







## Policy Insights

# Supporting firm creation and growth through business development services in Kyrgyzstan



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## **Foreword**

Kyrgyzstan's government is working to improve the country's business environment so as to facilitate the growth of private sector firms – in particular its micro, small and medium-sized enterprises (MSMEs). The government has identified the lack of public and private business development services (BDS) as a critical barrier to growth.

An OECD public-private Working Group (WG) was created in early 2019 to help design targeted policies to address this problem. The WG met three times in 2019 (Annex B). It was chaired by Mr Dastan Kadyrov, Deputy Minister of Economy, and prior to him Mr Eldar Abakirov, former Deputy Minister of Economy. The WG brought together stakeholders from different ministries, the presidential administration, the cabinet of ministers, business associations, companies, and NGOs active in the field, as well as representatives of the development community.

This peer review note reflects the work of the WG as well as the contribution of international experts from the Ministry of Economic Development of Poland and the Ministry of Justice of Uzbekistan. The final recommendations presented in the note will be peer reviewed during the OECD Eurasia Competitiveness Roundtable on 23 June 2020 in a virtual manner as part of a series of OECD Eurasia webinars. This exercise will involve both international experts and representatives from OECD member countries and other Central Asian countries.

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The main authors of this report are Ms Talisa zur Hausen and Mr Sebastian Kupferschmid, Policy Analysts, OECD Eurasia Division. The project was managed by Mr Grégory Lecomte and Mr Arnault Prêtet of the OECD Eurasia Division. Mr Xavier le Joncour and Julia Ashikbayeva provided analytical input and support. The report was reviewed and benefited from valuable input from Ms Anita Richter, Senior Policy Analyst; Mr Umur Göçke, Project Manager; and Mr Martin Kohtze and Mr Ali Fuad Turgut, Policy Analysts, OECD South East Europe Division. Final editorial and visual support was provided by Mr Christopher Marquardt, editor; Ms Vanessa Berry-Chatelain, OECD Global Relations Secretariat; and Ms Claudia Gemmel, OECD Global Relations Secretariat. Valuable administrative support was provided by Ms Anna Chahtahtinsky, OECD Eurasia Division.

## Acronyms and Abbreviations

AP	Accelerate Prosperity (initiative)
JIA	Association of Young Entrepreneurs
BIO	business intermediary organisation
BDS	business development services
BEEPS	Business Environment and Enterprise Performance Survey
BIO	business intermediary organisation
B2B	business-to-business
CCI	Chamber of Commerce and Industry
EBRD	European Bank for Reconstruction and Development
EC	European Commission
EEU	Eurasian Economic Union
ECP	Eurasia Competitiveness Programme
EU	European Union
EIC	Electronic Interoperability Centre
FDI	foreign direct investment
G2B	government-to-business
GDP	gross domestic product
GIZ	Deutsche Gesellschaft für Internationale Zusammenarbeit
GSP+	Generalised Scheme of Preferences Plus
HDI	Human Development Index
HR	human resources
IBC	International Business Council
JICA	Japan International Co-operation Agency
Kbps	kilobits per second
MSMEs	micro, small and medium-sized enterprises
NBKR	National Bank of the Kyrgyz Republic
NSSD	National Strategy for Sustainable Development
OECD	Organisation for Economic Co-operation and Development
OSCE	Organization for Security and Co-operation in Europe
OSS	one-stop shop
PPD	public-private dialogue
PRSC	Poverty Reduction Support Credit
RRG	Dutch Regulatory Reform Group
SMEs	small and medium-sized enterprises
SOE	state-owned enterprise
UNIDO	United Nations Industrial Development Organisation
USD	US dollar (currency)
WTO	World Trade Organization
WG	working group

## Key Indicators for Kyrgyzstan

Kyrgyzstan		
Population, 2020	6.5 million	
Surface area, 2020	$199,950 \text{ km}^2$	
GDP (USD, current prices), 2018	8.09 billion	
GDP per capita (USD, current price), 2018	1281.364	
Real GDP growth (y-o-y change), 2018	3.5%	
Government debt (% of GDP), 2019	54.3%	
Personal remittances received (percentage of GDP), 2019	28.47%	
Inflation (average consumer prices, y-o-y change), 2017	3.2%	
Exports of goods and services (% of GDP), 2019	37.52%	
Imports of goods and services (% of GDP), 2019	65.75%	
FDI stock, 2018	USD 3.9 billion, or 48.4% of GDP	
FDI, net inflows (% of GDP), 2018	0.57%	
Net lending/borrowing, percentage of GDP, 2017	-2.8%	
Current account balance (% of GDP), 2019	-9.9%	
Unemployment (% of total labour force), 2018	7.17%	
Labour force participation rate, total (% of total population ages 15+), 2018	59.72%	
Lending interest rate, 2017 <sup>1</sup>	19.8%	
Share of informal economy (% of GDP), 2018 <sup>2</sup>	23.4%	
Total number of SMEs (units), 2019	404 431	
Total number of SOEs (units), 2017	135	

Source: EBRD, Trading Economics, UNCTAD, World Bank, National Statistical Committee of the Kyrgyz Republic (<a href="http://stat.kg/ru">http://stat.kg/ru</a>), IMF.

<sup>&</sup>lt;sup>1</sup> Rate charged by banks on loans to prime customers.

<sup>&</sup>lt;sup>2</sup> 23.6% are provided by the National Statistical Committee of Kyrgyzstan. The World Bank indicator on informal employment (% of total non-agricultural employment) indicated 61% in 2013.

## **Executive Summary**

Kyrgyzstan's entrepreneurs and small companies can play a crucial role in boosting growth and employment creation and reducing the country's dependence on extractive industries and remittances. However, private firms in the country are currently struggling to survive COVID-19 and its devastating effects on the economy of Kyrgyzstan. Containment measures and the closure of borders have particularly hit SMEs and entrepreneurs. Key challenges include political uncertainty, widespread corruption, competition with a large informal sector, limited connectivity, burdensome regulations, skills mismatches, and an unfavourable business tax regime. The government is working to tackle these challenges and thereby improve the overall business environment, as reflected in the country's National Strategy for Sustainable Development (NSSD) for 2018-2040. It has also designed a series of measures to support firms to fight COVID-19.

As part of these efforts, the government has acknowledged the important role of public and private business development services (BDS) in supporting business creation and growth. These services can prove essential in providing support to small firms towards post-crisis recovery, in particular digital support, advice and training. This peer review note aims to support this work by recommending actions in three areas.

#### Fully-fledged public one-stop shops to simplify administrative procedures

In order to comply with regulatory requirements such as business registration, licences or certificates, businesses in Kyrgyzstan must currently interact with numerous agencies and ministries, at a significant cost in terms of time and effort. It remains especially hard for businesses outside the urban centres of Bishkek and Osh to access government services. Some initiatives are underway to provide services in a more efficient manner, but no fully-fledged one-stop shop (OSS) for businesses exists. This note recommends that Kyrgyzstan establishes a network of OSSs, each of which bundles all relevant businesses services (business registration, certificates, permits). Physical OSSs should leverage government efforts made under the Digital Kyrgyzstan programme to enable a digital OSS platform. Particularly in light of COVID-19 and the increased need for digital information and services, this note recommends that the government accelerate the digitalisation of its public sector, through its *Government as a Platform* programme.

## Easier access to information on private BDS to increase uptake

Business development services also encompass business-to-business (B2B) services, such as information, training or advisory services in such areas as accounting, legal services, and consulting. However, on the demand side, the companies surveyed for this report expressed limited knowledge and uptake of such services. On the supply side, providers lack information on business needs, as regular business surveys are rarely undertaken. The government could consider playing a facilitator role between firms and suppliers of B2B services. This would include providing information on B2B services to businesses at public OSSs and an online B2B platform, as well as regularly gathering information on business needs – through surveys or exchanges with business intermediary organisations (BIOs) and through business councils.

# Closer co-operation between the government and business intermediary organisations to help deliver better services to smaller businesses

A basic market for private business development services exists in Kyrgyzstan, but it remains weak. High-quality BDS are hard to access for small businesses, particularly on marketing and sales, due to high prices and the limited reach of suppliers outside a few urban centres. The government should co-operate with both the development community and BIOs to improve the provision of high-quality BDS to smaller firms.

#### Introduction

## Kyrgyzstan's economic growth has been primarily driven by remittances and minerals

Kyrgyzstan urgently needs to diversify production and exports, both to reduce the country's vulnerability to external shocks and to help generate more – and more productive – employment. While its economy is less state-dominated than those of its neighbours, the country's export basket remains relatively concentrated, with gold accounting for 37% of total exports in 2017 (OECD, 2018<sub>[1]</sub>; Simoes and Hidalgo, 2019<sub>[2]</sub>). The overall extractive sector, which, on average, generates around 10% of GDP and the bulk of total exports, is an important source of government revenues and, to a lesser extent, employment. Kumtor, the country's biggest gold mine, represented 8.6% of GDP and 18.4% of aggregate industrial output in 2018 (World Bank, 2018<sub>[3]</sub>), despite experiencing a 30% decline in output, which directly translated into reduced GDP growth. In 2019, growth bounced back, due to a 15% increase in output from Kumtor. The country's other major export is, in fact, labour: in 2018, remittances from labour migrants working abroad, mainly in Russia and Kazakhstan, amounted to 33% of GDP. This reliance on labour migration reflects the country's continuing inability to generate sufficient in-country high-productivity employment.

While gold exports and migrant remittances have done much to sustain growth and living standards in Kyrgyzstan, this growth model has two important downsides.

- The structure of the export basket leaves the economy exposed to fluctuations in international prices for a small number of commodities. In particular, the risks associated with the overreliance on a single mine are compounded by the fact that relations between the mine's majority owner and the government have been volatile. The government holds a 26% stake in the mine. Kumtor was initially expected to end production in 2026 (IGF, 2018<sub>[4]</sub>), but its productive life now seems likely to run somewhat longer. In 2019, plans for new mines were being discussed.
- Reliance on migrant remittances ensures that shocks affecting the Russian and Kazakh economies 76% of remittances stem from Russia (World Bank, 2019<sub>[5]</sub>) are quickly transmitted to Kyrgyzstan (Figure 1). Moreover, while labour migration has helped sustain consumption growth, it entails high social costs, to both migrants and sending communities (OECD, 2018, pp. 20-21<sub>[1]</sub>).

Nevertheless, the combined effect of migration and gold exports has helped decrease the share of the population living below the national poverty line, which fell by a third over ten years from 2007 (35%) to 2017 (26%). Household consumption rose, urban services developed, and there were marked shifts in the labour force from agriculture into informal urban employment (World Bank,  $2018_{[3]}$ ).

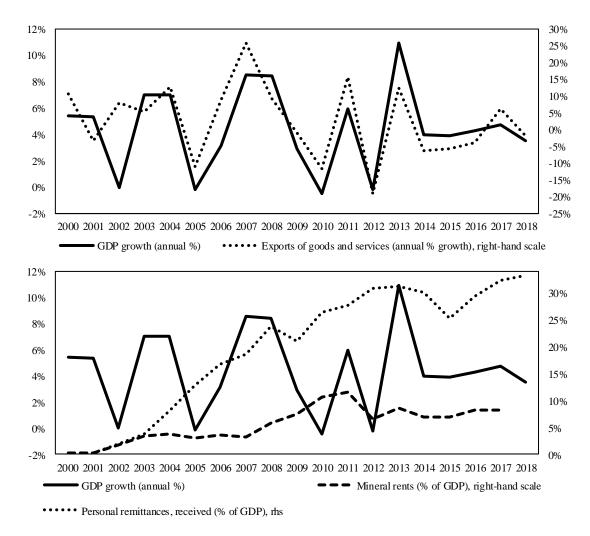


Figure 1. Growth is highly correlated with exports and increasingly dependent on remittances and mineral rents

Source: http://datatopics.worldbank.org/world-development-indicators/

The risks associated with this model have been thrown into stark relief by the global crisis of 2008-09 and the end of the "commodity super-cycle" in the mid-2010s, and now the COVID-19 pandemic and subsequent drop in oil prices. To increase its resilience to external shocks, Kyrgyzstan must become more diversified. More diversified economies have less volatile output, which is usually associated with higher growth in the long run (Ramey and Ramey,  $1995_{[6]}$ ). Diversification is also imperative in order to build inclusive growth, as the extraction sector alone will never be able to generate high-productivity employment on a sufficient scale (OECD,  $2018_{[1]}$ ). Kyrgyzstan needs to develop higher-productivity activities outside the mining sector that are capable of generating more – and more productive – jobs.

In some respects, Kyrgyzstan should be well placed to develop such activities. Despite both the recent economic shocks and a degree of domestic political instability, the country is in important respects a reform leader in the region. The EBRD's assessment of transition

quality shows it performing better than the average for Central Asia  $(CA)^1$  in integration and resilience, and it is roughly on par with the average in competition, governance and green growth  $(2018_{[7]})$ .

The country has a liberal foreign exchange regime: the som is not pegged to any other currency and the central bank intervenes only to smooth exceptionally sharp exchange-rate fluctuations. There are no capital controls or restrictions on converting or transferring funds into freely usable currency at the legal, market-clearing rate, including for repatriation.

The trade regime is likewise fairly liberal; Kyrgyzstan is a member of the World Trade Organization (WTO) and the Eurasian Economic Union (EEU). EEU membership, though, has led to a decline in the shuttle trading<sup>2</sup> enabled previously by tariff differentials between China and Russia (Esenaliev and Asylbekkyzy, 2017<sub>[8]</sub>). Kyrgyzstan also benefits from the EU Generalised Scheme of Preferences Plus (GSP+). Under GSP+, the EU grants Kyrgyzstan full removal of tariffs on over 66% of tariff lines covering a wide array of products (European Commission, 2019<sub>[9]</sub>). Nevertheless, EU-Kyrgyzstan non-minerals trade remains low. Overall, the country's exports remain concentrated in metals and mining (57% of total exports in 2018), followed by textiles (9.6%) and agricultural products (9.2%). Kyrgyzstan's main export partners are Kazakhstan (20%), the United Kingdom (17%) and Russia (14%) (Simoes and Hidalgo, 2019<sub>[2]</sub>).

The private sector plays a critical role in Kyrgyzstan. The number of state-owned enterprises (SOEs) has fallen to 135, as Kyrgyzstan has privatised a total of 7357 state assets since independence. This has enabled the economy to rebalance towards sectors like textiles and tourism. While the service, industry, and agricultural sectors each accounted for approximately one-third of GDP in 1990, the service sector now accounts for more than half of GDP, as compared to 26% for the industry sector and 12% for agriculture (National Statistical Committee, 2017<sub>[10]</sub>; EBRD, 2019<sub>[11]</sub>). With a contribution of 22% of gross value added and 28% of exports, foreign-owned companies also play a substantial role in the economy. The 3107 enterprises with foreign capital are mostly concentrated in the trade (37% of all enterprises with participation of foreign capital), industry (17%) and professional and scientific activities sectors (13%).

Micro, small and medium-sized enterprises (MSMEs) remain the dominant force in Kyrgyzstan's private sector landscape. They represent the principal types of firms in the agriculture and services sectors, such as wholesale, retail trade and hospitality (EBRD, 2019<sub>[11]</sub>). They contributed 41.5% of GDP in 2018 (34.6% excluding agriculture), in line with an average contribution of 40% in 2013-18. A closer look at the subcategories of MSMEs reveals that the share of individual entrepreneurs is higher than that of small or medium-sized enterprises in terms of both GDP and employment, where this category contributes 21% and 17%, respectively (National Statistical Committee, 2017<sub>[10]</sub>). Small firms, on the other hand, generated 6.6% to GDP, slightly above the 3.9% reported for medium-sized enterprises. Overall, in January-September 2019, the volume of gross value-added produced by small and medium-sized firms increased by 10.8% compared to the

<sup>&</sup>lt;sup>1</sup> EBRD's definition of CA: Kazakhstan, Kyrgyzstan, Mongolia, Tajikistan, Turkmenistan, Uzbekistan.

<sup>&</sup>lt;sup>2</sup> The OECD defines *shuttle trade* as the activity in which individual entrepreneurs buy goods abroad and import them for resale in street markets or small shops. Often the goods are imported without full declaration in order to avoid import duties.

corresponding period in 2018 – largely linked to growth in the wholesale and retail trade sectors (National Statistical Committee, 2019<sub>[12]</sub>).

As of September 2019, 12 000 small and medium-sized enterprises were operating in Kyrgyzstan, 11 300 of which were small enterprises; only 700 were medium-sized firms. Overall, private firms employed 84 000 people. Both the number of SMEs and SME employment are declining (the number of employees fell from 15 300 in 2018). The number of individual entrepreneurs, on the other hand, has been increasing (up by 2.8%), reaching 401 700 in 2019 (National Statistical Committee, 2019[12]).

# The COVID-19 had a deep impact on the key economic drivers of the country and prompted more private sector support

The COVID-19 pandemic coupled with the simultaneous fall in commodity prices further exacerbated some of the structural weaknesses of the Kyrgyz economy, in particular the dependence on gold exports, trade and remittances. Kumtor continued operations under COVID-19, albeit under strict hygiene protocols, and by end March 2020 reported a 37% higher output for the same period in 2019 – mostly linked to gold prices, which in April 2020 were 13.7% above the levels of late 2019. Overall Kyrgyzstan exported an additional 11.6% of gold in the first quarter of 2020, compared to the same period last year. Even so, the border closure with China hit trade flows hard, as 36% of imported goods originate from China. Chinese imports dropped by 27% in the first quarter, year on year. Reduced trade, also with Central Asia counterparts, led to a 20% drop in border revenues. The National Bank of the Kyrgyz Republic (NBKR) maintained its flexible foreign exchange regime under COVID-19, whilst undertaking limited FOREX interventions in order to prevent sharp exchange rate fluctuations.

Remittance inflows in the first quarter dropped by 15% compared to the same period last year, due to border closures and strict confinement measures in Russia, the main destination for Kyrgyz labor migrants. Immediately after the COVID-19 outbreak, an estimated 600 000 Kyrgyz migrants were stranded in Russia, forced to reside in unsanitary conditions, awaiting government support to return.

In present conditions, it is hard to assess the size of the formal private sector in Kyrgyzstan, with many businesses facing immediate liquidity shortages and unforeseen closures. According to the Ministry of Labour and Social Development, in April 2020, an estimated 1.8 m workers (out of 2.6 m workers) faced unemployment. The exact impact of COVID-19 on Kyrgyzstan's private sector thus remains to be seen, but experiences in OECD countries suggest that SMEs will be among those most affected, thus requiring targeted government support (see box 1).

#### Box 1. Supporting the private sector amidst COVID-19

Following the first identified COVID-19 cases in Kyrgyzstan, the government declared a country-wide state of emergency, including curfews, movement restrictions and quarantine measures across the country, which directly affected business activities. Trade largely halted, except for the import of essential goods.

The government has endorsed measures to support the recovery of its economy, and announced subsequent support packages to cushion its private sector. Economically,

Kyrgyzstan was affected by COVID-19 rather early, owing to its business linkages with China, so it introduced a 3-month business support package, with immediate measures, including extending the deadline to submit tax declarations and social contributions, and suspending audits and sanctions for all businesses. It also introduced a temporary ban on bankruptcy procedures for businesses until January 2021, as well as a deferral of loan repayments, and it froze prices on essential goods. Rents and utility payments were deferred.

On April 30, the government followed up with the adoption of the *Act on New Economic Freedom and Development*, with numerous measures for both immediate support and long-term recovery:

- taxation: reduction of social contributions, introduction of a social tax and transition to a funded pension system, reduction in the number of taxes and inspections;
- simplified business operations: reduction of licenses, ban on increasing number of licenses:
- enhanced access to finance: preferential financing for SMEs and patent-holders in export-oriented, processing and food security sectors; and
- other structural measures for investors and for the economy: minimum threshold credit lowered, revision of tariffs, launch of new infrastructure projects, adoption of a new investment code and enhanced protection of private property rights and guarantees for investors, and extension of privatisation across the country.

The government of Kyrgyzstan faces a challenging budgetary situation following the outbreak of COVID-19, with 20% less revenue by April 2020 compared to the same period last year. Lower remittances, reduced domestic revenue collection and export revenues put an immediate strain on public finances. The IMF projects a widening of the public deficit to 8.8% of GDP. In March 2020, Kyrgyzstan foresaw its public debt increasing from 54.1% in 2018 to 69% of GDP by the end of the year. The government therefore requested USD 400m budget support from the IMF, applied for temporary debt relief from the Paris Club, and initiated negotiations with China (66% of its debt is owed to China). Against this backdrop, the government will have to prioritise its support mechanisms, including digital efforts, as it seeks to reduce public expenditure by 25%. Immediate expensing or accelerated tax depreciation measures for a short period of time could be considered to support investment, but the government will also need to resist the temptation to implement these permanently (OECD, 2020<sub>[13]</sub>).

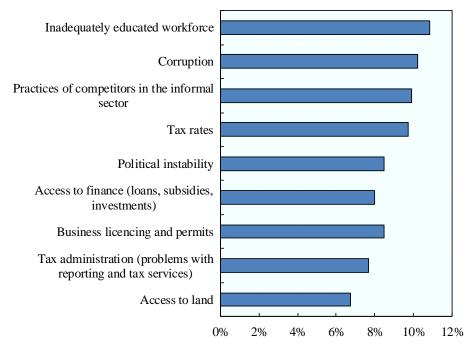
# Firms operate in a challenging business environment with barriers to formalisation and growth

Private firms in Kyrgyzstan struggle with a challenging business environment. In the World Bank's *Doing Business* assessment, Kyrgyzstan ranked 70<sup>th</sup> out of 190 countries in 2019, below neighbouring Kazakhstan (28<sup>th</sup>) but ahead of Uzbekistan (76<sup>th</sup>) and Tajikistan (126<sup>th</sup>). Some indicators remain particularly low, including those for access to electricity (174<sup>th</sup>), paying taxes (150<sup>th</sup>) and enforcing contracts (131<sup>st</sup>) (World Bank, 2019<sub>[13]</sub>). MSMEs face somewhat different challenges: In the survey conducted for this report, MSMEs in Kyrgyzstan identified a lack of needed skills in the labour market, corruption,

and competition from the informal sector as the main problems with the business environment.

Figure 2. Perceived obstacles to doing business in Kyrgyzstan

Which of the following would you consider the biggest obstacles to doing business in Kyrgyzstan?



Source: OECD survey, 2019.

High levels of corruption are also cited in other enterprise surveys and targeted interviews. It is further reflected in Kyrgyzstan's rankings by Transparency International and the EBRD-World Bank Business Environment and Enterprise Performance Survey (BEEPS), which finds that the frequency of bribery incidences in Kyrgyzstan is very high compared to both the Central Asian and BEEPS averages, at 31.4% for all firms, compared to 11.3% in Europe/ Central Asia and 17.2% in all countries (BEEPS, 2019<sub>[14]</sub>). Corruption, however, creates an important "implementation gap" between the *de jure* institutions and policies put in place to ensure the effective delivery of public services and the *de facto* operation of the public sector. This gap partly explains the discrepancy between Kyrgyzstan's claim to have the "lowest tax rate in the region" (Investment Promotion and Protection Agency, 2019<sub>[15]</sub>) and the frequent concerns raised by the business community, not only about tax rates but about interactions with tax authorities in general (World Bank, 2019<sub>[13]</sub>).

Partly as a result of these conditions, the informal sector is large; in 2017 it was estimated as 23.6% of GDP (EBRD, 2019<sub>[11]</sub>). In the 2019 Enterprise Survey, 51% of firms indicated that they faced competition from unregistered or informal firms, compared to 39% in Europe and Central Asia (BEEPS, 2019<sub>[14]</sub>). A large informal sector disadvantages formal businesses, while those engaged in the informal economy are particularly vulnerable, with an estimated 40% falling below the national poverty line (OECD/ILO, 2019<sub>[16]</sub>).

The main issues that explain the prevalence of informality – cumbersome administrative procedures, taxation, corruption, political instability and weak enforcement (Loayza, 1997<sub>[17]</sub>; Martinez and Williams, n.d.<sub>[18]</sub>) – correspond closely to the key challenges cited

by the firms surveyed for this report (Figure 2). Businesses also report being burdened by overcomplicated procedures and informal profit-seeking during interactions with various public offices (Chamber of Commerce and Industry, 2019<sub>[19]</sub>). These barriers – on top of irregular inspections, high tax rates and the inability to efficiently access critical services – impede private sector development.

To counter these barriers, the government initiated the 100 days of reforms in 2008, aiming at reforming selected indicators to ease doing business. Reforms included the introduction of a new tax code as well as the reduction of regulatory authorities (from 21 to 12) and of licenses required (500 to 101). Further, numerous laws<sup>3</sup> affecting entrepreneurs were amended and strategic programmes introduced, leading to simplified business registration procedures and licensing and permitting procedures (Hasanova, 2019<sub>[20]</sub>).

In order to encourage agents to formalise, the government has further introduced the *individual entrepreneurship* status,<sup>4</sup> which slightly differs from the sole proprietorship status commonly used in other countries in that it gives entrepreneurs access to a "patent" system that is less bureaucratic in terms of procedures and preferential in terms of taxation (Box 2). In this context, a patent is unrelated to technical patents, but remains a simple feebased certificate allowing individuals to operate formally. Instead of income and losses being taxed on the personal or business income tax return, the payment of the patent suffices for tax purposes. Due to these benefits, the status may create disincentives for firms to grow because, by registering as a micro or small business and losing their status, they cease to benefit from the preferential tax regime.<sup>5</sup>

#### Box 2. Individual entrepreneurship and the patent system

Individual entrepreneurs in Kyrgyzstan essentially operate on the basis of patents. In some sectors, such as textiles, they are legally allowed to employ up to 75 employees. In all other sectors except agriculture, individual entrepreneurs may have up to 35 employees (Ministry of Justice,  $2007_{[21]}$ ).<sup>6</sup> An individual entrepreneur with a patent is not required to report to the tax authorities and needs only to purchase a patent and then keep extending its validity period, which varies from 30 to 180 days. The patent holder is neither asked to keep record of income and expenses nor required to pay income tax. More than one million patents were issued in 2018, generating around 3.2% of total tax revenue. The number of issued patents has been increasing constantly, with a decrease in the share of collected taxes.

The effects of the patent system are complex. Patents stimulate growth and semiformalisation of individual entrepreneurs. However, they also encourage individual

<sup>&</sup>lt;sup>3</sup> Laws on State Support of SMEs (2015, 2017), on Inspections of SMEs (2011-2017), on Protection of Entrepreneurs' Rights (2013-2017), on Guarantee funds (2017), on Competition (2013-2017), and on Natural Monopolies (2014-2017).

<sup>&</sup>lt;sup>4</sup> This status refers to individuals who engage in entrepreneurial activities without forming a legal entity.

<sup>&</sup>lt;sup>5</sup> Provided that gross revenues do not exceed the annual registration threshold for value added tax specified in the Tax Code of the Kyrgyz Republic.

<sup>&</sup>lt;sup>6</sup> Industry: 35; construction: 75; transport: 35; agriculture: 50; scientific-technical: 25; wholesale: 30; retail and customer service: 25; other: 25.

entrepreneurs to stay small and discourage full entry into the formal economy, where the requirements are more complex.

Initially, the patent system was introduced in 2006 as an incentive for companies to formalise in the government's attempt to remove barriers to formalisation. However, it has been observed that entrepreneurs prefer to remain under the simplified regime to reduce the costs of tax accounting and tax payments, and therefore lack an incentive to grow to the extent that they re-enter the general tax regime. According to the World Bank, SMEs take advantage of the relatively high turnover threshold for the patent system and organise part of their activities in the informal economy or under what would otherwise be commercially counterproductive arrangements (e.g. splitting up firms), so as to remain in the patent system. The World Bank concludes that the current tax system constitutes a barrier to firms' growth and recommends a further simplification of the simplified tax regime along with a reduction of the turnover threshold for the patent system.

The ILO also carried out a study on the effect of the patent-regime in the garment industry in Kyrgyzstan and found that although the patent system fostered formalisation, it encouraged businesses to stay small, with the industry being highly sensitive to changes in the patent system. It therefore acknowledges that changes to the patent system could generate costs and insecurity among garment producers.

Although the individual entrepreneurship and patent system foster formalisation, they may simultaneously discourage firms from growing. Its net impact is therefore unclear.

*Sources:* (State Tax Service, 2019<sub>[22]</sub>; IFC, 2017<sub>[23]</sub>; World Bank Group, 2010<sub>[24]</sub>; ILO, 2012<sub>[25]</sub>; Kalikova&Associates, 2019<sub>[26]</sub>; Hasanova, 2019<sub>[20]</sub>)

Although the informal economy may create jobs and basic income, it simultaneously diminishes economic opportunities for those engaged in it. Undertaking informal activities automatically acts as a barrier to higher productivity, as informal firms aim to remain "under the radar" of the government in order to evade punitive measures. A large informal sector reduces the tax base and increases the burden on formal firms, thus distorting competition. Moreover, it is difficult – often impossible – for informal firms to undertake investments that might enable them to raise productivity. The social dimension is also considerable, as informal jobs lack social protections, resulting in considerable economic and social vulnerabilities (De Soto,  $1990_{[27]}$ ). In fact, informal workers tend to face a larger risk of falling into poverty, as they lack social protection policies (OECD/ILO,  $2019_{[16]}$ ).

During the outbreak of COVID-19, Kyrgyzstan's informal sector has seen these risks materialise. Informal workers typically have poorer access to social protection and essential services, lower savings (and thus income-replacement potential), less opportunity to telework and greater risk of poverty. Informal businesses also benefitted less from immediate government support programmes, which mostly focused on enhancing access to finance for formal firms, or deferred tax, rent and utility payments – though many informal firms may benefit from the last two measures. Lack of support to informal businesses reflects both limited fiscal space and the difficulty of grasping the real composition of the informal sector.

In order to decrease informality, the government must tackle the broader structural challenges affecting the business climate in the country. Simplified and low-cost business registrations and the issuance of permits and licenses through more efficient public business development services (BDS) can play an important role in this formalisation effort.

# Public and private business development services can support firm creation and growth

Businesses in Kyrgyzstan face a challenging business environment. Government efforts and reforms to improve the business environment have to continue in order to ensure the competitiveness of the country's private sector *vis à vis* international and neighbouring competitors. In addition to these efforts, better service provision to businesses (G2B and B2B) can both boost firm creation as well as enhance business development and growth. This report therefore seeks to provide an understanding of the current BDS landscape in Kyrgyzstan by looking at the public and private provision of services to businesses, as well as the needs that businesses express for these services.

Business development services (BDS) usually refer to services which "improve the performance of the enterprise, its access to markets, and its ability to compete" (OECD,  $2016_{[28]}$ ). BDS may be either private or public. *Private* BDS include consulting, training, advisory services, marketing, technology development, and business-linkage promotion (OECD,  $2017_{[29]}$ ). Such BDS are thus mainly business-to-business (B2B) services that tend to address economic, legislative, and regulatory issues that firms (particularly start-ups and small firms) may struggle to address without external support. BDS in such areas as human resource management, legal services, marketing, export and innovation provide businesses with the opportunity to outsource tasks and focus on their core competencies. They also offer businesses help to innovate, expand and internationalise (OECD,  $2012_{[30]}$ ; OECD,  $2017_{[31]}$ ). Evidence from OECD countries suggests that firms making use of BDS are more likely to succeed than their counterparts (OECD/EU,  $2014_{[32]}$ ; OECD et al.,  $2015_{[33]}$ ). Business advice, in particular, has a positive impact on firm performance (OECD, 2018, p.  $8_{[34]}$ ).

This report also addresses the provision of *public* BDS delivered by government institutions – so-called "government-to-business" or "G2B" services. These include services such as allowing firms to register and act as legal entities, paying taxes or obtaining relevant licenses. Table 1 provides an overview of selected business development services in Kyrgyzstan, and their usual delivery channels.

Table 1. Selected business development services and their usual delivery channels

Public (G2B) services	Private (B2B) services
Work permit	Consulting and advisory services
Business registration	Training and technical assistance
Registration of land mgmt. affairs	Policy and advocacy support
Delivery of tax reports and tax declaration	Marketing assistance/ Support for technology and product development
Data issuance	Market access services/ Promoting business linkages

Source: (JICA, 2019<sub>[35]</sub>; European Commission, 2002<sub>[36]</sub>).

BDS are particularly important for small firms and individual entrepreneurs that wish to create or grow their businesses. MSMEs experience more challenging conditions with respect to market access and resources, ranging from finance to skills and networks (OECD, 2017<sub>[31]</sub>). Since they lack the human and financial resources to handle many of these functions internally, MSMEs tend to be more reliant on external support than larger enterprises. Having less capacity to provide training to employees, they also often exhibit higher skill deficiencies.

## The government has made BDS a policy priority, but results have so far been limited

In its *Development Programme* (2018-2022), the Ministry of Economy acknowledges the important role of MSMEs in the economy, while also recognising the numerous challenges they face, including a lack of public financing, burdensome regulations, limited information and an unstable legal environment (Government of Kyrgyzstan, 2018<sub>[37]</sub>). As part of its plan for improving the regulatory framework for businesses, the government is committed to initiatives designed to improve both public and private business development services.

## The government is setting up business service centres

Public service provision in Kyrgyzstan is heavily concentrated in urban areas, with all licensors located in Bishkek. This, as well as the fact that no unified whole-of-government one-stop shop exists, creates a substantial administrative burden and leaves entrepreneurs confused: in recent surveys, 45% of entrepreneurs expressed difficulties in knowing where to obtain the public service they need. To counter this, the government is aiming at improving its service provision to businesses, both digitally and physically (JICA, 2019<sub>1351</sub>).

As part of this effort, the government recently published plans indicating the establishment of business service centres in several regions of the country. The government aims to achieve this by co-operating with international donors and the private sector through public-private partnerships. These efforts would build on existing ministry- or agency-specific one-stop shops, better known as *single windows* (examples are the Single Window of the Tax Authority and the Centre for Single Window in Foreign Trade).

Where a physical (as opposed to on-line) presence is required, ensuring that offices of private B2B providers – such as house training providers, consultants and banks – exist in the same business service centres would complement efforts to provide a whole-of-government one-stop shop. However, this concept is still in development. The Ministry of Economy's goal is to use the centres to simplify government interactions with businesses while building synergies with the efforts of other public and private institutions, as well as the development community.

Current initiatives include the introduction of entrepreneurship centres in Osh, Batken, and Jalalabad. These centres, planned together with the OSCE, will support entrepreneurs with physical and digital administrative procedures. Public services will be bundled and offered digitally through a digital government platform called *Tunduk*, which facilitates electronic inter-institutional services and communication in five areas: education and training, information services, government services (including licenses and permits), financial services and consulting.

Plans to establish a business service centre in Bishkek have been developed based on a feasibility study by the Japan International Co-operation Agency (JICA). The centre is to be established by the Ministry of Economy and JICA and will consist of two components:

a) government services to businesses, including 31 public services; and b) business training and educational courses. The development community and the private sector will be able to offer their own training services within the centre (JICA, 2019<sub>[35]</sub>).

While not focused on businesses *per se*, there are public service centres that offer general services to citizens, such as passport registration. The first of the so-called *Tson* centres was established in 2011 with the aim of automating processes regarding passport issuance. In 2015, a working group was established with the aim of optimising the centres. A survey conducted to assess satisfaction with the centres under the aegis of the working group led to a reduction of the number of centres from 55 to 41.

## Other BDS providers aim to fill the delivery gap, but uptake remains limited

The private BDS market remains mostly targeted towards larger firms. Interviews with suppliers confirmed this, as they expressed a preference for medium-sized or large firms, linked to their ability to pay for services. When comparing expenditures for BDS, medium-sized firms reported having spent 8% of their revenue, compared to 1% for small firms. Survey data show that BDS are used less by micro firms and individual entrepreneurs; individual entrepreneurs expressed the least uptake, far behind all other firm sizes. This is problematic considering that individual entrepreneurs and small firms make up most of Kyrgyzstan's private sector. Hence, 60% of businesses surveyed for this report had not received any BDS. However, this differs according to the type of BDS – entry barriers seem smallest for training, which had reached 40.8% of companies, while the use of external advisory services and external information was much lower, with 26.9% and 22% respectively. Of those that had used BDS, the largest group of respondents (49%) had received BDS through private providers, followed by the government (16%), business associations (15%) and NGOs (13%).

When asked the reasons for the low uptake of BDS, MSMEs cited high pricing (24%) and the difficulty of finding the services they needed. More than a third of businesses had tried to obtain BDS, but could not find the appropriate services. Small companies struggled most to access services, and firms located outside of the urban centres could not find BDS, as provision is heavily concentrated in Bishkek, Osh, Jalal-Abad and Chuy.

The low level of BDS uptake may also be linked to limited awareness of the benefits of BDS. The survey revealed that the majority of businesses have little awareness of BDS in Kyrgyzstan, both in terms of being aware of providers as well as in understanding the added value for their business. Of the various types of BDS, businesses were most aware of financial management services.

Despite the limited uptake, all businesses expressed a need and willingness to pay for BDS. Sales and marketing was noted as the most important business need across all business sizes, sectors and regions, followed by legal issues and regulations. In particular, individual entrepreneurs and micro firms – those showing the least uptake – expressed the greatest needs and weakest competencies throughout the OECD survey. The presence of specialised staff in a business increased with firm size, but was highly dependent on the topic area. Firms tend to have more staff specialised and training opportunities in financial management, whereas sales and marketing are lagging behind on all fronts.

## Recommendation 1: Improve the accessibility and efficiency of public services

## Challenge 1: G2B services are scattered and involve multiple procedures

Public services for businesses include, but are not limited to, business registration and the issuing of licenses and certifications (Table 1). They are offered by a wide range of different government agencies and ministries. This dispersion generates additional transaction costs. Businesses interviewed and surveyed by the OECD indicated a need for efficient and transparent public services. Of the businesses surveyed, 45% cited difficulties in knowing where to obtain public services, and only 22% had contacted state bodies to seek information on public services (JICA, 2019<sub>[35]</sub>).

Streamlining administrative processes and public service provision could reduce administrative burdens on MSMEs, enabling them to focus on core activities and lowering barriers to entry, growth and innovation. Increasing reliance on digital services can also, by reducing face-to-face interaction with officials, decrease opportunities for corruption, as well as transaction costs incurred by entrepreneurs and firms. Against the backdrop of COVID-19, they can support more convenient provision of services without risk of infection.

## Registration procedures have improved, but licensing and certification remain cumbersome

The 2015 Law on State Registration of Legal Entities authorises the Ministry of Justice to declare the registering firm as a legal entity. This is then automatically recorded with three other governmental bodies, including the National Statistical Committee, the State Tax Inspectorate, and the Social Fund. This process occurs at the Ministry of Justice's central "one-stop shop" (OSS) or one of its seven regional offices; application forms are on the ministry's website. This process is completed in five business days for a fee of KGS 407 (registration fee) and KGS 20 (bank processing fee), which amounts to approximately USD 6 (World Bank, 2019<sub>[38]</sub>; Kalikova&Associates, 2019<sub>[26]</sub>).

Although information regarding registration of domestic businesses can be found on the Ministry of Justice website, the interface is difficult to navigate, with additional steps required for various legal documents (World Bank, 2019<sub>[38]</sub>). Since early 2019, a pilot procedure has allowed businesses to register online as legal entities using ID cards and smart cards<sup>7</sup>. This system is being tested until January 2020, the goal being to subsequently launch it nationally (Ministry of Justice, 2019<sub>[39]</sub>).

Additional licenses, certificates and permits are required to operate the business, build new structures, and import, amongst other activities. In the ideal case, the process of obtaining them is transparent and does not financially constrain the applicant. In Kyrgyzstan, the *Law on the Licensing System in the Kyrgyz Republic* of November 2014 (with amendments of May 2017) outlines 65 categories that require licenses as well as 36 permits that can be requested, in line with Tajikistan's 65 areas of economic activity requiring a license (Government of Tajikistan, 2018<sub>[40]</sub>). However, the supplementary legislation has not yet been amended in accordance with the original law, thus creating contradictions and

<sup>&</sup>lt;sup>7</sup> The Cambridge Dictionary defines smart cards as a tool to make payments and store personal information, which can be read when connected to a computer system.

confusion for entrepreneurs (Hasanova,  $2019_{[20]}$ ). Although the number of licenses and permits is in line with regional norms, it is still high compared to OECD countries.

While the number of licences and permits in itself can be a useful rough measure of the regulatory burden for businesses, the transparency regarding these regulations and licences is a key indicator of the ease of businesses' interactions with public service providers. In order to assess this, the OECD has developed the *Regulatory and Administrative Opacity assessment*. It is also concerned with licensing and permits, where the index assesses the application of the silence is consent rule, as well as single contact points for getting information or for issuing licenses and permits. On a scale from 0 to 6, with 0 being the least opaque, Kyrgyzstan would rank at 6, compared to the average of 1.88 in OECD countries (OECD, 2018<sub>[41]</sub>).

The law on the licensing system specifies which governmental authority issues the relevant license and stipulates that the issuance of the license shall take 30 calendar days. Despite the law, however, Kyrgyz businesses expressed difficulty in knowing which authority handles which licensing and permit category (JICA, 2019<sub>[35]</sub>). Particularly if businesses require several licenses, it is highly possible that these are offered by numerous issuing bodies, adding time and costs for the business (Kalikova&Associates, 2019<sub>[26]</sub>). To counter this, Kazakhstan and Tajikistan have put in place single electronic registries for licenses and permits, so applications can be transferred to the relevant authorities, thereby shifting that burden from businesses.

Corruption in the provision of licenses, particularly in the mining sector, has brought about uncertainty for businesses. 2019 BEEPS data confirm regular informal payments: in the case of construction-related permits, the percentage of firms expected to give gifts rose from 43.1% in 2013 to 47.6% in 2019. In the case of import licenses, 6.7% of firms are expected to give gifts, in line with the Europe and Central Asia average of 7.2%. This figure stands in contrast to 29% expected to give gifts to obtain an operating license, higher than the 17.1% average in Europe and CA (BEEPS, 2019[14]).

The State Migration Service, the Ministry of Justice, the State Registration Service, the State Tax Service, the Agency on Advance and Protection of Investments and the State Legal Assistance provide other G2B services. The wide range of government institutions with which businesses must interact creates uncertainty and makes it difficult to locate the necessary documents (JICA, 2019<sub>[35]</sub>). These problems are compounded by low levels of government efficiency and poor co-ordination among the agencies and ministries involved. While Article 15 of the *Law on State and Municipal Services* codifies the rules on state services, it fails to provide clear legal guidance for the co-operation between state bodies.

In addition to uncertainty about where to obtain the necessary documents, businesses face costs arising from the fact that public service provision is heavily concentrated in metropolitan areas. This disadvantages entrepreneurs located in rural areas as they are forced to travel to government offices, which are often several hours drive away. Indeed, license-granting institutions are located only in Bishkek, which imposes substantial costs on firms located far from the capital (JICA, 2019<sub>[35]</sub>). This makes public service provision hard to access and unpredictable.

<sup>&</sup>lt;sup>8</sup> 2013: Regulatory and administrative opacity: index scale from 0 (least restrictive) to 6 (most restrictive)

#### Digitalisation efforts are further accelerating in the COVID-19 context

Kyrgyzstan has already revealed a strong trend in digitalising its government, as captured by the *e-Government Development Index*, which measures the readiness and capacity of national institutions to use ICTs to provide public services. Kyrgyzstan was ranked amongst the top 10 reforming countries in 2018, along with Uzbekistan and Kazakhstan. This upward trend was largely carried by a higher e-participation index, with enhanced access to information and increased citizen's involvement in the decision making process.

Recent reforms have the potential to improve the situation. For example, in order to prevent entrepreneurs from submitting identical reports to different state bodies, the state enterprise "Tunduk" co-operated with the National Statistical Committee, the State Tax Service and the Social Fund to combine and simplify the reporting forms for submission in electronic and paper form by entrepreneurs. The resulting unified reporting system is being built so that entrepreneurs submit reports to one state body, and other departments will receive the information they require through data exchange facilitated by Tunduk. In a similar vein, the State Tax Service and the Public Procurement Department under the Ministry of Finance in June 2019 eliminated the need to provide paper documents on the absence of tax debts of legal entities and individuals on the public procurement portal. Further government plans are in place to eliminate paper documents for government services.

In addition, the government is implementing the project *Government as a Platform*, which aims to develop digital services through the involvement of the private sector and the parallel development of digital payments. Interaction of information systems and data exchange on the platform is carried out through the Tunduk system. The State ICT Committee implements the platform together with a team of IT state enterprises as well as telecommunication companies and banks. The Platform automates the interaction between the state, the private sector and citizens, and provides a digital solution for receiving and paying for a wide range of public, municipal and private services.

As of October 2019, 73 national and municipal services – several of which are relevant to (small) businesses – are accessible through mobile phone applications of communication operators. Furthermore, 37 public services are provided digitally through the state electronic services portal, including services such as obtaining certificates of tax debt, tax registration, or payment of fines. By the end of 2019, the plan was to launch 189 services, reduce lines in public service centres by 30%, cover up to 500 000 users, and increase the level of user satisfaction by 80%.

#### Box 3. Kyrgyzstan's digitalisation efforts in response to the COVID-19 crisis

The outbreak of the COVID-19 pandemic provided a strong incentive for the government to accelerate its digitalisation agenda, with the increased, sudden need for reliable digital information and online government services. The government moved quickly to provide accurate, useful and up-to-date information and public services to its citizens through its national portal, mobile apps and social media platforms (Telegram and Facebook). Some of the key new services provided in immediate response to the pandemic included:

- the expansion of the electronic fiscal system by July 2020;
- issuance of an electronic permit for vehicles and residents in Bishkek in order to regulate movement during the curfew;

- the possibility to fill an online application to receive humanitarian aid in the form of food baskets through Tunduk;
- the introduction of a digital notary system starting from 1 March; and
- the incorporation of 85 additional government services into the *Government as a platform* programme.

Beyond rapid reaction mechanisms, the government is planning on establishing a new platform "Sanarip Aimak" (Digital Region) in all regions of Kyrgyzstan for the full exchange of information data between the government and municipal agencies. Under the *Act on New Economic Freedom and Development*, the government has also approved the use of 3 500m SOM (approximately USD 6m) for the digitalisation agenda in 2020, which will be used for the development of cashless payments, the expansion of digital services to businesses, particularly for tax payments and the transition to fully digital audits.

Recommendation 1A: Establish whole-of-government one-stop shops for businesses, possibly leveraging existing business service centres

# Provide key government services to businesses in physical and digital one-stop shops

One-stop shops allow applicants to obtain government services in one location that is as accessible, and has as few points of contact, as possible (OECD, 2008<sub>[42]</sub>). They are intended to accelerate and simplify the process of starting a new business; to grant necessary permits and licenses in a comprehensive manner; and to offer information on administrative and other procedures, the legal framework, and the investment climate (OECD, 2008<sub>[42]</sub>). In addition to making life simpler for entrepreneurs, one-stop shops can improve the co-ordination of the various government departments involved in delivering G2B services (World Bank, 2009<sub>[43]</sub>).

One-stop shops can also support business formalisation, considering they lower the time and cost of obtaining government services. In fact, the more cumbersome the registration procedure, the fewer registrations occur (OECD, 2008<sub>[42]</sub>). Studies show that weak or overcomplicated public services may reduce the incentive to formalise. High entry costs, the high cost of remaining legal, and generally complex administrative procedures create disincentives for entrepreneurs to formalise (Loayza, 1997<sub>[17]</sub>). Informal firms remain informal in order to circumvent burdensome regulations, the tax system and government interference (Friedman, 2014<sub>[44]</sub>). Small firms, in particular, consider fiscal obligations when deciding whether to register as they are more often affected by complex procedures and taxes compounded by a lack of information (OECD/ILO, 2019<sub>[16]</sub>).

In Kyrgyzstan, the business community has expressed a strong desire for a network of OSS. In a recent survey of around 400 entrepreneurs, 85% of respondents asked to receive public services in a one-stop shop and 84% requested these digitally (JICA, 2019<sub>[35]</sub>). The Ministry of Justice offers a limited OSS only for business registrations, however. It does not provide services from other ministries and agencies and is therefore unable to offer consolidated, whole-of-government service provision to businesses. Expanding the range of services offered – and thereby establishing a network of fully-fledged one-stop shops across the country – would thus be a welcome step and could be undertaken in partnership with private

players. Kyrgyzstan should aim to establish whole-of-government one-stop shops. This could be undertaken in partnership with the development community or private providers.

Experiences from the citizen service centres Tson can help identify ways to scale up services while remaining cost-effective. In the case of one-stop shops located in rural areas, other methods for the provision of public services are required. The cases of Georgia (Box 4) and Uzbekistan (Box 5) serve as an example of co-operation between the central government and municipal authorities in the delivery of services.

In terms of public-private co-operation for the provision of BDS, useful but not sufficient steps are underway, for instance, the Ministry of Economy and JICA have co-developed a plan to establish a business service centre in Bishkek. In this context, the two partners have prioritised selected public services. This has been achieved based on a feasibility study and a business survey. For the provision of licenses and services, the plan envisages the presence of twelve state agencies and ministries<sup>9</sup>. In order to increase the usefulness for users and to cross-finance the operation, the plan also aims to include private providers of BDS on the premises of the business service centre.

<sup>&</sup>lt;sup>9</sup> State agency on the regulation of fuel and energy complex, construction state agency, architecture and housing and public utilities, Ministry of Agriculture, Ministry of Health, Ministry of Economy, state migration service, state registration service, state tax service, Ministry of Justice, Agency on advance and protection of investments, state legal assistance.

#### Box 4. Georgia's one-stop shops

Georgia faced similar issues as Kyrgyzstan before the government decided to enact measures to improve the business environment. Supported by the donor community, these efforts catapulted Georgia to 6<sup>th</sup> place in the World Bank's *Doing Business* ranking.

In order to offer efficient and widespread public services, the government established public service halls and community centres – all functioning as one-stop shops for public services. Each public service hall currently offers up to 400 services, bringing together the services provided by the Civil Registry Agency and the National Agency of Public Registry, the National Archives, and Bureau of Enforcements as well as the Notary Chamber.

The community centres have the same delivery model as the public service halls but are operated and maintained by municipal authorities. Evaluations have characterised this model as being simple and transparent, particularly since the introduction of ICT solutions to the delivery of services. Between 2012 and 2014, 14 public service halls were opened across the country, serving up to 18 000 individuals per day, with an average waiting period of 5 minutes and service time of 6-7 minutes. Evaluations and customer satisfaction surveys are undertaken on a daily basis, allowing for continuous improvement of the delivery process. With public backing, the government has also embarked on a strong anticorruption drive and used large foreign investments to improve both physical and digital public services in the country.

Sources: Login Asia (n.d.[45]), Kakachia and O'Shea (2012[46]), OECD et al (2016[47])

A number of areas will have to be taken into account when setting up a one-stop shop:

1) **Organisational responsibilities and resources:** an assessment of government coordination in Kyrgyzstan is needed. A whole-of-government approach is then required to streamline procedures and simplify licensing and registration, to further work on cutting red tape. Ministries and all relevant agencies shall be included in this review process, which will feed into the OSS plan for approval processes. Themes to discuss are: division of labour, guidelines, when the various ministry need to get involved, and how information and data are shared. In order to decide upon these topics and align approaches, best practice recommends conducting regular face-to-face meetings between ministry executives and future OSS employees (OECD, 2008<sub>[42]</sub>).

Examples in OECD countries show that some of the actors involved may resist collaboration and the integration of systems, which may block the establishment of the OSS from the start. This occurred in Scandinavia, New Zealand and Canada, where specific ministries denied approval processes to one-stop shops, as they did not agree with the delegation process or feared the monopolisation of funding. To counter this, scholars recommend making all actors aware of the benefits of sharing labour across horizontal and vertical levels. To mitigate rivalries in general, a reorganisation model is recommended in which all functions are included within one single agency; this agency can then decide on its working methods and act as an extended arm to the relevant ministries. Kyrgyzstan should therefore decide which agency or ministry is hosting this agency, and ensure that the agency "has a real policy advocacy function vis-à-vis the country's decision makers" (OECD, 2008<sub>[42]</sub>; Australia and New Zealand School of Government, 2017<sub>[48]</sub>). The recent experience of neighbouring Uzbekistan in rebuilding its system for public services (Box 5)

provides an instructive example of building an organisational structure with a strong mandate to co-ordinate and enforce inputs from the different ministries.

- 2) **Service delivery**: to realise a change in service delivery, a cultural transformation is required. Shared values amongst OSS employees are needed, and the willingness to offer a culture of service to the recipients of public services. Customer service promotion mechanisms, together with staff performance measures and quality audits, may shift work effort towards client service goals. A front runner in this area is Georgia, where all public service halls (its OSS) are run in a customer-centric manner. Customers give feedback after every session with the front office, and feedback can be submitted online at any point.
- 3) **Resources:** setting up physical or digital one-stop shops usually incurs significant costs, as governments are faced with: acquiring new spaces and buildings; marketing and branding the new services; reorganising staff and management, which includes potentially hiring new staff; offering training in new processes; setting up back-end administrative processing systems; and putting in place the web architecture necessary to offer a virtual portal. These costs should not be underestimated; the assumption that the costs are immediately offset through more efficient and digital processes has not proven correct. Implementation timeframes have usually been lengthy, as administrative processes have had to be adjusted and redesigned to cope with changing service delivery arrangements. It is thus crucial to design a realistic timeline, and pay equal attention to front and back office structures.

Given the government's limited budget, to mitigate costs it could build on existing structures, such as the Tson centres, and attach the OSS to them to jumpstart integrated service provision to businesses. Also, it could better define, adjust and harmonise the target models of existing structures such as the planned business service centres and similar initiatives. Another option would be to expand the existing Ministry of Justice OSS to include other G2B services offered by other ministries or agencies (Australia and New Zealand School of Government, 2017<sub>[48]</sub>).

Kyrgyzstan's geography, its low population density and thus the low critical mass for the development of businesses as well as weak road and rail connections (Pělucha and Kasabov,  $2020_{[49]}$ ) underline the need for a specific approach to service delivery in rural areas.

To tackle service delivery in rural areas, numerous OECD countries have introduced innovative policies such as delivering services in existing rural structures including post offices, supermarkets or municipal offices; and partnering with existing players such as local business associations. These existing rural service providers can also help the government to better understand the needs, potential locations and innovative delivery mechanisms which could work (OECD, 2010<sub>[50]</sub>). Other options for the delivery of public services in rural areas can also include the use of trucks and buses that are linked to public service agencies, such as in the example of Uzbekistan (Box 5).

#### Box 5. Uzbekistan's Public Services Agency and Public Services Centres

Created in December 2017 under the Ministry of Justice, Uzbekistan's Agency for Public Services established a unified state policy in the provision of public services to individuals and legal entities. This entailed eliminating unnecessary administrative procedures, establishing a unified registry of public services, and supervising the activities of state bodies and other organisations (assessing their effectiveness in the provision of public services and applying fines for officials of state bodies who have violated legislation). The Agency is partly funded through an extra-budgetary fund, and partly through a 20% share of the fees for the provision of public services. It reports to the Presidential Administration as well as the Ministry of Justice.

One-stop shops, titled Public Services Centres (PSCs), were established in 2018 and initially offered 37 public services – a number that is expected to increase to more than 160 by the end of 2020. The PSCs reduced the number of interactions between businesses and the public administration, whilst decreasing the risk of corruption. They further provide a single contact point for all requests to the government without the need to contact multiple agencies. Since their establishment, the PSCs have been already able to deliver more than six million services to businesses and citizens. In order to expand service delivery in rural areas, buses and cars are used to provide services, they are in turn linked to the 48 branches of public service centres in the country.

In order to fully establish the activities of the Agency and its regional departments, more than 30 legislative documents and by-laws had to be drafted or adjusted. This includes specialised regulations covering the agency itself, but also amendments and supplementations to the Administrative Code of the Republic of Uzbekistan. In addition, administrative regulations for the provision of public services provided at the Centres were developed, including guidance on the amount of time it should take users to use the service, documents provided, samples of completed questionnaires, and the required payment.

*Source*: Agency for Public Services under the Ministry of Justice of Uzbekistan, (Ministry of Justice of Uzbekistan, 2020<sub>[51]</sub>)

4) **Capability**: an important factor shaping a successful OSS is competent staff. This requires proper training and a long-term dedication to staff development. In addition, a clear division of labour has to be put in place: both the vertical division between those that oversee the OSS, and the horizontal division between those that implement the processes. One issue with OSS is "the range of staff capabilities needed to carry out all the processes involved in serving the target group of users" (Australia and New Zealand School of Government, 2017, p. 9<sub>[48]</sub>). To counter this, some OSS have put in place a "no wrong door" function, thus accepting all customers, and redirecting them to specialist services in case the OSS employees cannot answer their needs. Kyrgyzstan could aim to replicate this system by providing a well-trained front office capable of redirecting users with specialised needs while remaining the main point of contact.

## Co-ordinate the creation and future development of planned and existing business service centres

The business service centres described above can operate as one-stop shops, offering both public and private services in one place. It is crucial that the government ensures that these

service centres are in line with and complement each other, in terms of both services and the selection of locations. For the time being, the development community is trying to improve co-ordination of private-sector development projects, for instance by subdividing their regions of focus. In the short term, the government should co-ordinate with the development community in this regard to avoid project duplication and to ensure that services offered are aligned and administered where they are needed. Over the long-term, the government needs to disperse services regionally. For this, it could establish a board consisting of representatives of each business service centre. This would allow for continuous improvement, knowledge exchange, and better alignment of all centres.

The business service centres planned in co-operation with JICA or the OSCE are a good first step towards providing better and more efficient public services. As shown in the experience of Kyrgyzstan's business education centre (Box 6), it is important to plan ahead to ensure sustainability when external funds are no longer available. Centres should therefore be established within existing structures, physically in buildings that are already in place, and institutionally together with associations with experience in offering services. Furthermore, instead of subsidising 100% of the salaries or running costs, co-financing mechanisms should be put in place allowing for an easier transition period to a financially self-sustaining model.

#### **Box 6. Business Education Centre**

The Business Education Centre (BEC) was established in 2016 under the Chamber of Commerce and Industry, in co-operation with GIZ. Designed as a training centre, it addresses the educational needs of the business community in Kyrgyzstan. It predominantly operates in Bishkek, with infrequent outreach activities in regions. Its goals are:

- To provide high-quality fee-based services in the field of personnel capacity building for current and potential CCI members (conduction of training, lectures, workshops, master classes, internships);
- To facilitate transfer of the best international business education technologies;
- To address business needs in the field of business expertise and consultancy;
- To promote professional education reforms in the Kyrgyz Republic, as well as build a dialogue between the private sector and educational system.

GIZ in particular provided support in developing the concept and activity plan as well as providing constant advisory support. Starting from January 2019, the centre started working independently offering business education courses that are relevant to businesses and entrepreneurs, up-to-date and aligned with the best international standards, and feebased. Training courses cover such areas as export to the EU, public relations (PR) and marketing, tax system, illegal state inspections, and courses on food safety. The topics are designed after surveying CCI members and adapting topics accordingly. 1300 participants have attended educational events since 2016.

Challenges for the centre are to find good trainers, particularly for the regions. For the time being, most educational courses are offered either by non-Kyrgyz experts or experts from Bishkek who are urban-focused. This also raises the price of training courses, which could affect the sustainability of the centre. Furthermore, in Bishkek itself an oversupply of free training courses exists, offered by various development partners, putting pressure on other service providers to attract participants that are willing to pay. In order to motivate participants to take part and pay, the CCI conducts surveys on training needs and topics – an endeavour which could be replicated.

Source: Chamber of Commerce and Industry (2019[19]); GIZ.

## **Recommendation 1B: Digitalise public services for businesses**

## Develop a digital OSS for public (G2B) services

In addition to integrating the internal communications and processes of government bodies into the Tunduk system, the government should work on improving access to, and the visibility of, digital services within the business community.

In 2017, it was reported that a *National Business Portal* was to be launched as part of the National e-Services Portal. Such a portal could provide a single point of entry for businesses and could increase service uptake (National Institute for Strategic Studies, State Committee of Information Technologies and Communications and World Bank, 2017<sub>[52]</sub>). As of this writing (May 2020), no such separate portal has been established. However, multiple services, including information on certificates and tax debt, are already provided

(along with other services) on the general e-government portal: <a href="www.e.gov.kg">www.e.gov.kg</a>. At present, the portal serves as citizens' access point for selected G2B services, as well as citizen services such as passports, traffic fines, criminal records, pension entitlements and the registration of intellectual property. To use the platform, citizens can use their electronic identity cards (e-IDs) or log in via a token.

Creating a dedicated digital portal for public services relevant for businesses can make access to services more user-friendly and thus help increase their uptake within the business community. The portal should be business-centred and clustered around the needs of businesses at the different stages of their life cycles (formalisation/registration, expansion/change of company type, paying taxes and social contributions, export activity, closure of activities). The current plan revolving around *Government as a Platform* thus provides a good basis for co-operation between the private sector and the government, in order for businesses to feed into the creation of the digital portal.

The development of the platform should be receptive to feedback and continuously be developed in co-operation with the private sector (recommendation 2B). The *Government as a Platform* project, which aims to implement a feedback system through a built-in chatbot and online consultant, should be further pursued. New, simplified procedures should be better promoted, for instance through business associations, the media and other relevant channels (e.g. social media). In establishing such a platform, Kyrgyzstan could incorporate some of the key lessons from Mexico, whose experience provides a good example of how to design a business-centred platform in close co-operation and continuous dialogue with the private sector (Box 7).

#### Box 7. Mexico's business platform

Mexico's "Gobierno de México" e-government platform (<u>www.gob.mx</u>) was designed to provide Mexican citizens and businesses with an integrated digital platform for all government services, data, and tools.

Its development involved several phases. In 2014, an *alfa* (alpha) version was launched to research and identify citizens' needs. Consultations with civil society and private sector took place and their feedback was incorporated. Private-sector-orientated services were tested that same year, during which period user experiences were assessed, the platform was stress-tested, and design agility was examined, leading to further prototyping.

The site was then scaled up and launched in 2015, along with several built-in feedback mechanisms. A permanent management body, the Digital Government Unit, was established within the central government.

Gob.mx is now the sixth most visited website in Mexico, with 73 million visits, 39% of which are registered from mobile devices. Over 27 000 online petitions were submitted, and 4000 services are available. Additional agencies are being migrated to the platform.

Key success factors in the establishment of the platform include a strong legal framework as a prerequisite for successful development as well as its establishment by presidential order, ensuring sufficient political buy-in.

Source: OECD (2018[53]).

However, there are several barriers that may limit the uptake of the digital services offered. Socio-demographic factors, such as the education of users, can impact the eventual use of platforms. It is thus important to provide accessible and easily usable platforms, on top of teaching digital skills across the country. In addition, online training might be required to strengthen the capacity of some users.

Furthermore, across OECD countries, "broadband penetration and a high level of interactive service provision are important prerequisites for the provision and take-up of those services" (OECD,  $2009_{[19]}$ ). The data in Table 2 show that internet access in Kyrgyzstan remains limited, suggesting a continued, if declining, disparity between urban and rural areas (Freedom House,  $2016_{[54]}$ ). The Digital Central Asia South Asia (CASA) Program, which aims to expand digital access in selected countries of Central Asia, can work towards reducing this disparity, but government officials should keep in mind that a large number of entrepreneurs located outside urban centres will still prefer, or only be able to access, physical services (Singh,  $2017_{[55]}$ ).

Table 2. Mobile broadband subscriptions and internet usage have been growing

	Kyrgyzstan	Tajikistan	Kazakhstan
2019 Percentage of mobile connections that are broadband (3G - 5G)	55%	51%	76%
2019 Internet users as % of total population (penetration)	47%	26%	79%
2017 Cost of monthly fixed- line broadband subscriptions (in PPP\$ and as % of GNI p.c. <sup>10</sup> ), cap per month (in GB)	USD 8.4, unlimited (27.8 PPP\$, 8.9% of GNI p.c.)	USD 7.0, 15 GB (25.7 PPP\$, 8.5% of GNI p.c.)	USD 5.9, 10 GB (17.0 PPP\$, 0.9% of GNI p.c.)
2017 international bandwidth per capita (Kbps) <sup>11</sup>	65.4	2.1	87.2
2017 ICT development index (ranking out of 176 countries)	109	n.d.	52

Sources: DataReportal, ITU, UNPOG, ICT Development Index

Note: n.d. = no data

Although fixed-line broadband connections in Kyrgyzstan remain limited by international standards, this is mitigated by the high level of mobile internet penetration. One solution for users lacking access to adequate broadband and mobile data connections could involve the provision of basic terminals to selected rural (and to a lesser extent urban) areas that allow users without a stable internet connection to make use of the platform. Similar solutions already exist for citizen services provided through Tson.

<sup>&</sup>lt;sup>10</sup> 2% of GNI p.c. target set by the Broadband Commission for 2025.

<sup>&</sup>lt;sup>11</sup> For comparison, international bandwidth per capita in 2016 was 104.3 Kbps in USA and 796.2 Kbps in Singapore. Less than 10 Kbps per capita is considered to be virtually unstable and is a serious obstacle to growth.

#### Continue to digitalise internal government systems using Tunduk

The development of digital service provision and OSS requires the introduction of integrated digital systems across ministries that allow government agencies to share documentation and data easily. In order to operationalise its *Digital Kyrgyzstan* digitalisation strategy, the government has set up Tunduk, a state-owned Electronic Interoperability Centre (EIC) based on the Estonian "X-Road" system. <sup>12</sup> To facilitate the implementation of e-governance, the Tunduk State Enterprise aims to connect all information systems into a single electronic network – including the information systems of government agencies, local governments, and government institutions and enterprises, as well as legal entities and individuals.

The Tunduk system is designed to improve the efficiency of interactions between public authorities while significantly reducing corruption and bureaucratic obstacles for citizens and entrepreneurs through its automated data exchange. The introduction of the system is in line with the government's plan to reduce the public sector by 20% over the next three years. Each participant in the Tunduk system has a history of its interactions with other participants signed using an electronic signature. In order to exchange information with other state bodies through the Tunduk system, participants need to have information systems and databases. However, in 2018 not all state bodies had access to the necessary databases. Accordingly, Tunduk performed analytical work to determine which databases should be implemented at all state agencies to enable the provision of public services in electronic format. As a result of the analysis, a plan (*Development of Priority Databases of State Bodies*) was developed and approved by the Prime Minister, resulting in the identification of 125 priority databases to be implemented within 28 state bodies in 2018-

As of February 2019, the EIC had concluded agreements with 54 ministries and departments, and technical measures had been taken to connect 39 ministries (EIC, 2019<sub>[56]</sub>). As of February 2020, 62 government agencies and 28 commercial organisations have been connected to Tunduk. 191 government services are available through the government portal, and 85 additional government services have been incorporated in the framework of the project *Government as a platform* (276 in total). Thirteen certificates have been automated and 1.5 million certificates have been issued electronically. More than 20 m online transactions have been made between government agencies (EIC, 2019<sub>[57]</sub>).

Furthermore, 38 state bodies and their subordinate organizations, as well as 14 commercial organisations, carried out electronic data exchange amongst themselves. The agencies are communicating and exchanging documents through cloud computing data centres and integrated portals, with 7 million interactions reported in October 2019 alone.

By connecting different state agencies to a single digital network, the government can begin to develop integrated services through an automated single-window or OSS for citizen services. This innovation will not only improve the speed and efficiency of service delivery, but will also decrease the risk of corruption (von Arx and OSCE,  $2019_{[58]}$ ).

Priority services for digitalisation were selected by the EIC based on an inventory of documents requested from citizens and provided to government agencies. The inventory contains information on the number of requested documents, the time required to provide these and the list of documents necessary to obtain them. In order to facilitate the uptake of digital services by businesses, the EIC should make sure that newly-included services with

<sup>&</sup>lt;sup>12</sup> https://e-estonia.com/solutions/interoperability-services/x-road.

relevance to businesses should be actively communicated to the private sector, including through business associations.

Building on the links that have been built with mobile service providers, Tunduk should establish an application programming interface (API) link, enabling private or public providers to create a gateway for digitally obtaining and transmitting information. APIs work as a link between systems via an agreed protocol and set of functions. In essence, the functions are similar to a regular website; however, instead of returning data and code that is interpreted by the web browser and rendered as a human-readable web page, the API returns machine-readable data. This enables a variety of different solutions. For example, in-company processes can automatically trigger requests for specific government licences when importing or exporting certain kinds of products; human resources (HR) processes can result in the automatic registration of staff for social security contributions; and business management software can build direct links to government systems for the payment of taxes or requests for certificates. Such an approach has several advantages as it would provide a high level of adaptability to client demand, allow for competition between different providers of business software and, in the future, enable direct machine-to-machine communication (OECD, 2019<sub>[59]</sub>).

In response to COVID-19, OECD members and partner economies have scaled up their digital agendas and measures in favour of businesses. Some of them have helped businesses move online and connected smaller firms with larger global IT providers. India provides a good example of these measures in favour of the private sector (Box 8).

#### Box 8. India's digital platform for businesses

Immediately following the outbreak of COVID-19, India's government acknowledged the need for an online platform dedicated to India's private sector, with access to reliable information, support and government services, as well as a location for businesses to seek how to best support and innovate during the crisis. The government acknowledged its lack of financial and human resource capabilities to develop digital tools to respond to the crisis, and thus aimed to establish co-operations with, or foster partnerships among private companies, social entrepreneurs and international organisations.

India therefore set up the business platform <u>Investinindia</u>, with regular updates on government initiatives and services in response to COVID-19. With rapidly changing regulations, the government highlighted the importance of real-time information, including daily reports, information on funding mechanisms, notifications by region, relief efforts and innovations, and frequently asked questions.

The platform allows businesses to request special provisions and pose questions through multiple channels. It further seeks to bring together relevant actors, in order to offer innovative solutions, or to identify and fill demand and supply shortages across the country. On top of the toolkit posted on the site on *How To Take your Business Online*, the communication tool allows businesses to share best practices amongst each other. To best finance innovative ideas, and support businesses in need, the Indian government also launched a relief fund, which has collected USD 1.27 bn by May 2020.

#### Recommendation 2: Assess demand and act as a broker

Challenge 2: The government lacks information on business needs for BDS and firms receive little guidance on the availability and quality of services

#### The delivery of BDS is complicated by market failures

Businesses in Kyrgyzstan, as in many OECD countries, face market failures regarding the provision of BDS, as they lack information on the supply and quality of BDS, which leads to a continuous mismatch between suppliers of services and the recipients thereof. The demand side for BDS is affected by a lack of information and guidance on existing services available, thus preventing potential clients from identifying or contacting providers. On the supply side, providers of BDS have limited information about dynamic business needs.

This demand-side market failure has been highlighted by the survey conducted for this report. Seventy percent of businesses surveyed were not aware of BDS availability (Figure 3). Awareness is highest for financial management services and lowest for strategic management advisory work. Policy intervention is thus required to inform businesses of the benefits and availability of services, including information campaigns and B2B portals (OECD, 2017<sub>[29]</sub>).

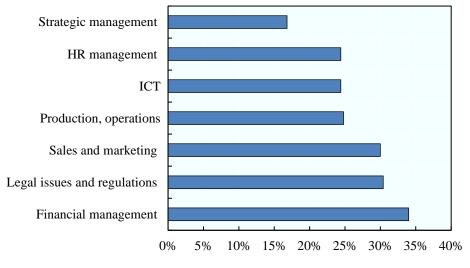


Figure 3. Awareness of BDS

Source: OECD survey, 2019.

Small firms tend to be unfamiliar with how specific markets, regulations or supply-chains function. Consequently, they often underestimate the benefits of external advice, support and networks (European Commission, 2002<sub>[36]</sub>; OECD/EU, 2014<sub>[32]</sub>). In addition to a lack of guidance and limited awareness of the benefits of BDS, small businesses are constrained by limited financial and human resources, which affect their ability to use sometimes costly and time-intensive services. This general trend is also confirmed by recent survey data: 61% of businesses acknowledge a lack of information about activities which could foster

their growth and 70% cite difficulties in dealing with financial tools, legal frameworks and operations, including promotion and market analysis (JICA, 2019<sub>[35]</sub>).

More than a third (36%) of the companies surveyed by the OECD had sought external support, but indicated that they were unable to receive the services they needed. This share was higher in rural areas (39%) than in Bishkek (31%) or Osh (33%). For small companies, the share of unmet demand was close to half of all companies (47%). A third of companies cited unfulfilled demand for services in sales and marketing; for individual entrepreneurs this was even higher (40%). A quarter (26%) cited legal issues and regulations, which was most relevant to small and medium-sized companies (35%).

The survey also concluded that the main reasons for businesses not seeking support were either high prices or a failure to find the services they needed, linked to the information asymmetry on existent services. Both adversely affect small firms with limited resources. Companies face difficulties in accessing BDS throughout Kyrgyzstan, but these problems are greatest outside the main urban centres.

#### Information on business needs is lacking

On top of the demand-side market failure, suppliers receive little guidance on the needs of businesses. This prevents them from offering tailored BDS, further enhancing a mismatch of services.

Information on business needs is scarce and the government does not regularly undertake efforts to generate such information. However, some data exist. For example, the International Business Council (IBC) and the Chamber of Commerce and Industry (CCI) regularly conduct surveys on the obstacles businesses face. From 2004 until 2016, the IBC conducted an annual survey on the business environment; a small sample of 23 businesses representing various sectors were questioned and the results were published. The CCI also runs a survey in which it poses seven questions to 100 firms on the difficulties encountered in conducting business in Kyrgyzstan.

The *National Institute for Strategic Studies*, acting on behalf of the government, also surveys entrepreneurs on the current situation in the business sector and expectations for the near future, as well as on factors affecting business development; these surveys are conducted on a quarterly basis to determine the dynamics of changes in the business climate (Nisi, 2017<sub>[60]</sub>; Chamber of Commerce and Industry, 2019<sub>[19]</sub>). However, the results are not publicly available, nor is it clear how they feed into policymaking.

Despite these surveys, however, more-specific research and information on business needs is lacking. This makes it harder for BDS providers and the development community to adapt their selection of training and consulting themes to client needs. Survey data gathered for this report reveals significant gaps in the market with respect to some of the needs expressed by businesses. Sales and marketing, followed by legal issues and regulations, remain the most important needs across all business sizes, sectors, and regions (Figure 4). Interviews with businesses also highlighted the mismatch of training topics and evident business needs. Particularly, newly introduced trade agreements demand new skills that could be built and developed through specialised training.

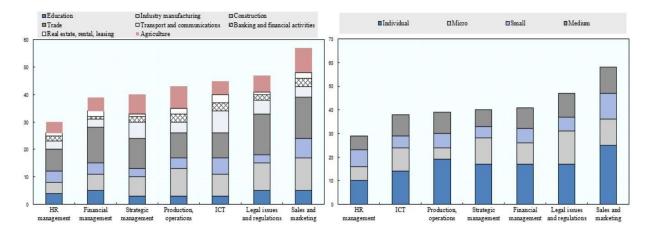


Figure 4. Critical business needs by sector of activity (left) and firm size (right)

Source: OECD survey, 2019.

In addition to surveys, public-private dialogue (PPD) can also help increase knowledge and awareness of business needs. To this end, the government has established the *Council for Development of Business and Investment*, which analyses the investment landscape and offers legislative recommendations to the government. It is chaired by the Prime Minister and involves government representatives, development partners and business associations (UNCTAD, 2016<sub>[61]</sub>). In 2017 the Kyrgyz Parliament also created a *Business and Entrepreneurship Development Council*, whose primary function is to strengthen cooperation between the country's legislative body and the private sector. The council consists of members of parliament, cross-sectoral businesses, and members of business associations. It meets regularly to discuss measures to improve investment, promotion of entrepreneurship, and legislation in order to facilitate doing business (U.S. Department of State, 2018<sub>[62]</sub>). However, while some PPD platforms are in place, they are still limited to a small number of councils that do not specifically focus on business needs, discerned by sector or size. This limits the ability to adapt public and private BDS to business needs.

The government and its partners should therefore work to correct both demand- and supply-side market failures and act as a facilitator for the development of a financially sustainable business-support infrastructure. To enhance the awareness of BDS, the government should offer basic information about private BDS in one-stop shops or points of interaction with entrepreneurs. For MSMEs to better grasp the added benefits of BDS, communication and outreach campaigns (both physical and digital) are necessary. The following recommendation outlines how to bridge the gap between suppliers and consumers of business development services (OECD et al., 2015<sub>[33]</sub>).

# Recommendation 2A: Conduct regular consultations and surveys of private-sector needs

Good practices from OECD countries show that the government can and should act as a broker facilitating information flows between MSMEs and BDS suppliers. This would involve undertaking regular business-needs diagnosis, signposting MSMEs to existing suppliers, and facilitating dissemination of information for businesses. It may also involve taking steps to recognise or accredit BDS providers in certain activities, so as to ensure

conformity to certain standards. However, such measures should be taken sparingly, to avoid the creation of unnecessary barriers to entry and competition.

Due to a growing awareness of market failures in BDS across OECD countries, some OECD governments have tended to intervene heavily in private BDS markets in recent years, resulting in market distortions. To avoid this, the OECD recommends building, rather than crowding out, the private BDS market, while underlining that the public sector has clear responsibilities "for diagnosis, problem identification and solutions, then signposts to external experts for project delivery" (OECD, 2018, p. 14<sub>[34]</sub>).

# Carry out regular surveys and engage with entrepreneurs and small companies to assess their needs

Businesses in Kyrgyzstan express their need to catch up with economic and regulatory developments, including the GSP+ scheme<sup>13</sup> and Kyrgyzstan's accession to the EEU. Challenges mostly relate to low quality standards and lack of knowledge about how to improve in this regard. Business associations repeatedly mention difficulties in finding qualified trainers. Exporting firms in particular face changing demands on the external market, requiring training and external support to catch up. Therefore, it remains crucial to keep track of changing business needs, so that the government can implement early-reaction mechanisms, including university courses and training of trainers.

In OECD countries, it is common for governments to conduct surveys in order to assess business needs and better adapt policymaking, sometimes in partnership with chambers of commerce. In this regard, the government has two choices, depending on the budget at hand: either run its own surveys or partner with business associations that already conduct regular surveys. While running its own survey, the government should select a sufficiently large sample of firms, representative in size, sector, location and contribution to GDP. It should offer the survey in both Kyrgyz and Russian languages and should ask simple questions covering exact areas of need, capability gaps and challenges. Ideally, private-sector representatives should be involved in the survey design.

The survey could further include the perception of public services, and gather tailored feedback on how businesses make use of digitalised public services. In 2019, the OECD conducted a survey of business needs, detailed in Box 9. It could be used as a basis for future surveys.

The government would also have the option to use BIOs as relevant channels. For instance, the government could tap into the IBC and the CCI surveys on the obstacles businesses encounter, or better adapt the survey of entrepreneurs conducted by the National Institute for Strategic Studies. Questions on needs and competencies could include:

- To what extent does your business have internal staff capabilities in the following areas: sales and marketing, production processes, ICT, HR management, financial management, strategic management?
- For the external advice/training that you have previously obtained, what was the
  main reason that influenced your decision to obtain them (lack of knowledge or
  experience within the firm, contracting a specific service as a legal requirement,

<sup>&</sup>lt;sup>13</sup> GSP+ stands for Generalised Scheme of Preferences Plus which allows eligible developing countries to pay no duties on some exports to the European Union.

less costly than in-house learning, better quality than in-house learning, use of the service by the competition, previous use of the service, advice from peers, other)?

- To what extent does your business require support (training, consulting, advice)?
- In the future, in which area would you most likely seek external BDS support (e.g. sales and marketing, production processes, ICT, HR management, financial management, strategic management)?

When partnering with such institutions, some institutions may – for good reason – focus on their own constituencies. This can generate useful information, but it may leave some firms and sectors un- or under-represented. For this reason, it is critical to ensure that the survey coverage is broad and representative.

#### Box 9. OECD survey of business needs

In May-July 2019 the OECD conducted a survey in Kyrgyzstan of the current use and demand for business development services. Some 250 micro, small- and medium sized enterprises, as well as individual entrepreneurs – in proportion to their share of the country's GDP (excluding Kumtor) – were surveyed.

The interviews were carried out with the top management of the companies in either Russian or Kyrgyz. Eight sectors were selected: education, industrial production, construction, trade, transport and communications, banking and financial activities, real estate and renting, and agriculture.

A total of 58 questions were posed, clustered in the following themes: business performance, business environment, need and awareness of BDS, use of external information, advice and training, business associations, reasons for seeking business support services, and further needs. The research methodology was tablet-assisted personal interviewing (TAPI), and the selection methodology followed the snowball method.<sup>1</sup>

See Annex C of this report for more detail.

In addition to surveys, targeted interviews with specific sector representatives could provide more detailed perceptions. In the Netherlands, the Regulatory Reform Group (RRG) used interviews with businesses to collect information on burdens and irritations in doing business in order to adapt business-relevant public services. They also aimed to trace whether both micro and large businesses are affected by and perceive regulatory changes. This helps to assess the effect of measures already put in place, highlighting whether better communication on results is required (OECD, 2010<sub>[63]</sub>).

### Organise regular public-private dialogues on public services with businesses

In OECD countries, formal consultations with businesses take place on a regular basis to help build trust, identify crucial reform requirements, and collect and discuss feedback from businesses (OECD, 2010<sub>[63]</sub>). Denmark, for example, established several working groups (WGs) comprising representatives from selected business organisations to take part in consultations on public services with relevant ministries.

<sup>&</sup>lt;sup>1</sup> Snowball sampling is a technique wherein research participants recruit other participants for a test or study.

It is important for survey results to be analysed and discussed, ideally in the scope of dedicated public-private WGs. A good example is France, where the government put together dedicated BDS WGs to pick up on survey outcomes: the government surveyed 5000 individuals and 2800 businesses through a panel process. To enhance the consultation process, it established a network of representative bodies that regularly receive the survey results in order to discuss and provide suggestions on the areas of simplification. Workshops are organised, and a website has been established to facilitate consultation, voting on measures and proposing ideas (OECD, 2010<sub>[63]</sub>). Follow-up in such activities is critical: a high-level consultation can help focus attention on an issue and secure government commitment. This commitment typically involves more-specialised technical work involving expert groups or sub-committees to ensure ongoing co-operation.

The government has several options for improving its consultation with businesses on BDS. It can opt for discussing BDS during the existing co-operation channels (including the Council for Development of Business and Investment or the Business and Entrepreneurship Development Council) and include thematic discussions on BDS. The government could also put in place a WG dedicated to BDS comprising representatives of the private sector, state agencies, development actors, and ministries as well as BDS providers. The group could be in charge of overseeing the collection of the survey data, then communicating the results within an annual report published online. This report could include recommendations for relevant stakeholders – the government, private providers and the development community – on ways to best tailor their products. Although a fixed set of representatives should be selected, further sectoral representatives could be invited to participate on a regular basis, upon request.

# Regularly update services provided in one-stop shops in consultation with the private sector

The government should pursue an inclusive and systematic approach to its one-stop shops and to choosing the services provided there. It is crucial to involve representatives from the private sector who have first-hand experience with the administrative procedures involved and are able to provide data points that can serve as a useful adjunct to government assessments (OECD,  $2010_{[63]}$ ).

Existing mechanisms, such as the business council and other platforms, could already allow for this exchange to occur. Furthermore, the aforementioned surveys should pose questions related to the business service centres. The government should also make best use of the presence of a large and invested development community to provide support through extensive surveys (such as the feasibility study conducted by JICA), and should build on their activities to assess the best way forward for the planned business service centres.

#### Recommendation 2B: Enhance the availability of information on existing services

#### Identify private service providers and develop an online database of providers

To counter the low awareness on BDS in Kyrgyzstan, the government should take on the role of an intermediary by conducting a mapping exercise with all BDS suppliers, grouped by broad category of service. This can be done together with the development community and other actors that seek to improve their co-ordination mechanisms on BDS. Montenegro serves as a good example as its Ministry of Economy together with the United Nations Industrial Development Organisation (UNIDO) mapped all 300 BDS providers present in the country (OECD/ETF/EU/EBRD, 2019<sub>[64]</sub>). This information has then been posted on

the ministry's website and is free to access. To this end, Kyrgyzstan's existing donor coordination council<sup>14</sup>, which exchanges regularly on private sector related activities, could be leveraged.

The government should develop a web-based information portal containing information on companies, institutions and agencies offering programmes including a BDS component. Both BDS and linked government schemes could be described and classified by category. BDS providers should be allowed to register and publish their services on the website. Business service centres could then make use of this platform and guide businesses towards the services they need; businesses could also seek information on BDS directly.

Over the long term, the information portal could list private quality-assured BDS providers that have been screened and selected by a government institution, such as an SME agency. In Belarus, for instance, the Entrepreneurship Department, operating under the auspices of the Ministry of Economy, has established a certification process for private business-support providers; the private providers who end up being certified then form part of a nationwide database. However, for this exercise to work, an SME agency or similar is needed, with sufficient competence to select relevant stakeholders for the certification process (OECD, 2017<sub>[29]</sub>).

In the United Kingdom, the Department for Business, Energy and Industrial Strategy runs an information portal<sup>15</sup> on which BDS suppliers in a range of categories can signpost their offers. The online platform provides information on starting and growing a business – including training videos, case studies, market research and sectoral data, an online forum, and information about BDS providers (OECD, 2018<sub>[34]</sub>). It functions in a user-friendly manner, allowing businesses to select BDS by categories – including type of support (finance, equity, grant, loan, expertise and advice, recognition awards), business stage (not yet trading, start-up, established), industry, number of employees, and region.

Kyrgyzstan could further aim to replicate the experience of Moldova, whose SME agency provides extensive business information – both physically through flyers and staff in business information centres, and digitally through a website dedicated to entrepreneurs (OECD, 2014<sub>[65]</sub>). The government could establish a similar website, in co-ordination with other actors, and use the dedicated working group to best tailor the site to local business needs. The site will have to function on mobile platforms, in order to facilitate its usage across regions and income levels.

#### Provide information and guidance on BDS when interacting with businesses

A recent study in Kyrgyzstan provided evidence that businesses would be willing to use more BDS if more information were available and if they received guidance on potential providers, even if they had to travel to access the information. The potential sessions requested by the surveyed MSMEs were to last between one and two hours. The study therefore suggests a willingness of businesses to learn how to grow, further shown by 61% of businesses stating that they lacked knowledge on developing their business (JICA, 2019<sub>[35]</sub>).

<sup>14</sup> http://www.donors.kg/.

 $<sup>^{15}</sup>$  <u>https://www.gov.uk/government/organisations/department-for-business-energy-and-industrial-strategy.</u>

This note therefore recommends that the government make use of one-stop shops to inform and link businesses requiring public services to B2B providers of relevant services, such as legal consultation, information on foreign markets and export requirements, market research, and reliable statistics – that is, any service needed to support their growth plans (JICA, 2019<sub>[35]</sub>). The government should use the business service centres, one-stop shops and other locations where public services are provided to inform businesses about available services that can foster their growth. For this, staff in the centres have to be trained in advising businesses. Information can also be made available through leaflets and websites. Advising businesses on areas of support and directing them towards potential suppliers would be an important step in their growth development (OECD, 2017<sub>[29]</sub>).

Similar information needs to be provided by the CCI and other business associations. The government could encourage the dissemination of information to them and involve them in communication campaigns (recommendation 3).

Box 10 discusses the experience of Poland's Polish Agency for Enterprise Development (PARP) in providing training and advisory services, and in establishing a one-stop shop to link businesses to relevant public services.

#### Box 10. Poland's experience in providing public services to business

In Poland, public services to business are delivered mainly by specialised institutions integrated within the Polish Development Fund Group, among them the Polish Agency for Enterprise Development (PARP). PARP was set up in 2000 to support innovation and skills. The Agency complements the SME Development Centre with on-line training and advisory services for enterprises at various stages of development. It also runs a Database of Development Services (training courses, postgraduate studies and counselling) comprising accredited entities only. This approach allows for a greater share of private entities in BDS supply and for the maintenance of required standards.

PARP is assisted by accredited business support organisations, such as business support centres, innovation and technology transfer centres, technology incubators, and technology and science parks operating throughout the country.

To simplify the interaction between the government and entrepreneurs, a one-stop shop (www.biznes.gov.pl) has been launched and is to be developed further, in line with the "Paperless & Cashless Poland" programme. The portal is not only an umbrella information website, but also a centralized platform for delivering an ever-more-comprehensive range of e-services to business. Its most important functionalities, particularly in light of COVID-19, are the Help Centre for Entrepreneurs and the e-Services module which allow agents to handle official matters online thanks to various digital identity verification tools.

## **Recommendation 3: Stimulate private supply**

# Challenge 3: The market for private business development services is underdeveloped for small businesses

A glance at the market for providers of private BDS reveals a wide array of stakeholders and providers: the private sector, business associations, the government, educational institutions and the development community. The OECD survey shows that private providers play a key role in delivering BDS to companies. Out of the total BDS supply indicated by the survey, 49% was offered by private providers, followed by the government (16%), business associations (15%), and NGOs (13%). Other providers amounted to 38%, potentially indicating either the development community or informal providers of BDS, including acquaintances or relatives with business experience.

#### Private BDS providers tend to focus on medium-sized firms

Private providers of BDS in Kyrgyzstan include law firms, marketing agencies, consultancies, training centres, and auditing and accounting firms, among others. They either provide the support services that businesses seek to outsource or offer consulting and advisory services. In most cases, they focus on medium-sized or large companies.

Interviews also revealed that businesses perceive a lack of high-quality service providers, particularly in the auditing and accounting realm, as international certifications are expensive and staff lack the English language capability required to become acquainted with updated standards.

Furthermore, business associations, educational institutes (training centres, universities) and the development community (NGOs, international organisations) act as service providers to supplement private BDS. These institutions tend to take an educational role in BDS by providing training, including specific programmes for disadvantaged groups.

The government has also gotten involved in the private BDS market by co-establishing the business service centres, technology centres (e.g. the "Smart Build" technology centre launched in 2017) and innovation hubs to foster start-up creation and growth (Box 11). These are, however, only slowly gaining traction next to the public services the government has put in place, including a single window of the tax authority or the Single Window Centre for Foreign Trade, the so-called Tulpar system (Figure 5). Up to now, the main endeavour in the private BDS market has been to provide better and more-targeted information rather than offering direct private services.

#### Box 11. Start-up support in Kyrgyzstan

Even more than established MSMEs, start-ups in Kyrgyzstan tend to be heavily affected by high administrative and compliance requirements amidst an overall challenging business climate. They particularly struggle to obtain finance, as banks tend to be risk-averse towards young firms. Alternative modes of finance, including venture capital or business angels, are rare. Support mechanisms, such as business incubators, are only starting to develop. A systematic government approach to fostering start-up creation is

lacking, with the current start-up support landscape featuring only a few scattered initiatives.

The legislative framework is also unsupportive. For instance, a law on the regulation or establishment of new companies from university laboratories has not yet been put in place.

However, the government has introduced several programs and innovation structures to support business incubators and start-up development. Currently, the state intellectual property service of Kyrgyzstan, Kyrgyzpatent (<a href="http://patent.kg/en">http://patent.kg/en</a>), is planning to establish a Technopark University. Similarly, the public Kyrgyz-Turkish Manas University recently founded an incubator for IT and emerging technologies.

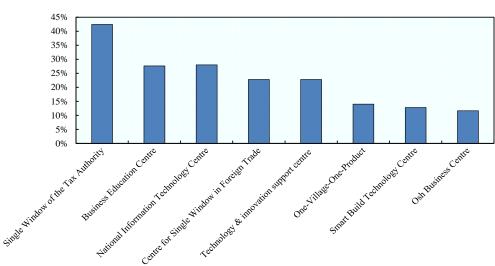
Collaboration with the development community has also fostered an increase in start-up support. For instance, the Accelerate Prosperity (AP) initiative of the Aga Khan Development Network focuses on start-ups through an acceleration programme. AP provides seed financing, coupled with training and consulting, in three areas: sales and marketing, financial management and investment. Further, the Russian-Kyrgyz Development Fund has announced the implementation of a start-up financing program in Batken, Talas and Naryn regions, wherein it will allocate USD 1 million. Other support mechanisms include international start-up events and "hackathons" organised by KG Labs Public Foundation to build start-up skills and strengthen the start-up ecosystem in Kyrgyzstan.

The government could continue to support the start-up community through targeted support involving tailoring the planned business service centres to start-ups – through the provision of integrated business incubators and expert advice on start-up themes in particular (business planning, marketing, access to finance, tax administration).

Source: UNECE (2019[66]).

Which of the following institutions or departments offering support to firms do you know?

Figure 5. Firm awareness of sources of business support



The provision of services is highly concentrated in the main urban areas, with the majority of respondents having sought BDS in Bishkek, Jalal-Abad and Chuy. Only a minority of interviewed firms had obtained BDS so far; 29.6% of firms sought external advisory or consulting services, 40.8% received training, and 22% sought external information. Uptake is highest in the banking and construction sectors (Figure 6).

Received External Advisory/ Consulting Services
Received Trainings
Received External Inf.

Agriculture
Real estate, rental, leasing
Banking and financial activities

Transport and communications

Trade

Construction
Industry manufacturing
Education

0% 20% 40% 60%

Figure 6. Use of BDS by sector

Source: OECD survey, 2019.

Overall, the private BDS market in Kyrgyzstan remains targeted towards larger firms. This is not surprising as larger firms have more resources and tend to have more sophisticated, complex BDS needs. This selective supply is also reflected in the OECD survey data, as services were less used by micro firms and individual entrepreneurs (Figure 7). In fact, individual entrepreneurs expressed the least uptake, far behind all other firm sizes. This became particularly evident in interviews with suppliers of BDS, who stated that they prefer medium-sized, larger firms, or the development community over small firms, considering that they are better able to pay. In fact, when comparing the expenditure on BDS, medium-sized firms reported having spent 8% of their revenue, compared to 1% for small firms.

60% ■ Received external information ■ Received trainings ■ Received external advisory/ consulting services 50% 40% 30% 20% 10% 0% Individual Medium Micro Small

Figure 7. Use of BDS by company size

Source: OECD survey, 2019

At the same time, individual entrepreneurs and micro firms both expressed greater needs and weaker competencies throughout the OECD survey. Unsurprisingly, specialised staff increases with firm size, and highly depends on the area (Figure 8): financial management is over-represented, followed by production processes and HR management. Sales and marketing and strategic marketing are lagging behind, coinciding with needs expressed by firms throughout the survey (Figure 4 above).

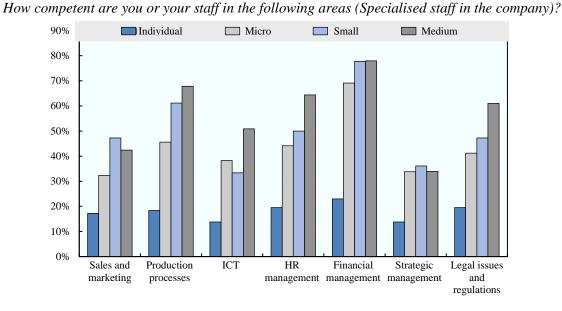


Figure 8. Firm competence and specialised staff

The rationales given by firms not seeking external support concerned either pricing (24%), lack of time to seek external support (11%), or inability to find services they needed (17%). Micro firms were the most affected by high prices, with individual entrepreneurs complaining most about lack of time to seek support. Medium-sized firms can, due to their size and capacity, afford BDS more, and thus spend more of their revenue on outsourcing tasks. When it comes to paying for those services, most firms paid from their own revenues. This has not changed since the last assessment of Kyrgyzstan's BDS market in 2001 (GTZ/Helvetas, 2002<sub>[67]</sub>).

The regional dispersion of the country also fosters an agglomeration of firms and service providers in urban areas. This is entirely normal, but it results in a meagre supply of BDS in outlying areas, as well as diverse competencies across the country. The government could do more to improve service accessibility in terms of both pricing and location. Business associations and the development community, already active in both spheres, could support this effort.

# Recommendation 3A: Support and partner with business intermediary organisations in the delivery of services

Business intermediary organisations (BIOs) include chambers of commerce, business associations, and organisations funded and founded by businesses in subsectors or industries of the economy. They provide their members with the opportunity to network amongst themselves in order to share information and resources. Business associations are well-known for their referral mechanisms, which involve both established and informal methods (Asian Development Bank, n.d.<sub>[68]</sub>). When it comes to BDS, they can refer their members to external service providers to reduce search costs, liaise with the government on the needs of their association, and, in the case of Kyrgyzstan, even act as a BDS provider (Hartmann, 2019<sub>[69]</sub>).

In Kyrgyzstan, 16-20% of all businesses are estimated to belong to BIOs (EBRD, 2019<sub>[11]</sub>). The BIOs hold multiple roles: they represent and advocate for the needs of their members, but also act as service providers offering training, business schools, and advisory services to their members. The government could tap into this service delivery mechanism and support it both financially and through awareness campaigns.

The OECD survey finds that 15% of businesses had previously sought BDS through business associations, and of those that did, 83% were satisfied with the results. At the same time, the survey shows that businesses struggle to obtain BDS. Thirty-six percent of all businesses, in fact, aimed to contact BDS providers in the past year but failed to obtain any services. Both figures could therefore be up-scaled, if the government would support business associations in their delivery of services, including by facilitating the search for BDS.

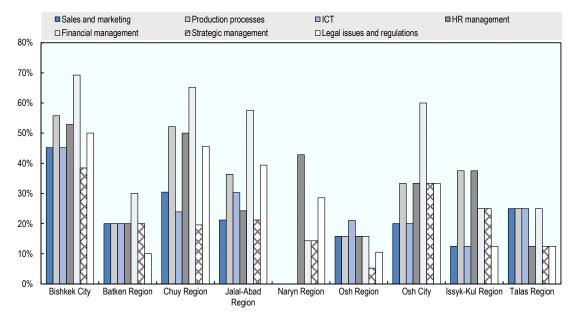
Membership of one or more business associations may have a positive effect on the uptake of BDS, as it will allow firms to become more aware of, and referred to BDS providers. Thus, business associations could be leveraged as both promoters as well as direct providers of BDS, offering adapted services to their members. For instance, the Chamber of Commerce and Industry of Kyrgyzstan offers training courses on tax administration for small businesses, based on requests from its members. In addition to providing basic training, BIOs in Kyrgyzstan also undertake the important role of signposting their members to specialised service providers.

Strengthening the role of BIOs could expand the range of services tailored to the needs of businesses in Kyrgyzstan, particularly in outlying areas. The Ministry of Economy has already included enhanced co-operation and support for selected associations within its *programme for the development of the private sector* (Ministry of Economy, 2019<sub>[70]</sub>). The government could further support BIOs as well as coordinate and align with the development community to offer co-payment mechanisms in the delivery of BDS (Committee of Donor Agencies, 2001<sub>[71]</sub>).

Figure 9 reveals diverging competencies in the different regions in Kyrgyzstan, supporting the co-operation of the government with actors active in the regions. In interviews with business associations, it became evident that they aim to expand and focus on offices in non-urban locations in Kyrgyzstan; the government could support this.

Figure 9. Firm competencies highly depend on the region of operation

How competent are you or your staff in the following areas? (Specialised staff in the company)



Source: OECD survey, 2019

#### Partner on service delivery

The Ministry of Economy can involve business associations in all its dialogue platforms on BDS and leverage on their surveys. This process should be integrated into the programme of work, particularly considering the frequent changes in the government (on average every ten months since 1991). The government is therefore even more reliant on stable partners, including business associations and actors on the ground (EBRD, 2019[11]). It could thus partner with BIOs in the service centres to ensure that they provide information or deliver additional private services that the government does not have the capacity for. Offices or desks of BIOs can be opened in the centres with appropriate information to ensure that small firms are signposted to BIOs when they visit public centres.

The government could further tap into the outreach and role of business associations in rural areas. Several of Kyrgyzstan's business associations have a strong regional presence. The government should therefore prioritise working with business associations that are

active and effective in providing services in the regions. This is particularly relevant during crises, when business associations can channel information from the government to their members. Business associations like France's MEDEF stepped up efforts to support their members during the crisis by offering a toolkit on teleworking and hygienic working during a pandemic.

In Kyrgyzstan, meetings between Ministries and business associations during the pandemic resulted in the common selection of essential businesses, in order to make sure that the supply of goods remained uninterrupted during the crisis. Surveys conducted by business associations also fed into government policies. Such methods of co-operation can be expanded beyond the crisis to strengthen trust in the abilities of business associations, even as providers of government services.

Other support mechanisms exist and can be supported by BIOs, such as networking events and fairs to raise awareness of BDS and their benefits. Events could be organised by business associations (in co-operation with local providers) and supported by the government.

The Chamber of Commerce in Uzbekistan, for example, offers numerous support programmes to its members, including preparation of business plans, accounting services, tax assistance, financial consulting, training courses, and legal assistance. The services are therefore comprehensive, and are further adapted to quarterly surveys with members. Furthermore, the Chamber is part of numerous government councils, in which it shares the experience of its members. It takes part in sessions of the government, and supports it in the preparation and discussion of laws relevant to business development. The Chamber is part of a commission in charge of administrative reform and implementation, as well as the Co-ordination Council to Stimulate the Development of SMEs. Under a recent Presidential Decree, the Chamber regularly receives relevant information on SME development, including decisions and orders of the Cabinet of Ministers and statistical data from the State Committee. This allows the Chamber to adapt its service provision, but also entitles it to provide these services to its members (Chamber of Commerce and Industry of Uzbekistan, 2019<sub>[72]</sub>). Kyrgyzstan could aim to replicate this method of co-operation.

#### Support capacity-building of service providers

The OECD fact-finding mission, which included interviews with BDS providers, revealed that business associations lack good trainers, particularly in areas which are rapidly developing, like ICT and trade. Because local capacities are limited, business associations are forced to seek trainers from abroad, usually Kazakhstan or Russia. This substantially increases the cost, and thus the availability and accessibility, of training, particularly for smaller companies with limited funds available.

Both short- and long-term approaches to this issue must be taken. Over the short term, training courses for local trainers can be offered. It could also prove useful to design training curricula that include digital elements as well as in-person training. Over the long term, education systems have to be adapted to business needs – and must emphasise topics such as accounting, business management and issues related to business internationalisation – in order to develop both skilled workers and knowledgeable trainers.

#### Recommendation 3B: Make the best use of the development community

Interventions stemming from the development community have to be carefully designed in order to avoid crowding out the private BDS market. In Kyrgyzstan, the development

community has a strong presence, and acts as both a user and a supporter of BDS. It is therefore crucial for development organisations to align their BDS efforts with the government in order to multiply the effects of their intervention and avoid duplication. In 2001, the Committee of Donor Agencies for Small Enterprise Development (now known as the Donor Committee for Enterprise Development) put in place guiding principles for donor intervention in the BDS market that remain highly relevant today (Box 12).

#### Box 12. Principles of donor intervention on BDS

Donor intervention should be based on:

- 1. a fundamental belief in the principles of a market economy, where the State has a role in providing an enabling environment, in correcting or compensating for market failures, and in the provision of public goods, but not in the direct provision of private goods that can be more efficiently provided by the market;
- 2. the assumption that the majority of BDS are private goods and are thus similar in nature to any other service, so market rules apply; and
- 3. the expectation that with appropriate product design, delivery and payment mechanisms, BDS can be provided on a commercial basis, even for the lowest-income segment of the entrepreneurial SE sector.

Source: Committee of Donor Agencies (2001[71]).

# Map and regularly update the development community's support programmes for businesses

In fact-finding interviews and during Working Group discussions, activities of the development community in Kyrgyzstan have sometimes been identified as overlapping and unaligned with government priorities. Given the importance of avoiding measures that would unnecessarily distort the development of a private market, it is crucial for the government to co-ordinate with the development community to make the most of their support and align their efforts. For this to occur, the development community should be invited to the working groups on BDS (given in recommendation 2) in order to thematically adapt their BDS offers.

Development partners will also have to co-ordinate amongst themselves in order to avoid overlapping projects. They could share lessons learnt on a more systematic basis and guide each other in their selection of projects, with a view to preventing the duplication of projects or implementing projects which could distort the development of a private BDS market. The donor co-ordination platform is a first step in the right direction. This will allow better co-ordination amongst projects, and could be linked to the governments' efforts to map donors' support programmes on BDS.

For instance, the government of Uganda established a Poverty Reduction Support Credit (PRSC), which is essentially a matrix of actions, including benchmarks and outputs, codeveloped between the government and donor organisations. The policy matrix allowed the government to not only maintain an overview of donor projects, but also to align them with the government's strategy – and to promote collaboration between the donor institutions themselves (OECD, 2003<sub>[73]</sub>).

#### Carefully design financial incentives

Case studies and research have shown that free-of-charge BDS suffer from a valuation problem and can harm the natural development of a private-sector-led BDS market. It is therefore crucial for the development community to rethink the services it offers by aligning them with company needs – while not distorting the existing market for private BDS market (Philip, n.d.<sub>[74]</sub>).

As a general rule, services should not be offered free of charge. Subsidies, grants, vouchers may be applied in order to stimulate the market and aid start-ups and very small businesses, but these should be limited and designed as a short-term solution or focused on very specific moments in a firm's life cycle. Small fees for either training or services should be applied, as even relatively modest sums can ensure commitment by the entrepreneur, which tends to make the services more successful (OECD/EU, 2014<sub>[32]</sub>). Thus, the intervention should be designed to achieve specific market development objectives; be time-bound according to the achievement of set objectives; include an exit strategy; and focus on technical assistance and incentives (Committee of Donor Agencies, 2001<sub>[71]</sub>).

OECD governments have made use of financial instruments to encourage businesses to take up BDS. In Kyrgyzstan, the EBRD has already initiated a similar scheme, thereby stimulating the consulting market (Box 13). Considering the agglomerated presence of the development community and their involvement in BDS, the government could partner with them to co-create further financial instruments. For instance, matching grant schemes and voucher programs could help stimulate the demand for BDS. These financial incentives could increase the uptake of BIO services while simultaneously enabling small firms to afford BDS, based on survey data.

#### Box 13. EBRD's small business programme

Since 1992 the EBRD has been present in Kyrgyzstan, where it has invested EUR 789 million and implemented 185 investment projects to date. Alongside investment projects, the EBRD helps local SMEs to access advisory services from local consultants and international advisers, covering up to 90% of net costs of the service (businesses bear the cost of taxes). Since 2005, EBRD has enabled over 950 businesses to access advice.

The EBRD's network of local consultants consists of 230 consultants that meet the standards set by the EBRD, and the consulting service usually lasts between four and six months. Consulting is available to businesses nationwide, and 64% of projects take place outside main cities. The service helps businesses develop business plans, undertake feasibility studies, and raise accounts to international standards; this has allowed 7% of clients to secure external funding. It also offers advice in other areas like organisation, marketing, green technologies and quality management. More than 80% of clients reported an increase in turnover (with a median increase of 26%), 62% of businesses experienced a boost in productivity, and 56% of businesses reported job creation.

Source: EBRD (2019[75]).

These tools should be implemented cautiously, as they may have a negative effect on market development by establishing artificially low prices for recipients, encouraging providers' dependence on sponsorship, and potentially harming non-subsidised programmes. However, the intervention is justified at a very early stage of service

development to temporarily address both demand- and supply-side constraints while increasing awareness of BDS (Asian Development Bank, n.d.<sub>[68]</sub>; OECD, 2017<sub>[29]</sub>).

### Make use of matching grant schemes to enhance awareness on BDS

Matching grant schemes are an instrument in which a partial contribution is provided towards beneficiaries' expenditure on BDS; the grants are offered on a cost-sharing basis, with beneficiaries matching the grant. The idea is to offer financial incentives to firms in order to overcome barriers including "unclear benefits stemming from failure risks and SMEs being inexperienced with certain activities and services" (Asian Development Bank, n.d.<sub>[68]</sub>). The scheme can act as an entry point for firms to experience BDS and become aware of its benefits.

#### Put in place carefully designed vouchers to stimulate short-term demand

Vouchers can allow SMEs to acquire BDS from accredited providers. They tend to be both standardised and indiscriminate and apply to all businesses in their growth phase to enhance their outreach and disbursement efficiency. These schemes tend to "primarily address demand-side constraints, namely information problems and low willingness to pay for BDS resulting from scepticism about their usefulness" (Asian Development Bank, n.d.<sub>[68]</sub>).

Voucher programmes were implemented in Indonesia in the early 2000s in order to offer discounts on training and counselling services for SMEs. The programme increased the usage of BDS and, most importantly, encouraged providers to adapt their services to the actual demand at hand. The evaluation of the programme, however, found that it merely incentivised those businesses that had already expressed interest in BDS and stated a need (Asian Development Bank, n.d.<sub>[68]</sub>).

The OECD survey showed that a high interest for BDS and a willingness to grow exist amongst Kyrgyz businesses. The government, in co-operation with the development community, could therefore aim to introduce vouchers that cover a substantial share of the cost, by co-operating with BIOs and providing vouchers for their members to test the services they offer. This will also expand the membership of BIOs as well as trigger them to offer more – and, in particular, more demand-oriented – services.

#### Encourage the development community to use and build the capacities of BIOs

For BDS interventions to be locally owned as well as sustainable, it is important for donors to build on institutions that are already in place. They should choose partner organisations which are closest to beneficiaries and have experience in terms of delivery of BDS (Committee of Donor Agencies, 2001<sub>[71]</sub>). Interventions should therefore aim at cooperating with BIOs in the provision of BDS, be it through service delivery or training. As the associations become more established and commercial BDS expand, donors can choose to withdraw their support.

The development community could also help BIOs further strengthen their capacity to deliver BDS. For instance, "training of trainers" (TOT) activities can have a multiplier effect on final beneficiaries. Several such activities are already in place, such as cooperative efforts between donors and the CCI, or with the business association JIA. Furthermore, as part of the EU's Central Asia Invest Programme, several projects are in place to improve human-capacity development and service delivery by BIOs in Kyrgyzstan. Future activities could build on these efforts and develop specific expertise in areas most needed.

The development community has further stepped up its efforts to support governments and domestic businesses in the current turmoil. This includes expanded financial support and services directed to SMEs and tax and fiscal measures that were suggested and sometimes funded by the international community through budget support. BIOs in most Central Asia countries have helped identify the needs of businesses during the crisis, including through surveys, and can be key partners in these efforts to address more acutely these immediate needs, channel information, and deliver specific services, for instance on new types of support and sanitary measures, thus being a cornerstone in both donors' and governments' responses to the post-crisis period.

### Way forward

This section outlines an indicative timeline for implementing the policy recommendations given above. It takes into account the need for the government to 1) provide better and more-efficient public services and 2) take on a stronger role by acting as a broker in order to stimulate private supply. At the same time, whilst intervening in the market for private BDS, it is important to minimize intervention and market distortion, and to avoid the government's direct provision of services. The growth of businesses in Kyrgyzstan – particularly small firms – is hindered both by the challenging business environment and the lack of information on and access to BDS. The recommendations and implementation timeline are therefore designed to address the market failures at hand whilst simultaneously respecting the private forces of the BDS market.

The timeline for implementing the recommendations will be fine-tuned during, and based on, OECD capacity-building workshops that will support implementation in 2020 and 2021. The workshops will be led by the Ministry of Economy (in particular the Department on Regulation of Entrepreneurship) and will include other stakeholders that can support the implementation process. The OECD will assist the process and invite experts to share their knowledge on the relevant policy areas.

COVID-19 has highlighted the need to further support businesses and in many OECD countries has led to the acceleration of the digitalisation agenda. This has been a long-lasting priority for Kyrgyzstan that could deserve more focus and resources in the years to come. Business Intermediary Organisations have also played a key role during the crisis in most countries, further highlighting the importance of further involving them in the design and roll-out of information and services to businesses.

#### Suggested timeline for implementation

	Indicative implementation timing		
Recommendations	Short-term <1 year	Medium-term 1-3 years	Long-term >3 years
1 Improve accessibility and efficiency of public services			
A: Establish whole-of-government one-stop shops for businesses, leveraging existing service delivery centres			
B: Digitalise public services for businesses     Continue to digitalise internal government communications using Tunduk			
Develop a digital one-stop shop for G2B services			
2 Assess demand and act as a broker			
C: Conduct regular consultations and surveys on private sector needs			
D: Enhance the availability of information on existing services     Identify private service providers and develop an online database and registry of providers     Provide information and guidance on BDS when interacting with businesses			
3 Stimulate private supply			
E: Support and partner with business intermediary organisations in the delivery of B2B services			
F: Make best use of the development community  Map and update development community's support programmes to businesses  Carefully design financial incentives  Encourage the use and build capacities of BIOs			$\longrightarrow$

## Annex A: Defining firm sizes in Kyrgyzstan

The definition of firm sizes, including MSMEs, in Kyrgyzstan is based on both number of employees and turnover. The thresholds vary according to the sector, as shown in Table A.1.

*Individual entrepreneurs* are defined as entrepreneurs which are engaged in economic activities with gross revenues not exceeding the annual registration threshold for value added tax provided for by the Tax Code of Kyrgyzstan. Importantly, they are not counted as legal entities, and thus not captured in the table below.

Table A.1. Firm sizes classified by number of employees, turnover, sector

Activity	Micro	Small	Medium	Large					
Agriculture, Hunting, and Forestry		16.50 margle/ 51.200 ma							
Fishing and fish farming									
Mining industry	Um to 15 magnin/		51 200	51 200 magnla/	> 200 magnla/				
Manufacturing industry	Up to 15 people/ KGS 150 000	16-50 people/ KGS 500 000	51-200 people/ KGS 2 million	> 200 people/ > KGS 2 million					
Production and distribution of water, gas, and electricity	KGS 130 000	KGS 300 000	KGS 500 000	NGS 2 II	NGS 500 000 NGS 2 mmiles	KGS 200 000 KGS 2 minion	RGS 200 000 RGS 2 minion	KGS 300 000 KGS 2 IIIIIII0II	7 ROS 2 manion
Construction									
Trade									
Repair of cars, household goods and personal items									
Hotel and restaurant services									
Transport and communication									
Financial activities	Up to 7 people/			16-50 people/ KGS 2 million	> 50 people/ KGS 2 million				
Real estate transactions	KGS 230 000		38 500 000 KGS 2 million	KGS 2 million					
Rental and provision of services to customers									
Education									
Health and social services									
Provision of community, social and personal services									

Source: Government of Kyrgyzstan (1998[76]).

## **Annex B: Methodology**

#### Working groups and fact-finding missions

Within the framework of the project, the OECD Eurasia Competitiveness Programme (ECP) and the Government of Kyrgyzstan established a public-private Working Group to enhance the delivery of public and private business development services to the private sector in Kyrgyzstan. The Working Group met three times and brought together representatives from government agencies, the private sector, business associations, and other development partners. The ECP, with contributions from international experts and peer reviewers of selected OECD member and non-member countries, carried out data collection, analysis and consultations with stakeholders in Kyrgyzstan to identify businesses' priorities for enhancing private sector competitiveness. Data analysis also included a survey that was conducted in May-July 2019 (Annex C).

Several missions took place in preparation for the peer review of Kyrgyzstan:

- 13 February 2019: first working group meeting and launch of the project, overseen by the Ministry of Economy, in order to frame issues and share insights with local stakeholders:
- **14-16 May 2019**: fact-finding mission to Bishkek to interview BDS providers and launch the BDS demand survey;
- **16 July 2019:** second working group meeting to present the findings of the survey and showcase the Polish experience in order to discuss preliminary recommendations:
- 6 November 2019: third and final working group meeting with international experts to discuss the peer review note and its recommendations.

This draft report was submitted for digital peer review on 23 June 2020 at the seventh session of the OECD Eurasia Competitiveness Roundtable, a policy network that brings together high-level representatives and technical experts from Eurasian and OECD member countries and partner organisations. The Roundtable meets annually and serves as a platform for peer review and knowledge sharing on the implementation of competitiveness reforms in the Eurasia region. It will be facilitated by two experts who will provide an overview of their work related to business development and insights into the policy experience in OECD and Eurasian countries:

- Ms Martyna Wieczorek, from the Department of Small and Medium Enterprises under the Ministry of Economic Development of Poland; and
- Ms Adile Keshfetdinova, from the Public Services Agency within the Ministry of Justice of Uzbekistan.

The peer review is expected to help Kyrgyzstan define further steps for policy reform implementation. Progress towards implementing these recommendations will be discussed in two years' time at the 2022 OECD Eurasia Competitiveness Roundtable.

## **Annex C: Survey results**

In order to build a reliable understanding of the challenges and needs of MSMEs in Kyrgyzstan with regard to BDS, a survey was conducted in the scope of this report. 250 MSMEs in all regions of Kyrgyzstan were interviewed, and efforts were made to ensure that the sample is representative of the GDP composition of Kyrgyzstan's economy.

Table C.1. Surveyed firms by region/ size

			Micro (individual	
Region	Small	Medium	enterprises)	Total
Batken region	2	2	6	10
Jalal-Abad region	13	6	14	33
Issyk-Kul region	1	3	4	8
Naryn region	1	1	5	7
Osh region	1	3	15	19
Talas region	2	1	5	8
Chui region	16	14	15	45
Bishkek city	60	25	20	105
Osh city	8	4	3	15
Total	104	59	87	250

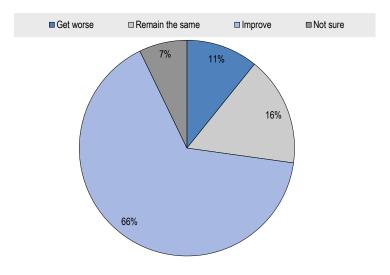
Source: OECD survey, 2019.

Table C.2. Surveyed firms by sector

Education	Manufacturing	Construction	Trade	Transport and communications	Real estate	Agriculture	Finance
19	52	30	61	24	9	43	12

Figure C.1. 66% of firms are optimistic about their business opportunities

In my view, my business opportunities during the next 3 years will:



Source: OECD survey, 2019.

Figure C.2. 49% of BDS were provided by private sources

Who provided the training, information or advice (BDS)?

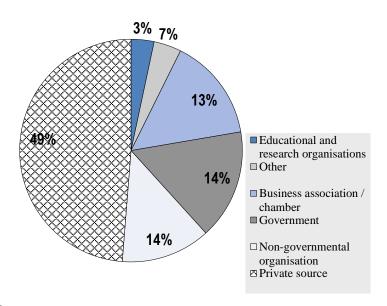
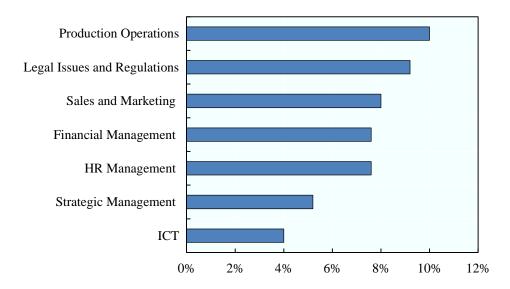


Figure C.3. 40.8% of firms have received training in all themes

In the last two years, have you or has the staff of your firm received any training on the following topics?



Source: OECD survey, 2019.

Figure C.1. 45% of training was delivered as seminars or roundtables

Which type of training did you receive?

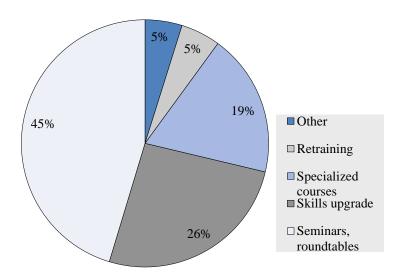
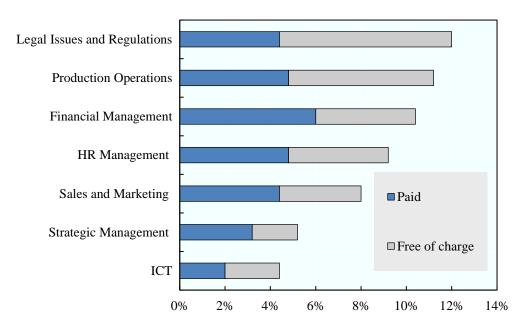


Figure C.2. 22% of firms sought external information, most prominently in Legal Issues and Regulations

In which area have you or the staff sought external information? Have you paid for this information?



Source: OECD survey, 2019.

Figure C.3. 29.6% sought external advisory or consulting services, mostly in Legal Issues and Regulations

In which area have you or your staff sought external advisory or consulting services?

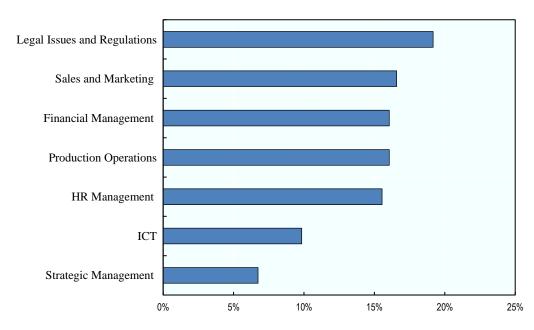
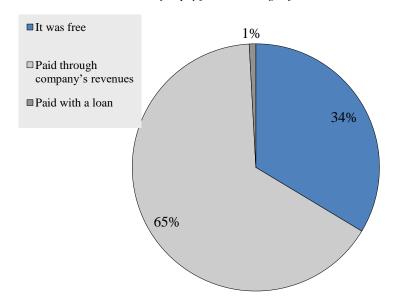


Figure C.4. 65% of BDS were paid through company revenues, with a third of services being offered for free

How did you pay for the training, information or advice?



Source: OECD survey, 2019.

Figure C.5. Lack of knowledge is clearly the main reason for requesting BDS

For the external advice/training that you obtained, what was the main reason that influenced your decision to obtain them?

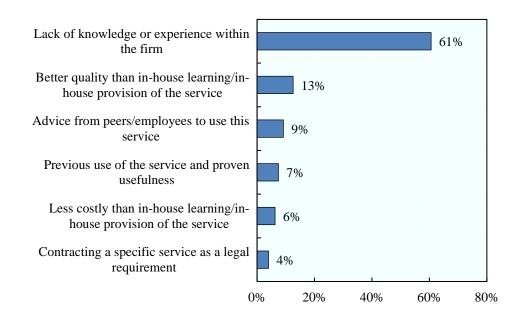


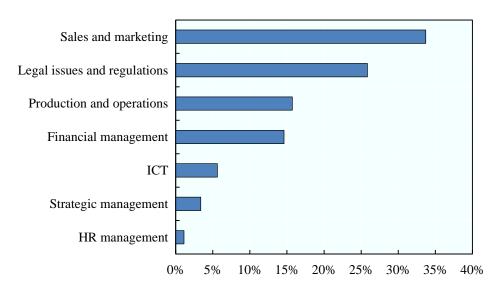
Table C.3 shows the size, region and sector of firms stating that they lack knowledge or experience within the firm. Overall 61% of firms indicated they lack internal capabilities, which is in line with JICA's findings: 71% have various problems with financial instruments, legal frameworks and tools, and 93% lack specialists to help them grow (JICA, 2019<sub>[35]</sub>).

Table C.3. 61% of all surveyed firms express a lack of knowledge or experience within the firm  $\frac{1}{2}$ 

Business Size	Individual	55%
	Micro	51%
	Small	67%
	Medium	50%
Region	Bishkek City	51%
	Batken Region	60%
	Chuy Region	65%
	Jalal-Abad Region	55%
	Naryn Region	33%
	Osh Region	50%
	Osh City	46%
	Issyk-Kul Region	50%
	Talas Region	83%
Sector	Education	47%
	Industry manufacturing	58%
	Construction	62%
	Trade	52%
	Transport and communications	44%
	Banking and financial activities	42%
	Real estate, rental, leasing	43%
	Agriculture	64%

Figure C.6. 36% of respondents were not able to receive external support in sales and marketing

In the past 12 months, did you need external support/advice, but you could not get it? Which areas?



Source: OECD survey, 2019.

Figure C.10. Sales and marketing as most expressed BDS, by firm size

In the future, in which area would you most likely seek external support on BDS?

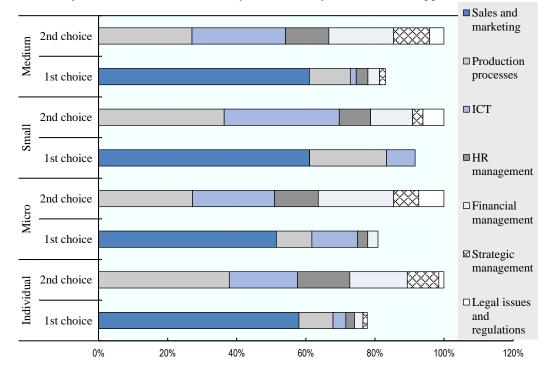
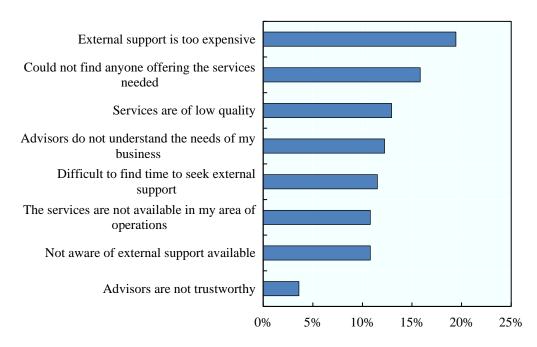


Figure C.11. 20% of firms state that BDS are too expensive – preventing them from accessing external support services

What was the main reason for not seeking external support?



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## SUPPORTING FIRM CREATION AND GROWTH THROUGH BUSINESS DEVELOPMENT SERVICES IN KYRGYZSTAN

National governments working to support firms facing the COVID-19 crisis have strong incentives to support entrepreneurship and private-sector development. As they struggle to survive the crisis, entrepreneurs and SMEs need accessible and high-quality public services. In addition to improving delivery of public services to firms, governments can help stimulate the market for private business services, such as business advisory or training.

This Policy Insight discusses the hurdles firms in Kyrgyzstan face in accessing public and private business development services (BDS). The report suggests three sets of actions to the government: (1) offering streamlined government to business services in physical and digital one-stop shops; (2) supporting greater uptake of private business services; and (3) working with other relevant actors, such as business associations and the development community to build a stronger BDS market, which can ultimately foster much needed business development.

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