ICR Review

Operations Evaluation Department

Report Number: ICRR10161

1. Project Data:	
OEDID:	L4051
Project ID:	P035762
Project Name:	Financial Sector Adjustment Loan (FSAL)
Country:	Kazakhstan
Sector:	Financial Adjustment
L/C Number:	L4051
Partners involved:	None
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2. Project Objectives, Financing, Costs and Components :

The Bank has supported Kazakhstan's stabilization and structural adjustment efforts through Technical Assistance and Rehabilitation Loans in FY94, and Financial and Enterprise Development and Structural Adjustment Loans in FY95. The Kazakhstan FSAL of 1996 provided US$180 million in two equal tranches to support the Government's financial sector reform program and underpin the overall economic reform effort. It will strengthen the framework for secured lending by allowing the mortgaging of land and permitting pledging of non real estate assets, bringing borrower accounting standards to international levels, and passage of bankruptcy legislation. It will foster development of banks, completing privatization of all but the specialized state banks, upgrading skills of bank managers, issuing a new chart of accounts for banks, and developing audit standards. Further, it would facilitate inter-bank payments and liquidity management, remove regulatory barriers to bank competition, tighten prudential supervision and resolve problem loans and problem banks.

3. Achievement of Relevant Objectives :

Most of the objectives of the loan were accomplished. A number of legal and regulatory reforms were implemented. Bankruptcy and Company Laws were introduced. Major proportions of non-performing loans were transferred to specialized debt resolution institutions. Non viable banks were closed and state banks were privatized and the number of banks has been reduced from 184 to 82. The number of banks in which the state holds shares was reduced from 73 to 5. New financial instruments have been developed and payments clearing centers have been established. Prudential regulation is being gradually tightened.

4. Significant Achievements :

The project has helped establish the basis for a sound financial system. As a result of the improved conditions for secured lending, there has been a significant increase in bank lending to the real sector. Increased soundness of banks is reflected in an almost 50 percent increase in individual savings accounts.

5. Significant Shortcomings :

No significant shortcomings are noted. A waiver was, however, required for release of the second tranche because the specific conditions relating to privatization or liquidation of a major problem bank, Alem Bank (successor to the former trade bank), were not met. When negotiations for its sale stalled, the Government chose not to liquidate it, fearing repercussions in the fragile financial market. Instead, it was merged with Turan Bank, a bank that had already been restructured and privatized. The combined bank TuranAlem was then drastically restructured and recapitalized. The government provided US$90 million for recapitalization and the Central Bank lent it US$60 million. The Government's shares in the merged bank have since been sold to private domestic investors. Thus, the original objectives of the project were met. However, it is not known what part of the cost of recapitalization was recouped through the sale or if the loan is being repaid.

6. Ratings:	ICR	OED Review	Reason for Disagreement /Comments
Outcome:	Satisfactory	Satisfactory	

Institutional Dev .:	Partial	Substantial	Considerable progress was made in strengthening the Central Bank and entrenching sound prudential regulations .
Sustainability :	Likely	Likely	
Bank Performance :	Highly Satisfactory	Highly Satisfactory	
Borrower Perf .:	Satisfactory	Satisfactory	
Quality of ICR :		Satisfactory	

7. Lessons of Broad Applicability :

The ICR suggests that some of the key elements of successful reform of the financial sector include : (1) denying insolvent enterprises access to banking system credit; (2) having government absorb the losses of non-performing loans it had directed banks to make, while giving the banks legal authority to work out the rest of their non-performing portfolio; (3) gradually easing entry of foreign banks over two to three years, while domestic banks are taking steps to become stronger and more competitive; (4) dividing banks into weaker and stronger groups, allowing stronger banks to engage in a wider variety of banking operations while they attain international banking standards, while restricting weaker bank's activities until they address their portfolio problems .

8. Audit Recommended? ○ Yes ● No

9. Comments on Quality of ICR :

The ICR is satisfactory.