

**FOR
AGENDA**

EBS/08/21

February 20, 2008

To: Members of the Executive Board

From: The Secretary

Subject: **Republic of Tajikistan—Report on Noncomplying Disbursements and Breach of Obligations Under Article VIII, Section 5**

Attached for consideration by the Executive Directors is the Managing Director's report on noncomplying disbursements made by the Republic of Tajikistan and Tajikistan's breach of obligations under Article VIII, Section 5, which is tentatively scheduled for discussion on **Wednesday, March 5, 2008**. Draft decisions appear on pages 6 and 7.

Questions may be referred to Mr. Piñerua (ext. 34279) and Mr. Cakir (ext. 34341) in MCD.

This document will shortly be posted on the extranet, a secure website for Executive Directors and member country authorities.

Att: (1)

Other Distribution:
Department Heads



Office Memorandum

To: Members of the Executive Board

February 20, 2008

From: The Managing Director

Subject: **Republic of Tajikistan—Report on Noncomplying Disbursements and Breach of Obligations Under Article VIII, Section 5**

I. INTRODUCTION

1. **In a November 2007 letter requesting the start of discussions on a new arrangement, the Tajik authorities acknowledged for the first time that the National Bank of Tajikistan (NBT) had been guaranteeing external debt obligations of the cotton sector.** A follow-up fact-finding mission that visited Dushanbe in December 2007 found that, in an effort to secure financing for the cotton sector, the NBT had not only issued guarantees, but had also pledged a large proportion of its international reserves as collateral by depositing the reserves at creditor banks. In addition, the mission was informed by the authorities that the NBT had issued large amounts of domestic credit to the cotton sector over the last five years, which had not been reflected in its balance sheets prior to last November. This information had not previously been reported to Fund staff.

2. **The information provided to the December mission by the authorities, and subsequently confirmed in a letter from President Rakhmon, indicates that misreporting occurred in the context of the last PRGF arrangement.** As a result, Tajikistan received five noncomplying disbursements between January 2004 and February 2006 amounting to SDR 49 million.¹ Moreover, the inaccuracy of the reported data gives rise to a breach of obligations under Article VIII, Section 5 of the Fund's Articles of Agreement.

3. **This report discusses the circumstances that led to the noncomplying disbursements and breach of Article VIII, Section 5.** It recommends that: (i) the Republic of Tajikistan repays the noncomplying disbursements within twelve months, with a first payment expected six months from the date of the Board's decision on this matter; and (ii) the Executive Board not require any further remedial action be taken by the Tajik authorities with respect to the breach of obligations under Article VIII, Section 5.

¹ The relevant framework for handling misreporting cases is described in the Executive Board's Guidelines on Misreporting and Noncomplying Disbursements in Arrangements under the Poverty Reduction and Growth Facility and the Exogenous Shocks Facility (Misreporting Guidelines).

II. BACKGROUND

4. **On December 11, 2002, the Executive Board approved a three-year PRGF arrangement for Tajikistan in the amount of SDR 65 million (75 percent of quota).** With the completion of the sixth and final review on February 6, 2006, all the resources available under the arrangement were disbursed.² The PRGF arrangement included a continuous performance criterion prohibiting the NBT from issuing directed credits as well as, *inter alia*, performance criteria on the net international reserves (a floor) and on the net domestic assets of the NBT (a ceiling).

III. NONCOMPLYING DISBURSEMENTS

5. **Five reviews under the 2002 PRGF arrangement were completed between 2004 and 2006.**³ On the basis of the information previously reported to the Fund by the authorities, the disbursements that followed the Executive Board's decisions to complete the fourth and sixth reviews under the 2002 arrangement were made on the basis that all performance criteria were observed; further, the Executive Board completed the second review under the 2002 arrangement granting a waiver of nonobservance of a performance criterion and the Fund subsequently released a disbursement. Specifically, related to these disbursements, Tajikistan was understood to be in observance with all the relevant quantitative performance criteria on net international reserves (NIR) and net domestic assets (NDA) of the NBT, and with the continuous structural performance criterion prohibiting the NBT from issuing directed credits. In addition, on two separate occasions, waivers were granted for the nonobservance of performance criteria prohibiting the NBT from issuing directed credits (third review) and on NIR of the NBT (fifth review) on the basis that the deviations were either minor or had been reversed.

6. **Revised data provided by the authorities in December 2007 show that the NBT's international reserves are now largely encumbered and that significant directed credit operations have taken place over the last five years.** The December 2007 mission learned from the authorities that, in order to obtain financing for the cotton sector⁴, the NBT not only issued written guarantees⁵ to foreign creditors but also, from 2001, pledged its reserves as collateral, by depositing its reserves at the creditor banks. As of December 2007, total NBT pledges amounted to about \$240 million—compared to gross reserves, as reported to the Fund, of about \$350 million—with an additional \$80 million in contingent claims on the

² At the time of the fifth review, the arrangement was extended until February 10, 2006, to provide sufficient time to allow for the implementation of some structural benchmarks under the program.

³ Taking account of the four-year statute of limitation period covering misreporting cases, only disbursements starting in January 2004 could be considered as noncomplying.

⁴ Most of the \$325 million in external cotton debt has a very short-term maturity, requiring frequent rollover. Close to \$300 million are due at end-March 2008.

⁵ The NBT started granting these guarantees late in the first quarter of 2006, after the 2002 PRGF arrangement had expired.

NBT in the form of written guarantees.⁶ The mission also found that, in 2002, the NBT began providing off-balance sheet credits to the cotton sector at nonmarket rates through Kredit Invest—an asset management company that was also the intermediary for the foreign loans mentioned above. As of December 2007, the National Bank of Tajikistan held previously unreported claims on Kredit Invest amounting to 880 million somoni—about \$255 million, or 60 percent of reserve money. Until November 2007, these claims had not been reflected on the balance sheets of either the NBT or Kredit Invest.

7. **Based on the new information provided to staff, it is now clear that the assessment that the performance criteria mentioned in paragraph 5 were met, as well as the justification for the waivers granted by the Executive Board, was based on inaccurate information.** Therefore, all applicable floors on net international reserves and ceilings on the net domestic assets of the NBT under the 2002 PRGF, as well as the continuous structural performance criterion limiting the NBT from issuing any directed credits, were not observed. Thus, taking account of the 4-year limitation period covering misreporting cases, Tajikistan received five noncomplying disbursements between January 2004 and February 2006, amounting to SDR 49 million. Two of the noncomplying disbursements made in 2004, amounting to SDR 19.6 million, were subject to debt relief under the MDRI.

Tajikistan: Misreporting on Performance Criteria Under the 2002 PRGF Arrangement

| Disbursement Date | Performance Criteria 1/ | Performance Criteria | Actual | | |
|----------------------|-------------------------|-------------------------|----------|---------|------------|
| | | | Reported | Revised | Difference |
| January 30, 2004 | Second Review | | | | |
| | Ceiling on NDA | 162.1 | 128.1 | 178.3 | 50.2 |
| | Floor on NIR | 5.5 | 38.5 | -42.2 | -80.7 |
| August 5, 2004 | Third Review | | | | |
| | Ceiling on NDA | 120.0 | 73.0 | 189.0 | 116.0 |
| | Floor on NIR | 30.0 | 49.0 | -31.7 | -80.7 |
| March 30, 2005 | Fourth Review | | | | |
| | Ceiling on NDA | 55.0 | 30.0 | 252.8 | 222.8 |
| | Floor on NIR | 66.0 | 70.0 | -20.2 | -90.2 |
| July 27, 2005 | Fifth Review | | | | |
| | Ceiling on NDA | 40.0 | 34.0 | 337.7 | 303.7 |
| | Floor on NIR | 70.0 | 67.0 | -52.2 | -119.2 |
| February 10, 2006 | Sixth Review | | | | |
| | Ceiling on NDA | 101.0 | 41.0 | 449.0 | 408.0 |
| | Floor on NIR | 59.0 | 78.0 | -41.2 | -119.2 |

Source: National Bank of Tajikistan

1/ Ceilings on NDA are in millions of somoni and floors on NIR are in millions of U.S. dollars.

⁶ International reserves, therefore, net of pledges and guarantees amounted to about \$30 million in December 2007.

8. **On January 11, 2008, I wrote to the President of Tajikistan,** informing him of the Fund staff's revised assessment of performance under the 2002 arrangement, as well as the possible implications in terms of misreporting and breach of Article VIII, Section 5 obligations. In this letter, I also sought the views of President Rakhmon before making a recommendation to the Executive Board on how to proceed (Attachment I).

IV. THE AUTHORITIES' RESPONSE AND CORRECTIVE ACTIONS

9. **President Rakhmon wrote to me on February 5, 2008** (Attachment II). In his letter, he acknowledges that misreporting did take place, accepts that the relevant performance criteria under the 2002 PRGF arrangement were not observed, and outlines some of the measures the authorities have already taken to address the problems that led to the misreporting. These include the appointment of a new NBT Governor and Deputy Governors, their agreement to hold a special audit of the National Bank of Tajikistan—for which they are seeking Fund technical support—and a commitment to implement the recommendations of the recent FSAP mission, which include critical steps to improve governance at the NBT. He also outlines in his letter measures to put the cotton sector on a sounder footing to avoid a recurrence of the debt problem, for which they are seeking support from the Asian Development Bank and the World Bank. Moreover, he proposes the adoption of a well-defined debt management strategy and steps to increase the financial transparency of the operations of key state-owned enterprises. Finally, he highlights the country's current difficult and uncertain balance of payments situation, including the impact of energy and food shortages that have resulted in a humanitarian crisis, and requests a new PRGF arrangement.

V. RECOMMENDATIONS

10. **While I welcome the remedial actions outlined in President Rakhmon's letter, the provision of inaccurate data to the Fund over the past six years has seriously undermined the credibility of the authorities with IFIs and other donors.** In the coming months, the Tajik authorities will need to take decisive actions to restore credibility and resume the path of policy reforms. President Rakhmon's letter acknowledges that misreporting occurred, giving rise to five noncomplying disbursements under the 2002 PRGF arrangement. Since the deviations from the performance criteria on net international reserves and net domestic assets of the NBT, and the continuous structural performance criterion on prohibiting the NBT from issuing directed credits were neither minor nor temporary, I recommend that Tajikistan repay the three noncomplying disbursements (amounting to SDR 29.4 million) that were not discharged under MDRI relief.⁷

⁷ In 2006, the Fund approved Tajikistan's request for grant assistance from the MDRI Trust (Decision No. 13646-(06/1), adopted January 5, 2006). Following this decision, the trustee of the MDRI Trust repaid to the Fund on behalf of Tajikistan an amount equivalent to Tajikistan's eligible debt (which included the repayments of the noncomplying disbursements associated with the second and third review under the PRGF arrangement). Thus, these two noncomplying disbursements have already been discharged by MDRI debt relief. The grant assistance received under the MDRI Trust is not subject to a misreporting framework.

11. **Notwithstanding the seriousness of the misreporting case, I believe that Tajikistan's current very difficult economic circumstances warrant an extension of the repayment period beyond the 30-day period called for in the Misreporting Guidelines.** The gross international reserves of the NBT (net of pledges, but not guarantees), stood at \$113 million (about SDR 72 million, or close to ½ month of imports) at end-January 2008. If full repayment were to be required within 30 days of the Board's decision, the repayments would account for about 40 percent of gross reserves, putting the country in an unduly vulnerable position, at a time when it is facing serious exogenous shocks to energy and food supplies. Therefore, I recommend that the repayment be made within 12 months, with the first payment expected six months from the Board's decision on this matter and monthly payments of SDR 4.9 million thereafter, to allow the country some breathing room in dealing with the current economic situation. Staff's preliminary assessment of balance-of-payments prospects over the next two years indicates that the repayment of the noncomplying disbursements on this basis would leave the reserves essentially flat at around the current very low level, covering less than one month of imports.⁸

VI. ARTICLE VIII, SECTION 5

12. **Staff considers that the provision of the inaccurate information by Tajikistan gave rise to a breach of obligation under Article VIII, Section 5.**⁹ In accordance with Fund procedures, consultation with the Tajik authorities took place on the country's capacity to provide accurate information to the Fund (Attachment I). The authorities confirmed the provision of inaccurate information to the Fund on the net international reserves and net domestic assets of the NBT and did not contend that it related to institutional capacity issues (Attachment II). Therefore, in my judgment, the inaccurate information provided by the Tajik authorities in the context of surveillance gives rise to a breach of obligations under Article VIII, Section 5. Nevertheless, in view of the corrective actions taken and the ongoing efforts of the authorities to improve the governance structure of the NBT and implement measures to improve and strengthen the monitoring and reporting of data provided to the Fund as noted in President Rahkmon's letter, I recommend that no further remedial action be required by the Executive Board in connection with Tajikistan's breach of these obligations.

Attachments (2)

⁸ This projection hinges crucially on the ability of the authorities to: a) avoid a call on the \$80 million in NBT guarantees; and b) secure official financing from the Asian Development Bank, World Bank, and European Commission amounting to \$60 and \$40 million in 2008 and 2009, respectively.

⁹ Article VIII, Section 5 obliges members to provide the Fund with certain information it deems necessary for its activities, including surveillance. The procedures associated with the application of Article VIII, Section 5 are established in "Strengthening the Effectiveness of Article VIII, Section 5," Decision No. 13183-(04/10), January 30, 2004.

Proposed Decisions

The following draft decisions, which may be adopted by a majority of the votes cast, are proposed for adoption of the Executive Board:

A. Noncomplying Disbursements and Early Repayment Expectation

1. The Fund notes the report of the Managing Director set forth in EBS/08/21 (2/20/08) on three noncomplying disbursements made to the Republic of Tajikistan on March 30, 2005, July 27, 2005, and February 10, 2006, respectively, for an amount equivalent to SDR9.8 million each, following the fourth, fifth, and sixth reviews under the three-year arrangement under the Poverty Reduction and Growth Facility (EBS/02/188, Supplement 1, 11/13/02), and decides that the Republic of Tajikistan shall be expected to repay the Fund an amount equivalent to SDR29.4 million together with any interest accrued thereon in six equal installments to be paid as follows:

- (a) the first installment in an amount equivalent to SDR 4.9 million to be paid no later than September 5, 2008;
- (b) the second installment in an amount equivalent to SDR 4.9 million to be paid no later than October 6, 2008;
- (c) the third installment in an amount equivalent to SDR 4.9 million to be paid no later than November 5, 2008;
- (d) the fourth installment in an amount equivalent to SDR 4.9 million to be paid no later than December 5, 2008;
- (e) the fifth installment in an amount equivalent to SDR 4.9 million to be paid no later than January 5, 2009; and
- (f) the sixth installment in an amount equivalent to SDR 4.9 million plus any remaining amount of the outstanding noncomplying disbursements with any interest accrued thereon to be paid no later than February 5, 2009.

2. The amounts specified in paragraphs 1(a) through (f) shall be applied to repay the noncomplying disbursements, with any interest accrued thereon, in the order in which the disbursements were made (EBS/08/21, 2/20/08).

B. Breach of Obligations Under Article VIII, Section 5

The Fund takes note of the report of the Managing Director set forth in EBS/08/21 (2/20/08) on the misreporting by the Republic of Tajikistan of information on net international reserves and net domestic assets of the National Bank of Tajikistan, and finds that the Republic of Tajikistan has breached its obligation under Article VIII, Section 5 of the Articles of Agreement to report accurate information to the Fund (EBS/08/21, 2/20/08).



INTERNATIONAL MONETARY FUND
WASHINGTON, D. C. 20431

DOMINIQUE STRAUSS-KAHN
MANAGING DIRECTOR

CABLE ADDRESS
INTERFUND

January 11, 2008

His Excellency
Emomali Rakhmon
President of the Republic of Tajikistan
Office of the President
Rudaki Avenue 42
734051 Dushanbe
Tajikistan

Dear Mr. President:

I was informed by IMF staff that Tajikistan may have received disbursements from the Poverty Reduction and Growth Facility (PRGF) Trust Fund on the basis of inaccurate information provided to IMF staff by the National Bank of Tajikistan (NBT). The recent disclosure of new information and data covering 2001–07 on possible directed lending to the cotton sector by the NBT and the potential encumbrance of the NBT's international reserves, which were provided to IMF staff during a December 2007 mission, warrants a major reassessment of Tajikistan's performance under the three-year PRGF arrangement approved by the IMF Executive Board on December 11, 2002. This is a serious matter, particularly in light of the magnitude of the possible misreporting and Tajikistan's previous instances of noncomplying disbursements.

On the basis of the information previously reported to the IMF by the authorities, the disbursements that followed the IMF's Executive Board's decisions to complete the fourth and sixth reviews under the 2002 arrangement were made on the basis that all performance criteria were observed; further, the IMF Executive Board completed the second review under the 2002 arrangement granting a waiver of nonobservance of a performance criterion and the IMF subsequently released a disbursement. In particular, related to these disbursements, Tajikistan was understood to be in observance with the quantitative performance criteria on net international reserves (NIR) and net domestic assets (NDA) of the NBT, and with the continuous structural performance criterion on prohibiting the NBT from issuing directed credits. In addition, on two separate occasions under the 2002 arrangement, waivers were granted for the nonobservance of performance criteria on prohibiting the NBT from issuing directed credits (third review) and on NIR of the NBT (fifth review) on the basis that the deviations were either minor or had been reversed. However, in view of the revised data, it now appears that the assessment that all the performance criteria mentioned above had been

met, as well as the justification for the waivers granted by the IMF's Executive Board, was based on inaccurate information.

Tajikistan may, therefore, have received five noncomplying disbursements between January 2004 and February 2006 amounting to SDR49 million, as detailed in the attached table. Two of the possible noncomplying disbursements made in 2004, amounting to SDR19.6 million, were subject to debt relief provided under the Multilateral Debt Relief Initiative (MDRI).

Under the IMF's policy on misreporting and noncomplying disbursements from the PRGF Trust Fund, I am required to report all instances of misreporting to the IMF's Executive Board. The Board may decide either to require that Tajikistan make an early repayment of the disbursements that have not been discharged by MDRI debt relief, or to grant waivers for the nonobservance of the relevant performance criteria. A waiver is normally granted only if the nonobservance is minor or temporary, or if corrective actions had subsequently been taken to achieve the objectives of the program supported by the arrangement under which the disbursements were made.

Furthermore, if—in addition to possible misreporting on information under the 2002 PRGF arrangement—inaccurate information has also been provided to IMF staff in the context of surveillance, such provision of inaccurate information may give rise to a breach of Tajikistan's obligations under Article VIII, Section 5 of the IMF's Articles of Agreement, which imposes on members an obligation to provide the IMF with information that the IMF deems necessary for its activities, subject to the member's capacity to report accurate information. Under applicable IMF procedures, I am required to report to the IMF Executive Board any breaches of obligation under the IMF's Articles of Agreement. In this regard, the Board could decide that the voluntary adoption by Tajikistan of remedial measures to address the causes of any misreporting could be an alternative to the imposition of sanctions by the Executive Board.

I would like to invite your views before making a recommendation to the IMF's Executive Board on how to proceed. I would appreciate receiving your response by February 8, 2008 or earlier, if possible, so that we can move expeditiously to resolve this matter. If, after receiving your response, I find that a noncomplying disbursement or a breach of Article VIII, Section 5 did occur, I will submit a report to the IMF Executive Board with recommendations on how to proceed.

Yours sincerely,



Attachment

cc: Mr. Davlatov, Presidential Advisor
Mr. Alimardon, Chairman of the National Bank of Tajikistan
Mr. Najmuddinov, Minister of Finance

Tajikistan: Misreporting on Performance Criteria Under the PRGF Arrangement

| Disbursement Date | Performance Criteria | Disbursements | Test Date | Performance Criteria | Actual | | Performance Margins | |
|-------------------|--|-----------------|--------------------|-----------------------------|-------------------------|---------------------------|---------------------|-----------------|
| | | | | | Originally Reported | Revised | Originally Assessed | Revised |
| January 30, 2004 | Second Review (EBS/03/171) Ceiling on net domestic assets of the NBT (In millions of somoni) Floor on total net international reserves (In millions of U.S. dollars) Prohibit the NBT from issuing directed credits | SDR 9.8 million | End-September 2003 | 162.1 5.5 Continuous | 128.1 38.5 Met | 178.3 -42.2 Not met | -34.0 33.0 | 16.2 -47.7 |
| August 5, 2004 | Third Review (EBS/04/98) Ceiling on net domestic assets of the NBT (In millions of somoni) Floor on total net international reserves (In millions of U.S. dollars) Prohibit the NBT from issuing directed credits 1/ | SDR 9.8 million | End-March 2004 | 120.0 30.0 Continuous | 73.0 49.0 Not met | 189.0 -31.7 Not met | -47.0 19.0 | 69.0 -61.7 |
| March 30, 2005 | Fourth Review (EBS/05/38) Ceiling on net domestic assets of the NBT (In millions of somoni) Floor on total net international reserves (In millions of U.S. dollars) Prohibit the NBT from issuing directed credits | SDR 9.8 million | End-September 2004 | 55.0 66.0 Continuous | 30.0 70.0 Met | 252.8 -20.2 Not met | -25.0 4.0 | 197.8 -86.2 |
| July 27, 2005 | Fifth Review (EBS/05/105) Ceiling on net domestic assets of the NBT (In millions of somoni) Floor on total net international reserves (In millions of U.S. dollars) 2/ Prohibit the NBT from issuing directed credits | SDR 9.8 million | End-March 2005 | 40.0 70.0 Continuous | 34.0 67.0 Met | 337.7 -52.2 Not met | -6.0 -3.0 | 297.7 -122.2 |
| February 10, 2006 | Sixth Review (EBS/06/10) Ceiling on net domestic assets of the NBT (In millions of somoni) Floor on total net international reserves (In millions of U.S. dollars) Prohibit the NBT from issuing directed credits | SDR 9.8 million | End-September 2005 | 101.0 59.0 Continuous | 41.0 78.0 Met | 449.0 -41.2 Not met | -60.0 19.0 | 348.0 -100.2 |

Source: National Bank of Tajikistan

1/ A waiver of non-observance for the performance criterion on prohibition of directed credit by the NBT was granted on the basis that the credit has been repaid before the completion of the review and that NBT management strengthened oversight of credit operations.

2/ A waiver of non-observance for the performance criterion on net international reserves was granted on the basis that the shortfall in NIR target was due to a short delay in the disbursement of a program grant.

President
of the Republic of Tajikistan

No. 23. I/I - 3
dated February 2, 2008

His Excellency
Mr. Dominique Strauss-Kahn
Managing Director of the International Monetary Fund
Washington, D.C. 20431

Dear Mr. Strauss-Kahn,

First, I would like to express to you personally and to the International Monetary Fund (IMF) our gratitude for your constant support and the assistance provided to Tajikistan. We esteem highly our cooperation with the Fund and look forward to our continued mutually advantageous relations.

The problems mentioned in your letter of January 11, 2008 regarding the misreporting of information during the period of implementation of the preceding program and compliance with Article IV are issues of deep concern for us. I have learned that the quantitative performance criteria on net international reserves (NIR) and net domestic assets (NDA) of the National Bank of Tajikistan (NBT) and the continuous structural performance criteria on prohibiting the NBT from issuing directed credits under the 2002 arrangement were not observed, as your letter also notes.

Our economic structures cooperated closely with the IMF mission in December 2007 on the disclosure of information concerning this incident. We consider it our obligation to address the problems associated with the misreporting of information, including problems in the cotton sector, and to provide accurate information. To this end, I sent a delegation to Washington, D.C. on January 12–15, 2008 to discuss key issues and take steps to correct the deficiencies.

Thus far, for the purpose of correcting existing deficiencies, I have appointed a new Chairman of the National Bank of Tajikistan and his deputies. To prevent a recurrence of past errors, the task of the new management of the Bank is to take steps in cooperation with your staff. To achieve our objectives, we plan to implement the recommendations of the previous Financial Sector Assessment mission (FSAP).

We have agreed to hold a special audit of the NBT, to be carried out by a recognized international firm. The technical assignment for the audit will be coordinated with Fund staff. We anticipate that the aim of the audit will be to establish a reliable foundation for the provision in the future of monetary data and data on external debt, and also to define steps to ensure the transparency of all financial operations of the NBT, including accounts not on the

balance sheet. We will inform Fund staff on the course of performance of the audit, including providing drafts of the Special Audit Report and its final version, as well as all annexes thereto. We also intend to publish key features of the report on the performance of the special audit and take steps to address them. We would be grateful to the Fund for urgent assistance to develop a draft of the technical assignment for a special audit.

We will take steps to eliminate weaknesses with respect to the provision of data and to establish a reliable system, utilizing technical assistance from the Fund, in order to ensure accurate data for surveillance purposes as well as future programs.

We are working with the Asian Development Bank (AsDB) and the World Bank to develop a strategy for restructuring Kredit Invest. We will also hold negotiations with foreign creditors to review time frames for guarantees given. At the same time we will seek alternative domestic financing sources.

To further ensure transparency and adherence to reforms, we will provide for sustainability of the debt level by developing a corresponding debt strategy with a legislatively mandated ceiling for the debt-to-GDP ratio.

Provision will be made for transparency of financial operations pertaining to state enterprises, particularly TALKO and Barki Tochik, including liquidation of their debts for taxes and other payments.

As for addressing problems of the cotton sector, we have adopted Resolution of the Government No. 111, and we have undertaken an obligation to implement it with the assistance of the World Bank and the AsDB with respect to a new mechanism for financing the cotton sector and providing greater freedom to the private sector. The Law of the Republic of Tajikistan "On Mortgages" has been submitted to the Parliament, and the Land Code has been amended to allow private farmers to use their land use right as property-based security for borrowing. In addition, provision will be made for greater freedom for private farmers to grow products that are profitable for them.

Along with the aforementioned, we are pursuing the objective of market-oriented reforms in the agricultural sector to ensure that the cotton sector is put on a profitable footing. We trust that the aforementioned measures will put an end to interference of local authorities and administrative bodies in financing for the cotton sector, thus eliminating similar problems in the future.

Your letter also indicates that the IMF's Executive Board may require that Tajikistan make early repayment of unused funds that have not been discharged under the Multilateral Debt Relief Initiative (MDRI). The government of the Republic of Tajikistan will respect the decision of the Executive Board; but I would like to ask you and the Executive Board to take into consideration the exceptionally difficult circumstances and external factors that Tajikistan is facing, including a sharp increase in world prices for energy resources and grain, and problems in the energy system due to natural disasters. Early repayment of the

aforementioned funds will significantly reduce the international reserves that we have and bring them to a very low level. In turn, the low level of international reserves will significantly affect the economy as a whole, making it more vulnerable to external risks.

If this request is unacceptable and the Board decides that repayment is necessary, then we would hope very much that the payments could be made on a quarterly basis over one year.

Given the already low level of reserves and the need to address problems in the cotton sector, and also taking into consideration our most rigorous measures to correct the deficiencies, we hope that in parallel with the special audit we will be able to move expeditiously to implementation of a new Fund program—the Poverty Reduction and Growth Facility (PRGF). As you know, approximately two thirds of the population of Tajikistan live in rural regions with relatively high poverty levels, and financing of the cotton sector is of exceptional significance. We hope very much that we can find an optimal way to address the situation with the assistance of the IMF, the World Bank, the AsDB, and donors.

I would like avail myself of this opportunity to renew the assurances of my highest consideration, and I look forward to continued mutually advantageous cooperation.

With best wishes,

/s/

Emomali Rakhmon