that the Central Asian countries require support in dealing with this legacy and the EU has taken the initiative to call on EBRD's nuclear safety expertise.

3.5 EBRD co-operation with MDBs

Coordination among development partners in the Kyrgyz Republic has been formalised in the form of a Development Partners Coordination Council, with sector working groups acting under the Council. The Bank will continue playing an active role in the donor community raising issues for policy dialogue and joint activities. A particular attention will be paid both centrally and through the Bank's resident office on mobilising capital grants for infrastructure projects from existing partners and attracting new ones.

The Bank will continue closely working and seeking investment opportunities and policy dialogue synergies with major IFIs, i.e. WB, ADB, IFC in power and energy, infrastructure, financial sector, corporate governance, anti-corruption, public procurement, business climate and other areas.

The Bank will maintain close cooperation with SECO and the Swiss Embassy on joint co-financing of municipal and infrastructure projects, conducting water sector and rural development policy dialogue, strategic management of its joint local dairy equity investment, and supporting advice for small business. Possibilities to cooperate in the power sector with SECO will be discussed. The Bank will explore opportunities to mobilise jointly SECO and DFID resources to scale-up its support to SMEs through an integrated approach, leveraging its recently reinforced SME finance and development capabilities, possibly on a regional basis (including Tajikistan).

The Bank will continue closely working with the EU Delegation, IFCA and EIB coordinating its policy dialogue, in particular in water strategy, road rehabilitation and management, power and energy, energy and resource efficiency and SMEs support. The Bank will seek to mobilise TC and capital grants from EU to support municipal infrastructure feasibility studies in many cities and co-finance water and solid waste projects. The Bank plans to co-finance waste disposal projects in the southern regions, as well as water projects across the country.

The EBRD will continue to seek to attract partners to co-finance the Business Development and Investment Council secretariat and activities. Support has already been provided by USAID and IFC, but remains limited to certain activities. For example USAID has financed regional expansion of the platform into Naryn and Osh as well as specific business forums and events, but a more sustainable approach and support is needed.

ANNEX 1 – POLITICAL ASSESSMENT

The Kyrgyz Republic is committed to the principles outlined in Article 1 of the Agreement Establishing the Bank and is making good progress towards implementation of the principles of multiparty democracy and pluralism through the introduction of a parliamentary system of government and election of a multiparty parliament. However, many challenges remain.

The Kyrgyz Republic went through a period of political upheaval in 2010-2011, but has emerged with a more democratically-oriented political system. A parliamentary coalition was formed in early April 2014 and the new government is headed by a prime minister who has an established track record of supporting reforms in the country. The government has an ambitious agenda focusing in particular on fighting corruption and improving investment climate.

In April 2014 the Kyrgyz Parliament was granted the rare Partner for Democracy status by the Parliamentary Assembly of the Council of Europe (PACE) as an encouragement to further develop democracy in the only Central Asian country to have opted for a parliamentary system of governance.⁴

A great deal has been achieved in recent years but the country is still confronted with a number of challenges in upholding the rule of law, respecting human rights and promoting inter-ethnic reconciliation.

The parliamentary model of government which has emerged from the 2010 crisis remains new and not yet sufficiently developed, which continues to affect the smooth functioning of different branches of power. The speed of formation of the last parliamentary coalition in 2014 was a positive factor adding to the maturity of the Kyrgyz Republic's political system. The root causes of social instability and inter-ethnic tensions in the southern regions, including poverty, unemployment and deeply rooted corruption, are yet to be fully addressed. Corruption in particular, remains a serious issue, constituting a threat to the political, economic and social development of the country, as acknowledged by the authorities.

In the regional context, the Kyrgyz Republic remains heavily dependent on cooperation with neighbouring countries. Located at an important trade crossroads and being a transshipment point, the country both benefits from and depends on extensive trade flows and investment from China, Kazakhstan and Russia, as well as other partners. The Kyrgyz Republic seeks to join the Customs Union with Russia, Kazakhstan and Belarus in a process which is expected to be finalised by 2015.

Representative and Accountable Government

Free, fair and competitive elections

The Constitution which was introduced in 2010 provides for a democratic government with universal suffrage and elections are held on a regular basis. In recent years, elections in the Kyrgyz Republic have generally been deemed free and fair by international observers, despite some irregularities.

⁴ Parliamentary Assembly of the Council of Europe, Request for Partner for Democracy status with the Parliamentary Assembly submitted by the Parliament of the Kyrgyz Republic, Final version, Resolution 1984 (2014).

The new Constitution introduced a semi-parliamentary system of government and increased the number of parliamentary seats from 90 to 120⁵. Members of parliament are elected for a five-year term through a proportional party list system within a single nation-wide constituency. Only political parties are entitled to nominate candidates for parliament, effectively preventing individuals from standing for office as independent candidates. The last parliamentary elections took place on 10 October 2010 and contributed to the consolidation of the democratic process in the country. According to international monitors, these elections were characterised by “political pluralism, a vibrant campaign and confidence in the Central Commission for Elections and Referenda (CEC)”⁶. At the same time, the OSCE/ODIHR urged electoral legal reforms. To gain seats in parliament, a political party had to surpass a 5 per cent national and 0.5 per cent regional threshold, both calculated against the number of registered voters rather than based on turnout. Though originally designed with intention to stabilize the country, the unusual regional threshold compromised the principle of proportional representation. On the basis of the 2010 election results, five political parties were assigned seats in parliament. Three out of those five parties in parliament have formed the current majority coalition.

The 2011 presidential election took place under a new legal framework including provisions of the 2010 Constitution, the newly adopted constitutional Law on Presidential and Parliamentary Elections, and the Law on Election Commissions to Conduct Elections and Referenda. The election was monitored by international observers and, according to the final report of the OSCE/ODIHR Election Observation Mission, “was conducted in a peaceful manner, but shortcomings underscored that the integrity of the electoral process should be improved to consolidate democratic practice in line with international commitments. Candidate registration was inclusive, giving voters a wide choice, and the electoral campaign was open and respected fundamental freedoms. These elements, however, were overshadowed by significant irregularities on election day, especially during the counting and tabulation of votes”⁷. Nevertheless, Almazbek Atambayev’s victory has been the first peaceful transfer of power since independence and constitutes an another important step in the completion of the transitional period after the 2010 events. The citizens of the Kyrgyz Republic had the opportunity to choose from many candidates and make informed choices as a result of free broadcast and print media. The outcome reflected the will of the electorate to enhance stability and consolidate democracy.

Separation of powers and effective checks and balances

The Constitution of 2010 provides for a system of checks and balances between executive, legislative and judicial power. According to the Constitution, the Kyrgyz Republic is a parliamentary republic with an enhanced role of the parliament and the prime minister and reduced powers of the president, although the latter retains the right to veto legislation and to appoint defence and the security agencies. Despite earlier scepticism, the separation of powers between executive and legislative branches of power as defined in the new Constitution has proven its viability, while the system is still evolving.

⁵ OSCE/ODIHR Election Observation Mission, Parliamentary Elections 10 October 2010 - Report, 20 December 2010, p.5.

⁶ OSCE/ODIHR Election Observation Mission, Parliamentary Elections 10 October 2010 - Report, 20 December 2010, p.1.

⁷ OSCE/ODIHR Election Observation Mission, Presidential Election 30 October 2011 - Final Report, 10 January 2012, p.1.

Under the new Constitution the president is elected for six years and cannot run for another term in office. The president's role is to provide a balance in passing new legislation, to appoint certain members of government (those responsible for defence and national security issues) and to represent the country internationally. Since the 2011 elections the president has been able to boost his influence but not at the expense of parliamentary oversight.

The highest representative body is the Zhogorku Kenesh, the parliament, which exercises legislative power and defined oversight functions and is elected for a five-year term. A single political party may, depending on the outcome of the elections, take a maximum of 65 parliamentary seats.

The executive power is exercised by the government, headed by a prime minister. The candidacy for the post of prime minister is proposed by the coalition, forming the parliamentary majority. In the event that a coalition loses its parliamentary majority, a new government is formed.

The judicial system consists of the Supreme Court and local courts. There is no separate Constitutional Court with a Constitutional Chamber placed within the Supreme Court.

Effective power to govern of elected officials

The Kyrgyz Republic's democratically elected officials have the effective power to govern, despite the influence of business elites and, to a lesser extent, of organised crime groups which has been commented on by observers on a few occasions. The military is under civilian control and does not play a decisive role in the country's political decision-making process. Overall, religious, corporate or other non-elected entities do not possess excessive powers over elected officials.

Civil Society, Media and Participation

Scale and independence of civil society

The civil society organisations (CSO) sector in the Kyrgyz Republic is considered one of the strongest and most active in Central Asia. There are currently over 10,000 CSOs registered and approximately 3,500 of them are operational. The majority of CSOs are dependent on funding from international donors. The civil society is consulted by the government and the parliament in designing policy programmes, however not systematically. CSOs are also involved in monitoring elections and reforms in the courts and police systems.⁸

The activities of CSOs are regulated by the Non-Profit Organisations Act. There are ongoing concerns about possible restrictions on CSOs in several legislative proposals aiming at introducing restrictive reporting obligations to state authorities. These included the now rejected draft laws on money laundering, unregistered CSOs and treason. The pending law on Foreign Agents remains a matter of concern for CSOs in the Kyrgyz Republic.

⁸ The International Centre for Non-For-Profit Law, NGO Law Monitor: Kyrgyz Republic, last updated 28 May 2014, [HTTP://WWW.ICNL.ORG/RESEARCH/MONITOR/KYRGYZ.HTML](http://www.icnl.org/research/monitor/kyrgyz.html)

The right to form trade unions is envisaged by law and labour rights are broadly respected in practice. Many unions still operate as quasi-official institutions representing interests of the state rather than those of workers.

Independent pluralistic media that operates without censorship

Freedom of the press and freedom of expression are enshrined in the Constitution and are guaranteed by law. The law specifically prohibits press censorship.

Since the Kyrgyz Republic gained independence, its media has been transformed from a state-run system into a pluralistic media landscape, with both private and state-owned outlets. New media laws and registration procedures have been introduced.

Although challenges remain, independent observers report positive changes in the media environment after 2010. Among them are the decisions to establish a public broadcaster and to decriminalize libel, which were both commended by the OSCE Representative on Freedom of the Media.

The country's media outlets are mostly free from government control and function in a relatively open environment. However, significant concerns in this area include safety of journalists, level of their professionalism and self-censorship. A growing number of people are gaining access to the Internet. While online content is not censored, the authorities reserve the right to restrict access to some unspecified "extremist" websites.

Multiple channels of civil and political participation

Citizens of the Kyrgyz Republic generally have access to multiple channels of civil and political participation. There are many political parties and independent civil society organisations which represent a broad range of political and civil views. In the last few years, civil society has been engaged in public consultative councils at the ministries and state agencies. However, the effectiveness of such participation often depends on the attitudes of government officials towards CSOs.

The government is required by law to provide citizens with information regarding policies and subjects that affect them. However in practice, official websites do not contain sufficient information and content is also not always delivered in a timely fashion.

Freedom to form political parties and existence of organised opposition

The political party landscape of the country is extremely fragmented. According to official data, 181 parties are registered in the Kyrgyz Republic. Five political parties are represented in parliament and several more at the local level. The legislative basis to form political parties is enshrined in the Constitution and is implemented in practice as confirmed by the existence of genuine opposition parties able to campaign freely and to oppose government policies.

The activities of political parties are regulated by the 1999 Law on Political Parties. The opposition is organised and represented in parliament. Political parties are obliged to publish annual income and expenditure reports that include information on donations but there is no legal provision for an independent audit to verify the accuracy of these reports. 29 political parties nominated candidates for running in the 2010 parliamentary elections.

Rule of Law and Access to Justice

Supremacy of the law

The Constitution is the supreme law of the country and is accepted by all political forces. The right to a fair trial is envisaged in the legislature, although the strong position of the prosecutor and lack of full independence of the judiciary continue to affect this right. Corruption in the judiciary in particular affects the right to a fair trial.

The Constitution provides that a state of emergency or martial law may be imposed only in the circumstances and under the procedures stipulated in the Constitution and the constitutional laws. The UN Human Rights Committee pointed to the lack of information on the progress made to review the legislation governing states of emergency with a view of bringing it into compliance with Article 4 of the International Covenant on Civil and Political Rights (CCPR). According to the Committee, the state of emergency imposed in June 2010 in connection with inter-ethnic violence did not comply with the safeguards of Article 4, including failure to protect the right to life and prohibition of torture.⁹

Independence of the judiciary

Some progress has been made in the establishment of the judicial framework in areas crucial for the functioning of democratic institutions. However, despite efforts aimed at strengthening the judiciary, lack of its full independence is concerning. This includes the process of the selection and dismissal of judges as well as potential influence of the executive power over the judiciary. Since independence, the judiciary has been chronically underfunded, which makes reforms in this area more difficult.

Government and citizens equally subject to the law

The Constitution guarantees the equality of all citizens before the law. Impunity remains a problem, with the prosecutor general's office not always taking steps to prosecute officials who violate the laws.

Effective policies and institutions to prevent corruption

Corruption is a serious challenge, as acknowledged by the authorities. It affects the entire society and has a detrimental impact on the development of the country. According to Transparency International's Corruption Perception Index, the Kyrgyz Republic ranked 150 out of 177 countries in 2013, slightly improving from the 154th place the previous year.¹⁰ The law provides criminal penalties for corruption for officials but it is not enforced effectively. Corruption, which is endemic at all levels of the society, cronyism and strong power exercised by the previous presidential family were among the reasons leading to a popular uprising in 2010. Since then, the country has intensified its efforts to fight corruption. The government, the president and the parliament have all declared anti-corruption reforms a priority. In 2011 an Anticorruption Agency was created under the State National Security Committee and the issue is also highlighted in the government's Sustainable Development Strategy for 2013-2017. This represents a positive change in comparison to previous administrations which were trying to downplay the significance of the problem, although does not diminish the complexity of the task of eradicating the deeply-rooted corruption.

⁹ UN Human Rights Committee, Concluding observations on the second periodic report on the Kyrgyz Republic, International Covenant on Civil and Political Rights, 23 April 2014, CCPR/C/KGZ/CO/2, p.3.

¹⁰ Transparency International, Corruption Perceptions Index, 2013 and 2012.

Civil and Political Rights

Freedom of speech, information, religion, conscience, movement, association, assembly, and private property

As a member of the UN and the OSCE, the Kyrgyz Republic has ratified the core international treaties on civil and political rights and the fundamental conventions of the International Labour Organisation (ILO), which form an integral part of the country's legal system.

However, according to local and international observers, the implementation of these commitments has been uneven and inconsistent. While the fundamental freedoms of religion, conscience, movement, association and assembly are generally upheld, they are unevenly enforced. The latest review of the implementation of the Covenant on Civil and Political Rights referred to positive aspects but also identified a number of areas of concern. In particular, The UN Human Rights Committee observed that there is no evidence that domestic courts directly applied the provisions of the CCPR.

On the positive side, the overall achievements included the abolition of the death penalty, the adoption of the 2010 Constitution, the establishment of the Human Rights Coordination Council further to the government's resolution of 18 November 2013 which mandated to enforce the implementation of international human rights obligations, and the ratification of a number of Optional Protocols to major international instruments.¹¹

With regard to the freedom of expression, the Committee expressed concern about the persecution of human rights defenders, journalists and other individuals expressing critical opinions of state institutions in relation to the June 2010 events.

The law provides for the right of peaceful assembly and there were numerous public demonstrations throughout the country in the last few years. The freedom of association is generally respected in practice with the law requiring registration of trade unions, political parties and CSOs with the Ministry of Justice.

Political inclusiveness for women, ethnic and other minorities

The Kyrgyz Republic is a multi-ethnic society and the Constitution and the laws prohibit discrimination based on race, gender, disability, language, or social status. However, these laws are not enforced systematically.

There are no legal restrictions on the participation of women in politics and women are holding senior positions in the government and parliament. At the same time, there are continuing reports of acts of violence against women, including bride kidnapping and domestic violence. In many instances violence against women remains underreported.

While noting the efforts to integrate minorities into political and public life, there are concerns that minorities are not well represented in public institutions at both the national and local levels. According to the 2009 census, ethnic Kyrgyz constitute 71 per cent of the population with the two biggest ethnic minority groups being Uzbeks (14.5 per cent)

¹¹ UN Human Rights Committee, Concluding observations on the second periodic report of the Kyrgyz Republic, International Covenant on Civil and Political Rights, 23 April 2014, CCPR/C/KGZ/CO/2, pp. 1-8.

concentrated in the south, and Russians (9 per cent) living mainly in the north of the country. The causes of inter-ethnic conflict of 2010 are not fully addressed and there are reports about failure to investigate human rights violations fully, effectively and without discrimination.

There are continuing reports of violence against lesbian, gay, bisexual and transgender (LGBT) persons by both state and non-state actors, and there are concerns about the failure on part of the state to address such violence.

Freedom from harassment, intimidation and torture

Torture and other cruel, inhuman, or degrading treatment or punishment is prohibited by law. Despite acknowledgment of torture, only few cases of alleged torture made it to trial. Human rights monitoring organisations continue to report numerous cases of torture by law enforcement agencies.

In 2012 a National Centre to Prevent Torture and other Inhumane and Offensive Treatment and Punishment was established to monitor and prevent torture in detention facilities. While welcoming the amendment in the Criminal Code on the definition of torture, the UN Committee against Torture indicated that the current definition of torture in Article 305(1) of the Criminal Code limits criminal responsibility to public officials, excluding other persons acting in an official capacity. Furthermore, the specific offence of torture is not punishable by appropriate penalties, as required by the Convention against Torture, which was ratified by the Kyrgyz Republic.

ANNEX 2 – SELECTED ECONOMIC INDICATORS

	2007	2008	2009	2010	2011	2012	2013 <i>Estimate</i>
Output and expenditure							
	<i>(Percentage change in real terms)</i>						
GDP	8.5	7.6	2.9	-0.5	6.0	-0.9	10.5
Private consumption	2.5	13.4	-14.6	2.9	9.5	11.3	na
Public consumption	1.8	0.7	0.7	-0.2	1.3	2.2	na
Gross fixed capital formation	10.8	13.2	8.5	-7.1	-4.4	36.8	na
Exports of goods and services	25.8	9.1	-1.1	-11.7	15.7	-19.2	na
Imports of goods and services	11.0	13.6	-19.4	-6.9	14.9	12.4	na
Labour Market¹							
	<i>(Percentage change)</i>						
Gross average monthly earnings in economy (annual average)	30.6	36.0	15.2	14.2	30.6	16.8	5.0
Real LCU wage growth	na	na	na	na	na	na	na
Unemployment (end-year)	8.2	8.2	8.4	8.6	7.9	7.7	7.6
Prices							
	<i>(Percentage change)</i>						
Consumer prices (annual average)	10.2	24.5	6.9	7.8	16.6	2.8	6.6
Consumer prices (end-year)	20.1	20.1	-0.0	18.9	5.7	7.5	4.0
Fiscal Indicators							
	<i>(In per cent of GDP)</i>						
General government balance	-0.6	1.0	-1.1	-5.9	-4.6	-5.7	-3.8
General government revenues	30.3	29.9	32.3	30.5	31.8	33.8	33.9
General government expenditure	31.0	28.9	33.4	36.4	36.4	39.5	37.7
General government debt	56.8	48.5	58.1	59.7	49.4	49.0	47.7
Monetary and financial sectors							
	<i>(Percentage change)</i>						
Broad money (M3, end-year)	33.3	9.8	20.9	21.1	14.9	23.8	22.8
Credit to private sector (end-year)	83.7	22.8	-1.5	4.6	18.3	28.5	34.5
	<i>(In per cent of total loans)</i>						
Non-performing loans ratio	3.6	5.3	8.2	15.8	10.2	7.2	5.5
Interest and exchange rates							
	<i>(In per cent per annum, end-year)</i>						
Local currency deposit rate	4.7	6.0	5.3	4.6	5.3	5.2	5.6
Foreign currency deposit rate	2.2	1.6	2.2	2.9	2.8	2.9	2.8
Local currency lending rate	21.3	23.7	25.3	22.9	22.4	23.0	20.7
Foreign currency lending rate	18.1	19.5	20.6	19.3	17.8	17.3	16.4
Policy rate	8.8	15.2	0.9	5.5	13.6	2.6	4.2
	<i>(Soms per US dollar)</i>						
Exchange rate (end-year)	35.5	39.4	44.1	47.1	46.5	47.4	49.3
Exchange rate (annual average)	37.3	36.6	42.9	46.0	46.1	47.0	48.4
External sector							
	<i>(In millions of US dollars)</i>						
Current account	-94.4	-260.5	-53.7	-228.4	-389.2	-492.2	-160.8
Trade balance	-1,276	-1,879	-1,120	-1,202	-1,669	-3,211	-3,565
Merchandise exports	1,338	1,874	1,694	1,779	2,267	1,954	2,048
Merchandise imports	2,614	3,754	2,814	2,981	3,936	5,165	5,614
Foreign direct investment, net	207	377	189	438	694	372	549
Gross reserves, excluding gold (end-year)	1,177	1,225	1,588	1,718	1,834	2,067	2,238
External debt stock	3,560	3,423	3,947	4,240	4,754	5,190	6,007
Public external debt	2,080	2,084	2,503	2,646	2,826	2,992	3,158
Private external debt	1,480	1,339	1,444	1,594	1,928	2,198	2,849
	<i>(In months of imports of goods and services)</i>						
Gross reserves, excluding gold (end-year)	4.3	2.9	4.9	4.9	3.8	3.7	na
Memorandum items							
	<i>(Denominations as indicated)</i>						
Population (end-year, million)	5.3	5.3	5.4	5.5	5.5	5.6	5.6
GDP (in millions of soms)	141,898	187,992	201,223	220,369	285,989	310,471	350,028
GDP per capita (in US dollar)	719.8	959.4	864.3	875.1	1,120.5	1,181.8	1,280.2
FDI (in million of US dollars)	207	377	189	438	694	372	549
External debt - reserves (in US\$ million)	1,317	1,418	1,499	1,448	1,495	1,607	na
External debt/GDP (in per cent)	93.5	70.0	87.9	91.4	76.3	79.3	74.2
External debt/exports of goods and services (in per cent)	176	129.6	161.2	173.4	139.6	147.9	134.6
Broad money (M2, end-year in per cent of GDP)	30.3	25.8	28.4	31.4	27.8	31.7	34.5

ANNEX 3 - ASSESSMENT OF TRANSITION CHALLENGES

Market Str:	Market Inst:	Key challenges:
CORPORATES		
Agribusiness		
Medium	Medium	<ul style="list-style-type: none"> ▪ encouraging land and company consolidation to improve productivity in both primary and processing sectors; ▪ developing transport infrastructure to enhance competitiveness.
Manufacturing and Services		
Large	Medium	<ul style="list-style-type: none"> ▪ further improvement in business environment to attract more investments – both foreign and domestic in the sector to overcome the barriers created by the Customs Union; ▪ strengthening of the property rights, establishment of an impartial judiciary and creation of a stable and transparent tax regime.
Real estate		
Large	Medium	<ul style="list-style-type: none"> ▪ increasing the supply of modern commercial property in all sub-segments; ▪ ensuring effective enforcement of property rights and improving access to land and land information; ▪ increasing focus on modern construction techniques and technologies, including energy efficiency and sustainability.
ICT		
Large	Medium	<ul style="list-style-type: none"> ▪ further developing the telecommunications infrastructure (broadband internet); ▪ further increasing competition in the fixed line segment; ▪ privatising the fixed line incumbent Kyrgyztelecom; ▪ completing the privatisation of the mobile operator MegaCom; ▪ further developing the regulatory framework (e.g. ensuring the independence and sufficient capacity of the regulator and implementing competitive safeguards).
ENERGY		
Natural Resources		
Large	Large	<ul style="list-style-type: none"> ▪ successfully completing the on-going legislative and regulatory reform process in extractive industries; ▪ reducing State interference in the mining sector; ▪ increasing private-sector participation across the value chain in the production of hydrocarbons and minerals, including exploration, extraction and beneficiation activities; ▪ improving EHS&S standards; ▪ unbundling the gas supply and distribution company, KyrgyzGaz; ▪ completing the liberalisation process in the oil and gas downstream segment.

Market Str:	Market Inst:	Key challenges:
Sustainable Energy		
Large	Large	<ul style="list-style-type: none"> ▪ introducing cost reflective tariffs for end consumers; ▪ strengthening legal and institutional framework for supporting sustainable energy; ▪ strengthening capacity for implementation of carbon finance projects.
Power		
Medium	Large	<ul style="list-style-type: none"> ▪ promoting liberalisation; ▪ establishing an independent regulator; ▪ removing cross-subsidies and introducing cost reflective tariffs for end consumers; ▪ improvement of operating performance and reduction of losses especially in distribution/supply.
INFRASTRUCTURE		
Water and wastewater		
Large	Large	<ul style="list-style-type: none"> ▪ improving regulation (e.g. tariff methodology); ▪ developing contractual arrangements between the owner/policy maker and the company; ▪ further tariff increases and improvements in collection rates; ▪ corporate restructuring and further commercialisation (including restoration of physical supply, reduced water losses and increased water quality); ▪ introduction of meters and meter-based billing.
Urban Transport		
Medium	Large	<ul style="list-style-type: none"> ▪ developing city-wide urban transport policy (i.e. integrated urban transport strategy); ▪ increasing autonomy of publicly owned companies and developing contractual arrangements with the municipalities to allow for long-term financing to become possible; ▪ improving quality of services and operational performances; ▪ further private sector participation in service provision; ▪ introducing e-ticketing system for all modes of transport, including private operators, and improvements in collection rates.
Roads		
Large	Large	<ul style="list-style-type: none"> ▪ further increasing the resources allocated to the sector with prioritisation on road maintenance; ▪ introducing tendering procedures for periodic road maintenance; ▪ refining road user charges and reform of the Road Fund; ▪ formulating the privatisation plan for maintenance units; ▪ introducing service level agreements for routine maintenance.
Railways		
Large	Large	<ul style="list-style-type: none"> ▪ full corporatisation and establishment of arms-length relationship between the government and management;

Market Str:	Market Inst:	Key challenges:
		<ul style="list-style-type: none"> ▪ increasing financial transparency and sustainability; ▪ improvements in governance and procurement practice.
FINANCIAL INSTITUTIONS		
Banking		
Large	Large	<ul style="list-style-type: none"> ▪ broadening access to finance and facilitating increased competition among banks; ▪ reduction in share of FX lending (and funding) in the banking sector; ▪ improving corporate governance and business practices in the sector.
Insurance and other financial services		
Large	Large	<ul style="list-style-type: none"> ▪ broadening access to non-life and life insurance, including increasing a range of product available in the market; ▪ improving corporate governance and business conduct and strengthening skills base in the sector; ▪ private pension sector: (i) broadening access to the private pension products; (ii) facilitating establishment of new private pension funds and development of corporate governance, business conduct and skills base in the sector; ▪ leasing sector: (i) broadening access to leasing, including increasing a range of products available in the market; (ii) facilitating improvements in the legal and regulatory framework governing the sector.
Micro, Small and Medium-sized enterprises		
Large	Large	<ul style="list-style-type: none"> ▪ expanding general bank financial intermediation and lending to SMEs, in particular outside the capital city including by simplifying the loan application procedures for MSMEs; ▪ developing other sources of finance for SMEs including leasing and equity capital; ▪ extending the coverage of credit information services.
Private equity		
Large	Large	<ul style="list-style-type: none"> ▪ broadening companies' access to PE financing; ▪ improving corporate governance, accounting and business practices of corporate companies.
Capital Markets		
Large	Large	<ul style="list-style-type: none"> • facilitating increase in liquidity in local capital markets; • improving local capital markets infrastructure; • improving the legal and regulatory framework governing capital markets, including corporate bonds.

ECONOMIC INCLUSION GAP RATINGS

ECONOMIC INCLUSION		
Inclusion gap dimension	Inclusion gap	Key challenges
Regions		
Access to Services	Large	<ul style="list-style-type: none"> ▪ increasing access to infrastructure and services that substantially enhance the economic opportunities of the local population, specifically in relation to improved health, access to employment, training or entrepreneurial activities
Labour Market	Medium	<ul style="list-style-type: none"> ▪ improving access to local jobs and the continuing skills mismatch ▪ strengthening measures to formalise employment, especially in rural areas
Youth		
Labour Market Structure and Opportunities for Youth	Medium/Large	<ul style="list-style-type: none"> ▪ increasing labour market flexibility to reduce barriers to entry, particularly in relation to hiring / firing flexibility ▪ developing effective progression routes from training into employment through partnerships between employers and education providers (at secondary and vocational levels), for better job matching and the establishment of apprenticeships
Quantity and quality of education	Medium/Large	<ul style="list-style-type: none"> ▪ encouraging the private sector to engage more closely on the design and implementation of training curricula to address the skill mismatch and improve the employability of young labour market entrants, e.g. through Sector Skills Councils ▪ creating stronger progression routes from training into employment by fostering partnerships between employers and education institutions through scholarships, internships and the introduction of work based learning opportunities ▪ improving quality and availability of education
Gender		
Legal regulations	Medium	<ul style="list-style-type: none"> ▪ improving the enforcement of Law on State Guarantees for Ensuring Gender Equality, especially in relation to equal property ownership rights
Access to health services	Large	<ul style="list-style-type: none"> ▪ strengthening measures to reduce the maternal mortality rate in the country through improved awareness of and access to quality medical care

Labour policy and practice	Medium/Large	<ul style="list-style-type: none"> ▪ reducing discrimination on the basis of gender in employment and support non-discrimination policy development
Employment and firm ownership	Medium	<ul style="list-style-type: none"> ▪ strengthening the provision of career guidance at secondary and tertiary education levels in order to attract more female students into careers ▪ incentivising the private sector to adopt equal opportunities employment standards ▪ improving access to child care in order to attract more women to participate in the labour force
Access to finance	Small	<ul style="list-style-type: none"> ▪ supporting FIs in the development of financial and particularly non-financial products (e.g. business skills and financial literacy training) specifically aimed at female entrepreneurs in the SME segment. ▪ incentivising FIs to review collateral requirements for women-led businesses, e.g. by accepting the applicant's salary (in lieu of land or property) as collateral

ANNEX 4 – LEGAL TRANSITION

Introduction

This annex offers critical analysis on legal topics relevant to the Bank’s investment strategy in the Kyrgyz Republic during the forthcoming period. It is based on the assessments of commercial laws conducted by EBRD Legal Transition Programme¹² and also draws on the lessons learned from past and current technical cooperation projects led by the Bank. For ease of reference, the analysis is presented along the three main strategic orientations defined in this country strategy.

Fostering sustainable growth by strengthening regional linkages

Public procurement law

Public procurement rules are highly relevant to the development of infrastructure (e.g., roads) necessary to strengthen linkages with neighbouring countries. In the Kyrgyz Republic, public procurement is regulated by a 2004 law (the PPL), as amended. The PPL is based on the 1994 UNCITRAL standards and to a large extent is now outdated. The PPL provides specific procurement rules for government procurement and public institutions, including state – owned companies, however, there is no specific separate regulation for public procurement in the utilities sector.

According to recent assessments conducted by the Bank, the PPL shows a medium level of compliance with current international standards. Reforms are needed to upgrade the legislation to the standards of the 2011 UNCITRAL Model Law on Public Procurement (a model particularly relevant to CIS countries, given their previous reliance on the old UNCITRAL model law).

Regulatory reforms in the Kyrgyz Republic should address in particular the following shortcomings:

- absence of independent review and remedies mechanisms;
- preferential treatment of domestic bids;
- lack of advanced eProcurement procedures;
- absence of comprehensive provisions aimed at curbing corruption in the procurement process;
- insufficient regulation of procurement planning and contract management;
- lack of procedures for small value contracts and commonly purchased goods and services.

Presently, a new legislation is being developed and is discussed by parliament. Since 2012, the EBRD UNCITRAL Initiative, a joint technical cooperation programme of the EBRD and the United Nations Commission on International Trade Law (UNCITRAL) has been assisting the Kyrgyz government in revisions to the public procurement primary and secondary legislation. The project will continue in particular with a view to promoting eProcurement mechanisms.

¹² See WWW.EBRD.COM/LAW

Enabling SMEs to scale-up and bolster competitiveness

Judicial capacity and contract enforcement

A well-functioning judicial system is key to the development of the SME sector. The *EBRD Judicial Decisions Assessment* found court judgments in commercial law matters in the Kyrgyz Republic to be above the regional CIS average in terms of quality and predictability, a finding consistent with the EBRD's support for commercial law judicial training in the country from 2006 to 2011. However, the improvements in commercial law judgments are not evident in other areas of law. As in other countries of the region, the courts often wrongly apply general civil and procedural rules rather than relevant provisions of specific laws governing the dispute in question. Enforcement of court judgments is another major issue for the entire region. In the Kyrgyz Republic, one of the most problematic areas is non-compliance with time limitations for the relevant procedures, mainly due to lack of effective instruments to counter the improper behaviour of debtors making spurious claims that hinder the enforcement process. Insufficient staffing of the enforcement agency and lack of professional training on enforcement procedures are other factors contributing to the low rates of enforcement.

The impartiality of courts in Kyrgyz Republic is perceived to be questionable. This is consistent with data from the *EBRD / World Bank Business Environment and Enterprise Performance Survey*, where only 24% of local respondents considered that courts were fair, impartial and uncorrupted. Lack of easy access by lawyers and the general public to judicial decisions limits public scrutiny of courts output and results in common allegations of corruption. The courts are also believed to show particular deference to the government and entities in which the state has a substantial interest. The speed of justice remains another issue due to heavy caseloads; courts also suffer from limited financial resources, which is evident in the quality of court premises and equipment in many areas.

Recommended measures for strengthening the courts include: entrenching the system of initial training for candidate judges introduced in 2011 with EBRD assistance; ensuring a majority of judges in the composition of the Council of judges; providing greater funding and staff to the Judicial Training Centre; ensuring comprehensive free access to case law; enhancing capacity of bailiffs, including through providing professional training, introduction of simplified enforcement procedures and ensuring access to information regarding enforcement procedures; and greater use of alternative methods of disputes resolution (mediation, arbitration) in order to ease the caseload burden on the judicial system.

Pledge law

An efficient pledge law is an important feature of the business environment for SMEs. In the Kyrgyz Republic, the primary legislation governing secured transactions includes the Law on Pledge adopted by Government Decree No. 49 on 12 March 2005. This law has repealed and replaced the 1997 Pledge Law and the 1999 Mortgage Law. A number of changes have been made to the law since 2005. One of the most significant amendments provided for extrajudicial enforcement of creditor rights. The civil code provisions on pledge were amended in February 2007 to reflect the new law. More recent reforms took place in 2008-09 when the Kyrgyz Republic amended its civil code and pledge law to make secured lending more flexible, by allowing general descriptions of encumbered assets and of debts and

obligations. Technical amendments have been made multiple times since 2007, most recently in July 2011.

As regards potential improvements to the system, pledge registration could be modernised into a “notice” system which enables immediate registration of information as presented by the parties, and immediate access to all registered information by any member of the public. Such a notice system would eliminate any requirement for judicial review of registration applications or examination of pledge and provide the public with real-time access to all registered information via the internet and a user-friendly search engine.

Promoting sustainability of public utilities through commercialisation and private sector participation

Renewable Energy

The economy of the Kyrgyz Republic remains highly energy-intensive and relies to a large extent on energy imports. Energy security is a state priority and rapid expansion of the use of renewable energy sources (RES) is at the centre of the government’s policy efforts. The Energy Saving Programme (till 2015) and the longer-term Strategy for the Fuel and Energy Complex Development (till 2025) set the policy framework for the sector. The government has also approved a high-level action plan to implement the Energy Saving Programme, including reduction in the energy losses, introducing development of small-scale energy projects and modernisation of energy infrastructure. The current RES generation comes primarily from small-scale hydropower plants, which could attract more future investments. Biogas and solar power can be mainly applied in micro-generation, the residential sector and in small-scale industrial projects. Wind has a limited potential as the wind speed is low and the wind map has to be further developed. Geothermal sources are to be explored.

The lack of modern regulatory framework until recently has been a major barrier to sector development. In 2008, the first Renewable Energy Sources Law (RES Law) was enacted. The RES Law introduced basic principles of regulation of RES production and distribution, including licensing of RES facilities (other than those used for own consumption), cost-based tariffs for RES-produced electricity with separate coefficients for each RES type, import duty exemption for RES equipment and mandatory purchase of the RES-produced electricity. One of the amendments introduced to the RES Law in 2012 provides for the RES producers’ right to claim lost profit from energy companies for breach of their obligations under the RES Law. Despite the introduced incentives, the RES Law is considered insufficient for the proper stimulation of RES investment. This is primarily due to the short pay-off period (8 years) for cost-based tariffs. Another drawback of the RES legislative framework is the lack of supporting regulations which are vital for a framework-type law such as the RES Law. Development of RES is significantly hindered by a subsidised and very low cost of electricity in the country.

International donors are working with the government on improving the investment environment. The EBRD provides support to RES and energy efficiency development through the Kyrgyz Sustainable Energy Financing Facility (KyrSEFF) – a credit facility to local banks and non-bank micro-financial institutions, which would enable further lending for RES and EE projects based on the established eligibility criteria.

In the future, the government's efforts should be focused on aligning the legal and regulatory framework for the RES sector with best international practices and removing the financing and other barriers for development of RES projects. Lack of technical standards in the sector is still considered to be an impediment to the implementation of RES projects, along with high cost of imported technology (due to lack of domestic production thereof) and lack of targeted financing. Introducing appropriate financial incentives would be key to successful RES promotion. Setting up appropriate institutional support for the development and implementation of RES projects and a RES fund aimed at providing support to development and implementation of RES projects – should be another priority. Public awareness campaigns demonstrating benefits of implementation of RES facilities and targeted training curricula for the concerned population groups would also need to be considered.

Energy Efficiency

With high levels of energy intensity and relative dependence on energy imports (50% of primary energy use), the promotion and implementation of energy efficiency (EE) measures in all sectors of the economy are essential. Residential buildings sector is the largest energy end-user in the Kyrgyz Republic (it represents almost 42% of the final national energy consumption). At the same time, the residential building sector offers one of the largest energy saving potential with over 20,100 TJ up to 2025 and another 10,000 TJ up to 2050. Investment opportunities needed to realise the energy saving potential are estimated at approximately €12 billion. These investments are associated with improvement of existing housing stock up to the level required by the new building regulations. Energy prices are heavily subsidised both in terms of allowances to residents and by direct subsidies in form of tariffs set below cost recovery levels.

The target for energy savings set in the Energy Saving Programme is 1.2 million tons of standard fuel by 2015. The Energy Savings Law provides the basic legal framework for the sector, including the requirements to conduct energy audits. However, the overall sector regulation until recently remained scarce and insufficient. A large step forward was made in 2011, when the government adopted the Law on Energy Performance of Buildings (the “EPB Law”), which effectively transposes the EU Directive on Energy Performance of Buildings. The EPB Law was developed with the EBRD technical assistance and entered into force in February 2012. In September 2012, the EPB Law was supplemented by a number of supporting regulations also developed with the EBRD technical assistance. These include, among others, introduction of minimum energy efficiency requirements for new developments and major renovations of all types of buildings, energy performance assessment methodology, energy performance certification, regular inspections on commercial basis, and obligation of national authorities on monitoring and recording of energy performance certificates. This marks the first instance of a post-Soviet country adopting EE legislation on buildings compatible with the EU Directives and the international ISO EN standards.

The EBRD has provided further support to the national authorities with harmonisation of the technical standards/rules (SNIPs) with the new building legislation as well as some capacity building support and tools for implementation of the new legislation.

The Kyrgyz Republic ratified the Kyoto Protocol to the United Nations Framework Convention on Climate Change in May 2003.

Further to assisting with the development of the EPB legislation, the EBRD has provided assistance to national authorities with the implementation of the adopted legislation, appropriate revision of the technical standards and some capacity building. EE in other sub-sectors (energy, industry, transport) is still poorly developed, lacking appropriate policy instruments, financial incentives and relevant implementing regulations.

The recent legislative reform with respect to energy performance of buildings shows the government's commitment to harmonise the national framework with EU legislation. Reform efforts could be enhanced by upgrading the EE legislative framework for other sectors (transport, industry). Establishment of an independent EE agency and an EE-dedicated fund would contribute to the implementation of energy saving measures. ESCO models for financing EE improvements in public buildings should be considered. Strengthening capacity of public officials, residents (homeowners' organisations) and market participants as well as holding an awareness campaign promoting benefits of increasing EE in all sectors should be part of the government's reform agenda. To stimulate EE and RE development, the government should begin to phase out energy subsidies putting in place proper safety net mechanisms for vulnerable customers.

ANNEX 5 – GENDER PROFILE

Human Development and Gender Inequality

According to the UNDP Human Development Index (HDI), in 2013 the Kyrgyz Republic ranked 125th out of 187 countries. The HDI is comprised of three dimensions: health, education and gross national income. Within Central Asia countries, Uzbekistan and Tajikistan are the closest to the Kyrgyz Republic in terms of level of human development, ranking 116th and 134th respectively. The Kyrgyz Republic ranks 64th out of 149 countries in terms of the UNDP Gender Inequality Index (GII, based on reproductive health, empowerment and economic activity).

Labour force participation and Gender pay gap

According to the National Statistics Committee of the Kyrgyz Republic, economic activity rate was 51.8 per cent for women and 77.3 per cent for men in 2012. The gender gap in the labour force participation is even higher amongst the youth aged 15-28. For this age group, labour force participation is 38 per cent for women and 64 per cent for men. The unemployment rate was 9.5 per cent for women and 7.5 per cent for men. Men are more likely to be self-employed (31.8% of all male workers) as compared to women (18.3%), according to the World Bank.

The gender pay gap looking at differences in hourly earnings was 26.7 per cent in 2013, according to the Gender Statistics database of the United Nations Economic Commission for Europe (UNECE). The wage gap is underpinned by both vertical and horizontal segregation in the labour market. Women are concentrated in the public sector, which pays lower wages, while men tend to be concentrated in relatively better-paid sectors, including construction and transport as the table shows below.

Number of women and men employed in economy by types of economic activity, 2011)	Employees	
	% women	% men
Sector		
Construction	4	96
Transport and communications	10.7	89.3
Electric, gas and water	16.5	83.5
Mining	17.9	82.1
Extraterritorial organizations	20.0	80.0
Housekeeping services	35.4	64.6
Public administration	39.0	61.0
Operations with real estate, rent and consumer services	39.3	60.7
Financial services	45.8	54.2
Processing	47.5	52.5
Trade; repair of cars, home appliances	48.8	51.2
Municipal, social and personal services	56.0	44.0
Hotels and restaurants	63.9	36.1
Education	76.9	23.1
Health sector and social services	83.4	16.6

Source: UNFPA (2012) based on data from National Statistics Committee, 2011 (“Employment and Unemployment” Module of the Integrated Sample Survey of Households Budget and Labour)

According to the 2014 World Bank/IFC “Women, Business and the Law” report, women in the Kyrgyz Republic cannot engage in the following occupations in the same way as men do: construction, metalwork, factory work, jobs requiring lifting weights above the threshold and

jobs deemed hazardous. These restrictions in employment can affect women's economic opportunities as much as they influence women's incentives and abilities to get the job of their choice leading to their occupational segregation in the labour market.

Health, education and decision making in the public sphere

Disparities in higher education are relatively limited: 94.5 percent of women have reached at least a secondary level of education compared to 96.8 percent of their male counterparts. Of note, however is that there exist gender differences in the fields of study, which may be contributing to the occupational segregation in the labour force.

For every 100,000 live births, 71 women die from pregnancy related causes, twice the average of the EBRD's region of operation. This is due to *inter alia* a lack of access to medical services, lack of adequately trained health care workers, poor nutrition as well as lack of awareness of entitlements to healthcare.

23.3 percent of parliamentary seats are held by women - a higher share than the average of EBRD's countries of operations.

Entrepreneurship, access to finance

According to the OECD Social Institutions and Gender (SIGI) index, there is no legal discrimination against Kyrgyz women with regard to access to land. However, under land reforms introduced following the independence, land titles distributed following the break-up of collective farms were issued to households rather than individuals, and registered in the name of the household heads (mostly men). There is also widespread lack of awareness among women of their land rights. Under the family code, women and men have equal property rights in marriage, and when a couple marries, they must sign a marital contract stating the division of property between them. However, in rural areas in particular, the right of women to dispose of family property is often ignored, as under customary practices men own land and buildings, while women own moveable property within the home. In addition, legal protection is only accorded when the marriage has been registered.

According to the 2013 EBRD report "Legal barriers to women's access to credit: Morocco and the Kyrgyz Republic case studies"¹³, the formal lending regime in the Kyrgyz Republic is highly collateralised with banks generally requiring immovable collateral. Microfinance institutions tend to have a similar approach to collateral when it is required, but some 80 per cent of their lending is unsecured. As a result, there appears to be a gender gap within the market, which reflects the difficulties women face in moving from small loans with microfinance institutions to larger loans with commercial banks. The fact that 80% of recipients of micro-credit in the country are women may indicate that access to other forms of credit among women is difficult.

According to the Business Environment and Enterprise Performance Survey (BEEPS) 2013, 49.2 per cent of the 270 firms surveyed in the Kyrgyz republic had female participation in ownership, whereas 29% of firms had a female top manager. Women constituted 42.6% of permanent full-time workers and 11.3% of permanent full-time non-production workers.

¹³ The report was commissioned by the EBRD and prepared by the "Law and Development Partnership (LDP)"

ANNEX 6 – EBRD AND THE DONOR COMMUNITY

Donor funded technical cooperation (TC) in the Kyrgyz Republic has allowed the Bank to undertake early diagnostic work, including feasibility studies and preparation of investment opportunities, build capacities of prospective clients, in particular project implementation support in the infrastructure sector, and share transition experience from policy makers and private sector stakeholders from EBRD Countries of Operations in Central and Eastern Europe. In addition, the Kyrgyz Republic has benefited from non-TC grants from donors in the form of investment grants, incentive fees and guarantees.

Significant donor funds were provided to support projects in the municipal and environmental infrastructure (MEI), transport, energy sectors and have contributed to the growth of local private SMEs through a range of advisory and investment programmes, including the Business Advisory Services, the Enterprise Growth Programme, the Investment Councils and Local Currency Financing and Markets Initiative.

For the past four years, there has been an increased donor support in key MEI projects for water supply, public transport and, where possible, solid waste management with strong social and environmental benefits. The focus of donor grants is expected to remain in improving the basic infrastructure of urban areas in the Kyrgyz Republic. Additionally, donor funds are expected to support policy dialogue and legal transition with a view to helping the Government advance its reform agenda and building judicial capacity. Efforts will be made to ensure that donor funding benefits clients and end-beneficiaries in outer regions of the country to support regional inclusion.

To sustain these needs, the EBRD will rely on a number of donor funds administered by the Bank or managed externally, in addition to resources made available by its shareholders:

- **Multi-Donor Funds:**
 - **Early Transition Countries Fund (ETC Fund)** with contributions from 14 bilateral donors has financed projects in 11 countries for the last 10 years and the Kyrgyz Republic is one of the biggest recipients of these grants. ETC Fund will continue to provide TC grants across a range of sectors, focusing on priorities such as improving access to and delivery of affordable basic services in MEI, strengthening the financial sector and promoting private enterprise, in particular the SME sector.
 - **EBRD Water Fund** will support projects in municipal water and wastewater rehabilitation and framework TC projects.
- **Bilateral donors:** grants will be sought from donors through their bilateral donor who have expressed interest in supporting activities in the Kyrgyz Republic across sectors and activities such as business advice and municipal infrastructure. Historically, Switzerland has been a particularly active donor in the Kyrgyz Republic
- **The EU Investment Facility for Central Asia (IFCA)** will remain an important source of funding for TC and non-TC grants for Central Asia, mainly in support of investment operations co-financed with other IFIs in such sectors as environment, energy, and private sector development. For the next EU financial framework (2014 – 2020) it is likely IFCA funding will remain similar to the current level, i.e. EUR 20 million per annum (no pre-set allocation by country). It is understood that additional funding from the EU national programmes may be channelled through the IFCA. The 2014 - 2020 **EU**

National Programme in Kyrgyz Republic is likely to focus on three key areas: Rule of Law, Education, and Integrated Rural Development, which the Bank may try to access.

- **EBRD Shareholder Special Fund (SSF)** endowed by the Bank's net income. The SSF is a complementary facility to donor resources and will provide TC and non-TC support in areas where there is a shortage or lack of support, but where it remains as a priority area for the Bank to advance transition.
- **The Environmental Remediation Account for Central Asia:** a multilateral Account, initiated by the EU and managed by the EBRD, which will address the extensive legacy of uranium mining and processing in the Kyrgyz Republic, the Republic of Tajikistan and the Republic of Uzbekistan. The resources of the Account will be used to remediate high priority sites to protect the environment and the health of the local population and prevent potential cross-boundary contamination as well as strengthening Recipient Countries' capacity and legal framework in managing radioactive waste from mining and milling processes.