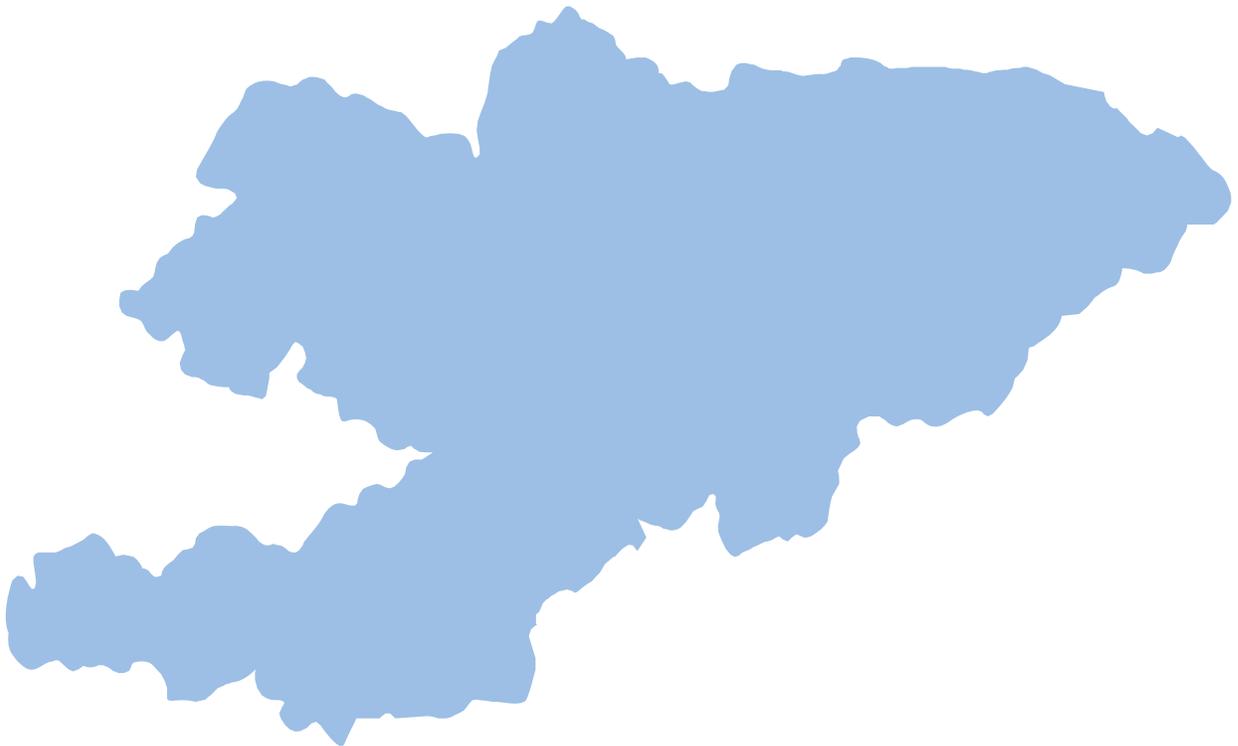




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Kyrgyz Republic Economic Performance Assessment



January 2005

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Kyrgyz Republic

Economic Performance Assessment

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Sponsored by the Economic Growth office of USAID's Bureau of Economic Growth, Agriculture and Trade (EGAT), and implemented by Nathan Associates Inc. under Contract No. PCE-I-00-00-00013-00, Task Order 004, the Country Analytical Support (CAS) Project, 2004-2006, has developed a standard methodology for producing analytical reports to provide a clear and concise evaluation of economic growth performance in designated host countries. These reports are tailored to meet the needs of USAID missions and regional bureaus for country-specific analysis. Each report contains

- A synthesis of data drawn from numerous sources, including World Bank publications and other international data sets currently used by USAID for economic growth analysis, as well as accessible host-country data sources;
- International benchmarking to assess country performance in comparison to similar countries and groups of countries;
- An easy-to-read analytic narrative that highlights areas in which a country's performance is particularly strong or weak, thereby assisting in the identification of future programming priorities.

Under the CAS Project, Nathan Associates will also respond to mission requests for in-depth sector studies to examine more thoroughly particular issues identified by the data analysis in these country reports.

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Note on Data Sources

In addition to our standard sources, we rely heavily in this report on data from the International Monetary Fund (IMF), the National Statistical Committee of the Kyrgyz Republic, the National Bank of the Kyrgyz Republic, and the Kyrgyz Republic's Poverty Reduction Strategy Paper (PRSP) Progress Report of July 2004.

In general, data for the Kyrgyz Republic is of reasonable quality for a low-income country, though some areas could be improved. The IMF Report on the Observance of Standards and Codes (ROSC) in the Kyrgyz Republic, released in November 2003, stated that the country substantially improved the quality of macroeconomic statistics over the previous several years and generally followed the recommendations of technical assistance missions. The data concepts, definitions, and classifications were mostly in compliance with international standards. In June 2005, the UN Economic and Social Council stated in a report on the role of official statistics in the Kyrgyz Republic that the country had an efficient state statistics system and that the National Statistical Committee was independent of the government. Similarly, Global Insight, which analyzes and forecasts macroeconomic developments in the Kyrgyz Republic for government and private clients on a regular basis, finds Kyrgyz official data adequate and uses them in models and reports.¹

At the same time, international agencies point out where further improvement is needed. According to the IMF, existing statistical problems include the estimation of underreporting, referring to the quality of national accounts; the coverage of enterprises for the balance of payments; discrepancies in data provided by the Ministry of Finance and the National Bank; and the compilation of wage data, especially in-kind payments.

¹ CAS team member from Global Insight was one of the writers for this report.

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HIGHLIGHTS OF KYRGYZ REPUBLIC'S PERFORMANCE

Economic Growth	Growth performance in 2000–2004 was mixed, but generally improved toward the end of the period. Growth performance has substantially deteriorated in 2005, apparently because of political turmoil.
Poverty	Poverty rates have declined substantially. There is evidence, however, that the poorest strata of the population are not benefiting from economic progress.
Economic Structure	The Kyrgyz Republic is a predominantly agricultural country with important gold production. Policymakers need to encourage industrial growth and diversification.
Demography and Environment	The Kyrgyz population has been growing over the past several years, and the UN expects that it will continue to do so over the next 25 years, though at a slightly slower pace. The age dependency ratio is quite high but declining.
Gender	Gender indicators reveal relative equity.
Fiscal and Monetary Policy	Some progress has been made in reducing the budget deficit as government revenue has been rising and expenditures have remained at sustainable levels. More needs to be done to increase revenues. Monetary policy has reduced inflation.
Business Environment	Business environment indicators are mixed. While the cost of starting a business fell and the regulatory quality index was on par with wealthier countries, corruption is rampant and contract enforcement is burdensome.
Financial Sector	Despite impressive improvements in recent years—monetization has increased and private sector credit has soared—the financial sector remains inefficient.
External Sector	External sector developments are mixed. Exports posted strong increases, but were concentrated in a few commodities, primarily gold. Imports posted even greater increases. The country relies heavily on foreign aid and loans because it is not an attractive destination for foreign investment.
Economic Infrastructure	Infrastructure development is quite low by absolute standards. Railroad quality is especially poor. At the same time, progress in communications development has been substantial.
Health	Many health indicators are on par or better than the average for the region (life expectancy, access to improved sanitation, and maternal mortality rate), but generally worse than in Russia, Romania, and Bulgaria.
Education	Most education indicators are strong. Government spending on education points to its commitment to further improvement.
Employment and Workforce	The moderate economic expansion was accompanied by an increase in the number of unemployed and the unemployment rate, as job creation was not sufficient to accommodate the growth of the economically active population.
Agriculture	Agriculture is less productive than the rest of the economy, but appears to be in good shape by regional standards.

Note: The methodology used for comparative benchmarking is explained in the Appendix..

KYRGYZ REPUBLIC: NOTABLE STRENGTHS AND WEAKNESSES—SELECTED INDICATORS

Indicators, by topic	Strengths	Weaknesses
Growth Performance		
Gross fixed investment (% of GDP)		✓
Real GDP growth (%)		✓
Poverty and Inequality		
Population below minimum dietary energy consumption (%)	✓	
Population living on less than \$1 PPP per day (%)	✓	
Demography and Environment		
Age dependency rate (dependents per worker)		✓
Population growth rate (%)	✓	
Gender		
Ratio of male to female: adult literacy rate and gross enrollment	✓	
Fiscal and Monetary Policy		
Inflation rate (%)	✓	
Business Environment		
Corruption perception index		✓
Cost of starting a business (% GNI per capita)	✓	
Procedures and time (days) to enforce contract		✓
Regulatory quality index	✓	
Time to register property (days)	✓	
Time to start a business (days)	✓	
Financial Sector		
Domestic credit to private sector (% GDP)		✓
Monetization (M2, % GDP)	✓	
Cost to create collateral		✓
Real interest rate		✓
Interest rate spread, lending rate minus deposit rate (%)		✓
External Sector		
Aid (% of GNI)		✓
Concentration of exports (top three exports, 3-digit SITC, % of exports)		✓
Present value of debt (% GNI)		✓
Exports growth, goods and services (%)	✓	
Gross international reserves (months of imports)	✓	

Indicators, by topic	Strengths	Weaknesses
Economic Infrastructure		
Telephone cost, average local call		✓
Quality of infrastructure index—railroads		✓
Science and Technology		
FDI technology transfer index		✓
Patent applications filed by residents		✓
Health		
Maternal mortality rate (deaths per 100,000)	✓	
Education		
Primary education expenditure (% GDP)	✓	
Pupil-teacher ratio in primary schools		✓
Employment and Workforce		
Unemployment rate (%)		✓
Rigidity of employment index	✓	
Agriculture		
Agriculture value added per worker (1995 U.S. dollars)	✓	
Cereal yield (kilograms per hectare)		✓

Note: The chart identifies selective indicators for which the Kyrgyz Republic's performance is particularly strong or weak relative to benchmark standards; details are discussed in the text. A separate Data Supplement presents a full tabulation of the data examined for this report, including the international benchmark data, along with technical notes on the data sources and definitions.

1. Introduction

This paper is one of a series of Economic Performance Assessments prepared for the EGAT Bureau to provide USAID missions and regional bureaus with a concise evaluation of a broad range of indicators relating to economic growth performance in designated host countries. The report draws on a variety of international data sources¹ and uses international benchmarking against reference group averages and comparator countries (Bulgaria, Romania, and Russia) to identify major constraints, trends, and opportunities for strengthening growth and reducing poverty.

The methodology used here is analogous to examining an automobile dashboard to see which gauges are signaling problems. Sometimes a blinking light has obvious implications—such as the need to fill the fuel tank. In other cases, it may be necessary to have a mechanic probe more deeply to assess the source of the trouble and discern the best course of action.² Similarly, the Economic Performance Assessment is based on an examination of key economic and social indicators to see which ones are signaling problems. In some cases a “blinking” indicator has clear implications, while in other cases a detailed study may be needed to investigate problems more fully and identify an appropriate course for programmatic action.

The analysis is organized around two mutually supportive goals: transformational growth and poverty reduction.³ Rapid and broad-based growth is the most powerful instrument for poverty reduction. At the same time, measures aimed at reducing poverty and lessening inequality can help to underpin rapid and sustainable growth. These interactions create the potential for stimulating a virtuous cycle of economic transformation and human development.

Transformational growth requires a high level of investment and rising productivity. This is achieved by establishing a strong *enabling environment for private sector development*, involving multiple elements: macroeconomic stability; a sound legal and regulatory system, including secure contract and property rights; effective control of corruption; a sound and efficient financial system; openness to trade and investment; sustainable debt management;

¹ Sources include USAID’s internal Economic and Social Database (ESDB) and readily accessible public information sources. The ESDB is compiled and maintained by the Development Information Service (DIS) under PPC/CDIE. It is accessible to staff through the USAID intranet.

² Sometimes, too, the problem is faulty wiring to the indicator—analogue here to faulty data.

³ In USAID’s White Paper on *U.S. Foreign Aid: Meeting the Challenges of the Twenty-first Century* (January 2004), transformational growth is a central strategic objective, both for its innate importance as a development goal, and because growth is the most powerful engine for poverty reduction.

investment in education, health, and workforce skills; infrastructure development; and sustainable use of natural resources.

In turn, the impact of growth on poverty depends on policies and programs that create opportunities and build capabilities for the poor. We call this the *pro-poor growth environment*.⁴ Here, too, many elements are involved, including effective education and health systems; policies facilitating job creation; agricultural development (in countries where the poor depend on farming); dismantling barriers to micro and small enterprise development; and progress in gender equity.

The present evaluation of these conditions must be interpreted with caution, because a concise analysis of this sort cannot provide a definitive diagnosis of economic problems, or simple answers to questions about programmatic priorities. Instead, the aim of the analysis is to spot signs of serious problems for economic growth, based on a review of selected indicators and subject to limits of data availability and quality. The results should provide insight about potential paths for USAID intervention that complement on-the-ground knowledge and further in-depth studies.

The remainder of the report discusses the most important results of the diagnostic analysis in three sections: overview of the economy; private sector enabling environment; and pro-poor growth environment. Table 1-1 summarizes the topic coverage. The appendix presents the criteria used in selecting indicators, explains the benchmarking methodology, and provides a table showing the full set of indicators examined for this report.

Table 1
Topic Coverage

Overview of the Economy	Private Sector Enabling Environment	Pro-Poor Growth Environment
<ul style="list-style-type: none"> • Growth Performance • Poverty and Inequality • Economic Structure • Demographic and Environmental Conditions • Gender 	<ul style="list-style-type: none"> • Fiscal and Monetary Policy • Business Environment • Financial sector • External sector • Economic Infrastructure • Science and Technology 	<ul style="list-style-type: none"> • Health • Education • Employment and Workforce • Agriculture

⁴ A comprehensive poverty reduction strategy also requires programs to reduce the *vulnerability* of the poor to natural and economic shocks. This aspect is not covered in the template since the focus is economic growth programs. In addition, it is difficult to find meaningful and readily available indicators of vulnerability to use in the template.

2. Overview of the Economy

This section reviews basic information on the Kyrgyz Republic's macroeconomic performance, poverty and inequality, economic structure, demographic and environmental conditions, and indicators of gender equity.¹ Some of the indicators cited here are descriptive rather than analytical, and are included to provide context for the performance analysis.

GROWTH PERFORMANCE

Kyrgyz growth performance in 2000–2004 was mixed and unstable. The situation generally improved toward the end of this period after zero growth in 2002. Economic expansion accelerated to 7.0 percent in 2003 and 7.1 percent in 2004. GDP growth in 2004 was exactly the same as in Russia and the low-income former Soviet Republics (hereafter, LI-FSR), higher than in Bulgaria (5.7 percent), but lower than in Romania (8.3 percent) (Figure 2-1). In 2000–2004, GDP increased 5.0 percent per year on average—a moderate rate, below the range predicted by the GDP regression. In the same period, real GDP growth was lower than in any other country of the Commonwealth of Independent States (CIS).

Economic expansion in the Kyrgyz Republic benefited from rising productivity and employment, although productivity growth was only 2.0 percent per year in 1999–2003. Productivity growth accelerated toward the end of this period, climbing 4.3 percent in 2003 but was still slightly less than in LI-FSR countries (4.9 percent), Bulgaria (4.7 percent), and Romania (4.7 percent), and lagged far behind Russia (7.4 percent). Apparently, labor productivity at the end of the period benefited from a surge in fixed investment in 1999–2000. In 2001–2003, investment contracted in absolute terms and relative to GDP; by 2003, it fell to 15.3 percent of GDP, below the range predicted by the regression, the LI-FSR average (16.1 percent), as well as the shares for Bulgaria (19.6 percent), Romania (22.5 percent), and Russia (18.2 percent) (Figure 2-2). According to the IMF's 2004 Article IV consultation, labor productivity growth in the Kyrgyz Republic benefited from improved capacity utilization, a trend observed in many transition countries.²

¹ The separate Data Supplement provides a full tabulation of the data for Kyrgyz Republic and the international benchmarks, including indicators not discussed in the text, as well as technical notes for each indicator.

² IMF, "Kyrgyz Republic: Article IV Consultation," Country Report No. 05/47, February 2005.

Figure 2-1. Real GDP Growth

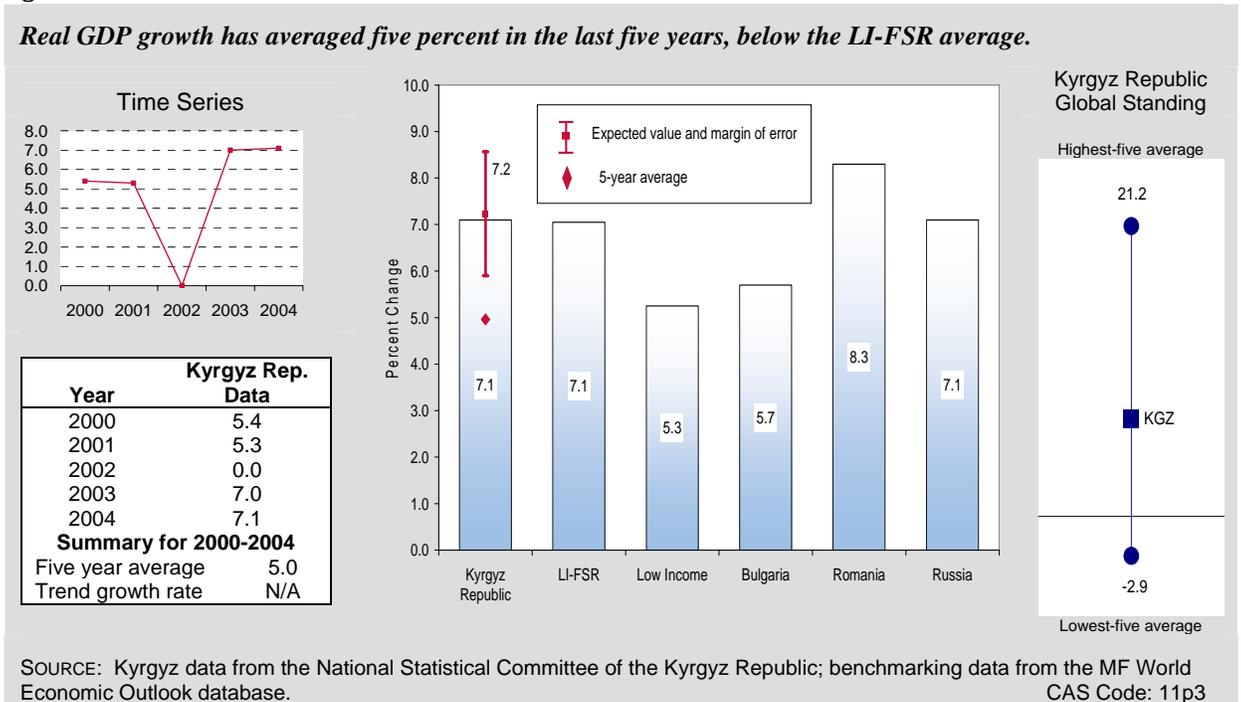
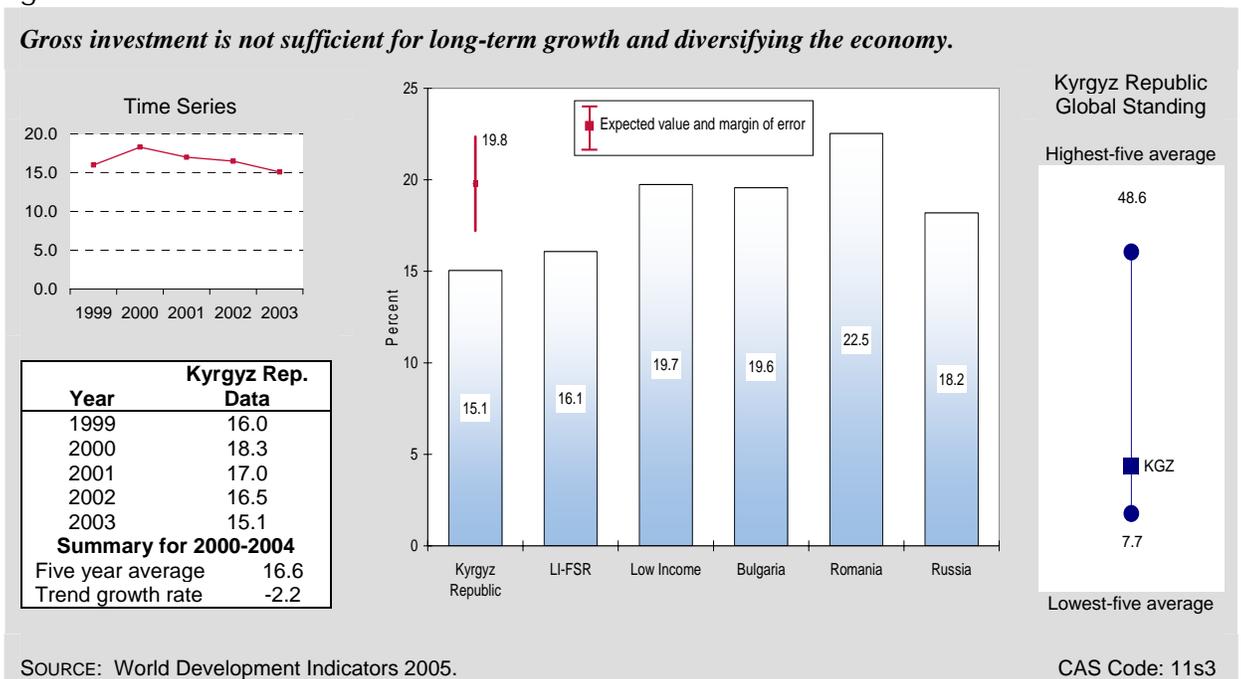


Figure 2-2. Gross Fixed Investment as Percent of GDP



Gold production dominates Kyrgyz industry and exports; the Kumtor gold field is among the world's largest. Fluctuations in gold production have a major impact on the GDP. For example, GDP remained unchanged in 2002 because of a fall in the gold sector; if Kumtor operations were excluded from national account calculations, GDP would have risen by 3.1 percent.³

Measured in current U.S. dollars, per capita GDP increased 55.6 percent from 2000 through 2004, reaching \$433, slightly exceeding the averages of low-income (LI) countries (\$419) and the LI-FSR countries (\$400). At the same time, per capita GDP was much higher in Bulgaria (\$3,074), Romania (\$3,207), and Russia (\$4,903), which are all lower middle-income countries. When measured in terms of PPP, the Kyrgyz Republic's per capita GDP also surpasses the benchmark groups. In 2004, it equaled \$1,933, while in LI and LI-FSR it equaled \$1,850 and \$1,560, respectively. The level of this indicator in the Kyrgyz Republic lagged far behind those in Bulgaria (\$8,500), Romania (\$7,642), and Russia (\$10,180).

Unfortunately the good macroeconomic performance that began emerging in 2003–2004 was not sustained this year, largely because of political turmoil that followed the parliamentary elections of February 2005. According to the National Statistical Committee of the Kyrgyz Republic, GDP contracted 0.4 percent year-over-year in January–September and industrial production plunged 11.7 percent in January–November because gold production was constantly interrupted. Without Kumtor production factored into overall industrial production, industrial output declined 2.9 percent. Agricultural production, freight transportation, and fixed investment also dropped. A marked increase in retail and wholesale trade and, apparently, household consumption, prevented a more substantial decline in GDP.

To advance reform, resume economic growth, and consolidate the gains made in 2003–2004 the Kyrgyz Republic needs political stability. The country should make every effort to diversify away from heavy reliance on gold exports and to promote investment, including foreign direct investment to reduce dependence on foreign aid. Special attention should be paid to job creation in light of rising unemployment.

POVERTY AND INEQUALITY

Poverty indicators have shown signs of improvement in recent years, although the poorest strata of the Kyrgyz population have benefited little. The share of population living below the national poverty line fell by nearly 15 percentage points since 1999, reaching 40.8 percent in 2003, a rate well below the 53.9 percent regression benchmark for a country with the Kyrgyz Republic's characteristics.⁴ In 2004, the rate fell to 35 percent.⁵ The share of the population living on less

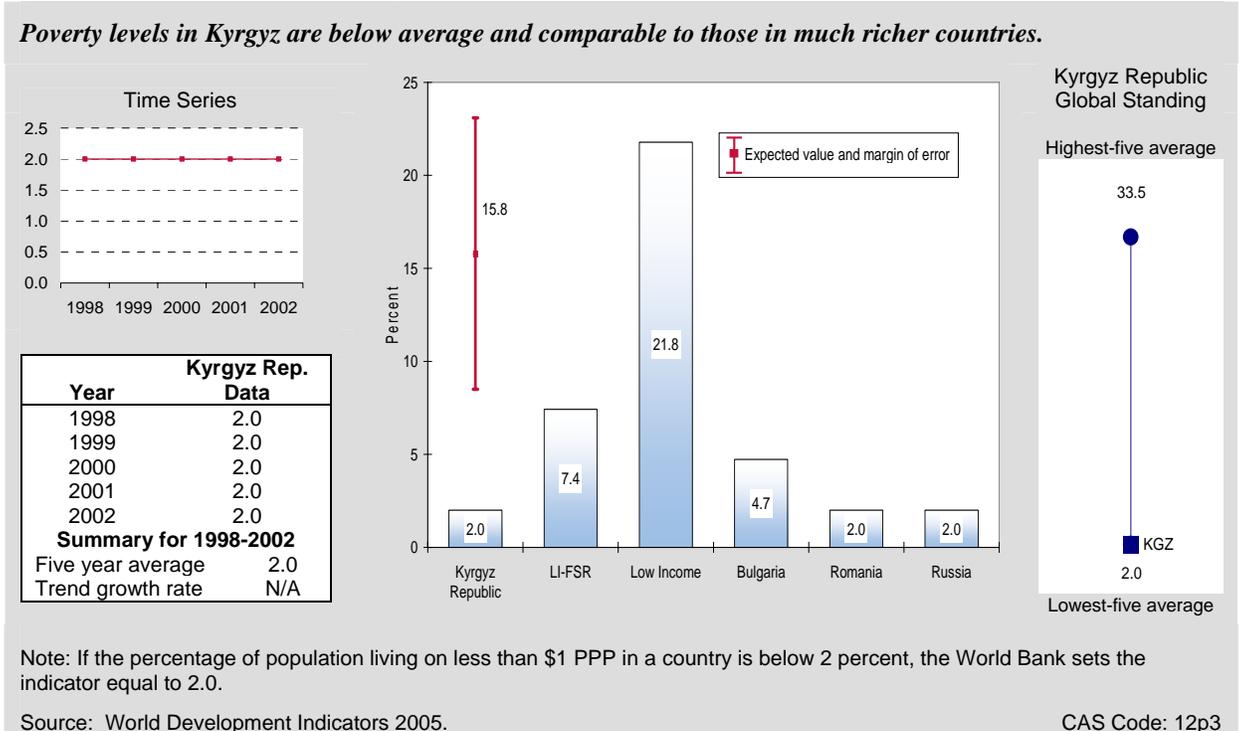
³ Ibid.

⁴ Each country defines its poverty line independently, so rates are not necessarily comparable.

⁵ IMF, "Kyrgyz Republic: Sixth Review under the Three-Year Arrangement under the Poverty Reduction and Growth Facility and Request for the New Three-Year PRGF Arrangement," Country Report No. 05/119, March 2005. Estimates are not yet official.

than \$1 PPP per day is also low by benchmark comparisons⁶ (Figure 2-3). At 2.0 percent, the rate is below the regression benchmark of 15.8 percent and the average rate of 7.4 percent in the LI-FSR region; on par with much richer countries, such as Romania and Russia (both 2.0 percent); and below the rate for Bulgaria (4.7 percent). The share of the population receiving less than the minimum dietary energy consumption is also low—6.0 percent versus the 28.8 percent regression benchmark and the 19.0 percent LI-FSR average.

Figure 2-3. Population Living on Less than \$1 PPP per Day



According to the 2004 PRSP Progress Report, however, extreme poverty remained unchanged over the same period even as the incidence of poverty declined.⁷ In 2002, the poorest 20 percent of the population received 7.7 percent of income; the regression benchmark is 8.4 percent and the average for the LI-FSR region is 7.9 percent. This share is on par with all three comparator countries.

If economic growth is to benefit all population strata, programs aimed at improving the standard of living for the poorest are warranted. Since most Kyrgyz poor live in rural areas,⁸ promoting

⁶ If the percentage of population living on less than \$1 PPP per day is below 2, the World Bank sets the indicator at 2.0.

⁷ IMF, "Kyrgyz Republic: Poverty Reduction Strategy Paper Progress Report," Country Report No. 04/200, July 2004.

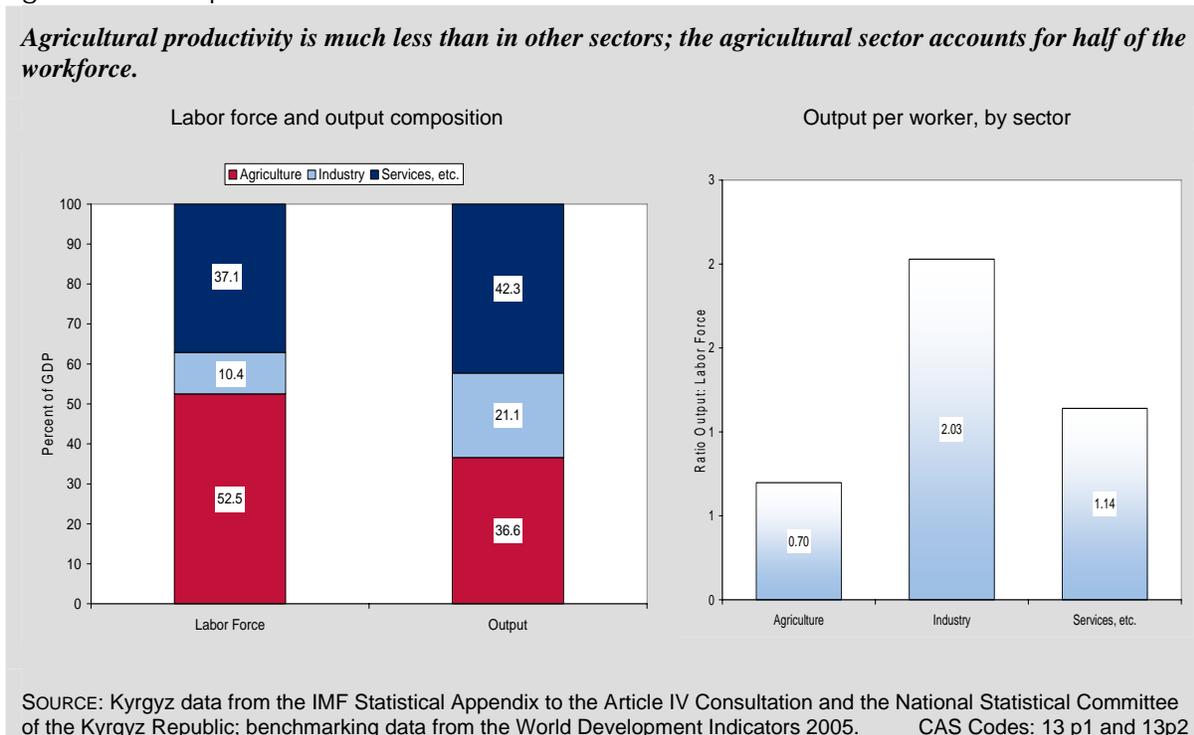
⁸ Ibid.

economic development in those areas, including job creation and nonagricultural small and medium enterprises (SMEs), may be helpful.

ECONOMIC STRUCTURE

The Kyrgyz Republic’s employment structure is similar to that of other LI-FSR countries. In 1999–2003, Kyrgyz industry on average accounted for 10.6 percent of the employed, a little less than the LI-FSR country average of 13.9 percent, but substantially less than in Bulgaria (27.6 percent), Romania (26.2 percent), and Russia (29.4 percent). At the same time, Kyrgyz agriculture accounted for 52.7 percent of the employed and services 36.6 percent; in LI-FSR countries the shares were 51.0 percent and 35.1 percent, respectively. Comparing the ratio of the share of the labor force and of output in agriculture indicates that agriculture is more productive in the Kyrgyz Republic than, on average, in the LI-FSR countries (Figure 2-4). Nevertheless, agriculture is less productive than the rest of the Kyrgyz economy.

Figure 2-4. Output Structure and Labor Force Structure as a Percent of GDP



Overall, SME production comprised 47.9 percent of GDP in 2003, up from 42.7 percent in 2000. This increase, however, masks a decline in the activity of nonagricultural SMEs, which was more than offset by rising output from agricultural SMEs. According to the USAID/Pragma Enterprise Development Project, from 1999 through 2003 employment at nonagricultural SMEs declined by 24.1 percent⁹ and their share of value added dropped from 16.9 percent of GDP in 1999 to 12.6

⁹ Pragma used data provided by the National Statistical Committee of the Kyrgyz Republic.

percent in 2003. Moreover, value-added generated by these nonagricultural enterprises declined in absolute terms. The decline in this share was partially compensated for by an increase in the share of value-added generated by individual entrepreneurs from 10.5 percent to 13.4 percent. At the same time, agricultural SMEs were booming. The contribution of peasant farms and farming enterprises to Kyrgyz GDP rose from 14.6 percent to 21.3 percent.

Gold production is by far the most important industrial sector. According to Interfax, metallurgy, an overwhelming portion of which is gold production, accounted for 50 percent of industrial output in the Kyrgyz Republic in the first eight months of last year.

The large share of employment in Kyrgyz agriculture, while in line with the regional average, is a principal challenge to poverty reduction given the sector's low productivity. Therefore, the Kyrgyz Republic needs to take steps to improve agricultural productivity while shifting employment to nonagricultural sectors.

DEMOGRAPHY AND ENVIRONMENT

The Kyrgyz Republic's population rose 1.0 percent per year on average in 2000–2004, standing out in a region where population is declining or stagnant. According to the United Nations World Population Prospects database, population declined in Bulgaria, Romania, and Russia during the same period.¹⁰ The same source projects that the Kyrgyz population will rise to 6.4 million in 2030, while the populations of Bulgaria, Romania, and Russia will rapidly decline. The Kyrgyz population stood at 5.1 million in 2004.

The age dependency rate in the Kyrgyz Republic dropped from 0.69 dependents per worker in 1999 to 0.61 in 2003 because of a decline in the ratio of children to workers, while the old age dependency rate was stable. The Kyrgyz dependency rate is on par with the LI-FSR average (0.62), but much higher than in Bulgaria (0.44), Romania (0.44), and Russia (0.42) See Figure 2-5. According to UN projections, the age dependency rate will continue to decline in the Kyrgyz Republic, reaching 0.46 in the next 25 years.¹¹ This contrasts favorably with projected dependency rate increases in Bulgaria, Romania, and Russia. The Kyrgyz population will age, but will remain young in absolute terms and relative to populations in comparator countries. The UN expects that the median age in the Kyrgyz Republic will rise from 23.8 years in 2005 to 33.0 years in 2030. While the trends are favorable, an aging population will place a substantial financial burden on the budget, and authorities need to prepare for increased expenditures to care for the elderly.

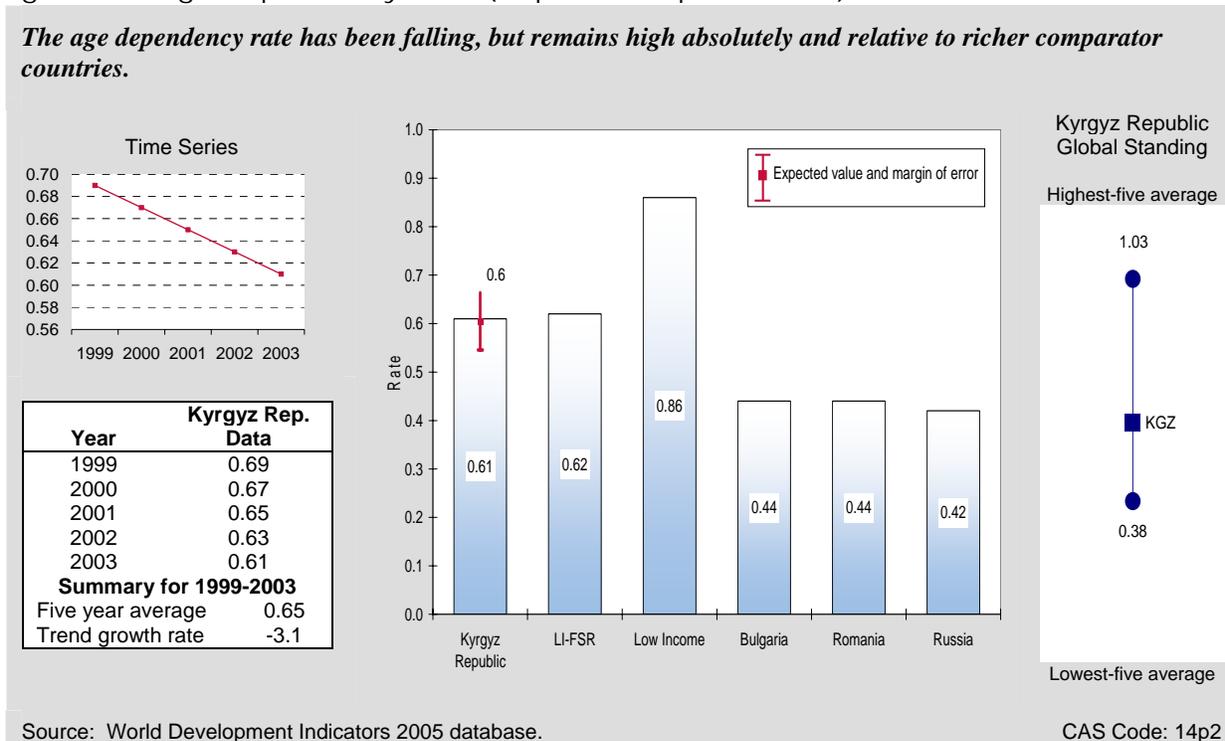
The Kyrgyz adult literacy rate stood at 98.7 percent in 2003, above the range predicted by the benchmark regression and the rates in Bulgaria (98.6 percent) and Romania (97.3 percent). Literacy rates that are close to perfect are common in the former Soviet Union—for Russia and for the LI-FSR countries the latest available figures are 99.6 percent and 99.2 percent, respectively.

¹⁰ United Nations, World Population Prospects database.

¹¹ Ibid.

The Kyrgyz Republic’s score on the Environmental Sustainability Index is 48.4, a little better than the average score of the LI-FSR group (46.9) and of Romania (46.2).¹² At the same time, the higher scores of Bulgaria (50.0) and Russia (56.1) show that improvement is possible. The analysis of index components indicates that the most troubled areas of environmental sustainability in the Kyrgyz Republic are international collaborative efforts, environmental governance, and private sector responsiveness.

Figure 2-5. Age Dependency Rate (Dependents per Worker)



GENDER

Gender indicators for the Kyrgyz Republic point to equity in Kyrgyz society. The share of literate males is only 1 percent higher than that of females (as evidenced by a 1.01 ratio of male to female adult literacy rates in 2003). This ratio is on par with that of the LI-FSR region (1.01), Bulgaria (1.01), Romania (1.02), and Russia (1.00). Equity can also be observed in gross enrollment rates—with 1.01 males enrolled per each female enrolled at all levels of education. Again, performance is on par with the LI-FSR region overall (1.02). In richer countries, such as Bulgaria, Romania, and Russia, more women are enrolled than men as evidenced by ratios below one.

The difference in male and female life expectancy is more of a health than a gender issue. In 2003, the ratio of Kyrgyz male life expectancy to female was just 0.89. Although women are

¹² The Environmental Sustainability Index ranges from 0 (poor performance) to 100 (excellent performance).

expected to live longer than men in general, Kyrgyz male life expectancy of 64.5 years is unacceptably low by absolute measures.

3. Private Sector Enabling Environment

This section reviews indicators related to the enabling environment for rapid and efficient growth in the private sector. Sound fiscal and monetary policies are essential for macroeconomic stability, which is a necessary (though not sufficient) condition for sustained growth. A dynamic market economy also depends on institutional foundations such as secure property rights, an effective system for enforcing contracts, and an efficient regulatory system that does not impose undue barriers on business. Financial institutions play a major role in mobilizing and allocating saving, facilitating transactions, and creating instruments for risk management. An enabling environment also ensures access to the global economy or external sector, an important source of potential markets, modern inputs, technology, and finance, as well as the competitive pressure necessary for efficiency and productivity. Equally important is development of the physical infrastructure to support production and trade. Finally, developing countries need to adapt and apply science and technology to attract efficient investment, boost competitiveness, and stimulate productivity growth.

FISCAL AND MONETARY POLICY ¹⁸

The Kyrgyz Republic has made good progress in reducing its deficit and should continue to do so to achieve fiscal sustainability. The deficit was reduced to 4.2 percent of GDP in 2004. The gap between this deficit and the one percent deficit predicted by the regression benchmark is unfavorable, as is the difference with budget balance figures for comparison countries (a 1.8 percent surplus in Bulgaria, a 2.3 percent deficit in Romania, and a 2.2 percent surplus in Russia).

Government expenditure has remained largely in check over recent years, standing at 27.3 percent of GDP in 2004. This level of expenditure is substantially above that predicted by the

IMF Program Status for Kyrgyz Republic

In October 2005, the Kyrgyz Republic completed its first review under the three-year PRGF arrangement; and the IMF approved a US\$1.8 million disbursement. The executive board commended Kyrgyz authorities for preserving macroeconomic stability despite the difficult political environment.

¹⁸ In 2005, the WDI database adopted a new system for classifying fiscal data, even though most developing countries still use the old classification. The database now has fiscal data for very few developing countries; due to the limited sample size, most of the group averages derived from WDI are not meaningful. In this section, comparisons are based on absolute standards, or benchmarks derived from 2004 WDI data, as well as figures for Bulgaria, Romania, and Russia.

benchmark regression (17.9 percent), indicating government's commitment to providing the social services necessary to reduce poverty and achieve Millennium Development Goals. But the declining share of expenditure on capital, which is essential for long-term growth, is troubling. Expenditure on capital fell from 32 percent in 2000 to 19 percent in 2004, while the share of wages and salaries rose from 20 percent in 2000 to 29 percent in 2004. Another problem is the high public external debt. Even with Paris Club debt relief in 2005 that reduced external debt (discussed in the section on the External Sector), additional fiscal consolidation is needed to reduce debt overhang.¹⁹ To the credit of the government, revenue rose from 17.7 percent of GDP in 2000 to 22.2 percent in 2004, above the regression benchmark of 18.3 percent²⁰ (Figure 3-1). This improvement is largely due to better tax administration.²¹ Nonetheless, revenue is still below that in Romania (29.9 percent) and Russia (27.4 percent).²² Any scheme to revise the tax system to generate more revenue, however, should be done cautiously because high taxes and problems with tax administration are closely linked to the large shadow economy, a major concern of Kyrgyz authorities.²³ Less intrusive taxation could encourage businesses to formalize operations.

In monetary policy, the Government of the Kyrgyz Republic has been able to control inflation, which fell to less than a quarter of its level five years ago²⁴ (Figure 3-2). Inflation of 4.1 percent in 2004 is low by absolute standards and is below all benchmark values—the regression result, the LI-FSR average, and rates in the three comparator countries. Low inflation has occurred in the face of high money supply growth, which averaged 24.1 percent over last 5 years, consistent with steady and rapid remonetization. Low inflation, coupled with strong productivity growth, is necessary to contain labor costs and encourage non-gold exports.²⁵

Additional donor assistance in tax administration and policy could be useful to support further gains in revenue.

BUSINESS ENVIRONMENT

Institutional barriers to doing business, including corruption in government, are critical determinants of private sector development and prospects for sustainable growth. Kyrgyz business environment indicators are mixed, with some notable strengths and weaknesses.

¹⁹ IMF, "Kyrgyz Republic: Sixth Review."

²⁰ IMF preliminary expenditure and revenue figures for Tajikistan indicate little change in 2005, even with the new government taking control. Revenues are estimated at 23.0 percent of GDP, and expenditures at 27.6 percent. IMF, "Kyrgyz Republic: First Review under the Three-Year Arrangement under the Poverty Reduction and Growth Facility," Country Report No. 05/402, November 2005.

²¹ Ibid.

²² Bulgaria's revenue is even higher, 38 percent, but is not used as a benchmark because such high revenue may indicate an intrusive government.

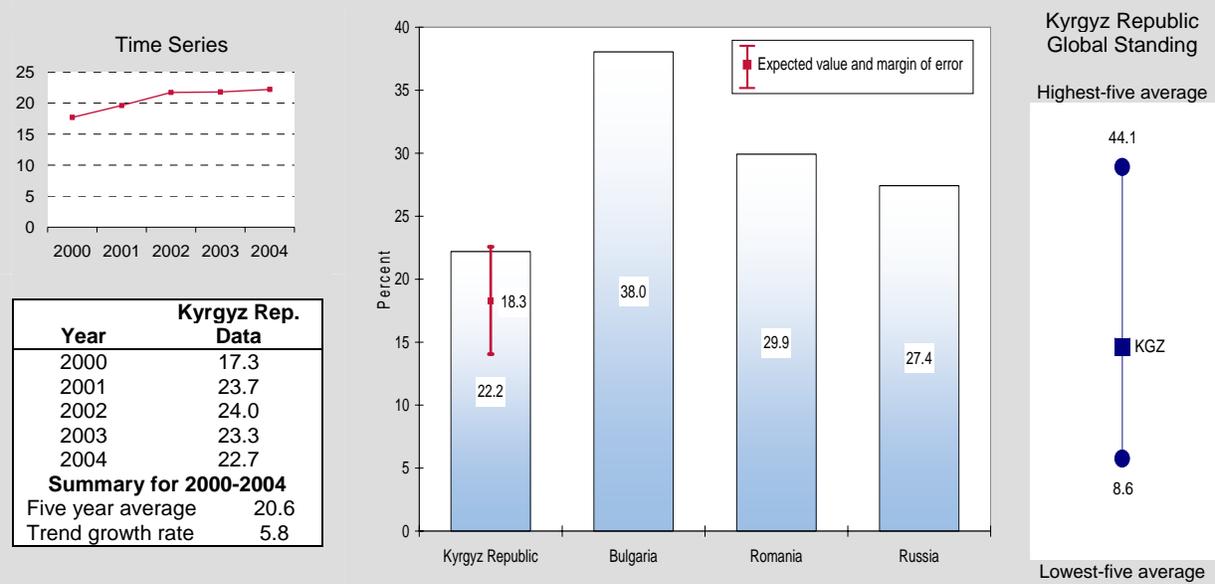
²³ IMF, "Kyrgyz Republic: Sixth Review."

²⁴ Inflation is a Millennium Challenge Account indicator.

²⁵ IMF, "Kyrgyz Republic: Sixth Review."

Figure 3-1. Government Revenue as Percent of GDP

Kyrgyz government revenue needs to keep rising to ensure that provision of necessary public services is fiscally sustainable.

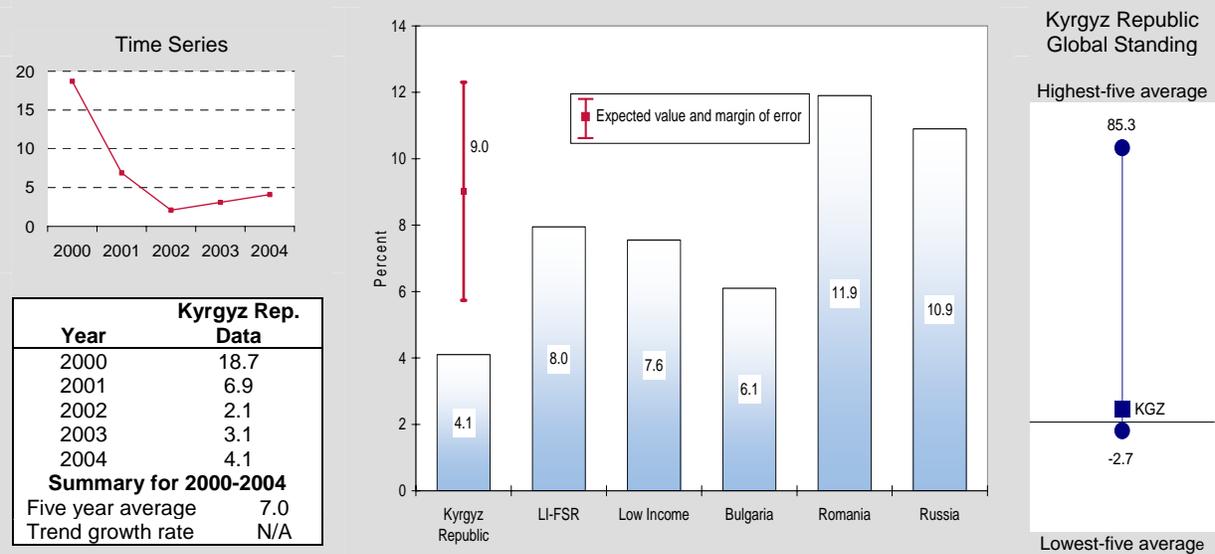


Note: LI and LI-FSR averages are not calculated because the World Development Indicators database adopted a new system for classifying fiscal data in 2005.

SOURCE: Kyrgyz data from the IMF's Sixth Review under the Three-Year Arrangement under the PRGF; benchmarking data from the respective IMF Article IV Consultations for comparator countries. CAS Code: 21p2

Figure 3-2. Inflation Rate

Inflation has fallen from double-digit levels and is evidence of sound monetary policy.

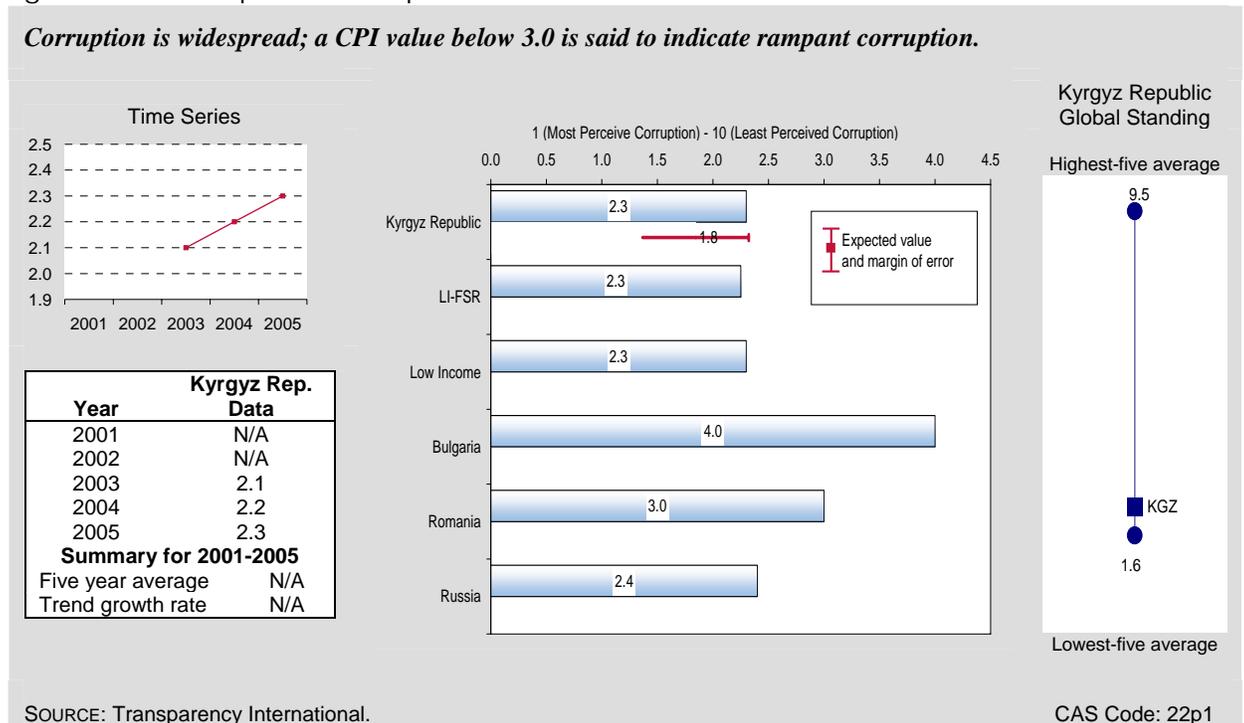


Source: World Economic Outlook database.

CAS Code: 21p4

Corruption in the Kyrgyz Republic is widespread and is a major impediment to doing business (Figure 3-3). Although on par with the income-regional group index and the range of values predicted by the regression, the Kyrgyz Republic's score on the Corruption Perception Index of 2.3 is below Bulgaria's score of 4.0, Romania's score of 3.0 and even Russia's score of 2.4.²⁶ More important, it is high in absolute terms; any value below 3.0 is said to indicate rampant corruption. Improvement may be slight—the index rose from 2.1 over three years—but evidence suggests that most of the government's attempts to counter corruption have been ineffective and need to be reassessed, intensified, or both.²⁷ Mr. Bakiev, the new president, announced that fighting corruption is among the government's top priorities.²⁸

Figure 3-3. Corruption Perception Index



The Kyrgyz Republic's ranking in the Ease of Doing Business index (84 out of 155 countries) is better than the average ranking for the region (111), but worse than that of the comparator countries (Bulgaria 62, Romania 78, Russia 75). An examination of index components reveals clear weaknesses and strengths. Starting a business in the Kyrgyz Republic requires relatively few procedures and relatively little time, and the cost of starting a business (10.4 percent of GNI per capita) is below the average for LI-FSR (17.0 percent).²⁹ The cost declined from 11.6 percent just

²⁶ Corruption Perception Index values range from 1 (most perceived) to 10 (least perceived).

²⁷ IMF, "Kyrgyz Republic: Poverty Reduction Strategy Paper Progress Report," Country Report No. 04/200, July 2004.

²⁸ IMF, "Kyrgyz Republic: First Review under the Three-Year Arrangement under the Poverty Reduction Growth Facility," Country Report No. 05/402, November 2005.

²⁹ This is a Millennium Challenge Account indicator.

the year before, so the country is beginning to close the gap with the rate in Bulgaria (9.6 percent), and heading toward the cost seen in Romania and Russia, at 5.3 and 5.0 percent, respectively. But enforcing a contract takes 492 days and 46 procedures, which is well above all benchmarks.

The Kyrgyz Republic's score of -0.1 on the Regulatory Quality Index is identical to Romania's and better than the LI-FSR average of -0.8 and Russia's of -0.5.³⁰ The absolute maximum of 2.5 and Bulgaria's score of 0.6 leave plenty of room for improvement. Similarly, its score on the Rule of Law Index³¹ is on par with the LI-FSR score (-1.0 versus -1.1), but needs to rise at least to the levels observed in the three comparator countries (0.1 in Bulgaria, -0.2 in Romania, and -0.7 in Russia).³²

The EBRD Transitions Indicators identified the Kyrgyz Republic as the most progressive structural reformer of CIS countries in 2004.³³ But the country must continue to improve its business environment, especially to overcome the disadvantage of distance from key markets and of trade restrictions imposed by neighboring countries. Programs that reduce corruption, enhance the regulatory regime, and improve fairness and consistency in enforcing legal rights are top priorities.

FINANCIAL SECTOR

A sound and efficient financial sector mobilizes savings, fosters productive investment, and improves risk management. Although still weak, the Kyrgyz financial sector has experienced notable and substantial improvements in recent years.

Rapid monetization of the Kyrgyz economy indicates rising confidence in the banking sector; money supply as a share of GDP rose from 11.3 percent in 2000 to 20.1 percent in 2004 (see Figure 3-4). Currently, monetization is on par with Romania's rate (22.1 percent) and higher than the average for LI-FSR (15.4 percent).³⁴ Monetization is expected to continue, although at a slower pace,³⁵ perhaps reaching the levels of Russia (25.7 percent) and eventually Bulgaria (44.6 percent).

Increasing credit to the private sector is another recent accomplishment (see Figure 3-5). Domestic credit to the private sector rose from 4.2 percent of GDP in 2000 to 6.9 percent of GDP in 2004. Despite the recent rise, credit is still substantially lower than the LI-FSR average (14.0

³⁰ Regulatory Quality Index values range from -2.5 (poor performance) to 2.5 (excellent performance).

³¹ This is a Millennium Challenge Account indicator.

³² Rule of Law Index values range from -2.5 (poor performance) to 2.5 (excellent performance).

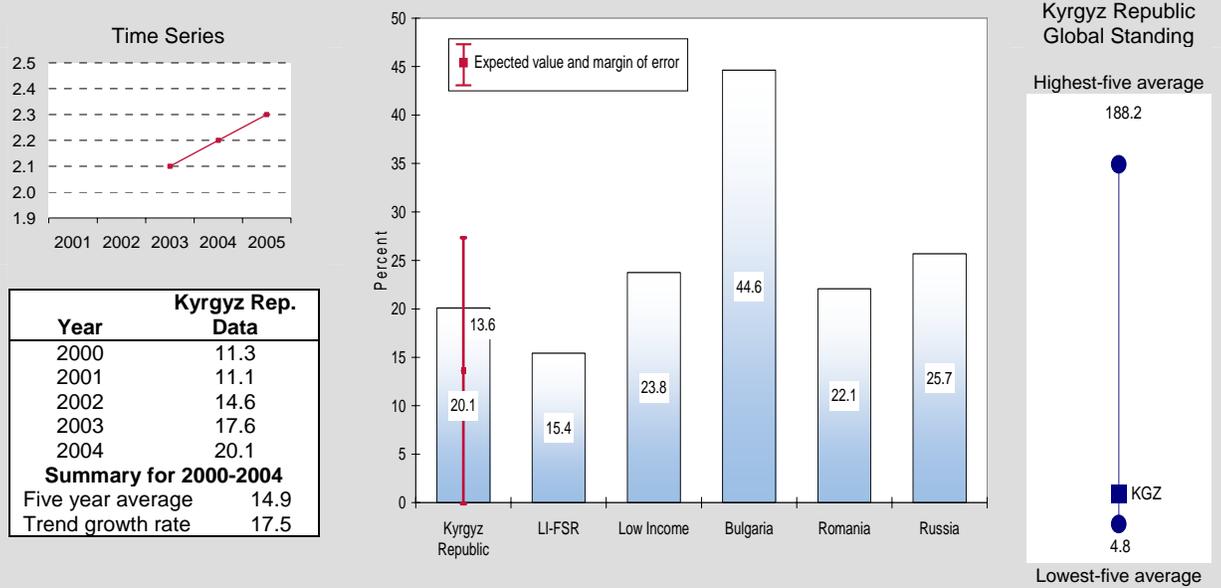
³³ Although the EBRD Transition Index is not a standard indicator for this series of reports, transitional process is an important determinant for growth of any post-Soviet economy.

³⁴ Money supply ratio to GDP is not compared here to the regression benchmark because of high standard errors that render comparisons statistically invalid.

³⁵ IMF, "Kyrgyz Republic: 2004 Article IV Consultation and Request to Extend the PRGF Arrangement," Country Report No. 05/47, February 2005.

Figure 3-4. Money Supply (M2) Perception of GDP

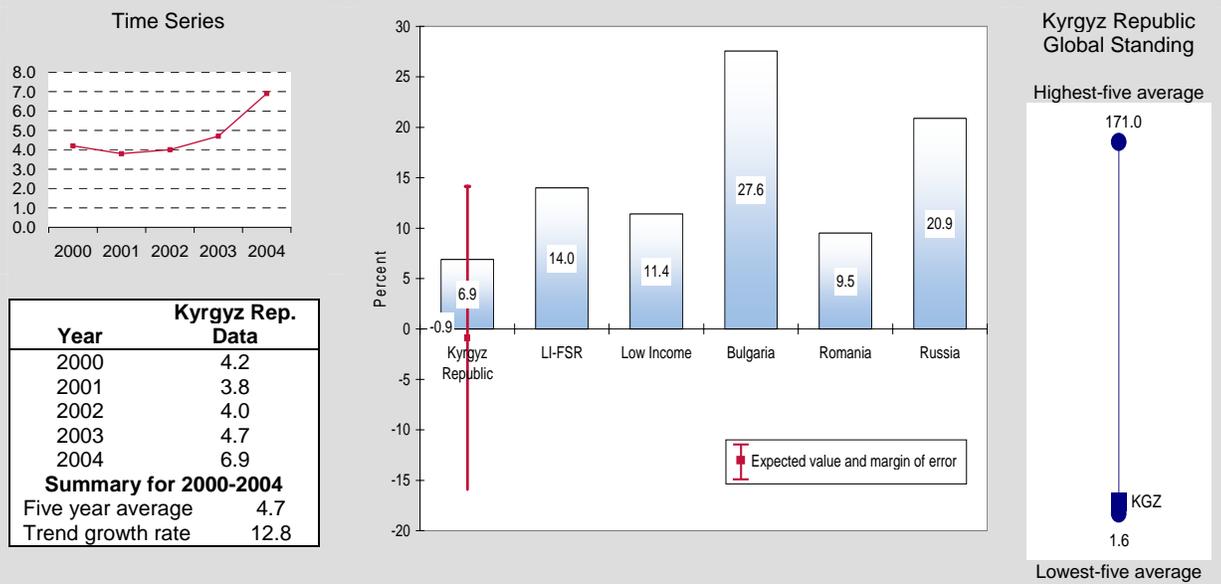
Steady and rapid remonetization is a major macroeconomic achievement and signals confidence.



SOURCE: Kyrgyz data from the IMF Sixth Review under the Three-Year Arrangement under the PRGF; benchmarking data from the World Development Indicators 2005. CAS Code: 23p3

Figure 3-5. Domestic Credit to Private Sector as Percent of GDP

Credit to the private sector has been rising recently, but remains well below all benchmarks.



Source: Kyrgyz data from IMF Sixth Review under the Three-Year Arrangement under the PRGF; benchmarking data from World Development Indicators 2005. CAS Code: 23p1

percent) and very far from the rates for all three comparator countries (Bulgaria 27.6 percent, Romania 9.5 percent, and Russia 20.9 percent).³⁶ On a positive note, the IMF projects credit to rise to 11.5 percent in 2007.³⁷ In light of this growth, authorities may need to attend to the quality of bank supervision and regulatory framework for the financial system as a whole to guard against banks expanding loan portfolios without adequate monitoring of risk.

Rising credit has been accompanied by greater efficiency, but substantial additional improvement is still needed. For example, the interest rate spread, a measure of banking sector efficiency, declined but is still high. Falling from 25.3 percent in 1999, it stood at 14.2 percent in 2003, above the regression benchmark for a country with the Kyrgyz Republic's characteristics (11.5 percent), the LI-FSR average (6.9 percent), Bulgaria's spread (5.9 percent), and Russia's spread (8.5 percent).³⁸ Similarly, the real interest rate declined to 14.8 percent in 2003, but remained high in comparison to the LI-FSR average of 6.1 percent.

A score of 8.0 on the Legal Rights of Borrowers and Lenders Index reflects positively on the Kyrgyz Republic's financial sector.³⁹ The score is well above the LI-FSR average and Bulgaria's score of 6.0, and even higher than Romania's (4.0) and Russia's (3.0).

Despite these respectable improvements, the Kyrgyz financial sector still has a way to go to be considered adequate, especially given low levels of investment. Furthermore, the March revolution has weakened business expectations and forced investors to take a wait-and-see approach.⁴⁰ Close attention to financial market regulation is warranted because of rapid credit growth and dedollarization. Donor programs to assist in bank supervision and to improve efficiency are likely to be helpful.

EXTERNAL SECTOR

Fundamental changes in international commerce and finance, including reduced transport costs, advances in telecommunications technology, and lower policy barriers, have fueled a rapid increase in global integration over the past 25 years. The international flow of goods and services, capital, technology, ideas, and people offers great opportunities for Kyrgyz Republic to boost growth and reduce poverty by stimulating productivity and efficiency, providing access to new markets and ideas, and expanding the range of consumer choice. Globalization also creates new challenges in the need for institutions, policies, and regulations to take full advantage of international markets; develop cost-effective approaches to cope with adjustment costs; and establish systems for monitoring and mitigating the associated risks.

³⁶ Domestic credit to the private sector is not compared here to the regression benchmark due to high standard errors, making any comparison statistically invalid.

³⁷ IMF, "Kyrgyz Republic: Sixth Review."

³⁸ The interest rate spread for Romania is not readily available.

³⁹ The Legal Rights of Borrowers and Lenders Index ranges from 0 (poor performance) to 10 (excellent performance).

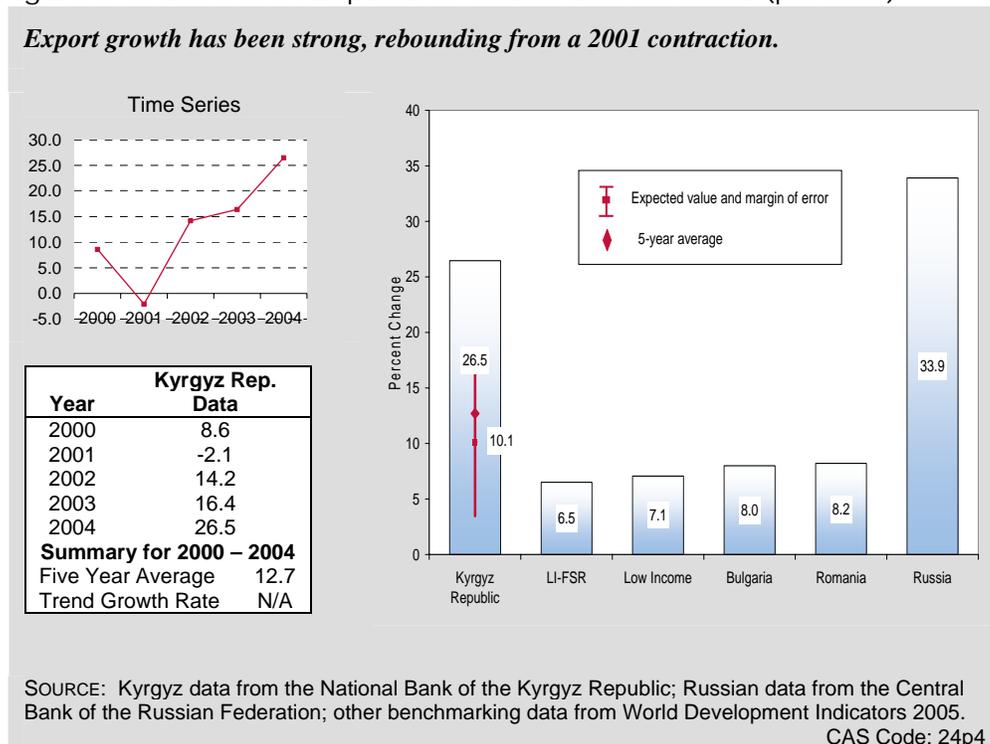
⁴⁰ IMF, "Kyrgyz Republic: First Review under the Three-Year Arrangement under the Poverty Reduction and Growth Facility," Country Report No. 05/402, November 2005.

As the following analysis shows, Kyrgyz external sector developments are mixed. Exports posted strong growth, but were too concentrated in a few commodities, primarily gold. The depletion of gold deposits and decline in gold export revenues may threaten the country's financial stability and impede economic growth. The Kyrgyz Republic is not an attractive destination for foreign investment. Therefore, the country relies heavily on foreign aid and has relied on external borrowing. Debt relief and fiscal reforms have improved the external debt situation but more needs to be done.

International Trade and the Current Account

Kyrgyz foreign trade expanded at a robust pace in 2000–2004. In 2004, exports of goods and services were 78.6 percent higher than in 1999. Exports of precious metals (mostly gold) and stones accounted for 40.5 percent of merchandise exports; exports also grew in other categories, such as food, textiles, and textile products⁴¹ (Figure 3-6). Export growth was especially strong in 2004 (26.4 percent), exceeding the range predicted by the benchmark regression as well as the latest available figures for the LI-FSR region (6.5 percent), Bulgaria (8.0 percent), and Romania (8.2 percent). It lagged behind Russia's export growth (33.9 percent), which was boosted by high world oil prices.

Figure 3-6. Growth in Exports of Goods and Services (percent)



⁴¹ The National Statistical Committee of the Kyrgyz Republic.

Kyrgyz exports are highly concentrated—the top three export commodities account for 60.5 percent of exports, much more than in Bulgaria (17.4 percent) and Romania (24.0 percent), and even more than in Russia (54.3 percent), which also depends heavily on two commodities.

In 2004, Kyrgyz foreign trade volume (exports plus imports) accounted for 94.0 percent of GDP, up from a low of 74.5 percent in 2001.⁴² This high ratio, which is a function of the small size of the economy and large gold exports, is slightly less than the regression benchmark for a country with the Kyrgyz Republic's characteristics (96.1 percent). It is higher than trade-to-GDP ratios in Romania (71.6 percent) and Russia (52.6 percent), but lower than, on average, in the LI-FSR group (109.8 percent) and in Bulgaria (116.2 percent), the smallest of the three comparator countries.

Export diversification, which is clearly necessary, will require investment and a better foreign trade environment. In 2000–2004, the Kyrgyz Republic scored 4.0 on the Trade Policy Index.⁴³ Although the same as Bulgaria's and Romania's, the score was not as good as Russia's (3.0) or the LI-FSR group's (3.5).

Despite rising exports, the country's foreign trade balance was in deficit over the 2000–2004 period because foreign aid and strong domestic demand stimulated imports. In 2004 the deficit was 8.8 percent of GDP, up from 6.1 percent in 2000. Nevertheless, because of a 140 percent increase in current transfers, the current account deficit shrank from 5.7 percent of GDP to 3.4 percent from 2000 to 2004 (Figure 3-7), below the range predicted by the benchmark regression and less than the deficits in Bulgaria (8.4 percent) and Romania (5.8 percent). At the same time, it exceeded the average deficit in the LI-FSR countries (2.0 percent of GDP). Russia ran an 8.3 percent current account surplus in 2003.

International Financing and External Debt

The Kyrgyz Republic still relies heavily on foreign aid. Although the share of aid in GNI shrank from 24.1 percent in 1999 to 10.7 percent in 2003, it exceeded the average aid-to-GNI ratio in LI-FSR countries (7.5 percent) (Figure 3-8). The ratio is also several times higher than those for Bulgaria (2.1 percent), Romania (1.1 percent), and Russia (0.3 percent).

Current private transfers are another significant source of foreign financing and are becoming increasingly important. According to balance of payments statistics provided by the IMF,⁴⁴ net current private transfers increased from \$20.4 million in 2000 to \$94.6 million in 2003, or from 4.0 percent of merchandise exports to 16.0 percent. It is likely, however, that the actual amount of private transfers was much more substantial than what the balance of payments shows, as has been the case in several other former Soviet countries.

⁴² The National Bank of the Kyrgyz Republic.

⁴³ The Trade Policy Index ranges from 1 (for excellent) to 5 (for poor). The index is a Millennium Challenge Account indicator.

⁴⁴ IMF, "Kyrgyz Republic: Statistical Appendix," Country Report No. 05/31, February 2005.

Figure 3-7. Current Account Balance as a Percent of GDP

The current account deficit has been reduced and needs to decline further given high external debt.

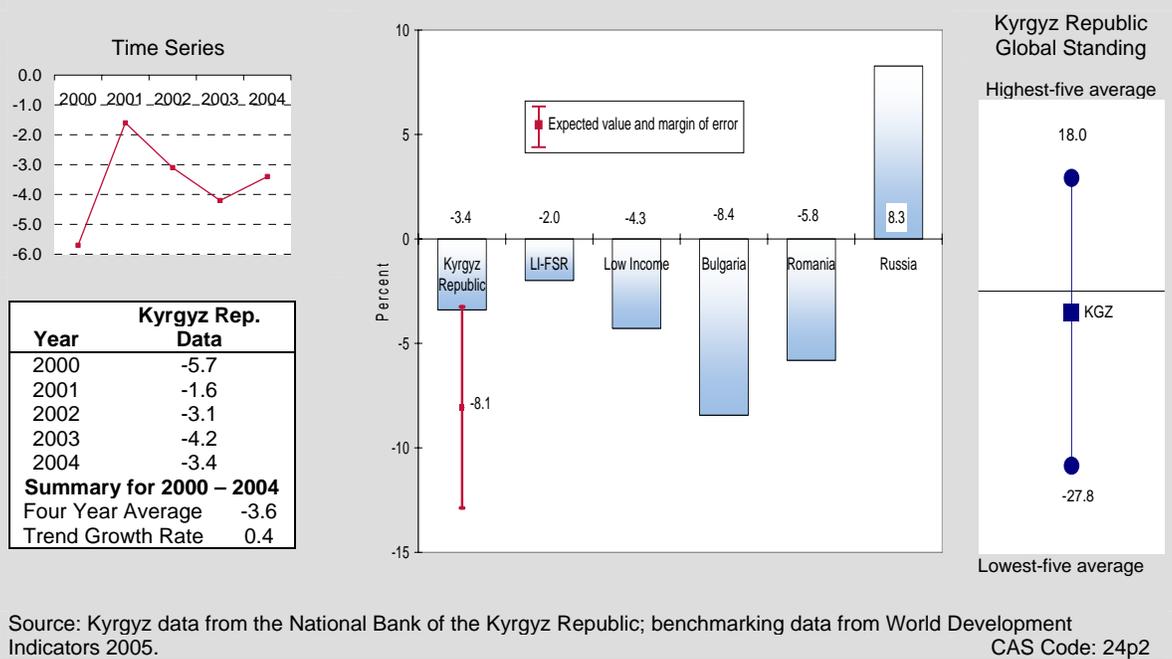
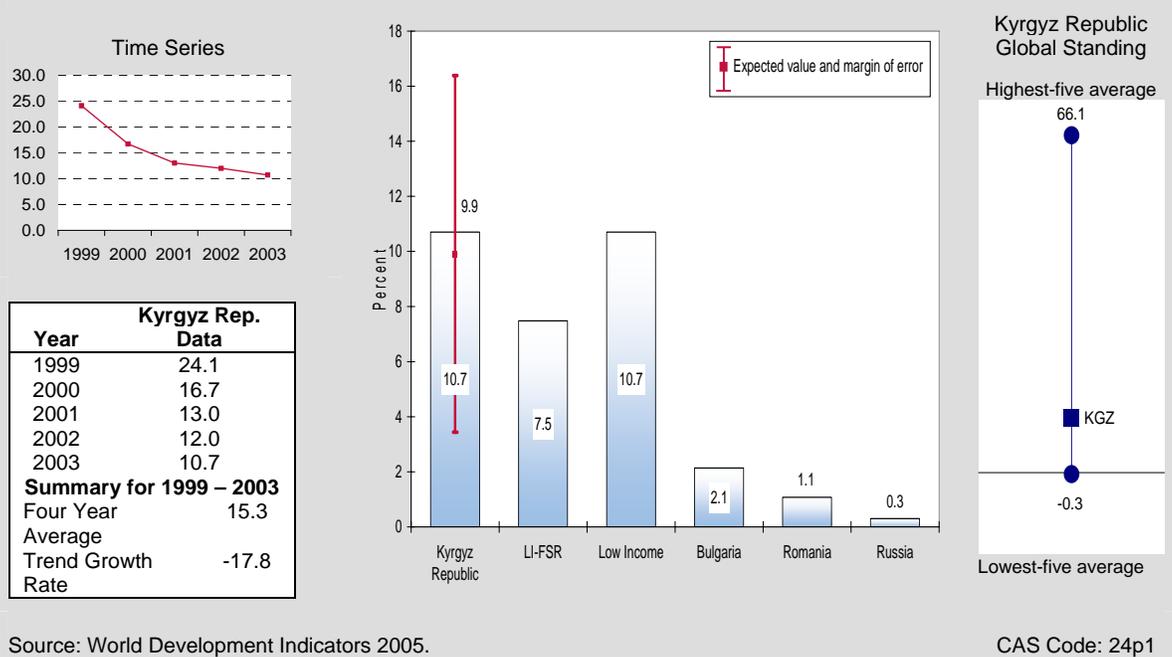


Figure 3-8. Foreign Aid as a Percent of GNI

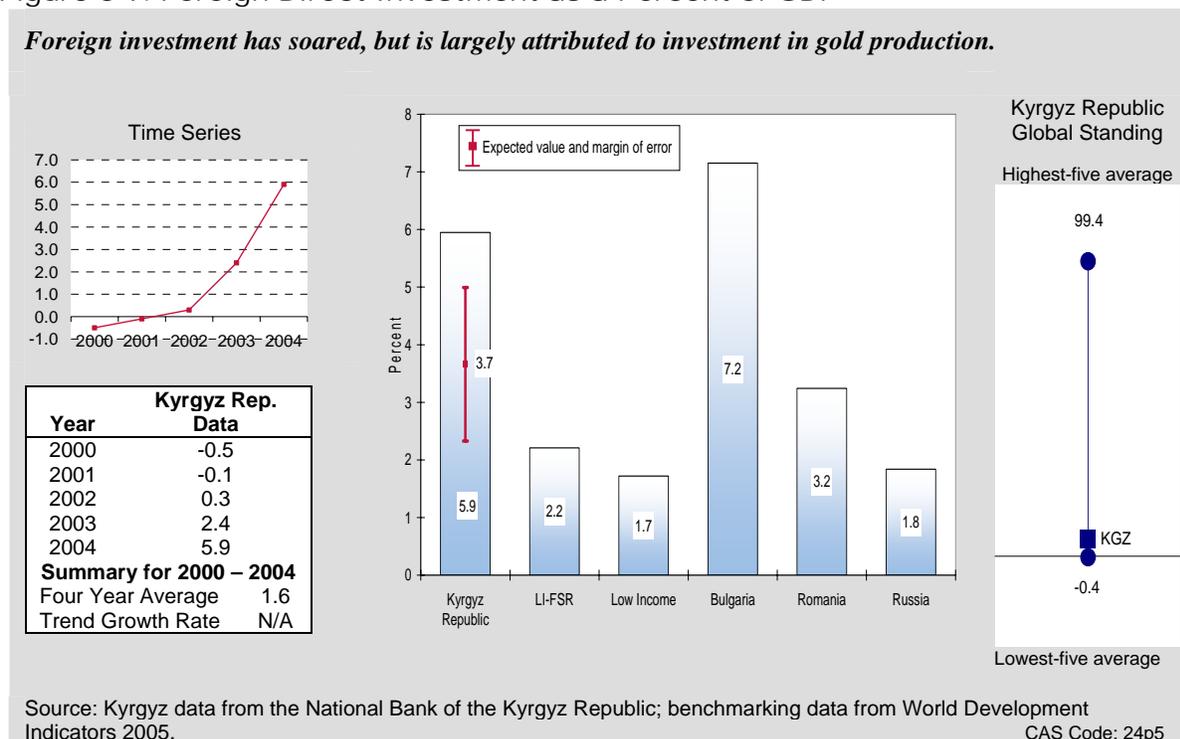
The foreign aid to GDP ratio has declined but remains above regional averages.



Kyrgyz economic development has also been financed through foreign borrowing. The present value of debt declined from 104.6 percent of GNI in 2000 to a still extremely high 97.9 percent in 2003. This was above the range predicted by the benchmark regression, the average present value of debt in the LI-FSR group (86.1 percent), and the debt present value-to-GNI ratios in Bulgaria (85.5 percent), Romania (46.0 percent), and Russia (52.1 percent). Not surprisingly, the average annual debt service ratio—23.6 percent of exports in 1999-2003—also substantially exceeded the benchmark indicators. On a positive note, in March 2005 the Paris Club of creditor nations granted the Kyrgyz Republic relief equivalent to a 35 percent reduction of the net present value of bilateral official debt.⁴⁵ This relief has substantially reduced the country’s debt-to-exports ratio.

Foreign direct investment (FDI) in the Kyrgyz Republic in 2000–2004 averaged a mere 1.6 percent of GDP per year. This is in accord with the country’s low score (0.12) on the 2002 Inward FDI Potential Index, which measures the attractiveness of an economy to foreign investors.⁴⁶ At the same time, this area is experiencing a positive trend: by 2004, FDI rose to 5.9 percent of GDP,⁴⁷ exceeding the range predicted by the regression benchmark, the LI-FSR average (2.2 percent), and even the Romanian and Russian FDI-to-GDP ratios (3.2 percent and 1.9 percent, respectively) (Figure 3-9). Nevertheless, it was still less than in Bulgaria (7.2 percent).

Figure 3-9. Foreign Direct Investment as a Percent of GDP



⁴⁵ IMF, "Kyrgyz Republic: Letter of Intent, Memorandum of Economic and Financial Policies and Technical Memorandum of Understanding," October 7, 2005.

⁴⁶ The Inward FDI Potential Index ranges from 0 (very poor performance) to 1 (excellent performance).

⁴⁷ Largely, however, this increase can be attributed to investment in gold production.

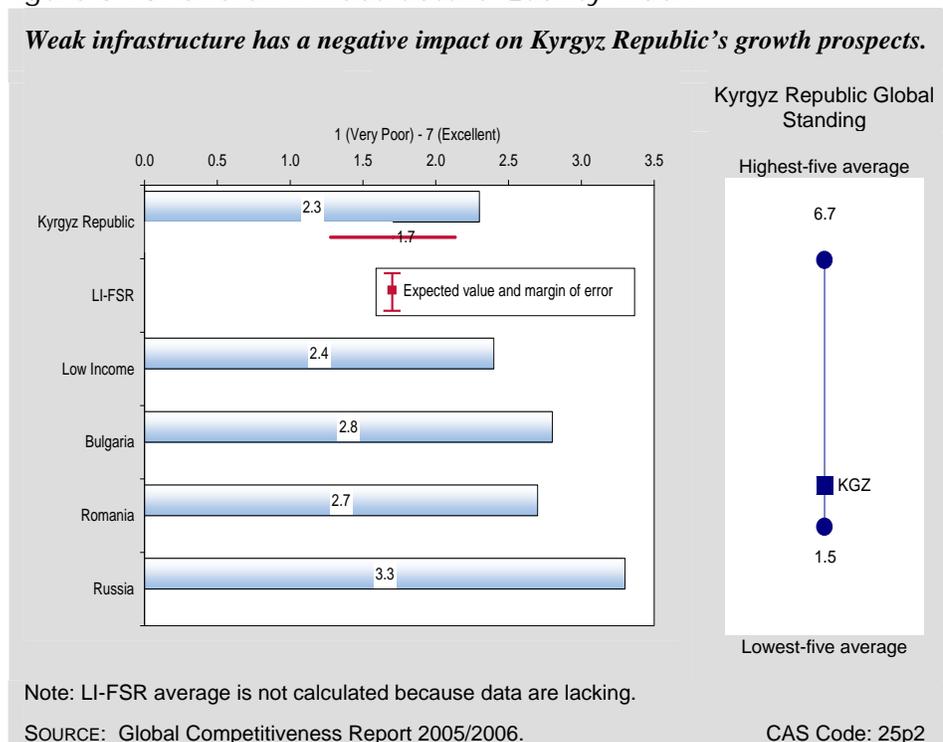
The Kyrgyz central bank's foreign exchange reserves rose from 4.2 months of imports in 2000 to 6.0 months in 2004, a level normally considered sufficient to protect the stability of a country's currency. This level well exceeded the range predicted by the benchmark regression, average reserves in LI-FSR group (2.0 months), as well as reserves in Romania (4.3 months). Kyrgyz reserves, however, fell short of reserves in Bulgaria (6.2 months) and Russia (7.4 months).

The Kyrgyz Republic needs to diversify the commodity structure of exports, especially given the rapid depletion of the Kumtor gold field. It also needs to build on the debt relief granted by the Paris Club and further improve its external financial position. Making the country more attractive to foreign investors by stabilizing the political situation and improving the business environment will do much to improve the external financial position.

ECONOMIC INFRASTRUCTURE

Physical infrastructure for transportation, communications, power, and information technology is the basis for strengthening competitiveness and expanding productive capacity. The level of infrastructure development in the Kyrgyz Republic is quite low by absolute standards. Its score on the Infrastructure Quality Index for 2005 was 2.3, above that predicted by the benchmark regression, but marginally less than the LI average of 2.4 (Figure 3-10).⁴⁸ Bulgaria scored 2.8, Romania 2.7, and Russia 3.3. Judging by the index components, port and railroad development are especially poor.

Figure 3-10. Overall Infrastructure Quality Index



⁴⁸ The Infrastructure Quality Index ranges from 1 (poor) to 7 (excellent).

According to selected indicators, the Kyrgyz Republic has made significant progress in developing its communications sector and is doing better than the LI-FSR region. In 2003, telephone density, measured as the number of fixed line and mobile subscribers per 1,000 inhabitants, was 102.7 in the former versus 91.1 in the latter. At the same time, the costs of an average local call were relatively high and Kyrgyz telephone density was well below that of Romania (523.6 subscribers), Russia (362.3), and Bulgaria (846.9). A similar situation is found with the number of Internet users per 1,000 people.

The Kyrgyz Republic may benefit from international donor support in upgrading and extending transportation routes, especially railroads, and in accelerating the growth of communications.

SCIENCE AND TECHNOLOGY

Science and technology are central elements of a dynamic growth process, because technical knowledge is a driving force of rising productivity and competitiveness. Even for low-income countries like the Kyrgyz Republic, transformational development increasingly depends on acquiring and adapting technology from the global economy, and applying it in ways that are appropriate to their level of development. A lack of capacity to access and utilize technology prevents an economy from leveraging the benefits of globalization.

Unfortunately, reliable international indicators for science and technology are not readily available for the Kyrgyz Republic. The data that are available indicate that science and technology in the country are not developed. The average number of patent applications filed in 1998–2002 (91.6) was low compared to the LI-FSR regional average (181.5), to Bulgaria (306), and to Romania (1,486). In Russia, 20,049 applications were filed. The Kyrgyz government's spending on R&D was insignificant, averaging 0.18 percent of GDP in 1998–2002. Although on par with the LI-FSR regional average of 0.2 percent of GDP, this share was less than in Bulgaria (0.5 percent), Romania (0.4 percent), and Russia (1.3 percent). Foreign investment is not very helpful in the development of technology in the Kyrgyz Republic either. The Kyrgyz Republic scored 3.5 on the FDI Technology Transfer Index in 2005, below the LI average score of 4.4, and the scores of Bulgaria (4.4), Romania (5.1), and Russia (4.0).⁴⁹

⁴⁹ The FDI Technology Transfer Index ranges from 1 (FDI brings little new technology) to 7 (FDI brings a lot of new technology). The LI-FSR average is not computed because of a lack of data.

4. Pro-Poor Growth Environment

Rapid growth is the most powerful and dependable instrument for poverty reduction, yet the link between growth and poverty reduction is not mechanical. In some cases, income growth in poor households exceeds the overall rise in per capita income; in others growth benefits the non-poor far more. A pro-poor growth environment stems from policies and institutions that improve opportunities and capabilities for the poor, while reducing their vulnerabilities. Pro-poor growth is associated with improvements in primary health and education, the creation of jobs and income opportunities, skill development, micro-finance, agricultural development (for countries like Kyrgyz Republic with large populations of rural poor), and gender equity.⁵⁰ This section focuses on health, education, employment and the workforce, and agricultural development.

HEALTH

The provision of basic health service is a major form of human capital investment, and a significant determinant of growth and poverty reduction. Although the EGAT bureau does not provide health programs, an understanding of health conditions can influence the design of economic growth programs.

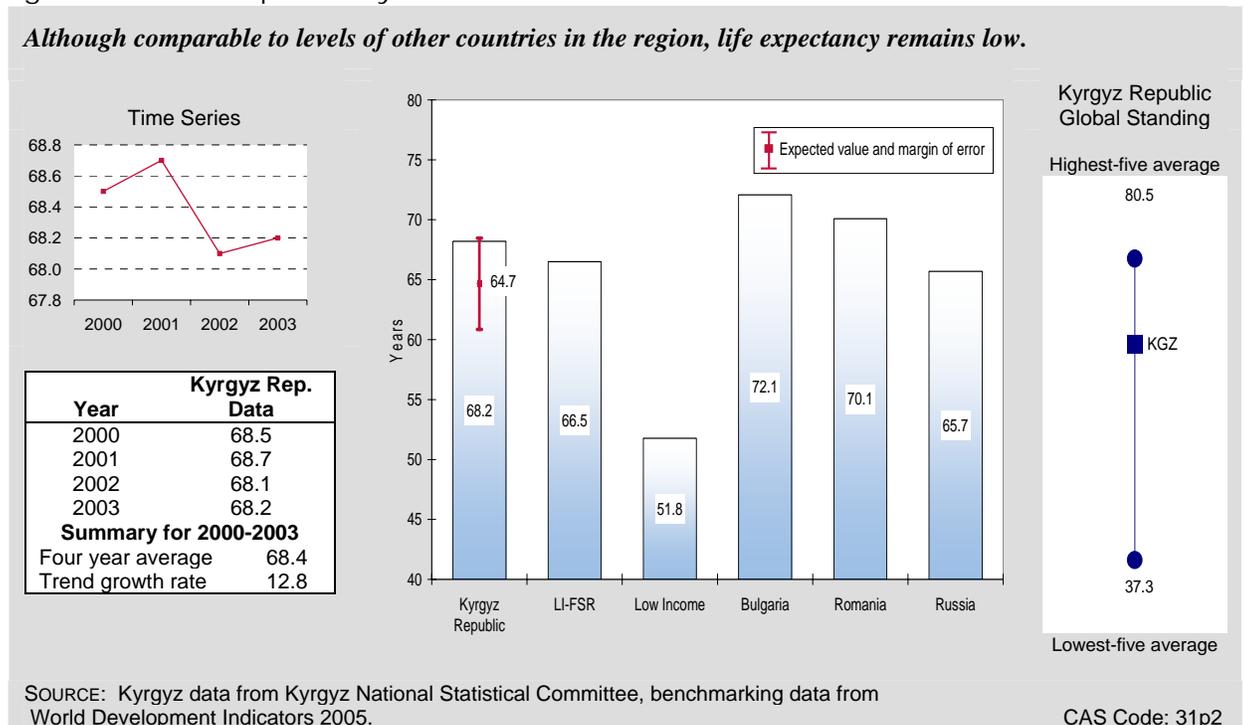
By regional norms, the health of the Kyrgyz population is good but could stand improvement, especially when compared to richer countries such as Bulgaria, Romania, and Russia (see Figure 4-1). Life expectancy, the broadest indicator of health status, was 68.2 years in the Kyrgyz Republic in 2003. Although above the regression benchmark for a country with the Kyrgyz Republic's characteristics (64.7 years) and the average for the LI-FSR region (66.5 years), life expectancy has stagnated in recent years. It is lower than in Bulgaria (72.1 years) and Romania (70.1 years), and higher than in Russia (65.7 years)—not necessarily an exemplar performer. The maternal mortality rate is low by regional standards: 51 deaths per 100,000 births in the Kyrgyz Republic versus 68 on average for LI-FSR and 67 for Russia. As with life expectancy, it is worse than the rates of Romania (49) and Bulgaria (32), indicating the potential for progress.

Secondary indicators help explain why health performance is adequate by regional norms, but inferior when compared to countries the Kyrgyz Republic aspires to catch up with. For example, access to improved sanitation (60.0 percent in 2002) is on par with the LI-FSR average (58.5) and

⁵⁰ Since this report focuses on economic growth performance, it does not cover emergency relief.

higher than in Romania (51.0 percent), but has ample room to grow to reach the rates of Bulgaria (100.0 percent) and Russia (87.0 percent). Access to improved water sources is low even by regional norms (76.0 percent versus 82.5 percent on average for LI-FSR), and lower in comparison to Bulgaria (100.0 percent) and Russia (98.0 percent), albeit higher than the rate of Romania (57.0 percent). At 2.1 percent of GDP, the government's spending on health is too low to have a substantial positive impact, and is below the LI-FSR regional average of 2.4 percent and well below rates in Bulgaria (4.5), Romania (4.2), and Russia (3.5).

Figure 4-1. Life Expectancy



The HIV/AIDS rate is only 0.1 percent, but warrants attention. According to the World Bank, the rates of growth in the number of HIV infections across Central Asia are among the highest in the world; without concerted action, an epidemic is likely, as has been observed in Russia, Ukraine, and Moldova. In addition to the human costs, the economic costs of an epidemic could be significant. The spread of HIV/AIDS, absent intervention, could reduce the Kyrgyz Republic's GDP by 1.4–2.4 percent by 2010 and 2.3–8.4 percent by 2020.⁵¹ Recognizing the danger, the government is open to reform and is the leader in Central Asia in taking early action.⁵²

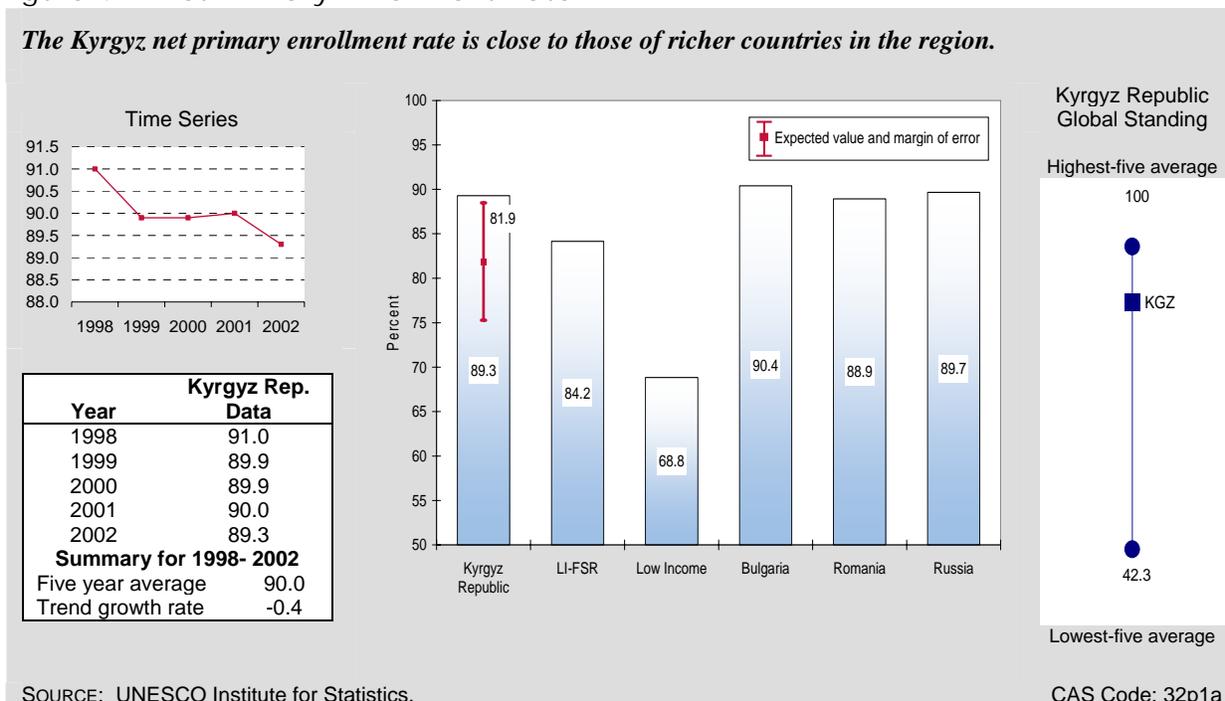
⁵¹ Godinho, Joana, *et al.*, "Reversing the Tide: Priorities for HIV/AIDS Prevention in Central Asia," World Bank study ECSHD/ECCU8, March 2005.

⁵² *Ibid.*

EDUCATION

Kyrgyz education indicators are generally steady and encouraging. The Kyrgyz net primary enrollment rate was 89.3 percent in 2002 (Figure 4-2). Although slightly lower than in previous years, the level is above the regression benchmark for a country with the Kyrgyz Republic’s characteristics (81.9 percent) and the LI-FSR average (84.2 percent). In fact, the rate is closer to those in countries with higher incomes: Bulgaria, 90.4; Romania, 88.9; and Russia, 89.7.

Figure 4-2. Net Primary Enrollment Rate



The Kyrgyz government seems to be committed to improving education. At 3.8 percent of GDP in FY2005, government expenditure on primary education is well above averages in the LI-FSR region (2.8 percent) and in LI countries overall (1.8 percent).⁵³ The pupil-to-teacher ratio in primary schools, a proxy indicator for the quality of education, is also high: 24.5 pupils per teacher in 2002. Although close to the average ratio in the LI-FSR region (22.3), the ratio is higher than that of all three comparator countries: 16.8 in Bulgaria, 17.4 in Romania, and 16.9 in Russia.

EMPLOYMENT AND WORKFORCE

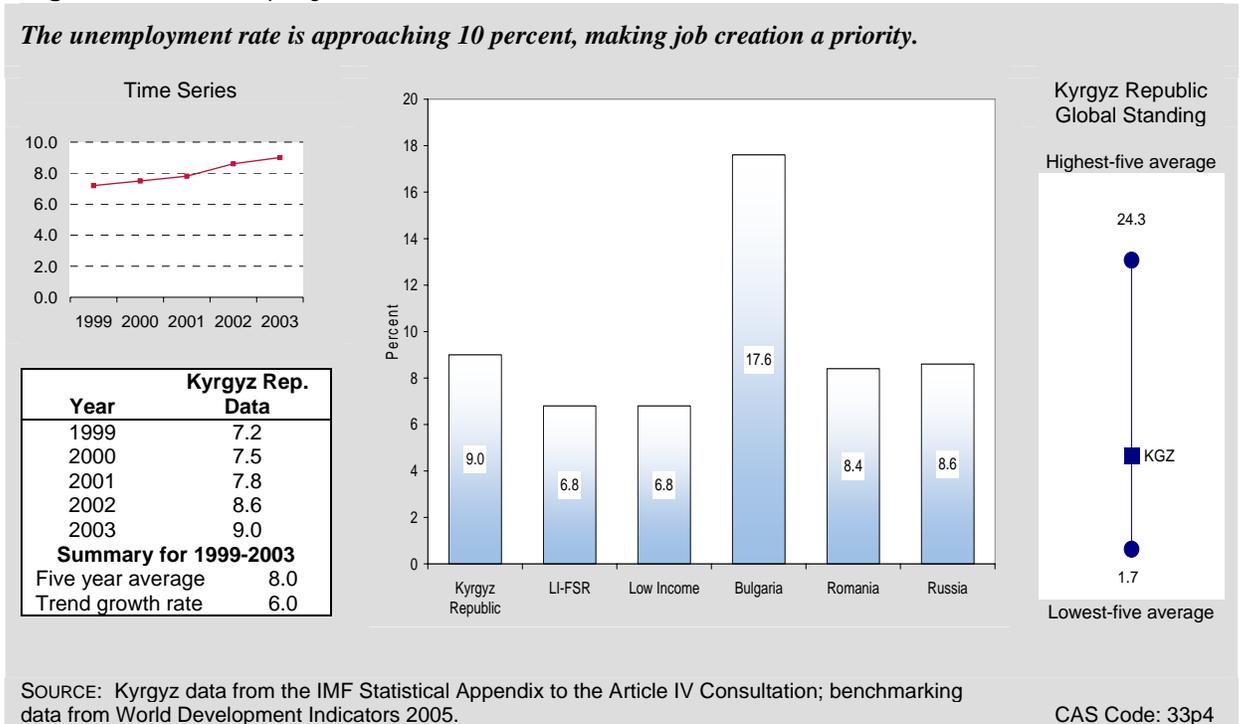
Productive employment provides livelihoods and reinforces social cohesion. The moderate economic expansion in the Kyrgyz Republic was accompanied by rises in the number of unemployed⁵⁴ and the unemployment rate, as job creation was not sufficient to accommodate the

⁵³ Expenditure on primary education is a Millennium Challenge Account indicator.

⁵⁴ IMF, “Kyrgyz Republic: Statistical Appendix,” Country Report No. 05/31, February 2005.

growth of the economically active population. The unemployment rate increased from 7.2 percent in 1999 to 9.0 percent in 2003, exceeding the unemployment rate in the LI-FSR countries, Romania, and Russia (Figure 4-3). It was still less than one half of Bulgaria's unemployment rate. Programs supporting economic growth in labor-intensive sectors, especially in the face of declining gold production, will be an important remedy to the Kyrgyz Republic's unemployment woes.

Figure 4-3. Unemployment Rate



The Kyrgyz labor force participation rate was stable at 73.5 percent from 2000 through 2003, marginally less than the average in the LI-FSR region (73.9 percent) and in Bulgaria (73.6 percent). It was also lower than in Russia (77.5 percent), but noticeably higher than in Romania (67.9 percent). This rate is sufficient to sustain economic activity, and it appears that the practice of early retirement common in many transition countries may not be widespread in the Kyrgyz Republic.⁵⁵

The Kyrgyz Republic scores 38 on the Rigidity of Employment Index, which gauges the liquidity of the labor market by determining the ease of hiring and firing workers. This score is significantly better than the scores for the LI-FSR group (54), Bulgaria (44), and Romania (59).⁵⁶

⁵⁵ IMF data ("Kyrgyz Republic: Statistical Appendix," Country Report No. 05/31, February 2005) show a steady decline in the labor force participation rate from 72.7 percent in 1999 to 68.7 percent in 2003, a worrisome trend and different from the picture presented by the WDI data, which we normally use in Economic Performance Assessment reports.

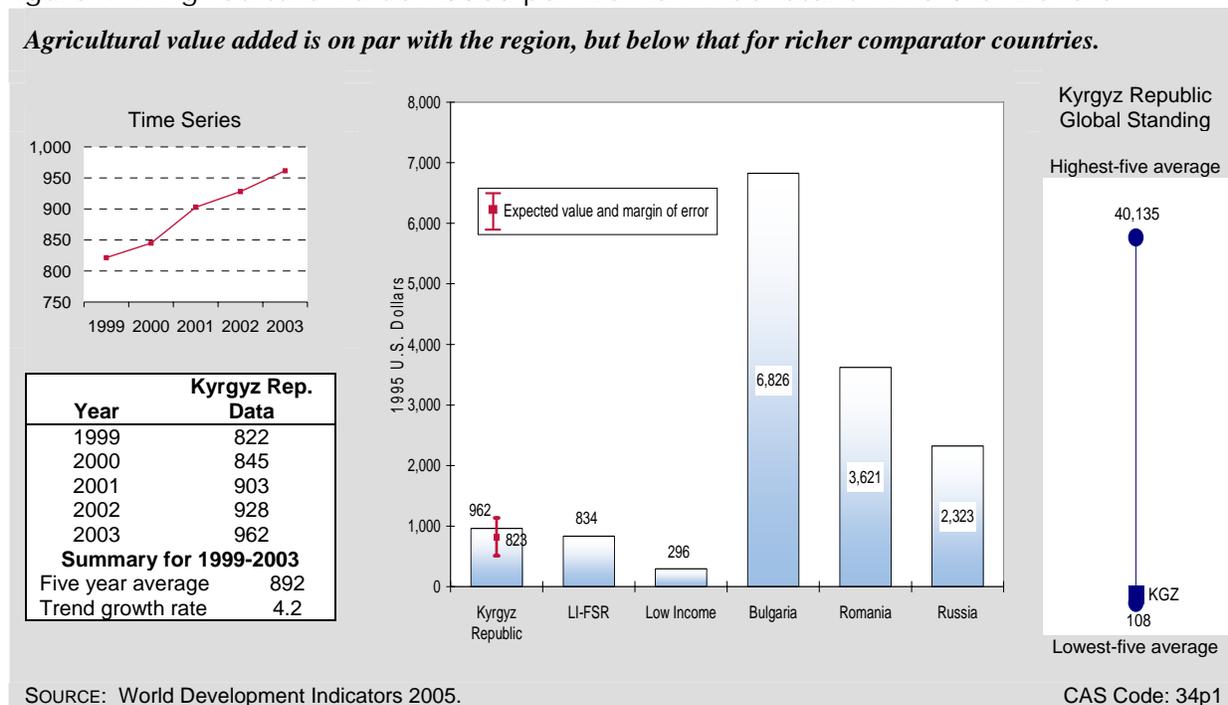
⁵⁶ The Rigidity of Employment Index ranges from 0 (minimum rigidity) to 100 (high rigidity).

It is also marginally better than the range predicted by the regression. Russia’s labor market is more liquid, scoring 30 on the index.

AGRICULTURE

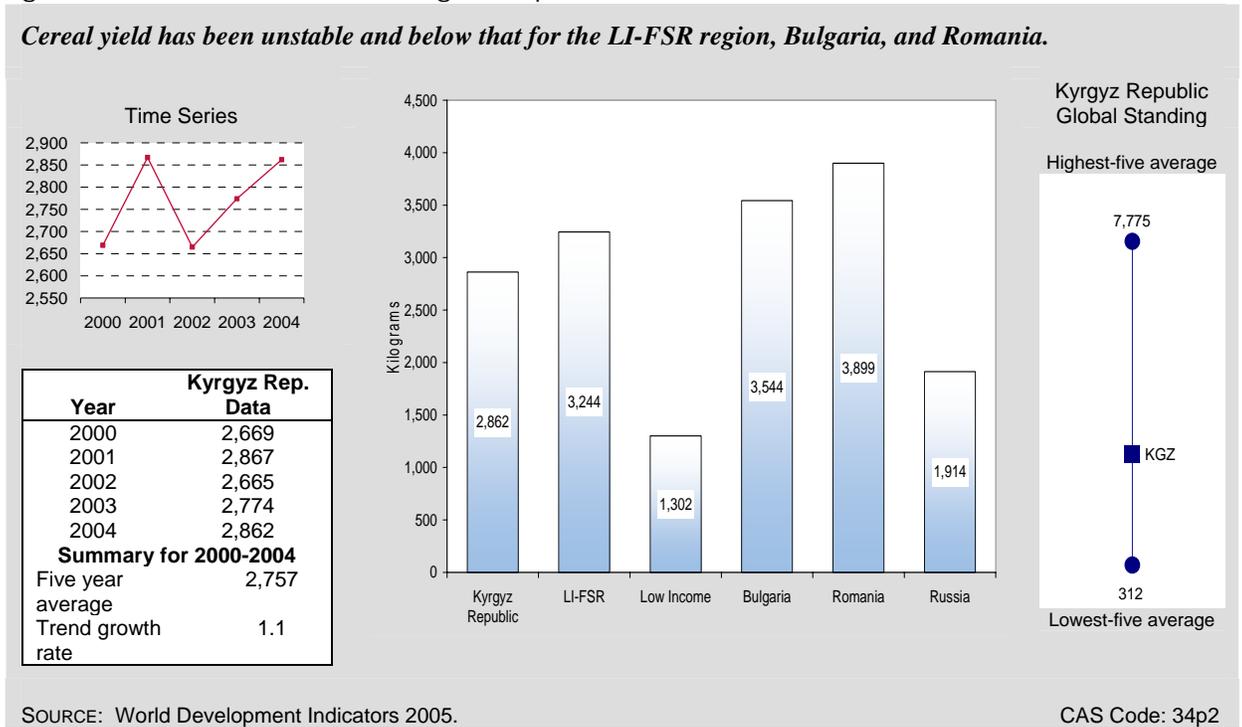
The agriculture sector is less productive than the rest of the Kyrgyz economy, but judging by value added per worker, it seems to be in a better shape than agriculture in the LI-FSR region overall. In 2003, a Kyrgyz agricultural worker generated about \$962 in value-added (constant 1995 prices), while the LI-FSR average was \$834. But the country lagged far behind Bulgaria (\$6,826), Romania (\$3,621), and Russia (\$2,323) (Figure 4-4). At the same time, despite an improvement in 2000–2003, Kyrgyz cereal yield remained less than in the LI-FSR countries, on average, and in Bulgaria and Romania. It was higher than in Russia (see Figure 4-5).

Figure 4-4. Agriculture Value Added per Worker in Constant 1995 U.S. Dollars



The World Development Indicators’ crop and livestock production indices for the Kyrgyz Republic show declines in 2004 (figures are in the Data Supplement). These figures do not appear realistic because agricultural production, according to the National Statistical Committee of the Kyrgyz Republic, increased by 4.1 percent in 2004. Agricultural production fell by 4.1 percent year-over-year in the first three months of this year, apparently because of the political instability that has harmed many other sectors.

Figure 4-5. Cereal Yield in Kilograms per Hectare



The Kyrgyz Republic may benefit from policies aimed at shifting agricultural workers to more productive sectors, supporting nonfarm employment, and moving production and employment to more productive agricultural subsectors.

Appendix

CRITERIA FOR SELECTING INDICATORS

The economic performance evaluation balances the need for broad coverage and diagnostic value, on the one hand, and the requirement of brevity and clarity, on the other. The analysis covers 15 EG-related topics, and just over 100 variables. For the sake of brevity, the text highlights issues for which the “dashboard lights” appear to be signaling problems and which suggest priorities for USAID intervention. The table at the end of this appendix lists all indicators examined for this report. The separate Data Supplement contains the complete data set for Kyrgyz Republic, including data for benchmark comparisons, and technical notes for every indicator.

For each topic, we begin the analysis by screening *primary performance indicators*. These “level I” indicators are selected to answer the question: Is the country performing well or not in this area? The set of primary indicators also includes descriptive variables such as per capita income, the poverty head count, and the age dependency rate.

Where level I indicators suggest weak performance, we then review a limited set of *diagnostic supporting indicators*. These “level II” indicators provide additional details, or shed light on *why* the primary indicators may be weak. For example, if economic growth is poor, one can examine data on investment and productivity as diagnostic indicators. If a country performs poorly on educational achievement, as measured by the youth literacy rate, one can examine determinants such as expenditure on primary education and the pupil-teacher ratio.¹

The indicators have been selected on the basis of the following criteria. Each one must be accessible through USAID’s Economic and Social Database or convenient public sources, particularly on the Internet. They should be available for a large number of countries, including most USAID client states, to support the benchmarking analysis. The data should be sufficiently timely to support an assessment of country performance that is suitable for strategic planning purposes. Data quality is another consideration. For example, we use subjective survey responses only when actual measurements are not available. Aside from a few descriptive variables, the indicators must also be useful for diagnostic purposes. Preference is given to measures that are widely used, such as Millennium Development Goal indicators, or evaluation data used by the Millennium Challenge Corporation. Finally, we have attempted to minimize redundancy. If two indicators provide similar information, preference is given to the one that is simplest to

¹ Deeper analysis of the topic using more detailed data (level III) is beyond the scope of papers in this series.

understand or is most widely used. For example, both the Gini coefficient and the share of income accruing to the poorest 20 percent of households can be used to gauge income inequality. We use the income share because it is simpler and more sensitive to changes.

BENCHMARKING METHODOLOGY

Comparative benchmarking is the main tool for evaluating each indicator. The analysis draws on several criteria, rather than a single mechanical rule. The starting point is a comparison of performance in the Kyrgyz Republic relative to the average for countries in the same income group and region—in this case, former Soviet republics with low income.² For added perspective, three other comparisons are examined: (1) the global average for this income group; (2) respective values for three comparator countries selected by the Kyrgyz Republic mission (in this case Bulgaria, Romania, and Russia); and (3) the average for the five best and five worst performing countries globally. Most comparisons are framed in terms of values for the latest year of data from available sources. Five-year trends are also taken into account where this information sheds light on the performance assessment.³

For selected variables, a second source of benchmark values uses statistical regression analysis to establish an expected value for the indicator, controlling for income and regional effects.⁴ This approach has three advantages. First, the benchmark is customized to the Kyrgyz Republic's specific level of income. Second, the comparison does not depend on the exact choice of reference group. Third, the methodology allows one to quantify the margin of error and establish a “normal band” for a country with the Kyrgyz Republic's characteristics. An observed value falling outside this band on the side of poor performance signals a serious problem.⁵

Finally, where relevant, the Kyrgyz Republic's performance is weighed against absolute standards. For example, if the Corruption Perception Index for a given country is below 3.0, this is a sign of serious economic governance problems, regardless of the regional comparisons or regression result.

² Income groups as defined by the World Bank for 2005. For this study, the average is defined in terms of the mean; future studies will use the median instead because the values are not distorted by outliers.

³ The five-year trends are computed by fitting a log-linear regression line through the data points. The alternative of computing average growth from the end points produces aberrant results when one or both of those points diverges from the underlying trend.

⁴ This is a cross-sectional OLS regression using data for all developing countries. For any indicator, Y , the regression equation takes the form: Y (or $\ln Y$, as relevant) = $a + b * \ln \text{PCI} + c * \text{Region} + \text{error}$ – where PCI is per capita income in PPP\$, and Region is a set of 0-1 dummy variables indicating the region in which each country is located. Once estimates are obtained for the parameters a , b and c , the predicted value for Kyrgyz Republic is computed by plugging in Kyrgyz Republic-specific values for PCI and Region. Where applicable, the regression also controls for population size and petroleum exports (as a percentage of GDP).

⁵ This report uses a margin of error of 0.66 times the standard error of estimate (adjusted for heteroskedasticity, where appropriate). With this value, 25% of the observations should fall outside the normal range on the side of poor performance (and 25% on the side of good performance). Some regressions produce a very large standard error, giving a “normal band” that is too wide to provide a discerning test of good or bad performance.

LIST OF INDICATORS

	Level	MDG/MCA/EcGov ^a	CAS Indicator Code
OVERVIEW OF THE ECONOMY			
Growth Performance			
Per capita GDP, \$PPP	I		11P1
Per capita GDP, current US\$	I		11P2
Real GDP growth	I		11P3
Growth of labor productivity	II		11S1
Investment Productivity - Incremental Capital-Output Ratio (ICOR)	II		11S2
Gross fixed investment, % GDP	II		11S3
Gross fixed private investment, % GDP	II		11S4
Poverty and Inequality			
Human poverty index	I		12P1
Income-share, poorest 20%	I		12P2
Population living on less than \$1 PPP per day	I	MDG	12P3
Poverty headcount, by national poverty line	I	MDG	12P4
PRSP Status	I	EcGov	12P5
Population below minimum dietary energy consumption	II	MDG	12S1
Poverty gap at \$1 PPP a day	II		12S2
Economic Structure			
Labor force structure	I		13P1
Output structure	I		13P2
Demography and Environment			
Adult literacy rate	I		14P1
Age dependency rate	I		14P2
Environmental sustainable index	I		14P3
Population size and growth	I		14P4
Urbanization rate	I		14P5
Gender			
Adult literacy rate, ratio of male to female	I	MDG	15P1
Gross enrollment rate, all levels, ratio of male to female,	I	MDG	15P2
Life expectancy at birth, ratio of male to female	I		15P3
PRIVATE SECTOR ENABLING ENVIRONMENT			
Fiscal and Monetary Policy			
Govt. expenditure, % GDP	I	EcGov	21P1
Govt. revenue, % GDP	I	EcGov	21P2
Growth in the money supply	I	EcGov	21P3
Inflation rate	I	MCA	21P4
Overall govt. budget balance, including grants, % GDP	I	EcGov	21P5
Composition of govt. expenditure	II		21S1
Composition of govt. revenue	II		21S2
Composition of money supply growth	II		21S3

	Level	MDG/MCA/EcGov ^a	CAS Indicator Code
Business Environment			
Corruption perception index	I	EcGov	22P1
Doing business composite index	I	EcGov	22P2
Rule of law index	I	MCA / EcGov	22P3
Cost of starting a business, % GNI per capita	II	MCA / EcGov	22S1
Procedures to enforce contract	II	EcGov	22S2
Procedures to register property	II	EcGov	22S3
Procedures to start a business	II	EcGov	22S4
Time to enforce a contract	II	EcGov	22S5
Time to register property	II	EcGov	22S6
Time to start a business	II	EcGov	22S7
Financial Sector			
Domestic credit to private sector, % GDP	I		23P1
Interest rate spread	I		23P2
Money supply, % GDP	I		23P3
Stock market capitalization rate, % of GDP	I		23P4
Cost to create collateral	II		23S1
Country credit rating	II		23S2
Legal rights of borrowers and lenders index	II		23S3
Real Interest rate	I		23S4
External Sector			
Aid , % GNI	I		24P1
Current account balance, % GDP	I		24P2
Debt service ratio, % exports	I	MDG	24P3
Export growth of goods and services	I		24P4
Foreign direct investment, % GDP	I		24P5
Gross international reserves, months of imports	I	EcGov	24P6
Gross Private capital inflows, % GDP	I		24P7
Present value of debt, % GNI	I		24P8
Remittance receipts, % exports	I		24P9
Trade, % GDP	I		24P10
Concentration of Exports	II		24S1
Inward FDI Potential Index	II		24S2
Net barter terms of trade	II		24S3
Real effective exchange rate (REER)	II	EcGov	24S4
Structure of merchandise exports	II		24S5
Trade policy index	II	MCA / EcGov	24S6
Economic Infrastructure			
Internet users per 1000 people	I	MDG	25P1
Overall infrastructure quality	I	EcGov	25P2
Telephone density, fixed line and mobile	I	MDG	25P3
Quality of infrastructure – railroads, ports, air Transport, and electricity	II		25S1
Telephone cost, average local call	II		25S2

	Level	MDG/MCA/EcGov ^a	CAS Indicator Code
Science and Technology			
Expenditure for R&D, % GNI	I		26P1
FDI and technology transfer index	I		26P2
Patent applications filed by residents	I		26P3
PRO-POOR GROWTH ENVIRONMENT			
Health			
HIV prevalence	I		31P1
Life expectancy at birth	I		31P2
Maternal mortality rate	I	MDG	31P3
Access to improved sanitation	II	MDG	31S1
Access to improved water source	II	MDG	31S2
Births attended by skilled health personnel	II	MDG	31S3
Child immunization rate	II		31S4
Prevalence of child malnutrition (weight for age)	II		31S5
Public health expenditure, % GDP	II	EcGov	31S6
Education			
Net primary enrollment rate	I	MDG	32P1
Persistence in school to grade 5	I	MDG	32P2
Youth literacy rate	I		32P3
Education expenditure, primary, % GDP	II	MCA/ EcGov	32S1
Expenditure per student, % GDP per capita – primary, secondary, and tertiary	II	EcGov	32S2
Pupil-teacher ratio, primary school	II		32S3
Employment & Workforce			
Labor force participation rate, females, males, total	I		33P1
Rigidity of employment index	I	EcGov	33P2
Size and growth of the labor force	I		33P3
Unemployment rate	I		33P4
Agriculture			
Agriculture value added per worker	I		34P1
Cereal yield	I		34P2
Growth in agricultural value-added	I		34P3
Agricultural policy costs index	II	EcGov	34S1
Crop production index	II		34S2
Livestock production index	II		34S3

^a Level I = primary performance indicators, Level II = supporting diagnostic indicators

MDG = Millennium Development Goal indicator

MCA = Millennium Challenge Account indicator

EcGov = Major indicators of *economic governance*, which is defined in USAID's *Strategic Management Interim Guidance* to include "microeconomic and macroeconomic policy and institutional frameworks and operations for economic stability, efficiency, and growth." The term therefore encompasses indicators of fiscal and monetary management, trade and exchange rate policy, legal and regulatory systems affecting the business environment, infrastructure quality, and budget allocations.