



Ex-post evaluation of Macro-Financial Assistance operation to the Kyrgyz Republic over the period 2013 - 2016

Final Report

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List of Abbreviations

ADB	Asian Development Bank
CPI	Consumer price index
CU	Customs Union
DCI	Development Cooperation Instrument
DFID	Department for International Development (UK)
DG DEVCO	Directorate-General for International Cooperation and Development
DG ECFIN	Directorate-General for Economic and Financial Affairs
DG ECHO	Directorate-General for European Civil Protection and Humanitarian Aid Operations
DIPECHO	Disaster-Preparedness ECHO
DPO	Development Policy Operations
DSA	Debt Sustainability Analysis
EACU	Eurasian Customs Union
EAEU	Eurasian Economic Union
EBRD	European Bank for Reconstruction and Development
ECF	Extended Credit Facility
EDB	Eurasian Development Bank
EEAS	European External Action Service
EEU	Eurasian Economic Union
EIB	European Investment Bank
EIDHR	European Initiative for Democracy and Human Rights
EIU	Economist Intelligence Unit
EU	European Union
EUR	Euro
EURASEC	Eurasian Economic Community
FATF	Financial Action Task Force
FDI	foreign direct investment
FMIS	Financial Management Information System
GDP	Gross Domestic Product
GIZ	Deutsche Gesellschaft für Internationale Zusammenarbeit

GSP+	Generalised Scheme of Preferences
GTAC	Governance Technical Assistance Credit
IBC	International Business Council
IcSP	Instrument contributing to Stability and Peace
IDA	International Development Association
IDB	Islamic Development Bank
IFCA	Investment Facility for Central Asia
IMF	International Monetary Fund
INTOSAI	International Organization of Supreme Audit Institutions
KGS	Kyrgyz som
KZT	Kazakhstani tenge
LGBTI	lesbian, gay, bisexual, transgender, and intersex
MDBF	Medium Term Budget Framework
MDTF	Multi-Donor Trust Fund
MFA	Macro Financial Assistance
MTDS	Medium Term Development Strategy
NBKR	National Bank of the Kyrgyz Republic
NSI	Nuclear Safety Instrument
NSSD	National Strategy for Sustainable Development
OA	Operational Assessment
OSCE	Organization for Security and Cooperation in Europe
PCA	Partnership and Cooperation Agreement
PEFA	Public Expenditure and Financial Accountability
PFM	Public Finance Management
PIP	Public Investment Programme
RCF	Rapid Credit Facility
RIP	Regional Indicative Programme
RUR	Russian Ruble

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SDPK	Social Democratic Party of Kyrgyzstan
	Special Drawing Rights
SDR	
SECO	State Secretariat for Economic Affairs
SIA	Social Impact Analysis
SIDA	Swedish International Development Cooperation Agency
SRC	Sector Reform Contracts
TAF	Technical Assistance Facility
US	United States
USAID	United States Agency for International Development
USD	United States Dollars
VAT	Value Added Tax
WB	World Bank
WTO	World Trade Organization

Abstract

The Kyrgyz economy faced pronounced economic difficulties in the wake of the 2008 global financial crisis. These were further intensified owing to violent and widespread ethnic protests that erupted in mid-2010 and growing political instability. Against this background, the European Commission, among other major international donors, announced the mobilisation of EUR 118 million of assistance through various instruments, including a EUR 30 million package of macro-financial assistance (MFA). The MFA was disbursed in full, in two instalments, over the period June 2015 - April 2016. The MFA disbursements were linked to the fulfilment of seven reform conditions pertaining to the areas of public finance management, finance, trade, and investment.

This study constitutes an evaluation of the EU MFA to the Kyrgyz Republic. Specifically, it investigates and analyses the extent of the programme's relevance, effectiveness, efficiency, EU added value and coherence. The study draws on evidence gathered through a multi-methods approach, comprising both quantitative and qualitative research techniques. The study concludes that the EU MFA was relevant, coherent, effective and efficiently implemented. In addition, the MFA instrument provided the EU with added leverage to prevent the enactment of two highly-contested legislations – the 'anti-LGBTI' and 'foreign agents' laws.

Acknowledgements

The authors would like to express their sincere thanks to all those who contributed to this study, especially all the interviewees who generously gave time both in the interviews and, in many cases, with follow-up materials and responses to questions.

Аннотация

Экономика Кыргызстана столкнулась с серьезными экономическими трудностями вследствие глобального финансового кризиса 2008 года. Они еще более усугубились из-за широко распространенных этнических протестов, вспыхнувших в середине 2010 года и принявших насильственные формы, и возросшей политической нестабильности. В контексте сложившейся ситуации Европейская комиссия, наряду с другими крупными международными донорами, объявила о мобилизации 118 миллионов евро в виде различных финансовых инструментов, включая пакет макрофинансовой помощи (macro-financial assistance, MFA) в размере 30 миллионов евро. Макрофинансовая помощь была полностью выплачена двумя частями в период с июня 2015 года по апрель 2016 года. Получение пакета макрофинансовой помощи было увязано с выполнением семи условий по проведению реформ, касающихся управления государственными финансами, финансов, торговли и инвестиций.

Это исследование представляет собой оценку макрофинансовой помощи, предоставленной ЕС Кыргызской Республике. В частности, в нем исследуется и анализируется степень целесообразности программы, ее действенности, эффективности, обоснованности и дополнительные ценности для ЕС. Исследование опирается на доказательства, полученные в результате применения многостороннего подхода, включающего как количественные, так и качественные методы исследования. В исследовании сделан вывод о том, что макрофинансовая помощь ЕС была целесообразной, обоснованной и реализовывалась эффективно. Кроме того, этот пакет макрофинансовой помощи предоставил ЕС дополнительные преимущества в виде предотвращения принятия двух крайне спорных законодательных актов — «анти-ЛГБТИ» и в отношении «иностранных агентов».

Благодарность

Авторы выражают искреннюю благодарность всем, кто внес вклад в это исследование, особенно всем людям, давшим интервью и во многих случаях впоследствии предоставившим материалы и ответы на вопросы.

*Ex-post evaluation of Macro-Financial Assistance operation to the Kyrgyz Republic over
the period 2013 - 2016*

1 Executive Summary

This report presents the results of the ex-post evaluation of the Macro-Financial Assistance operation provided to Kyrgyzstan over the period 2015 - 2016. The evaluation was commissioned by the Directorate-General for Economic and Financial Affairs (DG ECFIN). The work was undertaken by ICF in collaboration with Cambridge Econometrics and two local independent experts based in Bishkek specialising in economics and current affairs.

1.1 Background to the MFA operation in Kyrgyzstan

Kyrgyzstan's economy was badly affected by the 2008-9 global financial crisis. Growth decelerated sharply in 2009 (from 7.6 per cent in 2008 to 2.9 per cent in 2009) as a result of several external shocks. The events of April and June 2010¹ further disrupted economic activity during the year (the economy contracted by 10 percent in the second quarter of 2010) and fuelled the need to increase public spending on reconstruction and social assistance. This in turn resulted in significant balance of payments and budgetary financing needs.

Against this background, an international donors' conference was organised in Bishkek in July 2010. Donors pledged US\$1.1 billion in assistance over a period of 18 months to help the Kyrgyz Republic deal with the consequences of the 2010 events. The European Commission, among the major donors, announced the mobilisation of EUR 118 million of assistance through various instruments including MFA of EUR 30 million.

The MFA was intended to "*contribute to help the Kyrgyz Republic to address the lingering economic consequences of the global recession and of the ethnic conflict. It would reduce the short-term financial vulnerability still faced by the economy, while supporting reform measures (including those in the International Monetary Fund (IMF) and World Bank (WB) programmes) aimed at achieving a more sustainable balance of payments and budgetary situation over the medium-term*"². The use of the MFA instrument was exceptional in this case as Kyrgyzstan does not fall within the classical geographical scope of the MFA instrument (consisting of candidate and potential candidate countries and countries bordering the EU covered by the European Neighborhood Policy)³. In the 2011 ex-ante evaluation⁴, the use of the MFA instrument in Kyrgyzstan was justified "*...by the strength of the political and economic reform momentum in the country and by its position in a region of strategic economic and political importance for the EU*". The operation thus, went beyond purely macro-economic considerations and had a strong political dimension.

The MFA was disbursed in full, in two instalments, over the period June 2015 - April 2016:

- The first instalment comprised: a EUR 10 million grant (disbursed in June 2015) and a EUR 5 million loan (disbursed in October 2015);
- The second instalment comprised: a EUR 5 million grant (disbursed in February 2016) and a EUR 10 million loan (disbursed in April 2016).

The disbursement under the MFA operation was, *inter alia*, dependent on the satisfactory fulfilment of seven reform conditions that focused on the following areas:

¹ In April 2010, a popular uprising toppled the previous regime and violent inter-ethnic clashes broke out in the south of the country in June 2010 resulting in hundreds of deaths. In the wake of the violence, 75,000 people fled to neighbouring Uzbekistan and a further 300,000 were displaced inside the country,

² European Commission. 2011. Ex-ante evaluation statement on EU macro-financial assistance to the Kyrgyz Republic.

³ https://ec.europa.eu/info/business-economy-euro/economic-and-fiscal-policy-coordination/international-economic-relations/macro-financial-assistance-mfa-non-eu-partner-countries_en

⁴ EC(2011) Ex-ante evaluation statement on EU macro-financial assistance to the Kyrgyz Republic, SEC(2011) 1619 final. Available at: <http://eur-lex.europa.eu/legal-content/EN/ALL/?uri=CELEX:52011SC1619>

- Public Finance Management (four conditions);
- Financial Sector (one condition);
- Trade Policy (one condition);
- Investment and Business Environment (one condition).

1.2 Purpose of the evaluation

This evaluation assesses, ex post, the contribution of the MFA facility to the macro-economic and structural adjustment of Kyrgyzstan. In so doing it examines:

- Whether the ex-ante considerations determining the design and terms of the operation were appropriate, taking due account of the economic, political and institutional context; and
- Whether the outcome of the programme met the intended objectives which were both macroeconomic and political in nature.

1.3 Methodology

This evaluation was based on a mixed-methods approach and was carried out in line with the requirements set out in the Better Regulation guidelines. It relied on various qualitative and quantitative techniques to establish a comprehensive evidence base for the evaluation and to provide the basis for triangulation of results. The following methods were used to build the evidence base for the evaluation:

- **Desk research**, entailing a review and analysis of all relevant literature, official documentation and macroeconomic data;
- **Semi-structured interviews with key stakeholders**, of which a number were undertaken face-to-face during the course of missions to Bishkek and Washington D.C. Interviews were held with relevant staff from the European Commission, the EU Delegation to Kyrgyzstan in Bishkek, officials from the relevant ministries and agencies in Kyrgyzstan (including the Ministry of Finance and the National Bank of the Kyrgyz Republic), representatives of local civil society organisations and the business community, and representatives from international financial institutions (IMF and the WB) as well as key bilateral donors;
- **Internal brainstorming session on counterfactual scenarios**, that took place at the initial stage of the evaluation and involved the core members of the ICF and Cambridge Econometrics teams as well as the local economist;
- **A focus group with various development partners**, including representatives from the European Investment Bank (EIB), Asian Development Bank (ADB), World Bank (WB) and Deutsche Gesellschaft für Internationale Zusammenarbeit (GIZ) (all based in Bishkek);
- **A debt sustainability analysis (DSA)**, assessing the sustainability of the Kyrgyz Republic's public debt before and after the MFA operation; and
- **A social impact analysis (SIA)**, examining the extent to which the MFA potentially cushioned the social impact of the crisis.
- A **validation workshop**, hosted on Commission premises on January 15, 2019. The workshop was attended by European Commission representatives, members of the ICF project team, and various Kyrgyz stakeholders. The aim was to discuss the study findings and recommendations for future MFA operations.

1.4 Findings and conclusions of the evaluation

1.4.1 Relevance

1.4.1.1 Size of the assistance

The MFA disbursements accounted for about 0.3 per cent of Kyrgyzstan's GDP in 2015 and 2016 respectively. Further, it accounted for 14 per cent and 12 per cent of the

total assistance package (budget support financing exclusively) provided by multilateral and bilateral donors in 2015 and 2016 respectively. All things considered, the size of the assistance was judged appropriate, given the country's financing needs as well as the criteria governing the use of the MFA instrument.

1.4.1.2 Form of the assistance

The MFA operation comprised a 50-50 split between grants and loans, reflecting the compromise reached between the Council of the European Union (who strongly opposed grant-only financing to Kyrgyzstan) and the European Parliament (who were more in favour of grants). The concessional financing terms and un-earmarked character of the MFA package constituted important attributes that were positively received by the Kyrgyz authorities. Additionally, there was no substantive evidence of the loan component of the MFA having negatively impacted on the country's debt sustainability position. The form of the MFA could therefore be deemed appropriate.

1.4.1.3 Timing of disbursements

There were significant delays in the approval and implementation of the operation. The assistance was requested in 2010 and was eventually disbursed over 2015-16. Although the MFA disbursements took place much later than envisaged, the operation was still relevant as the Kyrgyz economy was negatively impacted by a sharp fall in exports to Russia (2015) and an important contraction in gold production (2016). This was, however, by coincidence and not by design.

1.4.1.4 Conditionalities associated with MFA support

The MFA reform package targeted structural weaknesses and vulnerabilities affecting the Kyrgyz economy. The MFA conditions were generally in line with the priorities set by the Kyrgyz government as well as other donors / IFIs (as part of their support programmes). These were also consistent with wider objectives associated with EU MFA operations, notably to promote structural measures/reforms capable of driving and maintaining macroeconomic stability.

The pace of reform implementation was swift, with six out of the seven conditions having been met prior to the Memorandum of Understanding (MoU) being approved, signed and ratified. It is not uncommon for national authorities to commence implementation of (or even fulfil) MFA conditionalities before the MoU is signed. This may be to speed up the disbursement of successive tranches (which are linked to the fulfilment of the reforms). However, in the Kyrgyz context, several stakeholders argued that the fulfilment of MFA conditionalities prior to the signature of the MoU, *de facto* made the conditionalities redundant and was tantamount to handing 'free' money to the Kyrgyz authorities and believed that negotiations with the Kyrgyz authorities should have been re-opened and updated. In our view, these arguments are misplaced as such an approach would prevent authorities from embarking upon essential reforms until the MoU is signed. Moreover, in the Kyrgyz context, this was not desirable and judged potentially harmful. Renewed negotiations would have entailed new rounds of consultation with the Member State Committee as well as relevant Kyrgyz stakeholders, creating further unnecessary delays.

Overall, the MFA-induced reform package is judged to be relevant, notably in terms of the political, economic and institutional conditions that prevailed in Kyrgyzstan at the time of the negotiations.

1.4.2 Effectiveness

Effectiveness was measured through two strands of analysis: (1) the role and contribution of the MFA in promoting macroeconomic stabilisation; and (2) the extent of progress achieved in terms of the implementation of structural reforms, notably the specific policy actions attached as conditions for the disbursement of the assistance and as specified in the MoU for the MFA.

1.4.2.1 Role and contribution of the MFA in promoting macroeconomic stabilisation

With the disbursements corresponding to circa 0.3 per cent of GDP in 2015 and 2016 respectively, the EU MFA was not negligible and contributed to the stabilisation of the Kyrgyz economy.

In the absence of the EU MFA ('Scenario 1'), the Kyrgyz government could potentially have resorted to other options. More concretely, it could have withdrawn some of its reserve deposits at the central bank, undertaken cuts in public expenditure (notably among 'unprotected categories' of public spending), and/or sought increased assistance from Russia. These measures would have allowed for the expected negative impact on aggregate demand to be contained, with ultimately a reduced impact on GDP and economic growth.

The hypothetical absence of both the EU MFA and IMF support programme ('Scenario 2') would have had far more severe implications. This is because the absence of the IMF Extended Credit Facility (ECF) programme would have most certainly affected the WB's readiness to provide budget support to Kyrgyzstan. As a result, if the assistance associated with the EU MFA, the IMF ECF and the WB DPO(s) provided in 2015 had not actually materialised, this would have corresponded to USD 62 million, or approximately 1 per cent of GDP in 2015 only. In this instance, the options available to the Kyrgyz government to close this financing gap would have been very similar to those presented under 'Scenario 1,' though its size would have most certainly required deeper public cuts. Ensuing impacts on domestic prices, households' disposable incomes and foreign direct investment (FDI) would have been more severe.

In parallel, the absence of the IMF ECF would have meant that some of the reforms initiated by the programme would not have been implemented and, consequently, the technical assistance and disciplining role of the IMF, in terms of reform implementation, would have been absent.

1.4.2.2 Progress achieved in terms of the implementation of structural reforms

Overall, *sensu stricto*, Kyrgyz Republic fulfilled the economic and structural policy conditions related to the disbursement of the MFA in a satisfactory way. The evidence gathered suggests that the MFA support package brought about additional impetus for reform in priority areas, encouraging the implementation of specific, short-term, measures that may have otherwise been overlooked or further delayed by national authorities. The focus of reform priorities under the EU MFA was also closely aligned to those set by other important donors (e.g. IMF, WB).

The fact that most of the MFA conditions had been fulfilled by the time of the approval and signature of the MoU (in late 2013 and 2014 respectively), however, evoked the possibility for re-negotiations among stakeholders consulted during the study. Re-opening discussions around the MFA reforms could nonetheless have amplified political tensions that prevailed at the time between the Kyrgyz government and the EU, as a result of the numerous delays that surrounded the approval of the MFA and its subsequent disbursement. Additionally, the MFA (in the Kyrgyz context) bore greater political, rather than economic, significance. Re-negotiations could have undermined the EU's political goodwill and defeated the true purpose of the MFA operation.

Finally, although not initially envisaged, the MFA conferred added leverage to the EU in its discussions of the 'anti-lesbian, gay, bisexual, transgender, and intersex (LGBTI)' and 'foreign agents' bills with the Kyrgyz authorities.

1.4.3 Social impact

The MFA operation in Kyrgyzstan primarily served a political purpose. This, along with the absence of any explicit social conditions in the MoU suggest that the MFA

operation did not intend to bring about any significant social impact. However, even though the MFA instrument did not explicitly target particular areas of social development, it is worth highlighting the crucial role it played, alongside other stakeholders (notably civil society), in preventing the enactment of the 'foreign agents' and 'anti-LGBTI' bills.

1.4.4 Debt sustainability

In the event that the MFA had not been disbursed, Kyrgyzstan's debt sustainability would not have been impacted much. This is, in part, because of the size of the MFA and the fact that the delay between the 2011 announcement of the operation and the 2015/16 disbursements limited any confidence gains for the Kyrgyz economy. Conversely, had both the MFA and IMF financing not been provided, this would likely have negatively affected confidence in the Kyrgyz economy and the impact of reforms that were implemented as part of the IMF support package. Overall, the public debt outlook in Kyrgyzstan following the MFA operation has been, and is expected to remain, stable.

1.4.5 Efficiency

1.4.5.1 Design of the MFA operation

Concerted efforts between the EU and other key donors, notably the IMF and WB, helped signal the desired reform steer to Kyrgyz authorities in priority areas. Additionally, there were no specific contradictions between the MFA conditionalities and national policies.

1.4.5.2 Implementation of the MFA operation

The monitoring of the operation was deemed appropriate and proportional. Formal and regular missions constituted an important channel of dialogue between the Commission, the EU Delegation to the Kyrgyz Republic, and Kyrgyz authorities, ensuring the operation was running as smoothly and efficiently as possible.

1.4.6 EU added value

EU added-value was most apparent in, firstly, reinforcing structural reforms in several priority areas. Secondly, the MFA operation is likely to have had a significant positive impact on bilateral political relations. As such, it (coincidentally) came at a politically-important moment ahead of parliamentary elections when the country was also experiencing economic difficulties. Thirdly, the size of the MFA operation (EUR 30 million) corresponded to about 0.3 percent of Kyrgyzstan's GDP in 2015 and 2016 respectively – not a negligible amount. Fourthly, though the MFA operation was not designed to promote social reform directly, it provided the EU with (added) leverage to prevent the enactment of the highly-contested 'anti-LGBTI' and 'foreign agents' laws.

With the numerous procedural delays encountered, however, the EU added value was arguably reduced. The MFA's added contribution, notably in terms of boosting the EU's external image and reiterating its commitment to supporting the Kyrgyz authorities in their reform efforts, would thus appear to have been negligible in the long-term, in particular in comparison with the EU's Development Cooperation Instrument.

Overall, the MFA did provide some added value, but this was hampered by the exceptionally long time needed to implement the operation.

1.4.7 Coherence

The MFA was aligned with the principles set out in the Partnership and Cooperation Agreement (PCA) signed between the EU and Kyrgyz Republic which provides an overarching legal framework for cooperation and bilateral relations between the two countries. The MFA conditionalities / reforms were designed to be coherent with the objectives of the operation as well as other EU and international donor support

programmes, notably in the PFM and banking areas. As such, the MFA operation was both, internally as well as externally coherent.

1.5 Recent developments

The EU-MFA, coupled with the IMF's ECF arrangements, has enabled Kyrgyzstan to make substantial progress in strengthening its fiscal and external situation. Growth performance between 2016 and 2017 has been satisfactory, averaging at about 5 per cent annually. A different picture has nonetheless been observed for 2018. Economic performance/growth has been well below average and is predicted to be in the order of 2-3 per cent. The medium-term growth prospects for the country have thus been reduced owing to various exogenous factors, including a relatively slow recovery of the Russian economy, difficulties in attracting foreign direct investments, etc. On the basis that such trends are likely to persist into the coming years, annual growth rates are expected to be lower over the period 2019 - 2021, at an average of 4.0 to 4.1 per cent per annum⁵. Going forward, fiscal consolidation remains an issue and, thus, an important priority for the government. In September - October 2018, the IMF mission visited the Kyrgyz Republic and started negotiations on the possibility of having a new programme. Meanwhile, the EU continues to provide substantial aid to the Kyrgyz Republic, notably through three budget support programmes in the areas of: (1) rule of law (EUR 13.5 million); (2) education (EUR 70 million); and (3) integrated rural development/social protection and public finance management (EUR 30 million). Other budget support assistance continues to come from Russia, the WB, and the ADB.

1.6 Recommendations

There are three main recommendations emerging from this evaluation:

- *Recommendation 1*: In instances where: (1) an MFA operation deviates from the general principles of the instrument, for example in a country beyond the usual geographical scope; (2) the objectives of the operation go beyond economic stabilisation considerations; and / or (3) the assistance in relative terms is small, then in such circumstances an alternative evaluation framework should be considered, in line with the general Better Regulation principle of proportionality. In such instances, there are a number of opportunities to better calibrate the evaluation framework to address the factors affecting the level of analysis of the MFA operation.
- *Recommendation 2*: An indicative timetable, outlining the timing and responsibilities for the different stages of the MFA process, could be negotiated and provided upfront to the authorities in the beneficiary countries to help manage expectations.
- *Recommendation 3*: The Commission's ex-ante assessment could provide a more detailed assessment of the expected added value of the MFA operation (at various levels – financial, social, etc.) in line with the EU's latest guidance on added value (COM (2018) 490: 'The principles of subsidiarity and proportionality: Strengthening their role in the EU's policymaking').

⁵ Source: Official Medium-Term Forecast of the Social and Economic Development of the Kyrgyz Republic

2 Краткое резюме

В этом отчете представлены результаты оценки фактической эффективности макрофинансовой помощи, предоставленной Кыргызстану в период с 2015 по 2016 гг. Оценка была инициирована Генеральным директоратом по экономике и финансам (Directorate-General for Economic and Financial Affairs, DG ECFIN). Работа была проведена консалтинговой компанией ICF в сотрудничестве с компанией Cambridge Economics и двумя местными независимыми экспертами из Бишкека, специализирующимися на экономическом анализе и анализе текущей ситуации.

2.1 Основные сведения о предоставлении макрофинансовой помощи Кыргызстану

Экономика Кыргызстана сильно пострадала от глобального финансового кризиса 2008-2009 гг. В результате внешних потрясений в 2009 году темпы экономического роста резко снизились (с 7,6 процента в 2008 году до 2,9 процента в 2009 году). События апреля и июня 2010 года⁶ еще больше подорвали экономическую активность (экономика сократилась на 10 процентов во втором квартале 2010 года) и вызвали необходимость увеличить государственные расходы на реконструкцию и социальную помощь. Это, в свою очередь, привело к значительному росту потребностей в области платежного баланса и бюджетного финансирования.

В связи со сложившейся ситуацией в июле 2010 года в Бишкеке была организована международная конференция доноров. Доноры обязались предоставить 1,1 миллиарда долларов США в виде помощи в течение 18 месяцев, чтобы помочь Кыргызской Республике справиться с последствиями событий 2010 года. Европейская комиссия, наряду с другими крупными донорами, объявила о мобилизации 118 миллионов евро в виде различных финансовых инструментов, включая пакет макрофинансовой помощи (macro-financial assistance, MFA) в размере 30 миллионов евро.

Пакет макрофинансовой помощи был призван *«содействовать Кыргызской Республике в преодолении затяжных экономических последствий мирового экономического спада и локального этнического конфликта. Он позволит уменьшить краткосрочную финансовую уязвимость, с которой все еще сталкивается экономика страны, и поддержать меры по реформированию (в том числе в рамках программ Международного валютного фонда (МВФ) и Всемирного банка (ВБ)), направленные на достижение более устойчивого платежного баланса и бюджетного финансирования в среднесрочной перспективе»*⁷. В этом случае использование пакета макрофинансовой помощи было исключением, поскольку Кыргызстан обычно не попадает в географический охват предоставления макрофинансовой помощи (куда входят страны-кандидаты в члены ЕС, потенциальные страны-кандидаты и страны, граничащие с ЕС, на которые распространяется Европейская политика соседства)⁸. В итогах проведения в 2011 году оценки ожидаемой эффективности⁹ использование пакета макрофинансовой

⁶ В апреле 2010 года в результате народного восстания был свергнут предыдущий режим, а в июне 2010 года на юге страны произошли жестокие межэтнические столкновения, в результате которых погибли сотни людей. В результате этих вспышек насилия 75 000 человек бежали в соседний Узбекистан, а еще 300 000 человек были перемещены внутри страны.

⁷ Европейская комиссия, 2011 г. Заявление об оценке ожидаемой эффективности предоставления макрофинансовой помощи ЕС Кыргызской Республике.

⁸ https://ec.europa.eu/info/business-economy-euro/economic-and-fiscal-policy-coordination/international-economic-relations/macro-financial-assistance-mfa-non-eu-partner-countries_en

⁹ ЕС (2011 г.), Заявление об оценке ожидаемой эффективности предоставления макрофинансовой помощи ЕС Кыргызской Республике, КЦББ (2011 г.) 1619, окончательная версия. Доступно по адресу: <http://eur-lex.europa.eu/legal-content/EN/ALL/?uri=CELEX:52011SC1619>

помощи в Кыргызстане было оправдано «... важностью политических и экономических реформ в стране и ее положением в регионе, имеющим стратегическое экономическое и политическое значение для ЕС». Таким образом, ситуация вышла за рамки чисто макроэкономических соображений и получила выраженный политический подтекст.

Макрофинансовая помощь была выплачена двумя частями в период с июня 2015 года по апрель 2016 года:

- Первый взнос состоял из гранта в размере 10 миллионов евро (выделенного в июне 2015 года) и кредита в размере 5 миллионов евро (предоставленного в октябре 2015 года).
- Второй взнос состоял из гранта в размере 5 миллионов евро (выделенного в феврале 2016 года) и кредита в размере 10 миллионов евро (предоставленного в апреле 2016 года).

Предоставление пакета макрофинансовой помощи, *inter alia*, зависело от удовлетворительного выполнения семи условий проведения реформ в следующих областях:

- управление государственными финансами (четыре условия);
- финансовый сектор (одно условие);
- торговая политика (одно условие);
- инвестиционная и деловая среда (одно условие).

2.2 Цель оценки

В рамках этой оценки оценивается фактическая эффективность предоставления Кыргызстану пакета макрофинансовой помощи с целью проведения там макроэкономических и структурных изменений. При этом рассматривается:

- Оправдались ли предварительные прогнозы, определяющие структуру и условия предоставления помощи с учетом экономического, политического и институционального контекста страны.
- Были ли в результате реализации программы достигнуты поставленные цели, носившие как макроэкономический, так и политический характер.

2.3 Методология

При проведении этой оценки использовался смешанный подход, а также учитывались требования, изложенные в принципах лучшего регулирования (Better Regulation). Для создания комплексной доказательной базы и обеспечения основы для перекрестного анализа результатов применялись различные качественные и количественные методы. Для создания доказательной базы оценки использовались следующие методы:

- **Кабинетные исследования**, включающие обзор и анализ всей соответствующей литературы, официальной документации и макроэкономических данных;
- **Полуструктурированные интервью с ключевыми заинтересованными сторонами**, многие из которых были проведены при личном общении в рамках осуществления поездок в Бишкек и Вашингтон, округ Колумбия. Были проведены интервью с соответствующими сотрудниками Европейской комиссии, Представительства ЕС в Бишкеке, с должностными лицами соответствующих министерств и ведомств Кыргызстана (включая Министерство финансов и Национальный банк Кыргызской Республики), представителями местных организаций гражданского общества и деловых кругов, представителями международных финансовых институтов (МВФ и ВБ), а также с ключевыми донорами, предоставляющими финансовую помощь на двусторонней основе;

- **Внутренний мозговой штурм с использованием гипотетических сценариев**, который происходил на начальном этапе оценки с участием ключевых представителей компаний ICF и Cambridge Econometrics, а также местного экономиста;
- **Фокус-группа с участием различных партнеров по развитию**, в том числе представителей Европейского инвестиционного банка (ЕИБ), Азиатского банка развития (АБР), Всемирного банка (ВБ) и Немецкого общества международного сотрудничества (Deutsche Gesellschaft für Internationale Zusammenarbeit, GIZ) (все имеют представительства в Бишкеке);
- **Анализ приемлемого уровня задолженности (debt sustainability analysis, DSA)**, позволяющий определить приемлемый уровень государственного долга Кыргызской Республики до и после предоставления пакета макрофинансовой помощи; а также
- **Анализ социальных последствий (social impact analysis, SIA)**, исследующий степень, в которой пакет макрофинансовой помощи потенциально может смягчить социальные последствия кризиса.
- **Валидационный семинар**, проведенный в здании Комиссии 15 января 2019 года. В этом семинаре приняли участие представители Европейской комиссии, члены проектной группы компании ICF и различные заинтересованные стороны из Кыргызстана. Его цель состояла в том, чтобы обсудить результаты и выводы исследования и выработать рекомендации для предоставления пакета макрофинансовой помощи в будущем.

2.4 Результаты и выводы оценки

2.4.1 Целесообразность

2.4.1.1 Размер помощи

Выплаты в рамках пакета макрофинансовой помощи составили примерно 0,3 процента от ВВП Кыргызстана в 2015 и 2016 годах, соответственно. Кроме того, она составила 14 и 12 процентов от общего пакета финансовой помощи (только финансирование бюджета), предоставленной многосторонними и двусторонними донорами в 2015 и 2016 годах, соответственно. Принимая во внимание все обстоятельства, размер помощи был признан целесообразным, учитывая потребности страны в финансировании, а также критерии, регулирующие предоставление пакета макрофинансовой помощи.

2.4.1.2 Форма оказания помощи

Пакет макрофинансовой помощи состоял в соотношении 50 на 50 из грантов и кредитов, отражая компромисс, достигнутый между Европейским Советом (который решительно выступал против финансирования Кыргызстана исключительно за счет грантов) и Европейским парламентом (который склонялся к предоставлению грантов). Условия льготного финансирования и нецелевой характер пакета макрофинансовой помощи стали важными факторами, которые были положительно восприняты властями Кыргызстана. Кроме того, не было выявлено никаких существенных доказательств того, что кредитный компонент пакета макрофинансовой помощи отрицательно повлиял на положение страны с точки зрения приемлемого уровня задолженности. Таким образом, форма пакета макрофинансовой помощи может считаться целесообразной.

2.4.1.3 Сроки выплат

В процессе утверждения и реализации проекта происходили значительные задержки. Помощь была запрошена в 2010 г. и, в конечном итоге, выплачена в период с 2015 по 2016 гг. Несмотря на то, что выплаты макрофинансовой помощи производились намного позже, чем предполагалось, она все еще была актуальна, поскольку на экономику Кыргызстана негативно повлияло резкое сокращение

экспорта в Россию (2015 г.) и значительное сокращение добычи золота (2016 г.). Однако, это случилось по стечению обстоятельств, а не в соответствии с изначальным замыслом.

2.4.1.4 Условия предоставления макрофинансовой помощи

Условием предоставления макрофинансовой помощи была реализация пакета реформ, нацеленных на структурные недостатки и уязвимости, влияющие на экономику Кыргызстана. Условия предоставления макрофинансовой помощи в целом соответствовали приоритетам, установленным правительством Кыргызстана, а также другими донорами/МФИ (international financial institution [международное финансовое учреждение]) (в рамках их программ поддержки). Они также соответствовали более масштабным целям, связанным с предоставлением макрофинансовой помощи ЕС, в частности, содействию реализации структурных мер/реформ, призванных стимулировать и поддерживать макроэкономическую стабильность.

Реформы реализовывались быстрыми темпами: шесть из семи условий были выполнены еще до утверждения, подписания и ратификации Меморандума о взаимопонимании (MoV). Обычной практикой является то, что национальные органы власти начинают выполнение условий предоставления макрофинансовой помощи (или даже в полной мере выполняют их) еще до подписания MoV. Это может происходить с целью ускорения выплаты траншей (связанных с реализацией реформ). Однако в контексте ситуации в Кыргызстане некоторые заинтересованные стороны утверждали, что выполнение условий предоставления макрофинансовой помощи до подписания Меморандума о взаимопонимании *de facto* сделало эти условия бесполезными и означало передачу «свободных» денег кыргызским властям, и считали, что переговоры с кыргызскими властями следует возобновить. По нашему мнению, эти аргументы неуместны, так как такой подход не позволил бы властям приступить к существенным реформам до подписания Меморандума о взаимопонимании. Более того, в контексте ситуации в Кыргызстане это было нежелательным и даже потенциально вредным. Возобновление переговоров повлекло бы за собой новые раунды консультаций с Комитетом государств-членов ЕС, а также с соответствующими заинтересованными сторонами в Кыргызстане, что привело бы к дополнительным ненужным проволочкам.

В целом, пакет реформ, увязанный с предоставлением макрофинансовой помощи, признан целесообразным, особенно с учетом политических, экономических и институциональных условий, преобладающих в Кыргызстане в период ведения переговоров.

2.4.2 Эффективность

Эффективность измерялась посредством двух направлений анализа: (1) роль и последствия предоставления макрофинансовой помощи для стабилизации макроэкономической ситуации в стране; и (2) степень прогресса, достигнутого с точки зрения реализации структурных реформ, в частности, конкретных политических действий, предусмотренных в качестве условий для предоставления пакета макрофинансовой помощи и прописанных в Меморандуме о взаимопонимании.

2.4.2.1 Роль и последствия предоставления макрофинансовой помощи для стабилизации макроэкономической ситуации в стране

Размер выплат в рамках предоставления макрофинансовой помощи ЕС, соответствующий приблизительно 0,3 процента от ВВП в 2015 и 2016 годах соответственно, был довольно значительным и способствовал стабилизации экономики Кыргызстана.

В случае непредоставления пакета макрофинансовой помощи ЕС («Сценарий 1») правительство Кыргызстана потенциально могло прибегнуть к другим источникам финансирования. А конкретно, оно могло забрать некоторые из своих резервных депозитов из центрального банка, сократить государственные расходы (особенно «незащищенные категории» государственных расходов) и/или обратиться за помощью к России. Эти меры позволили бы минимизировать ожидаемое негативное влияние на совокупный спрос, что в конечном итоге привело бы уменьшению последствий для ВВП страны и к экономическому росту.

Гипотетическое непредоставление пакета макрофинансовой помощи ЕС и МВФ («Сценарий 2») имело бы гораздо более серьезные последствия. Это связано с тем, что отсутствие программы МВФ по выдаче пролонгированных кредитов (Extended Credit Facility, ECF) наверняка повлияло бы на готовность ВБ предоставить бюджетную поддержку Кыргызстану. Таким образом, если бы помощь ЕС, МВФ и ВБ, оказанная в 2015 году, не была фактически предоставлена, дефицит бюджета составил бы 62 миллионов долларов США, или примерно 1% ВВП только в 2015 году. В этом случае варианты, доступные правительству Кыргызстана для ликвидации этого дефицита, были бы очень похожи на варианты в «Сценарии 1», хотя, учитывая его размер, безусловно, потребовались бы более значительные сокращения государственных расходов. И последствия для внутренних цен, реальных доходов домохозяйств и прямых иностранных инвестиций (ПИИ) были бы более серьезными.

Помимо этого, непредоставление помощи МВФ означало бы, что некоторые из реформ, инициированных в рамках программы, не были бы реализованы, и, следовательно, техническая помощь и дисциплинирующая роль МВФ в области осуществления реформ не были бы задействованы.

2.4.2.2 Прогресс, достигнутый в сфере реализации структурных реформ

В целом, *sensu stricto*, Кыргызстан в удовлетворительной степени выполнил условия изменения экономической и структурной политики, связанные с выплатой макрофинансовой помощи. Собранные данные свидетельствуют о том, что пакет макрофинансовой помощи придал дополнительный импульс реформам в приоритетных областях, способствуя осуществлению конкретных краткосрочных мер, реализация которых в противном случае могла бы быть проигнорирована или еще более отсрочена национальными властями. Приоритетные области реформ в рамках пакета макрофинансовой помощи ЕС были тесно связаны с приоритетами других важных доноров (например, МВФ, ВБ).

Однако тот факт, что большинство условий предоставления макрофинансовой помощи были выполнены к моменту утверждения и подписания Меморандума о взаимопонимании (в конце 2013 и 2014 гг., соответственно), сделал вероятными повторные переговоры между заинтересованными сторонами, с которыми проводились консультации в ходе проведения исследования. Однако возобновление дискуссий о реформах, обусловленных предоставлением макрофинансовой помощи, могло бы усилить политическую напряженность, возникшую в то время между правительством Кыргызстана и ЕС в результате многочисленных задержек с утверждением пакета макрофинансовой помощи и его последующими выплатами. Кроме того, в контексте ситуации в Кыргызстане, предоставление макрофинансовой помощи имело больше политическое, чем экономическое значение. Возобновление переговоров могло бы подорвать политическую репутацию ЕС и помешать достижению истинной цели предоставления макрофинансовой помощи.

Наконец, хотя изначально это и не предполагалось, пакет макрофинансовой помощи предоставил ЕС дополнительные рычаги влияния на власти Кыргызстана при обсуждении законопроектов, направленных «против лесбиянок, геев, бисексуалов, трансгендеров и интерсексуалов (ЛГБТИ)» и «иностранных агентов».

2.4.3 Социальные последствия

Предоставление макрофинансовой помощи Кыргызстану в первую очередь преследовало политические цели. Это, наряду с отсутствием каких-либо явных социальных условий в Меморандуме о взаимопонимании, свидетельствует о том, что предоставление пакета макрофинансовой помощи не имело намерений оказывать какое-либо значительное социальное воздействие. Однако, несмотря на то, что пакет макрофинансовой помощи не был явно нацелен на какие-то конкретные области социального развития, стоит подчеркнуть крайне важную роль, которую он сыграл, наряду с другими заинтересованными сторонами (особенно гражданским обществом), в предотвращении введения в действие законов, направленных против «иностранных агентов» и «ЛГБТИ».

2.4.4 Приемлемый уровень задолженности

В случае непредоставления пакета макрофинансовой помощи приемлемый уровень государственного долга Кыргызстана изменился бы незначительно. Отчасти это связано с размером макрофинансовой помощи и тем фактом, что задержка между объявлением в 2011 году о намерении предоставить помощь и фактическими выплатами в 2015-2016 гг. не способствовала росту доверия к экономике Кыргызстана. И напротив, если бы пакет макрофинансовой помощи и помощь от МВФ не были бы предоставлены, это, вероятно, отрицательно сказалось бы на доверии к экономике Кыргызстана и на результатах реформ, осуществленных в рамках пакета макрофинансовой помощи. В целом, прогноз в отношении выплаты государственного долга Кыргызстаном после предоставления пакета макрофинансовой помощи является и, как ожидается, останется стабильным.

2.4.5 Действенность

2.4.5.1 Разработка пакета макрофинансовой помощи

Согласованные усилия ЕС и других ключевых доноров, в частности МВФ и ВБ, помогли указать властям Кыргызстана желаемый курс реформ в приоритетных областях. Кроме того, особых противоречий между условиями предоставления пакета макрофинансовой помощи и национальной политикой не было.

2.4.5.2 Реализация пакета макрофинансовой помощи

Мониторинг реализации пакета макрофинансовой помощи был признан соответствующим и надлежащим. Официальные и регулярные миссии являлись важными площадками для диалога между Комиссией, Представительством ЕС в Кыргызской Республике и властями Кыргызстана, обеспечившего, что предоставление пакета макрофинансовой помощи проходило максимально гладко и эффективно.

2.4.6 Дополнительная ценность для ЕС

Во-первых, дополнительная ценность для ЕС была наиболее очевидна в обеспечении проведения структурных реформ в нескольких приоритетных областях. Во-вторых, пакет макрофинансовой помощи, вероятно, оказал значительное положительное влияние на двусторонние политические отношения. Фактически предоставление помощи (по случайному совпадению) произошло в политически важный для страны момент перед парламентскими выборами, когда Кыргызстан также испытывал экономические трудности. В-третьих, размер макрофинансовой помощи МИД (30 млн евро) соответствовал примерно 0,3 процентам ВВП Кыргызстана в 2015 и 2016 годах соответственно, что немаловажно. В-четвертых, хотя пакет макрофинансовой помощи не был непосредственно направлен на содействие социальным реформам, он предоставил ЕС (дополнительные) рычаги для предотвращения принятия крайне спорных законов «анти-ЛГБТИ» и в отношении «иностранных агентов».

Однако из-за многочисленных процедурных задержек дополнительные преимущества для ЕС, возможно, уменьшились. Таким образом, дополнительные преимущества предоставления пакета макрофинансовой помощи для ЕС, особенно в том, что касается улучшения внешнего имиджа ЕС и подтверждения его приверженности поддержке кыргызских властей в проведении реформ, по-видимому, будут незначительными в долгосрочной перспективе, особенно по сравнению с программой ЕС «Сотрудничество в целях развития».

В целом, пакет макрофинансовой помощи действительно обеспечил ЕС некоторые дополнительные преимущества, но этому препятствовало исключительно долгое время, которое понадобилось для реализации проекта.

2.4.7 Обоснованность

Пакет макрофинансовой помощи был приведен в соответствие с принципами, изложенными в Соглашении о партнерстве и сотрудничестве (Partnership and Cooperation Agreement, PCA), подписанном между ЕС и Кыргызской Республикой и предоставляющем всеобъемлющую правовую основу для сотрудничества и двусторонних отношений между странами. Условия предоставления макрофинансовой помощи / реформы были разработаны таким образом, чтобы соответствовать целям проекта, а также других программ поддержки ЕС и международных доноров, особенно в области Управления государственными финансами (Public Finance Management, PFM) и в банковской сфере. Таким образом, предоставление макрофинансовой помощи было согласованным как на внутреннем, так и на внешнем уровнях.

2.5 Последние достижения

Пакет макрофинансовой помощи ЕС в сочетании с договоренностями о предоставлении помощи МВФ позволили Кыргызстану добиться существенного прогресса в улучшении своего финансового и внешнеполитического положения. Показатели роста в период с 2016 по 2017 год были удовлетворительными, составив в среднем около 5 процентов в год. Тем не менее, в 2018 году наблюдалась иная картина. Экономические показатели/темпы роста были значительно ниже среднего и, по прогнозам, в ближайшие годы составят порядка 2-3 процентов. Среднесрочные перспективы роста страны были невелики из-за различных внешних факторов, включая относительно медленное восстановление российской экономики, трудности в привлечении прямых иностранных инвестиций и т.д. Исходя из того, что эти тенденции, вероятно, сохранятся и в ближайшие годы, ожидается, что в период 2019–2021 гг. ежегодные темпы роста будут сниженными и составлять в среднем 4,0–4,1 процента в год¹⁰. В дальнейшей перспективе консолидация в налогово-бюджетной сфере также останется проблемой и, следовательно, важным приоритетом для правительства страны. В сентябре - октябре 2018 года миссия МВФ посетила Кыргызскую Республику и начала переговоры о возможности реализации новой программы. Между тем, ЕС продолжает оказывать существенную помощь Кыргызской Республике, в частности, посредством трех программ бюджетной поддержки в следующих областях: (1) верховенство закона (13,5 миллионов евро); (2) образование (70 миллионов евро); и (3) комплексное развитие сельских районов/социальная защита и управление государственными финансами (30 миллионов евро). Остальная финансовая поддержка по-прежнему поступает из России, ВБ и АБР.

2.6 Рекомендации

На основе этой оценки были сделаны три основные рекомендации:

¹⁰ Источник: Официальный среднесрочный прогноз социально-экономического развития Кыргызской Республики

- Рекомендация 1: В случаях, когда: (1) проект предоставления пакета макрофинансовой помощи отклоняется от общих принципов документа, например, реализуется в стране за пределами обычного географического охвата; (2) цели предоставления пакета макрофинансовой помощи выходят за рамки стабилизации экономического положения страны; и/или (3) финансовая помощь в относительном выражении невелика, в таких обстоятельствах следует рассмотреть альтернативную систему оценки в соответствии с общим принципом лучшего регулирования (Better Regulation) — соразмерность. В таких случаях существует ряд возможностей для усовершенствования калибровки системы оценки с целью учета всех факторов, влияющих на уровень анализа проекта по предоставлению макрофинансовой помощи.
- Рекомендация 2: Ориентировочный график предоставления пакета макрофинансовой помощи с указанием сроков и обязанностей на различных этапах проекта может быть заранее согласован и предоставлен властям стран-бенефициаров, чтобы надлежащим образом формировать ожидания.
- Рекомендация 3: Предварительная оценка Комиссии может давать более детальную оценку ожидаемых дополнительных преимуществ проекта по предоставлению пакета макрофинансовой помощи (на различных уровнях — финансовом, социальном и т.д.) в соответствии с последним руководством ЕС по дополнительным преимуществам (COM (2018) 490: «Принципы субсидиарности и пропорциональности: усиление их роли при формировании политики ЕС.»)

3 Introduction

3.1 This Report

This document constitutes the Draft Final Report as part of an independent, external *ex post* evaluation of the EU's Macro Financial Assistance (MFA) to the Kyrgyz Republic over the period 2013 – 16.

3.2 Scope of the evaluation

This evaluation focuses on the EUR30 million MFA operation approved and disbursed to Kyrgyzstan over the period October 2013 – April 2016. The operation took the form of a EUR15 million medium-term loan and a EUR15 million grant and was disbursed as follows:

- The first instalment, comprising EUR10 million in grant and EUR5 million in loan, was disbursed in June and October 2015 respectively;
- The second instalment, comprising EUR5 million grant and EUR10 million in loan, was disbursed in February and April 2016 respectively.

3.3 Purpose of the evaluation

The objective of this *ex-post* evaluation was:

- to analyse the impact of the MFA on the economy of Kyrgyzstan, and in particular, on the sustainability of its external position; and
- to assess the added value of the European Union's (EU) intervention.

Specifically, the evaluation seeks to draw lessons with respect to the EU's financial assistance, i.e.

- whether the *ex-ante* considerations, determining the design and terms of the operation were appropriate, taking due account of the economic, political and institutional context; and
- whether the outcome of the programme met the objectives.

The evaluation covers three main areas of analysis:

- the economic impact of the MFA operation on the economy of Kyrgyzstan;
- the value added of the EU intervention; and
- the sustainability of the country's external position as a result of the assistance.

These aforementioned areas have been assessed along the following criteria: (1) relevance; (2) effectiveness; (3) efficiency; (4) EU added-value; and (5) coherence with other EU policies.

Finally, the evaluation also comprises two additional strands of analysis that assess the impact of the MFA on the social sector and the public debt sustainability.

3.4 Structure of this report

The remainder of this report is structured as follows:

- **Section 2** provides an overview of the key economic and political developments in Kyrgyzstan during the period leading up to the crises that prompted the IMF-EU assistance as well as in the period over which the EU-MFA operation was implemented. It also provides a detailed description of the main characteristics of the MFA operation, including associated conditionalities;
- **Section 3** presents the methodological approach to the study, and outlines the main caveats and limitations;
- **Section 4** provides a brief update on economic developments and policy implementation since the completion of the MFA;

- **Sections 5 to 9** provide the assessment against each of the five evaluation criteria, including conclusions for each of them;
- **Sections 10 and 11** focus on the social impact and debt sustainability analyses respectively, and
- **Section 12** provides the conclusions.

The main report is supported by annexes, provided separately.

4 Context and content of the Macro-Financial Assistance to Kyrgyzstan during 2013 – 2016

4.1 Introduction to the analysis

This section describes the context and subject matter of the evaluation in the following sections:

- Section 4.2 describes the overall macroeconomic and political background that triggered the need for the MFA operation that was implemented during the period 2013 - 2016;
- Section 4.3 outlines key considerations behind the design of the MFA operation; and
- Section 4.4 outlines key macroeconomic developments during the implementation of the operation.

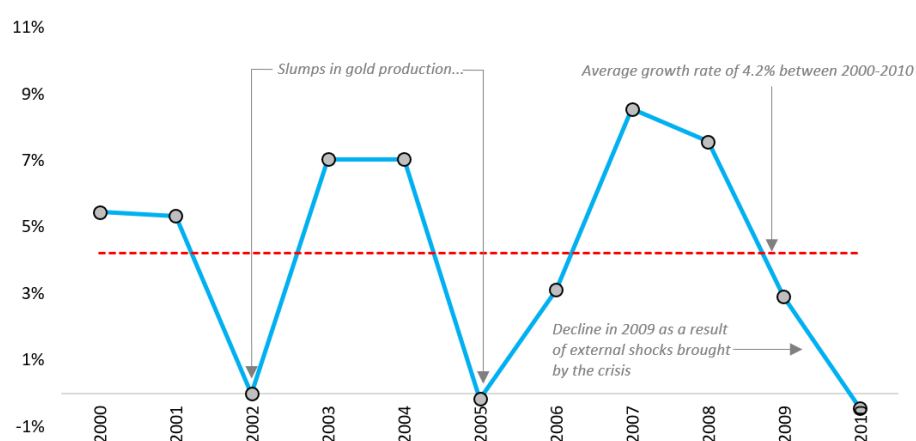
The analysis draws on the review of: (1) official documentation provided by DG ECFIN; (2) inputs from local experts based in Bishkek; and evidence gathered through stakeholder interviews conducted as part of the missions to Washington D.C and Bishkek (including *inter alia*, the national administration, Commission officials in DG ECFIN and the EU Delegation as well as experts from the IMF and the WB).

4.2 Economic and political context leading to the need for MFA operation

After a difficult period in the 1990s, Kyrgyzstan's economic situation substantially improved in the new millennium. Responsible macroeconomic policies, new opportunities and positive developments in the economies of neighbouring countries allowed for several years of solid economic growth (albeit still volatile) and significant poverty reduction.

In the 2000s, the country enjoyed relatively high economic growth. On average, real GDP grew by 4.2 per cent annually between 2000 and 2010 (Figure 1), though average growth rates observed among Kyrgyzstan's regional peers, (notably Kazakhstan, Tajikistan and Uzbekistan) were still much higher (9.3, 9.0 and 7.3 per cent respectively¹¹).

Figure 1. Kyrgyzstan economic growth between 2000 and 2010



Source: IMF data

Growth in the 2000s was driven by commercial services and, in particular, wholesale and retail trade, communication, financial services and tourism. The share of these

¹¹ World Bank, 2017. The World Bank Data. Available at: <https://data.worldbank.org/indicator/NY.GDP.MKTP.KD.ZG>

sectors in the national economy rose from 27 per cent in 1996 to 40 per cent in 2008¹². As a result of the liberalisation of customs regulations and the taxation regime for physical persons involved in international trade, Kyrgyzstan became a 'trade hub'¹³¹⁴. A growing Kyrgyz diaspora in Russia¹⁵ and parallel rapid increases in remittance inflows also furthered economic growth. In that regard, Kyrgyzstan currently ranks second in the world in terms of the share of national output that is accounted for by remittances (30 per cent as of 2016¹⁶). Nearly all inflows have been coming from Russia. Strong economic growth contributed to the reduction of poverty. As such, by 2010, 4.1 per cent of the country's population lived on less than USD 1.9 a day, down from 42.2 per cent in 2000¹⁷.

Kyrgyzstan's strong economic performance did not last. The 2008 global financial turmoil adversely affected GDP growth in 2009, albeit fairly moderately. Output growth declined from a buoyant 7.6 per cent in 2008 to 2.9 and -0.5 per cent in 2009 and 2010 respectively. This was largely due to external shocks, including a fall in remittances from migrant workers, lower demand for exports and shrinking foreign investments¹⁸.

In addition to the adverse impact entailed by the crisis, growing political instability further plunged Kyrgyzstan into an economic slowdown. As such, although President Bakiyev was re-elected in July 2009, European monitoring organisations (such as the OSCE) described the elections as significantly marred. Violent and widespread protests ensued in the following year. These demonstrations, known as the Second Kyrgyz Revolution, kick-started in the cities of Talas and Bishkek by opposition leaders who were protesting against rising government corruption and increased living expenses. The government of President Bakiyev was eventually overthrown in April 2010 and a new interim government, led by Roza Otunbayeva, was established.

Despite some temporary stabilisation, the conflict between ethnic Kyrgyz and Uzbeks escalated in early June 2010, to the extent that the newly-formed government introduced the state of emergency on June 12. The clashes resulted in over 400 people killed and more than 80,000 people displaced. They also led to a decline in tourism and agricultural activities as well as disruptions in trade (i.e. due to the temporary closure of most checkpoints at the borders, notably with Kazakhstan)¹⁹. Subsequently, the first half of the year was marked by a constitutional referendum on June 27, 2010, by which voters approved a new constitution. The act sought to limit

¹² Mogilevsky, R. and Omorova, A. 2011. Assessing Development Strategies to Achieve the MDGs in the Kyrgyz republic. Available at:

http://www.un.org/en/development/desa/policy/capacity/output_studies/roa87_study_kgz.pdf

¹³ Mogilevsky, R. and Omorova, A. 2011. Assessing Development Strategies to Achieve the MDGs in the Kyrgyz republic. Available at:

http://www.un.org/en/development/desa/policy/capacity/output_studies/roa87_study_kgz.pdf

¹⁴ There are two main markets serving this purpose: Dordoi market near Bishkek, the capital of the country, on the Kyrgyz-Kazakh border, and Kara-Suu market near Osh, the second large town, on the Kyrgyz-Uzbek border.

¹⁵ As of 2017 there were approximately half a million of registered Kyrgyz workers in Russia with approximately another half a million of undocumented ones.

¹⁶ World Bank, 2017. Personal remittances as % of GDP. Available at:

<https://data.worldbank.org/indicator/BX.TRF.PWKR.DT.GD.ZS?end=2016&locations=KG&start=2000>

¹⁷ World Bank, 2017. The World Bank Data. Available at:

<https://data.worldbank.org/topic/poverty?locations=KG>

¹⁸ European Commission, 2011. Ex-ante evaluation statement on EU macro-financial assistance to the Kyrgyz Republic.

¹⁹ Eventually, the second half of 2010 was still much better than expected. This was because of improved security, the return of political stability, better-than-expected agricultural performance, and a timely fiscal stimulus. See for instance: IMF, February 2011. Statement at the conclusion of the IMF Staff Mission to the Kyrgyz Republic. Available at: <http://www.imf.org/en/News/Articles/2015/09/14/01/49/pr1138>

presidential power and enhance the role of Parliament and the Prime Minister. The referendum also confirmed Otunbayeva as President until December 31, 2011. In October 2010, the Parliamentary elections were held, resulting in the formation of a governing coalition among three parties (Ata Jurt, SDPK, and Respublika), with Almazbek Atambayev as Prime Minister.

In addition to growth, the aforementioned events affected the performance of other key economic indicators. The public debt to GDP ratio, for instance, grew to 60 per cent in 2010 (Figure 2 overleaf), while fiscal deficit widened to -5.9 per cent of GDP in the same year reflecting the budgetary cost of the crisis-related spending and the impact of a weaker economic activity that resulted in lower tax revenues²⁰ (Figure 3).²¹ Current account balance also widened to -2.2 per cent, though still much smaller than in 2008, a deterioration driven mainly by the disruption in trade flows (Figure 5). Inflation, on the other hand, fell to 8 per cent in 2010, mainly as a result of the slowdown brought in by the crisis that entailed a dampening effect on prices (Figure 4).

Following the global economic crisis and inter-ethnic violence, a donor conference for the Kyrgyz Republic was organised in Bishkek in July 2010. A total of USD 1.1 billion was pledged and to be disbursed quickly (over the next 30 months). The main objective of this financial provision was to support essential public expenditures and services, to support social needs as well as to back critical investment (mostly in public infrastructure, energy and transport). This was around the same time when the President and the Minister of Finance of Kyrgyzstan formally requested the EU MFA to complement the financing available from the IMF, the details of which are outlined in subsequent sections.

²⁰ However, it was still much smaller deterioration than foreseen in August 2010 by the IMF in the context of the RCF programme (it projected a deficit of 12 per cent of GDP). This was largely due to some missing capacity to implement the reconstruction process.

²¹ EC. 2011. Ex-ante evaluation MFA to Kyrgyz Republic.

Figure 2. Public debt, in % of GDP, 2000 - 2010

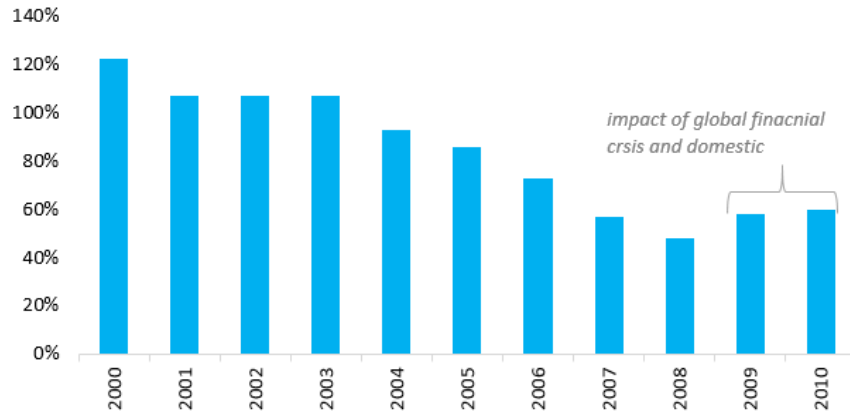


Figure 3. General government balance, in % of GDP, 2000 - 2010

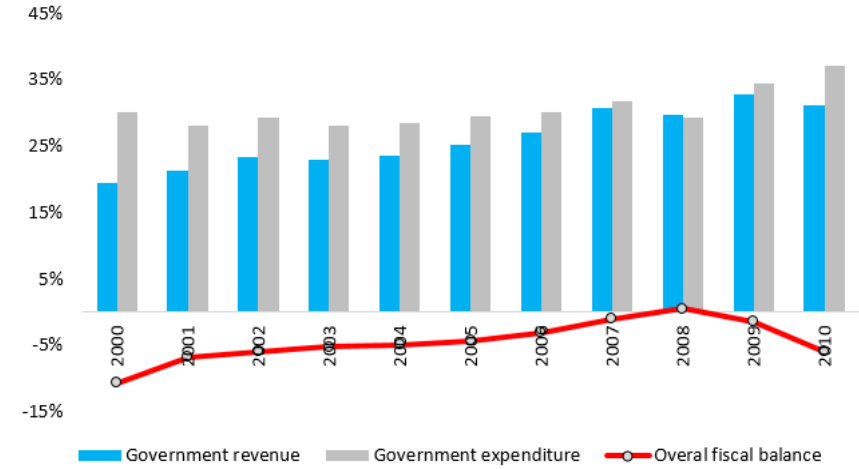


Figure 4. Inflation, 2000 - 2010

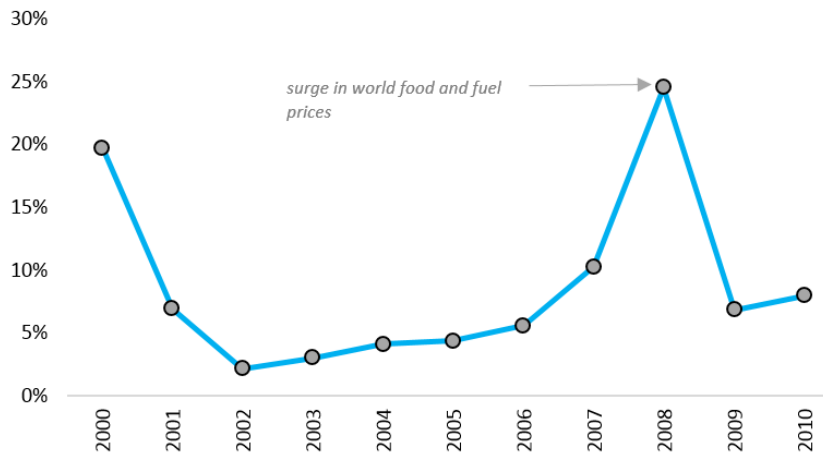
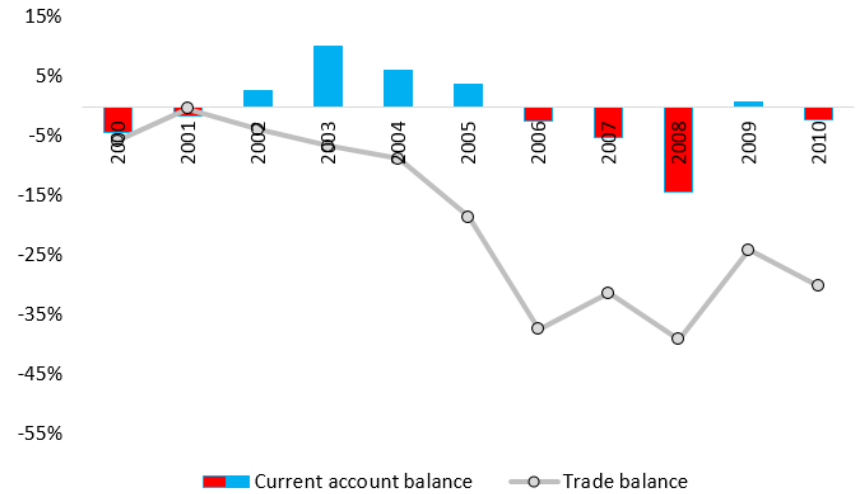


Figure 5. Current account deficit, in % of DGP, 2000 - 2010



Source: IMF and WB data

4.3 Design and implementation of MFA

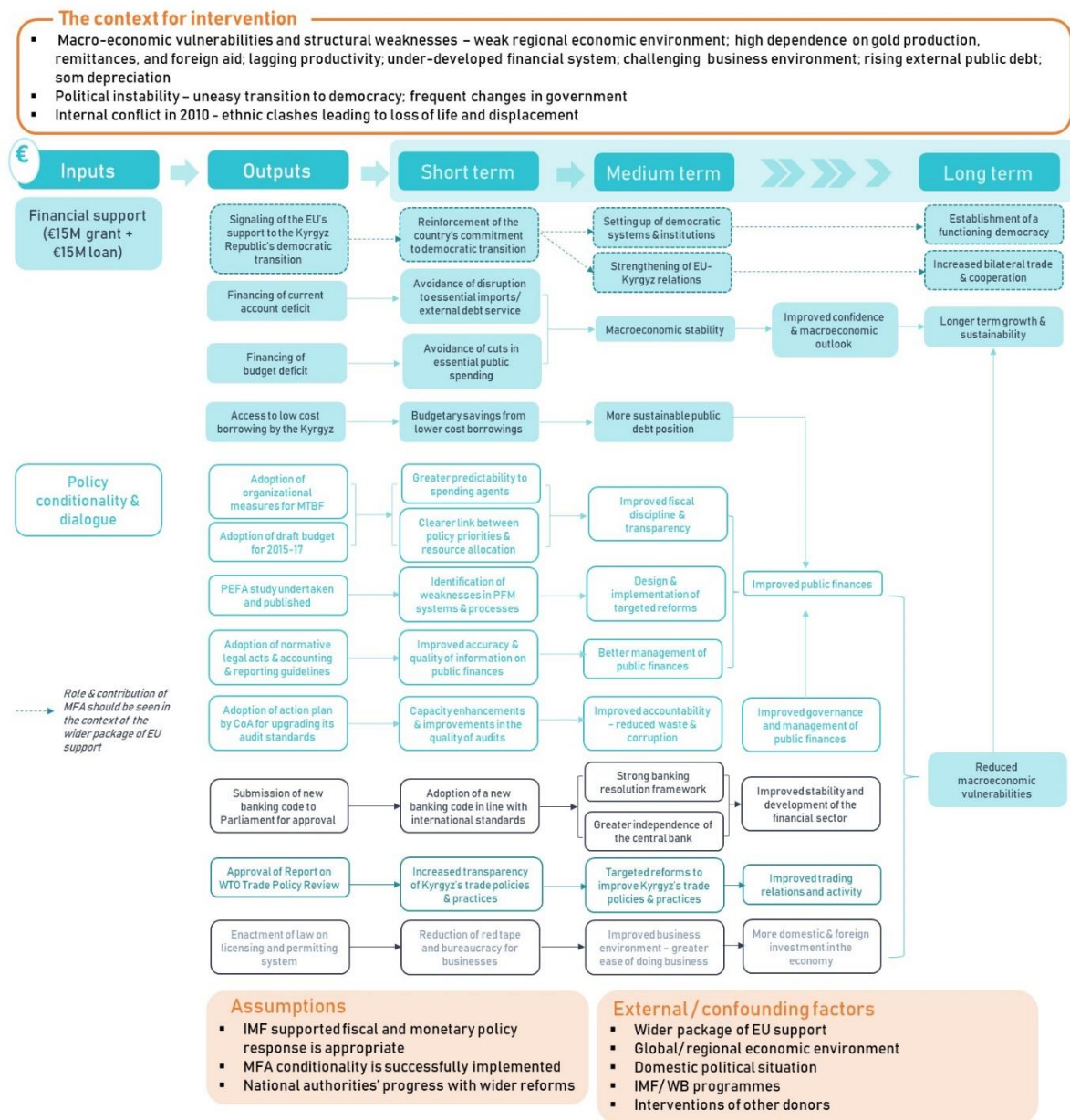
4.3.1 Intervention logic for the MFA

A theory of change describes the causal mechanisms or pathways through which an intervention is expected to bring about the desired change(s) and is underpinned by critical thinking about other influencing factors and assumptions about how and why that sequence of change might come about. It consists of the following building blocks:

- The needs, problems or issues that are being addressed by an intervention;
- The activities (outputs) and expected effects (results and impacts) of an intervention;
- The assumptions that explain how the activities would lead to the effects in the context of the intervention;
- The main external factors (confounding factors) that also influence the direction and scale of effects.

Figure 6 illustrates the theory of change for the MFA operation in the Kyrgyz Republic. It has been developed on the basis of desk research, a wider literature review, stakeholder interviews and expert opinion.

Figure 6. MFA intervention logic



The ToC depicts how the MFA financial assistance (15 million loan and 15 million grant) to the Kyrgyz Republic was expected to support the country's democratic transition, and to contribute to the country's macroeconomic stability in the medium term, and growth and sustainability over the longer term. It also illustrates, the role of policy conditionality in reducing macroeconomic vulnerabilities (via improved economic governance, public finances, more stable financial sector and improved business environment), thus reinforcing stability and longer term growth outlook.

Key underlying assumptions for the sequence of changes to materialise are:

- The national government's fiscal and monetary policy response designed in cooperation with the IMF is appropriate. For example, the timing and pace of fiscal expansion/ consolidation is appropriate;
- MFA conditionality is successfully implemented; and
- There is commitment to wider reforms that are needed to address the country's underlying macroeconomic vulnerabilities.

Finally, the ToC takes account of the role of other factors that might influence the direction and scale of effects, most notably:

- The wider package of EU support;
- Global / regional economic environment, particularly considering the country's economic linkages with Russia and other regional economies;
- The domestic political situation and the impact that this has on investor / private sector confidence and on ownership and commitment to reforms; and
- The role of other actors notably the IMF, WB and bilateral donors in promoting reforms and providing financial assistance.

4.3.2 Key features of the operation

4.3.2.1 Negotiation and approval

The MFA operation that will be the subject of this evaluation was requested by the Kyrgyz authorities in October 2010 shortly after a prominent donor conference (Box 1).

Box 1 Origins of the MFA operation

In July 2010, following the global economic crisis and inter-ethnic violence, a donor conference for the Kyrgyz Republic was organised in Bishkek. USD 1.1 billion were pledged and supposed to be disbursed quickly (over the next 30 months). The main objective of this financial provision was to support essential public expenditures and services, to support with social needs and to back critical investment (mostly in public infrastructure, energy and transport). The European Commission, among the major donors, immediately announced the mobilisation of EUR 118 million of assistance through various instruments including:

- EUR 12 million of new assistance: EUR 5 Million in humanitarian emergency assistance and EUR 7 million from the stability instrument;
- EUR 106 million from existing development assistance, including EUR 55 million of EU development assistance ready to be launched in 2010 with a focus on special safety nets, education and agriculture; and EUR 51 million for the 2011 - 2013 period to advance reform in the areas of social protection, education and rule of law.

Shortly after, via a letter dated October 2010, the President and the Minister of Finance of the Kyrgyz Republic formally requested the EU MFA to complement the financing available from the IMF. The possible MFA assistance was discussed at the highest political level, including during the visit of President Otunbayeva in Brussels in March 2011.

The MFA assistance was proposed end 2011 after a DG ECFIN mission to Bishkek. It was informed by the IMF's assessment of Kyrgyzstan's residual financing needs and, factored in various uncertainties around some of the pledges made at the donor conference, notably the

one from the Eurasian Economic Community Anti-Crisis Fund (worth USD 106.7 million).

The EC proposal was not put forward earlier since the IMF's Rapid Credit Facility (RCF) of SDR 22.2 million implemented in September - December 2010 was not sufficient for that purpose. Instead, the Commission had to wait until agreement on the ECF IMF programme, an agreement which was delayed for months (until April 2011), partly reflecting delays in the formation of a new government.

An EC mission to Kyrgyzstan was organised shortly after the conclusion of the 2011 EFC agreement end of May 2011, while discussions with Member States (i.e. with the Economic and Financial Committee Alternates and with the Financial Counsellors Working Party) took place in the autumn.

The actual MFA proposal of the European Commission was adopted in December 2011. The approval was delayed owing to a procedural disagreement between the Council and European Parliament (see Box 2). It eventually took place in October 2013²².

One of the key difficulties related to the implementation of MFA has been a lengthy decision-making process that requires an agreement on Commission proposals for MFA between the European Parliament and the Council under the ordinary legislative procedure. This has often led to considerable delays between the submission of the Commission proposal and actual disbursement, despite a rapidly changing environment and acute nature of the crisis requiring prompt action²³.

In the case of the Commission proposal for MFA to the Kyrgyz Republic, the adoption of the Commission proposal by the co-legislators was further complicated by the parallel negotiations between the co-legislators on a Commission proposal for Framework a Regulation on Macro-Financial Assistance (MFA) of January 2011. The major objective of this Commission proposal was to streamline and expedite decision-making and to replace the lengthy Ordinary Legislative Procedure with implementing acts (Commission decisions following a binding consultation of a Member State Committee²⁴). However, the European Parliament and the Council agreed at some point to keep the ordinary legislative procedure after long negotiations blocking the entire MFA instrument including the Commission proposal for MFA to the Kyrgyz Republic. Therefore, the Commission withdrew its proposal for a MFA Framework Regulation in May 2013 and instead the European Parliament and the Council agreed on a non-binding Joint Declaration on MFA for all future MFA proposals²⁵, (Joint Statement annexed to the Decision regarding the provision of Macro-Financial-Assistance to Georgia). This means that MFA decisions continue to be adopted under the Ordinary Legislative Procedure.

Box 2 Origins of the delays for the approval of the proposal – early 2011 till the end of 2013

4.3.2.2 Disbursement

The EUR 30 million operation took the form of a EUR 15 million medium-term loan and a EUR 15 million grant. Both loan tranches were characterised by very long maturity and low interest rate (Table 1).

²² Decision No 1025/2013/EU of the European Parliament and of the Council of 22 October 2013 providing macro-financial assistance to the Kyrgyz Republic (OJ L 283, 14.8.2013, p. 1).

²³ European Parliament indicated the lengthy decision making process as one of the main shortcomings of the MFA instrument already in 2003.

²⁴ European Commission, MFA to non-EU countries. Available at: http://ec.europa.eu/economy_finance/eu_borrower/macro-financial_assistance/index_en.htm

²⁵ Available at: <http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//NONSGML+TA+P7-TA-2013-0320+0+DOC+PDF+V0//EN>

This operation was the first MFA operation that was implemented in Kyrgyzstan. The use of the MFA instrument in Kyrgyzstan was exceptional in the sense that Kyrgyzstan does not fall within the traditional geographical scope of the MFA instrument (consisting of candidate and potential candidate countries and countries bordering the EU covered by the European Neighbourhood Policy)²⁶. The Joint Declaration of the European Parliament and the Council of 2013 foresees that only “*in exceptional and duly justified circumstances*”, other third countries “*that play a determining role in regional stability, are of strategic importance for the Union, and are politically, economically and geographically close to the Union*”²⁷ can benefit from the MFA instrument²⁸. In the 2011 ex-ante evaluation²⁹, the use of the MFA instrument in Kyrgyzstan was justified “*...by the strength of the political and economic reform momentum in the country and by its position in a region of strategic economic and political importance for the EU.*”

The objectives of the operation thus went beyond purely macro-economic arguments which are stated in the MoU, namely to “*support the restoration of a sustainable external financial situation for the Kyrgyz Republic, to alleviate its balance of payments needs and thereby support its economic and social development.*” These are cited in, *inter alia*, the 2013 Declaration³⁰:

- the need “to continue providing assistance (...) in the implementation of their reform programme” (Recital 4);
- the appropriateness “to provide a political signal of the Union’s strong support to democratic reforms in Central Asia” (Recital 5);
- the objective to “support the Kyrgyz Republic’s commitment to values shared with the Union, including democracy, the rule of law, good governance, respect for human rights, sustainable development and poverty reduction, as well as its commitment to the principles of open, rule-based and fair trade.” (Recital 17);
- an opportunity to “strengthen the efficiency, transparency and accountability of public finance management systems in the Kyrgyz Republic” (Recital 17).

4.3.2.3 Delays in the approval and disbursement of the MFA

This operation was also characterised by a long timetable between approval and disbursement. The MFA documents (i.e. the MoU, the Loan Facility Agreement and the Grant Agreement) were signed in October 2014 (one year after the approval of the operation due to some legal issues – see Box 3) and ratified by the Kyrgyz Parliament in February 2015.

Box 3 Origins of the delays between the Decision and signature of the MFA documents – end 2013 – beginning 2015

The main reason for the delays over the course of 2014 were of a legal nature. More

²⁶ https://ec.europa.eu/info/business-economy-euro/economic-and-fiscal-policy-coordination/international-economic-relations/macro-financial-assistance-mfa-non-eu-partner-countries_en

²⁷ This possibility is included the 2013 Joint Declaration available at <http://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1496069109525&uri=CELEX:32013D0778> [accessed on 30 November 2017]. It was already foreseen in the preceding Genvat criteria, available at: <http://data.consilium.europa.eu/doc/document/ST-12592-2002-INIT/en/pdf> [accessed on 30 November 2017].

²⁸ There had already been a precedent with another Central Asian country, Tajikistan, which benefit from the instrument over the period 2001 - 2006 (based on a 1997 decision updated in the year 2000, namely: Council Decision 97/787/EC as amended by Decision 2000/244/EC).

²⁹ EC (2011) Ex-ante evaluation statement on EU macro-financial assistance to the Kyrgyz Republic, SEC(2011) 1619 final. Available at: <http://eur-lex.europa.eu/legal-content/EN/ALL/?uri=CELEX:52011SC1619>

³⁰ Official Journal of the European Union. 2013. ‘Decision No 1025/2013/EU of the European Parliament and of the Council of 22 October 2013 providing macro-financial assistance to the Kyrgyz Republic.’ Available from: OJ L 283, 14.8.2013, p. 1.

specifically, the governor of the National Bank of Kyrgyz Republic at the time did not want to sign the MoU, the loan facility agreement and the grant agreement, as it is usually required for all MFA operations. From the EU's perspective, the signature of the Central Bank is needed in order to have co-ownership by the central bank of the required reforms in line with established practice for the IMF letters of intent and as some of the information obligations under the MoU concerning specific data and statistics concern the central bank. Furthermore, MFA is generally transferred to the National Bank. On the Kyrgyz side, the National Bank did not want to be considered as the borrower and to be linked in any ways to the reimbursement of the debt *per se* (beyond holding the money). It also did not want to endorse the reforms included in the annex which are for the government to implement while the National Bank should remain fully independent and should not be asked to endorse reforms.

Finally, a compromise was found when it was decided that the governor would sign "acting as financial agent the Kyrgyz Republic in charge of servicing the external debt of the Kyrgyz Republic"³¹. From a legal point of view, the National Bank of Kyrgyz Republic is thus not a party of the agreement next to the Kyrgyz Republic.

Yet, by the time agreement on MoU was reached, the 2011 IMF programme had expired (in July 2014). A new three-year ECF was agreed with the IMF in April 2015 and from then onwards, disbursements followed more swiftly. The operation was disbursed in full, in two instalments, over the period June 2015 - April 2016:

- The first instalment comprised: a EUR 10 million grant disbursed in June 2015 and a EUR 5 million loan disbursed in October 2015;
- The second instalment comprised: a EUR 5 million grant disbursed in February 2016 and a EUR 10 million loan disbursed in April 2016.

4.3.2.4 Key MFA conditionalities

In terms of the conditions which had to be met for the disbursements to be released, the MoU³² specified that the implementation of the IMF programme needed to remain on track.

As far as policy conditionalities linked to the second tranche were concerned (see Table 1 overleaf), there were seven specific conditions under four reform areas, namely:

- Public Finance Management (PFM);
- Financial sector;
- Trade policy and Investment; and
- Business environment.

However, due to the subsequent delays, six out of seven specific conditions were outdated at the time of the first disbursement (see Sections 5 and 6).

The selection of the conditions was managed by DG ECFIN staff who undertook two missions to Kyrgyzstan, i.e. in May and October 2013 respectively. In addition to the consultations held with the Ministry of Finance and responsible authorities, the design of the conditionalities also benefited from contributions from the EU Delegation (i.e. cross-checking for potential duplications with existing Budget Support programmes), EEAS and other DGs such as DG DEVCO. The choice of conditionality was also consulted with other donors, in particular the IMF and WB.

In addition, and as by default in every MFA operation, DG ECFIN commissioned an Operational Assessment (OA) which focused on the reliability of the circuits and

³¹ Memorandum of Understanding between the European Union and the Kyrgyz Republic. Provided together with the Terms of Reference.

³² Memorandum of Understanding between the European Union and the Kyrgyz Republic. Provided together with the Terms of Reference.

procedures in place at the Central Bank, the Ministry of Finance and other Ministries and bodies of the recipient countries, involved in managing MFA funds.

Table 1. Overview of MFA to Kyrgyz Republic

Rationale for the MFA operation	for the MFA characteristics	Main Areas of Reform
<p>"Support the restoration of a sustainable external financial situation for the Kyrgyz Republic, to alleviate its balance of payments needs and thereby support its economic and social development" (MoU)</p>	<p>EUR 15 million (loan), 2 disbursement dates: - EUR 5 million loan in October 2015 * Maturity: 14 years ** Interest rate: 1.375%</p>	<p>The structural reforms covered the following areas:</p> <p>Area 1: Public Finance Management</p> <p>(1) Medium-Term Budget Framework: approval of a draft resolution on organisational measures for the preparation of the Medium-Term Budget Framework 2015 - 2017 and approval of the draft republican budget of the Kyrgyz Republic for 2015 - 2017.</p> <p>(2) PEFA: reaching agreement on the Terms of Reference of the PEFA.</p> <p>(3) Reform of the accounting and reporting systems: endorsement of the following normative legal acts and methodological documents: (i) Accounting policy of the public administration sector; (ii) Regulation for preparation of financial reporting; and (iii) Regulation for the organization and maintenance of accounting and book-keeping.</p> <p>(4) External auditing: development and approval of an Action Plan for upgrading its audit standards to INTOSAI standards.</p>
<p>NB: Additional political objectives as spelled out in the 2013 Decision</p>	<p>- EUR 10 million loan in April 2016 * Maturity: 15 years ** Interest rate: 0.70%</p>	<p>Area 2: Financial sector</p> <p>(5) Submission of a new Banking Code to the Parliament</p>
	<p>EUR 15 million (grant), 2 disbursement dates</p>	<p>Area 3: Trade policy</p> <p>(6) Official approval of the report on its trade policy to be presented in the Trade Policy Review Body of the WTO and development of a draft action plan responding to the recommendations of the WTO Secretariat.</p> <p>Area 4: Investment and business environment</p> <p>(7) Enactment of the law "On licensing and permitting system in the Kyrgyz Republic"</p>

4.4 Economic developments during the implementation

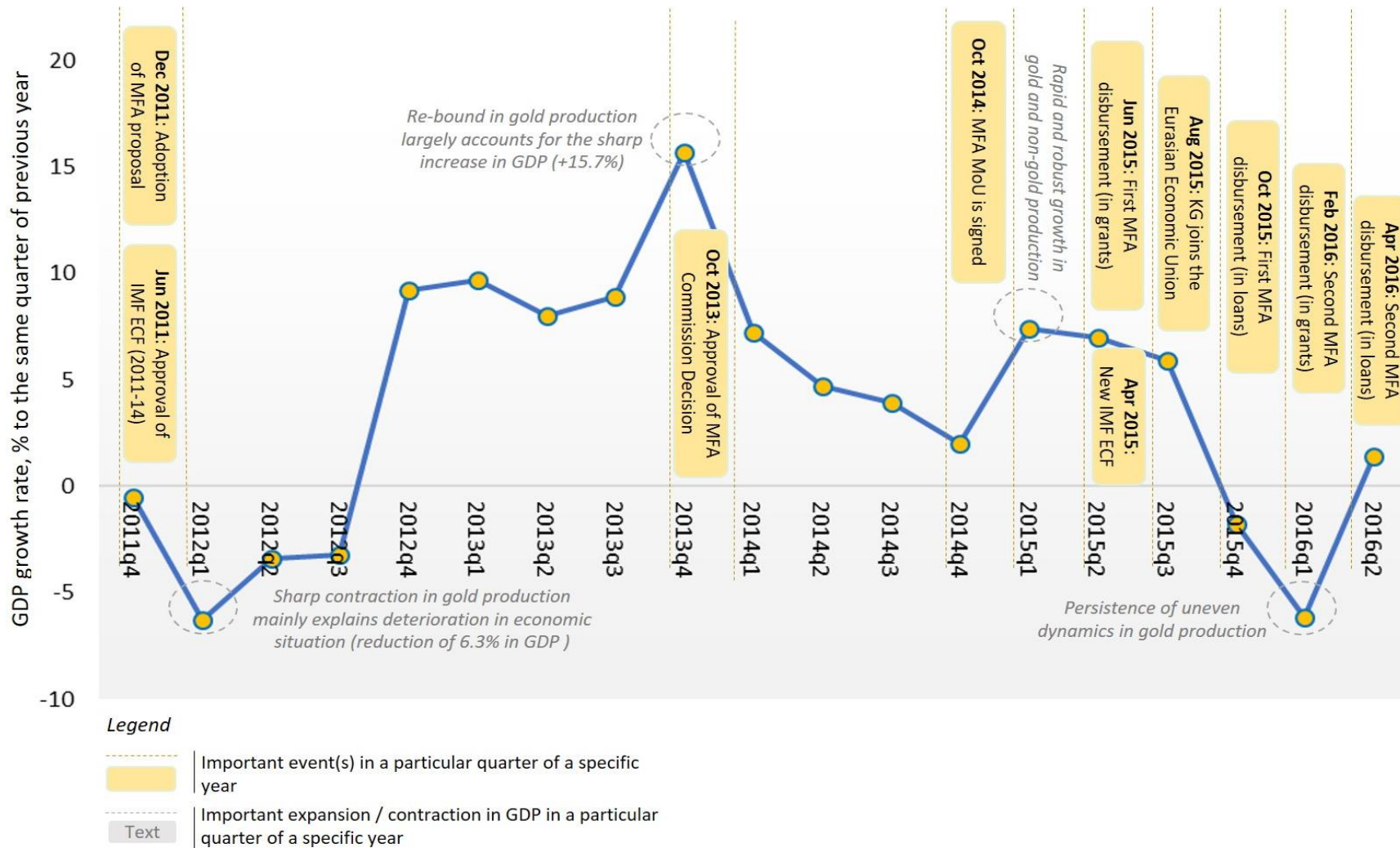
4.4.1 Evolution between Q4 2011 and Q2 2016

This subsection discusses important economic developments that took place during the implementation of the MFA operation in Kyrgyzstan. Specifically, the analysis focuses on the following time periods:

- **Late 2011 – late 2015**, i.e. the period between the adoption of a proposal for the provision of MFA to Kyrgyzstan by the European Commission (December 2011) and the first (full) disbursement (October 2015).
- **Late 2015 – early 2016**, i.e. the period up to the second (full) disbursement (April 2016).

Figure 7 overleaf depicts an overview of Kyrgyzstan's economic situation, measured by GDP growth rate over the aforementioned periods. Specific events that help explain the developments observed over these periods are discussed in greater detail in subsequent subsections and in latter parts of the report.

Figure 7. Trends in quarterly GDP growth rates observed for Kyrgyzstan, 2011(Q4)-2016(Q2)



Sources: National Statistical Committee of the Kyrgyz Republic; National Bank of the Kyrgyz Republic

4.4.1.1 Evolution observed between Q4 2011 and Q4 2015

In 2011, full resumption of trade and services flows, continued reconstruction works, and improved investor confidence fuelled an increase in economic activity³³. Renewed confidence in the Kyrgyz economy could have been due to, though not the sole result of, the IMF's announcement of a three-year Extended Credit Facility (ECF) arrangement (over the period June 2011 - July 2014) and the European Commission's proposed MFA to Kyrgyzstan, signalling important structural reform actions in key areas. Concurrently, however, foreign / external debt rapidly expanded and, as of the end of 2011, it amounted to nearly USD 2.8 billion³⁴. Kyrgyzstan's external debt accounted for more than half of its (annual) gross domestic product (GDP), estimated at USD 5 billion³⁵. This seemingly increased dependence on external resources could explain the (small) contraction observed in GDP growth in the fourth quarter of 2011 (when compared to the same quarter in 2010)³⁶.

Most of 2012 was marked by profound economic problems. Specifically, production in the gold-mining sector contracted by 40 per cent owing to geological issues at Kumtor, Kyrgyzstan's largest gold mine³⁷. Sluggishness in gold production adversely impacted on Kyrgyzstan's gold exports which, coupled with an increase in imports of equipment for energy infrastructure projects, led to an increase in the country's current account deficit. This stood at 15.3 per cent of GDP in 2012³⁸. Over the first three quarters of the year, GDP growth (with the activity of the Kumtor gold mine) thus receded and remained below growth rates observed in similar quarters in 2011. By the end of 2012, overall national output had contracted, and negative growth was observed for the year as a whole (-0.9 per cent). Nonetheless, it should be cautioned that the observed contraction masks the full extent of Kyrgyzstan's economic performance. As such, strong and positive growth was observed in other sectors of the economy, and together with robust remittance inflows, contributed to a non-gold GDP growth rate of 6.3 per cent for 2012. This is depicted in Figure 8 overleaf.

³³ Asian Development Bank. 2011. Asian Development Bank Outlook 2011. Available at: <https://www.adb.org/sites/default/files/publication/28300/ado2011-kgz.pdf>

³⁴ Country Watch. 2018. Kyrgyzstan 2018 Country Review. Available at: <http://www.countrywatch.com/Content/pdfs/reviews/B3M3Q544.01c.pdf>

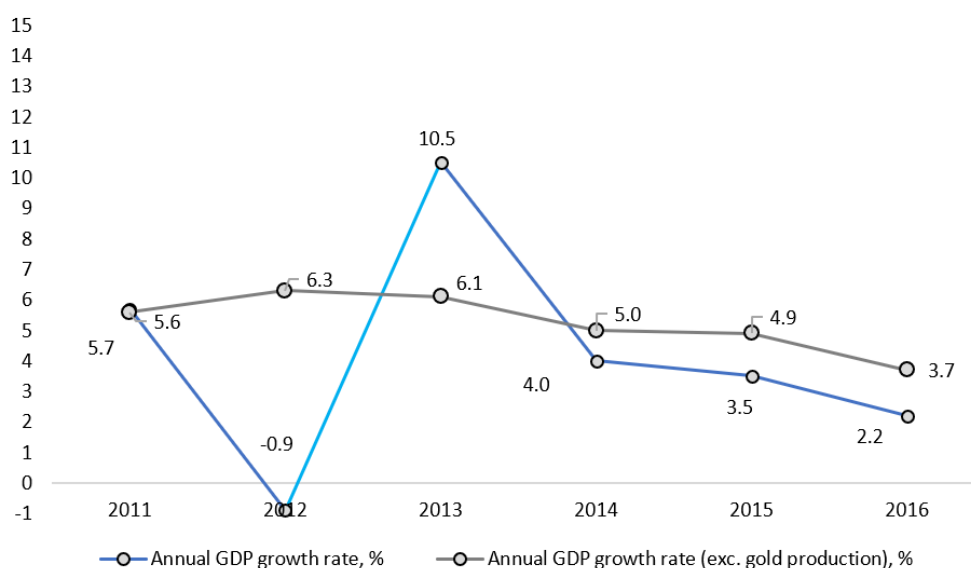
³⁵ Country Watch (2018)

³⁶ Statistics from the National Statistical Committee of the Kyrgyz Republic; and the National Bank of the Kyrgyz Republic

³⁷ DG ECFIN Mission Reports

³⁸ DG ECFIN Mission Reports

Figure 8. Kyrgyzstan's annual GDP growth rate [with and without gold production)], 2011 - 16



Sources: CIA World Factbook; National Statistical Committee of the Kyrgyz Republic

In spite of some of the economic difficulties met in 2012, economic growth surged in 2013. A memorandum of understanding, designed to allow for joint ownership of the Kumtor mine, was reached by the Canadian-based gold mining company, Centerra, and the Kyrgyz government. The agreement led to the resolution of a longstanding dispute which drove gold mining and production activities to resume³⁹. The non-gold economy also performed well, driven by strong private transfers from abroad and higher credit to the private sector. As such, international net-money transfers were reported to be 9.8 percent (in dollar terms) higher in the first half of 2013 than in the same period in 2012. Together with accelerated growth of credit to the private sector, this fostered private consumption and investment that further spurred economic activity and growth. In sum, the recovery in gold production and sustained improvement in the rest of the Kyrgyz economy allowed the Kyrgyz economy to expand by a near 11 per cent, the highest growth experienced by the country since independence⁴⁰.

The strong recovery period observed in 2013 was short-lived though. Growth of the Kyrgyz economy slowed down significantly over the course of 2014, reflecting a deteriorating external environment and major supply-side constraints. The annual GDP and non-gold GDP growth rates observed for the year were much lower than in the preceding year, at 4 and 5 per cent respectively. Specifically, this contraction was driven by a sharp fall in exports to Russia and other neighbouring countries (owing to economic deceleration in these countries) on the one hand, and on the other, lower agricultural production entailed by adverse weather conditions and a poor harvest⁴¹. Nonetheless, although export growth was negative for the year (-6.4 per cent), imports fell more rapidly and more sharply (-7.2 per cent), which, together with lower income outflows, helped reduce the current account deficit – from 15 per cent (in 2013) to 13.7 per cent of GDP in 2014.

³⁹ DG ECFIN Mission Reports

⁴⁰ The World Bank. 2014. Kyrgyz Republic Economic Report No.5. Available at: http://www.donors.kg/images/ECSP1_KGZ_Spring_2014.pdf

⁴¹ The World Bank Group. 2015. Adjusting to a Challenging Regional Economic Environment. Available at: <http://www.worldbank.org/content/dam/Worldbank/Publications/ECA/centralasia/Kyrgyz-Republic-Economic-Update-Spring-2015-en.pdf>

Recovery was back on track in 2015. In the first half of the year, robust growth was observed, although largely on account of 'front-loaded' gold production. Non-gold GDP growth was also relatively strong, mainly driven by the solid performance of the agricultural and services sectors⁴². The Kyrgyz economy, however, slowed down in the second half of the year, causing GDP growth for the final quarter to decrease by about 2 per cent (when compared to the same period in the previous year)⁴³. This reduction could, to some extent, be explained by Kyrgyzstan's vulnerable balance of payments situation, reflecting a structurally large and sustained current account deficit.

4.4.2 Evolution observed between Q4 2015 and Q2 2016

The Kyrgyz economy further contracted in the first half of 2016, reflecting a sharp decline in gold output (-35.6 per cent) and a weak performance of the non-gold sector, in particular, industry and services⁴⁴. Additionally, relations between Centerra Gold and the Kyrgyz government deteriorated in the first half of 2016. The ongoing dispute resulted in a much lower gold output, which in turn had a detrimental effect on foreign investor sentiment and contributed to the economic contraction observed in the first half of the year⁴⁵.

The first MFA disbursement was released in tranches in the second and fourth quarters of 2015 respectively. Considering the satisfactory progress of the Kyrgyz authorities with the implementation of policy conditionalities under the MFA and IMF programmes, the Commission approved the release of the second disbursement in February and April 2016 respectively. Amidst continued efforts by Kyrgyz authorities to take forward structural reform actions, a gradual recovery of the gold sector and an increase in private consumption, fuelled by increased remittances and government spending, the Kyrgyz economy grew faster in the latter part of the year, with moderate growth of 3.8 per cent recorded for 2016 as a whole⁴⁶.

⁴² DG ECFIN Mission Reports

⁴³ Statistics from the National Statistical Committee of the Kyrgyz Republic; and the National Bank of the Kyrgyz Republic

⁴⁴ The World Bank Group 2016 'Kyrgyz Republic.' Available at: <http://pubdocs.worldbank.org/en/727751476375092599/Kyrgyz-Republic-Macroeconomic-and-Poverty-Outlook-1610-en.pdf>

⁴⁵ EBRD. 2016-17. Kyrgyz Republic. Available at: http://2016.tr-ebrd.com/wp-content/uploads/2016/11/TR2016_CA_KyrgyzRepublic.pdf

⁴⁶ DG ECFIN Mission Reports

5 Methodological approach

This section describes our overall approach to the evaluation as well as the specific methods used to collect and analyse data. It concludes with a discussion on the limitations of the evidence base underpinning the evaluation, and in light of this, an assessment of the reliability and validity of the evaluation findings.

5.1 Evaluation design

The evaluation was designed to respond to a specific set of evaluation criteria and questions, as articulated in the Terms of Reference. An evaluation matrix was developed during the inception phase of the assignment to guide the choice and design of specific research methods, as well as to provide a framework for subsequent data analysis and interpretation. More specifically, it specifies:

- The questions addressed by the evaluation (these were taken from the Terms of Reference);
- The evidence required to answer each evaluation question;
- The data sources and methods used for compiling the required evidence; and
- The judgement criteria on which the evaluative conclusions have been based.

The evaluation matrix designed for this evaluation is presented in Annex 1. It reflects the following key elements of our approach:

- *A theory based approach* – this involved making explicit, the underlying theory of change for the MFA operation in the Kyrgyz Republic (see Section 2), and subsequently testing this theory to draw conclusions about whether and how the MFA contributed to observed results.
- *Participatory approaches to data collection and analysis* – our approach incorporated a focus group discussion with key stakeholders to develop a shared understanding of the evaluation objectives and results and to provide additional layers of insight and interpretation to the data.
- *The use of mixed methods* – our approach combined both quantitative and qualitative research methods to facilitate a deeper understanding of the evaluation issues and to build a rich and comprehensive evidence base for the evaluation
- *Triangulation* - multiple lines of inquiry and evidence were used for answering each evaluation question.

5.2 Methods and data sources

The table below provides a high-level overview of the data collection methods and analytical techniques used to address each evaluation criteria. A description of how each of these methods was applied to this evaluation is provided in the sub-sections that follow. Where application, we also discuss the limitations of the specific methodologies in the context of this evaluation.

Table 2. Overview of the methods and techniques used for the evaluation

	Relevance	Effectiveness	Efficiency	Coherence	EU added value
Documentary review	●●●	●●	●●●	●●●	●●●
Macroeconomic data analysis	●●●	●●●	●●●		
Key informant / stakeholder interviews	●●●	●●	●●	●●●	●●●
Focus group	●	●			●●

discussion					
Qualitative counterfactual analysis		•••			
Social impact analysis		•••			
Debt sustainability analysis		•••			
Expert validation workshop	••	••	••	••	••

••• a very important method for addressing the evaluation criterion

•• an important method for addressing the evaluation criterion

• a complementary method

5.2.1 Documentary review

The evaluation is based on an in-depth review of documentation assembled from a variety of sources, as indicated in Table 3 below. A full list of references is available in Annex 2.

Table 3. Documentary sources of evidence for the evaluation

Source documentation	of Types of documentation	Usefulness for the evaluation
European Commission, ECFIN	DG	<ul style="list-style-type: none"> - Ex-ante assessment of the MFA ••• - Operational assessment - Commission proposal and MFA decision - MoU - Grant/ Loan Agreements - DG ECFIN Mission Reports - Compliance statements - MFA annual reports
European Commission, other DGs and the EU Delegation in Bishkek		<ul style="list-style-type: none"> - Partnership and Cooperation Agreement •• - Multi-annual Indicative Programme 2014 - 2020 Kyrgyzstan - EU - Kyrgyz Republic Cooperation for Development - Annual Action Programmes - Selected EU Delegation publications
IMF		<ul style="list-style-type: none"> - Letter of Intent ••• - Article IV staff reports - IMF reviews
WB		<ul style="list-style-type: none"> - WB DPO implementation completion and results' reports
Other		<ul style="list-style-type: none"> - EIU Country Reports •••

- Sovereign ratings reports
- Academic and grey literature on political and economic developments and implementation of structural reforms in Kyrgyzstan
- Reports and data produced by other bilateral/ multilateral donors and IFIs including ADB, EIB, EBRD and GIZ on their activities in the Kyrgyz Republic
- Selected indexes (i.e. WB Doing Business, Open Budget Index, EIU Democracy Index)
- Selected financial and economic press (i.e. Financial Times and the Economist)

●●● useful ●● somewhat useful

5.2.2 Macroeconomic data analysis

Data on key macroeconomic indicators (Table 4) was compiled from various sources and trends and patterns were analysed. Specifically, the evaluation examined how the key macroeconomic indicators have evolved over time and specifically, the direction and magnitude of the changes observed over the period of interest (before, during and after the MFA implementation) as well as any deviations from the initial projections made by the IMF and the underlying reasons for these.

Table 4. Key Macroeconomic Indicators and Data Sources

Component	Data Type	Description	Key data source(s)
<i>The Real Economy</i>	National accounts	Indicators of macroeconomic Performance	Ministry of Finance, and major international sources (e.g. IMF and WB)
<i>The Balance of Payments</i>	Balance of payments statistics	Indicators of external sustainability and trade conditions	Balance of payments: Ministry of Finance, National Bank of Kyrgyz Republic, IMF, WB, The Harvard Atlas of Economic Complexity (i.e. for import/export structure and volume)
<i>The Government</i>	Government finance statistics	Indicators of the government's fiscal sustainability (expenditure, budget balance, debt, etc. data)	Ministry of Finance, National Bank of Kyrgyz Republic and major international sources (i.e. IMF)
<i>The Financial System</i>	Monetary statistics	Banking sector, financing condition, interest rates etc.	Ministry of Finance, National Bank of Kyrgyz Republic and IMF

Component	Data Type	Description	Key data source(s)
The Labour Market	Other economic statistics	Indicators of socio-economic performance	Ministry of Finance, National Bank of Ukraine and major international sources (i.e. IMF and WB)

The access and the quality of the macroeconomic data in the Kyrgyz context has been satisfactory. Some exceptions concern for instance the data related to the financial assistance provided by Russia that is somehow obscure and the study required an assumption regarding the specific grant disbursement in the late 2015 that was announced by the Kyrgyz officials, but without any evident traces in the data published by the Ministry of Finance.

5.2.3 Interviews with key informants/ stakeholders

A series of face-to-face, in-depth interviews were conducted with all key informants and stakeholders, including non-governmental actors such as business representatives and civil society organisations. The table below indicates the number and types of stakeholders interviewed.

Table 5. Overview of the interviews conducted

Stakeholder Group	No of interviews	Roles and responsibilities of interviewees
European Commission	8	DG ECFIN (6) – those responsible for design and monitoring of MFA operation in the Kyrgyz Republic DG DEVCO (2) – those responsible for budget support operations in the region
EU Delegation in the Kyrgyz Republic	3	Head of Cooperation & economic and political advisers
EEAS	1	Desk officer for the Kyrgyz Republic
IMF	7	IMF ResRep Locally based economists Former and current Chief Missions and their team
WB	2	Person responsible for the Development Policy Operation in the Kyrgyz Republic Economists based in Kyrgyz Republic
Kyrgyz Authorities	12	Officials from the Presidential administration, Office of the Prime Minister, Ministry of Finance, National Bank and Chamber of Accounts
Non-governmental stakeholders in the Kyrgyz Republic	6	Representatives of businesses (2), civil society organisations (3), a local think tank (1)
Bilateral donors	2	Representatives from the German and French embassies
Total	41	

In several cases (i.e. Ministry of Finance, National Bank of the Kyrgyz Republic (NBKR), IMF, WB and the EU Delegation) written follow-ups took place to seek additional data/ clarification.

The study team encountered some challenges when organising and conducting interviews, most notably:

- *Loss of institutional memory:* Given the unusually long-time lag between design and implementation of the MFA operation, there inevitably had been some staff turnover among the organisations involved in the operation. For example, the current Head of Cooperation at the EU Delegation has only joined in 2017;
- *Ability to recall* in certain cases: Stakeholders were also unable to recall in detail certain aspects related to the MFA operation or/and relevant context due to the time that had elapsed;
- *Reluctance of some national stakeholders to provide a candid account:* We observed a consistent and relatively pronounced reluctance among interviewees to express their views on matters that could have been seen by them as potentially sensitive, especially in relation to implementation of structural reforms;
- *Inability to secure interviews:* With a limited number of stakeholders responsible for certain MFA conditions (e.g. Ministry of Economy).

5.2.4 Internal brainstorming session on counterfactual scenarios

At the inception stage of the evaluation, an internal brainstorming session on counterfactual scenarios was organized. Participants included the core ICF and Cambridge Econometrics teams and local experts.

The session allowed the team to test and further develop initial ideas as well as generate potential counterfactual scenarios that were not 'discovered' during the earlier research phase. More specifically, it enabled the team to:

- Shortlist the hypothetical counterfactual scenarios that would have been *the least* likely, with a detailed evidencing of the reasons for rejecting these scenarios.
- Identify the most plausible counterfactual scenarios that would have been *the most* likely with a detailed evidencing of reasons for such state and main caveats.

For both type of possibilities, gaps in information, caveats, further inquiry lines, and potentially most relevant sources of information including their quality and reliability were discussed and summarized in a form of the note that constituted the relevant material for the assessment of counterfactual at further stages of research (during interviews with the IMF and WB in Washington D.C., interviews with Kyrgyz authorities and a focus group with development partners in Bishkek. The extended version of the workshop note is presented in Annex 11).

5.2.5 Focus Group with development partners

Towards the end of the evaluation, a one-day focus group discussion was organised with locally-based development actors to complement as well as cross-check information collected from other sources such as desk research and key informant interviews. Representatives of the following organisations participated in the focus group discussion:

- Eurasian Development Bank;
- World Bank;
- Asian Development Bank;
- United Nations Development Programme - Kyrgyzstan;
- Deutsche Gesellschaft für Internationale Zusammenarbeit - Kyrgyzstan; and
- European Bank for Reconstruction and Development.

The detailed list of participants is presented in Annex 4.

A key limitation of the discussion was that most participants had very limited awareness and knowledge of the MFA. Consequently, the discussion may not have been as informative and insightful as initially envisaged.

5.2.6 Qualitative counterfactual analysis

It is conceptually and methodological challenging to isolate the effect of MFA from other interventions (such as the IMF programme, other EU interventions, support from other donors etc.) and other exogenous factors and/ or unobservable factors. Previous MFA evaluations have relied upon econometric modelling (i.e. estimating unobserved counterfactual outcomes with the help of macroeconomic models and then comparing these hypothetical counterfactual outcomes with observed macroeconomic outcomes). This approach has some important limitations. Firstly, it is almost impossible to construct reliable counterfactual scenarios using econometric techniques or macroeconomic models in a crisis context⁴⁷. Secondly, this approach has yielded little by way of meaningful insights in past MFA evaluations.

In light of these issues, we adopted a more qualitative approach. More specifically, we applied counterfactual reasoning within a qualitative framework (using a theory-based approach) to draw inferences regarding the role and contribution of the MFA in promoting macroeconomic stabilisation and cushioning the social impact of the crisis (see also sub-section 3.2.8 on social impact analysis). Evidence and insights collected from desk research, interviews, focus group and expert opinions were used to deduce what might have happened in the absence of the MFA (and IMF). We also paid particular attention to ensuring that the counterfactual scenario(s) and any inferences drawn were grounded in logic and economic theory.

A quantitative approach, was, however, used to assess the impact of MFA on debt sustainability of the Kyrgyz Republic (see sub-section below).

Under both alternatives (no MFA, and no MFA and IMF), there were three plausible options that emerged as a result of the research, which would not have been mutually exclusive. This in turn makes inferences about likely economic outcomes less certain (i.e. public cuts, as a result of both alternatives, could have been of a different magnitude, depending on the support from Russia and the extent to which government would have drawn on its reserves at the NBKR).

5.2.7 Debt Sustainability Analysis (DSA)

In line with the ToR requirements, the study team carried out a DSA to evaluate the contribution of the MFA towards sustainability of public debt in the Kyrgyz Republic. This involved an analysis of key debt-burden indicators and macroeconomic variables which influence the path of a country's debt and its capacity to manage this burden sustainably in the medium term to long term. Debt burden indicators of interest included:

- The present value of public debt to GDP;
- The present value of public debt to fiscal revenue; and
- Public debt service to fiscal revenue.

The role of the MFA in facilitating sustainability of the Kyrgyz Republic's public debt was based on counterfactual modelling. More specifically, the team analysed the possible trajectories of debt-burden indicators under the following scenarios:

⁴⁷ Macroeconomic variables might not behave during a crisis the way their historical pattern, and thus statistical models, would predict. Moreover, the crisis could have changed the usual relationships between variables. For example, a crisis could have changed consumer and business behaviour in such a way as to make statistical relationships diverge from their historical pattern, making them more risk averse and cautious for example. Other relationships that are normally linear, may change the character (i.e. and become non-linear and more challenging to capture by standard models).

- Baseline scenario depicting observed outcomes i.e. what actually happened;
- An alternative scenario (scenario 1) depicting what would have happened if there had been no MFA programme;
- A second alternative scenario (scenario 2) depicting what would have happened if there had been no MFA and no IMF-ECF programmes for the Kyrgyz Republic.

By comparing outcomes across the three scenarios, the inferences were drawn regarding the MFA's contribution to the sustainability of Kyrgyz Republic public debt. A DSA toolkit developed by the IMF and the WB that is the benchmark tool for analysing debt sustainability of countries, was used for the purpose.

To generate the alternative scenario inputs required for the DSA toolkit, a macroeconomic stock-flow model for the Kyrgyz Republic was constructed. For each scenario, a set of quantitative assumptions were developed as inputs for the stock-flow model. The key outputs from this model were then fed into the DSA toolkit to provide estimates of the implications for debt and debt sustainability.

The analysis has some limitations that need to be explicitly acknowledged. It is difficult to isolate and quantify the impact of MFA because it was combined with other finance (i.e. IMF and WB assistance) and no record is available on the amounts that specifically went to debt operations. More generally, the nature of the MFA mechanism implies that it was not possible to trace down how MFA funding was used specifically i.e. maintain public expenditure, meet the foreign debt repayment obligations etc.

The quality and the granularity of the available data used for the analysis was satisfactory.

Further detail of the methodology for the DSA and the results of the analysis can be found in Annex 14.

5.2.8 Social Impact Analysis (SIA)

The purpose of the SIA was to draw inferences about the role and contribution of the MFA operation in cushioning the social impacts of the crisis. This was done by analysing trends in the following social indicators prior to, during and after the MFA operation:

- The job creation rate;
- The national unemployment rate;
- Levels of unemployment, employment and economic inactivity among the working age population;
- Real wage growth (both regional and national);
- Spending on the social fund and social benefit programmes;
- Education enrolment rates and outcomes;
- The number of healthcare facilities (changes over time);
- Inflation and the cost of living; and
- National and regional poverty rates.

Counterfactual reasoning (as discussed in sub-section 5.2.6) was applied to deduce the extent to which the MFA operation contributed to the observed outcomes.

5.2.9 Expert validation workshop

A validation workshop took place on Commission premises on January 15, 2019. The aim was to validate the draft report on the "ex-post evaluation of Macro-Financial Assistance operation to the Kyrgyz Republic over the period 2013-2016." The study findings were discussed with a view to validating information, data and evidence on each evaluation criterion, i.e. relevance, effectiveness, efficiency, EU-added value, and coherence. In addition, potential recommendations as regards the design and implementation of future MFA operations were discussed.

5.3 Discussion of validity and reliability of the findings

In our judgement, the overall reliability and validity of the evaluation is *strong*. There are multiple lines of evidence and inquiry contributing to answering each evaluation question, mitigating the limitations associated with individual research activities. Moreover, a series of measures were undertaken by the study team to ensure the reliability and validity of the overall findings of this evaluation as indicated in the table below.

Table 6. Overview of the main elements underpinning reliability and validity of findings

Criteria for judging quality	Measures undertaken for improving quality	Judgement
Credibility (internal validity) - the extent to which the findings are plausible, believable and trustworthy; and thus can be defended when challenged.	<p>Triangulation - combining and cross-checking theory and evidence generated by multiple perspectives, theories, methods, and data sources</p> <p>Respondent validation- sharing interview write-ups with interviewees to ensure accuracy and completeness</p> <p>Hypothesis exploration: multiple hypotheses were tested to identify the best, most probable explanation</p>	Strong
Transferability (external validity) - the degree to which findings can be transferred to other contexts by the readers. This means that the results are generalizable and can be applied to other similar settings, populations, situations and so forth	Detailed description of the context of the MFA operation and methodology to assist the reader in being able to generalise the findings and apply them appropriately	Medium
Reliability (dependability) - the consistency with which the results could be repeated and result in similar finding	<p>Triangulation- evidence compiled from different sources was corroborated and cross-validated</p> <p>Thorough record keeping, ensuring a clear decision trail and transparency in data interpretation</p> <p>Information synthesis: going beyond simply collecting, listing and describing distinct data elements in the interpretive process</p>	Strong
Confirmability (objectivity) - the degree to which the results could be confirmed or corroborated by others	<p>Stance analysis: taking account key informants' and stakeholders' backgrounds to assess how their perspective might have biased the information they provided</p> <p>Acknowledging biases in sampling and critical reflection of methods, ensuring sufficient depth and relevance of data collection and analysis</p> <p>Explanation critique - the interpretive chain of reasoning and inferences drawn have been subject to 'peer' review and critical challenge by stakeholders</p>	Strong

6 Implementation state of play

This section presents the evolution of the economy since the completion of the MFA operation up to the current time.

6.1 Evolution from Q2 2016

Growth performance in 2016 - 2017 was typical for Kyrgyzstan with growth rates close to the GDP long-term average (2000 - 2015) value about 4.5 per cent. This was supported by some recovery in the neighbouring economies (especially Russia and Kazakhstan) and increase in remittances sent by the Kyrgyz migrants from these countries. The debt and fiscal situations have somewhat improved, and inflation remains below 5 per cent per annum (see details in sub-section 6.1.1).

By assessment of the IMF, *"The authorities are committed to prudent macroeconomic policies and implementation of structural reforms and see them as essential to promoting higher and more inclusive growth and to increase economic resiliency. Monetary policy remains appropriately focused on maintaining price stability."*⁴⁸ Still, fiscal consolidation remains an issue on the government's economic policy agenda. Structural reforms (e.g. in the area of public finance management), improvement of the business environment and investment climate also require more of government's attention. The WB makes major emphasis on the lack of reforms in the ailing energy sector of the Kyrgyz economy.⁴⁹ The structural reform indices did not demonstrate much improvement during these years. For example, the ranking of Kyrgyzstan in the WB's Doing Business index fell from 67 in DB2016 to 77 in DB2017; the Open Budget Index has barely changed between 2015 (54/100) and 2017 (55/100).

The economic performance in 2018, however, is well below the country's average; the GDP growth rate for January - September was just 1.2 per cent, substantially lower when compared to last year's performance. The 2018 economic growth rate is forecast, by the Kyrgyz Ministry of Economy, IMF, Eurasian Development Bank (EDB) and other organisations, to be around 2-3 per cent. The medium-term growth prospects are shaped by downside risks (i.e. very slow recovery of the Russian economy, difficulties with attraction of foreign direct investments etc.). The official Medium-Term Forecast of the Social and Economic Development of the Kyrgyz Republic for 2019 - 2021 operates with annual growth rates for these years of 4.0-4.1 per annum. The IMF (World Economic Outlook, October 2018) predicts the growth rate of 4.5 per cent in 2019, but only 2.4 per cent in 2023. The latter value may be related to the gradual closure of Kumtor gold mine (because of the deposit depletion) expected to start in 2022-2023.

6.2 Policy implementation

The following section provides a brief snapshot on EU assistance as well as key programmes deployed by other donors following the MFA operation.

6.2.1 Continued support from the EU and other European institutions

The EU operates in the Kyrgyz Republic on the basis of the Partnership and Cooperation Agreement which has been in force since 1999 (see Section 9). At the end of 2017, the EU and the Kyrgyz Republic launched negotiations on another comprehensive bilateral agreement. Kyrgyzstan is one of the countries of Central Asia where the EU implements its "European Union and Central Asia: Strategy for a New Partnership." This strategy has been in force since 2007; a major revision is scheduled for 2019.

⁴⁸ IMF (2018).

⁴⁹ WB (2017) Kyrgyz Republic Economic Update No. 5. Spring 2017.

In this framework, the EU provides a substantial aid to the Kyrgyz Republic. For the timeframe 2014 - 2020, the EU will have allocated EUR 174 million of bilateral aid to the Kyrgyz Republic in grants. In 2016 - 2017, the EU implemented three budget support programmes in the country in the following areas: 1) rule of law (EUR 13.5 million), 2) education (EUR 70 million), and 3) integrated rural development/social protection and public finance management (EUR 30 million). These programmes provide resources for implementation of the reforms which are critical for development of the relevant sectors and the country's general governance system. The EU also provides very substantial technical assistance in such areas as democratisation through electoral reform, public finance management, education, rule of law, nutrition, tourism, border management and environment.

In 2016, the EU provided the Kyrgyz Republic with the GSP+ status. The GSP+ scheme offers Kyrgyzstan zero customs duties on over 6,200 EU tariff lines. In exchange, Kyrgyzstan has committed to the effective implementation of 27 core international conventions on human and labour rights, environmental protection and good governance.

EBRD has cumulative investments of EUR 704 million in the Kyrgyz Republic; its current portfolio includes 62 projects worth EUR 182 million. In 2016 and 2017, the Bank implemented 24 and 15 projects, respectively, with investments for these two years amounting to some EUR 140 million. These projects concentrate in energy, transport, urban development and other public infrastructure. European Investment Bank also has some presence in Kyrgyzstan with urban waste management project.

6.2.2 Assistance from other donors

6.2.2.1 Possibility of a new IMF programme

In 2016 - 2018 Kyrgyzstan continued implementation of the IMF programme. The fourth and fifth reviews Under the Extended Credit Facility Arrangement for the Kyrgyz Republic had been completed with some delay in December 2017 and published only in February 2018. These reviews assessed the programme performance as "mixed" and several quantitative performance criteria and structural benchmarks were missed. The sixth final review has never been completed, so the Kyrgyz Republic lost SDR 9.5 million (USD 13.5 million) in budget support from IMF. The programme expired in April 2018.

In September - October 2018, the IMF mission visited the Kyrgyz Republic and started negotiations on the possibility of having a new programme. The IMF was cautious about the prospect of the new programme, the fact reflected in a significant number of prior actions that would be included in it, should both parties agree.

The IMF conducted Article IV consultations with the Government in October 2017. However, as of October 2018, the report had not yet been published. It is pending approval from the government. A press release from the IMF mentioned that its Executive Board provided a number of recommendations aiming at strengthening monetary and fiscal policies in Kyrgyzstan. Among other things, the Board "urged the NBKR to refrain from assuming equity positions in lending or investment entities."⁵⁰ Yet, in October 2018, the NBKR has purchased some 70 per cent of shares of the ailing Rosinbank becoming the majority shareholder of the bank. The NBKR declared an intention to re-capitalise the bank thus significantly deviating from the IMF's recommendations.

6.2.2.2 Other multilateral and bilateral donors

There is a number of multilateral and bilateral donors providing budget support in the form of both programmatic / investment loans and grants. Some notable contributors

⁵⁰ IMF (2018).

are the Russian Federation, the WB, and the ADB. The WB and ADB programmes aim at the implementation of different structural reforms in the Kyrgyz economy, while the Russian budget support is provided with no policy conditionality attached.

The main source of investment loans remains the People's Republic of China, which provides loans through Eximbank of China. The WB, ADB, EBD, Islamic Development Bank (IDB), European Bank of Reconstruction and Development and some other donors also tend to focus their financing on specific projects, such as road, energy and other infrastructure investments consolidated under the Public Investment Programme (PIP), a specialised facility within the republican budget of Kyrgyzstan. The amount of external support received in 2016 - 2017 has been somewhat higher than what was available for the government before 2016 (Table 7).

Table 7. Budget support received by the government of the Kyrgyz Republic

Type of donor/ budget support	of 2015			2016			2017		
	Billion KGS	Million USD	% GDP	Billion KGS	Million USD	% GDP	Billion KGS	Million USD	% GDP
Grants and loans – total	30.3	469	7.0	34.9	499	7.6	37.4	543	7.6
Grants total	9.3	144	2.2	9.9	141	2.2	13.4	194	2.7
General budget support	7.1	110	1.7	6.5	93	1.4	7.8	113	1.6
PIP	2.2	34	0.5	3.4	49	0.7	5.6	81	1.1
Bilateral	3.9	60	0.9	2.6	38	0.6	5.0	72	1.0
Multilateral	5.4	84	1.3	7.3	104	1.6	8.4	122	1.7
Loans total	20.9	325	4.9	25.0	358	5.5	24.1	349	4.9
General budget support	3.8	58	0.9	4.2	61	0.9	1.9	27	0.4
PIP	17.2	266	4.0	20.8	297	4.5	22.2	322	4.5
Bilateral	13.4	208	3.1	17.2	246	3.8	16.8	244	3.4
Multilateral	7.5	117	1.7	7.8	112	1.7	7.3	105	1.5

Sources: MoF, NSC, NBKR

7 Relevance of the MFA

Question 1: To what extent was the MFA operation design (including adequateness of financing envelope, focus of conditionality) appropriate in relation to the outputs to be produced and objectives to be achieved?

The answer to this question was based on a consideration of the following issues (i) adequacy of the size of the financial assistance relative to the Kyrgyz Republic's financing needs, (ii) appropriateness of the form of financial assistance, (iii) timing of the operation and (iv) design and focus of conditionality given the country's reform needs, domestic capacity and ownership, the activities of other donors and the inherent characteristics of the MFA instrument itself.

7.1 Size and timing of the operation

7.1.1 Kyrgyzstan's external financing needs

By 2010, Kyrgyzstan's external position had considerably worsened. This period of sluggish growth and macroeconomic decline left the country with pressing external and fiscal financing needs⁵¹.

The IMF estimated a balance of payments financing gap of USD 271 million and USD 149 million for 2011 and 2012 respectively⁵². After deducting net financing from the IMF and disbursements of budgetary support operations from the WB, this implied a residual external financing gap of about USD 330 million for the two years, to be covered by other donors. As indicated in Table 8 below, donor financing was expected to come from the ADB, the EURASEC Anti-Crisis Fund, other bilateral donors, and the EU. EU support comprised disbursements under the EU sectoral budget support programmes which amounted to a total of USD 33.5 million for the 2011 - 12 period.

Table 8. Kyrgyzstan's gross external financing requirements, 2011 - 12 and 2015 - 16 (in USD million)

Financing requirements	2011	2012	2015	2016
Estimated financing gap	271.0	149.0	171.5	76.8
IMF ECF disbursement	29.8	29.7	28.9	28.9
WB	30.0	n/a	40.9	34.5
EURASEC anti-crisis fund	106.7	n/a	n/a	n/a
ADB	50.6	n/a	n/a	n/a
Other grants	n/a	n/a	70.0	0.0
EU	16.4	17.1	n/a	n/a
EU MFA – in USD million	20.5	20.5	16.498*	16.776*
	Originally planned		Based on actual disbursements	
EU MFA – as a share of the 8% financing gap	8%	14%	10%	22%

Sources: EC (2011) 'Ex-ante evaluation.'; IMF (2015) 'IMF Country Report No. 15/113'

⁵¹ European Commission (2012) 'Report from the Commission to the Council and the European Parliament on the implementation of macro-financial assistance to third countries in 2011.'

⁵² European Commission (2012) 'Report from the Commission to the Council and the European Parliament on the implementation of macro-financial assistance to third countries in 2011.'

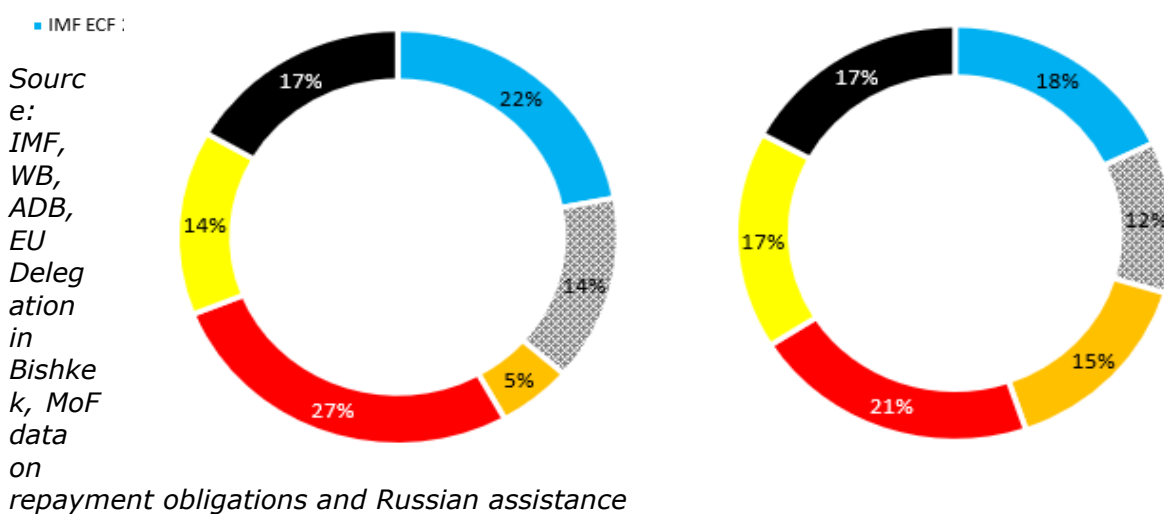
[*]: Exchange rate conversion using InforEuro (with the rate in the month of actual disbursement)

7.1.2 The size of the MFA operation

As per the ex-ante evaluation for this MFA (produced in December 2011), it was envisaged that the MFA would be disbursed in 2011 and 2012. The MFA would have represented 10 per cent of the financing gap (or 12.4 per cent of the residual financing gap i.e. the estimated financing gap factoring in IMF and WB support), or approximately 0.3 per cent of GDP in 2011 and 2012 respectively, if it had been disbursed in these years.

Yet, as a result of prolonged (procedural) delays (see sub-section 5.3.3), the MFA disbursements took place in 2015 (EUR 15 million) and 2016 (EUR 15 million). MFA disbursements corresponded to around 0.3 per cent of the GDP each year and represented approximately 10 per cent of the annual public expenditures on 'public health' over the same period⁵³. In absolute terms, the EU MFA was substantially less than the IMF financing provided over the same period of time (which amounted to EUR 23 million in 2015 and EUR 23 million in 2016). Nonetheless, it was of a similar order of magnitude as the budget support provided by the WB and ADB (see Figure 9). Assistance from Russia accounted for the largest share of budget support every year. The extent of budget support provided via three EU Sector Reform Contracts (SRCs)⁵⁴ (see Section 9) was relatively more sizable in 2016.

Figure 9. Share of selected budget support programmes in Kyrgyzstan (2015 (left) and 2016 (right))



Overall, the MFA accounted for 14 per cent and 12 per cent of the total assistance package (budget support financing exclusively) provided by the multilateral and bilateral donors in 2015 and 2016 respectively. If one considers the total value of EU budget support provided to Kyrgyzstan in both years (i.e. combined MFA and SRC support), the EU MFA stood at 17 and 27 per cent of the total budget support package respectively.

7.1.3 Timing of the operation

In general, the interviews with key stakeholders (including the Ministry of Finance and the Presidential administration), and a basic comparison of the key

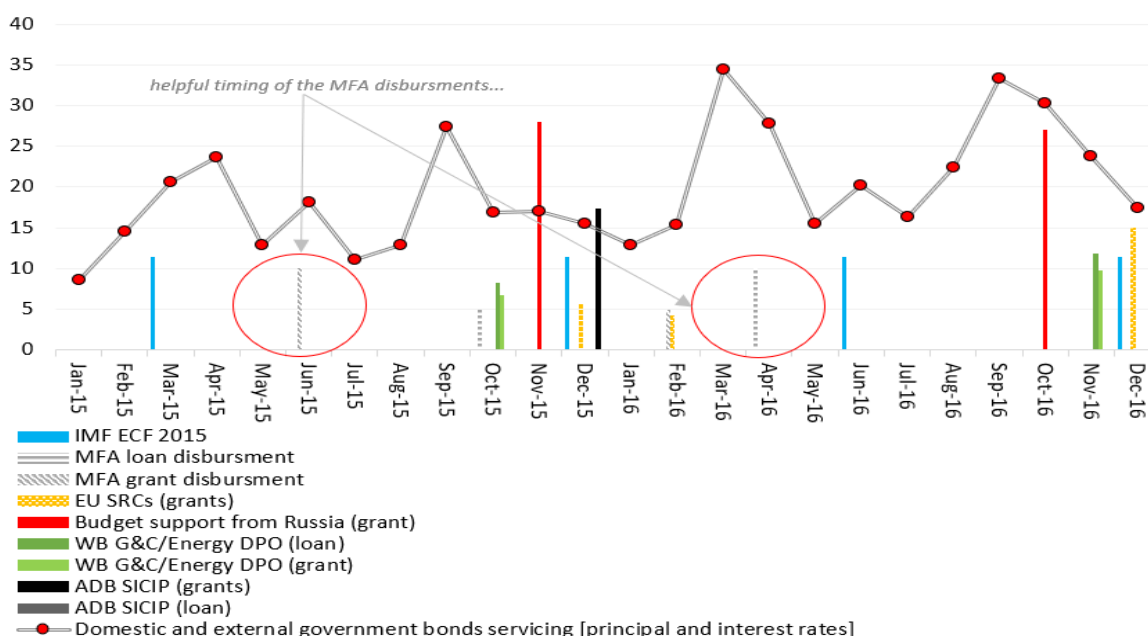
⁵³ Assuming the foreign exchange of som/EUR of 0.013 (as of 31st December 2015). The annual government expenditure on 'public health' stood at 12,729 million som and 13,337 million som in 2015 and 2016 respectively.

⁵⁴ Three programmes covered electoral, education and social protection areas

macro-economic indicators from the two periods (i.e. deficit figures and the average output growth for 2011-12 *versus* 2015 - 16 period) suggest that the EU MFA was somehow less vital during the latter period. The socio-economic and political situations were still fragile over the period 2011-12 (as the country was only recovering from the crisis in 2010), while the public deficit was hovering around 5-6 percent leaving very limited fiscal headroom for the government. Given the delay of the MFA, the Ministry of Finance did not include the revenue from the MFA into the draft public budgets in 2015 (though having done so in previous years, i.e. 2011, 2012 and 2013). This can serve as an indication of reduced expectations and somehow a lower weight that the government attached to the MFA funding once the time passed.

Nonetheless the MFA was still relevant (although less critical) when the actual disbursements took place in 2015-16. The exogenous shock from Russia (induced by a dramatic fall in oil prices and to some extent its aggression on Ukraine) led to a significant depreciation of the Kyrgyz Som between early 2015 and mid-2016⁵⁵. In parallel, the country's fiscal position began to deteriorate which eventually allowed for the MFA disbursements to coincide with important debt repayment obligations (as depicted in Figure 10 below). Furthermore, the period in the run-up to the parliamentary elections (in November 2015) made an extra unassigned source of funding (i.e. the MFA, in the form of foreign currency grant/concessional loan) very attractive to the Kyrgyz government who, at the time, was in the process of introducing new voting technologies (based on biometric voter identification and automated counting of ballots). In light of these electoral reforms, significant funding was needed and ardously solicited by the Kyrgyz government from the international donor community. In this context, the disbursement of the MFA could be interpreted, at the political level, as indirect EU support to the organisation of democratic parliamentary elections in Kyrgyzstan. Thus, despite a marked delay of the operation, the time of the disbursements remained relevant even if by sheer coincidence.

Figure 10. MFA and other budget support type assistance provided to Kyrgyzstan in 2015/16 versus debt repayment obligations, in EUR million



Source: IMF, WB, ADB, EU Delegation in Bishkek, MoF data on repayment obligations and Russian assistance.

⁵⁵ The som lost 16 per cent of its value against the USD between 1st January 2015 and 1st April 2016. The exchange rate of som has been typically highly correlated with Russian ruble

Note: for budget support from Russia the chart includes KGS2,232.1 million (around USD 30 million) of Russian grant provided via the published Cash Plan for the MoF in October 2016. Similar document for 2015 was not published, but Deputy Minister of Finance informed that Russia would provide USD 30 million grant to Kyrgyzstan (interview from 22 Oct 2015).

* Exchange rate USD into EUR as of the last day of the month based on the OFX.com available at: <https://www.ofx.com/en-gb/forex-news/historical-exchange-rates/yearly-average-rates/>

Conclusions

The MFA operation in Kyrgyzstan, though smaller than the extent of financing offered by the IMF, was judged a satisfactory amount. The small-scale nature of the EU MFA was explained by the fact that it was provided to Kyrgyzstan on an exceptional basis and was only intended to supplement the assistance offered by the IMF (in the context of the ECF arrangement) and support from other international and bilateral donors, such as the WB and ADB.

Nonetheless, in spite of its small-scale nature and the delay associated with its disbursement, the MFA operation in Kyrgyzstan was still viewed as relevant, offering the Kyrgyz government more fiscal room to manoeuvre and contain the mounting economic difficulties the country was facing when the Russian economic crisis began unfolding.

7.2 Form of the financial assistance

Grant versus loan

The EU MFA should, by default, take the form of loans⁵⁶. Grant-only arrangements may be considered, though this depends on the beneficiary country's circumstances in terms of its development and debt sustainability levels. The Commission's ex-ante evaluation recognised that Kyrgyzstan fell in the group of countries qualifying for grant support⁵⁷:

- Kyrgyzstan's per capita income was reported to be well below the WB's threshold for qualifying for International Development Association (IDA) support (1,175 USD per capita)
- Its poverty ratios were high and increasing (with over 30 per cent of people living below the general poverty line and over 50 per cent in the rural areas).
- All debt ratios exceeded the recommended thresholds (except for the debt service ratio, reflecting the large share of concessional debt).

The Commission's assessment was consistent with similar reviews from the WB, the ADB and the IMF which concluded that Kyrgyzstan ought to be treated as a "fully concessional assistance country." The European Parliament and the Council of the European Union considered the possibility of offering the Kyrgyz Republic a full grant, but the general preference was for a "50-50 split between [...] grant and loan components."⁵⁸ This was justified considering that other forms of support, notably in grant form, have been in place in Kyrgyzstan for some time, comprising mainly humanitarian and development assistance⁵⁹. The MFA grant component accounted for

⁵⁶ European Commission (2011) 'Report from the Commission to the Council and the European Parliament on the implementation of macro-financial assistance to third countries in 2010.'

⁵⁷ European Commission (2011) 'Ex-ante evaluation statement on EU macro-financial assistance to the Kyrgyz Republic.'

⁵⁸ European Commission (2011) 'Ex-ante evaluation statement on EU macro-financial assistance to the Kyrgyz Republic.'

⁵⁹ Interviews with EU officials (EU and Kyrgyzstan-based).

10 per cent and 6 per cent of the overall grant assistance provided to the country in 2015 and 2016 respectively⁶⁰.

The loan itself was provided on concessional terms and this highly concessional form of the MFA has been seen by Kyrgyz authorities as exceptionally attractive⁶¹. The grant component was also well-received, which is not surprising given that grants are generally non-repayable and bear no risk to the recipient.

Un-earmarked character of the MFA

The MFA differs fundamentally from conventional project financing – it provides the recipient with flexibility to use the loans / grants for whatever purpose as deemed appropriate. This feature of the MFA has been highlighted by the Kyrgyz government officials as another important and attractive characteristic of the financing (often not exhibited by other forms of external aid offered)⁶². For instance, while China approved over EUR 1 billion loans in 2015 and 2016, those were assigned to specific investment projects⁶³ (of which many were delivered by Chinese subcontractors paid directly by the Chinese creditor/lender) which thus did not leave the government with much discretion over the spending of those resources. Akin to the EU MFA, budget support provided by Russia is not formally earmarked, though it has not been uncommon for the Kyrgyz government to formally / officially state how the budget support received would be spent (e.g. housing for military personnel).

However, given the un-earmarked character of the MFA operation, it is not possible to establish the exact destination of the financing provided⁶⁴.

Conclusions

On the basis of Kyrgyzstan's per capita income levels, poverty, and debt ratios at the time of the MFA negotiations, grant support was first considered. There was nonetheless some degree of discord among Member States, the Council of the European Union and the European Parliament as to the form of assistance and, eventually, a compromise was reached. The MFA operation would comprise a mix of grants and loans. This was deemed appropriate in the context of the overall package of EU support (which comprised a significant grant component funded by other EU instruments).

7.3 Design and focus of conditionality

MFA is designed to meet the recipient country's external and/ or budgetary financing needs and to promote structural reforms. It is therefore based on strict economic policy conditions⁶⁵. Various aspects of the design of the MFA instrument need to be considered in order to establish whether the operation (and associated conditions) were relevant, given the political, social, economic and institutional context of Kyrgyzstan. These are discussed in subsequent sub-sections.

⁶⁰ The total grant assistance provided to Kyrgyzstan accounted 2.2 per cent of GDP in 2015 and 2016 respectively. Based on the data from the Ministry of Finance and the IMF.

⁶¹ Interviews with key Kyrgyz authorities.

⁶² Interviews with key Kyrgyz authorities.

⁶³ For instance, North-South road (USD 297.7 mln), Energy transmission line Datka-Kemin (USD 389.8 mln) and Reconstruction of the Heat and Power Plant in Bishkek (USD 386 mln) as part of Public Investment Programme.

⁶⁴ In terms of the mechanics of the transfer of the MFA financing, the monies were initially disbursed to the forex account of the Ministry of Finance at the National Bank of Kyrgyz Republic. From then on, the financing can be used to boost the foreign reserves and/or finance the government expenditure. It is not possible to trace the final allocation of the MFA funding.

⁶⁵ European Parliament (2017) 'Macro-financial assistance.'

7.3.1 The extent to which the operation addressed priority areas for reform

The nature/focus of the policy reforms (upon which the disbursement of the MFA is conditional) is typically informed by a country-specific needs assessment. Traditionally, at EU-level, such assessments comprise: (1) an ex-ante evaluation; and/or (2) an Operational Assessment. The latter generally focuses on the beneficiary countries' PFM systems, specifically the procedures and the organisation of the ministries of finance and central banks, as well as the management of accounts receiving EU funds⁶⁶.

The Commission's 2011 ex-ante evaluation for Kyrgyzstan listed, *inter alia*, the country's structural reform needs, which spanned the following areas: (1) public finance management (PFM); (2) banking; (3) trade; and (4) poverty alleviation. The need for PFM reform, notably in the areas of PFM systems and budget transparency, was also highlighted in the Commission's 2012 Operational Assessment⁶⁷. Ultimately, the MFA operation was accompanied by conditions/reforms in the aforementioned policy areas, except for poverty alleviation. Additional reforms were instead targeted at enhancing the business/investment environment. The specific conditions that were part of the MFA package to Kyrgyzstan are detailed in Annex 10.

In general, the reform areas targeted by the MFA were deemed appropriate⁶⁸. These represented areas of vulnerabilities for Kyrgyzstan and were at the forefront of the reform package driven by the Kyrgyz government and the international donor community. The relevance of each targeted reform area is discussed below.

Relevance of reform areas targeted by the MFA operation

Public finance management

The country's PFM system had scored poorly in the 2009 PEFA⁶⁹. Consequently, PFM became a priority area for action for the Kyrgyz government. Strategic steers in the PFM area were detailed in the government's Medium Term Development Programme 2012 - 14, while a new PFM Reform Action Plan was approved in 2012⁷⁰.

Testament to the Kyrgyz government's reform priorities in the PFM area were various concrete measures having been (or expected to be) implemented, including the establishment of a basic legal framework for the introduction of a Single Treasury Account and the enactment of a new public procurement law and an anti-money laundering law (in line with the 2012 Financial Action Task Force (FATF) standard). The new law aimed "to remove loopholes in public procurement, decrease opportunities for corruption, and increase the value for money obtained from public funds."⁷¹

However, in spite of these efforts, the 2012 Operational Assessment concluded that "few improvements" had been made. It noted that delays in implementing reform were particularly common and that PFM reforms had yet to materialise. Specifically, the system of external audit was recognised as an important weakness and longer-term support in capacity-building was thus recommended. Technical advice and

⁶⁶ European Commission (2011) 'Report from the Commission to the Council and the European Parliament on the implementation of macro-financial assistance to third countries in 2011.'

⁶⁷ European Commission (2012) 'Operational Assessment of the financial circuits and procedures in the Kyrgyz Republic.'

⁶⁸ Evidence gathered from desk review and stakeholder interviews (with EU and Kyrgyz stakeholders).

⁶⁹ European Commission (2012) 'Operational Assessment of the financial circuits and procedures in the Kyrgyz Republic.'

⁷⁰ European Commission (2011) 'Ex-ante evaluation statement on EU macro-financial assistance to the Kyrgyz Republic.'

⁷¹ European Commission (Date unknown) 'Macro-financial assistance to the Kyrgyz Republic: Disbursement of the second tranche'

support were already being provided by various development partners, notably through the PFM Multi-Donor Trust Fund (MDTF). Specifically, the MDTF focused on: (1) enhancement of the budget process; (2) improvement of the Medium Term Budget Framework (MTBF); (3) internal audit and control; and (4) capacity-building in PFM. Reforms in other PFM-related areas, notably public procurement, accounting standards and public external audit were not covered by the MDTF, but benefited from separate donor technical assistance projects, such as the WB Governance Technical Assistance Credit (GTAC).

Given the pressing need to drive and sustain reform in this area, the MFA conditionality in the PFM area was justified.

Banking

Kyrgyzstan's banking system was severely affected by the 2008-9 financial crisis. As noted by the Commission, "a weakly-regulated banking sector, in particular with respect to flaws in early intervention, bank resolution, and external pressure on the central bank, was a major channel of the negative economic impact of the crisis [...] as it suffered from diminished depositor confidence and the economic effects from the ethnic violence events in the south of the country."⁷²

In light of these severe deficiencies, the Kyrgyz government embarked on a series of banking sector reforms, which comprised inter alia the amendment of several banking regulations and the enactment of a Banking Code. The latter aimed to bring the Kyrgyz bank resolution framework in line with international standards, including the Basel Core Principles, and strengthen the independence of the central bank. It also sought "to limit the scope of judicial review of decisions taken by the central bank with respect to license revocation and bank resolution, enhance legal protection for the central bank's staff, establish the central bank as the sole authority to hold and manage official foreign reserves," and "strengthen the internal oversight of the central bank."⁷³ Other major government initiatives, such as the Sustainable Development Programme (part of the wider National Sustainable Development Strategy for 2013 - 2017) focused on strengthening the financial system.

Various development partners have been supporting banking reforms in Kyrgyzstan. The IMF's 2011 ECF arrangements with Kyrgyzstan comprised various structural reform conditionalities, in part focused on strengthening the financial sector (including, by endowing the central bank with adequate powers to resolve banking problems). In that context, IMF assistance was sought in preparing the Banking Code. This translated in "intensive technical assistance and the posting of a resident legal advisor for 18 months in Bishkek."⁷⁴ Similarly, the WB's Financial Sector Development Project (2012 - 2020) for the Kyrgyz Republic seeks to enhance financial sector stability and increase access to financial services. Specifically, the project was designed inter alia "to improve the legal, regulatory, and supervisory framework for the banking sector and to increase the NBKR's capacity to monitor and address vulnerabilities."⁷⁵

The MFA conditionality (pertaining to the submission of a new Banking Code to Parliament) was aimed at backing ongoing reforms in the banking sector. The draft Banking Code was submitted by the Kyrgyz government to Parliament in September 2013. However, its adoption was much delayed, given "the innovations it introduced,

⁷² European Commission (Date unknown) 'Macro-financial assistance to the Kyrgyz Republic: Disbursement of the second tranche.'

⁷³ European Commission (Date unknown) 'Macro-financial assistance to the Kyrgyz Republic: Disbursement of the second tranche.'

⁷⁴ European Commission (Date unknown) 'Macro-financial assistance to the Kyrgyz Republic: Disbursement of the second tranche.'

⁷⁵ World Bank (2012) 'KG Financial Sector Development Project.'

the complexity of issues,” and “the need to translate the code to the Kyrgyz language.”⁷⁶ The Economic and Budgetary Committee of the Parliament eventually adopted the draft Banking Code (on 15 June 2015). It was, however, reduced to a standard law, the approval of which was expected in March/April 2016. The passage of the law has been lingering in Parliament since then. The 2017 IMF country report for Kyrgyzstan indicates that various amendments to the law were sought by Parliament. These were submitted by the Kyrgyz authorities concerned but rejected by the Ministry of Justice on constitutionality grounds⁷⁷. The authorities committed to resubmitting to Parliament the necessary amendments, requesting their approval and adoption in 2018.

The delays encountered with regards to the enactment of the new Banking Law have raised questions (from stakeholders consulted during the study) as to the extent of the role played by the EU MFA. For some, the MFA conditionality could have been “more ambitious,” hence allowing actions / policies from development partners, such as the IMF, to bear fruit more quickly. The rationale for more ambitious conditionality appears justified, though it should be noted that the MFA conditionality was developed in close collaboration with development partners, notably the IMF, and focused on aspects of the reform process deemed necessary. The extent of resistance met with local authorities could potentially not have been foreseen, given the government’s own commitment to reforming the banking sector (notably by enacting a new Banking Code) after the 2008 - 09 financial crisis.

Trade

The Kyrgyz Republic became a member of the World Trade Organisation (WTO) in 1998. Since then, the Kyrgyz government has been supporting measures in trade policy and trade facilitation sectors to increase trade and transport flow. In recent years, the Kyrgyz Republic also started preparations to join the trilateral customs union (CU) of Belarus, Kazakhstan, and Russia (which later became known as the Eurasian Customs Union (EACU)), which is expected to further open export markets as well as improve the economy’s competitiveness and investment environment.

The second review of the trade policies and practices of the Kyrgyz Republic at the WTO took place on 19-21 November 2013. The review was based on a report by the WTO Secretariat and a report by the Government of the Kyrgyz Republic. While noting the extent of the progress made in matters pertaining to foreign trade, the WTO members pointed to a number of areas where further improvements could be made, including: tariff rates and non-tariff measures; transparency and notification obligations; investment strategy; and regulatory matters (e.g. intellectual property and government procurement). Reassurances were also asked by WTO members with regards to Kyrgyzstan’s accession to the EACU, specifically in relation to the extent to which WTO processes will be maintained / followed.

Through the MFA condition on trade, the EU stressed the importance of WTO membership and encouraged the Kyrgyz Republic to constructively interact with the WTO Secretariat. The opening and closing statements made by the Kyrgyz Republic at the WTO review session on 19 and 21 November 2013 confirmed that most of the recommendations received on the WTO report were being fulfilled. Specific actions included the adjustment of import tariffs to address the identified breaches of bound tariff rates. In the same vein, the Kyrgyz government confirmed its intention to consult and negotiate with the WTO members once its accession to EACU was confirmed.

⁷⁶ IMF (2016) ‘IMF Country Report No. 16/186.’

⁷⁷ IMF (2018) ‘IMF Country Report No. 18/53’

Given the need to sustain reform in this area, the MFA conditionality in this area was justified.

Business/investment

Kyrgyz authorities have, for long, attached a high priority to fostering a business environment that is conducive to investment and private-sector growth. To this end, much focus has been placed on achieving a stable and predictable investment climate through a number of reform actions, e.g. proper contract enforcement, strengthened property rights, reduced red tape, etc.

Various development partners have been assisting the Kyrgyz authorities in pursuing these reforms. The IMF, in its 2012 - 14 Medium Term Development Strategy (MTDS), indicated that support to Kyrgyzstan would, in part, be "oriented towards the recovery and strengthening of good investment climate in the country, state regulation free from bureaucratisation and provision of economic freedom to the economic entities." The EBRD, on the other hand, reiterated its support to the Council for Business Development and Investment (the then Investment Council), notably in addressing the main barriers to doing business in Kyrgyzstan.

The WB's 2013 Doing Business Report indicated that the Kyrgyz Republic was among the top ten countries that had improved their rankings substantially since 2005. Nonetheless, it was recommended that the authorities do more to improve the institutional and regulatory environment by improving conditions to starting a business, streamlining the licensing process (and inspection regimes), and protecting investors.

The MFA condition (pertaining to the investment and business environment) was put forward in view of helping the Kyrgyz authorities address several persistent weaknesses associated with the business environment, notably red tape. It was therefore relevant and justified.

7.3.2 The extent to which the design and focus of the MFA operation in Kyrgyzstan was in line with general/wider objectives of the EU's MFA operations

An overarching objective of the EU MFA is "to restore a sustainable external financial situation, while encouraging economic adjustments and structural reforms."⁷⁸ Various pre-MFA/early-stage consultation documents and formal EU communication, including the Commission's 2011 ex-ante evaluation of MFA to the Kyrgyz Republic, included similar references and stressed the need for the operation "to focus on structural measures most relevant for ensuring macroeconomic stability."⁷⁹ This underlying objective/purpose of the Kyrgyz MFA operation (which stems from wider EU MFA objectives) provided a framework for the design and focus of the MFA conditionalities (see sub-section 2.3 (intervention logic)).

7.3.3 Relevance of specific MFA conditionalities

As regards the relevance of specific conditionalities, various stakeholders consulted during this study expressed the view that the MFA conditions were generally "less ambitious" when compared to the conditions attached to other donors' support (e.g. the IMF). This is, however, not a valid criticism given that the MFA instrument constitutes emergency financial assistance that seeks to address economic vulnerabilities in periods of crisis. Conditions are therefore purposely designed so as to enable prompt disbursement of financial assistance with the aim of addressing the immediate economic crisis while, at the same time, supporting a longer-term reform

⁷⁸ European Commission (Date unknown) 'Macro-Financial Assistance (MFA) to non-EU partner countries.'

⁷⁹ European Commission (2011) 'Ex-ante evaluation statement on EU macro-financial assistance to the Kyrgyz Republic.'

programme. Moreover, the relatively small size of MFA (as compared to IMF programmes) also implies that MFA conditions have to be proportional and cannot be as far reaching as the IMF reforms.

Additionally, the MFA was considered an “extra political gesture” to Kyrgyzstan by the EU⁸⁰. As part of an official visit to Brussels in 2013, several discussions took place between the Kyrgyz President, his delegation and key EU officials⁸¹. During these meetings, the EU displayed widespread support for Kyrgyzstan’s efforts to carrying out democratic reforms. The President of the European Parliament, Martin Schulz, called Kyrgyzstan “a strategically important partner in the region” and reiterated his institution’s support for strengthening the country’s parliamentary democracy. In the same vein, the European Commission’s former President, Jose Manuel Barroso, praised Kyrgyzstan’s efforts to consolidate its democracy and assured the Commission’s full support for the Kyrgyz government’s commitment to set on a new political course, focused on the promotion of social and political stability and security as a foundation for economic and social recovery. To aid this process, the EU confirmed the provision of MFA to Kyrgyzstan. A separate agreement was also signed between the EU and Kyrgyzstan’s Ministry of Justice. The agreement pledged the allocation of some EUR 13 million for the implementation of further needed reforms in the areas of democracy and rule of law⁸². The fact that the operation bore greater political significance could explain the relatively more ‘relaxed’ nature of the conditions agreed as part of the MFA support package offered to Kyrgyzstan.

Finally, the MFA conditions were developed in close collaboration with various donors, notably the IMF, to ensure they complemented ongoing reforms in similar target reform areas. Coordinated actions would have reinforced the reform steer (driven by the donor community) and helped strengthen the government's reform commitment. This could in turn explain strong reform ownership and drive among local authorities.

Overall, on the basis of the above assessment, the specific conditions attached to the MFA can be deemed appropriate. Reform implementation in each target area is further discussed below.

PFM reforms – Condition 1

Resolution No. 96-r on organisational measures to prepare the Medium-Term Budget Framework and draft republican budget for 2015 - 2017 was adopted on March 19, 2014. The Resolution, as foreseen in Condition 1, set out “organisational measures for preparation of the draft republican budget of the Kyrgyz Republic for 2015 - 2017” and required “ensuring consistent budget ceilings in those documents.” The corresponding decision for the period of 2016 - 2018 was in turn adopted in spring 2015.

This condition was met prior to the signature of the (MFA) MoU in October 2014.

PFM reforms – Condition 2

In 2014, the Public Expenditure and Financial Accountability (PEFA) assessment was performed, and a final presentation of the report was made in May 2015. The new PEFA provided a comprehensive assessment of the public expenditure, procurement and financial accountability systems of the Kyrgyz Republic. The report showed considerable improvement, in particular of the PFM infrastructure since 2009, though

⁸⁰ Interviews with EU officials

⁸¹ Sources: The Central Asia-Caucasus Analyst. 2013. ‘Kyrgyzstan's President Visits Brussels.’ Available at: <https://www.cacianalyst.org/publications/field-reports/item/12823-kyrgyzstans-president-visits-brussels.html>; The European Commission. 2010. ‘Joint Economic Assessment: Reconciliation, Recovery, and Reconstruction – The Kyrgyz Republic.’; 2010 High Level Donors Meeting; European Commission. 2010. Ref. Ares(2010)883286 - 30/11/2010

⁸² See previous footnote

indicated that some key elements to ensure the coherence of the structure were still lacking.

This condition was met prior to the signature of the (MFA) MoU in October 2014.

PFM reforms – Condition 3

The Order 'On the Adoption of Normative Legal Acts and of Accounting and Reporting Guidelines for Budget-funded Institutions' was issued by the Ministry of Finance on 30 December 2013. This comprised:

the adoption of the Accounting Policies of the Public Administration Sector;

the Regulation on Preparation of Reporting of the Public Administration Sector; and

the Regulation on Organisation of Accounting of the Public Administration Sector. They will enter into effect at the date of introduction of a Single Treasury Account and of a Single Account Plan.

This condition was met prior to the signature of the (MFA) MoU in October 2014.

PFM reforms – Condition 4

An Action Plan, foreseeing the implementation of seven measures to upgrade Kyrgyzstan's audit standards to INTOSAI standards, was adopted by the Chamber of Accounts on June 8, 2015 (by the order Nr. 04-4/62). The Action Plan confirmed the implementation of INTOSAI standards across various areas, notably:

- financial control;
- competence-building of the Chamber of Accounts staff;
- pilot projects for efficiency audit and development of a methodology for efficiency audits;
- pilot projects for IT audit and development of a methodology for IT audits; and
- methodology for public procurement audits.

This condition was still being implemented at the time of the signature of the MoU and ratification of the MFA operation. It was met by the time the first disbursement was released.

Condition 5

The draft Banking Code, that was foreseen under this condition, was submitted by the Government to the Parliament in September 2013. This marked full compliance with the MFA condition. The Economic and Budgetary Committee of the Parliament adopted the draft Banking Code on 15 June 2015, though in the form of a standard Law. The approval of the Law by Parliament is still pending.

This condition was met prior to the signature of the (MFA) MoU in October 2014.

Condition 6

The second review of Kyrgyzstan's trade policies and practices were held over the period: 19-21 November 2013. The review was based on a report by the WTO Secretariat and a report by the Government of the Kyrgyz Republic, which was officially approved (by the Kyrgyz government) on October 23, 2013.

At the WTO review session, the Kyrgyz government indicated that most of the recommendations received on the WTO report had been / were being fulfilled, including by adjusting import tariffs to address the identified breaches of bound tariff rates.

This condition was therefore met prior to the signature of the (MFA) MoU in October 2014.

Condition 7

The law "On licensing and permitting system in the Kyrgyz Republic" entered into force on October 19, 2013. A further revision of the Law, aimed at streamlining the business licenses and permits system in the Kyrgyz Republic and limiting its number to 91 activities, was proposed and sent for public consultations in the second half of 2015.

This condition was met prior to the signature of the (MFA) MoU in October 2014.

Overall conclusions

The scope and intended objective(s) of the MFA conditions were pertinent at the time of the EU-Kyrgyz negotiations. The pace of implementation was swift, with six out of the seven conditions having been met prior to the MoU being approved, signed and ratified. There are several possible reasons for this, including: (1) the MFA having been accounted for in national accounts (hence the need for timely implementation to ensure that the MFA would be disbursed); and (2) a strong signal from the international donor community (including the EU), as a result of coordinated actions, as regards the need and rationale for the implementation of reforms in specific sectors, thereby reinforcing reform commitment on the part of the Kyrgyz government and relevant authorities.

7.3.4 The extent to which the MFA conditions/reforms were still relevant at the time of disbursement

MFA operations typically require timely implementation of agreed reforms as the disbursement of second and subsequent tranches is conditional upon satisfactory completion of reforms. Specifically, as per Article 1(4) of Decision No 1025/2013/EU, the reforms are expected to be implemented within a period of two and a half years after the entry into force of the MoU. As far as the Kyrgyz MFA operation is concerned, the associated conditions were negotiated on the assumption that they would have to be met by June 2014, i.e. before the expiry of the 2011 IMF Extended Credit Facility (ECF)⁸³. Sufficient time was therefore, accounted for reform implementation in the early stages of the design and implementation process.

The MFA proposal was, eventually approved in October 2013 (after various procedural delays – see sub-section 4.3.2), resulting in a short implementation window for the Kyrgyz authorities. It however, appears that the announcement of the MFA operation led (relevant) Kyrgyz authorities to commence implementation of policy conditionality ahead of signature (and ensuing ratification) of the MoU. The MFA operation was accounted for in national budgets (see sub-section 5.3). This encouraged the Kyrgyz authorities to commence the implementation process swiftly, so as to avoid unnecessary problems of national accounting as well as to prevent undue delays further down the line. As such, had they commenced the implementation of reforms only upon signature and ratification of the MoU, this would potentially have had a knock-on effect on the timing of disbursements. Most of the conditions had therefore been met by the time of the signature of the MoU (see sub-section 5.3.3.3), though at a much quicker pace than what was initially envisaged.

Some stakeholders questioned the possibility for re-opening the negotiation of the MoU to introduce a fresh set of conditions. In the context of the MFA, however, the re-negotiation of reforms is not desirable. This would entail new rounds of consultation with the Member State Committee as well as relevant stakeholders in the recipient country and ultimately a new ratification of the MoU by the Kyrgyz Parliament. A new Commission Decision would have to be issued and, for a second time, the MoU pertaining to the MFA operation would have to be drafted, approved, signed and ratified by Parliament (in the recipient country). This would have resulted in further delays and hindered the design and implementation process. In the case of

⁸³ Interviews with EU officials and international donors.

Kyrgyzstan, specifically, further delays would have amplified the tensions that arose between the Kyrgyz government and the EU (owing to persistent procedural delays in agreement and disbursement of the MFA on both the EU and Kyrgyz end). As such, delays in disbursement were on a few occasions publicly criticised by President Atambayev.

Conclusions

The reform areas targeted by the MFA operation in Kyrgyzstan were generally in line with the priorities set by the Kyrgyz government as well as other donors / IFIs (as part of their support programmes). These were also consistent with wider objectives associated with EU MFA operations, notably to promote structural measures/reforms capable of driving and maintaining macroeconomic stability. Overall, at a thematic level, all areas of conditionality were relevant and well chosen.

As for specific conditions, these were also considered relevant at the time of the negotiations. Most of the conditions were, however, met prior to the signature and ratification of the MoU which led to discussions among stakeholders as regards: (1) the appropriateness of the conditions by the time the MFA was formally approved and disbursed; and (2) the extent to which the EU could have re-opened the negotiations and revised the specific MFA conditions. This was, however, considered minimal and potentially harmful. Our judgement is that this could have triggered further tensions between the EU and the Kyrgyz government. The delays surrounding the agreement and disbursement of the EU MFA had adversely impacted the EU-Kyrgyz relationship and, consequently, a re-negotiation of the conditions could have worsened the already-aggravated diplomatic tension. In addition, a swift implementation of MFA conditions is not uncommon. As such, the MFA support package is generally accounted for in the recipient country's national accounts. In the case of Kyrgyzstan, one could argue that this would have incentivised the timely implementation of reforms by the authorities so as to minimise the risk of delays at the time of disbursement and resulting problems of accounting if the MFA had not materialised as it was originally planned.

8 Effectiveness of the MFA

Question 2: *To what extent have the objectives of the MFA operation been achieved?*

The objectives of MFA to Kyrgyzstan are, as set out, inter alia, in the Memoranda of Understanding (MoU)⁸⁴ to “support the restoration of a sustainable external financial situation for the Kyrgyz Republic, to alleviate its balance of payments and budgetary needs and thereby support its economic and social development.” Beyond this, the objectives are also to support structural reforms.

There are therefore, two strands of analysis to answering the question on effectiveness:

1. *Part 1:* The role of MFA in promoting macroeconomic stability, easing external financing constraints and alleviating Kyrgyzstan’s balance of payments and budgetary needs
2. *Part 2:* Effectiveness of structural reforms.

8.1 Part 1: The role of MFA in promoting macroeconomic stability

In order to assess the role of MFA in promoting macroeconomic stability, easing external financing constraints and alleviating Kyrgyzstan’s balance of payments and budgetary needs, a two-step approach has been applied:

Step 1: Examining the observed macroeconomic outcomes

This step involves the analysis of the actual developments and the extent to which MFA’s objectives have been achieved, irrespective of the actual role of the MFA.

Step 2: Assessing the role and contribution of MFA to observed outcomes

Based on the context explored in Step 1, Step 2 involves a qualitatively driven approach to assess the role and contribution of the MFA. It relies on inferences taken from the desk research, interviews, insights from the focus group with development partners and expert opinions and seeks to explore the potential consequences had the MFA (with or without IMF support) not been provided. In addition, summary of the Debt Sustainability Analysis evaluating the role of the MFA for the sustainability of the public debt during the implementation period is added to this assessment.

8.1.1 Step 1: Examining the observed macroeconomic outcomes

The following section describes the evolution and underlying factors behind the GDP growth and its main components, external sector, public sector finances, inflation and the developments in the banking sector in the period between 2011 and 2016.

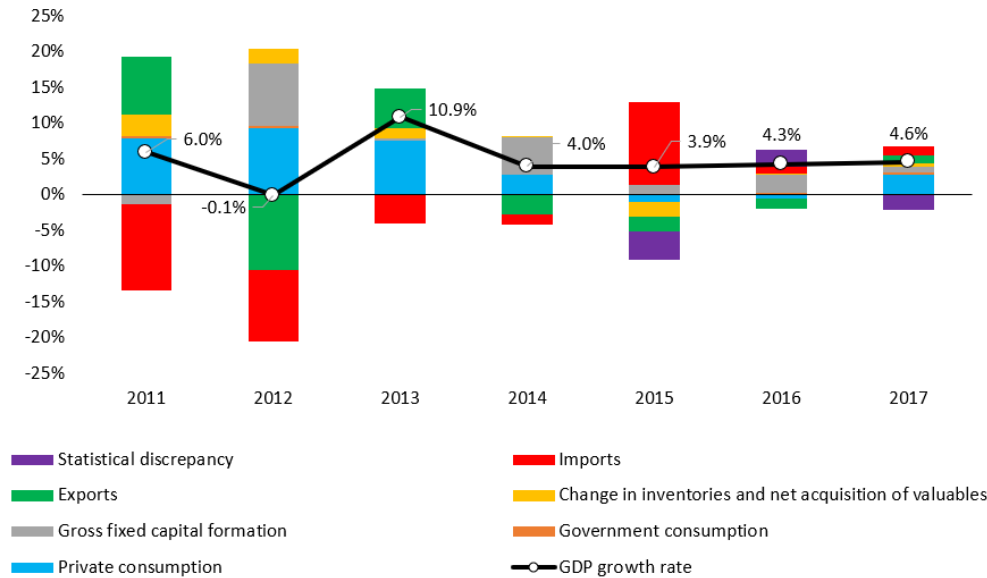
GDP growth

GDP growth performance during 2011 - 2017 was rather stable with annual growth rate averaging at the level of the Kyrgyz economy’s long-term growth rate of 4.5 per cent per annum (Figure 11). The negative growth rate in 2012 was explained by a technical accident at Kumtor gold mine, the largest enterprise of Kyrgyzstan, with adverse effect for the GDP. Fast recovery in 2013 is related to the enterprise’s return to its normal production cycle (low base effect for growth rate). For the most part of the period under consideration, the GDP growth was driven by private consumption fuelled by increasing remittances of the Kyrgyz migrants (except 2015 - 2016, see the next sub-section). Investments into fixed capital were another source of growth. These investments were financed by foreign direct investments and by domestic savings (gross domestic savings increased from -15.9 per cent GDP in 2012 to 1.5 per cent GDP in 2017; source: WDI). The increase in private consumption and investments in fixed capital in 2011 - 2014 resulted in the growth of imports. However, in 2015 - 2017 imports fell substantially without any significant reduction in

⁸⁴ MoU for MFA I and MoU for MFA II signed in February/March 2013 and May 2014 respectively.

private consumption and with continuing growth in investments – this means that some substitution of imports by domestic production was taking place. Other GDP expenditure components did not make much contribution to GDP growth during this period.

Figure 11. Decomposition of real GDP trend, 2011 - 2017, in % of GDP



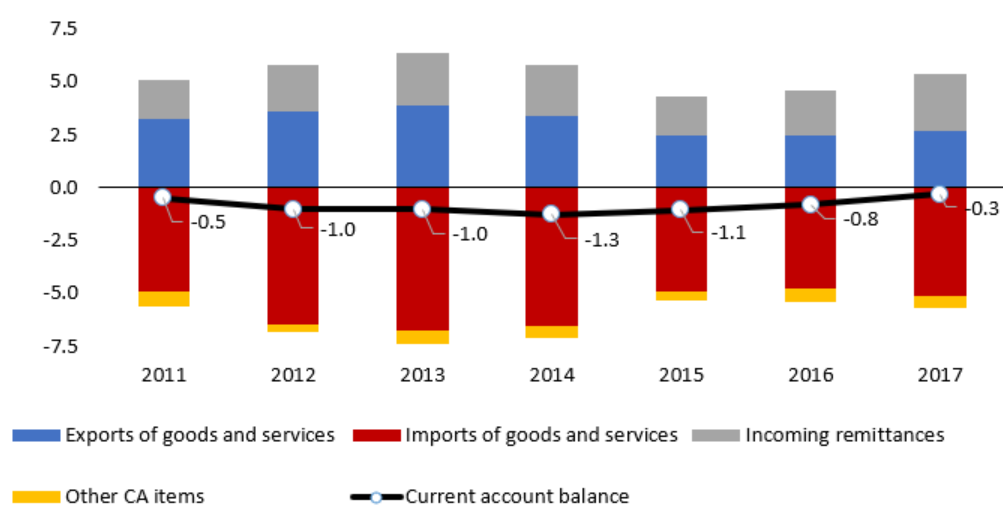
Source: NSC

In terms of the economic sectors, the fastest growth has been registered in construction (average annual growth rate above 15 per cent per annum; this correlates with the growth in investments into fixed capital) and retail trade (the average growth rate close to 8 per cent per annum; this correlates well with the growth in private consumption). Other sectors which demonstrated growth performance above average include communications, transport, and industry.

External sector

It is typical for the Kyrgyz economy to have large negative trade and current account balances (Figure 12). The balance of trade in goods and services during the period 2011 - 2017 fluctuated between -27 per cent of the GDP and -44 per cent of the GDP. The current account deficit was as high as 17 per cent GDP in 2014, but it fell to 4 per cent in 2017. As exports are relatively small and generate insufficient foreign exchange to pay for imports, other sources of imports financing include remittances, FDI, and foreign aid. Remittances sent by Kyrgyz migrants mostly from Russia (more than 90 per cent of the total remittance inflow), but also from Kazakhstan and some other countries are now the most important source of foreign currency for the economy of Kyrgyzstan.

Figure 12. Current account balance and its main components, in USD billion



Source: NBKR

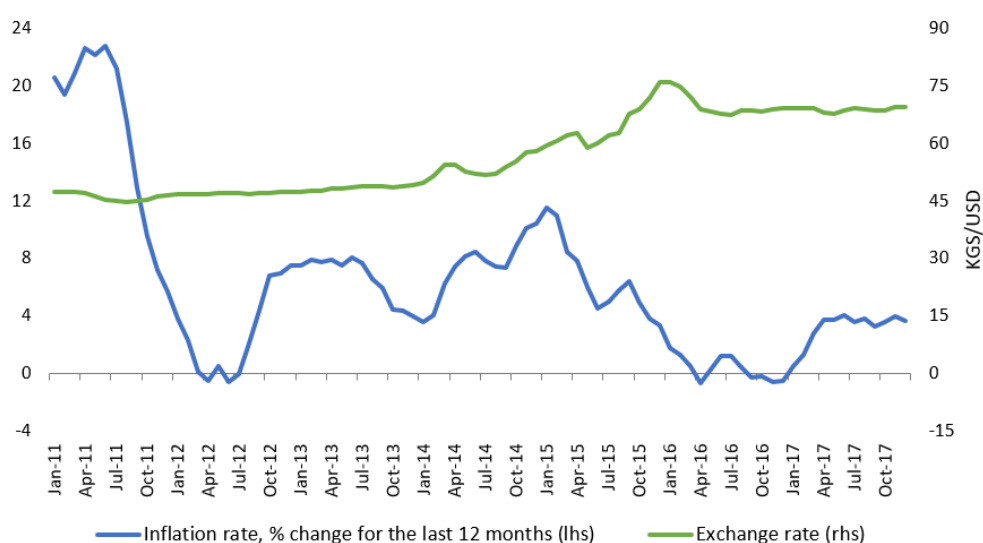
The external sector of Kyrgyzstan experienced a major shock in 2014 - 2016. During the second half of 2014, global energy prices started to fall sharply. This resulted in economic decline and major currency devaluation in Russia and Kazakhstan, two key economic partners of Kyrgyzstan. This had a multi-channel impact on the Kyrgyz economy. First, due to recession in the neighbouring countries the incomes of the Kyrgyz migrants in these countries somewhat fell with associated decline in their remittance-sending capacity.⁸⁵ Secondly, the devaluation of Russian ruble and Kazakh tenge to the US dollar was much more substantial than the devaluation of the Kyrgyz Som to dollar (see below the sub-section on exchange rate). Hence, the Kyrgyz Som appreciated in relation to Russian ruble and Kazakh tenge (from approximately 1.5 KGS/RUR to 1.0 KGS/RUR and from 3KZT/KGS to 5KZT/KGS, respectively). This undermined the price competitiveness of Kyrgyz goods on the Russian and Kazakh markets (key markets for all non-gold exports from Kyrgyzstan). As a result, exports fell during 2014 - 2016 and started to somewhat recover in 2017 only. Imports fell even more dramatically due to Kyrgyz Som's devaluation against USD. Because of the larger fall of imports than the combined reduction in exports and remittances, the current account balance showed an improvement during 2015 - 2017.

Inflation

The economy entered 2011 with high inflation echoing the turbulent political events of 2010 (Figure 13). However, tight monetary policy allowed for fast dis-inflation so the CPI-based 12-months inflation rate fell to zero in the first half of 2012. The inflation rate then stayed at one-digit level for 2012 - 2014 until a new shock related to the KGS/USD devaluation in 2014 - 2015. This was a reaction to the sharp devaluation of the Russian ruble (see above). The super-tight monetary policy employed to stop the devaluation consisted of selling USD from the NBKR reserves; as a result, the country's monetary base shrunk by 23 per cent between July 2014 and March 2015. Simultaneously, the NBKR's reserves fell from USD2.3 billion in July 2014 to USD1.7 billion in January 2016. This policy resulted in disinflation and eventual nominal appreciation of KGS to USD. For the most part of 2016, the 12-months inflation rate hovered around zero. In 2017, it rose to c. 4 per cent. As for the exchange rate, since 2016 it has fluctuated in the range KGS67-70/USD.

⁸⁵ The remittance situation had been partially alleviated by the accession of Kyrgyzstan to the Eurasian Economic Union (Russia and Kazakhstan are two founding members of this Union) which had become effective since 12 August 2015. The legal status of and employment opportunities for the Kyrgyz migrants in Russia and Kazakhstan had somewhat improved after that.

Figure 13. Inflation rate (left axis) and official exchange rate (right axis)



Sources: NSC, NBKR

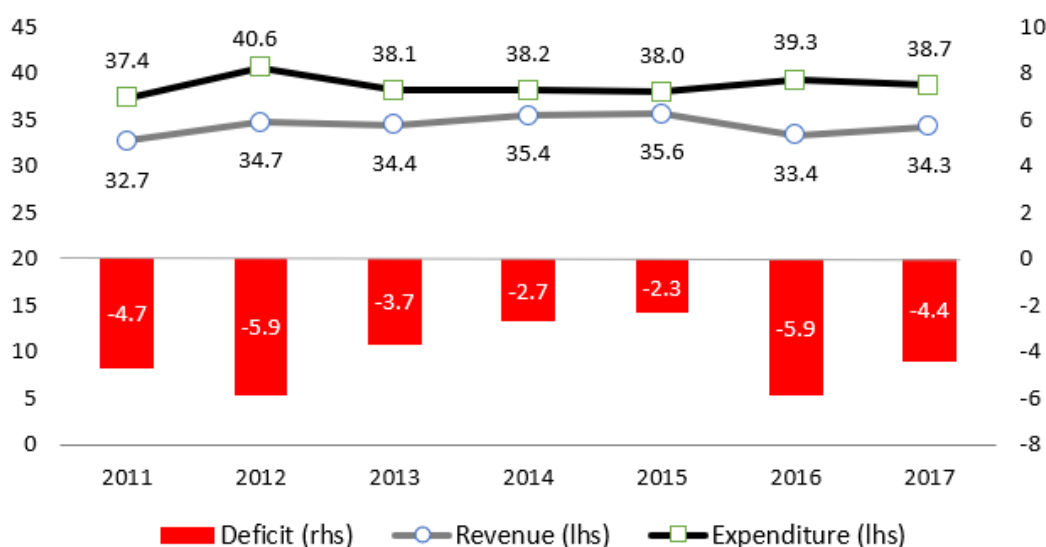
General government budget

Starting from 2011, the general government⁸⁶ expenditure and revenue stayed close to 40 per cent GDP and 35 per cent GDP, respectively (Figure 14). The gap between revenues and expenditures was closed by concessional borrowing from bilateral and multilateral donors as well as by some domestic borrowing on commercial terms. The fluctuations in the size of the government budget deficit are explained by the uneven public investment flow⁸⁷ as well as by some revenue flow irregularities. For example, the above-mentioned accession to the EAEU implied a removal of the Kazakh-Kyrgyz customs border which adversely affected the collections of VAT on imports from the EAEU countries in 2015 - 2016. The reduction of imports related to KGS devaluation in 2014 - 2016 (see above) also resulted in a downfall of different taxes levied on imports (VAT, excises, import duties); the total government revenue fell by 2.2 GDP percentage points in 2016 in comparison to 2015. This lost revenue has been mostly compensated using available reserves (cash balances on the Treasury accounts) and increased issuance of T-bills and T-bonds. In 2017, the increase in receipt of foreign grants by 0.5 per cent GDP allowed improved the revenue situation to some extent.

⁸⁶ The general government budget includes central and local governments' budgets plus the extra-budgetary Social Fund consolidating pension and medical insurance contributions.

⁸⁷ Many of the public investment projects in transport and energy infrastructure financed by borrowing from bilateral (mostly China) and multilateral donors (WB, ADB, EBRD, IsDB and other) are large relative to the size of the economy, so start/completion of some of them may cause a sharp surge/fall in the total government expenditure.

Figure 14. General government revenue & expenditure (left axis), and deficit (rights axis), in % of GDP

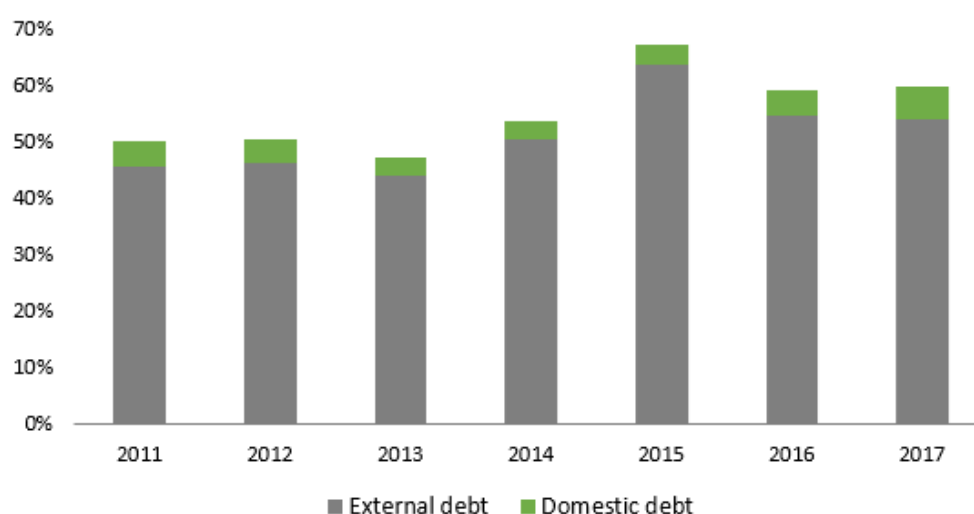


Source: IMF

Public debt

External public debt increased gradually in 2011 - 2014 driven mostly by e massive borrowing from China to finance large infrastructure projects (Figure 15). The share of the debt to China in total external debt of Kyrgyzstan has grown from 10 per cent in 2011 to 42 per cent in 2017. The external debt situation deteriorated in 2014 - 2015 when the mostly USD-denominated debt grew significantly due to the KGS devaluation to USD. The debt-to-GDP ratio exceeded the ceiling of 60 per cent of the GDP established in Kyrgyz law. The situation somewhat eased in 2016 when the NBKR managed to stabilize the KGS/USD exchange rate. In 2015, Russia started its USD300 million debt write-off programme (USD30 million every year); this also contributed to debt reduction.⁸⁸ According to the joint assessment of the IMF and IDA,⁸⁹ the Kyrgyz Republic remains at moderate risk of debt distress, but the debt situation is still vulnerable to large external shocks.

Figure 15. Public debt, in % of GDP



⁸⁸ Russia had fully written-off the remaining part of the debt, over USD 200 million, in early 2018.

⁸⁹ International Monetary Fund (2018) Kyrgyz Republic. IMF Country Report No. 18/53.

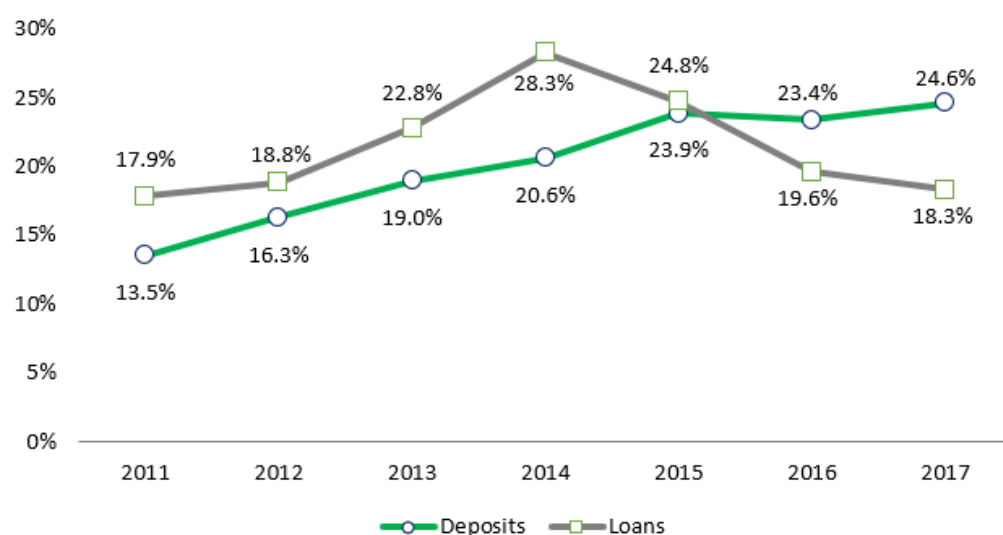
Source: MoF

The domestic debt in Kyrgyzstan is not large, but it increased significantly in 2016 - 2017 (from 3.6 per cent GDP at the end of 2015 to 5.9 per cent GDP at the end of 2017). As mentioned above, the government used the domestic borrowing in the form of T-bills and T-bonds to partially compensate for tax losses.

Financial sector

The financial sector grew rapidly (albeit from a low base) in 2011 - 2014 (Figure 16). However, during this seemingly stable growth period, many banks, micro-financial organizations and their borrowers accepted a very significant currency risk having their assets in national currency and liabilities in foreign currency (mostly USD). The high levels of dollarisation, made the financial sector vulnerable. The 2014 - 2015 KGS devaluation to USD (see above) had a strong negative impact on the financial system. The non-performing loan/total loan ratio surged from 4.5 per cent before devaluation to almost 9 per cent at the end of 2016 (Figure 17)⁹⁰. NBKR reacted by introducing stricter lending regulations (e.g. limiting borrowing in foreign currency for those enterprises or individuals who have mostly Som-denominated income). This resulted in switching of bank clients from borrowing in USD to borrowing in KGS – the share of KGS-denominated banking loans in total loans increased from 42 per cent at the end of 2013 to 62 per cent at the end of 2017, resulting in a rapid de-dollarization of the financial system. These changes affected interest rates: the increased demand for KGS-denominated loans coupled with the increased government domestic borrowing led to some increase in KGS loan interest rates (the average weighted interest rate for Som-denominated loans increased from 20 per cent to 25 per cent per annum). On the contrary, the USD dollar interest rate was falling due to lower demand and, later, due to start of infusion of cheap credits by the Russian-Kyrgyz Development Fund (starting from 2015, but especially in 2016 - 2017). So, average weighted interest rate for USD-denominated loans fell to historical low 10.5 per cent per annum at the end of 2017 (compare to 20 per cent in 2011).

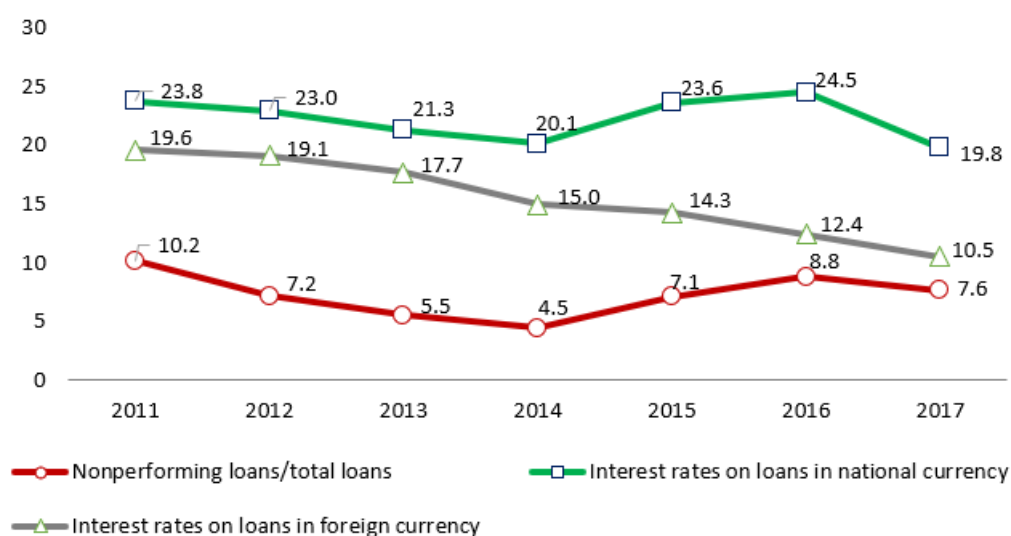
Figure 16. Deposits and loans by banks and micro-financial organizations, in %



Source: NBKR

⁹⁰ It is worth noting that similar shock resulted in much more severe consequences in neighboring Kazakhstan (the ratio was above 20%) and Tajikistan (the ratio reaching almost 70% level).

Figure 17. Non-performing loans and banking loan interest rates, in %



Source: NBKR

8.1.2 Step 2: Assessing of the role and contribution of MFA to observed outcomes

Under this section we consider the counterfactual position for two alternatives:

- Alternative 1: no MFA
- Alternative 2: no MFA and IMF

These two hypotheses serve as the frameworks to contemplate the most plausible counterfactual scenarios and their hypothetical implications.

8.1.2.1 Alternative 1: no MFA - the counterfactual position

Whether financing could have been available from other sources to replace MFA and on what terms

Fundamentally, assessing the plausibility of alternative developments had the MFA not been implemented, is an inherently challenging exercise and any results warrant caveats and caution in interpretation. The counterfactuals have been developed based on brain-storming with local economists, evidence gathered through semi-structured interviews with key informants and stakeholders and a Focus Group with Bishkek-based development partners and desk research. Emerging scenarios were subject to sense checks to make sure that they corroborated with macro-economic data and theory and validated through discussions with the Steering Group.

Error! Reference source not found. below lists the most relevant counterfactual scenarios that were subject to an in-depth analysis in terms of their subjective probabilities.

Figure 18. Summary of likelihood of the counterfactual scenarios (based on partial findings only) – Alternative 1

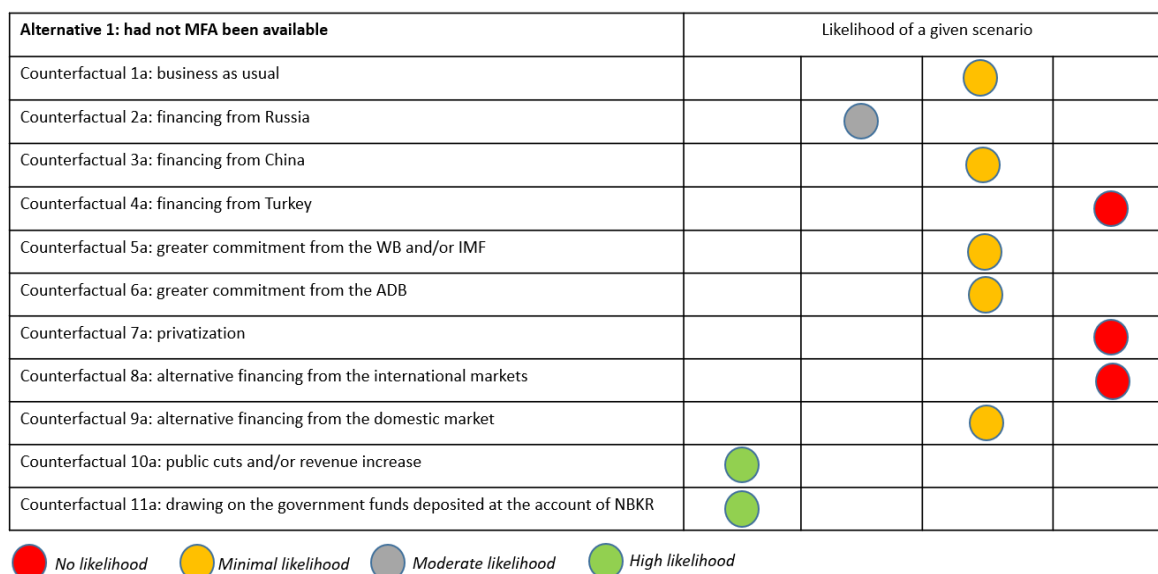


Figure 19 overleaf provides a stylised overview of all alternative sources of finance and policy responses available to the Kyrgyz authorities in the absence of the MFA. These propositions were tested with the participants at the Focus Group in Bishkek, and key informants⁹¹. Overall, we found a high level of consensus among all stakeholders regarding the hypothetical scenarios for Alternative 1 (and 2).

It is followed a discussion on the key findings of the evaluation with respect to each of the following alternatives courses of action that the Kyrgyz authorities could potentially have pursued in the absence of the MFA:

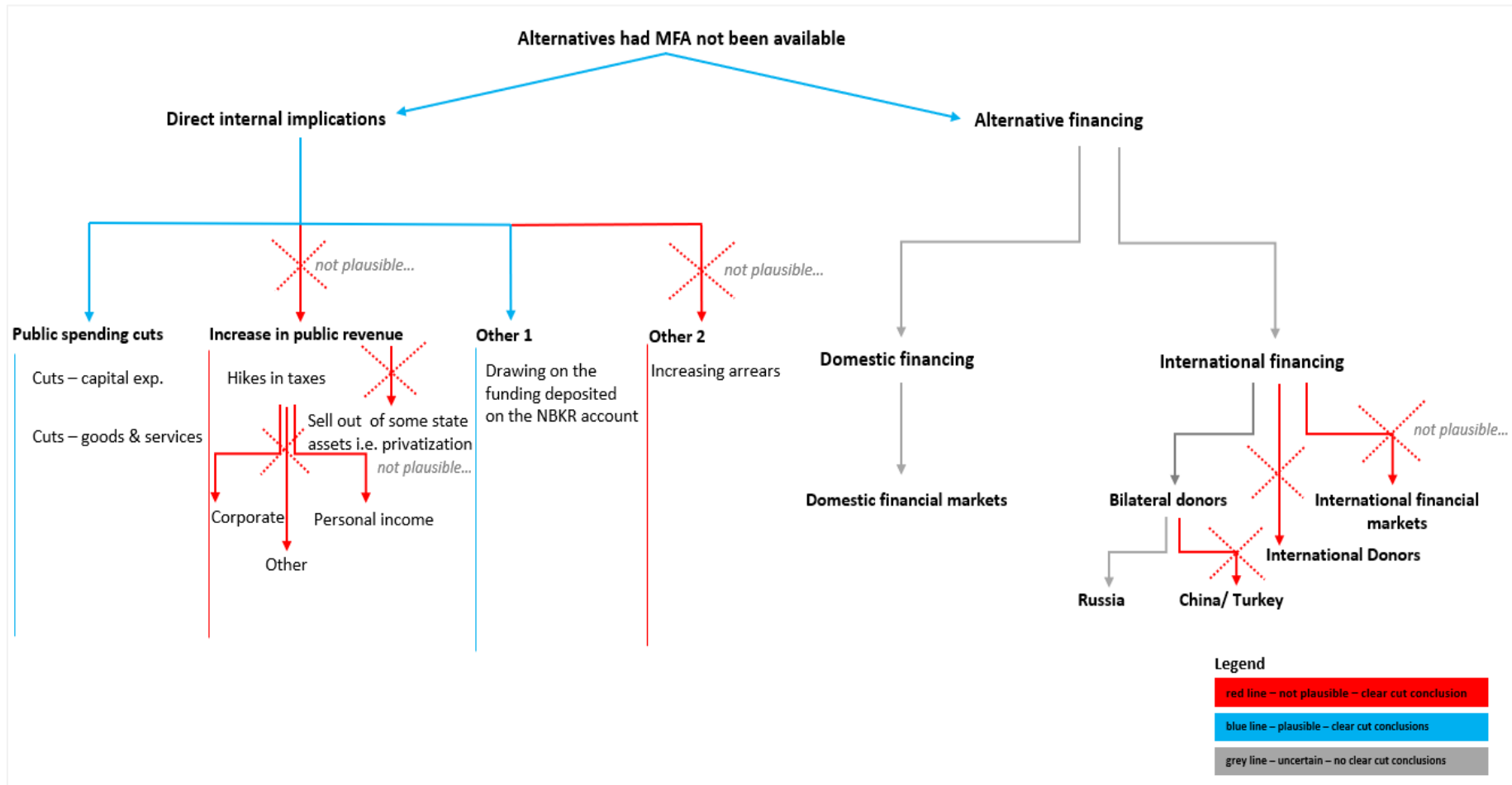
- Increased financing from the IMF or the WB to compensate for the non-availability of MFA;
- Increased financing from bilateral donors;
- Borrowing from domestic financial markets;
- Borrowing from international financial markets;
- Policy response in the form of sharper fiscal adjustment or generating revenue from taxes or privatisation or other sources.

Annex 9 provides a more detailed evidence base related to each of these scenarios.

Overall, we have found that some scenarios would not have been mutually exclusive. More concretely, the combination of cuts in public expenditures coupled with the withdrawal of some government’s reserves from its account at the NBKR and some increase in assistance from Russia emerged as the most plausible counterfactual scenario.

⁹¹ In particular the IMF (both, US and Kyrgyzstan based staff), the EU Delegation and the WB

Figure 19. Alternative scenarios for obtaining finance had MFA not been available (but with IMF continuing)



Source:

ICF

International donors

The possibility of greater support from the IMF under Alternative 1 was rejected by the Fund's staff⁹². Although the first WB interviewee⁹³ speculated that the Bank could have possibly stepped in to fill in the gap created by the absence of the MFA, this perception has not been validated by the WB staff based in Kyrgyzstan⁹⁴. Likewise, the evidence gathered also does not suggest that the absence of the MFA would have triggered any additional financing from the ADB.

Bilateral donors

There is little evidence of the past attempts as well as the appetite of the Kyrgyz government to seek budget support from Turkey. While China has been a source of very significant financing, this was predominantly in the form of project financing assigned to infrastructure investment, and not budget support type assistance.

There were some discrepancies in views regarding the extent to which Russia could have stepped in. While Russia has indeed been a crucial bilateral donor and has been providing budget support to the Kyrgyz Republic, its size typically has not exceeded USD 30 million per annum⁹⁵ while filling in the MFA gap that had emerged in the absence of it would have required circa USD 65-70 million⁹⁶ in 2015 alone (or USD ~45 million in 2015 and 2016 respectively). Yet, the political context i.e. excellent relations between former Kyrgyz President Atambayev and President Putin as well as the closure of the US military base in Manas in 2014 would probably have constituted a very good platform for the Kyrgyz Republic to secure additional financial assistance from Russia in 2015 and 2016⁹⁷.

While the MFA consisted of a grant and loan component, it is not certain whether alternative Russian support would have come in a similar or even identical format. For reference, Russian budget support assistance in 2015 and 2016 came entirely in the form of grants⁹⁸. In this context one could also reflect on whether more Russian support would have prevented the Kyrgyz legislators to drop the "anti-LGBTI" and "foreign agent" legislation.

Domestic financial markets

Under this option, the government could have raised the necessary financing (to replace the MFA) in domestic currency. While the domestic debt market has been relatively shallow (stock of domestic securities was circa 3 per cent of GDP in early 2016⁹⁹), the government increased its borrowing from ~USD 46 million in 2015 to ~USD 68 million in 2016. Yet, the yield on the 2-years government T-bond between May 2015 and June 2016 was high and oscillated between 15.7 per cent and 18 per cent. Therefore, this option would have been far more expensive than seeking some more concessional support i.e. from Russia.

International financial markets

Even though Kyrgyzstan received its first rating from Moody's in late 2015, several factors suggest that this was not a plausible alternative to the MFA: potentially

⁹² Interview with the IMF team that took place during the mission to Washington D.C.

⁹³ WB Economist who Co-lead on DPO-2 and Competitiveness and Governance DPO

⁹⁴ Local WB Economist and Senior Economist

⁹⁵ Budget support exceeding USD 30 million, unlike the amount below this threshold, requires the approval of the Russian parliament (Duma)

⁹⁶ Actual USD amount would depend on the points of time at which disbursements would take place given forex evolution (EUR - USD) during the year

⁹⁷ Views expressed by number of interviewees during the mission to Kyrgyzstan

⁹⁸ Kyrgyzstan did not borrow any money from Russia since 2009

⁹⁹ ...of which banks held 1.3 percent of GDP and institutional investors (social fund and deposit protection agency) held 1.4 percent

prohibitive interest rates¹⁰⁰, no trace of concrete discussions/ actions undertaken by the government¹⁰¹ and some doubts about the capacity of the Debt Department of the Ministry of Finance to handle the first historical issuance of bonds on the international markets back in 2015/2016. In addition, IMF ECF programme with Kyrgyzstan prohibits non-concessional borrowing.

Fiscal adjustment/ other internal resources

An increase in government revenue i.e. through privatisation of some state assets and/ or hikes in taxes was unlikely as the country's track record in privatisation was very modest and the changes in the country's tax regime would have required a lengthy legislative process and political will that was absent (more details in Annex 9). However, what seems more probable is that the government would have reduced some spending from the 'unprotected spending' category i.e. capital expenditures accounted for KGS 5.4 billion (ca. USD 84 million) and KGS 8.4 billion (USD 120 million) in 2015 and 2016 respectively. Some cuts in expenditures on goods and services (i.e. travel expenses, communication expenses etc) could have also taken place. It is very unlikely that spending cuts would have affected 'protected spending' categories.

In addition, the opportunity of alternative funding that emerged during the discussions with the IMF in Washington DC was the fiscal buffer in the form of the government's reserves deposited at the NBKR. As of early 2015, there was circa USD 200 million available to use, and the government could have drawn on it as well.

Whether the economic outcomes would have been weaker or different in the absence of the MFA financial support

There was strong consensus among the interviewees (including the Ministry of Finance and the IMF), Focus Group participants and the local experts that the hypothetical spending cuts affecting categories like capital investment and goods and services could have materialised, but their cumulative size over the analysed period would have been almost certainly significantly lower than EUR 30 million (because of other alternative and complementary sources of financing namely, from Russia and/or government funding deposited at the NBKR). Cuts in public expenditure would however, have impacted aggregate demand and consequently output growth to a limited degree only (proportionate to the size of cuts assumed).

The study has not found any evidence supporting the hypothesis that the absence of the MFA financing could have led to some perceptible repercussions in terms of business confidence. The extent of awareness surrounding the MFA support was/ has been marginal which could have been due to the delays encountered in the early stages of the implementation process. For this reason, the potential impact on the foreign exchange market resulting in the depreciation of the Som and possibly the rise in inflation, in line with the standard national accounts interpretation, would have been improbable.

The Debt Sustainability Analysis (DSA) (more under Section 11) shows that the absence of the MFA would have mainly affected the revenue side, a variable that in turn affects the debt dynamics. For the sake of simplicity and clarity, the DSA assumed that the public cuts would have corresponded to the total size of the MFA (EUR 30 million). While it is different what the counterfactual analysis shows (here, it suggests that the absence of the MFA would have been offset by other sources too, not only cuts) this simplistic assumption allows to get a sense of the possible magnitude of the no-MFA alternative. More specifically, the estimate shows that having the MFA operation in place will lower the present value of the debt-to-GDP

¹⁰⁰ For instance, Tajikistan raised USD 500 million from its inaugural 10-year international bond. Yet, it did it at the fixed rate of 7.125% and only in 2017. Available at: <https://www.ft.com/content/1dd9f200-93d5-11e7-bdfa-eda243196c2c>

¹⁰¹ For instance, diagnostics/ preparatory work of the Debt Department of the Ministry of Finance

ratio by 1.6 percentage points on average over 2015 - 2025, compared to not having the MFA.

The Social Impact Analysis (SIA) (more under Section 10) shows that while the shortfall would likely have resulted in some cuts to government procurement of non-essential items (most probably less than EUR 30 million corresponding to the total MFA envelope), it seems likely that most core policies relating to the social situation would have been unaffected by the absence of Macro Financial Assistance. It also shows that as there were no conditions in the MoU which relate specifically to social policies and/or outcomes, the social impact of the conditionality is likely negligible (even though some conditions can be seen as beginning of further, more front-loaded reforms). However, the MFA operation provided the EU with some leverage to advance the cause of NGOs and other donors relating to the 'foreign agents' and 'anti-LGBTI' laws (Box 4). The passage of these laws was ultimately abandoned by the Kyrgyz government.

Box 4 Wider context of the withdrawal of the 'foreign agents' and 'anti-LGBTI' laws in Kyrgyzstan

In March 2015, Kyrgyzstan's (then) President, Almazbek Atambayev, visited Brussels for meetings with various EU leaders. An important and recurring theme discussed between Kyrgyz and EU representatives during the Kyrgyz President's visit pertained to two draft laws which were under consideration by Kyrgyzstan's Parliament: (1) the 'foreign agents' law, which intended "to force virtually any NGO that receives foreign funding to adopt the label of "foreign agents" or else stop its work;" and (2) the 'anti-LGBTI' law, which foresaw a ban on the "propaganda of non-traditional sexual relations." Both laws had been inspired by similar legislation adopted in Russia.

Presidents of the European Commission, the European Council and the European Parliament raised concerns about the human rights threats posed by these laws and sought concrete commitments from President Atambayev to abandon the passage of these laws in Kyrgyzstan. The evidence gathered indicates that the EU's diplomatic efforts (reinforced by instruments such as the MFA) contributed to stopping the passage of the two bills.

Other actions undertaken at EU level included the adoption of a Resolution in January 2015, whereby the European parliament called on the Kyrgyz government "to put an immediate end to the criminalisation of homosexuality." The Resolution also "reminded the Kyrgyz Parliament of its international obligations and of the Partnership and Cooperation Agreement with the EU, which includes full respect for human rights as an essential element of the partnership" and warned that "the eventual adoption of" the anti-LGBTI bill "could affect relations with the EU in line with Article 92 (2) of the Partnership and Cooperation Agreement." Further, the Resolution encouraged Kyrgyz authorities to "follow the recommendations made by the Parliamentary Assembly of the Council of Europe in Resolution 1984 (2014) on the Request for Partner for Democracy status, in particular recommendations 15.24, 15.25 and 15.26," which stress the importance of:

"combating all forms of discrimination and violence based on sexual orientation and gender identity;"

"not following up on the draft law based on the model of laws relating to the prohibition of "homosexual propaganda"; and

"fighting, in law and in practice, all forms of discrimination based on gender; ensuring and actively promoting effective equality between women and men; fighting discrimination against lesbian, gay, bisexual and transgender people (LGBT); fighting all forms of gender-based violence."

Both bills triggered a vigorous response from local civil society organisations, the wider international donor community and other key actors. Evidence gathered from interviews with a representative of civil society however suggests that the likelihood of the MFA not being disbursed also had an important bearing on the Kyrgyz government's final decision to abandon the two bills.

Sources: Worldwide Movement for Human Rights. 2015. 'EU: Use Brussels visit of Kyrgyzstan's president to secure human rights commitments;' Lelik, A. 2016. 'Kyrgyzstan: Anti-LGBT Bill Hits the Buffers.' The European Parliament 's Intergroup on LGBTI rights. 2015. 'EU leaders demand

answers from Kyrgyz President over anti-LGBTI, anti-NGO bills;’ European Parliament. 2015. ‘European Parliament resolution on Kyrgyzstan, homosexual propaganda bill (2015/2505(RSP)).’

Whether the economic outcomes would have been weaker or different in the absence of the MFA conditionalities

All of the MFA conditions attached to this operation required moderate effort from the authorities and therefore the outcomes and subsequent impacts envisaged were expected to be of a moderate scale. As explained in sub-section 5.3.3.3, this is to be expected. The MFA instrument constitutes emergency financial assistance and mainly intends to address (short-term) economic vulnerabilities in periods of crisis. Proposed reforms are therefore purposely designed so as to enable timely implementation and, subsequently, the prompt disbursement of financial assistance. In addition, the EU MFA is generally factored into the recipient country’s national accounts. This is expected to encourage the swift implementation of reforms (upon which the second disbursement of the MFA is conditional) as this ensures the release of MFA payments by the agreed dates and helps prevent unnecessary delays and/or the MFA failing to materialise.

In the case of Kyrgyzstan, the reforms were determined by the very limited time that was available for their implementation (given that the IMF programme was nearing its end and various procedural delays had hindered the timely implementation of the operation) and by major political considerations (see sub-section 8.2.2). In addition, it should be noted that some of the conditions were intended to pave the way for more extensive reforms (driven by the EU and/or other international donors) over the medium to longer term. For instance, the approval of the Terms of Reference for the PEFA assessment (condition 2) or the development and approval of an Action Plan by the Chamber of Accounts (condition 4), could not have translated into meaningful economic outcomes on their own. However, when assessed over longer time horizons, and when subsequent reforms would have been implemented and materialised, their impacts would be more significant.

Overall, while it appears reasonable to assume that the absence of the MFA conditions/reforms would not have had any significant impact on economic outcomes (largely owing to their limited scope and short-term nature), it ought to be recognised that the MFA support package brought about additional impetus for reform in priority areas, encouraging the implementation of specific, short-term, measures that may have otherwise been overlooked by national authorities, primarily owing to a lack of financing¹⁰². The EU MFA may have helped pave the way for more extensive reforms in some of these areas.

If and how MFA reinforced IMF / WB reforms

There was some degree of commonality as regards the reform areas covered by the EU MFA and other donor support programmes (e.g. IMF, WB, etc. (see Section 9)). Within these areas (e.g. PFM, banking), the EU MFA provided additional impetus for reform, though to a limited degree. For instance, while the IMF praised the role of the MFA in the context of the Banking Code, having triggered additional political endorsement for the reform, it remarked that reform ownership (among Kyrgyz authorities) was eventually low. As a result, the adoption of the Banking Code did not materialise in the end. Similarly, in the PFM area, the IMF’s ‘Financial Management Information System’ (FMIS) project was eventually dropped.

Overall, it would appear that the MFA did not play a significant role towards reinforcing actions promoted by other donors, notably the IMF and the WB (and vice-versa). As such, on the one hand, the degree of reform interdependence or cross-conditionality

¹⁰² This issue was specifically raised by the Chamber of Accounts. They had, for a number of years, relied on EU support (possibly including the EU MFA) which helped towards capacity building, an update of their Performance Audit Manual, and training for all CoA staff on public sector auditing. Without EU support, these changes may not have been undertaken owing to a lack of financing available at local level.

among the donors' respective support programmes was minimal while, on the other, reform ownership in certain areas (e.g. banking) was low among Kyrgyz authorities and, in spite of some degree of overlap across the different programmes, it was difficult to drive the implementation of certain measures.

8.1.2.2 Alternative 2: no MFA and IMF - the counterfactual position

The combined absence of the IMF and EU-MFA would have most likely affected the financing provided by other donors. This is because the absence of the IMF ECF programme would have most certainly affected the WB's readiness to provide budget support to the Kyrgyz Republic, and perhaps the ADB one too. More specifically, even though the presence of the IMF programme is not a pre-requisite for the WB budget support, it is highly desirable and may guide the decision of the bank's management as it implicitly confirms the adequacy of the macroeconomic framework which in turn is an imperative for the WB budget support.

As a result, if the assistance from the key donors provided in 2015 had not actually materialised (i.e. USD 29 million from the IMF, USD 16.5 million from the WB and USD 16.5 million *via* the MFA¹⁰³ respectively), this would have corresponded to USD 62 million, or ~1 per cent of GDP in 2015, a very substantial part of the overall financing gap for that year (~2.5 per cent¹⁰⁴). Therefore, unlike under Alternative 1 with the absence of the comparatively small amount from the MFA only (~0.3 per cent of GDP in 2015), the gravity of the situation resulting from the absence of the IMF and MFA programmes (and potentially other donors like WB) would have possibly made an assistance from Russia even more indispensable compared to a 'no MFA' scenario (though its scale remains very uncertain).

Otherwise, a similar pattern (in terms of the most plausible/ implausible options), as presented in Figure 19, would have emerged. In addition, options under Alternative 2 (similar to Alternative 1) are also generally not mutually exclusive and, in practice, the combination of some of them could have taken place. The important difference between Alternatives 1 and 2, given the size of the IMF support and some possible fallout from other donors' programmes, would have been the scale of cuts to public spending (greater under Alternative 2).

Besides the absence of the highly concessional financial envelope under the 'no IMF and MFA' alternative, the lack of IMF support would have also had a major dampening effect on business and investor confidence.

Whether the economic outcomes would have been weaker or different in the absence of the MFA and IMF financial support

While a disorderly adjustment would have been unlikely given the relative size of the gap and the existing alternatives (i.e. a ramped up support from Russia), the depth of the spending cuts would most likely have been considerable, and according to the IMF, most likely affecting social spending. Cuts in public spending could have been mitigated to a limited extent by drawing on government funds deposited at the NBKR and increased Russian assistance.

In addition, the erosion of business and investor confidence caused by the absence of the IMF would have backfired in the form of even greater depreciation of the Kyrgyz Som (already high under the IMF programme), inflating the foreign-denominated debt stock and the costs of servicing it, and eventually leading to a rise in domestic prices and some loss of foreign direct investment (FDI).

In parallel, the absence of the IMF would have meant that some of the reforms initiated by its ECF programme would not have been implemented and the technical assistance and disciplining role of the IMF (in terms of the fiscal policies) would have

¹⁰³ An equivalent of the 1st tranche of EUR 15 million disbursed in 2015

¹⁰⁴ Estimated financing gap in 2015, as per IMF estimation, was USD 171 million

been absent. This is something that would have impacted, among others, the fiscal stance in the short but also mid-term horizon.

Conclusions

The absence of the MFA would not have engendered significant, adverse economic impacts. Nonetheless, the MFA disbursements were a non-negligible amount, corresponding to circa 0.3 per cent of the GDP in 2015 and 2016 respectively.

Moreover, there is no evidence suggesting that the absence of the MFA would have had any material impact on business and investor confidence. Further, given the (short-term) nature of the conditionality package and the fact that most of the MFA conditions had already been met by the time the MoU was signed, it seems unlikely that the MFA conditions bore any significant impact on longer-term economic outcomes.

In terms of the hypothetical absence of both the MFA and IMF ECF, the repercussions would have been far more severe. The depth and breadth of the public cuts would have likely been more considerable, potentially even including reduced social spending. This in turn would have significantly and adversely impacted aggregate demand and output growth.

In addition, a 'no MFA and IMF' alternative would have also resulted in foregone benefits from the IMF reform package, which constituted an important contributing factor towards restoring fiscal discipline. Additionally, the loss in investor and business confidence would have potentially been more pronounced, triggering *inter alia*, an even greater depreciation of the Kyrgyz Som and a further dampening effect on FDI.

8.2 Part 2: Effectiveness of structural reforms

The following section provides the information on the framework used to assess the effectiveness of the MFA induced reforms (sub-section 6.2.1) and the results from this assessment (sub-section 6.2.2).

8.2.1 Analytical framework

All four reform areas to which conditionalities were attached have been examined namely, (i) Public Finance Management, (ii) Financial Sector, (iii) Trade policy and (iv) Investment and business environment related reform.

- An analysis of the effectiveness of MFA focused on assessing:
- The nature and scope of the conditionality attached to the MFA operation;
- The implementation of the conditionality;
- Evidence for actual or expected impact of reforms (both direct and indirect); and
- The level of ownership of the programme and the capacity of the authorities to implement it;
- Evidence of MFA contribution to the reform progress.

The above assessment was based on the following sources of evidence:

- Review of documentation including compliance statements and evidence provided by the recipient government and the Commission's assessment of progress;
- Stakeholder interviews exploring the following issues:
 - Implementation and durability of the reforms;
 - Additionality (the specific role of MFA in promoting the reforms);
 - Complementarity with conditions attached to assistance provided by other multilateral/ bilateral donors;
 - Overall impact of structural reform.
- Detailed feedback from the local experts;
- Insights gathered from the Focus Group with development partners that took place in Bishkek in September 2018.

8.2.2 Assessment of the effectiveness of MFA conditionality

Overall, *sensu stricto*, Kyrgyz Republic fulfilled the economic and structural policy conditions related to the disbursement of the MFA in a satisfactory way, as illustrated by the disbursement schedule over the period June 2015 - April 2016. There was no need for waivers.

However, six out of the seven conditions had already been met in 2013 - 2014, i.e. before the MoU was eventually signed in October 2014. There are a number of possible reasons for the swift implementation of reforms, discussed in sub-section 5.3.3.3 and elaborated again below.

Firstly, as the EU MFA was already significantly delayed (largely independent of the Commission – see Box 5), there was a genuine intention from the Commission staff to speed up the implementation of the operation. Given that the progress of the IMF programme is a key pre-condition for the MFA disbursement, this meant that the second disbursement (and therefore the fulfilment of the MFA conditions) were expected to take place before the expiry of the IMF's 2011 ECF programme, due in June 2014. Ergo, conditions had to be designed in such a way that they would have been feasible to fulfil within a short period of time (approximately 3-4 months). It should be noted that this is not atypical but an important and recurring feature of MFA operations. As explained in previous sections, the MFA constitutes emergency financial assistance and is expected to be disbursed within a reasonable timeframe. The implementation of reforms is expected to cover a limited time-span so as to enable the timely disbursement of the financing in view of addressing short-term vulnerabilities (generally a more pressing concern than the need to establish a longer-term reform programme).

Box 5 Delay related to the countersigning of the MoU by the NBKR

As outlined in sub-section 2.3.2, much of the delay pertaining to the MFA operation in Kyrgyzstan was entirely independent of the Commission. As such, over the course of 2014, further delays in the implementation of the MFA resulted from the NBKR's refusal to sign the MoU as a 'borrower', as requested by DG ECFIN.

Central banks are typically responsible for monetary policy and price stability, while debt management stays with the Treasury. Within this set-up, a central bank remains independent and cannot underwrite the liabilities that accrue to the government. In the Kyrgyz context specifically, Article 5 of the Law of the Kyrgyz Republic "*On the Public and Non-Public Debt of the Kyrgyz Republic*" (declared invalid on January 1, 2017 with the entry into force of the "*Budget Code of the Kyrgyz Republic*"), the Ministry of Finance of the Kyrgyz Republic is the only agent of the Government of the Kyrgyz Republic in managing public debt, implementing external borrowing and issuing state guarantees. Also, according to paragraph 5 of Article 1 of the Law of the Kyrgyz Republic "*On the National Bank of the Kyrgyz Republic*", the National Bank is not liable for the Kyrgyz Republic's debt obligations.

Therefore, while it seems appropriate that the NBKR eventually signed the MoU as 'financial agent' (and not 'borrower'), without bearing the responsibility for the loan component of the MFA, the delay caused by the NBKR's rejection of the European Commission's initial proposition to act as a 'borrower,' seems unnecessary and could have been avoided.

The fact that the reforms had been implemented fairly rapidly raised concerns among stakeholders consulted during the study about their appropriateness (at a time when significant/demanding structural reforms were needed in Kyrgyzstan) and whether the negotiations relating to the MFA conditions should have been re-opened.

In short, the Commission faced the following dilemma:

- re-opening negotiations around the MFA conditions that would have allowed it to amend the reform package but which, at the same time, would have led to more delays as regards the disbursement of the MFA (by at least

another 1-2 years¹⁰⁵), possibly further aggravating the relationship with the Kyrgyz government;

versus

- going ahead with the existing operation and the existing set of conditions, even if a majority had already been met prior to the MoU being signed) which, to some extent, (adversely) impacted on other EU budget support programmes implemented at the time (e.g. programmes of the EU Delegation in Bishkek (see Box 6 below)). There was no further evidence provided as regards the nature and magnitude of these impacts.

Box 6 Perceived adverse effects of not re-negotiating the MFA conditions

Representatives at the EU Delegation explained that not re-opening the MFA negotiations sent the wrong message to Kyrgyz authorities – i.e. that limited reform efforts could still lead to substantial disbursements). The MFA was therefore seen as a lost opportunity to induce greater and more meaningful reform efforts in the country.

While the EU Delegation acknowledged that the numerous delays had become an issue affecting the EU-Kyrgyzstan political dialogue, it also stated that the decision to go ahead with the operation, without a review of the conditions, backfired. According to the EU Delegation, some specific reform conditions attached to its programmes were demanding and required continued reform commitment and efforts on the part of the Kyrgyz government/authorities. The MFA that, in their view, came at a very limited cost to authorities was inconsistent with this approach and was an undesirable signal, given the typical challenges in implementing structural reforms in the Kyrgyz context.

It had indeed become obvious to the Commission that, due to the delays encountered both at the EU and Kyrgyz level, most of the MFA conditions had already been met prior to the MoU being approved and signed. As explained in previous sections, the Commission however decided not to re-open the negotiations to avoid further delays that would have only amplified tensions that prevailed at the time between the Kyrgyz government and the EU. And indeed, the evidence gathered from interviews with the EU Delegation in Bishkek, the Presidential Office, the Ministry of Finance, EEAS and IMF staff, along with some evidence in the press¹⁰⁶, confirmed that a very long process leading to the implementation of the MFA constituted a considerable strain on the political relationship between both partners.

Further, the MFA granted to Kyrgyzstan was considered an “extra political gesture” by the EU¹⁰⁷. A greater weight was placed on the operation’s political objectives/outcomes, notably to reaffirm the EU’s commitment to helping a “strategic partner” at a time of great need and to highlight the EU’s endorsement of the efforts displayed by the Kyrgyz government in carrying out democratic reforms to strengthen the country’s parliamentary democracy. The fact that the operation bore greater political (than economic) significance potentially lessened the need to re-negotiate the MFA conditions, as a means to signal the EU’s political goodwill.

Finally, it should be recognised that the pace of the implementation of the MFA conditions may also have been influenced by certain administrative procedures. As explained in sub-section 5.4.3, the MFA support package would have been accounted for in Kyrgyzstan’s national accounts. One could therefore argue that this would have incentivised the timely implementation of reforms by the authorities, so as to minimise

¹⁰⁵ Reopening of the negotiations would require, inter alia, renewed consultations between the European Commission and the Member State Committee, and between the Commission and Kyrgyz authorities. Ultimately, a new MoU would need to be ratified by the Kyrgyz Parliament.

¹⁰⁶ 24.kg, 2015. Almazbek Atambayev about himself, Europe, Bakiyev, foreign agents and elections. Available at: <https://24.kg/archive/en/community/175146-news24.html/>

¹⁰⁷ Interviews with EU officials

the risk of delays at the time of disbursement and resulting problems of accounting, if the MFA had not materialised as it was originally planned.

Conclusions

The MFA operation to Kyrgyzstan was of an exceptional nature and was considered to be an additional political gesture of the EU (rather than solely an anti-crisis support mechanism aiming to stabilise the economy). As such, it mainly sought to signal the EU's endorsement of the efforts demonstrated by the Kyrgyz government in furthering the country's transition towards a fully-fledged parliamentary democracy. It is therefore not surprising that political considerations played a more important role than what has been observed in a majority of past MFA operations, including in the design of the conditionalities and their execution.

The fact that most of the MFA conditions had been fulfilled by the time of the signature of the MoU evoked the possibility for re-negotiations. In our judgement, the Commission's decision to not re-open negotiations was fully justified.

Importantly, although not part of the MFA reform package as such, the MFA conferred added leverage to the EU in its discussions of the 'anti-LGBTI' and 'foreign agents' bills with the Kyrgyz authorities. These two highly controversial legislative proposals – if passed – would have seriously undermined the rights of the LGBTI community and would have severely affected the activities of Kyrgyzstan's civil society.

9 Efficiency

Question 3: Was the disbursement of the financial assistance appropriate in the context of the prevailing economic and financial conditions in the beneficiary country?

This question is addressed by an analysis of the timing of disbursements

Question 4: In what way has the design of the MFA assistance conditioned the performance of the operation in respect to its cost and its objectives?

This question is addressed by analysing:

- Entry conditions for the MFA operation (ownership and capacity for reform)
- Flexibility of operations to adjust to changes in context and/or feedback)
- The effectiveness of dialogue between the European Commission and Kyrgyz authorities
- The effectiveness of monitoring of the MFA operation
- The coordination of donor activity
- The existence of an EU leverage effect on the Kyrgyz government to maintain the focus on reform

9.1 Timing of the disbursement of financial assistance

As discussed in the sub-section 4.3.2, the subsequent delays made the implementation and the disbursement of this MFA operation to go far beyond the original anticipated dates. However, in spite of these protracted delays, the disbursements that took place between June 2015 and April 2016 turned out to be still relevant (sub-section 8.1.2), given the economic climate that prevailed in Kyrgyzstan at the time.

Conclusions

The negotiation process characterising the MFA instrument was lengthy, ultimately delaying financial disbursements. Nevertheless, the timing of the disbursements over the period June 2015 and April 2016 was still relevant owing to economic difficulties faced by Kyrgyzstan at the time in the wake of the Russian crisis.

9.2 Design of MFA assistance and efficiency of implementation

9.2.1 Ownership of the programme by the Kyrgyz authorities

The general level of the reforms' ownership of the Kyrgyz authorities has been seen by the key stakeholders as 'uneven' and 'dynamic'¹⁰⁸. The international donors perceived the Kyrgyz environment as more challenging compared to some other countries like Georgia and Armenia that championed the reforms and where the prevailing conditions for swift progress in structural reforms have been more conducive.

The ownership level in Kyrgyzstan was varying, partly in sync with the pendulum of the political cycle. While the IMF and DG ECFIN saw a substantial pick up in the appetite to embark on the challenging reforms in the late 2014, more difficulties were reported closer to the parliamentary elections in the late 2015. In the same vein, appetite to press on with the reforms has been also a function of the gravity of the situation – more financially constrained was the government, higher propensity to take up on the reforms¹⁰⁹. The geopolitical context and the strategic importance of the relationship with big neighbours, in particular with Russia, has been also a material factor weighing on the progress of certain reforms (i.e. the accession of the country to the Eurasian Customs Union and its implications for some trade policies).

In terms of the MFA specifically, the Ministry of Finance was the leading stakeholder on the Kyrgyz side and the Commission's interviewees pointed out to relatively higher

¹⁰⁸ Interviews with the representatives of the IMF, WB, DG ECFIN and the EU Delegation

¹⁰⁹ Observation from the IMF staff

ownership in this ministry compared to other Kyrgyz ministries that were directly involved in the MFA.

Lack of contradiction of the MFA with the national strategies is the pre-requisite for the appropriate level of ownership. In this respect, the evaluation did not find any evidence that the MFA would go contrary to the national reform plans i.e. those outlined in the 2013 - 2017 National Strategy for Sustainable Development.

9.2.2 Capacity for reform

In its assessment of its DPO-2 programme implemented in Kyrgyzstan between 2013 and 2015, the WB summarised that *'...the implementation of deep-seated reforms was affected by capacity constraints in certain areas and persisting institutional weaknesses. Frequent changes of the government and prime minister that resulted in shifting commitments to reform'*. It also pointed out that *'a steady, coherent leadership on reforms was at times absent'*¹¹⁰. Yet, the perspective of the IMF from its own programmes was not similar and the fund perceived the internal capacity as satisfactory and *'certainly not below what one would expect from the low-middle income countries'*¹¹¹.

In terms of the MFA conditionality specifically, the capacity was at the appropriate level. In the interview with the Chamber of Accounts, the local officials pointed out to the importance of the technical assistance support to progress with the implementation of the Action Plan, of which drafting and approval was the subject of the MFA conditionality. As a general comment, the EU Delegation in Bishkek indicated the vital role of the technical assistance accompanying many of its specific reforms, as part of the budget support programmes it was implementing.

9.2.3 Flexibility and adjustments to implementation given exogenous factors

Flexibility is most clearly observed in the willingness to apply waivers where conditions have not been sufficiently met but the need for disbursement is urgent. In case of the MFA to Kyrgyzstan, there were no waivers applied. In addition, the need of flexibility/adjustment was also reduced by the fact that most of the conditions were outdated.

9.2.4 Liaison with Kyrgyz authorities

Effective dialogue between the Kyrgyz authorities and the EU (via DG ECFIN and the EU Delegation) was critical in supporting the understanding and commitment to conditionalities and management of disbursements. Dialogue was primarily based on formal and regular missions led by DG ECFIN in collaboration with the EU Delegation to the Kyrgyz Republic. As part of the review missions, EU representatives also held meetings with relevant officials at the Ministry of Finance, the Ministry of Economy, the Office of the Prime Minister, the Central Bank, and the Court of Accounts¹¹².

The Ministry of Finance of the Kyrgyz Republic had a key liaison role, partaking in all major discussions with DG ECFIN and the EU Delegation around the MFA operation and the reform process, and coordinating with relevant authorities / responsible bodies on the implementation of the specific reforms.

9.2.5 Visibility of the MFA

Evidence gathered from Kyrgyz stakeholders and various development partners indicates poor visibility of the EU MFA in Kyrgyzstan. This lack of visibility was not only prevalent in the capital city of Bishkek, but equally severe in other cities (such as Osh), where awareness of the operation was judged almost inexistent¹¹³.

¹¹⁰ WB, May 2017. Implementation completion and the results report. The first and second development policy operations.

¹¹¹ The interview with the IMF staff based in Washington D.C.

¹¹² Various MFA Mission Reports

¹¹³ Views gathered from development partners during focus group discussions.

Though the EU is generally perceived as an important donor partner in Kyrgyzstan, the MFA operation did not receive as much attention (locally) when compared to other EU support programmes, especially those dedicated to reforms in the areas of the rule of law, the judiciary, and the electoral system. As the negotiations surrounding the terms/conditions of the MFA financing took place between the EU and senior officials of the Kyrgyz government only, it is believed that the donor community, local stakeholders (e.g. the media, the civil society) and the general public did not have all the necessary information to fully understand the purpose and intended objectives of the EU MFA. It was also recognised that, in the case of the EU MFA, the outcomes / impacts / benefits are not “tangible” per se, making it difficult to attribute and publicise specific economic gains / contributions to the operation¹¹⁴. Furthermore, delays in disbursement made public communication of this particular MFA more delicate.

Additionally, in terms of visibility, the MFA operation was not perceived to be on par with other support programmes, notably the IMF’s¹¹⁵. The IMF has a longstanding relationship with Kyrgyzstan, which could help explain the relative importance attributed to its programmes (and associated conditionalities / reform areas) by the media, civil society, the business community, and the general public.

9.2.6 Monitoring process

Field missions constituted a primary tool for monitoring the MFA operation. These were undertaken by the Commission and took place at the time of the negotiations of the EU MFA, and during the implementation of the specific conditions. The missions comprised several meetings with the EU Delegation, Kyrgyz authorities (notably the responsible bodies overseeing the implementation of specific reforms) and international donors.

The EU Delegation was also involved in the monitoring process, mainly in the form of logistical support (i.e. arrangements preceding field missions) and the provision of relevant data and their own interpretation of progress made in relation to the implementation of the MFA conditions.

The monitoring of the MFA operation in Kyrgyzstan was however reported to have been less stringent when compared to the extent of supervision undertaken in other recipient countries¹¹⁶. This is because Kyrgyzstan is “outside of the traditional scope of MFA,” and, consequently, the operation was subject to less scrutiny by the Commission¹¹⁷.

The key outputs of the monitoring process were mission reports prepared by DG ECFIN. There were no specific weaknesses flagged as regards the arrangements or approaches to data collection between the Commission and the national authorities.

9.2.7 The consequences of a joint EU and IMF/WB position on the negotiations with the national authorities

The EU MFA and support programmes led by the IMF and the WB displayed some degree of synergy, notably in the PFM, banking and trade policy areas. The MFA led to the implementation of adjustment measures that were consistent with reform priorities set by the IMF and the WB in these areas and, hence, helped reinforce their actions (as well as those of other donors). The WB, for instance, indicated that the EU MFA laid the groundwork for the PEFA, that was eventually undertaken in 2014. The

¹¹⁴ Views gathered from development partners during focus group discussions.

¹¹⁵ Views gathered from Member State representations, and development partners during focus group discussions.

¹¹⁶ Views gathered from officials at DG ECFIN.

¹¹⁷ Views gathered from officials at DG ECFIN.

PEFA was used as “a progress indicator” in discussions for DPO-II and helped inform the reform package agreed with Kyrgyz authorities¹¹⁸.

9.2.8 Leverage of Kyrgyz authorities (and other stakeholders)

The ability of the Kyrgyz authorities to use the MFA to promote / accelerate their own reform plans was observed in some government departments.

A key example was the Chamber of Accounts (CoA). A shared view among senior officials at the CoA is that reform of public sector auditing “is much needed” and “there is a will within the CoA to implement change.”¹¹⁹ In that sense, the MFA was opportune. It reflected the department’s reform priorities and signalled (to the Kyrgyz government and the public in general) their commitment to endorsing international best practices (notably the INTOSAI standards) and improving internal work practices.

Additionally, the EU, along with other prominent donors, strongly opposed the Kyrgyz government’s plans to pass the ‘anti-LGBTI’ and ‘foreign agents’ laws. The MFA constituted added leverage for the EU, reinforcing its seat at the discussion table and, indirectly, the role of civil society and other local stakeholders in preventing the enactment of the said laws.

Conclusions

Formal and regular missions constituted an important channel of dialogue between the Commission and Kyrgyz authorities. These were generally led by the Commission in close collaboration with the EU Delegation to the Kyrgyz Republic. The Ministry of Finance, on the other hand, endorsed the liaison role which involved negotiating the terms / conditions of the MFA operation and coordinating / undertaking / monitoring the implementation of reforms. Compliance with the necessary MFA conditions was, on the EU side, monitored by the Commission (through field visits) and the EU Delegation (on a more regular basis).

On the wider international scene, much coordination took place among the Commission and several donors, notably the IMF and the WB, to ensure that priority reform areas (targeted by their respective support programmes) were closely aligned. However, while these concerted efforts helped signal the desired reform steer to Kyrgyz authorities, international donors perceived the level of reform ownership in certain sectors (notably in the banking sector) as insufficient. Yet, in the narrower sense of the operation, the extent of reform ownership was appropriate (in particular at the Ministry of Finance and Chamber of Accounts). There were no specific contradictions between the MFA conditionalities and national policies and, in some instances, the MFA brought about added leverage for authorities in their pursuit of sectoral reforms that would probably not have been prioritised by the Kyrgyz government. Additionally, no significant deficiency in organisational capacity (for implementing MFA conditions) was flagged.

¹¹⁸ Views gathered from the World Bank during interviews.

¹¹⁹ Views gathered from the Chamber of Accounts during interviews.

10 EU-added value

Question 5: *What was the rationale for an intervention at EU level and to what extent did the MFA operation add value compared to other interventions by other international donors? Did the operation actually lead to the expected impacts and added value of international cooperation, and what can be learnt for future operations?*

Positive aspects of EU engagement include:

- Evidence of the financial added value of EU support – national authorities would have struggled to meet their financing needs in absence of the EU MFA
- Evidence that MFA reinforced the government’s commitment to socio-economic reform
- EU had a discernible influence on the design and application of conditionalities
- Leverage in pulling together and accelerating a multi-donor package
- Evidence of signalling and confidence building
- Lessons for future operations

10.1 Financial added value

The MFA was initially requested in 2010 to help the country deal with the economic impact of the 2008-9 global financial crisis and the political instability affecting the Kyrgyz Republic in the first half of 2010. It was however eventually disbursed in 2015 - 16. Despite the significant delay in the approval and implementation of the MFA, the Kyrgyz authorities generally recognised that it “came at the right moment”, was “still relevant”¹²⁰ and that it contributed to alleviating the financing pressure facing the country during 2015 - 16. From late 2014, there were several factors creating economic uncertainty and vulnerability, including: (1) the economic slowdown in Russia; (2) wide swings in gold production; (3) decreasing gold prices; and (4) the termination of recurring funding from the US (brought about by the closure of the Manas logistical airbase used by the US for its operations in Afghanistan). In 2015 - 16 the Kyrgyz economy was thus highly vulnerable to external shocks and faced with a precarious balance of payments situation.

Additionally, as mentioned previously (Section 5), the size of the MFA operation (EUR 30 million) corresponded to about 0.3 percent of Kyrgyzstan’s GDP in 2015 and 2016 respectively. The main attractiveness of the MFA versus alternative sources of financing was its highly concessional terms, which could have generated significant fiscal savings for the Kyrgyz government, thus increasing the financial value added of the instrument.

In the above context, the MFA has therefore provided Kyrgyz authorities with some fiscal breathing space at an important moment when the country was faced with various economic difficulties as well as preparing for parliamentary elections. More broadly, the MFA signalled to the region the EU’s commitment to supporting countries, like Kyrgyzstan, that embark on a clear path of reform in moments of economic difficulties.

Conclusions

The size of the MFA operation (EUR 30 million) corresponded to about 0.3 percent of Kyrgyzstan’s GDP in 2015 and 2016 respectively – not a negligible amount. The highly concessional terms at which the MFA was provided, generated significant fiscal savings for the Kyrgyz government. This is to some extent testament to the financial added value of the instrument. Moreover, the MFA provided Kyrgyz authorities with some fiscal breathing space at an important moment when the country was faced with various economic difficulties as well as preparing for parliamentary elections.

¹²⁰ Interviews with Kyrgyz authorities.

10.2 Social added impact

The EU MFA to Kyrgyzstan mainly focused on short-term economic adjustment and reform. The MFA operation nonetheless built on existing EU external financing instruments (see Section 9) that aim to support the Kyrgyz Republic's longer-term commitment to values shared with the EU (including democracy, the rule of law, good governance, respect for human rights, sustainable development, and poverty reduction) as well as its commitment to the principles of open, rule-based and fair trade¹²¹. As such, given the timing of the first disbursements, the EU MFA was also considered, at the political level, as an expression of the EU's support for electoral reform (ahead of the parliamentary elections that were held in October 2015) by allowing for the introduction of new voting technologies.

Further, though the EU MFA was not designed to promote social reform directly, it provided the EU with leverage to prevent the enactment of various contested legislations, notably the 'anti-LGBTI' and 'foreign agents' laws. Interviews conducted with EU and Kyrgyz stakeholders (see Section 6) confirm that the MFA played an important role in driving the Kyrgyz government to retract on the passage of these laws. However, other international donors, local NGOs, and civil society organisations led much of the advocacy work on the ground. The precise added value of the MFA in this area is therefore difficult to conclusively establish.

Conclusions

The MFA operation provided the EU with (added) leverage to prevent the enactment of various contested legislations, notably the 'anti-LGBTI' and 'foreign agents' laws. To this end, the added contribution of the MFA was high and potentially on par with that generated from various actions undertaken by other donors (e.g. WB, ADB, USAID) and the civil society who were also very active on this front.

10.3 Added impact on the promotion of (economic) reforms

The MFA conditions / reforms were judged necessary at the time of its negotiation with Kyrgyz authorities. As discussed previously, the MFA reform package was designed to address structural weaknesses constraining economic growth. Moreover, the MFA conditionalities were closely aligned with the reform priorities of the Kyrgyz government and those that underpinned existing EU support programmes (e.g. existing budget support operations). PFM reforms, for instance, were central to the disbursement of specific EU support packages, including Sector Reform (discussed in more detail in Section 9). Additionally, the reforms were designed in close coordination with the international donor community. MFA reforms aimed to supplement reform efforts driven by the likes of the IMF and the WB.

In essence, the key added value that was expected of the EU MFA was to help create an appropriate macroeconomic and structural reform framework, that was capable of increasing the effectiveness of the actions financed through other EU/international instruments. The extent to which this has been achieved is not clear-cut. With the numerous procedural delays surrounding the officialisation and disbursement of the MFA package, the EU's added value was arguably reduced¹²². As such, the Presidential Administration was particularly vocal in expressing their disappointment at the delays surrounding the implementation of the EU MFA. The former Kyrgyz President Atambayev was reported to be "very confused" and "not believing anymore that the MFA funds would be disbursed."¹²³ As such, he was publicly advertising that the EU

¹²¹ European Parliament (2013) 'Decision No 1025/2013/EU of the European Parliament and of the Council of 22 October 2013 providing macro-financial assistance to the Kyrgyz Republic.'

¹²² Interviews with EU officials, the EU Delegation and Kyrgyz authorities.

¹²³ European Commission (2013) 'Staff report on mission to the Kyrgyz Republic.'

“could not deliver on its promises,” and was reiterating the need to rely more on regional partners and to join the Eurasian Economic Union¹²⁴.

Conclusions

EU added-value was apparent in reinforcing the promotion of structural reforms in several priority areas. The MFA conditions generally supplemented the numerous actions already undertaken by key international donors, such as the IMF. This reinforced the rationale for certain adjustment measures and the need to advance reforms swiftly in targeted sectors.

However, with the numerous procedural delays encountered, however, the overall EU added value was arguably reduced. These delays were believed to have adversely impacted the extent of awareness / visibility surrounding the operation

10.4 Added leverage from coordination with international donors

As noted previously (Section 5), the EU established a strong level of coordination with the international donor community to help inform the structural reform package that would accompany the MFA operation. Specifically, interviews with EU officials and representatives of the donor community confirm a strong collaboration between the EU, the IMF and the WB, notably on PFM, banking and trade policy reforms. The overlap could have helped achieve further leverage for the donor community to advance the necessary reforms.

However, while reforms were complementary in some areas, the degree of reform interdependence or cross-conditionality among the respective support programmes was minimal. Owing to this, the extent to which the MFA brought about added leverage for the donor community to drive reforms may have been limited. As such, there were certain areas where reform ownership (among Kyrgyz authorities) was reported to be low, such as PFM and banking. Various projects led by the IMF, such as the Financial Management Information System (FMIS) and the Banking Code, were not materialising.

Conclusions

The degree of reform interdependence between the EU MFA and other donor programmes was not significant, suggesting that, while MFA reforms helped supplement some of the actions already undertaken by other donors (notably the IMF and the WB) on the ground, the extent of its influence (in terms of added leverage) on the overall reform package driven by the international community may have been limited.

10.5 Signalling effect to civil society and the general population

Previous ex-post evaluations of MFA operations suggest that the real added value of the MFA operations from the perspectives of recipient countries is the political signalling effect (“seal of European approval”) associated with the stabilisation / macroeconomic recovery programmes that are put in place and, eventually, the resulting confidence-boosting effects for civil society, the wider donor community and the private sector.

On that front, the general consensus is that there was little visibility of the MFA. Evidence gathered during stakeholder interviews and a workshop with development partners indicates that the EU MFA did not “catch eyes and ears” among civil society and the general population. As such, publicity surrounding the EU MFA was negligible, and consequently, awareness/understanding of the operation was minimal.

It was, however, remarked that other EU programmes, notably those targeted at specific reforms (e.g. electoral system, rule of law, democracy, etc.), tend to be more widely covered and have sparked greater interest over the years among local stakeholders and the general public. As such, it has proved easier to promote such programmes/projects as the objectives/intended outcomes of the assistance offered

¹²⁴ Interviews with EU officials

are clearer and “more targeted”¹²⁵. On the contrary, conditions associated with the EU MFA were viewed as “too technical” and difficult to convey to “laymen.”

The MFA’s added contribution, notably in terms of boosting the EU’s external image and reiterating its commitment to supporting the Kyrgyz authorities in their reform efforts to ensure sustainable political, economic and social development in the Kyrgyz Republic, would thus appear to have been negligible in the long-term, in particular in comparison with other EU development cooperation instruments.

The actual disbursement of the MFA nevertheless had a significant positive impact on bilateral political relations, as it (coincidentally) came at a politically important moment ahead of parliamentary elections, when the country was also experiencing economic difficulties.

Conclusions

There was little awareness of the EU MFA in Kyrgyzstan, which may have been the result of the numerous procedural delays that characterised the design / implementation of the operation. The extent to which the EU MFA helped to boost the EU’s external image and/or to reiterate its commitment towards supporting the Kyrgyz government in its reform efforts could therefore be considered limited.

10.6 Confidence boosting effect on the private sector

There is no clear-cut evidence of the extent of investor / business confidence-boosting brought about by the MFA operation. Owing to little coverage and poor visibility of the operation among the private sector / business community, one can safely assume that the MFA did not entail concrete effects on business / investor confidence. Views gathered from the International Business Council (IBC) and a large-scale telecommunications provider¹²⁶ corroborate this claim.

Conclusions

There was no evidence of confidence boosting effects on the private sector as a result of the EU MFA, potentially owing to little coverage and poor visibility of the operation.

¹²⁵ Workshop with development partners.

¹²⁶ An EU-based provider, with headquarters based in the Netherlands, is one of the largest suppliers of telecommunications services in Kyrgyzstan. They explained that they were aware of the MFA operation but recognised that very few entities within the business community would have been aware of the MFA operation.

11 Coherence

Question 6: *Were the measures of the MFA operation in line with key principles, objectives and measures taken in other EU external actions towards Kyrgyz Republic?*

11.1 Policy frameworks and principles

EU funding to Kyrgyzstan stems primarily from the Development Cooperation Instrument (DCI) and the EU's regional and thematic programmes (targeted at Central Asia), including: the European Initiative for Democracy and Human Rights (EIDHR); the Civil Society Organisations / Local Authorities Thematic Programme; and the Thematic Programme for Global Public Goods and Challenge¹²⁷.

In addition, to date, the European Commission has supported the Kyrgyz government's reforms through six budget support (BS) operations, including the MFA.

11.1.1 The Development Cooperation Instrument (DCI)

Since 2007, the EU provides development support to Kyrgyzstan through the DCI. Within this support framework, the EU is expected to channel a total of EUR184 million (in the form of aid and grants) to Kyrgyzstan over the period 2014 - 2020¹²⁸.

The EU's development support, through the DCI, is closely aligned to Kyrgyzstan's national strategies, including the 'National Strategy for Sustainable Development' (NSSD) 2013 - 2017 and the government's 'Programme and Plan on Transition of the Kyrgyz Republic to Sustainable Development' 2013 - 2017. It thus focuses on driving reform in the following areas: (1) the rule of law; (2) education; and (3) integrated rural development. Specific activities undertaken in each of these areas are set out in Box 7 below.

Box 7 Specific reforms driven by EU development support

Rule of law

In this area, a EUR13.5 million support programme is currently in place. It is being run by EU Member States' public bodies and is primarily aimed at fighting corruption and protecting citizens' rights by "building the capacity of oversight bodies, supporting reform of the judiciary and strengthening civil society organisations and the media." In the context of the 2017 presidential elections, a EUR13 million programme was put in place to strengthen the efficiency and integrity of the Kyrgyz electoral system. More recently, a new programme was established in view of providing "continued support to improving the legislative process and promoting judicial reform."

Education

Most EU assistance in the education sector is delivered via budget support. A EUR70 million support programme is currently in place and seeks to help the Kyrgyz government in implementing its Education Sector Strategy, newly revised in 2016. Specifically, EU support is targeted at supporting the Kyrgyz government in managing public finances dedicated to the sector. More broadly, the EU also support the government in implementing educational reforms, notably those focused on with a particular focus on girl pupils and children with special needs.

Integrated rural development

In this area, the EU supports the improvement of social protection systems in rural areas specifically. In 2014, a EUR30 million sector policy support programme (focused on social protection and public finance management) was established. The programme is aimed at "setting up more effective social protection and social insurance systems and compensating for cuts in social benefits and pensions and delays in payments." Additionally, it focuses on "improving childcare, targeting benefits, and establishing effective decentralised social services for vulnerable families and children." More recently, in 2016, addition, in 2016 a new

*

***** European Commission – see https://ec.europa.eu/europeaid/countries/kyrgyzstan_en

programme was put in place in view of promoting "income-generating activities and the provision of essential services in rural areas."

Sources: European Commission; EEAS

11.1.2 Regional and thematic support

11.1.2.1 Regional Indicative Programme (RIP) for Central Asia

Over the period 2014 - 2020, the EU will be allocating EUR255 million to regional cooperation projects in Central Asia (including Kyrgyzstan)¹²⁹. Under this framework, the EU provides support in areas related to energy, water, the environment, socio-economic development, and regional security (e.g. through greater integrated border management and drugs/crime prevention)¹³⁰. The RIP also foresees the establishment of a Technical Assistance Facility (TAF), focusing on institutional, administrative, legal, economic reform and trade issues.

11.1.2.2 Investment facility for Central Asia (IFCA)

Through the Investment Facility for Central Asia (IFCA), which was set up back in 2010, the EU seeks to back the priorities of partner governments in the Central Asian region and support them in undertaking priority investments that are capable of driving inclusive and sustainable growth. The IFCA aims at leveraging funds with eligible Financing Institutions for such investment projects, including the European Investment Bank (EIB) and the European Bank for Reconstruction and Development (EBRD).

To date, this has generally been done through the use of 'blending,' where grants from the EU (via IFCA) have been provided in conjunction with loans offered to Kyrgyz beneficiaries to fund vital infrastructure projects across the country on more affordable terms. This includes financing towards the rehabilitation and upgrading of solid waste, waste water and water management infrastructure in the country's largest cities. Specifically, over the period 1991-2013, the EBRD has lent a total of EUR548 million to the Kyrgyz Republic, of which EUR134 million were loans approved in 2013. The EIB which only started operating in the Kyrgyz Republic in 2014 has approved / is expected to approve three loans, amounting to a total of EUR120 million, to the Kyrgyz government.

11.1.2.3 Various thematic programmes

The aforementioned support is further complemented by the use of the EU's thematic instruments, notably the Instrument contributing to Stability and Peace (IcSP), the European Instrument for Democracy and Human Rights (EIDHR), the Nuclear Safety Instrument (NSI) and global education support and exchange programmes such as ERASMUS +. For the period 2014 - 2020 the EU's global envelope for EIDHR amounts to EUR1.3 billion and for IcSP EUR2.3 billion. For ERASMUS+, a separate regional envelope of EUR115 million is available. Over the period 2008 - 2013, an average annual amount of EUR3.8 million was disbursed to fund IcSP projects, while EUR705,000 was paid to EIDHR projects.

11.1.3 Humanitarian aid

In recent years, the EU has also provided food aid and emergency relief to Kyrgyzstan. As such, between 2007 and 2011, an average of EUR1.8 million was paid out in food aid from the DCI's thematic food budget line. In 2010, humanitarian assistance was provided by the Directorate-General for European Civil Protection and Humanitarian Aid Operations (DG ECHO) to the population affected by the inter-community violence in the south of the country. Though there are no ongoing ECHO relief programmes in the Kyrgyz Republic, the country is covered by a Disaster-

¹²⁹ European Union External Action (2018) 'EU-Kyrgyz Republic relations.'

¹³⁰ European Union External Action (2015) 'European Union – Kyrgyz Republic Cooperation for Development.'

Preparedness ECHO (DIPECHO) action plan for Central Asia and South Caucasus. The programme aims to increase awareness, preparedness and response capacities, and general resilience to natural disasters, at community, national and regional levels.

11.1.4 Budget support operations

Since 2010, the European Commission has supported the Kyrgyz government's reforms through six budget support (BS) operations. Collectively, these programmes amount to more than EUR100 million. The programmes vary in scope and size:

- Three programmes have supported reforms on social protection, though with a particular focus on social assistance payments and public finance management. They relate to the first (2011 - 12), second (2012 - 14) and fourth (2015 - 17) programmes and, collectively, amounted to nearly EUR50.0 million.
- Two others, the third (2013 - 15) and fifth (2016 - 18) programmes, have supported the implementation of the country's Education Sector Strategy 2012 - 2020 (which promotes a more inclusive and efficient education system). The two programmes amounted to about EUR41.0 million.
- The sixth programme (2016 - 18) supports electoral reform towards a more credible, inclusive and transparent electoral system. Disbursements provided/envisaged under this programme amount to a total of about EUR11 million.

Furthermore, Kyrgyzstan received EUR30 million in macro financial assistance that was disbursed in separate tranches in 2015 and 2016 respectively.

Conclusions

The EU offers support to Kyrgyzstan through various instruments, such as: the Development Cooperation Instrument, the Regional Indicative Programme (RIP) for Central Asia, the Investment Facility for Central Asia (IFCA), and various other thematic programmes, humanitarian and budget support operations respectively.

11.2 Coherence with other EU programmes and initiatives

11.2.1 General/wider objectives of EU support

11.2.1.1 The Partnership and Cooperation Agreement (PCA)

The PCA provides the legal framework for EU – Kyrgyz Republic cooperation and bilateral relations. The Agreement rests on three main pillars of cooperation and intended, long-term outcomes (of EU assistance) in a variety of sectors, such as social, finance, science, technology and culture:

- *Political dialogue.* The PCA sets the values which both the EU and Kyrgyz Republic are required to adhere to (e.g. respect of human rights and democracy). Additionally, it recognises the need for a political dialogue at several levels, including at the ministerial, parliamentary and, civil servants' levels. The ultimate objective is to help Kyrgyzstan consolidate its democracy, increase the convergence of positions on international issues of mutual concern, and foster security and stability in the region.
- *Economic relations.* Through the PCA, the EU commits to helping Kyrgyzstan in its transition to a market-based economy. For instance, a mutual most-favoured-treatment for the trade of goods (Article 8 of the Agreement) was introduced between the EU and Kyrgyzstan in view of increasing trade and investments and fostering more sustainable economic development.
- *Cooperation on development.* This underpins the nature/scope of EU assistance to the Kyrgyz Republic. As per Article 45 of the PCA, support is to be channelled to a variety of sectors, including economic and social development, human resources development, support for enterprises (including privatisation, investment and development of financial services), agriculture and food, energy and civil nuclear safety, transport, tourism, environmental protection and regional cooperation.

11.2.1.2 The EU Strategy for a New Partnership with Central Asia

The EU Strategy for a New Partnership with Central Asia was adopted by the European Council on 21-22 June 2007 “in recognition of the increasing importance of Central Asia for EU interests relating to security, stability, governance and energy diversification.”¹³¹

The Strategy builds on existing instruments, including the Partnership Cooperation Agreement, the Trade and Cooperation Agreements (where these are still in force), the EC Regional Assistance Strategy Paper 2007 - 2013, Indicative Programmes 2007 - 2010, and various thematic assistance programmes, such as, the European Instrument for Democracy and Human Rights. It sets out priorities for EU cooperation with the region as a whole, notably cooperation in the fields of human rights, rule of law, good governance and democracy; education; economic development; trade and investment; energy and transport; environmental policies; common threats and challenges; and intercultural dialogue.

The Strategy was last reviewed in 2015. It was concluded that the long-term priority areas set out in the Strategy remain relevant for European engagement in the region, though the EU should seek “to have more of an impact by focusing in a few specific areas” and thus be able to bring about sustained, long-term positive change that can successfully reshape Central Asian societies¹³².

11.2.2 MFA in the context of the overall EU support package

11.2.2.1 MFA and wider EU support

Decision No 1025/2013/EU pertaining to the provision of macro-financial assistance to the Kyrgyz Republic indicates that the MFA operation is intended to restore the country’s external finance situation and promote a policy programme that is capable of driving strong adjustment and structural reform and, over the longer term, to “improve the balance of payment position [...] and reinforce the implementation of relevant agreements and programmes with the Union.”¹³³ To ensure consistency with the EU’s external policy towards the Kyrgyz Republic, the EU MFA to Kyrgyzstan was therefore designed with consideration for reforms that could support the Kyrgyz Republic’s longer-term commitment to values shared with the Union (as set out in the PCA and the Union Strategy for Central Asia (2007 - 13)), including democracy, the rule of law, good governance, respect for human rights, sustainable development, and poverty reduction, as well as its commitment to the principles of open, rule-based and fair trade.

Though the EU MFA did not directly target the aforementioned areas of social reform, it provided the EU with leverage to prevent the enactment of the ‘anti-LGBTI’ and ‘foreign agents’ legislations, both judged contradictory to EU/ international human rights laws/principles. In that regard, the EU’s efforts were complemented by those of the EU Delegation, other international donors (e.g. the USAID, United Nations, WB) and local NGOs and civil society.

11.2.2.2 MFA and other budget support programmes

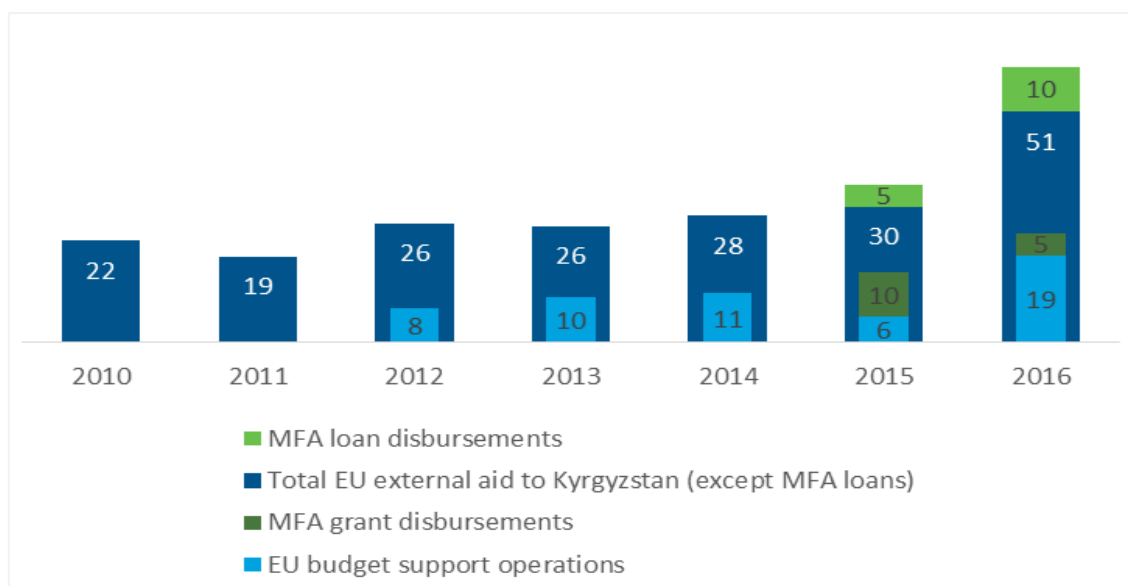
As depicted in Figure 20 below, over the period 2012 - 2016, between 30 and 50 per cent of EU assistance to the Kyrgyz Republic was delivered in the form of budget support or MFA grants.

¹³¹ EEAS (see: https://eeas.europa.eu/headquarters/headquarters-homepage/4939/eu-strategy-for-a-new-partnership-with-central-asia---implementation_en0)

¹³² European Parliament (2016) ‘Motion for a European Parliament Resolution on implementation and review of the EU-Central Asia Strategy.’

¹³³ European Parliament (2013) ‘Decision No 1025/2013/EU of the European Parliament and of the Council of 22 October 2013 providing macro-financial assistance to the Kyrgyz Republic.’

Figure 20. EU external aid to Kyrgyzstan, by type, over 2010 - 2016 (in EUR million)



Source: Annual Report on the implementation of the European Union's instruments for financing external actions and DEVCO disbursement data. Please note that there is little information available on the types of EU aid provided to Kyrgyzstan prior to 2012.

An important objective of EU assistance deployed via the MFA and other budget support instruments has been to help stabilise Kyrgyzstan's macroeconomic situation, while encouraging the necessary reform process. As mentioned previously, in addition to the MFA, Kyrgyzstan benefited from six other budget support programmes over the period 2011 - 16 – also referred to as Sector Reform Contracts (SRCs). Some are still ongoing.

SRCs have generally focused on social reforms in specific areas/sectors (e.g. social protection, education, electoral system). Nonetheless, there is some degree of consistency between the SRCs and the EU MFA as regards certain reform areas prioritised for Kyrgyzstan. As such, most of the earlier SRCs¹³⁴ included general PFM conditions (upon which the release of funding was conditional). Specific references to PMF reform(s) are made in individual SRCs¹³⁵. For instance, SRCs in the sectors of social protection and education included specific PFM conditions (for the disbursement of the 'variable' tranche), notably in the following sub-areas: Medium-Term Budget Framework / policy-based budgeting; transparency of budget processes; internal audit; budget preparation processes and public investment management.

Table 9 overleaf outlines specific areas (highlighted in blue) whereby the reform steer of the SRCs and the EU MFA is closely aligned.

¹³⁴ The EU Delegation indicated that there was no reinforcing between the MFA and SRC conditions over the period 2015 - 16.

¹³⁵ The full list of criteria to be eligible for budget support include: (1) a well-defined national or sectorial development or reform policy and strategy; (2) a stable macroeconomic framework; (3) good public financial management or a credible and relevant programme to improve it; (4) transparency and oversight of the budget (budget information must be made publicly available).

See <https://ec.europa.eu/europeaid/node/13967>

Table 9. Detailed comparison of MFA and EU budget support programme conditionality

Reforms	MFA	Sector Support Programme: Social Sector	Policy Support Programme: Social Protection and Public Management	Sector Support Programme: Finance	Policy Support Programme: Social Protection and Finance	Support to reform of education in the Kyrgyz Republic	to the sector of the Kyrgyz Republic	Sector reform contract Social Protection Kyrgyzstan	Education Sector Reform Contract	Strengthening Democracy through Electoral Reform – Sector Reform Contract
PFM	V	V	V			V		V	V	V (only general condition)
PFM – Medium-Term Budget Framework / Policy based budgeting	V	V	V			V		V	V	
PFM – PEFA	V									
PFM – Accounting, reporting / Treasury Management Information System / Financial Management Information System	V									
PFM – External auditing	V									
PFM – Transparency of budget processes		V						V		
PFM – Internal audit		V	V			V		V	V	
PFM – Budget preparation processes	V		V					V		
PFM - Public Investment Management			V					V		
Banking sector	V									
Trade policy: application of WTO commitments	V									
Investment and business environment	V									
Education sector								V	V	

Reforms	MFA	Sector Support Programme: Social Sector	Policy Sector	Sector Support Programme: Social Protection and Public Management	Policy Programme: Finance	Support to reform of education in the Republic	to the Kyrgyz	the contract Social Protection Kyrgyzstan	Sector reform Education Sector Reform Contract	Strengthening Democracy through Electoral Reform – Sector Reform Contract
Electoral reform										V
Social sector		V		V		V				
National statistics				V						

Source: MFA and DEVCO documentation

11.2.3 The extent to which the MFA operation complemented external/international support programmes

The EU MFA is generally intended to supplement the assistance provided by the IMF (in the context of an ECF arrangement) as well as other donors. Specifically, its disbursement is generally conditional upon “a satisfactory track record in the implementation of the [...] IMF credit arrangement” as well upon a “positive assessment [...] of progress made with respect to economic stabilisation and structural reforms.”¹³⁶ For this reason, MFA conditionalities often complement the reform package associated with the IMF’s arrangements with beneficiary countries. Further, the WB’s Development Policy Operations (DPOs) – DPO I and II – have focused on reform areas that bore some degree of similarity with those emphasised by the EU MFA. For instance, some of the core objectives of DPO I, comprised: “improving public sector accountability and efficiency in the management and use of public resources;” “sharpening competitiveness and enhancing the attractiveness for private investment [...]”; and improving the environment for development of private businesses,” notably through reforms in the banking sector¹³⁷. In the same vein, DPO II, focused on “the promotion of sustainable growth through more accountable use of public resources and an improved environment for doing business.”¹³⁸

More generally, it can be said that the areas of structural conditionality on which EU MFA (to a particular beneficiary country) is based are more widely determined through on-going cooperation with the international donor community, generally to avoid duplication and to supplement and increase the effectiveness of actions financed via other donor programmes in priority reform areas. PFM reforms, for instance, were designed to complement efforts in the area already being made, in the context of the Multi-Donor Trust Fund (MDTF), by the EU, various EU/EEA Member States (notably: Sweden (SECO), Switzerland (SIDA), the UK (DFID)), and several international donors (namely the IMF and the WB). Similarly, the reform pertaining to the banking sector was coordinated with certain IFIs, notably the IMF. As such, while the EU MFA focused on amending banking regulations and strengthening the central bank’s early intervention and resolution powers, the IMF programmes pushed for reforms designed to increase the central bank’s autonomy/independence.

Table 10 overleaf provides a high-level comparison of focal reform areas driven by the EU, via the MFA, and key donors, such as the IMF and the WB, through their respective support programmes in Kyrgyzstan. It is worth noting that, while reform efforts were aligned and there was some degree of commonality in terms of the reform areas covered by the IMF, other key donors (e.g. WB), and the EU, there was little overlap/interdependence across specific conditions (i.e. actions induced by the MFA did not directly influence/contribute to the progress of specific IMF/WB conditions/reforms).

¹³⁶ European Commission (2013) ‘Macro-financial assistance for the Kyrgyz Republic: Grant and Loan from the European Union of up to EUR 30 million - Memorandum of Understanding between the European Union and the Kyrgyz Republic.’

¹³⁷ World Bank (2017) ‘Kyrgyz Republic Programmatic Development Policy Operations I and II.’

¹³⁸ World Bank (2017) ‘Kyrgyz Republic Programmatic Development Policy Operations I and II.’

Table 10. Comparison of MFA, IMF and WB conditionalities

Areas of focus	MFA	IMF 2011	IMF 2015	WB DPO I	WB DPO II
PFM - Medium-Term Budget Framework	V				
PFM - PEFA	V				
PFM - Accounting, reporting / Treasury Management Information System / Financial Management Information System	V	V	V		
PFM - External auditing	V				
PFM - Internal auditing					V
PFM - Budget consolidation		V			
PFM - Budget law			V		
PFM - Debt management			V		
PFM - Public Investment Management			V		
PFM - Public Procurement			V	V	V
PFM - Structure of the MoF		V			
PFM - Budget discipline / transparency				V	V
Banking sector - Banking Code / Law	V	V	V		
Banking sector - AML		V	V		
Banking sector - Crisis Management and Bank Resolution		V	V		
Banking sector - De-dollarisation of the financial sector			V		
Banking sector - Level playing field across banks			V		
Banking sector - Macroprudential regulation			V		
Banking sector - Supervision			V	V	V
Banking sector - Small and medium enterprise access to finance and leasing					
Banking sector - Reinforcement of the NBKR's supervisory function					V
Banking sector - Strengthening of the Deposit Protection System					V
Banking sector - Access to finance					V

Ex-post evaluation of Macro-Financial Assistance operation to the Kyrgyz Republic over the period 2013 - 2016

Areas of focus	MFA	IMF 2011	IMF 2015	WB DPO I	WB DPO II
Trade policy - application of WTO commitments	V				
Investment and business environment – startup and operations				V	
Investment and business environment – Reduction of red tape	V				
Investment and business environment – Deposit protection arrangements					V
Investment and business environment – Business inspections				V	V
Investment and business environment – Increased accountability of executive directors					V
Energy sector			V	V	V
Fiscal policy - Expenditure management			V		
Public administration reform			V		
Social protection			V		
VAT / Tax policy / Tax administration reform/ Customs valuation		V	V		
Governance / anti-corruption				V	V
Judicial reform				V	V

Conclusions

The evidence gathered suggests that the MFA was coherent with key principles, objectives and measures taken as part of other EU external actions towards Kyrgyzstan.

The determination of the amount of the MFA was based on a complete quantitative assessment of the Kyrgyz Republic's residual external financing needs, its capacity to finance itself with its own resources, the extent of financing provided by the IMF, the WB, and multilateral donors, as well as the pre-existing deployment of other of the EU's external financing instruments, including the added value of the overall Union involvement.

There was also coherent alignment of MFA conditionalities / reforms with other EU and international donor support programmes, notably in the PFM and banking areas.

12 Social Impact Analysis

12.1 Introduction

As part of this evaluation we conducted a Social Impact Analysis (SIA) to evaluate the contribution of the EU's macro-financial assistance (MFA) operation towards the social situation in the Kyrgyz Republic.

The European Commission disbursed EUR 30m (about \$33m) over 2015 - 2016 to the Kyrgyz Republic under an MFA operation which was designed to support and stabilise the Kyrgyz economy. This MFA operation complemented an IMF rescue package of about \$92.4m provided to the Kyrgyz Republic under the Extended Credit Facility (ECF) programme which began in April 2015. Other key events include the signature of the Memorandum of Understanding (MoU), the Loan Facility Agreement and the Grant Agreement (October 2014).

The Memorandum of Understanding (MoU) which was signed prior to disbursement of the MFA had no explicit conditions on social outcomes in Kyrgyz Republic. Moreover, the funds provided were in the form of budgetary support and, as such, none of the funds were earmarked for any particular social programmes.

The absence of any explicit social conditions in the MoU presents a challenge with respect to the assessment of the social impact of EU's MFA operations. In light of this challenge, the conceptual framework adopted in the SIA entails the identification of (1) potential direct impacts of the MFA; and, (2) various channels through which social impacts might be realised.

The direct effects considered in the analysis include changes to business and investor confidence/behaviour, funding provided for public policies and regulatory/structural reform. On the latter point, the SIA assesses the extent to which structural reform has occurred and has alleviated issues, such as corruption and inefficiency. This direct impact also concerns potential legislation which was discouraged by the EU (and eventually dropped), such as the 'anti-LGBTI' and 'foreign agents' draft laws. The evidence gathered indicates that the EU's diplomatic efforts contributed to stopping the passage of the two bills.

The SIA considers the labour market, changes to nominal variables (e.g. exchange rates, inflation), the Kyrgyz social fund and developments in public reform as key channels of causation. With consideration to these putative direct impacts and channels, the selected social indicators are analysed to determine whether there is any empirical evidence of social impact or 'cushioning' from the socio-economic crisis. Indicators assessed include:

- the job creation rate;
- the national unemployment rate;
- levels of unemployment, employment and economic inactivity among the working age population;
- real wage growth (both regional and national);
- spending on the social fund and social benefit programmes;
- education enrolment rates and outcomes;
- the number of healthcare facilities (changes over time);
- inflation and the cost of living; and
- national and regional poverty rates.

Wherever possible, detail on how the MFA was spent is incorporated in the analysis. However, the extent to which MFA-use can be traced is highly limited. Thus, the analysis contained in the annex draws on economic theory where evidence is unavailable.

12.2 Conclusions

In summary, this analysis has sought to evaluate the contribution of the EU's macro-financial assistance programme towards the social situation in the Kyrgyz Republic. We have investigated this question by assessing several channels through which a package of the MFA's nature affects the social situation in a country. Such channels included: (1) the labour market; (2) nominal variables affecting the cost of living; (3) the Kyrgyz social fund (in addition to education and health spending); and (4) developments in public/legislative reform.

Using a counterfactual analysis approach, we compared what happened to the Kyrgyz Republic's social situation during and after the MFA operation (the baseline case) against two alternative scenarios. These alternatives reflect what would have happened if there had been no MFA operation (Alternative 1) and what would have happened if there had been neither MFA nor support from the IMF via the ECF (Alternative 2).

Evidence from the counterfactual analysis suggests that the social consequences stemming from the absence Macro Financial Assistance provided to the Kyrgyz Republic (Alternative 1) would have been relatively minor and contained (in absolute terms and relative to Alternative 2). While the shortfall would likely have put pressure on the account of the Central Bank and resulted in some cuts to government procurement of non-essential items (most probably less than EUR 30 million corresponding to the total MFA envelope), it seems likely most core policies relating to the social situation would have been unaffected by the absence of Macro Financial Assistance. It seems unlikely there would be many visible impacts on the labour market, the cost of living and provision of key public services (e.g. health, education, pensions).

However, the pressure placed by the EU on the Kyrgyz authorities to reject key legislative proposals had positive impacts on civil society and social justice. By preventing the enactment of the 'foreign agents' law, the EU MFA operation supported local NGOs and their causes (many concentrating on the poverty reduction and human rights protection). Further, by preventing the passage of the anti-LGBTI bill, the EU helped stop a potentially very disruptive legislation that would have infringed fundamental human rights, notably of minorities.

With respect to the second counterfactual (no MFA and IMF), evidence suggests that the social consequences would have been more severe. The considerable shortfall in budget support, exacerbated by the withdrawal of other IMF-dependant donor(s), would impact the economy considerably. The withdrawal of financial support would have likely necessitated less favourable external support and sharper cuts in public spending. Consequently, the scale of the shortfall means that real and visible impacts on the labour market, the cost of living and provision of key public services (e.g. health, education, pensions) would have been observed. In the absence of international macroeconomic support, the gloomy economic outlook would put downward pressure on the currency. This in turn would be expected to generate inflationary pressures in key commodities. It is not unlikely that, under such conditions, volatility in consumer prices would persist, negatively impacting the cost of living and poverty.

13 Debt Sustainability Analysis

13.1 Introduction

As part of this evaluation we also conducted a debt sustainability analysis (DSA) to evaluate the contribution of the EU's macro-financial assistance (MFA) operation towards the sustainability of public debt in the Kyrgyz Republic.

The European Commission disbursed EUR 30m (about \$33m) over 2015 - 2016 to the Kyrgyz Republic under a MFA operation which was designed to support the Kyrgyz economy by facilitating their efforts to restore external financial sustainability and to alleviate balance of payments issues. The MFA was disbursed in four tranches:

- a EUR 10m grant on 11 June 2015,
- a EUR 5m loan on 15 October 2015,
- a EUR 5m grant on 10 February 2016, and
- a EUR 10m loan on 13 April 2016.

This MFA operation complemented an IMF rescue package of about \$92.4m provided to the Kyrgyz Republic under the Extended Credit Facility (ECF) programme which began in April 2015. Some of the funds from the IMF programme were disbursed over a three-year period starting with about \$26.8m in 2015, \$26.6m in 2016, and \$26.5m in 2017, with the final tranche not disbursed. These programmes provided specific budget financing which likely boosted demand, but also broader support to the Kyrgyz economy in the form of improved investor confidence in the economy that comes with receiving international financial support, and enacting economic reforms agreed with international partners such as the EU and the IMF. Given the existence of some coordination in the designing and implementation of these two programmes, and the IMF's central role in stabilising the Kyrgyz economy, our analysis also refers to the IMF's ECF programme, although the focus of this evaluation remains with the MFA operation.

We evaluate the MFA's contribution using a counterfactual analysis approach in which we compare what happened to debt sustainability following MFA fund disbursements against what would have happened if the MFA operation was not in place.

We also assess what would have happened to key debt-burden indicators in case the government response to the absence of MFA funds had been to simply cut non-protected public spending. For this, we analyse debt-burden indicators and macroeconomic variables which influence the path of a country's debt and its capacity to manage its debt sustainably in the medium term to long term. In reality, assuming that the scale of cuts would have been probably mitigated to some extent by other options that are not mutually exclusive, these estimates show the most pessimistic scenario.

From a technical point a government is solvent if the present value of its future primary balances is at least as large as its public debt stock. This suggests that looking at a country's ability to service its public debt as per the debt's contract is a good starting point to assess debt sustainability. The ability to service debt is reflected in the debt-burden indicators we choose to proxy a country's capacity to meet debt obligations. Debt burden indicators of interest include ratios of debt stock and debt service relative to a country's capacity to repay, commonly represented by GDP and fiscal revenue. The debt burden indicators we assess include: (1) the present value of public debt to GDP ratio; (2) the present value of public debt to fiscal revenue ratio; and (3) the public debt service to fiscal revenue ratio.

These indicators are identified in the IMF DSA framework as relevant for public sector debt. Debt stock is assessed in present value terms as opposed to nominal terms because the present value measure accounts for the concessional component that is generally present and substantial in size in financing extended to low-income countries such as the Kyrgyz Republic. By comparing how these indicators responded to the MFA

operation against how they would have evolved if the MFA was not in place (the counterfactual case), we can estimate the impact of the EU's MFA programme on the Kyrgyz Republic's debt sustainability.

Despite the limited information available on how exactly the MFA was spent, its designation as budget support suggests that it went towards government spending. It can therefore be expected that the MFA may have enhanced the Kyrgyz Republic's ability to manage its debt obligations by providing liquidity in the short term and supporting GDP growth, thus improving debt sustainability prospects. This is partly because it boosted government revenues, part of which go towards servicing existing debt and/or reducing the need to take on new debt.

The MFA operation may also have funded an increase in (or maintaining of) government spending levels in a way that contributed towards the Kyrgyz Republic achieving its macroeconomic stabilisation efforts. Finally, the MFA had a concessional component, suggesting that the Kyrgyz Republic may have benefited from savings on the cost of borrowing, and so limited the accumulation of debt to some extent.

13.2 Conclusions

In summary, this analysis has sought to characterise the contribution of the EU's macro-financial assistance programme towards the sustainability of the Kyrgyz Republic's public debt. We have investigated this question by assessing the channels through which a package of the MFA's nature affects the macro-financial dynamics of a country's economy, with a focus on debt sustainability.

Using a counterfactual analysis approach, we compared what happened to the Kyrgyz Republic's public debt situation during and after the MFA operation (the baseline case) against an alternative scenario of what would have happened if there had been no MFA operation. The MFA disbursements amounted to EUR 15 million in 2015 and 2016 respectively, circa 0.3 per cent of GDP in each of these two years.

Following a comprehensive review of information partly based on our brainstorming sessions with local economic experts and interviews with local and international stakeholders, the consensus emerging indicates that the most likely response by the Kyrgyz Republic if the MFA operation was not in place would have been a mix of public spending cuts, drawing on the Government's reserves at the NBKR, and possibly further assistance from Russia. This assumes that the Kyrgyz Republic still had the IMF's rescue package in place.

However, in a scenario where both MFA and IMF programmes were not in place, the emerging consensus still points to the same policy response but at a larger magnitude given the joint package size and the potential of its absence to restrict concessional funding from other sources. In addition, the exceptional circumstances created by such a scenario increase the probability of a larger support package from Russia.

We have also sought to quantify the MFA's impact by looking at the evolution of key debt-burden indicators if the Kyrgyz Republic had simply cut spending in response to a situation where the MFA programme was not in place (a more pessimistic assumption as in reality cuts would have been probably mitigated to some extent by financing from Russia and drawing on government's reserves deposited at the NBKR).

We find that while public debt remains manageable across all scenarios that have been considered, not having the MFA programme elevates debt-burden indicators slightly towards less safe levels compared to where they would be with the MFA operation in place. Lower debt-burden indicators reinforce the Kyrgyz Republic's capacity to manage its public debt sustainably, and so support the rationale for the MFA package.

Over 2015 - 17, a period when MFA funds were disbursed, Kyrgyz economic performance was relatively satisfactory. Real GDP grew at just over 4% annually on average, inflation stood at 3.2% pa while public debt was 59.7% of GDP pa on

average. This performance is, at least in part, due to financial assistance the Kyrgyz Republic received during this period.

The MFA lowers the present value of the debt-to-GDP ratio further below the benchmark level above which debt sustainability becomes a concern. We estimate that having the MFA operation in place will lower the present value of the debt-to-GDP ratio by 1.6 percentage points on average over 2015 - 2025, compared to not having the MFA. The MFA operation will also result in the present value of the debt-to-revenue ratio being lower by over 4 percentage points on average over 2015 - 2025.

Looked at, in isolation, Alternative 1 (no MFA) would not have led to a large impact on Kyrgyz debt sustainability in part because of its size and the fact that the delay between the 2011 announcement of the operation and the 2015/16 disbursements limited any confidence gains for the Kyrgyz economy. On the other hand, Alternative 2 (no MFA and IMF) would likely have negatively affected confidence in the Kyrgyz economy and the impact of reforms that were implemented as part of IMF conditionalities. Overall, the public debt outlook in the Kyrgyz Republic following the MFA operation has been, and is expected to remain, stable in part because of support that the country received from international partners such as the EU and the reinforcing role those donors played in driving through necessary reforms associated with financial aid from donors.

14 Conclusions

This evaluation has assessed, ex post, the contribution of the MFA facility to the macroeconomic and structural adjustment of Kyrgyzstan. This has involved an examination of: (1) whether the ex-ante considerations determining the design and terms of the operation were appropriate, taking due account of the economic, political and institutional context; and (2) whether the outcome of the programme met the objectives.

A multi-methods approach, combining primary and secondary research techniques, was used to answer the evaluation questions. Evidence triangulation, involving the analysis of both quantitative and qualitative data and information from multiple and different sources, was used to increase validity and draw conclusive findings. It is important to note that certain research methods were more relevant to specific evaluation criteria and constituted the main, though *not* the sole, source(s) of evidence for answering associated research questions.

For instance, factual data gathered from desk research, primarily fed into the assessment of coherence which required a review of past/current EU programmes and other instruments, and programmes led by the Kyrgyz government and other international donors respectively. This is however not unusual as it is often unlikely that stakeholders have all of the necessary information at hand and/or are able to discuss these programmes extensively during interviews. As part of this evaluation, the information has therefore been sourced from the Commission's own *repertoire* which was generally adequate and helped supplement information gathered from primary research and/or fill any substantive gaps.

Similarly, interviews with key informants constituted an important information-gathering tool during the study. While such interviews have enabled the study team to collect useful insights into the MFA operation, the information gathered may have been limited at times owing to: institutional memory loss / reduced ability to recall (due to the time that has elapsed), reluctance to provide a candid account, unavailability/declined participation on the part of stakeholders.

To ensure that these methodological limitations would not have a considerable bearing on the study findings, various courses of action were taken, including: triangulation, to ensure that evidence generated by/from multiple perspectives, methods and data sources were sufficiently appraised and fed into conclusive findings; hypothesis exploration, to allow for multiple hypotheses to be tested and to identify the best, most probable explanation (especially where little evidence was gathered or the evidence collected did not permit for clear-cut conclusions to be drawn); information synthesis, comprising a descriptive account of the data/information gathered as well as a critical assessment of the findings (based on the views of key informants as well as those of the study team); and peer-review and validation of findings, to further credibility and validity of the research (by drawing upon the expert knowledge of an expert group or the objective, independent reviews of key stakeholders) and to allow the study team to revise and improve the study findings before publication.

14.1 Conclusions on the design (Relevance) and implementation (Efficiency and Coherence) of the operation

14.1.1 Relevance

14.1.1.1 Size of the assistance

After prolonged (procedural) delays, the MFA disbursements were made in 2015 (EUR 15 million) and 2016 (EUR 15 million), accounting for around 0.3 per cent of the GDP in each year.

In absolute terms, the EU MFA was substantially less than the extent of IMF financing provided over the period 2015 - 16. Other EU budget support (delivered through three

Sector Reform Contracts (SRCs)) was also relatively more important (in size) when compared to the MFA operation.

The EU MFA was nonetheless in line with (or more comparable to) budget support financing provided by other donor partners, notably the WB and ADB. Overall, the MFA accounted for 14 per cent and 12 per cent of the total assistance package (budget support financing exclusively) provided by the multilateral and bilateral donors in 2015 and 2016. Moreover, when assessed against the total value of EU budget support provided to Kyrgyzstan in 2015 and 2016 (i.e. combined MFA and SRC support), the EU MFA made up 17 and 27 per cent of the EU's total budget support package respectively.

The size of the assistance was judged appropriate, given the country's financing needs as well as the criteria governing the use of the MFA instrument.

14.1.1.2 Form of the assistance

The MFA operation comprised a 50-50 split between grants and loans, reflecting the compromise reached between the Council of the European Union (who strongly opposed grant-only financing to Kyrgyzstan) and the European Parliament. The MFA grant component accounted for 10 per cent and 6 per cent of the overall grant assistance received by the country in 2015 and 2016 respectively. The concessional financing terms and un-earmarked character of the MFA package constituted important attributes (of the operation) and were positively received by Kyrgyz authorities.

Further, the debt sustainability analysis does not provide evidence of a substantially negative impact of the loan component of the MFA on public debt. As such, not having the MFA programme was reported to elevate debt-burden indicators slightly towards less safe levels compared to where they would be with the MFA operation in place. Lower debt-burden indicators reinforce Kyrgyzstan's capacity to manage its public debt sustainably, and so support the rationale for the MFA package.

The form of the overall assistance could therefore be judged appropriate.

14.1.1.3 Focus of reforms

The MFA conditionality reform package targeted structural weaknesses and vulnerabilities affecting the economy. The MFA conditions were generally in line with priorities set by the Kyrgyz government as well as other donors / IFIs (as part of their support programmes). These were also consistent with wider objectives associated with EU MFA operations, notably to promote structural measures/reforms capable of driving and maintaining macroeconomic stability.

The pace of reform implementation was generally swift, with six out of the seven conditions having been met prior to the MoU being approved, signed and ratified. This is not an uncommon feature of MFA operations, though the extent to which the negotiations ought to have been re-opened was commonly debated among stakeholders. In the Kyrgyz context, this was not desirable and judged potentially harmful. As such, owing to (standard) administrative formalities, renewed negotiations would have created further, unnecessary delays and potentially hindered the design and implementation process. In the case of Kyrgyzstan, further delays would have amplified tensions that emerged between the Kyrgyz government and the EU at the time owing to persistent procedural delays in the early stages of the MFA operation.

Overall, the MFA-induced reform package can therefore be deemed relevant, notably in terms of the political, economic and institutional conditions that prevailed in Kyrgyzstan at the time of the negotiations and further down the line upon finalisation of the operation.

14.1.2 Efficiency

14.1.2.1 Timing of the operation

There were prolonged procedural delays surrounding the approval of the MFA. These in turn led to a postponement of the MFA disbursements. Although the MFA operation was still relevant at the time of the disbursements (i.e. June 2015 and April 2016), this was only coincidental and not by design.

14.1.2.2 Dialogue and monitoring

Formal and regular missions constituted an important channel of dialogue between the Commission and Kyrgyz authorities, ensuring the operation was running as smoothly and efficiently as possible. These were generally led by the Commission in close collaboration with the EU Delegation to the Kyrgyz Republic. In Kyrgyzstan, the Ministry of Finance endorsed the liaison role which involved negotiating the terms / conditions of the MFA operation and coordinating / undertaking / monitoring the implementation of reforms.

Compliance with the necessary MFA conditions was, on the EU side, monitored by the Commission (through field visits) and the EU Delegation (on a more regular basis). The monitoring was appropriate and proportional.

14.1.2.3 Reform coordination and ownership (including added leverage for Kyrgyz authorities)

Concerted efforts between the EU and other key donors, notably the IMF and WB, helped signal the desired reform steer to Kyrgyz authorities in priority areas. In general, there were no specific contradictions between the MFA conditionalities and national policies. In some instances (e.g. audit reforms), the MFA even brought about added leverage for authorities in their pursuit of sectoral reforms that would probably not have been prioritised by the Kyrgyz government.

More generally, however, the level of reform ownership was varying. This was reported to be due to several factors, including: the pendulum of the political cycle, the economic outlook, and other considerations, such as the geopolitical context and the strategic importance attached to the country's relationship with neighbouring countries, notably Russia.

Overall, the significant delays in approval and implementation of the operation appear to have undermined the EU's leverage and visibility of the MFA.

14.1.3 Coherence

The MFA was consistent with key principles, objectives and measures taken as part of other EU external actions towards Kyrgyzstan. There was also coherent alignment of MFA conditionalities / reforms with other EU budget support programmes, notably in the PFM area. For instance, EU Sector Reform Contracts (SRCs) in the sectors of social protection and education included specific PFM conditions, notably in the following sub-areas: Medium-Term Budget Framework / policy-based budgeting; transparency of budget processes; internal audit; budget preparation processes and public investment management.

The areas of structural conditionality on which the MFA operation was based were determined through on-going cooperation with the international donor community, generally to avoid duplication and to supplement and increase the effectiveness of actions financed via other donor programmes in priority reform areas. PFM reforms, for instance, were designed to complement efforts in the area already being made, in the context of the Multi-Donor Trust Fund (MDTF), by the EU, various EU/EEA Member States (notably: Sweden (SECO), Switzerland (SIDA), the UK (DFID)), and several international donors (namely the IMF and the WB). Similarly, the reform pertaining to the banking sector was coordinated with certain development partners, notably the IMF.

14.2 Conclusions on the effectiveness and added value of the MFA in supporting macroeconomic and financial stabilisation and structural reform

14.2.1 Effectiveness

14.2.1.1 Progress in terms of macroeconomic and financial stability, including debt sustainability

The MoU accompanying any MFA operation typically makes it explicit that the MFA is intended to complement the support and conditions specified by the IMF as part of its own support programme(s). In the Kyrgyz context, the MFA disbursements, amounting to EUR 15 million in 2015 and the same amount a year later, corresponded to circa 0.3 per cent of the GDP in 2015 and 2016 respectively, not a negligible amount. This increases to circa EUR 37 in 2015 (or 0.7 per cent of GDP) and the same amount (and the share of the GDP) a year later when combined with IMF disbursements.

Gathered evidence suggests that, had the EU MFA not been made available, the Kyrgyz government could have plausibly resorted to other options. More concretely, while prospects of raising additional revenue through increases in taxes and/or proceeds from privatisation were ruled out, the withdrawal of some of the government's reserve deposits at the central bank, along with a reduction in public spending and an increase in the level of assistance sought from Russia, were considered plausible alternative courses of action. Primarily, the cuts would have affected 'unprotected categories' of public spending, such as capital expenditures and spending on goods and services, though almost certainly the magnitude of these cuts would have been smaller than the total size of the MFA disbursements in each year (provided that complementary sources of financing were available). This would have allowed for the expected negative impact on aggregate demand to be contained, with an ultimately reduced impact on GDP and economic growth.

Furthermore, the DSA shows that the absence of the EU MFA ('Scenario 1') would not have had a major impact on the sustainability of the Kyrgyz debt. As such, given the low awareness/visibility levels around the EU MFA, the likelihood that the absence of the EU MFA would have led to significant, adverse impacts on private sector confidence appears highly unlikely. Following this line of reasoning, a presumed negative impact of the absence of the EU MFA on, *inter alia*, foreign exchange rates, inflation and households' disposable incomes, is also highly improbable.

The hypothetical absence of joint assistance from the EU (via the MFA) and the IMF (via the ECF) ('Scenario 2') would have had far more severe implications. This is because the absence of the ECF would have most certainly affected the WB's readiness to provide budget support to Kyrgyzstan, given the crucial importance of the stability of the macroeconomic framework required by the WB (and implicitly strengthened by the IMF programme) to deploy its budget support operation(s) (e.g. Development Policy Operation(s)). As a result, if the assistance provided by the EU, the IMF and the WB in 2015 had not actually materialised (i.e. USD 29 million from the IMF, USD 16.5 million from the WB and USD 16.5 million from the EU via the MFA respectively), this would have corresponded to a financing gap of USD 62 million, or ~1 per cent of GDP in 2015 only. In this instance, the options available to the Kyrgyz government to close this gap would have been very similar to those presented under 'Scenario 1,' though its size would have most certainly required deeper public cuts. In addition, an erosion of business and investor confidence, caused by the absence of the IMF support, would have been likely. This would have possibly backfired, in the form of an even greater depreciation of the Kyrgyz Som (already high under 'Scenario 1') and a resulting appreciation of Kyrgyzstan's foreign-denominated debt and associated servicing costs. Ensuing impacts would have included a rise in domestic prices / reduction in households' disposable incomes and a potentially substantial loss of FDI.

In parallel, the absence of the IMF support would have meant that some of the reforms initiated by its programme would not have been implemented and, consequently, the technical assistance and disciplining role of the IMF, in terms of reform implementation, would have been absent.

14.2.1.2 Progress in terms of reform implementation

Overall, *sensu stricto*, Kyrgyzstan fulfilled the economic and structural policy conditions related to the disbursement of the MFA in a satisfactory way. The evidence gathered suggests that the MFA support package brought about additional impetus for reform in priority areas, encouraging the implementation of specific, short-term, measures that may have otherwise been overlooked / further delayed by national authorities (e.g. reforms pertaining to public sector auditing). The focus of reform priorities under the EU MFA was also closely aligned to those set by other important donors (e.g. IMF, WB).

The fact that most of the MFA conditions had been fulfilled by the time of the approval and signature of the MoU (in late 2013 and 2014 respectively) however evoked the possibility for re-negotiations among stakeholders consulted during the study. The shared consensus however was that re-opening discussions around the MFA reforms could have amplified political tensions that prevailed at the time between the Kyrgyz government and the EU, as a result of the numerous delays that surrounded the approval of the MFA and its disbursement. Additionally, the MFA (in the Kyrgyz context) bore greater political, as opposed to economic, significance. It aimed to signal the EU's support for the democratic reforms undertaken by the Kyrgyz government as part of the country's transition to a parliamentary democracy. Re-negotiations could have undermined the EU's political goodwill and defeated the true purpose of the MFA operation.

To some degree, a re-negotiation of the reform package could have been beneficial to the Kyrgyz economy, though the nature and scale of the impacts associated with a re-negotiation are difficult to establish. As such, it would require gauging the political implications of an even greater delay of the operation (which in turn would require a counterfactual political analysis). As a minimum, it is however safe to assume that re-opening the negotiations would have triggered further delays and worsened the political dialogue between the EU and Kyrgyzstan. Further tensions would have gone contrary to the initial and core intention of the instrument which, as mentioned above, was to support Kyrgyzstan's efforts to transitioning to a parliamentary democracy.

Finally, although not initially envisaged, the MFA conferred added leverage to the EU in its discussions of the 'anti-LGBTI' and 'foreign agents' bills with the Kyrgyz authorities. These two highly controversial legislative proposals would have seriously undermined the rights of the LGBTI community and would have severely affected the activities of Kyrgyzstan's civil society. Both bills were ultimately dropped, and factual evidence suggests that the perceived high risk of losing the financial envelope (promised as part of the MFA operation) constituted a critical determining factor in the Kyrgyz government's decision to abandon the passage of the two laws.

Social impact of the MFA The MFA operation in Kyrgyzstan primarily served a political purpose. This, along with the absence of any explicit social conditions in the MoU, suggest that the MFA did not intend to bring about any significant social impact.

Evidence from the counterfactual analysis suggests that the social consequences stemming from the absence MFA financial envelope provided to the Kyrgyz Republic would have been relatively minor and contained. While the shortfall would likely have resulted in some cuts in government's capital expenditures and procurement of non-essential items, they would have been most certainly smaller than EUR 30 million corresponding to the total size of the MFA envelope. It seems therefore likely that most core policies relating to the social situation would have been unaffected by the

absence of MFA and therefore no visible impacts on the labour market, the cost of living and provision of key public services (e.g. health, education, pensions).

However, with respect to the second counterfactual (no MFA and IMF), evidence suggests that the social consequences would have been severe. The considerable shortfall in budget support, exacerbated by the withdrawal of other IMF-dependant donor(s), would impact the economy considerably. The deterioration of the Kyrgyz economy would have likely led to negative impacts on nominal variables. The Som would have likely deteriorated, leading to further inflationary pressure, which would have raised the cost of living for Kyrgyz households and depressed living standards. The withdrawal of financial support would have likely necessitated less favourable external support and sharper cuts in public spending, possibly reaching also social spending.

Importantly, even though the set of MFA conditions did not have any significant social impact, the operation impacted the social situation through a different channel. More specifically, the EU's partaking in the discussions around the highly-contested 'foreign agents' and 'anti-LGBTI' bills was reinforced by the prospect of the MFA operation. It played a crucial role in advancing the cause of civil society representatives and other multilateral and bilateral partners which was to prevent the enactment of the two laws.

14.2.2 EU added-value

EU added-value was most apparent in, firstly, reinforcing the promotion of structural reforms in several priority areas. The MFA conditions generally supplemented the numerous actions already undertaken by key international donors, such as the IMF. This reinforced the rationale for certain adjustment measures and the need to advance reforms swiftly in targeted sectors.

Secondly, the MFA operation served important political objectives in the Kyrgyz context. The actual disbursement of the MFA is thus likely to have had a significant positive impact on bilateral political relations. As such, it (coincidentally) came at a politically-important moment ahead of parliamentary elections when the country was also experiencing economic difficulties.

Thirdly, the size of the MFA operation (EUR 30 million) corresponded to about 0.3 percent of Kyrgyzstan's GDP in 2015 and 2016 respectively – not a negligible amount. Additionally, an important attribute of the EU MFA versus alternative sources of financing was its highly concessional terms which could have generated significant fiscal savings for the Kyrgyz government. As such, the EU MFA would have provided Kyrgyz authorities with some fiscal breathing space at a time when the country was faced with various economic difficulties as well as preparing for parliamentary elections.

Fourthly, though the MFA operation was not designed to promote social reform directly, it provided the EU with (added) leverage to prevent the enactment of various contested legislations, notably the 'anti-LGBTI' and 'foreign agents' laws. To this end, the added contribution of the MFA was high and potentially on par with that generated from various actions undertaken by other donors (e.g. WB, ADB, USAID) and the civil society who were also very active on this front.

With the numerous procedural delays encountered, however, the EU added value was arguably reduced. These delays were believed to have adversely impacted the extent of awareness / visibility surrounding the operation. As such, this was considered low, especially among the public and the civil society. The MFA's added contribution, notably in terms of boosting the EU's external image and reiterating its commitment to supporting the Kyrgyz authorities in their reform efforts to ensure sustainable political, economic and social development in the Kyrgyz Republic, would thus appear to have been negligible in the long-term, in particular in comparison with development cooperation instruments.

Overall, the MFA did provide some added value, but this was hampered by the exceptionally long time needed to implement the operation.

15 Recommendations

This section sets out a list of recommendations to the Commission in light of the findings gathered as part of the evaluation of the MFA operation in Kyrgyzstan.

Recommendation 1: In instances where: (1) an MFA operation deviates from the general principles of the instrument, for example in a country beyond the usual geographical scope; (2) the objectives of the operation go beyond economic stabilisation considerations; and / or (3) the assistance in relative terms is small, then in such circumstances an alternative evaluation framework should be considered, in line with the general Better Regulation principle of proportionality.

In such instances, there are a number of opportunities to better calibrate the evaluation framework to address the factors affecting the level of analysis of the MFA operation. The Commission may consider:

- Updating the MFA methodological guidelines that accompany the MFA evaluation framework contract with specific criteria for novel operations.
- Adjusting the terms of reference for an evaluation to better reflect the specificities of a novel operation.
- Applying the proportionate approach to evaluation outlined in the Better Regulation toolbox, which can reduce the number of criteria assessed in exceptional circumstances.

Recommendation 2: An indicative timetable, outlining the timing and responsibilities for the different stages of the MFA process, could be negotiated and provided upfront to the authorities in the beneficiary countries.

The delays encountered in the entry into force of the MFA caused much tension between the EU and the Kyrgyz government. Procedural delays, both on the side of the EU and the beneficiary country are however not uncommon when designing and implementing MFA operations. Providing an indicative timeline for agreeing, designing and disbursing the MFA to relevant authorities in the beneficiary countries could therefore help manage expectations.

Recommendation 3: The Commission's ex-ante assessment could provide a more detailed assessment of the expected added value of the MFA operation (at various levels – financial, social, etc.) in line with the EU's latest guidance on added value (COM (2018) 490: 'The principles of subsidiarity and proportionality: Strengthening their role in the EU's policymaking').

The MFA operation in Kyrgyzstan constitutes a good example whereby the Commission successfully used its leverage to bring about added social impacts (not initially foreseen in the early stages of designing the operation). The Commission may therefore wish to consider more extensively, while designing the MFA operation and when secondary objectives are stated in the Decision, whether or how the MFA instrument could provide added leverage to influence (either directly or indirectly) reforms in areas of significance to the Union, such as democracy, the rule of law, good governance, etc.

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