

The contents of this document are preliminary and subject to change.

GRAY/21/1447

June 2, 2021

**Statement by Mr. Merk and Mr. Krahnke on Kyrgyz Republic  
(Preliminary)  
Executive Board Meeting  
June 4, 2021**

We thank staff for an instructive set of reports and Mr. Trabinski and Mr. Imashov for their helpful Buff statement. **We largely concur with the staff appraisal.** Although restrained by persistent structural weaknesses, Kyrgyz Republic has achieved some progress in advancing the economy and fighting poverty over the past decade. However, the pandemic has slowed and set back some of this progress and is likely to cause scarring and increase fiscal vulnerabilities. That being said, decisive structural reforms and prudent macro policies, with a credible fiscal consolidation path after the crisis has eased, and supported by an independent monetary policy framework, could help to support potential growth and ensure overall stability in the economy.

**We agree with staff recommendations to rebuild fiscal buffers as soon as conditions allow.** Timely initiation of consolidation efforts would allow for a more gradual deficit reduction than delayed measures that might require harsh and abrupt cuts. Accordingly, we encourage the authorities to proactively explore options for streamlining current expenditures, especially those limiting a further expansion of the public wage bill, while prioritizing quality investments and means-tested spending for social assistance, education and health. *Could staff elaborate on the potential for undertaking spending reviews in these areas?* In order to contain fiscal risks from contingent liabilities, governance reforms and hardening of SOE budget constraints are crucial.

**The budget's high dependence on donor support underscores the urgency of demonstrating the authorities' unwavering commitment to reform and taking rigorous action to broaden domestic revenue mobilization.** With this in mind, we urge the authorities to address tax compliance gaps, including by strengthening institutional capacities in tax administration and promoting the formalization of the economy.

**We note staff's favorable assessment of the health of the banking sector and encourage the authorities to remain vigilant, particularly with respect to potential deterioration in credit risks should insolvencies become more prevalent.** We agree with staff and the authorities on the need for maintaining sound accounting, reporting, and provisioning standards. *Could staff give additional details on the authorities' plans to phase-out forbearance measures in the financial sector?*

**To enable a lasting and job-rich post-pandemic recovery, there is a need for the authorities to step up the structural reform momentum in areas such as transparency and anti-corruption, labor market and cutting red-tape.** Concerning labor market reforms, we particularly appreciate that staff highlights the valuable role which vocational education could play in matching workforce skills with labor market needs, as well as promoting employment opportunities for the youth. Moreover, we strongly encourage the authorities to remove obstacles that limit female labor force participation.

**With regard to recent developments around KCG, we note with some concern the implications for macroeconomic stability.** Hence, we urge the parties involved to engage constructively and in a good-faith manner that avoids disturbance in a key segment of the Kyrgyz economy and protects the environment. We call on the authorities to pursue decisive reforms to improve international investor confidence in a rules-based, predictable, and objective business environment. In case of downside risks materializing, the authorities should stand ready to make necessary policy adjustments.