

**Kyrgyzstan: Programme to Promote the Private Sector I and II**

**Ex-post evaluation**

<b>OECD sector</b>	24030 - Financial intermediaries of the formal sector	
<b>BMZ project ID</b>	1994 65 295, 1996 66 256	
<b>Project-executing agency</b>	Goskominvest (until the end of 2000) Ministry of Finance of Kyrgyzstan (from 2001)	
<b>Consultant</b>	iCee	
<b>Year of ex-post evaluation</b>	<b>2004</b>	
	<b>Project appraisal (scheduled)</b>	<b>Ex-post evaluation (actual)</b>
<b>Start of implementation</b>	Q III 1995	Q III 1995
<b>Period of implementation</b>	36 months (I and II)	96 months (I and II)
<b>Investment costs</b>	No information available	EUR 11.7 million
<b>Borrower's contribution</b>	No information available	EUR 2.7 million
<b>Financing, of which Financial Cooperation (FC) funds</b>	EUR 9.8 million	EUR 9.0 million
<b>Other institutions/donors involved</b>	none	none
<b>Performance rating</b>	<b>5</b>	
• <b>Significance/relevance</b>	5	
• <b>Effectiveness</b>	5	
• <b>Efficiency</b>	5	

**Brief Description, Overall Objective and Project Objectives with Indicators**

The objective of the programmes to promote the private sector I and II was to establish and strengthen competitive private enterprises, primarily in the manufacturing industry, by granting them medium and long-term investment loans. The overall objective was to contribute to the economic renewal in the industrial sector. The programmes comprised two credit lines totalling EUR 9.8 million and measures to train personnel in the amount of EUR 1.4 million. The indicator for the achievement of the programme objective and the overall objective was defined as follows: The programme objective is deemed to be achieved when two-thirds of the projects and the funds invested are operating profitably after a start-up period of not more than three years and meet their debt service obligations on a regular basis. The achievement of the programme objective was taken to imply the achievement of the overall objective.

**Project design / Major deviations from the original project planning and their main causes**

During programme implementation there were no major deviations from the originally chosen design. Goskominvest as programme-executing agency and loan approval agency (until the end of 2000) and the banks AKB-Kirgistan and AKB-Promstrojbank ("Promstrojbank"), which were in charge of the financial execution as trustees, were supported by a consultant (until 2003) and by the TC Programme "Programme to Support Small and Medium-sized Enterprises" (until the end of 1999). At the beginning of 2001 the tasks of the programme-executing agency were

transferred to the Ministry of Finance of Kyrgyzstan (foreign debt department). The consulting services included the preparation of bankable sub-loan applications as well as training measures to qualify the sub-borrowers, the programme-implementing agency and the banks interposed to process the loans.

AKB-Kirgistan and Promstrojbank acted as payment agencies for the programmes in question. A total of 100 sub-loans with an FC volume of EUR 9.0 million were disbursed between January 1995 and April 2002. The available FC funds of EUR 9.8 million could not be fully implemented in the first round. The sub-loans were extended under a big credit line and a small credit line. For loans granted under the small credit line the upper limit for sub-loans was EUR 76,531. Loans granted under the big credit line were required to have a volume of at least EUR 76,531. 18 sub-loans were granted under the big credit line and 82 under the small credit line. The funds mobilised by these sub-loans and by equity as well as funds borrowed on a short-term basis are estimated to be roughly 30% above the FC funds. The average loan amount extended was approximately EUR 366,000 under the big credit line and around EUR 31,000 under the small credit line. The big credit line was used for loans to textile enterprises (4), printing companies (2), food enterprises (4) and other manufacturing firms (8). The small credit line supplied agro-industrial firms to an extent that was initially not planned (60), as well as other manufacturing firms (9), service enterprises (9), raw materials (2) and small businesses (2).

For the big credit line the loan appraisal was conducted by the consultant in cooperation with Goskominvest, for the small credit line it was done within the framework of the above-mentioned TC programme and by the State Fund for Enterprise Development. Goskominvest as implementing agency bore the overall responsibility for the loan appraisals both for the small and for the big credit line.

Both the portfolio quality and the debt service are clearly insufficient. The clearly insufficient debt service is partly due to the economic difficulties which many sub-borrowers are facing. These resulted from a general deterioration of the economic conditions and a decline in domestic demand following the Russian crisis (1998), restrictions on trade with neighbouring countries, liquidity shortages of state customers and supply bottlenecks in the energy sector.

A major problem for the collection of overdue debt, however, is the debtor-friendly insolvency law of Kyrgyzstan. Under Kyrgyz law, if a debtor is able to claim before a court that he is seeking an out-of-court settlement with the creditor, the insolvency proceedings are suspended, which leads to further delays in the collection of overdue payments. Furthermore, some enterprises have claims towards the state which they illegally offset against their debt. In this connection it also needs to be taken into account that the banks as on-lending institutions without liability do not have a genuine interest in collecting these payments, so that arrears are handled loosely. Consequently, there are a number of enterprises that are quite able to pay but hope that the matter will fizzle out or, if the worst comes to worst, that the creditor will settle for a part payment. As ascertained during the on-site ex-post evaluation, this kind of behaviour spreads quickly and can influence the behaviour other enterprises quite strongly.

The chosen approach of putting the now dissolved state-owned Goskominvest in charge as programme-executing agency and the "Fund for the Promotion of the Private Sector" in charge of implementation of the small credit line and to treat the interposed banks as payment agencies only was a contributing cause to the poor portfolio quality. From today's point of view it would have been better to follow the concept of the European Bank for Reconstruction and Development, which was to establish the credit line with a bank and gradually have it assume joint responsibility. The tenacious adherence of the Kyrgyz authorities to the agreed programme architecture, however, made it impossible to place greater responsibility on the two banks. An internal power struggle for economic influence was obviously fought here which was eventually decided by the dissolution of the two agencies after the new government was formed in 2001. At this time, however, it was already too late to change the programme design because the credit line was largely committed and the banks' interest in taking responsibility was understandably low.

## Key Results of the Impact Analysis and Performance Rating

Lack of access to long-term credit continues to be a crucial obstacle to growth in Kyrgyzstan's small and medium-sized enterprise sector. 100 loans were granted under the programme with the aid of which around 1700 jobs were preserved or newly created – also considering the insolvencies. The stabilisation of the income situation prevented the employees of SMEs from slipping below the poverty line. The regional distribution of the loans produced moderate regional effects. Loans were extended without regard for gender. Environmental aspects were appropriately considered in the loan appraisals. In a combined assessment of all above impacts and risks we have arrived at the following rating of the developmental effectiveness of the programme.

The achievement of the programme objective - to create or strengthen competitive private enterprises, primarily in the producing or manufacturing sector - was clearly insufficient. After evaluating the available information, less than one quarter of the borrowers (22 out of 100) are performing the debt service as agreed, 73 are in arrears with some payments and five enterprises are not servicing their debt at all. In terms of volume, the share of non-performing loans is 59% of the total portfolio. Only one third of the enterprises financed out of the big credit line are operating with a profit. For the borrowers of the big credit line this figure is 40%. Still, 92 of the 100 enterprises that received a loan under the programme are still in existence. The programme had the learning effect of demonstrating where the problems in the legal system of Kyrgyzstan lie which are hampering the establishment of a functioning long-term credit system. We rate the **efficiency** of the programme as **clearly inadequate (sub-rating: 5)**.

The overall objective - to contribute to the economic renewal in the industrial sector - was to be deemed achieved when the indicators for the achievement of the programme objective were fulfilled. Measured by the indicators for the achievement of the programme objective, the overall objective was clearly missed. Inadequate access to long-term credit continues to constitute a major obstacle to the growth of SMEs in Kyrgyzstan. The availability of permanent access to long-term credit for SMEs can be plausibly expected to contribute to the economic renewal in the industrial sector. The programme approach of one-time provision of loans through a state agency with massive support from a consultant (loan appraisals) and the involvement of private banks as pure payment agencies has proven to be inadequate for reducing the obstacles to growth. Despite massive support from the consultant the chosen approach was unable to achieve even the full initial utilisation of the FC funds made available. Around EUR 800,000 could not be turned into loans. Besides, the selected concept failed to establish a revolving utilisation of the funds in the sense of a revolving fund. This was not explicitly sought at the time the programme was conceived but constitutes an indispensable element of a credit programme. The funds repaid are deposited in an account of the Ministry of Finance in local currency without bearing any interest and are continuously losing value because of inflation. A transfer of knowledge from the consultant to a Kyrgyz institution in the sense of establishing the credit technology locally did not take place. The programme will be terminated with the end of the consultant's assignment. The entire programme conception was neither suitable for building structures nor was it designed to bring about a durable solution to the development obstacle that was identified. We rate the **efficiency** of the programme as **clearly inadequate (sub-rating: 5)**.

We rate the allocation efficiency of the programme as clearly insufficient. Although the interest is positive in real terms and close to the market interest level, a misallocation of funds cannot be ruled out given the low repayment rate. Particularly the lack of enforceability of loan claims combined with state influence on the courts produces disincentives to repay loans. We also rate the production efficiency as clearly insufficient. Given the difficult environment of Kyrgyzstan the consultant had to make a very great effort, particularly since institutional sustainability was neither sought nor achieved because of the dissolution of Goskominvest and because of the low impact on the two banks. We rate the **efficiency** as clearly inadequate (**sub-rating: 5**).

In a combined assessment of all the above impacts and risks we rate the **overall developmental effectiveness of the programme** - also with special consideration for the restrictions of the Kyrgyz transition process - as **clearly insufficient (rating 5)**.

### General Conclusions applicable to other Projects

A credit programme should be conceived in agreement with the principles of reasonable local institutional establishment, long-term viability of the executing agency and banking professionalism of the management and staff. In particular, the long-term revolving use of funds for loans is indispensable.

If an indicator such as "profitability" is agreed, this also means that steps for reviewing this indicator have to be agreed as well, and the consultant or executing agency will have to report accordingly as well. If such an indicator cannot be reliably established, auxiliary indicators can be defined. One reasonable approach, for example, would be a general overview of parameters such as the survival of an enterprise and the tax payments it has transferred or payments it has made to social funds.

### Legend

Developmentally successful: Ratings 1 to 3	
Rating 1	Very high or high degree of developmental effectiveness
Rating 2	Satisfactory degree of developmental effectiveness
Rating 3	Overall sufficient degree of developmental effectiveness
Developmental failures: Ratings 4 to 6	
Rating 4	Overall slightly insufficient degree of developmental effectiveness
Rating 5	Clearly insufficient degree of developmental effectiveness
Rating 6	The project is a total failure

### Criteria for the Evaluation of Project Success

The evaluation of a project's "developmental effectiveness" and its classification during the final evaluation into one of the various levels of success described in more detail below concentrate on the following fundamental questions:

- Are the **project objectives** reached to a sufficient degree (aspect of project **effectiveness**)?
- Does the project generate sufficient significant **developmental effects** (project **relevance** and **significance** measured by the achievement of the overall development-policy objective defined beforehand and its effects in political, institutional, socio-economic and socio-cultural as well as ecological terms)?
- Are the **funds/expenses** that were and are being employed/incurred to reach the objectives **appropriate** and how can the project's microeconomic and macroeconomic impact be measured (aspect of **efficiency** of the project conception)?
- To the extent that undesired (**side**) **effects** occur, are these tolerable?

We do not treat **sustainability**, a key aspect to consider for project evaluation, as a separate category of evaluation but instead as a cross-cutting element of all four fundamental questions on project success. A project is sustainable if the project-executing agency and/or the target group are able to continue to use the project facilities that have been built for a period of time that is, overall, adequate in economic terms or to carry on with the project activities on their own and generate positive results after the financial, organizational and/or technical support has come to an end.