ASSESSMENT OF THE FEASIBILITY OF IMPACT BONDS IN KYRGYZSTAN

FINAL REPORT

NOVEMBER 2021

The Report was carried out as part of the UN Joint Programme for the Development of the Integrated National Financing Framework in the Kyrgyz Republic in collaboration with National Partners.

Final Report:

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Project Name	**Integrated National Financing Framework (000119485)**
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Executive Summary

This pre-feasibility study explores the potential for an impact bond to be developed and implemented in Kyrgyzstan in the employability and professional and vocational skills development arena, with a particular focus on youth, women and disadvantaged populations.

Through implementation of the medium-term National Sustainable Development Strategy (2021 - 2026), the Kyrgyz Republic envisages a highly educated nation equipped for technological innovation. It wants a growth trajectory that is less dependent on migrant remittances, natural resources, and a large informal economy. Yet such innovation requires a skilled workforce. A significant share of the youth and adults in the Kyrgyz Republic remain low-skilled and skills do not meet the needs of the 21st century. The COVID-19 pandemic and its negative impact on schooling and vocational training are likely to have further exacerbated skills deficits. The return of migrants to Kyrgyzstan due to the pandemic are placing additional pressures on an already struggling domestic labour market.

Social and development impact bonds (SIBs and DIBs) are a relatively new financial innovation which have quickly attracted interest in the development sector. Under SIBs and DIBs, private investors provide *up-front capital* to an organisation or company to deliver certain services to disadvantaged populations, then receive back their investment, plus a return, *only if pre-agreed results are achieved.* These are called 'outcomes.' Governments reimburse investors in the case of social impact bonds (SIBs), while donors or philanthropic foundations repay investors in the case of development impact bonds (DIBs). SIB and DIB structures do not necessarily bring in *new* (additional) money to a development problem, but instead provide *upfront* working capital and a mechanism that incentivises success. SIBs and DIBs have been commissioned to address a variety of social and environmental problems, that span youth engagement, education, employment, homelessness, rural livelihoods and biodiversity.

Differently from traditional bonds, SIBs/DIBs are intended to improve the *delivery of services to a target population.* In contrast, traditional bonds, including green bonds and sustainable bonds typically finance *physical infrastructure* (e.g. renewable energy or green transportation).

There are 214 known impact bonds across 35 countries worldwide. The majority have been implemented in high-income countries Impact bonds have also been contracted in 14 low and middle-income countries. The overall impact bond market remains fairly small at about US$ 437 million invested to-date. They remain highly niche products with a US$ 3.3 million average upfront capital investment. The internal rate of return on investment for SIBs/DIBs can be as high as 12-13% but also as low as 2%. Some SIB/DIB structure allow investors to obtain higher interest rates or premiums if the project is particularly successful.

Several basic criteria are necessary for social or development impact bonds to come to fruition. These include: meaningful and measurable outcomes; prior evidence of success; presence of skilled service providers; evidence that the impact bond will produce cost savings to outcome payer(s); stable macroeconomic and political environment; appropriate legal framework; interest on the part of potential outcome payer(s); interest from the impact investor community.

Because SIB/DIB structures are complex to design and negotiate, they incur substantial additional transaction costs including intermediary services, technical assistance, evaluation, and legal fees. Being a young market, the start-up costs of SIBs/DIBs have been fairly high to-date. It is important to note that currently there is no conclusive evidence that impact bonds are better than other ways of delivering public services.

In Kyrgyzstan, the government has adopted several key state development programmes which may provide an opportunity to advance a social or development impact bond which strengthens professional and vocational skills in these *state strategic sectors*. These include digital skills, the agro-industrial sector, tourism, construction, energy, industry, transport and mining. It could have a focus on youth and/or other disadvantaged populations, including the “new poor” due to COVID-19. The Batken and Osh regions have been identified as high priority regions for an impact bond.

The measures would be expected to generate cost savings through a long-term increase in productivity and more employment in the formal economy. At the same time, it is also important to note that reaching vulnerable populations can be more costly and complex; as such, the impact bond must set realistic and achievable outcomes. Programmes, in turn, need to be anchored in a clear diagnosis of participant needs which should be analysed in subsequent phases of this work.

Government ministries indicated a strong interest in exploring ways to mobilise new sources of finance for tackling unemployment and building professional and vocational skills in Kyrgyzstan, especially amongst youth. Overall, however the social impact model is not widely understood. Experience with prior results-based financing mechanisms in primary healthcare in Kyrgyzstan showed the approach was not well understood and donors opted to use their own institutional procurement and evaluation processes rather than domestic systems.

Despite these challenges, there are other programmes in Kyrgyzstan, which could be built on and which an impact bond could link to. These include an Asian Development Bank funded ‘Vocational Education and Skills Development’ project and the FAO’s ‘Social Protection Plus/Cash +’ programme. Both provide an opportunity to potentially integrate – and test – an impact bond structure within existing national programmes and institutional structures, rather than arrange it as an independent (and more costly) short-term project. In addition, UNDP in Kyrgyzstan is currently developing a Cash+ concept focused on green jobs and the integration of vulnerable people into the labour market. This provides a further opportunity to align this research with broader impact bond feasibility.

Success Indicators that could be used include: training received, skills improvement (as measured by course completion and certification), job placement and job retention, including after 6 and 12 months. A transaction of not less than US$ 2-3 million is estimated to be a lower bound at which the associated transaction costs (structuring, measurement and evaluation) are considered worth it.

Initial analysis revealed that Kyrgyzstan has a fairly well-developed legal framework for an impact bond. A SIB/DIB could potentially be well covered by the provisions in its law on public procurement, its national investment law, and it Public-Private-Partnerships (PPP) law, which *inter alia* outline standard procedures for public procurement, provide for equal treatment between domestic and international service providers, provisions for dispute resolution, procedures in case of non-performance of contractual obligations, repatriation of profits, and tax advantages.

As such, the bottlenecks for implementation of a SIB/DIB are less on the legislative side and instead relate to issues such as: the lack of familiarity with the social impact bond model; lack of private sector trust in state authorities; poor record on PPP implementation thus far; insufficient local experts to prepare and deliver a social impact bond to a high standard; weak investment climate and poor sovereign credit rating; skewing of the labour market by a high reliance on remittances, which results in a high reservation wage, especially for women, and; too few high quality service providers due to a lack of investment in the sector.

Several next steps are recommended to advance this work:

The rationale for an impact bond needs to be clear. Further clarity is needed on what problem the impact bond is trying to solve. Impact bonds are most relevant as a financial instrument when they provide *innovations* in service delivery to target populations. A useful next step for this work therefore is to survey those involved in current programmes (service providers, students, employers, donors and relevant state entities) to understand where the current challenges and gaps are in current service provision so that an impact bond can be structured to address these.

Outcomes and interventions must be organised around a clear diagnosis of participants'/beneficiaries' needs. Interventions also need to be developed in consultation with local stakeholders. In the next phase, analysis needs to be undertaken by institutions with a local presence to understand target populations' needs and design a mix of interventions best suited to meet those needs.

While impact bonds should test new and innovative ways to reach target populations, there should be clear evidence that interventions have a strong prospect of success, otherwise investors and outcome payers are not likely to back them. In the next phase of work, it will be important to evaluate which service providers have a strong track record in delivering high quality educational and training services. 'Market testing' days where prospective service providers are invited to learn about SIBs/DIBs and how to ultimately bid to become a service provider could be useful in the next phase of work.

A development impact bond is probably more suitable than social impact bond. The Kyrgyz Republic is classified as a lower-middle-income country, and is at moderate risk of debt distress. Borrowing on concessional terms is recommended as the most suitable and sustainable form of loan financing to preserve debt sustainability. Because social impact bonds usually carry market rates of return for investors, and are likely to be repayable in hard currency, a donor agency (or agencies) would likely be the most suitable outcome payer(s), rather than the Kyrgyz state. Several donors consulted for this study expressed an interest *in principle* in the model (like the Asian Development Bank and USAID), but also emphasised that further work was needed to identify suitable labour market interventions. There could also be further work undertaken to see how contributions from the extensive Kyrgyz diaspora could be integrated into an impact bond financial structure.

Further socialisation of the overall model is needed. Interviewees expressed an interest in learning more about success stories from other countries, and UNDP could curate a series of presentations from those involved in SIBs/DIBs in other countries, including Colombia, India, Uzbekistan and Finland.

A plan on how to 'institutionalise' the impact bond will be important to achieve lasting impact. Linking the bond to institutions like the Skills Dev elopement Fund and programmes like Cash+ which aim to reach vulnerable populations will help to integrate the project with existing labour market services and turn it from a (more costly) short-term project into an initiative which could be implemented over a longer-term time horizon.

Looking forward, while it is true there are significant labour shortages in the market, it is important to understand whether these are due to a lack of skills, or due to other factors like poor pay and conditions, or the high reservation wage due to remittances. With unemployment so high, and above official figures, there is also a significant surplus of labour. An impact bond can play a part on the *supply side* to boost skills and employability, but it is important to note that it cannot on its own overcome structural problems in the labour market.

Introduction

In 2020, the UN in the Kyrgyz Republic received financial support from the UN Joint SDG Fund to develop an Integrated National Financing Framework (INFF). The aim of the INFF in the Kyrgyz Republic is to support the government to identify financing options which can support the implementation of the long-term National Development Strategy (NDS) 2018-2040, and the medium-term National Development Programme 2021 - 2026 with a particular focus on the private sector.

It is recognised that achieving the aims of the NDS will require significant investments and financing from a range of public and private sources. This has now become even more important in the context of recovery from the devastating socio-economic impacts caused by the COVID-19 pandemic.

To support the mobilisation of new sources of finance, and enhance the impact of public and private finance, UNDP has commissioned this pre-feasibility study which explores the potential for an impact bond to be developed and implemented in Kyrgyzstan in the employability and professional and vocational skills development arena, with a particular focus on youth and disadvantaged populations.

Through implementation of the medium-term National Sustainable Development Strategy (2021-2026), the Kyrgyz Republic is planning for technological innovation, and a growth trajectory that is less dependent on migrant remittances, natural resources, and a large informal economy. Yet such innovation requires a skilled workforce. A significant share of the youth and adults in the Kyrgyz Republic remain low-skilled and skills do not meet the needs of the 21st century. In the Kyrgyz Republic, job creation is slow and lags behind the pace of demographic growth. The labour market is increasingly seeking adults with strong foundational skills; however, a large portion of adults in the Kyrgyz Republic perform well below this foundational level. Firm and worker productivity remain the lowest in the region. Wide disparities in access to jobs among youth and women exacerbate this challenge.

The COVID-19 pandemic and its negative impact on schooling and vocational training opportunities are likely to have further exacerbated skills deficits. These deficiencies are likely to affect not only today's students in the short-term, but also the skills proficiency of the future workforce and adults over the long-term. These challenges have been further exacerbated by the return of migrants to Kyrgyzstan, placing additional pressures on an already struggling domestic labour market.

Raising human capital can build a skilled and enterprising workforce, allowing the Kyrgyz Republic to reap the economic dividends of a youth bulge, be resilient to disruptive technology, and create high quality formal-economy jobs for its large and fast-growing young population.

In this context, this pre-feasibility report looks at the feasibility of applying a social or development impact bond model to professional and vocational skills development, employability and services that aim to foster entrepreneurship. It is based on interviews with key stakeholders in Kyrgyzstan from within the government, international donor community and potential partner organisations, as well as those with experience of the impact bond market. It is combined with a desk review of key materials related to social and development impact bonds, and includes several case studies that have involved UNDP as a partner. UNDP's role in each of the case studies is briefly outlined.

The report is structured as follows:

Section 1:
Provides an introduction to social and development impact bonds. It outlines how the model works, how they have been used, the rationale behind impact bonds, their pros and cons, and core feasibility criteria. The section also includes relevant case studies and explains the ways in which UNDP has engaged with various impact bonds to-date. It also briefly explains the difference between impact bonds and "conventional" bonds.

Section 2:
Explores the development imperative behind a focus on the labour market and skills development in a social impact bond. It explores potential indicators that could be used, experience with other results-based financing mechanisms, the adequacy of the legislative environment, potential partners to an impact bond and potential bottlenecks to implementation. A matrix is presented which assesses Kyrgyzstan's overall level of 'readiness' for an impact bond based on core feasibility criteria.

Section 3:
Outlines a series of recommended next steps for this work, including research requirements and stakeholder engagement.

Box 1: Links to the Integrated National Financing Framework

This study contributes to the development of an Integrated National Financing Framework in Kyrgyzstan in the following key ways:

1. Supports the strategic planning and allocation of public and private finance
2. Supports policymakers in Kyrgyzstan to build an understanding of new ways to unlock public and private finance in support of the SDGs
3. Strengthens the efficiency of public and private finance
4. Strengthens the policy environment for various sources of public and private finance
5. Grows partnerships with a broader range of actors in mobilising and implementing financing

Section 1: An Introduction to Impact Bonds

Introduction to impact bonds

Social and development impact bonds (SIBs and DIBs) are a relatively new financial innovation which has quickly attracted interest in the development sector. Under SIBs and DIBs, private investors provide *up-front capital* to an organisation or company to deliver certain services to disadvantaged populations, then receive back their investment, plus a return, *only if pre-agreed results are achieved.* These are called 'outcomes.' In the literature, SIBs and DIBs are also referred to as "payment for success", "payment for results" and "cash on delivery" mechanisms.

Outcomes can vary but should be *simple, measurable* and *specific*. Governments reimburse investors in the case of social impact bonds (SIBs), while donors or philanthropic foundations repay investors in the case of development impact bonds (DIBs). The term DIB is used when: 1. implementation takes place in a developing country, and; 2. a donor agency or philanthropy is the outcome funder/payer. They are different from typical development loans, which are repayable by the sovereign state irrespective of whether the activities funded are successful.

Under the model, risks are shifted from the public to the private sector and the model is meant to incentivise innovation and success. It is important to emphasise that SIB and DIB structures do not necessarily bring in *new* (additional) money to a development problem, but instead provide *upfront* working capital and a mechanism that incentivises success. Impact bonds are part of a growing trend in 'impact investing' – one which is likely to continue to expand in future years.

SIBs and DIBs have been commissioned to address a variety of social and environmental problems, that span youth engagement, education, employment, homelessness, rural livelihoods and biodiversity.

Social and development impact bonds by the numbers

The impact bond market is growing steadily and has spread across many world regions. There are 214 known impact bonds across 35 countries worldwide.[1] The majority have been implemented in high-income countries with the US and UK in the lead. Impact bonds have also been contracted in at least 15 low and middle-income countries. These are: Argentina, Cambodia, Cameroon, Colombia, Democratic Republic of the Congo, India, Kenya, Mali, Myanmar, Nigeria, Palestine, Peru, South Africa, Uzbekistan and Uganda. The main areas of interventions are health (6 DIBs), employment (6 DIBs), education (3 DIBs), social welfare (2 DIBs), agriculture and the environment (2 DIBs).[2] As such, Kyrgyzstan's interest in impact bonds in the employment arena is consistent with prior use of the instrument.

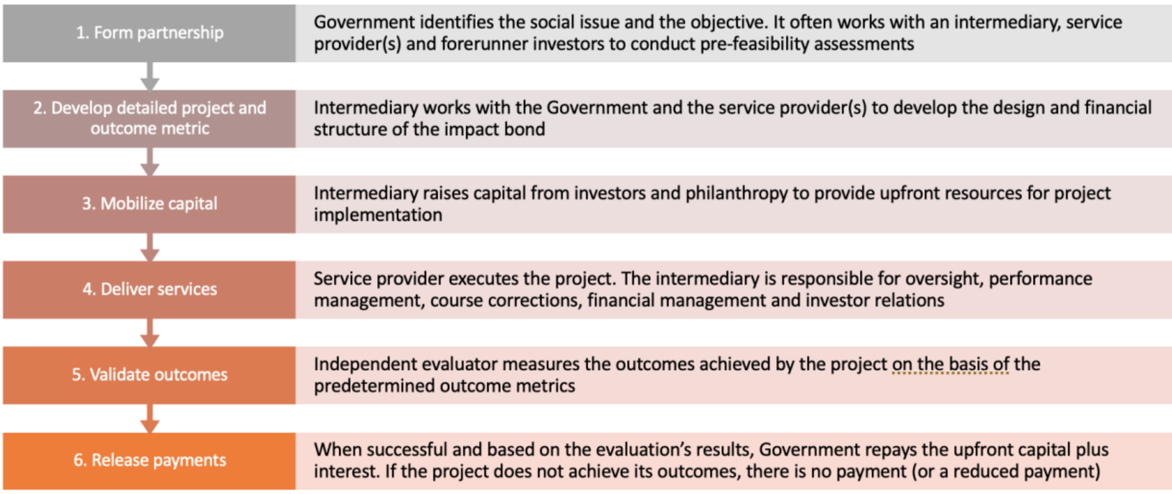
[1] Brookings Institute, Social and development impact bonds by the numbers, June 2021: https://www.brookings.edu/research/social-and-development-impact-bonds-by-the-numbers/
[2] Brookings Institute, Social and development impact bonds by the numbers, June 2021: https://www.brookings.edu/research/social-and-development-impact-bonds-by-the-numbers/

The overall impact bond market remains fairly small at about US$ 437 million invested to-date.[3] They remain highly niche products with a US$ 3.3 million average upfront capital investment.[4] Most impact bonds are implemented over an average 4-year project timeframe.

Impact Bonds: How they work

There are six key steps involved in the impact bond process. These are:

Figure 1: Key steps in the impact bond process



Source: Author's adaptation from Social Finance and UNDP[5]

Performance metrics

Under an impact bond structure, the government (and/or donor), investors and service providers need to agree on the *performance metrics* and the *timeframe* over which results will be measured. It is important to bear in mind there can be *primary* performance metrics (e.g. number of girls that enrol at school) as well as *secondary* performance metrics (e.g. *how well* they do at school). Achievement of these performance metrics will trigger the release of payments to the investor(s).

Financial structure

The various parties also need to agree on the financial structure of the impact bond. SIBs/DIBs can have more than one investor, and these investors may in turn receive a differentiated rate of return on their investment depending on how much risk they wish to assume.

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[3] Brookings Institute, Social and development impact bonds by the numbers, June 2021: https://www.brookings.edu/research/social-and-development-impact-bonds-by-the-numbers/
[4] Source: https://www.brookings.edu/wp-content/uploads/2019/01/Impact-Bonds-Snapshot-August-2019.pdf
[5] For further details, see: https://socialfinance.org/social-impact-bonds/

For example, a SIB/DIB might establish a multi-layered capital structure featuring *senior* investors (those with highest priority in repayment if outcomes are met), *subordinate* investors (those with lower rank in repayment if outcomes are net), *recoverable grants* (sums that are repaid at same value if outcomes are met), *non-recoverable grants* (non-repayable sums irrespective of outcome) and *guarantors* (entities that may guarantee some repayment to investors in the event outcomes are only partially met or not met at all).

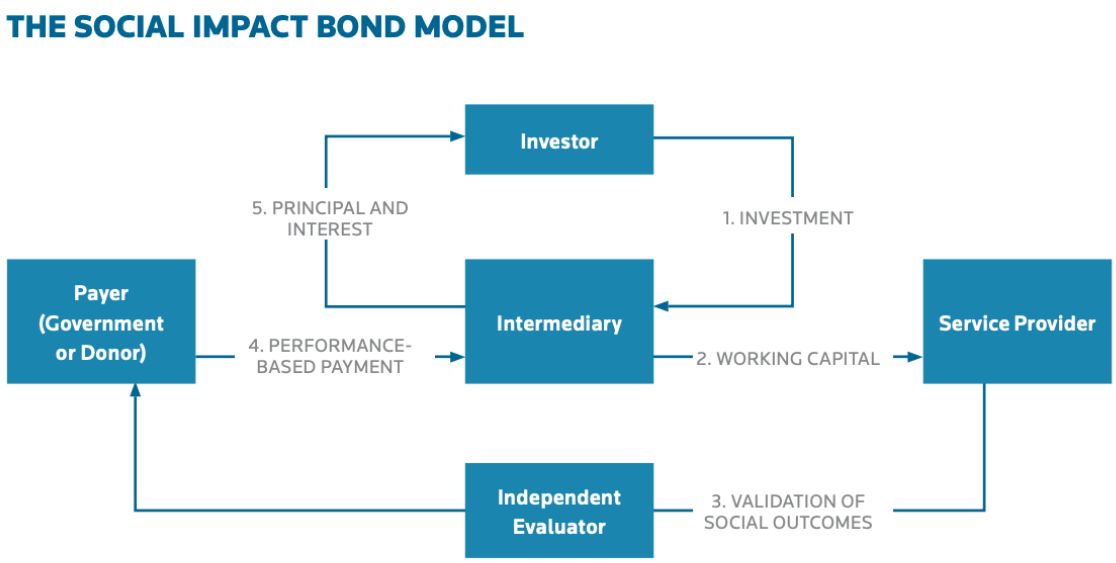
The internal rate of return on investment for SIBs/DIBs can be as high as 12-13% but also as low as 2%. Some SIB/DIB structure allow investors to obtain higher interest rates or premiums if the project is particularly successful.

Performance management

The SIB/DIB partners must also agree on the entity that will be responsible for measuring the extent to which the results/outcomes have been achieved, in most cases an independent third party. It is an essential precondition that performance can be measured in a timely, efficient and cost-effective manner, otherwise a SIB/DIB will not be possible.

Because SIB/DIB structures are complex to design and negotiate, they incur substantial additional transaction costs including intermediary services, technical assistance, evaluation, and legal fees. These transaction fees may be paid from the capital raised. Being a young market, the start-up costs of SIBs/DIBs have been fairly high to-date.

Figure 2: Impact Bonds: How they work



Source: Instiglio

Box 2: Social and development impact bonds: key stakeholders

Impact bonds require a close partnership between various public and private stakeholders. The main types of actor involved in the process are:

- **Outcome funder:** The Government or donor (aid agency or philanthropic entity) is responsible for paying back the principal and interest if the pre-agreed outcomes are achieved. They are called 'outcome funders'. In a DIB, the donor agency will repay the investor(s) instead of the Government.
- **Intermediary:** Receives the loan from the investor(s) and allocates this finance to the service provider for project execution. They help to ensure transparency and accountability for funds in DIB operations.
- **Investor(s):** institutions or individuals that provide upfront capital as a loan or other similar contractual arrangement to the intermediary or special purpose vehicle created to manage the SIB/DIB. The investors accept the financial and operational risks of the project in exchange for an interest payment. The SIB/DIB may be constructed as a multi-layered capital structure in which there are senior and subordinate investors, i.e. they accept differentiated levels of risk and return in a SIB/DIB structure.
- **Guarantors:** Third party that contributes to the partnership by offering a loan guarantee—often as a grant—to reduce the investor's risks. A few of the first SIBs in the United States had guarantors.
- **Service provider(s): independent** government entity, cooperative, NGO or private enterprise that executes the interventions required to achieve the desired outcomes. It signs a contract with the intermediary.
- **Evaluator:** the entity (e.g. consultancy, research institution, university) requested to confirm the achievement of the outcomes required to release repayments.
- **Beneficiary:** the population that benefits from the project financed by the SIB.

Why choose an impact bond? What is the rationale? Why are they attractive?

If impact bonds are complex and incur additional transaction costs, why use them? The original rationale of SIBs was to support projects that—if successful—result in cost-savings (or avoided costs) for the government that are large enough to repay the initial investment (capital plus interest). For example, the first SIB was launched in the UK to fund the rehabilitation of ex-prisoners from jail and reduce recidivism (reconviction rates).[6] The costs associated with criminal justice are extremely high so a large enough reduction in the rate of reconviction leads to cost-savings for the government. In this example, Social Finance—the intermediary—raised approximately US$ 8 million from 17 investors, and investors were paid back with an interest ranging from 2.5 to 13% by the Ministry of Justice and a philanthropic partner if the programme reduced recidivism by at least 7.5 %. The results for the first cohort of prisoners showed an 8.4% reduction in reconviction.[7]

[6] Social Finance UK
[7] Social Finance UK

For governments and donors, SIBs/DIBs can be an attractive option since they pay for results *ex post*, i.e. only when they are achieved. If the project fails to deliver, the government or donor(s) does not pay and the investors will lose part or all of their capital. From a public finance perspective therefore, SIBs/DIBs can ensure the effective use of scarce public funds. It can therefore ensure greater value added for taxpayer money than traditional grant approaches.

SIBs/DIBs may also be an instrument of choice when a government cannot invest in a social project despite the expectation of accruing both substantial cost savings and positive social/environmental outcomes. The government (or donors) might not be able or willing to invest in the first instance due to limited access to finance or the difficulty of accepting the project's risks. SIBs are most appropriate:

- When focusing on areas of priority for both the public sector and investors, particularly preventive actions and conservation measures;
- The additional cost of the intervention can be offset by the potential cost-savings;
- There is solid evidence backing the project's outcome metric.

Because SIBs/DIBs measure only outcomes (not project activities), they are also meant to foster innovation in service delivery to beneficiaries, while also foster collaboration amongst a diverse set of actors, as well as de-risk interventions from a public sector perspective. However, as discussed later, the extent to which impact bonds do actually foster innovations in service delivery remains an open question as investors may be more wary of approaches that are not tried and tested.

Current evidence on impact bonds

Despite these features, it is important to note that currently there is no conclusive evidence that impact bonds are better than other ways of delivering public services. There have also been few evaluations of impact bonds as a whole in developing countries.

Several studies have pointed to lessons learned from early experiences with impact bonds in developing nations. For example, a UK Department for International Development (DfID) study revealed a number of findings in relation to impact bonds in four DIBs (in India and several African countries).[8] These revealed that service providers welcomed the upfront capital that impact bonds provide, but noted that in many countries, there are very few capable service provider organisations. Investors meanwhile were concerned about reputational risk as the use of an impact bond structure brought heightened attention to the project, increasing exposure should results not materialise. While the DIBs evaluated fostered collaboration across partners, it also made the negotiation process more complex and less efficient.

Lessons learned from the Wildlife Conservation Bond for rhino protection (covered later in this section) revealed a need to identify – and involve – outcome payers and investors early in the impact bond development process. Specialist intermediary entities can help to identify and drive the final

[8] See: https://iati.fcdo.gov.uk/iati_documents/49920063.pdf

selection. Strong Theories of Change show the clear link between intervention, impact and final outcome.

The Brookings Institute meanwhile has explored the evidence as regards the extent to which social impact bonds actually deliver on the claims commonly made about them. The results of this 2016 study are summarised in the table below – though it should be noted that this research looked at social impact bonds in both developed and developing countries.

Table 1: Brookings Institute: extent to which impact bonds meet common claims

Common claim about impact bonds	Is this claim being met?	Is there room to grow?
Impact bonds crowd-in private capital	Yes, but this does not necessarily equate to *additional* capital	Yes
Impact bonds prioritise prevention	Yes	Yes. It is recommended to focus on younger children to achieve larger societal benefits
Impact bonds reduce risk for government	Yes, but not all risks are mitigated	Solid due diligence is required before entering into deals
Impact bonds shift focus to outcomes	Yes	N/A
Impact bonds achieve scale	No	Possibly, through impact bond funds
Impact bonds foster innovation	Evidence is mixed. Mostly no, but some services have been provided in new combinations, to new populations, or in new settings.	There is greater scope to work in conjunction with innovation platforms
Impact bonds drive performance management	Yes, but there is limited evidence of course correction in implementation	Yes, through the use of real-time data
Impact bonds stimulate collaboration	Yes	Yes, new players often face challenges to become involved
Impact bonds build a culture of monitoring and evaluation	Too early to say	Yes
Impact bonds sustain impact	Too early to say	Yes

Source: Brookings Institute[9]

[9] See: https://www.brookings.edu/wp-content/uploads/2016/07/Impact-Bondsweb.pdf

Impact bond feasibility criteria

Several basic criteria are necessary for social or development impact bonds to come to fruition. These include:

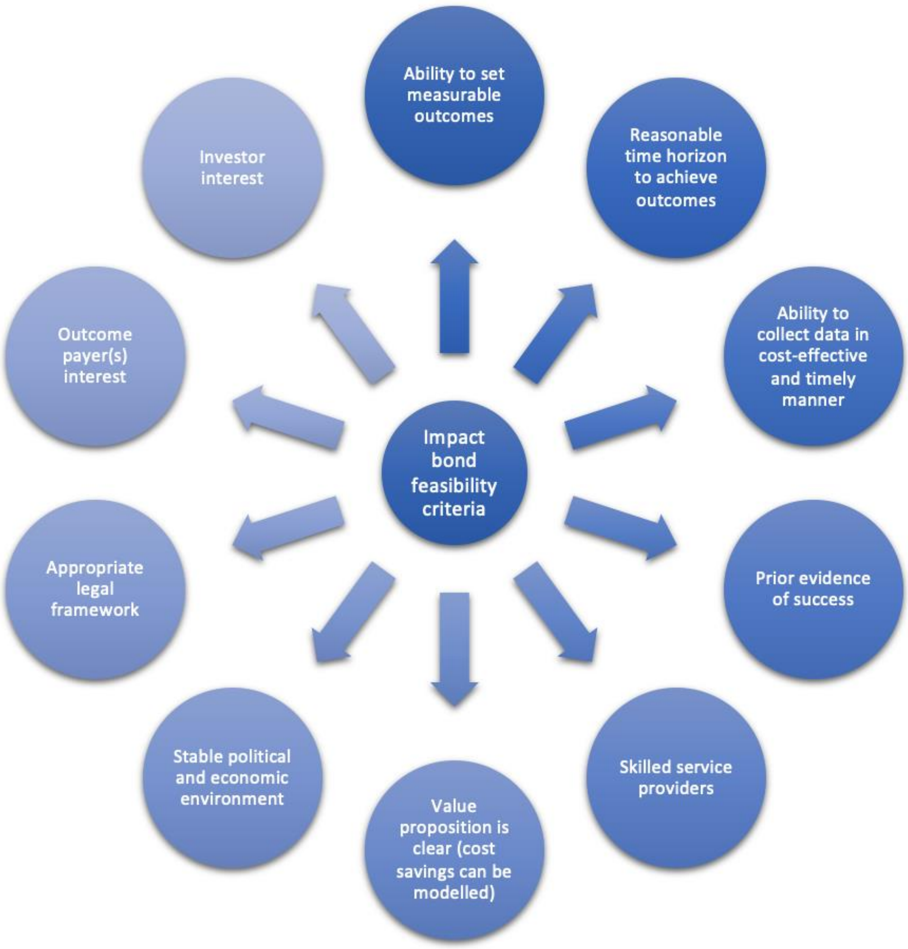
1. **Meaningful and measurable outcomes.** SIBs/DIBs require a robust metric (or metrics) to measure performance. The milestones for releasing payments to investors must be simple, verifiable and realistic. There must also be a reasonable timeline to achieve the outcomes. While the payment for success model is theoretically applicable to both developed and developing countries, challenges related to the collection of data for monitoring the extent to which outcomes have been achieved can be comparatively more difficult and costly in low-income countries. These considerations need to be factored into any analysis as to the viability of an impact bond.
2. **Prior evidence of success.** Both investors and outcome payer(s) will look at the extent to which previous interventions in the thematic area have been successful, and what strategies contributed to success. While impact bonds can help to fund innovations in service delivery to beneficiary groups, investors and outcome payer(s) are also unlikely to want to fund untested high-risk interventions.
3. **Presence of skilled service providers.** Service providers should have a strong track record of successful interventions in the thematic area, should be dedicated to the impact bond and must have the confidence of investor(s) and outcome payer(s). Service providers should take a proactive role in the design and implementation of the impact bond, since the impact bond is ultimately raising funds for their work. They must be able to understand - and meet - the challenges and rigours of the impact bond model. This includes the ability to adapt and course correct where changes to may be needed to the ways in which services are being delivered.
4. **Evidence that the impact bond will produce cost savings to outcome payer(s).** Impact bond models should generate meaningful long-term savings for outcome payer(s). This is one of the key attractive features of the financial model (its value proposition) and cost savings should be modelled in the design phase.
5. **Stable macroeconomic and political environment.** Impact bonds models are unlikely in countries where there is considerable economic and political instability, since this increases risk and uncertainty for both investors and outcome payers. As outlined in the following section, these factors may add risk to an impact bond project in Kyrgyzstan, as well as reduce donor appetite.
6. **Appropriate legal framework.** It is important to understand how to structure the legal relationship among the participating entities. These include issues such as procurement for services under the impact bond, taxation, governments/donors' abilities to contract across fiscal cycles and enforcement mechanisms.
7. **Interest on the part of potential outcome payer(s).** This is the government under a social impact bond, or a public or philanthropic donor in the case of a development impact bond. The payer willingness to engage in impact bond negotiations is the most important element, if not a pre-condition. It is critical to secure outcome payers upfront and ensure they are engaged through the product development. Outcome payers often have requirements for committing funding and these should be built into product design. Finally, donors are more

likely to fund interventions that are strongly aligned with national sustainable development priorities.

8. **Reasonable interest from the impact investor community.** Market research into prospective investors is required. It is also critical to develop a compelling "impact narrative" or storyline around the impact bond. Representatives from the investment community should also be involved in the development phase of the impact bond. Both investors and outcome payers must be comfortable with impact measurement processes.

The next section of this report evaluates Kyrgyzstan's "readiness" for an impact bond next to this expanded set of core feasibility criteria.

Figure 3: Social and development impact bonds: core feasibility criteria



Source: Author, 2021

What are the pros, cons, and risks?

The SIB/DIB model offers financial incentives and a structured approach to assess projects and measure results. However, the achievement of the impact still depends on the design of the projects financed. SIB/DIB models have a number of advantages, disadvantages and risks that must be carefully evaluated when considering whether this model is the most feasible or desirable approach. These are summarised in the table below.

Table 2: Impact bond pros, cons and risks

Impact Bond Advantages	Impact Bond Disadvantages	Risks
For *governments/donors*, SIBs/DIBs can reduce or minimise financial and operational risk while promote investment in social/environmental projects	Complex and time-consuming to design and negotiate with the various partners involved (feasibility and design phases can take several years)	Underlying project risks must be thoroughly assessed and priced. This is not always easy to do
Can result in cost savings for governments/donors if projects are successful	Impact bonds are not widely understood and knowledge about these instruments in not yet widespread	Investors may lobby for lower "success thresholds" so that they are sure to be repaid something
Helps to ensure public resources are well-spent on projects that have a measurable positive social/environmental impact, and projects are de-risked for the public sector	Requires verifiable quantitative metrics, which can be difficult to formulate for some projects. These results must in turn be able to be measured over a relatively short time-period. Challenges related to the collection of data for the design and monitoring of the outcome matrix can be comparatively more difficult and costly in low-income countries	Profit as incentives for investors may compromise social impact in exchange for higher return or lower risk. Trade-offs may exist in the selection of projects between the need to attract investors versus achieving more ambitious development objectives
For *investors,* SIBs/DIBs offer a “mission-aligned” investment opportunity, as well as a return on investment	The intricate structure of negotiations, coordination and implementation generate comparatively high administrative/transaction costs	The introduction of a profit incentive may negatively change the relationship between the service providers and beneficiaries
For *service providers,* SIBs/DIBs offer access to upfront finance for the delivery of services	Requires capable local service providers to deliver interventions	Critics of SIB/DIBs underline risks they may be used to promote the privatisation of critical social services
For service providers, enables greater flexibility in the delivery of	May not actually foster innovation in service delivery since investors and	

interventions since only outcomes, rather than activities, are measured	donors only want to fund *proven* models of intervention	
Introduces rigorous approaches to performance management and results measurement. This can help to achieve higher standards in programme design and delivery	Project interventions cost more than they would have done had they been financed via other more traditional financial instruments so the extent to which they remain value for money is an open question	
Financial instrument designed to improve service delivery and incentivise success	Too few experiences in developing countries to be able to draw conclusive evidence from	
Offers the potential to form new collaborations on critical social and development issues between public and private actors	Few investors and donors ready to invest in the model, in part due to reputational risk	
Helps secure relevant and up to date data, which can help decision-making across a variety of areas, not limited to the impact bond	Typically fund smaller niche interventions; there is limited evidence on the extent to which the model is scalable	

Box 3: How are impact bonds different from other bonds and from other forms of public-private partnership?

It is important to clarify that impact bonds are not bonds in the conventional sense. Impact bonds are very different to traditional "vanilla" bonds and other "themed" bonds that have emerged over recent years (such as 'green' bonds and 'sustainable' bonds).

Differently from traditional bonds, SIBs/DIBs are intended to improve the *delivery of services* (e.g. support services for the homeless or prisoners, child care, ecosystems conservation, etc.) with bondholders (i.e. initial investors) repaid only when pre-agreed results are achieved. With impact bonds, the risk sits with i*nvestors*.

In contrast, traditional bonds, including green bonds and sustainable bonds typically finance *physical infrastructure* (e.g. renewable energy or green transportation). This means they finance *capital stock accumulation*, not *service delivery*. With traditional bonds, investors are repaid according to the coupon (interest) rate and payment schedule set when the bond was issued, irrespective of whether the underlying project(s) financed are successful or not. As such, the risk sits with the entity which issued the bond (government or corporate entity). These bonds also increase government debt.

Green bonds and sustainability themed bonds have mushroomed in recent years, as interest in sustainability has increased; new financial instruments have emerged to cater to a growing pool of investors who wish to invest with both profit and purpose in-mind. Green bond issuance – by both sovereign and corporate issuers – came in at US$ 297 billion in 2020 across over 90 countries worldwide. Meanwhile US$ 248 billion in social bonds were issued in the same year. Most recently, pandemic-themed bonds have emerged from China.[10]

Most issuance has occurred in developed countries (for example European countries accounted for 55% of the green bond market in 2020), and issuance remains relatively small across many developing countries. Larger emerging economies like China, Thailand, Mexico, Chile, Colombia and Nigeria have all issued various kinds of green bond or sustainability themed bond. It is important to note that while there is no single universally-accepted definition as to what constitutes a 'green' bond or a 'social' bond, the International Capital Markets Association (ICMA) has developed a set of widely used principles, which are intended to provide clarity around eligible project categories, and comparable transparency and disclosure frameworks.[11]

Impact bonds also differ from other widely-used forms of public-private-partnership (PPPs). Under common PPP structures, private financiers provide capital for government projects and/or services upfront (similar to an impact bond). However, under PPPs, private financiers are repaid using revenues from the project(s) funded, and the private financier often has long-term operating and revenue rights under the project. They are typically used in transport and other infrastructure projects, like wastewater treatment and hospitals etc. where fees are collected from users which are used to repay private finance providers.

Themed bonds: a description	
Green bonds	Bonds dedicated to environmental benefits (e.g. renewable energy, low-carbon transportation, energy efficiency in buildings etc.)
Blue bonds	Bonds dedicated to environmental improvements connected to marine environments (e.g. sustainable fisheries and aquaculture)
Social bonds	Bonds dedicated to social benefits (like affordable basic infrastructure, affordable housing, access to finance and employment creation)
Sustainability bonds	Bonds dedicated to both social and environmental benefits, often marketed as aligned with the SDGs
Pandemic bonds	Bonds exclusively dedicated to the COVID-19 response

Country case studies and UNDP engagement in impact bonds

UNDP has been involved in the conceptualisation and design of several impact bonds over recent years. It is a relatively new area for the organisation, however it is steadily increasing its technical expertise on the instrument under the broader umbrella of UNDP's Finance Sector Hub.

Most of the social impact bonds UNDP has been involved in to-date are at the *development* stage; only one has so far progressed to the implementation stage (the Wildlife Conservation Bond in Southern Africa – detailed below). Several have also been discontinued which illustrates just how difficult it can be to get social impact bonds "over the line". Most recently, UNDP in India and the Pimpri Chinchwad Municipal Corporation (PCMC) signed an agreement to develop a social impact bond targeting healthcare services in India, with the local municipality (PCMC) acting as the outcome funder. As with others, this impact bond is at an early stage of development.[12] The country case studies below provide a snapshot of some of the main impact bond initiatives that have involved UNDP to-date, and the impact bond structures that are being used or have been proposed. One of UNDP's key roles to-date has been to identify possible entry points for an impact bond and to finance early-stage feasibility studies, sometimes in support with other development partners (like the European Bank for Reconstruction and Development – EBRD – which is co-developing a second stage feasibility study for an impact bond in Armenia targeting dairy farmers.

Interviews with various stakeholders in Kyrgyzstan revealed a strong desire to learn more about impact bond experiences in other countries. One option for UNDP is therefore to curate a series of discussions for Kyrgyz officials, NGOs and other stakeholders with organisations and funders that have been involved in impact bonds in other countries. This could help to socialise and educate on the impact bond model, while offer the opportunity to share lessons learned and enable Kyrgyz stakeholders to ask questions from those who have direct experience in the field.

[10] See: https://www.climatebonds.net/

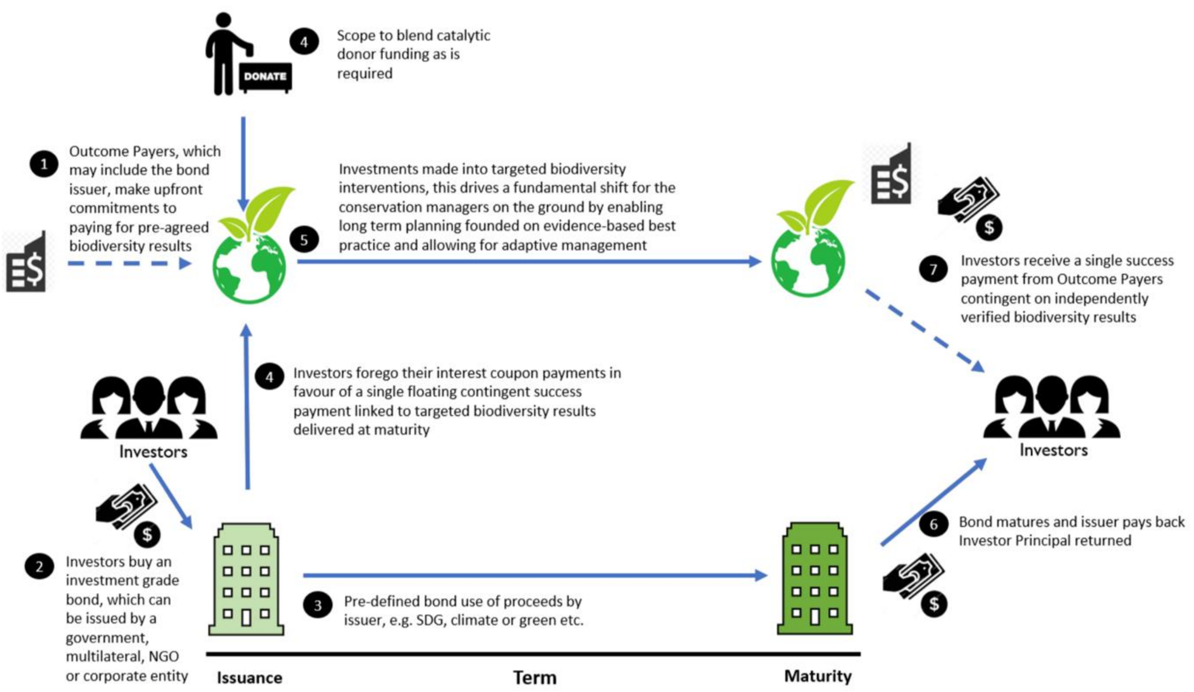
[11] See: ICMA Green Bond Principles: https://www.icmagroup.org/sustainable-finance/the-principles-guidelines-and-handbooks/green-bond-principles-gbp/

[12] See: https://economictimes.indiatimes.com/news/politics-and-nation/undp-and-pimpri-chinchwad-municipal-corporation-to-co-create-indias-first-social-impact-bond/articleshow/80012354.cms

Table 3: Wildlife Conservation Bond: South Africa

Wildlife Conservation Bond	
Country	South Africa
Status	Early implementation
Lead organization(s)	
Implementation partners	UNDP, the Royal Foundation, UK Aid and Zoological Society of London (ZSL)
Private investor(s)	Rhino bonds will be sold by the World Bank on international capital markets
Outcome Funder(s)	Global Environment Facility
Type mechanism	Development impact bond
Volume financing	US$45 million
Implementation period	5 years
Scope of mechanism	Wildlife conservation (rhinos)
Outcome metrics	Increase rhino population by 4% per annum
Investor rate of return	Returns for investors will be determined by the rate of growth of the populations of the animals (rhinos) in two South African reserves
Independent evaluator	
UNDP's role	Implementation partner
Observations	The development of the "Rhino" bond was paid for by the Global Environment Facility (GEF). Technical support was provided by ZSL, Conservation Alpha, Credit Suisse, Conservation Capital, DLA Piper

Figure 4: Wildlife Conservation Bond Structure

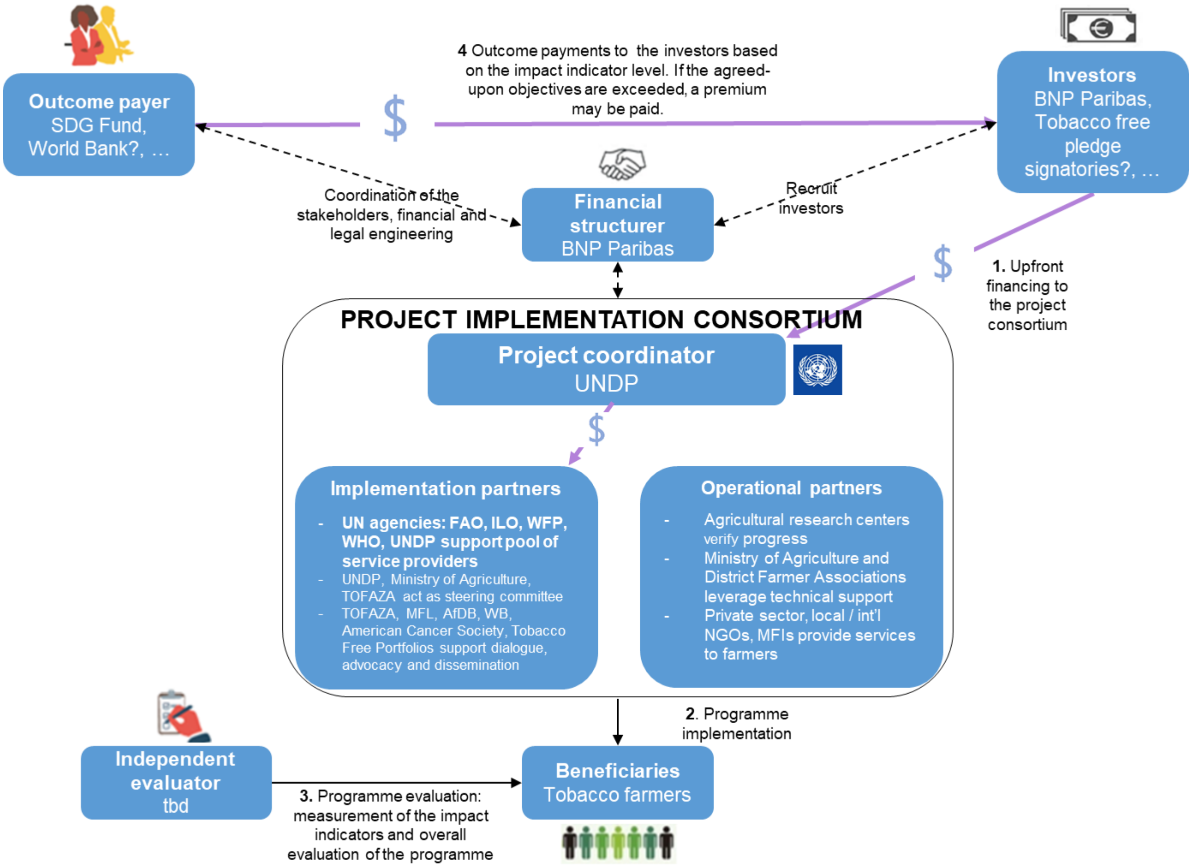


Source: UNDP

Table 4: Tobacco Control Social Impact Bond: Zambia

Tobacco Control Social Impact Bond	
Country	Zambia
Status	Full project proposal developed; not yet implemented
Lead organization(s)	UNDP
Implementation partners	UNDP, ILO, WFP, FAO jointly support pool of local service providers
Private investor(s)	None committed. *Proposed:* BNP Paribas plus other financial institutions with commitment to exclude tobacco from the investment, lending and insurance activities
Outcome Funder(s)	None committed. *Proposed:* World Bank and Joint SDG Fund
Type mechanism	Development impact bond
Volume financing	US$7 million
Implementation period	4 years
Scope of mechanism	Agriculture: support tobacco farmers to transition to alternative livelihoods
Outcome metrics	80% of targeted farmers transition to alternative livelihood
Investor rate of return	10.15% over 4 years
Independent evaluator	Not yet committed
UNDP's role	Central implementation partner. UNDP acts as the programme management unit tasked with contracting service providers and overseeing the T-SIB bond structuring, management and overall project implementation. UNDP is also tasked with ensuring there is national level support and buy-in for the TSIB, that stakeholders are informed about programme progress and that strategic direction from the project steering committee is followed.
Observations	Early feasibility study financed by UNDP's Innovation Facility (US$80,000). Full project proposal shortlisted for support from the Joint SDG Fund. Technical assistance provided by BNP Paribas to proposal design.

Figure 5: Zambia Tobacco Control Social Impact Bond Structure

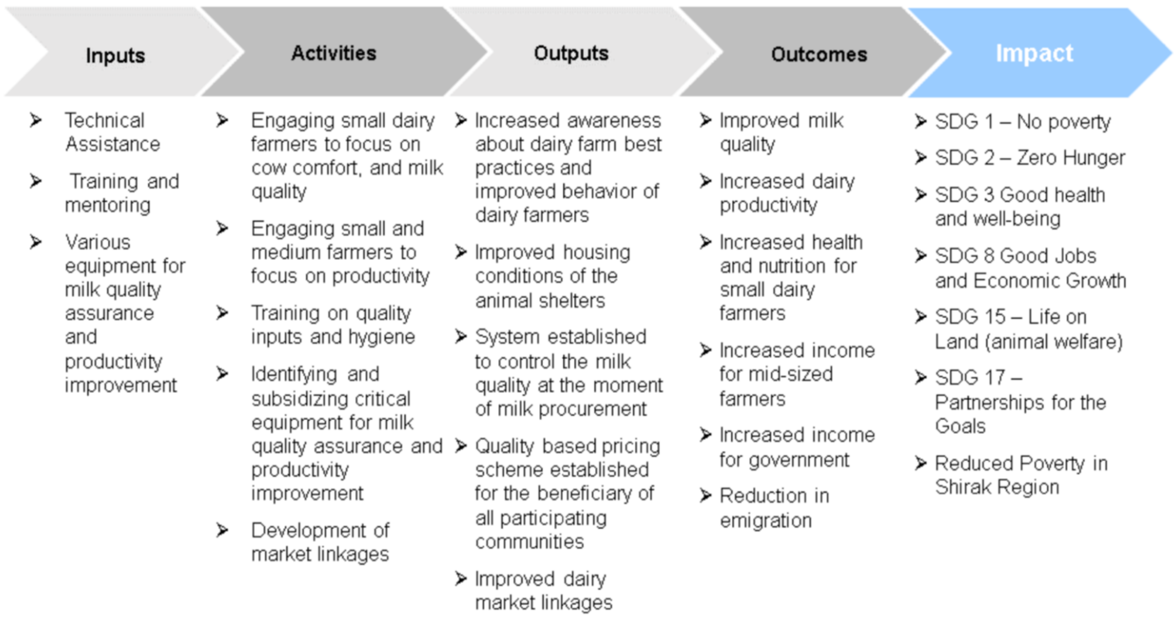


Source: UNDP 2020

Table 5: Dairy Productivity: Armenia

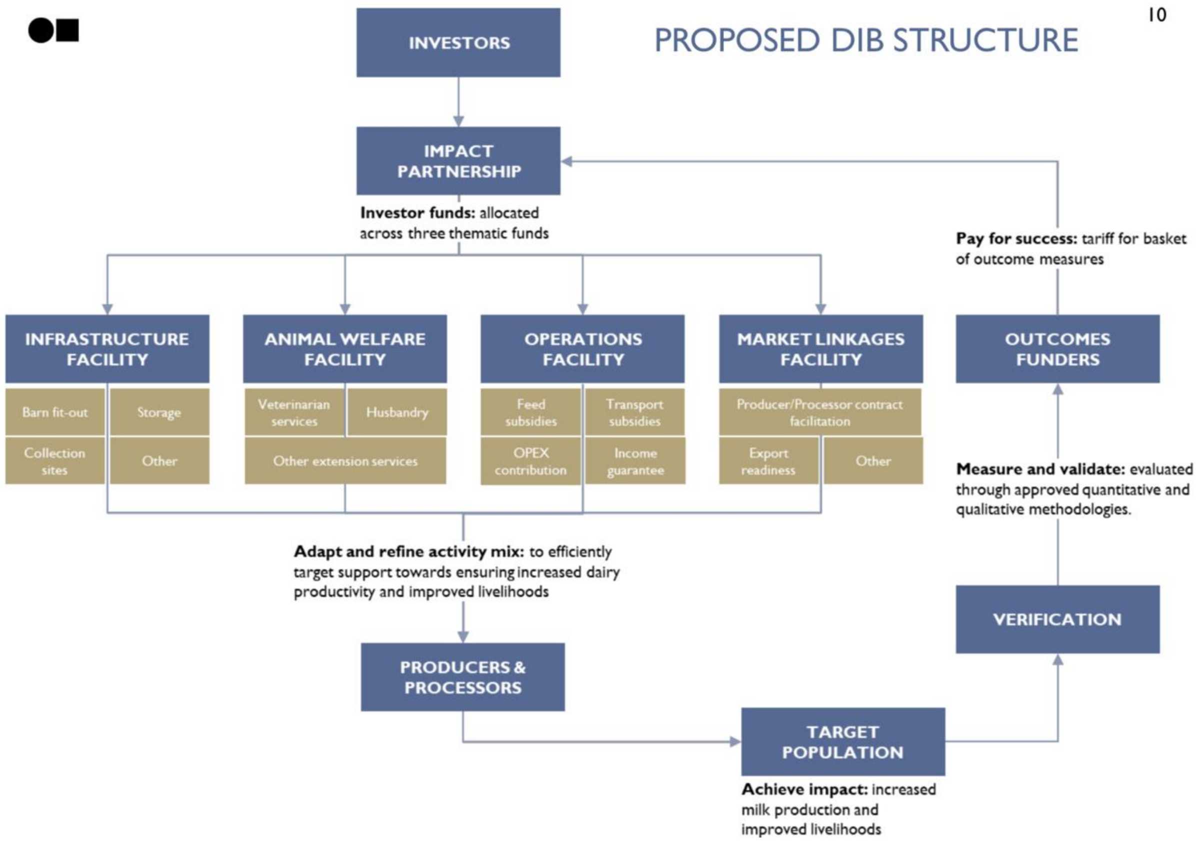
Improving Dairy Productivity in Armenia using an Impact Bond	
Country	Armenia
Status	Feasibility study completed; further analysis underway
Lead organization(s)	UNDP and European Bank for Reconstruction and Development (EBRD)
Implementation partners	
Private investor(s)	None committed.
Outcome Funder(s)	None committed.
Type mechanism	Development impact bond
Volume financing	Under further analysis. Initial proposal for EUR 1.2 million pilot phase
Implementation period	5 years
Scope of mechanism	Agriculture: support dairy farmers to increase productivity and product quality
Outcome metrics	Total volume of good quality milk sold by all project beneficiaries; annual average milk production per cow (kg/cow). Other metrics on household income and animal welfare also suggested.
Investor rate of return	Under further analysis
Independent evaluator	Not yet committed
UNDP's role	The EU provided funds to UNDP to undertake an initial feasibility study.
Observations	With funds from the Slovak Republic, EBRD and UNDP are partnering with Social Finance UK and Ecorys to further develop the analysis.

Figure 6: Theory of Change (ToC) for Armenia dairy impact bond



Source: UNDP

Figure 7: Proposed social impact bond structure for Armenia



Source: Social Finance, UK (2021)

Table 6: Cholera Impact Bond: Haiti

Haiti Cholera Impact Bond	
Country	Haiti
Status	Not yet implemented; advanced stage proposal developed
Lead organization(s)	Multi-partner initiative
Implementation partners	UNICEF, US Center for Disease Control, PanAmerican Health Organisation plus local NGOs
Private investor(s)	None currently committed
Outcome Funder(s)	US$10 million in principle commitment from USAID
Type mechanism	Development impact bond
Volume financing available	Up to US$ 26 million
Scope of mechanism	Healthcare (cholera)
Outcome metrics	1/ Reduction in number of cholera cases; 2/ Complete and timely response as measured by 48-hour response time; 3/ Number of suspected cholera cases tested; 4/ Number of households with improved access to safe water and water treatment
Investor rate of return	Not yet defined
Independent evaluator	Not yet committed
UNDP's role	Involved in technical design; MPTF as potential trustee for funds
Observations	Currently on-hold

Section 2: Impact Bonds and Kyrgyzstan

This section assesses the feasibility of an impact bond in Kyrgyzstan which focuses on employment, employability and skills development. It looks at potential areas of intervention (priority populations and sectors), possible payment metrics that could be used (and their advantages and limitations), the legal context, and potential partners. It ends with a summary table which assesses Kyrgyzstan's overall level of "readiness" for an impact bond.

2.1 Employment and skills in Kyrgyzstan: situation analysis

The National Development Strategy of the Kyrgyz Republic for 2018-2040, places a strong emphasis on employment and job creation. It states: *"the state's economic policy will be focused on employment, stable income, and the creation of productive jobs, taking into account all future labour market challenges."* It recognises that a competitive economy cannot be achieved without qualified human resources. In this regard, the strategy seeks to ensure that, by 2040, the economic well-being of the Kyrgyz people is achieved by creating productive jobs that provide decent employment and stable incomes, so that 80% of the able-bodied population has decent wages and working conditions. As such, an impact bond which focuses on employment and skills development would be well-aligned with the strategic development priorities of the Kyrgyz state.

Employment and skills development are critical development challenges in Kyrgyzstan. It is a non-diversified economy, which experiences significant fluctuations in growth rates. Economic activity is dominated by minerals extraction (gold, mercury and uranium), agriculture, and a reliance on remittances from citizens working abroad (remittances account for almost 30% of GDP). Cotton, wool, and meat are the main agricultural products, although only cotton is exported in any quantity. Kyrgyzstan also has high levels of public debt and is classified by the IMF and World Bank as at moderate risk of debt distress.[13]

Job creation is slow and lags behind the pace of demographic growth; firm and worker productivity remain the lowest in the region. According to the National Statistical Committee of the Kyrgyz Republic, the total employment rate for 2019 is 57% of the population (well below the target rate of 80%). Unemployment is concentrated in rural areas in particular (at 64.8% in rural areas versus 35.2% in urban areas) and amongst youth. The largest share of the unemployed is among those aged 20-24 (25.8%), 25-29 (21.1%) and 30-34 (10.7%). The data hides wide regional variations/disparities however: in the Osh region, 82.8% of people aged 18-24 are unemployed and in the Batken region, the figure is 75.4%. There is also a large informal sector. About 80% of people with disabilities are either economically inactive (72%) or unemployed (8%).[14]

COVID-19 further exacerbated a fragile economic and employment situation with a delay in planned investment and construction projects, and widespread disruptions to economic activity, which were

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[13] See World Bank Debt Service Suspension Initiative (DSSI): https://www.worldbank.org/en/topic/debt/brief/covid-19-debt-service-suspension-initiative
[14] Data from: Annual Journal "Employment and Unemployment 2019

only partially offset via targeted public policy measures. It also led many migrants to return home to the Kyrgyz Republic in 2020, increasing the numbers of unemployed. According to the ILO, by May 2020, about 20% of Kyrgyz migrants (160-200,000 people) lost their jobs in host countries due to COVID-19, and many labour migrants in Russia and Central Asia could not send remittances home to their families. The sectors where employment was hardest hit by the pandemic include trade, transport and warehousing, hospitality and catering, real estate operations, and arts and entertainment. According to estimates by the Ministry of Health and Social Development, in early April 2020, about 1.8 million people lost the opportunity to earn money because of the introduction of the state of emergency in the country. Many millions more are employed in the informal sector however and are without social protection measures. The situation is likely to lead to a further increase in informal and part-time employment. Women and youth will be most at risk, as elsewhere in the world, and this trend will continue for some time to come.

Through implementation of the National Sustainable Development Strategy (2018–23), the Kyrgyz Republic is planning for technological innovation and a more diversified economy that is less dependent on remittances, natural resources, and a large informal economy. Such innovation requires a skilled workforce, however. The labour market is increasingly seeking adults with strong foundational skills; however, a large portion of adults in the Kyrgyz Republic perform well below this foundational level. Most jobs in the Kyrgyz Republic require competency in literacy, numeracy, and information and communications technology (ICT). However, skills levels among the workforce are consistently low in absolute levels. The World Bank has shown that a substantial share of people is over-schooled, but under-skilled.[15] Moreover the COVID-19 crisis is likely to have further exacerbated these skills deficiencies due to the widespread closures of schools and other educational and training establishments.

At the same time, school age children account for more than 30% of the country's population, which is increasing demand for access to quality preschool and basic education. This will translate into increased demand for postsecondary and tertiary education as well as high quality – and relevant – training opportunities to produce workers with the relevant skills for the future. The World Bank has pointed to a clear need to make postsecondary and tertiary education relevant to labour markets as well as the need to enhance skills throughout life.

Analysis carried out by the Asian Development Bank (ADB) through its "Skills for Inclusive Growth" programme, in partnership with the Ministry of Health and Social Development, forecast labour market needs for 2021-2025. These show an increase in demand for qualified specialists with higher education as well as the need for specialists in information and communication technologies (ICT), teachers, specialists in medicine and paediatrics, social workers, food and food processing industries, and agronomy and veterinary medicine. Employers also set out their skills needs, including milk processing, wool processing, skilled vocational professions like plumbers and electricians, and drivers of specialised vehicles.[16]

[15] See, World Bank, Building the Right Skills for Human Capital Education, Skills, and Productivity in the Kyrgyz Republic, 2021: https://documents1.worldbank.org/curated/en/262271600915343998/pdf/Building-the-Right-Skills-for-Human-Capital-Education-Skills-and-Productivity-in-the-Kyrgyz-Republic.pdf
[16] See: http://www.donors.kg/images/DEVELOPMENT_PROGRAM_OF_KR_Unity_trust_creation.pdf

Box 4: Insights from stakeholder consultations

Stakeholder interviews provided valuable insights into how some young people feel about the overall employment situation in the country.[17] These include widespread pessimism about the lack of jobs, which leads, in turn, to a lack of confidence amongst young people; a lack of trust in organisations which provide educational and vocational training services so that parents may not support their children enrolling in courses, and; gender-specific challenges, for example girls often receive less support/encouragement to take educational courses and/or are married early which prevents them from further developing their skill-sets, especially in the southern region of the country.[18]

2.2 Advancing an employment-focused social impact bond within strategic state sectors

The Government has adopted several key state development programmes which may provide an opportunity to advance a social or development impact bond structure which strengthens professional and vocational skills *in these strategic sectors*. These include:

1. **Programme Medium-Term Development of the Kyrgyz Republic 2021-2026** which focuses on the development of *strategic branches* of the economy, including hydropower, agriculture and processing, tourism, mining, and the need to build education and human capital in these areas.

2. **Green Economy Programme for 2019-2023,** which envisages four main sectors to develop: 1) Green energy; 2) Green Agriculture; 3) Waste Management; 4) Sustainable public procurement. This will require skills across a wide spectrum of economic activity, including specialists in renewable energy, specialists in hydropower, recycling, energy efficient homes and buildings, the production of "green" goods, "green" organic agricultural products, specialists in the operation of "green" technologies, laboratory technicians, and many other areas.

3. **Kyrgyz Government Export Programme** for 2019-2022, which is anchored in four priority sectors: 1) Garment industry; 2) Dairy industry; 3) Processing of vegetables and fruits; 4) Green and innovative instrumentation. Ambitions to expand the dairy industry tenfold, garments and textiles fivefold and agriculture fourfold will increase demands on the labour market and will require a labour force with the requisite skills if these opportunities are to be realised.

[17] Based on stakeholder interviews.
[18] Information based on interviews.

4. **“Digital Kyrgyzstan” 2019-2023,** which aims to create new opportunities for the population through the development of digital skills to allow Kyrgyz people and local businesses to be competitive and in demand in the global market. It is anchored in three priority tasks: 1) Digital transformation of business processes and production chains, introduction of financial technologies, provision of competent specialists and development of ICT infrastructure; 2) Develop the regional digital infrastructure to open new opportunities for the private sector to expand markets; 3) The development of digital technologies, including blockchain.

A highly educated, technologically advanced population is seen as the foundation to building the country's competitive advantage. A social or development impact bond structure could present one tool to provide highly targeted bespoke educational and training opportunities, focused on youth and/or other disadvantaged populations, linked to boosting strategic state sectors in areas such as “green” jobs and the digital economy. It could also ensure that public resources – either the state budget or donor funds, depending who becomes the outcome payor – are well-used and spent on the achievement of results.

2.3 Awareness of impact bond models and previous experience with relevant programmes and models

Interviews with officials from various ministries revealed a strong interest in exploring ways to mobilise new sources of finance for tackling unemployment and building professional and vocational skills in Kyrgyzstan, especially amongst youth. Overall however, the social impact model is not widely understood, and the government has not to-date partnered with the private sector to any large extent in the delivery of social services. These are areas where the government has tended to work with the large development partners, many of whom continue to play a central role in financing these areas.

The state authorities have however worked with development partners on three programmes that are relevant to this prefeasibility study. The first is the Vocational Education and Skills Development Project funded by the Asian Development Bank.[19] The second is a results based financing programme focused on primary healthcare financed by the World Bank.[20] The third is the FAO’s Social Protection Plus/Cash + programme. Insights from all three are briefly presented below.

Asian Development Bank: Vocational Education and Skills Development Project

Since 2016, the ADB has been financing vocational education and skills development activities in Kyrgyzstan in an effort to build a more highly skilled workforce and boost worker productivity. Through this programme, the ADB reports that over four years, it has reached 15,000 trainees of which 47% were women. 55% were referred by employers. Courses provided were free between 2016 and 2020, though from 2021, they will be paid for by employers. Priority groups under this programme were reported as migrants, persons with disabilities and families on a low-income – however it was also

[19] See: Asian Development Bank: Kyrgyz Republic: Second Vocational Education and Skills Development Project: https://www.adb.org/projects/38298-023/main

[20] See: World Bank: Kyrgyz Health Results Based Financing: https://projects.worldbank.org/en/projects-operations/project-detail/P120435

emphasised that the programme must respond to the demands of individuals and the needs of employers, and that the programme needed to work with the applications it received.[21] The ADB cites a job placement rate of over 70%. ADB has now transferred responsibility for the Skills Development Fund to the national Ministry of Health and Social Development, which is seeking funding to continue its work. It was inactive in 2020, largely due to COVID-19. It was reported as an "effective but fragile" institution.[22] Bearing this in mind, it will be important to think about how a social or development impact bond would link to this programme, and how it would *complement* what it currently does (rather than add complexity to the marketplace). A highly targeted impact bond with restricted eligibility criteria (e.g. only certain populations or economic sectors would qualify) would be one way to achieve this, and would also be also be well suited to an impact bond structure.

World Bank: Kyrgyz Health Results Based Financing

The Kyrgyz Republic also has experience with a results-based financing mechanism through a World Bank funded programme which aims to improve the quality of primary healthcare services. There are some insights from implementation of this programme which are particularly relevant for a social impact bond model. Under the five-year programme - which also receives financial support from KfW and the Swiss Agency for Development and Cooperation - disbursements of funds are made to the government annually linked to the achievement of certain milestones. The government prepares a report annually, which is checked by an independent verifier. The World Bank noted that due to the COVID-19 pandemic, progress had unfortunately been slower than anticipated and the Bank would be rescheduling certain milestones.[23] It also pointed to weak capacities within the government and a lack of familiarity with the approach which made implementation more challenging. As such, the government had requested some modifications to the timeline for achieving certain milestones (rather than adjustments to the results themselves).[24] The Bank also noted that public procurement procedures and contracts for independent evaluators had been carried out according to World Bank and KfW rules respectively rather than according to domestic procurement processes and law, with a lack of capacity, and potential for delays in project implementation cited as the main reasons for opting *not* to use domestic systems and processes.

Stakeholder consultations questioned whether a payment-for-results mechanism might be employed rather than a social or development impact bond in Kyrgyzstan in light of the country's prior experience with this model. One advantage of an impact bond versus alternative results-based payment models is that financing is provided *upfront* by investors to fund programme activities. This offers certainty to service providers around their income. In contrast, under results-based financing structures, funds are released *ex post*, once certain performance milestones are reached. This can create uncertainty in the disbursement of funds, negatively affecting project performance.

[21] Based on interviews.
[22] Based on interviews.
[23] Based on interviews.
[24] Based on interviews.

FAO's Social Protection Plus/Cash + programme

Cash+ programmes have been piloted in Russia, and the idea is fairly well-known in the region. Cash+ programming is defined as interventions that flexibly combine (normally unconditional) cash transfers with productive assets, inputs, and/or technical training and activities to enhance the livelihoods, productive capacities and food and nutrition security of poor and vulnerable households. Cash+ models can support transitions to vibrant and diversified livelihoods, and can provide an important safety net against shocks and stresses for poor and vulnerable rural households. In 2017-2019, jointly with the Ministry of Labour and Social Development (MoLSD) and the Ministry of Agriculture, Food Industry and Melioration (MoAFIM), FAO piloted a social contract scheme based on its Cash+ model in the Suzak district of Jalal-Abad oblast. The intervention included 150 poor rural households. The pilot complemented the state cash transfer with support packages designed to help households diversify their agricultural production, and at the same time improve the food security and nutrition of households. The packages included provision of technical training, extension and advisory services, and production inputs. Results from the pilot phase include positive effects on the income and livelihoods, productive capacities and the food security and nutrition outcomes of the rural poor, including diversifying the diets of rural poor. The Cash+ pilot has also opened up a dialogue on strengthening policy coherence between social protection and other national poverty reduction and livelihood development programmes. Proposals for future phases include linking cash transfers to more climate-smart and environmentally sustainable activities, including beyond on-farm rural livelihoods and within the broader context of transitioning to a greener economy. There is also a need to focus on the "new poor" who have lost their jobs and incomes because of the COVID-19 crisis. Cash+ programming targeted on the "new poor" could have a specific focus on agro-forestry and sustainable forestation programmes, agricultural microcredit programmes or linking Cash+ transfers to payments for ecological services and organic agricultural production, sustainable water and pastureland management.[25] Expanding the programme to employment services in Batken has also been floated as an idea. A social impact bond could complement Cash+ programming through for example the provision of vouchers that would target skills development in particular strategic sectors, like the green economy. The Cash+ schemes also offers an opportunity to potentially institutionalise an impact bond approach within a larger programme, linking it to existing employment programmes, and benefiting from its institutional structures.

Overall, a lack of capacity within the government was cited as a key challenge to the effective implementation of development projects by most of the development partners consulted for this study. They emphasised that any attempts to develop a social impact bond structure must take these constraints into account.[26]

[25] All information from FAO
[26] Based on interviews.

2.4 Potential areas of intervention

Social impact bonds can be useful tools to test new service delivery models in the areas of education and skills development to target populations, like youth, women, disabled people or migrants. The analysis points to several potential priority areas of intervention for a social impact bond:

1. Close the mismatch in skills through a focus on **job specific** professional and vocational training with a particular focus on **youth** and on regions where youth unemployment is particularly elevated, like the **Osh** and **Batken** regions. The programme would address an underinvestment in relevant skills and seek to augment both technical and soft skills for employment readiness.
2. Build skills for the future through a highly targeted focus on **digital skills development and "green" jobs.** The interventions would aim to build key skills in areas in line with state strategic sectors.
3. Provide targeted employment services and skills development to support **migrant returnees** to enhance their integration into local job markets or the **"new poor"** as a result of COVID-19. This could include job placement services, training, and informational services.

It will be important to think about how a social impact bond in employability and skills development complements existing programmes and does not simply add complexities to the marketplace. It should also not be seen as a replacement for high quality publicly-funded education programmes. In this respect, a highly targeted programme focusing on specific target communities may be better suited to a SIB structure. This approach may also represent an opportunity to raise funds from Kyrgyzstan's sizeable external diaspora, who could be invited to participate in the impact bond as a financial partner alongside others. While there has been substantial experience in using the model to target youth and women/girls for example, there has been far less experience of using the instrument with returnee and migrant communities. Moreover, interviews with stakeholders indicated that free skills development training is currently open to all adults registered with the labour services, however in some regions, vulnerable people are not registered with these services which can make reaching them more complex.[27]

Participants in the programme would receive specialist professional and vocational training and employers supported to provide employment. Target beneficiaries could be issued with 'credits' or vouchers that could be used to help finance, in full or in part, qualifying courses that aim to upskill vulnerable populations, as part of a broader Cash+ scheme. The final design of the programme would need to be anchored in a clear diagnosis of participant needs which could be further analysed in subsequent phases of this work. The measures would be expected to represent value for money through a long-term increase in labour productivity.

When targeting more 'difficult to reach' communities like disadvantaged youth, women, the disabled and migrants etc., prior experience with SIB structures has shown that they must be carefully designed to avoid so-called 'perverse incentives.' These occur if service providers have an incentive to target populations that are relatively easier to reach and likely to achieve good employment outcomes even

[27] Based on interviews.

in the absence of the intervention. Common methods for responding to this challenge include introducing eligibility criteria to include only specific populations, introducing quotas or caps in which the numbers or portion of the vulnerable population is defined, and using differential pricing where higher prices are attached to results for specific populations.[28] Also bear in mind however that investors that provide the upfront capital for these interventions must also be persuaded that the programme's aims are realistic and achievable, and there are therefore good chances they will recoup their investment plus a small return. There is therefore a careful balance to be struck between participant needs and investor requirements.

2.5 Measuring success

Impact bonds that target labour markets and employability commonly use a range of metrics on which outcome payments to investors are based. These include the delivery or completion of training, and/or some associated skills improvement (*employability* metrics), as well as metrics related to employment itself, i.e. job placement and retention. Different labour market payment metrics have different advantages and limitations, as set out in the table below. It is important to design the programme in such a way as to maximise achievement of the intended benefit, while limiting perverse incentives. Perverse incentives occur when the impact bond is designed in such a way that maximises benefits to service providers and investors rather than the intended beneficiaries.

Table 7: Common payment metrics: labour market impact bonds

Payment metric	Advantages	Limitations	Measures to reduce perverse incentives
Training received (numbers of persons)	-Easily measured e.g. through course enrolment data - Low measurement cost	-Service providers could target populations that are relatively easier to reach -Service providers target *number* of people trained, rather than the quality of the services provided	- Payment metrics that specify a certain number of e.g. youth/women/disabled/migrants must be reached by the programme (e.g. 50%) - Measurement of course completion data
Skills improvement	-Proxy measures are fairly easy to employ like course completion or course certification by an accredited entity	- Course completion does not necessarily lead to employment	- Course completion/ certification data can help to measure the quality of the education/training provided

[28] See: Instiglio, Results-based Financing to Enhance the Effectiveness of Active Labor Market Programs, 2018: https://instiglio.org/wp-content/uploads/2021/02/IDRC-Final-Report.pdf

Job placement	-Incentivises service providers to find beneficiaries a job	-Service providers may be incentivised to place people in low-quality jobs or jobs unrelated to the skills they have trained for -Service providers may focus on beneficiaries that are easier to place	-Payments can be made conditional on job placements that meet certain minimum quality criteria (e.g. formal sector jobs that pay at least minimum wage)
Job retention	-Incentivises service providers to support beneficiaries to find better quality jobs	- Service providers may be incentivised to place people in any job that meets minimum criteria even if this is unrelated to their skills/courses undertaken	- Job placements should meet certain minimum criteria and/or be directly related to courses undertaken

Research from Instiglio on social impact bonds that target labour markets also suggests that each payment metric should ideally be weighted such that metrics related to employability (training received and skills improvement) and job retention should be afforded higher 'weights' in terms of payments to investors, with 3 and 6 month checkpoints often considered appropriate since some jobs may have initial trial periods.[29] In Kyrgyzstan, given that greater formalisation of the labour market is a key priority, jobs must meet minimum quality criteria in order to be covered by the impact bond.

Table 8: Examples of payment metrics that could be employed in a social or development impact bond in Kyrgyzstan

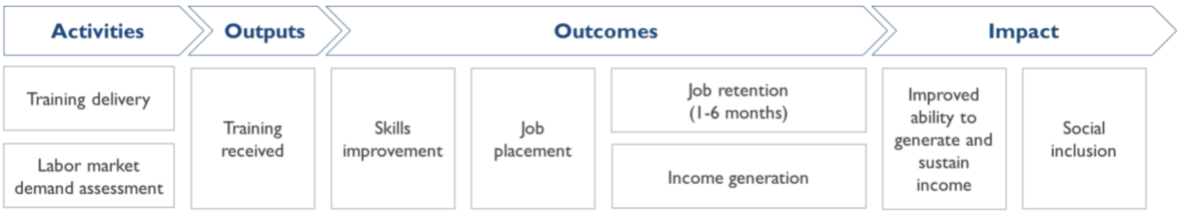
Potential payment metric	Performance Measurement
Training received	- Course enrolment - Number of persons from specific target communities that enrol and complete courses (e.g. youth, women, disabled, migrant returnees etc.) - Amount of 'credits' issued (and used) to target communities to pay for skills development courses - Number of persons mentored - Type of course undertaken (e.g. in state strategic sectors)
Skills improvement	- Course completion - Course certification - Course/skills assessment as performed by an accredited entity as specified in the SIB agreement
Job placement	- Number of beneficiaries placed in a job - Number of persons from specific target communities placed in a "decent" job (i.e. a job that meets certain specific quality criteria)

[29] See: Instiglio, Results-based Financing to Enhance the Effectiveness of Active Labor Market Programs, 2018: https://instiglio.org/wp-content/uploads/2021/02/IDRC-Final-Report.pdf

Job retention (3 months)	- Number of beneficiaries in a job after 3 months
Job retention (6 months)	- Number of beneficiaries in a job after 6 months
Job retention (12 months)	- Number of beneficiaries in a job after 12 months -Number of beneficiaries from target communities in a job after 12 months -Increase in income of programme beneficiaries
Reduced reliance on welfare benefits	- Reduction in number of welfare claimants in target population (cost savings)

There is no upper or lower bound on the size of a social impact bond however there is point below which the bond is not likely to be economically efficient. A transaction of not less than US$2-3million is estimated to be a lower bound at which the associated transaction costs (structuring, measurement and evaluation) are considered worth it.

Figure 8: Theory of Change for an impact bond focused on the labour market and skills development



Source: Instiglio 2021[30]

2.6 The legal framework for social impact bonds in Kyrgyzstan

The concept of "impact bonds" or "social impact bonds" are unfamiliar to Kyrgyzstan and are thus not stipulated in any legislation within the Kyrgyz Republic. In this section, we review laws which are likely to be applicable to social impact bonds in Kyrgyzstan and which are relevant where investors exist in different jurisdictions.

Legislation does not set out any limitations on how social programmes should be funded or delivered in Kyrgyzstan. However any service, including social services, are contracted according to the Law on Public Procurement, the main purpose of which is to regulate public procurement procedures to ensure that quality services are procured which also represent an efficient use of public funds (value for money). Procurement regulation provides for *equal treatment* between goods and services provided by national/local entities *and* those provided by foreign/international entities where the procuring institution is a state or local government body (including state and municipal institutions, and state-owned enterprises). This means that service providers to an impact bond in Kyrgyzstan could

[30] See: Instiglio, Results-based Financing to Enhance the Effectiveness of Active Labor Market Programs, 2018: https://instiglio.org/wp-content/uploads/2021/02/IDRC-Final-Report.pdf

in principle be international organisations (e.g. an international NGO) as well as a local entity who would enter into a competitive tender process. It also means that foreign entities would not need to set up a specific entity in the Kyrgyz Republic. The same rights are given by the Article 4 of the Investment Law as well as Article 15 of the Public-Private Partnerships (PPP) law. The PPP law gives contract winners the right to establish a local company, but does not oblige them to do so. Typical public procurement procedures apply, including the publication of tender documents and announcements, a competition period, evaluation and comparison of bids etc. Procurements via a direct contracting method may only be employed where the goods, works and services to be provided amount to less than 5,000,000 soms in a single year. While the public procurement law provides for standard public procurement provisions, it is also important to note that the World Bank and KfW opted to use their own institutional processes in their results-based financing programme in the area of primary healthcare. Reasons for this were cited as a lack of capacity in state institutions to manage international tenders for procurement, and that it would take too much time to use domestic systems and processes resulting in delays to programme implementation.[31]

Article 5 of the Investment Law guarantees that investors shall have the right to free export or repatriation of compensation in freely convertible currency. There are no legal restrictions on the repatriation of profits. The law also guarantees foreign investors the right to repatriate any property and information related to the investment. Article 14 meanwhile sets out the state's role when it comes to the support and protection of foreign investors. These include advising potential investors on legal, economic and other issues regarding a specific activity, assistance and protection when faced with legal actions, and other measures.[32]

Article 18 of the Investment Law relates to the settlement of disputes between foreign and domestic investors – which could arise should a local service provider fail to carry out their obligations/services under a social impact bond. This stipulates that any investment dispute between the foreign and domestic investors shall be considered by the judicial bodies of the Kyrgyz Republic unless the parties reach an agreement on another dispute settlement procedure, including national and international arbitration. The PPP law (Article 18) also stipulates that PPP agreements must contain essential conditions, such as the liability of the parties in case of non-performance or improper performance of obligations under a PPP agreement, the procedure for settling disputes, grounds for termination and the procedure for monitoring and controlling project implementation. This latter point is important. Social impact bond agreements contain provisions for the monitoring of project implementation and the measurement of outcomes. This process triggers repayments (or not) to investors. It would be important to seek a legal opinion as to whether an independent evaluator's report under a social impact bond agreement could be challenged in a court since the PPP law was not established with SIB structures in mind. This can form part of the next phase of the feasibility analysis.

Article 16 of the Investment Law stipulates investors' rights to freely hire employees who are not citizens of the Kyrgyz Republic in accordance with the legislation of the Kyrgyz Republic. Employees who are not citizens of the Kyrgyz Republic may also be hired to the management bodies of the

[31] Based on interviews.
[32] See: UNCTAD, Investment Law: https://investmentpolicy.unctad.org/investment-laws/laws/111/kyrgyzstan-investment-law

enterprise. This means that in principle, both local and foreign personnel could be involved in providing services under a social impact bond structure in Kyrgyzstan.

Tax regulation needs to be considered. The tax code provides for some benefits and advantages for socially responsible employers, and the disabled. These include some exemptions from income tax, such as an employer's expenses for the training and retraining of an employee (Article 167 of the tax code); the purchase of supplies by non-commercial organisations shall be exempt from VAT where these supplies are for social welfare and educational activities (Article 252); VAT exemptions on the delivery of goods/services by socially significant facilities (Article 256); VAT exemption on the importation of certain goods into the territory of the Kyrgyz Republic where these goods are destined for people with disabilities, educational and scientific purposes or under a contract for a socially significant facility (Article 257); exemptions from sales tax where work is carried out by a non-commercial organisation involving disabled populations or where educational/scientific activities are performed (e.g. kindergartens established on the basis of private ownership) (Article 315).

Finally, the implications of Kyrgyzstan's Budget Code which prohibits the state from providing guarantees to private sector entities must also be further evaluated in the next phase of work. This could potentially prevent the Kyrgyz state from being an outcome payor under an impact bond structure, especially if investors require that the impact bond be structured in such a way that they are guaranteed to recover at least some of their investment, irrespective of the final outcomes achieved. Alternatively, donors (aid agencies and/or philanthropies) could provide these (partial) guarantees as one way to overcome these potential hurdles.

2.7 Potential partners to an impact bond in Kyrgyzstan

Social impact bonds require partner organisations – non-profit entities or private companies – with the requisite skills and experience needed to implement services which will, in turn, lead to measurable positive outcomes within a specified timeframe. Entities may be either local or international organisations/companies. This section analyses key stakeholders engaged in social and development work in Kyrgyzstan, with a focus on employment and skills development, and explores the extent to which they are likely to be a potential partner to any eventual impact bond. The analysis is based on interviews with these various entities, combined with a desk review of current and recent programmes and priorities.[33]

Table 9: Stakeholder map: matrix and analysis of potential partners

Name of organization	Description of activities	What services could it provide to an impact bond?	Potential partner? Yes	No
Russia/Kyrgyz Development Fund	The mission of the Fund is to promote the modernization and development of the Kyrgyz Republic and promote	Financing investment projects on a commercial basis, by providing loans to small - medium and large enterprises		Unlikely

[33] Interviews carried out between June and August 2021.

	economic cooperation between Kyrgyzstan and Russia, with a focus on job creation and economic competitiveness.	up to $100K-$ 1 mn. The Fund could potentially be a financing partner (outcome funder) to the impact bond, however we have to keep in mind that the Fund has never supported Public-Private Partnership projects in the past.		
Institute for Youth Development	Supports youth development and creating new opportunities for youth in Kyrgyzstan	Holds license from the Ministry of Education and Science to deliver educational, training, mentoring and advisory services in various fields, including business development and entrepreneurship. The Institute could provide services in a SIB contract on training and employment issues.	Yes, high potential	
Young Entrepreneurs' Business Association "JIA", Committee on Labor and Employment	The association of legal entities "Business Association JIA" was created by entrepreneurs from different regions of Kyrgyzstan. Today the association is a platform offering opportunities for the business community in Kyrgyzstan to interact, bringing together more than 1,000 representatives of small and medium-sized businesses. JIA is the only association in Kyrgyzstan which is a member of the International Organization of Employers.	The Association could provide a good platform for promoting the SIB concept among its membership in the Kyrgyz Republic.	Yes, high potential	
Skills Development Fund	The Skills Development Fund (SDF) was formed in 2016 as part of a project supported by the Asian Development Bank. The main aim of the Skills Development Fund is to meet the needs of the population in skills development, as well as help employers to train and improve the skills of workers. It also aims to strengthen technical and vocational training.	The SDF could act as a central professional and vocational training and ensure that a SIB structure is based on a strong needs assessment and can link-up the various stakeholders involved in educational and skills development in Kyrgyzstan.	Yes, high potential	

Public-Private Partnerships Center	The PPP Center was established by the Kyrgyz Republic to support and accelerate the development of infrastructure projects of national and municipal importance and improve the quality of public and municipal infrastructure development services through the use of private-public partnership instruments.	The PPP Center could support on development of the SIB contract mechanisms	Yes, high potential	
European Bank for Reconstruction and Development (EBRD)	Multilateral Development Bank funds a variety of infrastructure projects across the region	Has worked with UNDP in Armenia to advance a feasibility study for an impact bond targeting improved productivity among dairy farmers.	Yes, high potential	
Eurasian Development Bank	Regional multilateral development bank	Focuses on infrastructure development rather than social service delivery		Unlikely
International Finance Corporation (IFC)	Private sector financing arm of the World Bank Group	Unlikely since IFC’s core focus is to fund private sector businesses that deliver commercial returns		Unlikely
UBS Optimus Foundation	International philanthropic foundation with a focus on innovative finance models	Has partnered as an outcome payor to a DIB structure in India. UBS has a special programme on development impact bonds	Yes, high potential	
Winrock International	International NGO present in Central Asia since the early 1990s to assist the development of the agricultural sector in the Kyrgyz Republic and other former Soviet republics	High relevance of its work in the agricultural sector to deliver technical assistance to farmers and to develop agribusinesses. Could potentially be a service provider	Yes, high potential	
Aga Khan Foundation	International philanthropic foundation	Foundation is involved in agriculture and education which are both areas relevant for a labour market focused impact bond. It is also active in the Osh region identified as a potential region for a SIB/DIB. It could potentially act as a service provider or an outcome funder but would need to be approached	Yes, high potential	

Service providers under an impact bond model should have a robust record of success. One potential partner to a social impact bond is Kyrgyzstan's Institute for Youth Development. It is a leading youth organisation within the country, and although it is fairly new (founded in 2014), it is actively engaged in providing educational services, professional training, mentoring and business development support to young people throughout the country.[34] It has a core focus on expanding economic opportunities and employability. Its work is supported by Japan, Germany and UNDP, with the institute is entirely dependent on donor funds. Key projects include business support – both finance, equipment and technical assistance – for businesses impacted by the pandemic, as well as financial support provided on a competitive basis to young people with business plans that create new job opportunities for youth.

Entities that have been partners to the ADB's Skills Development Programme could also be brought in as potential partners and service providers within a social impact bond. The ADB reports that it has worked with 87 organisations in the context of this programme, which include primary and vocational colleges, and universities from both the public and private sectors (with 70% from the public sector). Overall, the ADB pointed to the small-scale nature of most private service providers in this area.[35] It has not been possible to analyse which ones may be best suited to partner to an impact bond within the confines of a short initial scoping study, however in the next phase of this work may be useful to look at education and skills providers in specific target regions like Osh and Batken or specific technical specialisations (like digital skills). Overall, interviewees noted that Kyrgyzstan has a more vibrant NGO community than other countries in the region, which represents an enabling factor for an impact bond.[36] At the same time, interviewees also pointed to a chronic lack of investment in trained service providers and counsellors and a danger that too few institutions had the skills to provide basic worker services and other ongoing institutional support.[37]

2.8 Potential bottlenecks to an impact bond model in Kyrgyzstan

Our initial analysis suggests that the main bottlenecks to implementing a social or development impact bond are unlikely to be on the legislative side, as they are potentially well covered by the Public Procurement Law, the Law on Investments and the PPP Law, but rather related to other challenges. These include:

- Lack of familiarity with the impact bond model on the part of relevant state entities, and a culture of relying on donor aid financing, rather than engaging in partnerships/projects with the private sector;
- Insufficient local experts to prepare and deliver an impact bond to a high standard, including weak public procurement skills;
- Lack of private sector trust in state authorities, and lack of interest in cooperating with the state on a long-term basis;

[34] See: Institute for Youth Development: https://jashtar.org/en.html
[35] Based on interviews.
[36] Based on interviews.
[37] Based on interviews.

- Unsuccessful experiences of partnership between the state and the private sector in the implementation of investment projects (only 3 PPP projects implemented to-date, all of which are under inspection by law enforcement agencies);
- Despite the development of investor-friendly regulations, and efforts to improve the ease of doing business, the country is still seen to have a weak investment climate adding to perceived investor risk;
- Poor sovereign credit rating may deter investors, since it indicates a low overall confidence in the stability of the economy. Kyrgyzstan is not considered investment grade;
- Due to the overall vulnerability of the economy and fiscal constraints, low capacity of the government to finance outcomes under a social impact bond model;
- Skewing of the labour market by a high reliance on remittances, which means the reservation wage for many households is high, especially for women;
- Limitations on public debt accumulation envisaged by domestic legislation mean that outcomes would need to be funded through donors, not the public budget.

Table 11: Summary and overview: Kyrgyzstan's readiness for an impact bond

Impact bond basic criteria	Extent to which this condition met in Kyrgyzstan		
	Yes	**No**	**Unclear**
Ability to set measurable outcomes	Yes, targets could be set to increase skills and employability amongst certain populations or regions		
Reasonable time horizon to achieve measurable outcomes	Yes, skills development and employment success can be measured over a reasonable time period		
Ability to measure outcomes efficiently and cost effectively	Probably yes, though this would need to be analysed further		
Prior evidence of success	Yes, Skills Development Fund has proved an effective tool to support skills improvement and employability – though it has also been described as a fragile institution.		
Skilled service providers	Yes, there are national organisations like the Institute for Youth Development which could potentially be qualified partners but there would not be a large choice of locally-		

	based service providers due to an underinvestment in service providers for many years.		
Value proposition is clear			At this early stage, more work is needed on why this model is the best one versus other traditional financing approaches.
Stable political and economic environment			Kyrgyzstan's economic situation has been made more fragile due to the COVID-19 pandemic which introduces greater uncertainty for investors and outcome payers. Lack of trust and confidence in government for a SIB structure.
Appropriate legal framework			Yes, a SIB is likely to be fairly well covered by provisions contained in the Public Procurement, Investment and PPP laws. However development partners cite low capacity.
Outcome payer interest			Unknown. Not yet at an advanced enough stage
Investor interest			Unknown. Not yet at an advanced enough stage

Section 3: Next steps and recommendations

The Kyrgyz Republic is seeking a growth trajectory that is less dependent on remittances, natural resources, and a large informal economy. Raising human capital can build a skilled and enterprising workforce, allowing the Kyrgyz Republic to reap the dividends of a youth bulge, be resilient to disruptive technology, and create high quality formal-economy jobs for its large and fast-growing young population. A major challenge is to provide for quality education and vocational skills development opportunities that build the necessary skills for a modern dynamic labour market. Impact bonds focused on the labour market have enjoyed some successes in other countries, especially amongst target populations like youth, women/girls, migrants and other disadvantaged communities to boost employment and 'employability'. However they are not a panacea; they do not create new jobs per se, and are expensive to develop requiring a high level of commitment and capacity.

The analysis carried out in this prefeasibility study point to several steps which will need to be undertaken to design an effective social or development impact bond, and advance this work to the next phase:

- **The rationale for an impact bond needs to be clear. Further clarity is needed on what problem or deficiencies in current approaches to boosting labour market skills the impact bond is trying to solve.** It is true there are significant labour shortages in the market, however it is important to understand whether these are due to a lack of skills, or due to other factors like poor pay and conditions, or the high reservation wage owing to households being in receipt of remittances. An impact bond can focus on the *supply side* (i.e. fostering skills and employability), but it cannot on its own overcome structural problems in the labour market. There are several initiatives currently underway to boost vocational skills and employability, including those funded by the Asian Development Bank and GIZ. It will be important to map where these programmes are enjoying successes and where they are not, so that an impact bond can be designed to test new approaches to addressing the deficiencies in current service provision. Impact bonds are most relevant as a financial instrument when they provide *innovations* in service delivery to target populations. A useful next step for this work therefore is to survey those involved in current programmes (service providers, students, employers, donors and relevant state entities) to understand where the current challenges and gaps are in current service provision so that an impact bond can be structured to address these.

- **Outcomes and interventions need to be developed in consultation with the local stakeholders involved.** All stakeholders need to be aligned around the objectives of the impact bond such that there is ownership over the instrument and what it expects to achieve. This is more likely where the impact bond is strongly aligned with national and/or local sustainable development priorities, such as those articulated in national development programmes like Kyrgyzstan's "Unity, Trust, Creation" plan. Outcomes and interventions must be organised around a clear diagnosis of participants'/beneficiaries' needs. In the next phase, analysis needs to be undertaken by institutions with a local presence to understand target populations' needs and design a mix of interventions best suited to meet those needs. The support of development partners, philanthropic bodies and international organisations is likely to be necessary for the development of the outcome matrix.

- **Interventions need to be costed and modelled**. Once the target cohort and desired results are defined, a financial model will need to be developed which models various scenarios as regards how many beneficiaries could potentially be reached, how much the outcomes are likely to cost. This will then help to define minimum and maximum investor requirements.

- **Clear evidence of prior success.** While impact bonds should test new and innovative ways to reach target populations, there should also be clear evidence that interventions have a strong prospect of success, otherwise investors and outcome payers are not likely to back them. In the next phase of work, it will be important to evaluate which service providers have a strong track record in delivering high quality educational and training services. These service providers must, in turn, understand what the impact bond mechanism is all about. Other SIBs have used 'market testing' days where they invited prospective providers to learn about SIBs and how they could become engaged and ultimately bid to become a service provider under any eventual project.

- **A development impact bond is recommended over a social impact bond**. The Kyrgyz Republic is classified as a lower-middle-income country, and is at moderate risk of debt distress according to the World Bank. There is also a low level of overall trust in the government as regards preserving stable economic and political conditions. Borrowing on concessional terms is recommended as the most suitable and sustainable form of loan financing to preserve debt sustainability. Because social impact bonds usually carry market rates of return for investors, and are likely to be repayable in hard currency, a donor agency (or agencies) would likely be the most suitable outcome payer(s), rather than the Kyrgyz state. Donor partners consulted for this prefeasibility study, like the Russia-Kyrgyz Development Fund, Asian Development Bank and USAID indicated an interest *in principle* in an impact bond model, however indicated that further information was needed on the underlying project(s) to be supported with an impact bond, and a need to build the capacities of local stakeholders to understand results-based financing mechanisms. It should be emhpasised however that not all development partners could be consulted in the short timeframe for this early research. In terms of Kyrgyzstan's key development partners, the World Bank has had experience with both impact bonds and results-based financing modalities, while the Asian Development Bank has acted as an outcome payer to an impact bond targeting training and skills development, and employment services in Pakistan. Both could potentially be involved in the next stage of discussions.

- **Further socialisation of the overall model is needed.** In particular, several interviewees expressed an interest in learning more about success stories from other countries, which could represent a useful next step for this work. Entities that have been involved in designing and delivering impact bonds that target labour markets in other countries could be approached to deliver a series of presentations to relevant local stakeholders which explain their experience with impact bonds, and provide an opportunity for question and answer sessions. Options are outlined below and cover both social and development impact bond models:

- **Colombia:** Workforce Development Social Impact Bond, implemented from 2017-2018, focused on training and skills development, implemented with funds from the Inter-American Development Bank and the State Secretariat for Economic Affairs of Switzerland.[38]
- **India:** Educate Girls development impact bond in education, funded by UBS Foundation and which ran between 2015 and 2018.[39]
- **Uzbekistan:** Early Childhood Education Social Impact Bond, launched in 2019, in partnership with the World Bank and the Global Partnership for Education.[40]
- **Finland 'Koto-SIB':** A social impact bond started in 2017, and one of very few targeting the integration, skills and employment of migrants.[41]

- **A compelling impact narrative and storyline around the impact bond will need to be developed.** This will help to boost interest in the impact bond amongst investors, philanthropic entities and donor partners. Investor engagement is more successful when it starts early in the process and investors' appetite for the minimum and maximum investment requirement are known. Development partners can play a key signalling role for the impact bond through their close involvement at every stage of the development process.

- **A plan on how to 'institutionalise' the impact bond, for example within the Skills Development Fund, will be important to achieve lasting impact.** It will be important to think about how the impact bond can become more than a short-term niche project, and how it integrates with existing labour market services so that lessons learned, methods and tools can be shared, and knowledge about what is working – and how – can be mainstreamed across relevant institutions at the national level. Linking the impact bond to existing programmes like Cash+ can help ensure the impact bond becomes much more than the sum of its parts.

Lessons learned from other impact bonds include:

1	**Outcome payers like to see country prioritisation.** Institutional buy-in at a country level is critical. Donors are more likely to support clear country priorities.
2.	**Establish the counterfactual.** The impact bond must demonstrate that impact will be achieved and be able to set a baseline counterfactual against which success is measured.
3.	**Secure Outcome payers upfront.** It is critical to secure outcome payers upfront and ensure they are engaged through the product development. Outcome payers often have requirements for committing funding and these should be built into product design.

[38] See: Instiglio, Results-based financing to enhance the effectiveness of Active Labor Market Programs, 2018: https://instiglio.org/wp-content/uploads/2021/02/IDRC-Final-Report.pdf
[39] UBS Foundation, Educate Girls: https://www.ubs.com/global/en/ubs-society/philanthropy/optimus-foundation/our-impact/development-impact-bond.html
[40] See: Global Partnership for Results-Based Approaches: https://www.gprba.org/activities/uzbekistan-early-childhood-education-social-impact-bond
[41] See: Using social impact bonds to integrate refugees in Finland, 2018: https://golab.bsg.ox.ac.uk/community/blogs/using-social-impact-bonds-integrate-refugees-finland-will-it-work/

4.	**Understand investor appetite.** It is important to understand what outcomes investors are willing to pay for, and how much they are willing to commit.
5.	**Involve an investor representative early on.** This can help smooth the development process and encourage other investors to offer financing for the impact bond.
6.	**Design governance of the impact bond.** Governance and management framework for bond implementation should be designed upfront with outcomes payer, issuer, supplier and investors.

Source: Various (author's elaboration)

Labour market impact bond in Kyrgyzstan: potential added value and limitations

Advantages	Limitations
Impact bond targets recognised skills deficiencies in the labour market in Kyrgyzstan	Impact bond does not create new jobs per se and cannot address structural problems in the labour market
Impact bond targets specific disadvantaged communities that are currently underserved by other labour market skills services	Target populations may be harder to reach and impact bond cannot overcome certain structural barriers to unemployment/poor skills
May help to promote greater quality, diversity and competition in the provision of complementary labour market skills services	Could add complexity to the vocational training and skills development marketplace if its value-added is not clear
Carefully designed programme oriented around results	Intervention likely to be fairly small, especially in the early stage. Potential to scale not yet known

Source: Author's elaboration

Annex: **List of Interviews**

Ministry of Economy and Finance:
Head of Investment Policy Division Mr. Iskender Nurbekov;
Head of International Cooperation Department Mr. Nurbek Akjolov

Ministry of Agriculture, Water Resources and Regional Development:
Head of International Cooperation Department Ms. Lira Kasymbekova;

Ministry of Health and Social Development:
Head of Strategic Reforms Department Mr. Meder Ismailov;
Head of Employment Promotion Division Ms. Gulmira Alkanova;
Head of International Cooperation Division Mr. Narkiz Kulmanbetov

World Bank:
Ms. Asel Sargaldakova World Bank Health Specialist;
Ms. Christel Vermeersch – World Bank Health Specialist

Non-Government Foundation "The Youth Development Institute":
Program assistant/Credit specialist Ms. Asel Asanbekova

Association of Private Employment Agencies:
Head of the Association Mr. Sherbolot Askarbek (Obozov)

Skills Development Fund:
Head of the Fund Mr. Akynbekov Rysbek;

Asian Development Bank
Supervisor of the Skills Development Fund Mr.Mamatkalil Razaev

Ministry of Education Department of Primary Vocational Education
On behalf of the Ministry's Primary Vocational Education Department Mr.Ibragimov Bektur, Head of Division Ms. Gordeeva Irina

Business Association of Young entrepreneurs:
Head of the Association Mr.Omoshev Joodar

Consultant:
Sheila Marnie