

# TECHNICAL ASSISTANCE COMPLETION REPORT<sup>1</sup>

Division: CWFM

TA 6137-REG: Regional Financial Sector Development			Amount Approved: \$800,000	
			Revised Amount: n.a.	
Executing Agency: Asian Development Bank		Source of Funding: TASF	Amount Undisbursed: \$67,438.85	Amount Utilized: \$732,561.15
TA Approval Date: 13 November 2003	TA Signing Date: n.a.	Fielding of First Consultant: 11 December 2003	TA Completion Date Original: 31 May 2005	Actual: 31 January 2006
			Account Closing Date Original: 31 May 2005	Actual: 28 February 2006
<b>Description</b>				
<p>The single most important constraint to financial sector development in most of the economies in Central Asia and the Caucasus (CACs) is their small size. To overcome this constraint, the CACs must integrate their financial markets with each other or with larger countries. Although this goal is not achievable in the near future, progress can be made towards integration by harmonizing standards and regulations with international best practices. To that end, the technical assistance (TA) was designed to assist Azerbaijan (AZE), Kazakhstan (KAZ), the Kyrgyz Republic (KGZ), Tajikistan (TAJ) and Uzbekistan (UZB) to harmonize and strengthen (i) banking sector regulation with regards to risk management, (ii) financial disclosure standards, and (iii) the regulatory framework for corporate governance.</p>				
<b>Expected Impact, Outcome and Outputs</b>				
<p>The TA's expected impact is integration of CAC members' financial markets, and its outcome, the harmonization of financial sector regulatory, supervisory, corporate governance and financial disclosure standards. Its expected outputs included: (i) reviews of banking sector risk management regulations, (ii) surveys on risk management practices, (iii) country-specific strategies to introduce risk management in line with Basel Core Principles for Banking Supervision and Basel Capital Accord, (iv) implementation guidelines for International Accounting Standards (IAS), (v) strategy to strengthen regulation of corporate governance in nonfinancial joint stock companies (JSCs), and (vi) knowledge sharing among participating countries through training.</p>				
<b>Delivery of Inputs and Conduct of Activities</b>				
<p>Government reshuffles took place in KAZ, KGZ and TAJ during the initial stages of the TA, which reduced the authorities' responsiveness somewhat. The ADB inception mission in February 2004 addressed the issue by reaching out to the authorities who subsequently extended close cooperation on TA activities. The TA, however, was not implemented in UZB as the Government declined to participate for unspecified reasons after considerable interest during TA fact-finding.</p>				
<p>In line with the TA's mandate of taking proactive measures to establish risk management norms in accordance with the Basel Capital Accord, the TA was extended to accommodate specific activities that had to be immediately undertaken to help attain TA objectives in KGZ, e.g., (i) there was a clear need to prepare detailed guidelines on credit and operational risk given recent sharp increase in arrears outstanding, and (ii) an effective supervisory strategy and action plan was warranted to mitigate risks in the growing rural financial system. The additional activities led to the utilization of a total of 17 person-months (PMs) of international consulting services and 59 PMs of national consulting services under the TA, against the original plan to utilize 15 PMs for international and 55 PMs for local consultants. The inputs were nevertheless provided economically; there was sufficient TA savings to cover the additional PMs. Of the four international (individual) consultants, one was rated excellent, two were rated satisfactory, while one was rated marginal. Of the 10 national consultants, one was rated excellent, seven were rated satisfactory, one was rated unsatisfactory, while one was not rated. Overall, the consultants' performance was satisfactory.</p>				
<p>Consultants were mobilized quickly. ADB provided effective supervision to ensure that the TA objectives were met. ADB also ensured effective coordination between this TA and a TA for Financial Sector Reforms in the Kyrgyz Republic,<sup>2</sup> with regard to the implementation of the respective risk management components for that country. The clients were satisfied with the TA's substantive inputs. ADB's performance as the executing agency was satisfactory.</p>				
<b>Evaluation of Outputs and Achievement of Outcome</b>				
<p>Under the risk management component, the TA sponsored a regional workshop, organized jointly with the National Bank of the Kyrgyz Republic (NBKR) and the Financial Stability Institute (FSI) for the Transcaucasia, Central Asia and</p>				

<sup>1</sup> In preparing any country program or strategy, financing any project, or by making any designation of or reference to a particular territory or geographic area in this document, the Asian Development Bank does not intend to make any judgments as to the legal or other status of any territory or area.

<sup>2</sup> ADB. 2002. *Technical Assistance to the Kyrgyz Republic for Financial Sector Reforms*. Manila.

Russian Federation Regional Group on Banking Supervision. In addition, a seminar on new risk management regulation was held in Bishkek, attended by participants from the banking sector and officials from NBKR Supervision Department. The final report for this component detailed regional themes and harmonization opportunities for improving oversight of risk management in the respective countries' banking systems. The TA also supported subscription by NBKR to FSI Connect, an online information and learning resource on risk management for banking supervisors.

Under the financial disclosure component, the TA supported a survey of JSCs in three countries in order to inform the agencies responsible for implementing International Financial Reporting Standards (IFRS) about the accounting practices currently employed at JSCs and their readiness to convert to IFRS.<sup>3</sup> The information obtained also served to underscore the need for practical training workshops for JSC accountants and facilitated tailoring of the workshops to the specific needs of the trainees in each country. Under this component, the TA sponsored two regional workshops, as well as in-country workshops for accountants from JSCs.<sup>4</sup> The workshops provided access to current information on IFRS and were instrumental in accelerating its implementation, enhancing cooperation among the core groups within each country, facilitating the sharing of implementation guidelines between countries, and were a breakthrough for cooperation between professional associations. The proceedings of the regional workshops were published and distributed widely to the Governments, universities, businesses and accounting organizations. The consultants also assisted the countries in developing accounting manuals incorporating international best practices for converting to and using IFRS for financial reporting. These manuals were presented and discussed in the workshops. Further, the consultants helped in the development of a "roadmap" detailing implementation guidelines for the adoption and sustained use of IFRS. All countries started implementing recommendations in the "roadmap" showing that the TA outputs were well-received by the clients.

The corporate governance component provided a comprehensive analysis of the current status and needs for its strengthening in Central Asia focusing on: (i) the legal framework, (ii) current practices, (iii) regulatory activities, and (iv) training and promotion. The TA also sponsored two regional workshops on corporate governance. The workshops supported knowledge transfer and regional knowledge sharing on practical problems in introducing international standards and best practices of corporate governance. A corporate governance roundtable was held in Bishkek to discuss key issues that are critical to KGZ. All final reports under the TA, which were delivered in a timely manner, are available in the ADB website.<sup>5</sup> The clients appreciated the regional initiative in general and the regional workshops in particular.

### **Overall Assessment and Rating**

The TA was successful. The expected TA outputs were efficiently and economically produced within the TA budget. The TA inputs were effectively utilized to jumpstart harmonization and strengthening of risk management in the banking sector, accounting standards, and regulatory framework for corporate governance. The keys to success were emphasis on technical work at the working level, strong involvement of well qualified domestic consultants, and focus on country specific outputs such as targeted training, reform road maps, and regulatory guidelines. The promising reforms initiated under the TA merited subsequent ADB support, including TAs to enhance financial disclosure standards in Central Asia and the Caucasus.<sup>6</sup>

### **Major Lesson**

The TA provided a common forum for meeting between countries' representatives (which was absent until this TA). An important lesson from implementing the TA is the realization that substantial benefits could be gained from interaction and cooperation, not only between countries but even among different agencies within a country participating in a regional forum. This suggests that Governments should seek to undertake regional workshops designed for information exchange.

### **Recommendation and Follow-Up Action**

The TA embodies two of the five core specializations which ADB should focus on as identified in Strategy 2020, namely (i) regional cooperation and integration, and (ii) financial sector development. As such, ADB's continued support in these areas is warranted. In light of the current global financial crisis, a TA to help financial sector regulators in developing and implementing an appropriate policy response to address the impact of the crisis on financial intermediation is of utmost importance.

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<sup>3</sup> International Accounting Standards was renamed International Financial Reporting Standards in 2003 by the International Accounting Standards Board of the International Federation of Accountants.

<sup>4</sup> The core group of participants came from institutions that play a key role in accounting reform in each country: (i) the accounting policy or methodology department of the ministries of finance of the participating countries responsible for implementing International Financial Reporting Standards (IFRS); (ii) the tax division responsible for business taxation; and (iii) professional organizations for accountants and auditors. Selected representatives from other financial market regulators were invited as funds permitted.

<sup>5</sup> <http://www.adb.org/Documents/Reports/Consultant/36027-REG/>

<sup>6</sup> ADB. 2005. *Technical Assistance for Enhancing Financial Disclosure Standards in Transitional Economies*. Manila; ADB. 2008. *Technical Assistance for Enhancing Financial Disclosure Standards in Armenia, Azerbaijan, and Georgia*. Manila.