

1. CAS Data	
Country: Sri Lanka	
CAS Year: FY03; CASPR FY06	CAS and CAS-PR Period: FY03–07
CASCR Review Period: FY03–07	Date of this review: May 28, 2008

## 2. Executive Summary

- i. As the Sri Lanka Country Assistance Strategy (CAS) was a joint strategy between the Bank and IFC, this review of the CAS Completion Report (CASCR) covers the Bank-related aspects and is evaluated by IEG-WB; IFC-related aspects of the CASCR are reviewed by IEG-IFC, whose review is included as Attachment 1. This review covers the 2003 CAS and the 2006 CAS Progress Report (CASPR) for the FY03–FY07 period.
- ii. The CAS sought to contribute to poverty reduction through assistance aimed at fostering peace, growth and equity. The CAS was aligned with the prevailing Poverty Reduction Strategy Paper (PRSP) and coordinated with other donor assistance, and envisaged a tripling of program expenditures over the previous CAS period in the context of the 2002 cease-fire agreement. The relevance of the CAS diminished over time, however, as civil hostilities resumed and the government's support for the policy reforms anticipated in the CAS failed to materialize.
- iii. After the December 2004 tsunami, livelihood restoration and reconstruction was appropriately added as an additional CAS pillar. In the 2006 CASPR, Bank objectives were substantially scaled-back. Despite the breakdown in the cease-fire, and the derailing of the policy reform effort, the Bank continued to deliver support commensurate with base case lending levels.
- iv. IDA's commitments during FY03–07 totaled US\$813 million for 15 projects compared with a planned amount of US\$1.185 million for 24 projects. Portfolio performance over the CAS period improved, but projects exiting the portfolio during the CAS period exhibited outcomes substantially below Bank averages. Poor project outcomes, and a re-assessment of the Mahaweli project, are illustrative of the adverse effects that neglect of structural reform has on long-run project performance.
- v. The overall outcome has been rated *moderately unsatisfactory* by IEG. The efforts supported by the Bank to promote peace through reconstruction and reconciliation were overcome by the resumption of armed conflict. While growth has accelerated, insufficient progress has been made on fiscal consolidation, structural reform, and public sector management. Efforts to foster social equality remain frustrated by a concentration of economic activity in the Western Province, limited targeting of transfer payments, and low levels of competency achieved by students after primary schooling. Tsunami reconstruction was mounted rapidly and vigorously, but progress was geographically skewed towards affected communities in the South.
- vi. IEG concurs with most of the lessons of the CASCR. There is a need for the Bank to limit lending into an adverse policy setting. During the current policy dialogue hiatus, it is more important to build constituencies for reform, prioritize the Bank's analytic work and focus assistance where reform-readiness is firmly established and a significant impact on poverty reduction can be made. Lending triggers should be respected and based on factors within the government's control. Going forward, more emphasis is also needed to assist the government in generating up-to-date statistical information, particularly to track poverty reduction outcomes.

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### 3. CASCR Summary

#### **Overview of CAS Relevance:**

1. The FY03–06 CAS was developed at a time of great optimism. After nearly two decades of civil conflict, a cease-fire between the Liberation Tigers of Tamil Eelam (LTTE) and the Government of Sri Lanka was in effect and peace negotiations were underway; a PRSP had been approved and a private sector-oriented government was in power and implementing an economic reform program; and the country was experiencing a gradual recovery with annual economic growth of more than 5 percent.
2. The FY03–06 CAS was anchored in Sri Lanka PRSP and its objective of reducing poverty through contributing to peace and promoting economic growth with equity were relevant. The assistance program was only partly consistent with the strategy since the PRSP had identified infrastructure deficiencies as the key determinant of the lack of growth and equity outside the Western Province, and infrastructure was largely excluded from the Bank's program. The base-case lending program was set at three times the level of the previous CAS to help reinforce the peace process and to take advantage of perceived opportunities for reform. The CAS was to be anchored in an annual PRSC, with 2–3 annual investment operations and sector programs in the social sectors and for Northeast reconstruction. An ambitious AAA program was designed to fill knowledge gaps to support the reform process, to underpin lending operations, and to respond to government policy analysis requests. The strategy was recognized as inherently risky, with low and high-case lending triggers and scenarios clearly defined.
3. The Bank's strategy was quickly shown to be unrealistic, given the tenuousness of the peace process, the nation's fractious polity, and its weak institutional capacity to implement reforms. By early 2004, peace talks had stalled, and in late-2005, hostilities resumed. Following the April 2004 elections, the government changed and under the People's Freedom Alliance (UPFA) the PRSP was discarded; the new Government pursued military operations against the LTTE, while maintaining that it was committed to a political solution, and advocated policies of greater state intervention. Fiscal consolidation efforts proved weaker than anticipated and public debt levels approached critical thresholds.
4. On December 26th 2004, Sri Lanka was struck by a tsunami that claimed over 60,000 lives and displaced close to one million people. The Bank responded quickly with a rapid needs assessment and two large emergency operations.
5. The CAS was developed around 32 outcomes for each of three pillars: peace, growth, and equity. In the face of diminishing support for economic reform, the CASPR narrowed the scope to 19 strategic outcomes, with several of the CAS objectives consolidated and those related to enterprise deregulation, educational pluralism, and tertiary education dropped. Also a fourth pillar, tsunami reconstruction, was added. In the revised program of support in the CASPR, the focus shifted from policy-based lending towards lending operations that (i) support human development, (ii) further the recovery in conflict-affected areas and (iii) assist road and irrigation infrastructure.

#### **Overview of CAS Implementation:**

6. **Lending.** IDA's commitments during FY03–07 totaled US\$813 million for 15 projects compared with a planned amount of US\$1,185 million (US\$800 million in the CAS and US\$385 million in the CASPR) for 24 projects (see Annex Table 1). The CAS envisaged that program lending would provide half of total lending support from FY03–06. However, the first Poverty Reduction Support Credit (PRSC) was implemented in an unsatisfactory manner, the IMF's PRGF program was suspended, and subsequent PRSC's were indefinitely delayed.
7. The Bank's response to the tsunami was impressive, with IDA participating in a multi-donor reconstruction needs assessment and, within two months of the event, a portfolio restructuring of 10 operations was used to provide US\$75 million in credits and grants, and a Phase II emergency credit

was processed two weeks later. While the Bank's CAS did not anticipate financing in the road sector, establishment of a Road Sector Maintenance Trust fund in 2003 triggered subsequent bank support in the transport sector.

8. The CAS envisaged that lending would fall to US\$250 million over the CAS period if low-case triggers were met—i.e., a breakdown in the peace process and a failure to maintain the pace of structural and macro-economic reforms. Although lending levels were below targets in 2006 and 2007, total lending delivered during FY03–07, excluding emergency operations, was more than twice the level foreseen in a low-case scenario.

9. During FY03–07, Sri Lanka's average disbursement ratio was 28 percent, substantially better than Bankwide averages, while disbursements peaked at US\$202 million (FY03) and declined modestly to US\$157 million (FY07). The Bank's active portfolio as of October 12, 2007 comprised 13 IDA credits/grants and one Global Environmental Facility (GEF) grant for a total commitment (net of cancellation) of US\$778.4 million, with US\$422 million undisbursed. The portfolio also contained two restructurings, the Northeast Emergency Reconstruction Project and the Tsunami Emergency Reconstruction Project Phase II, which allowed the Bank to respond quickly to reconstruction needs in the conflict-affected North and East, and tsunami-affected areas. While problem projects were fairly limited in the first 3 years, this peaked at 4 projects in FY07 as a result of the conflict, but was brought down to 2 projects by the end of the year (see Annex Table 4). Implementation problems were anticipated and addressed quickly during the CAS period, with a proactivity rate of 100 percent each year.

10. Between FY03 and FY07, IEG evaluated 13 closed projects of which just 46 percent had satisfactory outcomes (South Asia Region, SAR, 79 percent; Bank wide 79 percent), 36 percent had a substantial institutional development impact (SAR 53 percent, Bank wide 55 percent) and 73 percent were considered sustainable (SAR 84 percent, Bank wide 79 percent) (see Annex Table 3). Factors contributing to weak project performance included project complexity, failure to implement reforms, insufficient attention to institutional capacity building, frequent counterpart staff changes, politicization of the public sector, and insufficient attention to building social consensus for reform. A lesson that repeatedly came from IEG evaluations was the need to secure an enabling policy environment prior to undertaking investment operations. This lesson was further reinforced by the PPAR of the Third Mahaweli Ganga Development Project, which downgraded that project's outcome rating from unsatisfactory to highly unsatisfactory because of its failure to address agriculture policy distortions, insufficient attention to irrigation cost recovery, a failure to provide settlers with secure land rights, and a lower than expected growth in farm income.

11. **Non-lending:** Of the original 31 planned studies in the CAS and CASPR for FY03–07, eleven were dropped and were replaced by other studies. A total of 39 reports were delivered, 8 more than envisioned and of which ten were policy notes. The analytical work has informed policy dialogue and has helped to shape the lending portfolio, especially in the areas of education, health, roads and water supply and sanitation. Bank ESW was also a valuable source of new knowledge for Sri Lanka's development partners, especially the cross sector studies such as the PER and the Development Policy Review. However, a lack of up-to-date statistical data impeded analytic work, and at an average of 6 reports/policy studies per annum, reports tended to compete with one another for the limited attention of a small circle of policy makers preoccupied with civil conflict, tsunami relief, and short political cycles.

#### **Overview of Achievement by Objective:**

12. Detailed achievements in each area are summarized below and compared with CAS objectives and indicators.

**Pillar I: Peace**

13. **Access to Services.** The CAS objective to restore access to education and irrigation services in conflict affected areas was partly achieved, but progress was short-lived. IDAs Second General Education project contributed to a restoration of primary school coverage and the Northeast Irrigated Agriculture Project's (NEIAP) support for irrigation and market access boosted paddy output, but resurgence of sectarian violence in late 2005 led to internal displacement of an estimated 210,000 persons and to the closing of the main transport artery to the North, which triggered shortfalls of basic foodstuffs, boosted construction costs, and disrupted basic services.

14. **Institutional framework.** The CAS objective to strengthen the institutional framework in conflict areas was partly and temporarily achieved through capacity building in program management, delivery of basic services, and community-led development under the NEIAP, the Northeast Housing Reconstruction Project, the North East Emergency Reconstruction Program (NEERP) and the Puttalam Housing Project. The Bank did help reestablish administration at the provincial and divisional levels, but progress was threatened by the resumption of the armed conflict. As of April 2008, conflict-affected parts of the North and East are under supervision of the military, the LTTE or other armed combatants, with civil institutions severely curtailed.

15. IEG rates IDA's contribution to country outcomes as *moderately satisfactory* in this pillar.

**Summary of Results vs. Original CAS Objectives: Peace**

PRSP long-term goals and targets	CAS medium-term Outcomes and Intermediate Indicators	Bank-Supported Activities Contributing to Outcomes
<b>Restore access to health, education and irrigation in conflict-affected areas.</b> 20 percent of damaged primary health care centers, damaged classrooms and damaged irrigation schemes to be repaired annually. 183 of a target of 197 schools rehabilitated, and 369 out of 379 water supply schemes rehabilitated by June 2005; number of students in basic education in the North and East rose by 3.2 percent per annum from 2002–2006.	<ul style="list-style-type: none"> <li>Education facilities restored in conflict-affected areas to pre-war levels. <i>Achieved, but sustainability threatened by conflict resumption.</i></li> <li>Water supply for irrigation increased in conflict-affected areas <i>Achieved, but progress threatened by resumption of armed conflict.</i></li> </ul>	<ul style="list-style-type: none"> <li>Northeast Irrigation Agriculture Project I delivered and II ongoing.</li> <li>North-East Emergency Reconstruction (<i>delivered and substantial contribution</i>).</li> <li>Northeast Housing reconstruction (ongoing)</li> <li>Puttalam Housing (<i>ongoing but progress at risk</i>)</li> <li>Social assessment of conflict areas study (<i>dropped</i>).</li> </ul>
<b>Strengthen institutional framework and capacity in conflict-affected areas to facilitate reconstruction and poverty reduction efforts.</b> Provincial and divisional administration temporarily strengthened during the cease fire.	<ul style="list-style-type: none"> <li>Build technical capacity to implement the reconstruction and poverty reduction efforts. <i>Partly achieved but progress reversed with conflict-affected parts of the North and east under supervision of the military, LTTE or other armed combatants.</i></li> </ul>	<ul style="list-style-type: none"> <li>North-East Emergency Reconstruction and Northeast Irrigated Agriculture Project (I and II) (<i>small contribution to project management and local administration capabilities</i>).</li> <li>Land Policy and Conflict Study (<i>delivered</i>).</li> </ul>

**Pillar II: Growth**

16. **Enabling macro environment.** The CAS objective was to create an enabling macro-economic environment for private sector driven investment and growth. Although growth increased, it was not fueled by fiscal consolidation and structural reform. Under the Economic Reform TA (ERTA) and the PRSC I, changes were made to the legislative framework to allow for greater private sector participation in infrastructure and to establish a multi-sector regulator. However, state enterprise losses have increased as petroleum subsidies soared, unbundling of the Ceylon Electricity Board (CEB) was opposed by the Unions, and the Public Utilities Commission of Sri Lanka (PUCSL) is still unable to regulate the sector.

17. **Factor markets.** The CAS objectives in promoting factor market reform were to: (i) expand employment opportunities and the flexibility of the labor market; (ii) increase efficiency of land utilization; and (iii) improve the soundness of the financial system. Factor market reform was supported through the Poverty Reduction Support Credit (PRSC), analytical work, and projects in Central Bank Strengthening and Land Titling and Related Services. Although unemployment has fallen, labor market regulations remain inflexible. Rural land markets remain dominated by state ownership and restrictions on land transfer. There has been progress in the banking sector with the CBSL reforms contributing to improved financial sector stability, and with measures taken to restructure the Bank of Ceylon and the People's Bank. However, plans for privatizing the People's Bank have been abandoned and two new public sector banks have been established.

18. **Rural economy.** Increasing productivity of the rural economy was to be encouraged by liberalizing agricultural trade, enhancing access to planting materials, improving water resource management, and boosting off-farm employment. Progress has been made in introducing sustainable off-grid energy sources with innovative Bank assistance to support private provision of mini-hydro power systems. However, the agriculture sector continues to record slow growth, fertilizer subsidies and restrictive agriculture trade policies were re-introduced, restrictive phytosanitary policies remain in place, the Mahaweli Authority has not yet been transformed into a river-basin planning agency, and transfer of irrigation O&M responsibilities to farmers has proceeded slowly.

19. **Public service.** The CAS objective was to improve the quality of public service delivery and improve the transparency and predictability of the legal framework through stemming growth in the public service and improving accountability, which was supported through capacity building in each lending project, as well as specifically through the Legal and Judicial Reform project, the E-Sri Lanka project, the World Bank Institute (WBI) work with Parliamentarians and the Press, and the Public Expenditure Review (PER) and policy dialogue process. A new Audit Act was prepared, and a National Procurement Agency (NPA) was established and assisted with an IDF grant. However, the public service continues to be very large, and is marked by over-staffing, political interference, fragmentation, and low levels of accountability. Moreover, World Bank governance indicators for voice and accountability, political stability, government effectiveness, rule of law, and control of corruption have all deteriorated between 2002 and 2007 (see Annex Table 9).

20. IEG rates IDA's contribution to country outcomes as *unsatisfactory* in this pillar.

#### Summary of Results vs. Original CAS Objectives: Growth

PRSP long-term goals and targets	CAS medium-term Outcomes and Intermediate Indicators	Bank-Supported Activities Contributing to Outcomes
<b>Create enabling macro environment for private sector driven investment and growth</b> GDP growth increased from 6.0 percent in 2003 to 7.4 percent in 2006, while inflation rose from 6.3 percent to 13.7 percent in the same period. Government debt as a percent of GDP declined from 107.9 to 94.7.	<ul style="list-style-type: none"> <li>Higher sustained economic growth. <i>Partly achieved, but modest Bank contribution.</i></li> <li>Results-based budgeting system established. <i>Not achieved, progress indicators for expenditure trends not reported beyond 2004.</i></li> <li>Improved financial performance of key state enterprises. <i>Not achieved with CEB losses equivalent to .75 percent of GDP in 2006 and modest bank contribution.</i></li> </ul>	<ul style="list-style-type: none"> <li>Poverty Reduction Support Credit I (<i>delivered</i>).</li> <li>Economic Reform TA (<i>delivered</i>).</li> <li>(ii) PRSC II, III and IV: (<i>not delivered</i>).</li> <li>Development Policy Review, Improving Rural and Urban Investment Climate, Roads Policy note, Garment and Textile Policy Note, Public Debt Policy Note, Public Expenditure Analysis TA (<i>delivered with modest impact</i>).</li> <li>Annual public expenditure analysis review (<i>dropped after 2004</i>).</li> </ul>
<b>Expand employment opportunities and the flexibility of the labor market:</b>	<ul style="list-style-type: none"> <li>Legal framework to increase flexibility in labor markets and promote harmonious labor</li> </ul>	<ul style="list-style-type: none"> <li>PRSC 1 and Economic Reform TA (<i>delivered</i>).</li> <li>Development Policy Review</li> </ul>

Unemployment fell from 8.1 percent (2003) to 6.5 percent (2006), and scant evidence on progress of labor market flexibility.	relations. No evidence of progress and limited Bank contribution.	(delivered). ▪ Youth Employment Study (not delivered).
<b>Improve the soundness of the financial system:</b> Non performing loans fell from 14.5 percent in 2002 to 5.4 percent in 2006, capital base and bank operating profits improved, but privatization of People's Bank stalled and 2 new public banks created.	▪ CBSL re-focused towards managing its core functions. Partly achieved and substantial Bank contribution.	▪ Central Bank Strengthening Project (delivered). ▪ Access to Finance and Housing Finance studies (delivered and well disseminated).
<b>Increase productivity in the rural economy:</b> Agriculture has grown slowly at 2–3 percent per annum, fertilizer subsidies and restrictive agriculture trade policies re-introduced in 2005.	▪ Off-farm income generation activities promoted through sustainable rural electrification, including in conflict ridden areas (Partly achieved and substantial bank contribution).	▪ PRSC I (delivered but insufficient progress on rural land reforms). ▪ Renewable energy for Rural Development (delivered and high impact). ▪ Promoting Agriculture and Rural Non-Farm Growth, and Rural and Urban Investment Climate (delivered and widely disseminated).
<b>Improve the quality of public service delivery:</b> The government re-established the independent Public Services Commission, and introduced strict time limits for the submission of annual accounts and performance reports by the line ministries and the state owned enterprises. Public sector employment grew by 9 percent between 2002 and 2006, compared to 3 percent for private sector employment; in 2006, public administration and defense expenditures increased sharply; and World Bank governance indicators all deteriorated between 2002 and 2007.	▪ Politicization of the civil service reduced and public service accountability improved, Not achieved, and modest Bank contribution with civil service continuing to exhibit over-staffing, politicization, and deteriorating governance standards.	▪ Economic Reform TA (delivered). ▪ E-Sri Lanka (ongoing). ▪ Legal and Judicial Reform (delivered but modest impact). ▪ Country Procurement Assessment Review, Decentralization and Service Delivery, Governance Policy Note, Development Policy Review, PER Policy dialogue (delivered but modest impact). ▪ ROSC Accounting and Auditing Assessment (delivered and widely disseminated).

### Pillar III: Equity

21. **Improve overall equity.** The CAS aimed to improve overall equity through rural poverty reduction, improvement in social outcomes in the estates sector and better targeting of welfare programs to the poor. Rural poverty levels have declined markedly between 2002 and 2006/07 according to the results of the 2006/07 Household Income and Expenditure Survey. However, the income gap between the Western Province and the remainder of the country continues to widen, severe disparities in income distribution remain, and poverty levels in the estate sector have increased. A new formula-based targeting methodology was piloted for Samurdhi cash transfers, while funding for that program has steadily eroded.

22. **Basic education.** Improving the quality of the basic education system was a CAS objective, to be achieved by boosting investment in education, especially in poor schools, including in learning resources and teaching materials. IDA support for better education quality was provided by the ongoing Teacher Education & Teacher Deployment and General Education II (GED-II) projects, by the Education Sector Reform TA project in 2003, and by the Education Sector Development Project of 2005, and by the 2004 review of the general education system. With IDA support, a norm-based unit cost resource

allocation formula was applied to school financing; new curricula have been developed; the textbook supply was vastly improved; and the share of trained teachers has been increased. However, learning outcomes remain unsatisfactory with the majority of primary school graduates failing achievement tests in their first language, math and the English language.

23. **Improve health status.** Given high rates of child malnutrition, the CAS objective of improved health status through greater effectiveness of existing health resources, decentralized health management and increased coverage of measles immunization was quite modest. IDA support for decentralized service delivery was provided by the Health Sector Development project and contributed to the preparation of district health plans and better care in the poorest districts. However, support for decentralized service delivery was weakened by attempts to recentralize several health functions in 2007.

24. **Curb spread of HIV.** Through the IDA supported National HIV/AIDs Prevention project, new programs for public education awareness of HIV risks have been developed, and tuberculosis control programs have been revitalized. However, HIV awareness and knowledge levels in underserved communities remain drastically low, and Bank project assistance on this has stalled.

25. **Improve service access in poor districts.** The CAS objective was to improve access to services in poor districts by empowering poor communities to implement sub-projects contained in their local development plans. Support for community driven development (CDD) has been provided through the successful Gemi Diriya project which has contributed to the design of the Government's Gama Naguma Program that is currently being rolled out.

26. IEG rates as *moderately unsatisfactory* IDA's contribution to country outcomes in this pillar.

#### Summary of Results vs. Original CAS Objectives: Equity

PRSP long-term goals and targets	CAS medium-term Outcomes and Intermediate Indicators	Bank-Supported Activities Contributing to Outcomes
<b>Improve overall equity in the country:</b> The 2002 and 2006/07 Household Income and Expenditure Surveys report a decline in the poverty headcount from 23% to 15%. Regional income inequality continues to widen with 60 percent of GDP originating in Colombo and the Western Province in 2006 compared to 58 percent in 2002. Gini coefficient of 0.4 for 2006/07 indicates that aggregate income inequality has remained unchanged from 2002. Funding for social assistance declined, while funding for power subsidies, a regressive transfer, rose.	Reduction of poverty especially in lagging rural areas and estates; improvement in social outcomes in the estate sector and better targeting of welfare programs to the poor. Rural poverty levels declined from 24.7% to 15.7% while estate poverty levels rose from 30% to 32%. No Bank assistance for income generation targeted to the Estates sector. No improvement has been made in targeting welfare programs while funding for the main program (Samurdhi) eroded to an almost insignificant 0.3 percent of GDP in 2006. Untargeted power subsidies, a regressive transfer, reached 2.1 percent of GDP in 2007 despite upward adjustments in petroleum prices in 2006 and 2007. Modest bank contribution.	<ul style="list-style-type: none"> <li>TA for Implementation of Welfare Reform (<i>ongoing and modest contribution</i>)</li> <li>PRSP-II: (<i>not delivered</i>).</li> <li>Poverty Assessment, Poverty Mapping, Poverty and Social Impact Analysis, Tea and Rubber Estate Study (<i>delivered and modest contribution</i>).</li> </ul>
<b>Improve the quality of basic education system.</b> 12,000 out-of-school children brought into the school system by 2006; Education capital expenditures rose to 35 percent in 2007 from less than 20 percent of total education outlays	<ul style="list-style-type: none"> <li>Investment in education increased, especially in poor schools, including in learning resources and teaching materials 88 percent of teachers qualified to teach in 2006, against a target of 86 percent. Substantial Bank</li> </ul>	<ul style="list-style-type: none"> <li>General Education Development I Project and the Improving Relevance and Quality of Undergraduate Education Projects (<i>delivered and major contribution</i>).</li> <li>Education Sector Reform TA</li> </ul>

in 2006. Learning outcomes are poor, with primary school pupils at the end of their primary cycle having extremely low cognitive achievement scores in their first language (37 percent), math (38 percent) and the English language (10 percent).	contribution particularly due to the introduction of a norm-based resource allocation mechanism. Quality improvement measures were insufficient to lead to satisfactory primary school learning outcomes.	(delivered, and major contribution) ▪ Education Sector Report, MDG report and Poverty Assessment (delivered and major contribution). ▪ Education Sector Development Project-II (ongoing).
<b>Improve health status of the population.</b> Child malnutrition remains high at 30 percent nationwide and 33 percent in the estates sector. The numbers of districts with low infant mortality rates rose from 14 (2001) to 17 (2003), while those with low maternal mortality rates rose from 12 in 2001 to 16 (2004).	▪ Effectiveness in the health sector's use of existing resources improved Progress in outcomes attributed to increase in per capita health spending from US\$13.7 in 2002 to US\$17.4 in 2006 rather than to efficiency gains. 100 percent of districts provided annual health plans in 2006. Some improvement in decentralized service delivery with a modest Bank contribution.	▪ Health Sector Development Project (ongoing)  ▪ Poverty and Social Impact Analysis (delivered). ▪ Health Sector Strategy (dropped).
<b>Curb Spread of HIV infection.</b> HIV prevalence rates estimated at 0.1 percent in 2005 but the proportion of women infected with HIV has increased from 21 percent in 1987–91 to 47 percent in 2002–05 raising the risk of higher future infection rates.	▪ Keep prevalence rate of HIV low by increasing awareness Partly achieved. General awareness is high but no evidence of awareness improvement in under-served communities and bank efforts have stalled. Only 40 percent of women working in rural tea estates, for example, have even heard of HIV/AIDS. Limited Bank contribution.	▪ Health Sector Development Project (delivered). ▪ National HIV/AIDs prevention project (ongoing and limited contribution.)
<b>Improve access to services in poor districts</b> Several ODA-financed community-driven development projects launched and a new community empowerment program is planned, but government's welfare policy is to phase-out transfer schemes and to promote micro- and SME credit.	▪ The number of empowered communities implementing sub-projects contained in their development plans expanded. Selected Bank projects have reached nearly 1,000 villages. , Achieved with substantial Bank contribution.	▪ Gemi Diriya Project (delivered and major contribution). ▪ Second Community Water Supply and Sanitation (ongoing and limited contribution). ▪ Gemi Diriya Project II (not delivered). ▪ Decentralization and Delivery of Services (delivered).

#### Pillar IV: Tsunami Reconstruction

27. **Restore livelihoods.** The restoration of livelihoods destroyed by the tsunami and the start of the recovery and reconstruction process was added as an additional series of CAS objectives in the 2006 CASPR. The Bank's needs assessment estimated the damage at about 7 percent of GDP, which helped inform a donor conference that subsequently mobilized US\$2.2 billion in reconstruction pledges. IDA assistance contributed to infrastructure repair, housing reconstruction and livelihood support. Tsunami reconstruction proceeded at a far slower pace in the North and East than in the South.

28. IEG rates IDA's contribution to this pillar as *moderately satisfactory*.

#### Summary of Results vs. Original CAS Objectives: Tsunami Reconstruction

Government short term goals	CAS medium-term Outcomes and Intermediate Indicators	Bank-Supported Activities Contributing to Outcomes
<b>Restore livelihoods destroyed by the tsunami and start the recovery and reconstruction process: US\$2.2 billion in</b>	▪ Restored housing of the poorest households in affected districts. <i>Partly achieved with substantial gaps remaining in</i>	▪ Tsunami Emergency Projects (I and II) (delivered and positive contribution to housing reconstruction and livelihoods)



reconstruction pledges and some 55,000 temporary houses were built for the displaced. By March 2007, 80 percent of eligible families had completed their houses with most uncompleted houses in the North East. Eighty percent of the self-employed and casual workers regained employment a year and a half after the tsunami.	housing reconstruction and livelihoods in affected communities in the North and East. 114 km road between Galle and Colombo was rehabilitated. Substantial Bank contribution. ▪ Livelihoods of the tsunami-affected families rebuilt to help revive the local economies of the affected districts. Partly achieved with cash grants, public works programs and water units delivered. Livelihood grant programs reached 100,000 families. Assistance provided primarily to affected families in the South.	restoration in the south). ▪ Preliminary Damage and Needs Assessment. Development Forum: The Economy, Tsunami and Poverty Reduction (delivered).
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**Achievement of CAS Objectives: Moderately Unsatisfactory**

Objectives	CASCR Rating	IEG Rating	Explanation / Comments
Objective I: Peace	Moderately Satisfactory	Moderately Satisfactory	Large-scale reconstruction and resettlement of internally displaced persons were supported from 2003–05 and resulted in a recovery of primary school access and boosted paddy output in the Northeast. Progress in outcomes suffered reversals with the resumption of armed conflict in 2005, however.
Objective II: Growth	Unsatisfactory	Unsatisfactory	GDP growth accelerated, the ratio of public debt to GDP declined, and progress was made in strengthening the banking sector. However, inflation has risen slightly, and insufficient progress was made in fiscal consolidation, public expenditure management, land titling, labor and water market policies, energy sector restructuring, rural economic reforms, and public sector reform. Governance indicators steadily deteriorated during the CAS period.
Objective III: Equity	Moderately Satisfactory	Moderately Unsatisfactory	The Western Province continues to dominate the growth process and inequality remains high and largely unchanged. While the education curricula have been improved and more teachers trained, learning outcomes remain unsatisfactory. Transfer payments have become less-targeted over the CAS period due to large untargeted power subsidies although fuel prices were increased in 2006 and 2007.
Objective IV: Tsunami Reconstruction	Satisfactory	Moderately Satisfactory	Financial resources were rapidly mobilized to finance tsunami reconstruction efforts. Some 39,000 houses were rebuilt or repaired and

			more than 100,000 families received livelihood grants. Reconstruction in the North and the East has proceeded more slowly because of the resumption of the conflict.
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**Comments on Bank Performance:**

29. IDA's assistance strategy for Sri Lanka was largely relevant because it addressed key constraints to poverty reduction. Using program credits and capacity building to underpin reform, and using small projects to meet PRSP targets for sectors such as education, health and water supply and sanitation was fully consonant with the IDA strategy. However, the CAS rationale for excluding infrastructure development in IDA's assistance program "in the spirit of selectivity" was insufficiently developed given the high PRS priority and extensive infrastructure deficiencies existing in the country. It was appropriate to halt the use of policy-based assistance after PRSC-I, and to respond forcefully to the 2004 tsunami disaster. It was equally appropriate to reduce lending levels in FY06 and FY07 when triggers suggested a move towards low-case lending support although, in addition to changing its mix of lending instruments, the Bank should have been more proactive in adjusting lending volumes to the adverse reform and deteriorating security situation. IDA's comprehensive program of AAA was consistent with its strategy and was designed to inform the policy debate, inform the donor community, and to design and implement investment projects.

30. Although portfolio ratings have shown steady improvement, low outcome ratings for projects that exit the portfolio are attributed, in part, to unrealistic project design, and to variable quality of Bank supervision. ICR reviews underscore the importance of political support and ownership to project performance, and attributes weaknesses in implementation to political interference, frequent changes in the leadership of Government Ministries and executing agencies, and flagging support for agreed reforms, all of which are long-standing factors suggesting that greater use of project and sector-specific readiness triggers should have been used. QAG finds that supervision varies considerably across projects - QAG rated supervision of the Teacher Education and Deployment project as highly satisfactory and supervision of the Distance Learning Initiative as moderately unsatisfactory.

31. In 2006, QAG undertook an assessment of 10 AAA reports prepared between 2004 and 2006, and found 7 to be satisfactory, 2 moderately satisfactory and one unsatisfactory. They also found that as a result of the abrupt change in government in 2004, report recommendations were modest and too general, while the use of good quality analytic work was hampered by lack of government interest.

32. With about 50 bilateral and multilateral donors active in Sri Lanka, hundreds of NGOs and private sector assistance providers, coordinating with them is a formidable task. Under the Multilateral Group and thereafter the Donor Assistance Coordinating Committee, IDA cooperated with other partners in scaling-up support for relief, rehabilitation and reconstruction. A Development Partners Coordination and Support Fund was established in November 2004, and attracted small contributions from three development partners to finance analytic studies on conflict related topics. IDA played a lead role at the 2005 and 2007 Development Forums and continues to be recognized for its high quality analytic work and leadership in policy dialogue. In response to the 2004 tsunami, the Bank served in a multi-donor steering committee and participated actively in sector and thematic working groups set up to coordinate relief.

33. There have apparently been no safeguard or fiduciary issues.

34. IEG rates Bank performance as *moderately satisfactory*.

#### 4. Overall IEG Assessment

<b>Outcome</b>	<i>Moderately Unsatisfactory</i>
<b>Bank Performance:</b>	<i>Moderately Satisfactory</i>
<p>35. The outcome rating gave more weight to the second pillar since half of the planned CAS program was allocated to support a program of policy reform that didn't materialize. Limited progress has been made towards fostering equity, reflecting slow agricultural growth, deep-rooted deficiencies in the quality of basic education services as well as severe infrastructure deficiencies outside the Western province. While notable initial progress was achieved in reconstruction in the North and East, these outcomes were effectively negated with the resumption of armed hostilities. Although the government and the international community rapidly responded to the devastating tsunami, rehabilitation of affected people's livelihoods has been slow and little assistance ever reached adversely affected communities in the North and East.</p>	

#### 5. Assessment of CAS Completion Report

36. The CASCR is clearly written and covers CAS objectives as written in the CAS and CASPR. It provides adequate information on the implementation and outcomes for most components of each objective of the CAS, although information on some targets is missing and the appropriateness of the lending level in light of CAS performance triggers is not discussed. Overall, the CASCR provides very useful lessons in several areas, and while IEG is in agreement with these lessons, those relating to delivering assistance in a conflict setting relate more to providing assistance during a cease-fire.

#### 6. Findings and Lessons

37. Eroding governance standards; a weak, fragmented, and politicized public service; a large debt overhang; and policymakers' preoccupation with an escalating armed conflict constitute a formidable constraint to using aid effectively. There is a need for the Bank to limit lending into an adverse policy setting. During the current policy dialogue hiatus, IDA can best address this complex set of challenges by prioritizing its ESW, building constituencies for reform, and focusing assistance in those sectors where reform-readiness is firmly demonstrated and a significant impact on poverty reduction can be made. Bank lending triggers have signalling value only if respected. In a setting fraught with risk, these should be well-defined and linked to actions firmly within the government's control.

38. Public policy in Sri Lanka is often made with reference to data that is either incomplete or out-of-date. Going forward, more emphasis is needed to assist the government to generate up-to-date statistical information, particularly with regards to progress in poverty reduction and the effectiveness of social sector outlays.



**ANNEXES**

<b>Annex Table 1:</b>	<b>Planned and Actual Lending FY03–07</b>
<b>Annex Table 2:</b>	<b>Planned Non-lending Services and Actual Deliveries</b>
<b>Annex Table 3:</b>	<b>IEG Project Ratings</b>
<b>Annex Table 4:</b>	<b>Portfolio Status Indicators by Fiscal Year, FY03–07</b>
<b>Annex Table 5:</b>	<b>IBRD/IDA Net Disbursements and Charges Summary Report for Sri Lanka</b>
<b>Annex Table 6:</b>	<b>Total Net Disbursements of Official Development Assistance and Official Aid, 2003–2006</b>
<b>Annex Table 7:</b>	<b>Sri Lanka Economic and Social Indicators</b>
<b>Annex Table 8:</b>	<b>Sri Lanka Millennium Development Goals</b>
<b>Annex Table 9:</b>	<b>Sri Lanka Governance Indicators, 2002–2006</b>
<b>Annex Table 10:</b>	<b>Summary of Achievement of the CAS Objectives</b> <b>Pillar I</b> <b>Pillar II</b> <b>Pillar III</b> <b>Pillar IV</b>

**ATTACHMENT**

<b>Attachment 1:</b>	<b>IEG-IFC Review of the Sri Lanka CAS Completion Report</b>
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**Annex Table 1: Planned and Actual Lending FY03–07**

**Base Case Scenario**

	Proposed FY	Approval FY	Proposed Amount	Approved Amount
<b>CAS 03</b>				
<b>2003</b>				
Second Community Water Supply and Sanitation	2003	2003	40.0	39.8
Economic Reform Technical Assistance	2003	2003	15.0	15.0
National HIV/AIDS Prevention	2003	2003	10.0	12.6
Improving Relevance & Quality of Undergraduate Education	2003	2003	30.0	40.3
PRSC I	2003	2003	110.0	125.0
<b>2004</b>				
E-Sri Lanka Development	2004	<i>slipped to FY05</i>	50.0	53.0
Rural Poverty Reduction Initiative (NEIAP II)	2004	2004	40.0	64.7
Health Sector Development	2004	2004	50.0	60.0
PRSC II	2004	<i>dropped</i>	90.0	<i>dropped</i>
<b>Additional Projects</b>				
Community Development and Livelihood Improvement "Gemi Diriya" Project		2004		51.0
<b>2005</b>				
NE Infrastructure Rehabilitation/Capacity Building	2005	2005	40.0	75.0
Public Sector Reform Technical Assistance	2005	<i>dropped</i>	15.0	<i>dropped</i>
Education Sector Development Project	2005	<i>slipped to FY06</i>	50.0	60.0
PRSC III: Public Sector Reform	2005	<i>dropped</i>	90.0	<i>dropped</i>
<b>Additional Projects</b>				
Tsunami ERL (Tsunami Emergency Recovery Project – Phase II)		2005		45.0
<b>2006</b>				
Land and Water Administration	2006	<i>dropped</i>	40.0	<i>dropped</i>
Services for the Urban Poor	2006	<i>dropped</i>	40.0	<i>dropped</i>
PRSC IV (To be determined)	2006	<i>dropped</i>	90.0	<i>dropped</i>
<b>Total CAS FY03–06</b>			<b>800.0</b>	<b>641.4</b>
<b>CASPR FY05</b>				
<b>2006</b>				
Governance and Capacity Building TA	2006	<i>slipped to FY08</i>	30.0	<i>slipped to FY08</i>
Education Sector Operation	2006	<i>dropped</i>	60.0	<i>dropped</i>
Sri Lanka - Road Sector Assistance	2006	2006	100.0	100.0
North East Housing Reconstruction (standby)	2006	<i>dropped</i>	15.0	<i>slipped to FY08</i>
<b>2007</b>				
Gemi Diriya II (Estates)	2007	<i>slipped to FY09</i>	50.0	<i>slipped to FY09</i>
Water Management	2007	<i>slipped to FY08</i>	50.0	<i>slipped to FY08</i>
Local Service Delivery	2007	<i>dropped</i>	50.0	<i>dropped</i>
Land Titling (standby)	2007	<i>dropped</i>	30.0	<i>dropped</i>
<b>Additional Projects</b>				
Sri Lanka: Puttalam Housing Project		2007		32.0
Renewable Energy - Additional Financing		2007		40.0
<b>Total CASPR FY06–07</b>			<b>385.0</b>	<b>172.0</b>
<b>Total CAS and CASPR</b>			<b>1,185.0</b>	<b>813.4</b>

Source: Sri Lanka CAS FY03–06, 2006 CASPR and WB Business Warehouse as of March 16, 2008.

**Annex Table 2: Planned Non-lending Services and Actual Deliveries**

	Proposed FY	Delivered to Client FY
<b>Planned</b>		
Social Assessment of the Conflict-Affected Areas	2003	dropped
Public Expenditure Analysis	2003	dropped
Country Procurement Assessment Review (CPAR)	2003	2003
Country Financial Accountability Assessment (CFAA)	2003	2003
Promoting Agricultural & Rural Non-Farm Growth	2003	2003
Safeguards Assessment Paper	2003	dropped
Health Sector Strategy	2003	dropped
Report on Millennium Development Goals (MDGs)	2004	2005
Investment Climate Survey (Urban and Rural)	2004	2005
Public Expenditure Analysis	2004	2004
Development Policy Review (DPR) emphasizing growth	2004	2004
AAA on General Education	2004	2004
Financing of Municipal Services	2004	dropped
Public Expenditure Analysis	2005	dropped
Poverty Update (Poverty Mapping Policy Note)	2005	2005
Nutrition and Environmental Health	2005	slipped to FY08
Land Policies: Lessons from the LIL (Land Policy and Conflict)	2005	2006
Public Expenditure Analysis	2006	2006
Country Economic Update	2006	dropped
Update on Rural Development Issues	2006	dropped
Review of Implementation of Social Programs (Social Protection Note)	2006	2006
Local Service Delivery (Decentralization & Delivery of Services) <sup>/1</sup>	2006	2006
Access to Finance <sup>/1</sup>	2006	2006
Poverty Assessment <sup>/1</sup>	2006	2006
Youth Transitions <sup>/1</sup>	2006	dropped
Tea and Rubber Estates Study <sup>/1</sup>	2006	2007
Study on Ageing <sup>/1</sup>	2007	slipped to FY08
Growth/Development Options for the North East (Sri Lanka Development Forum Report) <sup>/1</sup>	2007	2007
Agriculture Marketing and Trade (LK Ag Research and Extension Review) <sup>/1</sup>	2007	2007
Youth Employment <sup>/1</sup>	2007	dropped
Trade Study <sup>/1</sup>	2007	dropped
<b>Non-planned</b>		
Sri Lanka Land Policy Dialogue		2003
Sri Lanka: Clean Air and Fuels		2003
Sri Lanka: ICT Strategy and Road Map		2003
(LKD) PPIAF: Sri Lanka PSP in H2O&Sanitat		2003
Sri Lanka Code of Conduct		2003
Governance Policy Note		2004
Sri Lanka Public Debt		2004
LK ROSC Accounting and Auditing Assessment.		2004
Roads Policy Note		2004
Public Sector Reform TA		2004
PDTA Sri Lanka Prim Dealer Cap Adequacy		2004



**Annex Table 2: Planned Non-lending Services and Actual Deliveries (continued)**

Sri Lanka Capital Framework for PDs	2004
Sri Lanka Tsunami Damage & Needs Assessment	2005
Sri Lanka Development Forum Paper	2005
Sri Lanka Garment & Textile Policy Notes	2005
PSIA	2006
Sri Lanka - Insolvency ROSC	2006
Public Sector Reform Policy Note	2006
Gap Analysis of Pub. A&A Stds. - LK	2006
Housing Finance	2007
TA for Implementation of Welfare Reform	2007

1/ Project proposed in the CASPR.

Source: Sri Lanka CAS FY03-FY06, 2006 CASPR and WB Business Warehouse as of 03/16/08.

**Annex Table 3: IEG Project Ratings**

Exit FY	Project Name	Total Evaluated (US\$M)	IEG Outcome	IEG Sustainability	IEG ID Impact
2003	Energy Services Delivery	22.4	HIGHLY SATISFACTORY	LIKELY	HIGH
	LK-PRSC	127.5	MODERATELY UNSATISFACTORY	UNLIKELY	MODEST
	Pvt. Sector Infrastructure Dev <sup>1/</sup>	30.0	UNSATISFACTORY	UNLIKELY	MODEST
2004	Environmental Action 1 Project	13.9	SATISFACTORY	LIKELY	MODEST
			MODERATELY		
	Conservation of Medical Plants <sup>2/</sup>	4.6	SATISFACTORY	LIKELY	MODEST
2005	North-East Irrigated Agriculture Project	25.8	SATISFACTORY	LIKELY	SUBSTANTIAL
	Distance Learning Initiative - LIL	1.4	UNSATISFACTORY	LIKELY	MODEST
2006	General Education II	68.1	SATISFACTORY	LIKELY	SUBSTANTIAL
	Mahaweli Restructuring	56.7	UNSATISFACTORY	UNLIKELY	MODEST
	Teacher Education & Teacher Deployment	58.9	MODERATELY UNSATISFACTORY	LIKELY	MODEST
	LK Central Bank Strengthening	32.3	HIGHLY SATISFACTORY	LIKELY	HIGH
2007	Land Titling & Related Services (LIL) <sup>3/</sup>	4.6	UNSATISFACTORY	N.A.	N.A.
			MODERATELY		
	Legal And Judicial Reforms <sup>4/</sup>	17.0	UNSATISFACTORY	N.A.	N.A.

Region	Total Evaluated (No)	Total Evaluated (US\$M)	Outcome % Sat (No)	Sustainability % Likely (No)	Inst Dev Impact % Subst (No)
Sri Lanka	13	463.2	46	73	36
SAR	112	12,644.4	79	84	53
Bankwide	1,305	85,877.8	79	79	55

<sup>1/</sup> The close date of the project was extended to direct the undisbursed amount to the "North East Emergency Reconstruction Program."

According to IEG evaluation (of 2004), the closing date of the project was 06/30/2003, despite BW data shows a closing date in FY07 that reflects the closing date extension. Evaluated amounts have been adjusted to reflect the original project actual size.

<sup>2/</sup> Global Environmental Fund (GEF) Grant.

<sup>3/</sup> IEG rated "Risk to Development Outcome" as "High."

<sup>4/</sup> IEG rated "Risk to Development Outcome" as "Moderate."

Source: Business Warehouse 4a5 and 4a6 as of 03/18/2008.

**Annex Table 4: Portfolio Status Indicators by Fiscal Year, FY03-07**

<b>Fiscal year</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>	<b>2006</b>	<b>2007</b>
<b><u>Sri Lanka</u></b>					
# Projects	15	17	18	16	13
# Projects At Risk	4	2	1	1	2
% At Risk	26.7	11.8	5.6	6.3	15.4
Net Commitment Amount	532.5	693.4	867.4	806.6	778.4
Commitment At Risk	206.6	30.8	5.0	64.7	65.6
% Commitment at Risk	38.8	4.4	0.6	8.0	8.4
<b><u>Bhutan</u></b>					
# Projects	3	5	6	3	5
# Projects At Risk	0	0	0	0	1
% At Risk	0.0	0.0	0.0	0.0	20.0
Net Commitment Amount	36.1	72.9	79.9	43.8	61.8
Commitment At Risk	0.0	0.0	0.0	0.0	7.0
% Commitment at Risk	0.0	0.0	0.0	0.0	11.3
<b><u>Morocco</u></b>					
# Projects	16	12	10	12	12
# Projects At Risk	2	2	2	0	2
% At Risk	12.5	16.7	20.0	0.0	16.7
Net Commitment Amount	425.0	338.3	435.6	813.1	747.4
Commitment At Risk	98.6	14.6	42.2	0.0	53.2
% Commitment at Risk	23.2	4.3	9.7	0.0	7.1
<b><u>Maldives</u></b>					
# Projects	1	1	2	3	2
# Projects At Risk	1	0	0	0	0
% At Risk	100.0	0.0	0.0	0.0	0.0
Net Commitment Amount	17.6	17.6	19.6	42.2	25.3
Commitment At Risk	17.6	0.0	0.0	0.0	0.0
% Commitment at Risk	100.0	0.0	0.0	0.0	0.0
<b><u>Nepal</u></b>					
# Projects	10	9	12	12	13
# Projects At Risk	2	1	1	3	4
% At Risk	20.0	11.1	8.3	25.0	30.8
Net Commitment Amount	303.2	302.0	424.5	421.5	470.2
Commitment At Risk	78.0	75.6	75.6	145.2	138.7
% Commitment at Risk	25.7	25.0	17.8	34.5	29.5
<b><u>Philippines</u></b>					
# Projects	20	21	20	21	20
# Projects At Risk	0	3	2	3	3
% At Risk	0.0	14.3	10.0	14.3	15.0
Net Commitment Amount	1347.6	1113.3	1090.4	1383.1	1217.0
Commitment At Risk	0.0	240.0	46.3	94.6	84.0
% Commitment at Risk	0.0	21.6	4.2	6.8	6.9
<b><u>SAR</u></b>					
# Projects	142	149	156	145	161
# Projects At Risk	25	20	18	19	24
% At Risk	17.6	13.4	11.5	13.1	14.9
Net Commitment Amount	17405.1	17562.0	18041.1	17190.0	20473.8
Commitment At Risk	2537.0	3625.0	1745.0	2858.3	3366.3
% Commitment at Risk	14.6	20.6	9.7	16.6	16.4

Source: WB Business Warehouse Table 3a.4 as of 03/16/08,

**Annex table 5: IBRD/IDA Net Disbursements and Charges Summary Report for Sri Lanka  
(in US\$ million)**

<b>FY</b>	<b>Disbursed Amount</b>	<b>Repay Amount</b>	<b>Net Amount</b>	<b>Charges</b>	<b>Fees</b>	<b>Net Transfer</b>
2003	202.26	37.04	165.22	13.11	0.00	152.11
2004	81.16	39.82	41.34	14.90	0.50	25.94
2005	112.63	41.12	71.51	15.98	0.86	54.67
2006	146.05	40.58	105.47	15.45	0.89	89.14
2007	156.89	47.18	109.71	16.81	0.80	92.10
<b>Total (2003–07)</b>	<b>698.98</b>	<b>205.73</b>	<b>493.25</b>	<b>76.24</b>	<b>3.05</b>	<b>413.96</b>

Source: WB Loan Kiosk, Net Disbursement and Charges Report as of March 17, 2008.

**Annex Table 6: Total Net Disbursements of Official Development Assistance and Official Aid, 2003–2006 (in US\$ million)**

	2003	2004	2005	2006	2003–2006
Arab Agencies	4.26	3.69	2.96	4.86	15.77
Arab Countries	..	1.99	2.32	-0.15	4.16
AsDF (Asian Dev.Fund)	149.69	101.70	125.14	103.08	479.61
Australia	6.31	18.93	43.27	22.96	91.47
Austria	0.43	0.22	9.78	5.72	16.15
Belgium	0.09	0.09	5.37	0.77	6.32
Canada	5.82	5.45	45.69	15.36	72.32
Czech Republic	0.26	0.45	0.24	0.27	1.22
DAC Countries, Total	270.98	337.16	857.33	485.25	1950.72
DAC EU Members, Total	61.09	100.03	315.85	169.58	646.55
Denmark	1.05	12.41	23.88	38.18	75.52
EC	15.19	14.87	16.09	24.53	70.68
Finland	0.96	0.54	4.76	4.62	10.88
France	-1.32	4.66	40.67	-0.70	43.31
G7, Total	192.70	230.48	568.18	319.83	1311.19
GEF	5.19	2.76	1.40	3.36	12.71
Germany	16.31	28.57	75.23	63.94	184.05
Global Fund (GFATM)	3.10	2.32	1.79	0.96	8.17
Greece	..	0.16	4.62	2.45	7.23
Hungary	..	0.53	..	..	0.53
Iceland	..	..	1.13	1.98	3.11
IDA	168.32	31.65	114.30	113.33	427.6
IFAD	2.25	-0.13	-0.07	1.79	3.84
Ireland	0.39	0.06	5.03	0.38	5.86
Italy	-1.09	-1.18	20.82	2.46	21.01
Japan	172.26	179.53	312.91	202.73	867.43
Korea	17.15	16.55	33.21	22.65	89.56
Luxembourg	..	0.11	0.02	1.04	1.17
Netherlands	21.51	13.91	56.16	14.95	106.53
New Zealand	0.47	0.90	3.39	1.47	6.23
Non-DAC Countries, Total	17.50	20.76	49.98	37.81	126.05
Nordic Dev. Fund	2.12	2.36	4.20	4.01	12.69
Norway	28.55	30.33	65.98	37.28	162.14
Other Bilateral Donors	0.09	0.06	0.12	0.14	0.41
Poland	0.00	0.16	0.02	0.01	0.19
Portugal	..	0.11	0.54	1.20	1.85
SAF+ESAF+PRGF(IMF)	22.37	-8.30	..	..	14.07
Slovak Republic	..	0.38	..	..	0.38
Spain	..	0.60	3.53	7.15	11.28
Sweden	13.49	22.95	51.72	20.56	108.72
Switzerland	5.03	5.36	11.10	6.69	28.18
Thailand	..	..	..	0.19	0.19
Turkey	..	0.64	12.94	12.72	26.3

**Annex Table 6: Total Net Disbursements of Official Development Assistance and Official Aid, 2003–2006 (in US\$ million) (continued)**

	2003	2004	2005	2006	2003-2006
UNDP	3.19	2.48	2.56	3.11	11.34
UNFPA	-0.17	0.95	2.86	6.20	9.84
UNHCR	5.09	..	1.35	2.91	9.35
UNICEF	1.12	0.97	0.71	0.93	3.73
United Kingdom	9.27	16.82	13.72	6.86	46.67
United States	-8.55	-3.37	59.14	29.18	76.4
UNTA	4.94	3.26	4.65	2.97	15.82
WFP	1.80	3.38	6.72	0.79	12.69
<b>Multilateral, Total</b>	<b>388.46</b>	<b>161.96</b>	<b>284.66</b>	<b>272.83</b>	<b>1,107.91</b>
<b>All Donors, Total</b>	<b>676.94</b>	<b>519.88</b>	<b>1,191.97</b>	<b>795.89</b>	<b>3,184.68</b>

Source: OECD DAC Online database, table 2a. Destination of Official Development Assistance and Official Aid - Disbursements, as of 03/18/08.

Annex Table 7: Sri Lanka Economic and Social Indicators, 2003-2006

Series Name	Sri Lanka					Average 2003-2006					Lower middle income	South Asia
	2003	2004	2005	2006	2006	Sri Lanka	Bhutan	Morocco	Maldives	Nepal	Philippines	
<b>Growth and Inflation</b>												
GDP growth (annual %)	6.0	5.4	6.0	7.4	7.4	6.2	7.2	4.7	8.8	2.9	5.4	8.2
GDP per capita growth (annual %)	4.7	4.3	5.1	6.6	6.6	5.2	4.7	3.5	6.2	0.9	3.5	6.5
GNI per capita, PPP (current international \$)	3960	4230	4570	5010	5010	4443	5018	4520	1558	1558	5403	3002
GNI per capita, Atlas method (current US\$)	930	1040	1170	1300	1300	1110	1183	1640	2400	260	1248	643
Inflation, consumer prices (annual %)	6.3	7.6	11.6	13.7	13.7	9.8	4.0	1.7	2.6	5.1	5.8	..
<b>Composition of GDP (%)</b>												
Agriculture, value added (% of GDP)	19.0	17.8	16.8	16.4	16.4	17.5	26.2	15.8	..	38.8	14.4	19.6
Industry, value added (% of GDP)	26.4	26.8	26.1	26.5	26.5	26.4	38.5	29.8	..	21.0	32.3	26.9
Services, etc., value added (% of GDP)	54.6	55.4	57.1	57.1	57.1	56.1	35.4	54.4	..	40.1	53.3	53.4
<b>External Accounts</b>												
Exports of goods and services (% of GDP)	35.9	36.4	33.9	32.6	32.6	34.7	27.6	35.0	80.8	17.2	47.7	36.7
Imports of goods and services (% of GDP)	42.1	45.5	45.5	43.1	43.1	44.0	46.5	41.3	85.9	33.1	53.2	35.2
Current account balance (% of GDP)	-0.4	-3.2	-2.8	..	..	-2.1	..	2.6	-21.8	2.2	1.5	..
External debt (% of GNI)	57.4	57.7	49.3	..	..	54.8	81.3	37.5	47.1	50.5	63.9	28.1
Total debt service (% of GNI)	3.4	3.9	1.9	..	..	3.1	1.3	7.1	4.1	1.7	11.1	3.7
Total reserves in months of imports	3.5	2.8	3.2	..	..	3.1	..	9.3	3.0	7.4	3.8	11.4
Gross fixed capital formation (% of GDP)	22.0	25.0	26.1	26.5	26.5	24.9	60.7	24.9	32.4	18.9	15.7	31.7
<b>Fiscal Accounts<sup>1/</sup></b>												
Revenue and Grants (% of GDP)	16.2	15.8	17.4	18.1	18.1	16.9	33.3	23.7	45.0	13.7	15.2	..
Total Expenditure (and not lending, % of GDP)	24.0	23.5	24.7	25.5	25.5	24.4	35.7	27.8	50.8	14.9	18.7	..
Overall Balance, excluding grants (% of GDP)	-8.3	-8.2	-8.7	-8.4	-8.4	-8.4	-17.5	-15.1	-13.1	-3.4	..	..
Overall Balance, including grants (% of GDP)	-7.8	-7.7	-7.3	-7.4	-7.4	-7.6	-2.4	-4.1	-5.9	-1.2	-3.5	..
Government Debt, domestic and external (% of GDP) <sup>2/</sup>	107.9	107.5	96.3	94.7	94.7	101.4	81.1	61.0	41.1	53.2	65.7	..
<b>Social Indicators</b>												
<b>Health</b>												
Life expectancy at birth, total (years)	..	..	74.7	..	..	74.7	..	70.4	67.6	62.7	71.0	63.5
Immunization, DPT (% of children ages 12-23 months)	99.0	97.0	99.0	..	..	98.3	93.0	95.3	97.3	77.7	79.0	64.0
Improved sanitation facilities (% of population with access)	..	91.0	..	..	..	91.0	70.0	73.0	59.0	35.0	72.0	37.2
Improved water source (% of population with access)	..	79.0	..	..	..	79.0	62.0	81.0	83.0	90.0	85.0	84.4
Mortality rate, infant (per 1,000 live births)	..	..	12.0	..	..	12.0	65.0	36.0	33.0	56.0	25.0	61.8
<b>Population</b>												
Population, total (million)	19.3	19.5	19.6	19.8	19.8	19.5	0.6	30.0	0.3	26.9	82.4	1457.9
Population growth (annual %)	1.3	1.1	0.8	0.7	0.7	1.0	2.3	1.1	2.4	2.0	1.8	1.6
Urban population (% of total)	15.3	15.2	15.1	15.1	15.1	15.2	11.0	58.3	29.4	15.6	62.3	28.4
<b>Education</b>												
School enrollment, primary (% gross)	..	..	..	..	..	..	..	53.8	46.1	24.5	38.9	35.5
School enrollment, primary (% gross)	101.7	97.7	..	..	..	99.7	102.1	105.7	102.3	116.4	112.5	108.6
School enrollment, secondary (% gross)	81.0	82.5	..	..	..	81.8	83.5	47.2	73.2	43.8	85.0	71.8

<sup>1/</sup> IMF Sri Lanka: Article IV Consultations for Bhutan (2003 corresponds to FY 2003-04); 2007 Article IV Consultations for

Maldives; Nepal: IMF Country Report No. 07/366 (November 2007); Philippines: 2006 Article IV Consultation.

<sup>2/</sup> Data for Maldives only refers to Governmental external debt.

Source: WB World Development Indicators (September 2007 update) for all indicators excluding those noted.

**Annex Table 8: Sri Lanka - Millennium Development Goals**

	1990	1995	2000	2005
<b>Goal 1: Eradicate extreme poverty and hunger</b>				
Income share held by lowest 20%	9	8	7 ..	
Malnutrition prevalence, weight for age (% of children under 5)	..	32.9	29.7 ..	
Poverty gap at \$1 a day (PPP) (%)	0.7	1	0.8 ..	
Poverty headcount ratio at \$1 a day (PPP) (% of population)	3.8	6.6	5.6 ..	
Poverty headcount ratio at national poverty line (% of population)	20	25 ..	..	
Prevalence of undernourishment (% of population)	28	26 ..		22
<b>Goal 2: Achieve universal primary education</b>				
Literacy rate, youth total (% of people ages 15-24)	95 ..	..		96
Persistence to grade 5, total (% of cohort)	92 ..	..	..	
Primary completion rate, total (% of relevant age group)	92	99	92 ..	
School enrollment, primary (% net)	..	..	..	97
<b>Goal 3: Promote gender equality and empower women</b>				
Proportion of seats held by women in national parliament (%)	5	5	5	5
Ratio of girls to boys in primary and secondary education (%)	101 ..		102	102
Ratio of young literate females to males (% ages 15-24)	98 ..	..		101
Share of women employed in the nonagricultural sector (% of total nonagricultural employment)	39.1	44	46	43.2
<b>Goal 4: Reduce child mortality</b>				
Immunization, measles (% of children ages 12-23 months)	80	87	99	99
Mortality rate, infant (per 1,000 live births)	26	21	16	12
Mortality rate, under-5 (per 1,000)	32	25	19	14
<b>Goal 5: Improve maternal health</b>				
Births attended by skilled health staff (% of total)	..	94	96 ..	
Maternal mortality ratio (modeled estimate, per 100,000 live births)	..	..	92 ..	
<b>Goal 6: Combat HIV/AIDS, malaria, and other diseases</b>				
Contraceptive prevalence (% of women ages 15-49)	..	..	70 ..	
Incidence of tuberculosis (per 100,000 people)	60	60	60	60
Prevalence of HIV, female (% ages 15-24)	..	..	..	
Prevalence of HIV, total (% of population ages 15-49)	..	..	..	0.1
Tuberculosis cases detected under DOTS (%)	..	59	63	86
<b>Goal 7: Ensure environmental sustainability</b>				
CO2 emissions (metric tons per capita)	0.2	0.3	0.5	0.5
Forest area (% of land area)	36 ..		32	30
GDP per unit of energy use (constant 2000 PPP \$ per kg of oil equivalent)	7.3	8.7	8.7	8.3
Improved sanitation facilities (% of population with access)	69 ..	..		91
Improved water source (% of population with access)	68 ..	..		79
Nationally protected areas (% of total land area)	..	..	..	27.3
<b>Goal 8: Develop a global partnership for development</b>				
Aid per capita (current US\$)	43	31	14	61
Debt service (PPG and IMF only, % of exports of G&S, excl. workers' remittances)	14.8	8.8	10.8	4.2
Fixed line and mobile phone subscribers (per 1,000 people)	7	14	62	235
Internet users (per 1,000 people)	0	0	6	14
Personal computers (per 1,000 people)	0	1	7	27
Total debt service (% of exports of goods, services and income)	13.8	8	10.3	4.5
Unemployment, youth female (% of female labor force ages 15-24)	46.9	41.3	30.9	37.1
Unemployment, youth male (% of male labor force ages 15-24)	22.8	27	19.9	20.1
Unemployment, youth total (% of total labor force ages 15-24)	33.3	32.8	23.6	26.2
<b>Other</b>				
Fertility rate, total (births per woman)	2.5	2.2	1.9	1.9
GNI per capita, Atlas method (current US\$)	470	700	810	1160
GNI, Atlas method (current US\$) (billions)	7.9	12.7	15.7	22.8
Gross capital formation (% of GDP)	22.6	25.7	28	26.2
Life expectancy at birth, total (years)	71	73	74	75
Literacy rate, adult total (% of people ages 15 and above)	89 ..	..		91
Population, total (millions)	17	18.1	19.4	19.6
Trade (% of GDP)	67.2	81.6	88.6	79.6

Source: World Development Indicators database, as of 03/18/2008.



**Annex Table 9: Sri Lanka Governance Indicators, 2002 – 2006**

Governance Indicator	2002	2003	2004	2005	2006
<b><u>Voice and Accountability</u></b>					
Sources	8	9	10	11	12
Percentile Rank (0-100)	44.2	42.3	43.3	41.3	36.1
Governance Score (-2.5 to +2.5)	-0.21	-0.19	-0.24	-0.24	-0.35
Standard Error	0.18	0.15	0.16	0.15	0.15
<b><u>Political Stability</u></b>					
Sources	7	7	8	8	8
Percentile Rank (0-100)	19.2	19.7	13.9	10.1	8.2
Governance Score (-2.5 to +2.5)	-0.96	-0.95	-1.14	-1.35	-1.61
Standard Error	0.24	0.25	0.23	0.23	0.23
<b><u>Government Effectiveness</u></b>					
Sources	10	10	11	11	12
Percentile Rank (0-100)	57.8	55	44.1	39.3	42.2
Governance Score (-2.5 to +2.5)	-0.06	-0.17	-0.33	-0.41	-0.36
Standard Error	0.16	0.16	0.17	0.15	0.16
<b><u>Regulatory Quality</u></b>					
Sources	10	10	11	11	11
Percentile Rank (0-100)	60.5	57.1	55.6	48.8	50.2
Governance Score (-2.5 to +2.5)	0.22	0.1	0	-0.19	-0.11
Standard Error	0.2	0.17	0.18	0.18	0.18
<b><u>Rule of Law</u></b>					
Sources	13	14	15	15	16
Percentile Rank (0-100)	56.7	53.3	53.3	54.3	54.3
Governance Score (-2.5 to +2.5)	0.15	0.04	0.01	0.05	0.01
Standard Error	0.14	0.14	0.14	0.14	0.14
<b><u>Control of Corruption</u></b>					
Sources	9	10	11	11	12
Percentile Rank (0-100)	51.5	51.9	52.4	47.6	48.5
Governance Score (-2.5 to +2.5)	-0.21	-0.21	-0.18	-0.3	-0.29
Standard Error	0.15	0.15	0.16	0.16	0.16

**NOTE:**

**1. Voice and Accountability:**

Measures the extent to which country's citizens are able to participate in selecting their government, as well as freedom of expression, freedom of association, and a free media.

**2. Political Stability and Absence of Violence:**

Measures the perceptions of the likelihood that the government will be destabilized or overthrown by unconstitutional or violent means, including domestic violence and terrorism.

**3. Government Effectiveness:**

Measures the quality of public services, the quality of the civil service and the degree of its independence from political pressures, the quality of policy formulation and implementation, and the credibility of the government's commitment to such policies.

**4. Regulatory Quality:**

Measures the ability of the government to formulate and implement sound policies and regulations that permit and promote private sector development.

**5. Rule of Law:**

Measures the extent to which agents have confidence in and abide by the rules of society, in particular the quality of contract enforcement, the police, and the courts, as well as the likelihood of crime and violence.

**6. Control of Corruption:**

Measures the extent to which public power is exercised for private gain, including petty and grand forms of corruption, as well as "capture" of the state by elites and private interests.

Source: Governance Indicators database, March 2008

**Annex Table 10: Summary of Achievements of the CAS Objectives (Pillar I)**

<b>SL CAS CASPR 03-07: Pillar I Peace</b>		<b>Actual Results (as of February 2008)</b>	<b>Comments</b>
<b>Objectives</b>	1. Restore access to health, education and irrigation in conflict-affected areas	<b>PARTIALLY ACHIEVED</b>	Education facilities restored in conflict-affected areas to pre-war levels (achieved, but sustainability threatened by conflict resumption) Water supply for irrigation increased in conflict-affected areas (achieved, but progress threatened by resumption of armed conflict)
	2. Strengthen institutional framework and capacity in conflict-affected areas to facilitate reconstruction and poverty reduction efforts	<b>PARTIALLY ACHIEVED</b>	Progress made in re-establishing divisional administration reversed with conflict-affected parts of the North and east under supervision of the military, LTTE or other armed combatants
<b>Major Outcome Measures</b>	1. <u>Restore access to health, education and irrigation in conflict-affected areas</u>		Partially achieved
	Education facilities restored in conflict-affected areas to pre-war levels (Target: 197 schools rehabilitated)	183 of schools rehabilitated (98% of target)	Achieved
	Percentage of children enrolled in basic education (grades 6-9) in N&E	71% (2004)  - Number of students in basic education in the North and East: 195,444 (2002) - 220,493 (2006) 3.2% increase per annum from 2002-2006	Partly achieved
	Water supply for irrigation increased in conflict-affected areas (Target: 379 water supply schemes rehabilitated)	369 water supply schemes rehabilitated by June 2005 (97% of target)	Achieved
	Agricultural (paddy) Production in N&E ('000 MT) (202.4 for the period 1996-2001)	Paddy production increases five-fold from 202 MT in 1996-2001 to 1,372 MT (2002-2004)	Achieved
	2. <u>Strengthen institutional framework and capacity in conflict-affected areas to facilitate reconstruction and poverty reduction efforts</u>	The North East Reconstruction Fund (NERF) in 2003; and the Sri Lanka Tsunami Reconstruction Fund (SLTRF) in 2005 were to be major sources of support for reconstruction but never materialized.	Partially achieved
	Build technical capacity to implement the reconstruction and poverty reduction efforts	NEERP project financed the reconstruction of administrative buildings, procurement of vehicles and training to help strengthen the provincial and divisional administration. This led to the reopening of operations of divisional administration. Operations of the recently re-opened divisional administration have been suspended due to the resumption of the armed conflict.	Partially achieved.
<b>Ongoing pre-CAS 03-07 IDA Support</b>	1. <u>Restore access to health, education and irrigation in conflict-affected areas</u>		
	Second General Education Project	Approved FY98. Closed 11/05	IEG outcome: Satisfactory
	Teacher education & teacher deployment	Approved FY97. Closed 10/05	IEG outcome: Moderately unsatisfactory
	North-East Irrigated Agriculture Project (NEIAP I)	Approved FY00. Closed 06/05	IEG outcome: Satisfactory
	2. <u>Strengthen institutional framework and capacity in conflict-affected areas to facilitate reconstruction and poverty reduction efforts</u>		
	North-East Irrigated Agriculture Project (NEIAP I)	Approved FY00. Closed 06/05	IEG outcome: Satisfactory
<b>New IDA Lending Support</b>	1. <u>Restore access to health, education and irrigation in conflict-affected areas</u>		
	Rural Poverty Reduction Initiative (NEIAP II)	Approved FY04. Active	Latest PDO rating: Moderately satisfactory (12/19/2007)
	NE Infrastructure Rehabilitation/Capacity Building	Approved FY05. Active	Latest PDO rating: Satisfactory (12/26/2007)
	2. <u>Strengthen institutional framework and capacity in conflict-affected areas to facilitate reconstruction and poverty reduction efforts</u>		

**Annex Table 10: Summary of Achievements of the CAS Objectives (Pillar I)**

<b>SL CAS, CASPR 03-07: Pillar I Peace</b>		<b>Actual Results (as of February 2008)</b>	<b>Comments</b>
	NE Infrastructure Rehabilitation/Capacity Building	Approved FY05. Active	Latest PDO rating: Satisfactory (12/26/2007)
<b>Planned AAA</b>	<u>1. Restore access to health, education and irrigation in conflict-affected areas</u>		
	Social Assessment of the Conflict-Affected Areas	Dropped	
	<u>2. Strengthen institutional framework and capacity in conflict-affected areas to facilitate reconstruction and poverty reduction efforts</u>		
	Land Policy and Conflict	Delivered FY06	
<b>Additional AAA</b>			

\* In cases where results are not reported, IEG takes this lack of evidence as the equivalent of "not achieved"

**Annex Table 10: Summary of Achievements of the CAS Objectives (Pillar II)**

<u>SL CAS, CASPR 03-07: Pillar II</u> Growth		Actual Results (as of February 2008)	Comments
<b>Objectives</b>	1. Create enabling macro environment for private sector driven investment and growth	NOT ACHIEVED	Enabling environment for private sector driven growth remains constrained by inflation, fiscal deficits, high levels of public debt, large public enterprise losses, and structural policies which impede efficient resource use
	2. Expand employment opportunities and the flexibility of the labor market	NOT ACHIEVED	Labor market regulations modestly improved but working hours remain rigid, severance payments are extremely high and applications for worker termination are still subject to the approval of the Labour Commissioner
	3. Improve the soundness of the financial system	PARTIALLY ACHIEVED	CBSL reforms have contributed to improved financial sector stability, including a sharp decline in the NPL ratios across banks (from 14.5% in 2002 to 5.4% in 2006), a marked strengthening in the capital base of the banking industry, and a sustained improvement in banks' operating profits. However, plans for privatizing the People's Bank have been abandoned and two new public sector policy banks have been established
	4. Increase productivity in the rural economy	NOT ACHIEVED	Some Progress has been made in introducing sustainable off-grid energy sources to broaden access to rural power, with innovative Bank assistance, and some 782 off-grid private rural energy suppliers were in operation by FY07. However, agriculture has grown slowly at 2-3% per annum, fertilizer subsidies and restrictive agriculture trade policies were re-introduced in 2005, restrictive phytosanitary policies continue to impede access to improved planting material, the Mahaweli Authority has not yet been transformed into a river-basin planning agency and privatization of its seven business units has stalled, and transfer of irrigation O&M responsibilities to farmers has proceeded slowly and with limited efficiency gains.
	5. Improve the quality of public service delivery	NOT ACHIEVED	The public service continues to be very large, and is marked by over-staffing, political interference, fragmentation, and low levels of accountability. Public sector employment grew by 9% between 2002 and 2006, compared to 3% for private sector employment. Rather than streamlining the public sector, and despite facing severe fiscal pressures, in 2006, public administration and defense expenditures increased sharply. Moreover, World Bank governance indicators for voice and accountability, political stability, government effectiveness, rule of law, and control of corruption have all deteriorated between 2002 and 2007.
<b>Major Outcome Measures</b>	1. Create enabling macro environment for private sector driven investment and growth		Not achieved
	Higher sustained economic growth	Growth was fueled by a fiscal and monetary stimulus resulting in a macroeconomic setting fraught with risk	Partly achieved
	GDP Growth (4% in 2002)	Average 6.2% (2003-2007)	Growth rate achieved although little Bank contribution and macro-setting remains fraught with risk

**Annex Table 10: Summary of Achievements of the CAS Objectives (Pillar II)**

<u>SL CAS, CASPR 03-07: Pillar II</u> Growth	Actual Results (as of February 2008)	Comments
<u>Results-based budgeting system established</u>	System established in 2004 but not utilized for budgeting purposes	Not achieved
Budget allocations for operations & maintenance, % of total expenditure (31% in 2002)	28% (2004)	Not achieved (Not reported beyond 2004)
Budget allocations for infrastructure, % of capital expenditure/total expenditure (14.5% in 2002)	17.6% (2004)	Not achieved (Not reported beyond 2004)
<u>Improved financial performance of key state enterprises</u>	CEB losses equivalent to .75% of GDP in 2006	Not achieved
Total profit/losses of key SOEs (CEB: \$76m in 2002; CPC: \$75m in 2002)	- Electricity (CEB): \$38m (2003); -\$150m (2004); -\$67m (2005) - Petroleum (CPC): \$50m (2003); \$37m (2004)	Not achieved
Public transfers to SOEs	Electricity (CEB): \$111m subsidy (2005) Petroleum (CPC): n.a.	Not achieved
<u>2. Expand employment opportunities and the flexibility of the labor market</u>		Not achieved
<u>Legal framework to increase flexibility in labor markets and promote harmonious labor relations</u>	Market regulations remain inflexible: working	Not achieved
Unemployment in the formal sector (8.1% in 2003)		sector employment)
<u>3. Improve the soundness of the financial system</u>		Partially achieved
CBSL re-focused towards managing its core functions	CBSL restructured and focused on core mandate. However, two new policy banks have been established.	Partially achieved
Ratio of non-performing loans to total loans outstanding (State Banks: 16.9% in 2002; All commercial banks: 14.5% in 2002)	- State Banks: 11.4% (2004) - All commercial banks: 12.5% (2003); 8.9% (2004); 6.8% (2005); 5.4% (2006)	Achieved
<u>4. Increase productivity in the rural economy</u>		Not achieved
Off-farm income generation activities promoted through sustainable rural electrification, including in conflict ridden areas	Agriculture has grown slowly at 2-3% per annum, fertilizer subsidies and restrictive agriculture trade policies re-introduced in 2005	Not achieved
Number of economic activities using off-grid electricity	400 (2004); 782 (2007) households/small enterprises	Partially achieved
<u>5. Improve the quality of public service delivery</u>	WB Governance Indicators all deteriorated between 2002 and 2007; government staffing and outlays on public administration and defense increased over the CAS period	Not achieved
Politicization of the civil service reduced and public service accountability improved	Public sector leadership continues to suffer from high rates of turnover and political interference in staffing	Not achieved
Growth of public sector employment	Efforts to curb the growth in public sector employment were unsuccessful with the government cadre growing by 9% (2002-2006) while private sector employment grew by 3.1%	Not achieved
<u>Ongoing pre-CAS 03-07 IDA Support</u>		
<u>3. Improve the soundness of the financial system</u>		
LK Central Bank Strengthening	Approved FY02. Closed 12/05	IEG outcome: Highly satisfactory
<u>4. Increase productivity in the rural economy</u>		
Renewable energy for rural economic development	Approved FY02. Active	Latest PDO rating: Satisfactory (12/20/2007)
<u>5. Improve the quality of public service delivery</u>		
Legal and judicial reforms	Approved FY01. Closed 02/07	IEG outcome: Moderately unsatisfactory

\* In cases where results are not reported, IEG takes this lack of evidence as the equivalent of "not achieved."

**Annex Table 10: Summary of Achievements of the CAS Objectives (Pillar II)**

	<b>SL CAS, CASPR 03-07: Pillar II Growth</b>	<b>Actual Results (as of February 2008)</b>	<b>Comments</b>
<b>New IDA Lending Support</b>	<b>1. Create enabling macro environment for private sector driven investment and growth</b>		
	PRSC I	Approved FY03. Closed 12/03	IEG outcome: Moderately unsatisfactory
	Economic Reform Technical Assistance	Approved FY03. Closed 06/07	ICR outcome: Moderately unsatisfactory
	PRSC II, III and IV	Dropped	
	<b>2. Expand employment opportunities and the flexibility of the labor market</b>		
	PRSC I	Approved FY03. Closed 12/03	IEG outcome: Moderately unsatisfactory
	Economic Reform Technical Assistance	Approved FY03. Closed 06/07	ICR outcome: Moderately unsatisfactory
	<b>4. Increase productivity in the rural economy</b>		
	PRSC I	Approved FY03. Closed 12/03	IEG outcome: Moderately unsatisfactory
	Renewable Energy - Additional Financing	Approved FY07. Active	
	<b>5. Improve the quality of public service delivery</b>		
	Economic Reform Technical Assistance	Approved FY03. Closed 06/07	ICR outcome: Moderately unsatisfactory
	E-Sri Lanka Development	Approved FY05. Active	Latest PDO rating: Moderately Unsatisfactory (06/15/2007)
<b>Planned AAA and TA</b>	<b>1. Create enabling macro environment for private sector driven investment and growth</b>		
	Development Policy Review	Delivered FY04	
	Improving Rural and Urban Investment Climate	Delivered FY05	
	Public Expenditure Analysis (PER)	Delivered FY04, FY06	
	<b>2. Expand employment opportunities and the flexibility of the labor market</b>		
	Development Policy Review	Delivered FY04	
	Youth Employment	Dropped	
	<b>4. Increase productivity in the rural economy</b>		
	Promoting Agricultural & Rural Non-Farm Growth	Delivered FY03	
	Improving Rural and Urban Investment Climate	Delivered FY05	
	<b>5. Improve the quality of public service delivery</b>		
	Country Procurement Assessment Review	Delivered FY03	
	Development policy review	Delivered FY04	
	Public Expenditure Analysis (PER)	Delivered FY04, FY06	
	Decentralization and delivery of services	Delivered FY06	
<b>Additional AAA</b>	<b>1. Create enabling macro environment for private sector driven investment and growth</b>		
	Roads Policy note	Delivered FY04	
	Public Debt Policy Note	Delivered FY04	
	Garment and Textile Policy Note	Delivered FY05	
	<b>3. Improve the soundness of the financial system</b>		
	Housing Finance	Delivered FY07	
	<b>5. Improve the quality of public service delivery</b>		
	Governance policy note	Delivered FY04	
	LK ROSC Accounting and Auditing Assmt.	Delivered FY04	

\* In cases where results are not reported, IEG takes this lack of evidence as the equivalent of "not achieved."

**Annex Table 10: Summary of Achievements of the CAS Objectives (Pillar III)**

	<b>SL CAS, CASPR 03-07: Pillar III Equity</b>	<b>Actual Results (as of February 2008)</b>	<b>Comments</b>
<b>Objectives</b>	1. Improve overall equity in the country	<b>PARTIALLY ACHIEVED</b>	While the poverty headcount has fallen from 23% in 2002 to 14% in 2006/07, regional income inequality continues to widen with 60% of GDP originating in Colombo and the Western Province. The 2006/07 Household Income and Expenditure Survey shows no improvement in income inequality since 2002. Estate sector poverty levels have increased from 30% in 2002 to 32% in 2006/2007.
	2. Improve the quality of basic education system	<b>PARTIALLY ACHIEVED</b>	A norm-based unit cost resource allocation formula was applied to school financing that enhanced equity; and schools in "difficult areas" and "very difficult areas" received 40–70% more resources than other schools. However, learning outcomes remain unsatisfactory with primary school pupils at the end of their primary cycle having extremely low cognitive achievement scores in their first language (37%), math (38%) and the English language (10%).
	3. Improve health status of the population	<b>PARTIALLY ACHIEVED</b>	While district health plans have been prepared, and the number of districts with high infants and maternal mortality has declined, this may be due to an increase in public health per capita expenditures from \$13.7 in 2002 to \$17.4 in 2006 rather than to improvements in health service delivery efficiency.
	4. Curb spread of HIV infection	<b>NOT ACHIEVED</b>	HIV awareness and knowledge levels in underserved communities remain drastically low, and Bank project assistance on this has stalled.
	5. Improve access to services in poor districts	<b>PARTIALLY ACHIEVED</b>	Number of empowered communities implementing sub-projects contained in their development plans expanded but community empowerment is hindered by high levels of continued dependence on donor finance.
<b>Major Outcome Measures</b>	1. Improve overall equity in the country		Partially achieved
	Reduction of poverty especially in lagging rural areas and estates; improvement in social outcomes in the estate sector and better targeting of welfare programs to the poor		Partially achieved
	National poverty headcount ratio (23% in 2002)	National poverty headcount ratio (15% in 2006/2007)	Achieved
	Urban-rural gap in poverty headcount (17 percentage points in 2002)	2006/07 Gini Coefficient widens from 0.37 in 2002 to 0.4 in 2006/07. Urban-rural gap in poverty headcount reduces to 9 percentage points in 2006/07.	Partially achieved
	Coverage of Samurdhi among the poorest 10 percent of population (69% in 2000)	Funding levels for Samurdhi substantially reduced and targeting remains unchanged	Not achieved
	Share of poorest 20 percent of population in total Samurdhi benefits (25% in 2000)	Funding levels for Samurdhi substantially reduced and targeting remains unchanged	Not achieved
	Poverty headcount ratio for estate sector (30% in 2002)	Poverty headcount ratio for estate sector (32% in 2006/07)	Not achieved *
	2. Improve the quality of basic education system		Partially achieved
	Investment in education increased, especially in poor schools, including in learning resources and teaching materials		Partially achieved
	Survival rate to grade 9	78% (2004)	Not achieved *
	Proficiency of graduates in English	42% (2004) (Average English scores of graduates: 59 in 2005; 67 in 2007)	Achieved
	3. Improve health status of the population		Partially achieved
	Effectiveness in the health sector's use of existing resources improved		Partially achieved
	Percent of districts with satisfactory annual financial and physical progress reports	- Submitted Annual Health Plans: 0% (2004); 100% (2006)	Partially achieved

**Annex Table 10: Summary of Achievements of the CAS Objectives (Pillar III)**

	<u>SL CAS, CASPR 03-07: Pillar III</u> <u>Equity</u>	<u>Actual Results</u> <u>(as of February 2008)</u>	<u>Comments</u>
		- Submitted outcome and output based progress monitoring reports: 0% (2004); 75% (2006) Progress in reducing maternal mortality was associated with a an increase in public health per capita expenditures from \$13.7 in 2002 to \$17.4 in 2006 rather than to improvements in health service delivery efficiency	
	<u>4. Curb spread of HIV infection</u>		Not achieved
	<u>Keep prevalence rate of HIV low by increasing awareness</u>		Partially achieved
	HIV prevalence among women aged 15-24 remains below 1% (<1% in 2002)	<0.9% (2004); <1% (2007) (Number of new cases of HIV in young adults aged 15-24: 50 in 2002; 91 in 2004) HIV awareness and knowledge levels in underserved communities remain drastically low, and Bank project assistance on this has stalled. For example, only 40 percent of women working in rural tea estates, for example, have even heard of HIV/AIDS as compared to 90 percent of women in other rural and urban areas.	Partially achieved
	HIV prevalence among STD clinic population stays below 5%	Not reported.	Not achieved*
	<u>5. Improve access to services in poor districts</u>		Partially achieved
	Number of empowered communities implementing sub-projects contained in their development plans expanded	Selected Bank community-driven development projects have reached nearly 1,000 villages.	Achieved.
	Poverty incidence in participating villages by district Galle: 26 (2002) Matara: 27 (2002) Mon'gala: 37 (2002) Badulla: 37 (2002) Ratnapura: 34 (2002) Hambantota: 32 (2002) Polonnaruwa: 24 (2002) Matale: 30 (2002) Nuwara Eliya: 23 (2002) NATIONAL: 22.7 (2002)	No information reported on poverty incidence by districts available since 2002	Not achieved *
<u>Ongoing</u> <u>pre-CAS 03-07</u> <u>IDA Support</u>	<u>2. Improve the quality of basic education system</u>		
	Second General Education Project	Approved FY98. Closed 11/05	IEG outcome: Satisfactory

\* In cases where results are not reported, IEG takes this lack of evidence as the equivalent of "not achieved."



**Annex Table 10: Summary of Achievements of the CAS Objectives (Pillar III)**

	<b>SL CAS, CASPR 03-07: Pillar III Equity</b>	<b>Actual Results (as of February 2008)</b>	<b>Comments</b>
<b><u>New IDA Lending Support</u></b>	<b>1. Improve overall equity in the country</b>		
	PRSC II	Dropped	
	<b>2. Improve the quality of basic education system</b>		
	Improving Relevance & Quality of Undergraduate Education	Approved FY03. Active	Latest PDO rating: Satisfactory (12/03/2007)
	Education Sector Development Project	Approved FY06. Active	Latest PDO rating: Satisfactory (11/28/2007)
	<b>3. Improve health status of the population</b>		
	Health Sector Development	Approved FY04. Active	Latest PDO rating: Moderately satisfactory (11/02/2007)
	<b>4. Curb spread of HIV infection</b>		
	National HIV/AIDS Prevention	Approved FY03. Active	Latest PDO rating: Moderately unsatisfactory (03/29/2008)
	Health Sector Development	Approved FY04. Active	Latest PDO rating: Moderately satisfactory (11/02/2007)
	<b>5. Improve access to services in poor districts</b>		
	Second Community Water Supply and Sanitation	Approved FY03. Active	Latest PDO rating: Satisfactory (11/29/2007)
<b><u>Planned AAA and TA</u></b>	Community Development and Livelihood Improvement "Gemi Diriya" Project	Approved FY04. Active	Latest PDO rating: Satisfactory (12/19/2007)
	Gemi Diriya II (Estates)	Slipped to FY09	
	<b>1. Improve overall equity in the country</b>		
	Poverty Assessment	Delivered FY06	
	Poverty Mapping	Delivered FY05	
	Tea and Rubber Estate Study	Delivered FY07	
	<b>2. Improve the quality of basic education system</b>		
	AAA on General Education	Delivered FY04	
	Report on Millennium Development Goals (MDGs)	Delivered FY05	
	<b>3. Improve health status of the population</b>		
	Health Sector Strategy	Dropped	
	<b>5. Improve access to services in poor districts</b>		
<b><u>Additional AAA</u></b>	Decentralization and delivery of services	Delivered FY06	
	<b>1. Improve overall equity in the country</b>		
	Poverty and Social Impact Analysis (PSIA)	Delivered FY06	
	TA for Implementation of Welfare Reform	Delivered FY07	
	<b>3. Improve health status of the population</b>		
	Poverty and Social Impact Analysis (PSIA)	Delivered FY06	

\* In cases where results are not reported, IEG takes this lack of evidence as the equivalent to "not achieved."

**Annex Table 10: Summary of Achievements of the CAS Objectives (Pillar IV)**

<b>SL CAS, CASPR 03-07: Pillar IV Tsunami</b>		<b>Actual Results (as of February 2008)</b>	<b>Comments</b>
<b>Objectives</b>	1. Restore livelihoods destroyed by the tsunami and start the recovery and reconstruction process	<b>PARTIALLY ACHIEVED</b>	Financial resources were quickly mobilized to finance tsunami reconstruction efforts. Some 39,000 houses were rebuilt or repaired and more than 100,000 families received livelihood grants. Assistance was predominantly distributed in the South, compared to the adversely affected parts of the North and East.
<b>Major Outcome Measures</b>	1. Restore livelihoods destroyed by the tsunami and start the recovery and reconstruction process		Partially achieved
	Restored housing of the poorest households in affected districts		Partially achieved
	Number of totally damaged houses repaired (64,525 fully destroyed houses)	Approximately 80% of totally damaged houses repaired, including 15,600 (IDA financed) or 97% of the reconstruction target. Damaged houses in the north and east still to be repaired.	Partially achieved
	Number of partially damaged houses repaired (29,687 partially destroyed houses)	Approximately 80% of damaged houses have been repaired including 23,500 financed by IDA (62% of target) Partially damaged houses in the North and East are still to be repaired.	Partially achieved
	Livelihoods of the tsunami-affected families rebuilt to help revive the local economies of the affected districts	More than 80 percent of self-employed regained employment with a year and a half after the tsunami. The 114km of road section between Galle and Colombo has been rehabilitated. Livelihoods of adversely affected families in the North and East compromised by the resumption of the conflict.	Partially achieved.
	Share of deserving families reached through cash grants	The livelihood support component was successfully concluded in 2005 95.2% (2005) 100,000 families assisted. Families in the North and East not reached through the cash grants programs.	Partially achieved
	Percent disbursed of financing required for cash for work programs	41% (2005), 100% (2006)	Achieved
<b>Ongoing pre-CAS 03-07 IDA Support</b>			
<b>New IDA Lending Support</b>	1. Restore livelihoods destroyed by the tsunami and start the recovery and reconstruction process		
	Tsunami Emergency Recovery Project – Phase I (Component Z)	Approved FY05. Closed 03/07	N.A.
	Tsunami Emergency Recovery Project – Phase II	Approved FY05. Active	Latest PDO rating: Satisfactory (12/20/2007)
<b>Planned AAA and TA</b>			
<b>Additional AAA</b>	1. Restore livelihoods destroyed by the tsunami and start the recovery and reconstruction process		
	SL - Tsunami Damage & Needs Assessment	Delivered FY05	
	Sri Lanka Development Forum Paper	Delivered FY05	

\* In cases where results are not reported, IEG takes this lack of evidence as the equivalent to "not achieved."

<b>1. CAS Data</b>	
<b>Country:</b> Sri Lanka	
<b>CAS Year:</b> 2003 (CAS); 2006 (CASPR)	<b>CAS Period:</b> 2003-2006
<b>CASCR Review Period:</b> FY03-07	<b>Date of This Review:</b> April 9, 2008
<b>IEG-IFC CASCR Reviewer:</b> Asita De Silva	
<b>2. Assessment of the CASCR's Coverage of IFC Activities</b>	
<p>The CASCR contains a brief review of IFC's experience in Sri Lanka over the CAS period and identifies IFC's investment and advisory services operations during the period. It attributes IFC's limited role in the country to "the escalating conflict and a lack of bankable projects of sufficient scale." The CASCR would have benefited from a more insightful discussion as to the main obstacles, both internal and external, encountered in developing investment projects, as well as the reasons for lack of advisory service activity between 2003-2006.</p>	
<b>3. IFC Objectives over the CASCR Period</b>	
<p>IFC's objective in Sri Lanka over the last CAS period was to support the FY03 CAS pillar to foster growth and private sector participation in the economy. It aimed to help (i) develop financial markets by increasing the availability of financing for SMEs, expanding housing finance, adding value to the on-going consolidation of financial services, and supporting growth of privately-managed contractual savings institutions; (ii) expand the private provision of infrastructure services, especially in power, ports, water and telecommunications; (iii) support growth of export-oriented manufacturing and service companies, including IT companies; (iv) support privatization; and (v) support the growth of SMEs in conjunction with multilateral and bilateral partners. The FY06 CAS Progress Report (CASPR) reiterated these same objectives, with the exception of supporting privatization and added a further area of focus: (vi) encouraging the regional expansion of Sri Lankan companies' operations.</p> <p>The FY06 CASPR also identified three scenarios, which would determine the extent of the WBG's activity in the country. For IFC, the implications of each scenario were: (i) Scenario One - the base "muddling through" case: Investment opportunities were expected to be limited and IFC would focus on supporting SMEs through the South Asia Enterprise Development Facility (SEDF), while continuing to look for investment opportunities in manufacturing, including support to companies embarking on regional expansion programs; (ii) Scenario Two - the high "moving forward" case: New investment opportunities were expected to open up across a wide range of sectors, especially in public-private partnerships (PPPs) in infrastructure. IFC would also continue its support for SMEs through the SEDF; (iii) Scenario Three - the low "drifting back" case: In a worsening environment, IFC was expected to confine its activities to advisory services, particularly through SEDF. As discussed below, Scenario Three - the low "drifting back" case prevailed in the country since 2004.</p>	
<b>4. Relevance of IFC Objectives</b>	
<p>As with the World Bank's assistance program established in the FY03 CAS, IFC's objectives also reflected the optimism that prevailed in the wake of the 2002 peace agreement. This optimism proved short-lived, however, and both the security situation and macro-economic environment deteriorated after 2004. In this context, the objectives established in the FY03 CAS were overly ambitious. The FY06 CASPR acknowledged this and appropriately modified IFC's objectives based on the three possible scenarios noted above. The focus areas IFC identified remain relevant to Sri Lanka's development priorities. The financial sector continues to be dominated by two large state-owned banks and further development of a competitive private financial sector remains key to improving access to finance in the country. As acknowledged in the government's strategy documents, lack of infrastructure, particular outside Colombo, remains a critical constraint to greater and more regionally balanced growth and development. Given major capacity constraints to implementing large infrastructure projects in the public sector, an important need remains for a greater private sector role</p>	

in infrastructure development. Export-oriented manufacturing has been the key engine of growth in Sri Lanka over the past decade, and given a decline in the garments industry further development of new areas such as IT are critical to sustaining growth and creating employment opportunities. With the continuing uncertain security and economic environment in Sri Lanka, support for Sri Lankan companies seeking to diversify their operations through overseas expansion is also a fully appropriate objective.

## **5. IFC Activities During Period under Review**

### **Investment Operations**

IFC made three investments in Sri Lanka between FY03-07 for US\$37 million.<sup>1</sup> These included (i) an investment in the leading mobile telephone service provider in the country to help it expand and upgrade its network to support the company's growth objectives and relieve network congestion; (ii) three equity investments in the largest private commercial bank in Sri Lanka; and (iii) a recent GTFP trade facility for two private commercial banks. All three operations are performing successfully to date.

These investments were consistent with the objectives established in the FY03 CAS, but were considerably narrower than the broad range of potential investments elucidated in the CAS. IFC was not able to realize any investments in the infrastructure sectors beyond telecom or any export-oriented manufacturing, service, or IT investments. To a large extent, IFC activities were hindered by deterioration of the security situation and an unstable macroeconomic environment. As discussed in the IEG-WB review above, the government loosened its fiscal and monetary policies, creating a high inflation environment and the WB was unable to support significant progress on the reform agenda. In particular, the government's reform program to further improve the environment for the private sector, including through more privatizations stalled. The program had been intended to be supported by a series of 4 WB PRSC operations, of which only the first one took place. Investments in infrastructure projects with private participation during the CAS period dropped from an average US\$302 million a year in 1996-2002 to US\$32 million a year in 2003-06.

At the same time, however, Sri Lanka has a relatively well-established and resilient private sector that has steadily grown and diversified, despite the persistence of the civil conflict over the last 25 years. Albeit partly fueled by expansionary monetary and fiscal policies (as discussed in the IEG-WB review), the manufacturing sector grew by 4.6% between 2002 and 2006 and private investment rose from 16.8 percent of GDP in 2003 to 23.4% in 2006 (World Bank). In this respect, despite the security situation in the north of the country and the high inflation environment, it is unfortunate that IFC could not generate more investment transactions during the CAS period. In a difficult setting, a strong on-the-ground IFC team is needed to identify opportunities and assist entrepreneurs develop viable, bankable projects. During the CAS period, IFC strengthened its country team, and deepened its understanding of the complex and challenging country context and as a result, the current pipeline of projects is strong.

### **List of IFC investments in Sri Lanka FY03-07**

<i>ID</i>	<i>Name</i>	<i>FY</i>	<i>US\$ (000)</i>	<i>Type</i>	<i>Sector</i>
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<sup>1</sup> While the investment in the telephone company was originally approved for US\$50 million, only US\$15 million was eventually disbursed.

011707	Commercial Bank of Ceylon (CBC) (including 2 rights issues)	2003	20,272	Equity	Commercial Banking - General
011730	Dialog	2003	15,000	Loan	Mobile Telephony
025639	GTFP NTB/NDB	2007	1,960	Loan	Commercial Banking - Trade

### Advisory Services

Between FY03-06, IFC did not undertake significant AS work. Just two AS operations were initiated during this period: a post-tsunami water purification project and a FIAS competition policy review. Only after establishment of a South Asia Enterprise Development Facility in 2006, was significant further AS work undertaken. These included 6 operations approved in FY07 that addressed capacity building in the banking sector; tourism development; IT sector development; and business registration and licensing processes in Colombo.

Through the FY05 post-tsunami water project, IFC supported a US company's efforts to install water purification and disinfection systems in tsunami-affected areas of eastern Sri Lanka. By 2007, 44 units had been installed, providing some 300 million liters of clean water a year and reaching some 77,000 people (against targets of 50 units and 100,000 people). The project saw considerable delays in implementation, however, due to increased instability in the eastern region as well as wavering government commitment to the project. Under the SEDF program established in 2006, IFC prepared value chain analyses in the business/knowledge process outsourcing and tourism sectors, which helped IFC establish a strategy in the IT sector and develop several advisory projects. Among these was an FY07 project to help develop linkages between a large eco-tourism project and SME suppliers in surrounding areas. The project has been delayed, however, due to stoppage of construction on the Eco Lodge due to protests that construction would harm the surrounding rainforest. Another FY07 SEDF project helped local SME hotel operators better market their product internationally by linking them with a global hotel e-marketplace. Over 100 SME hotel providers have registered to date. A further FY07 SEDF project provided several local banks with assistance in improving their provision of financial services to SMEs, including through organization of an SME banking "roadshow" in 2007. A FY07 Business Enabling Environment project intended to help reduce the number of steps and costs involved in registering a business and obtaining licenses in Colombo, but project implementation has been ineffective to date due to administrative changes in the Colombo Municipal Council.

## 6. IFC Contribution to CAS objectives

**Overall.** In the context of a deteriorating overall environment, IFC made a positive, but very limited contribution to the CAS goal of stimulating further growth in the private sector during the CAS period through three investments and a limited number of advisory services operations. In particular:

**Financial markets.** Through its investment in the largest private commercial bank in Sri Lanka, (through an equity investment and two subsequent rights issues), IFC helped the bank expand its reach to the retail and SME markets, as well as establish best-in-class management and governance practices. Through representation on the board of directors as well as through advisory services to the bank's portfolio teams, IFC helped introduce practices such as rotation of auditors, helped establish value added technical assistance services for SME clients, and supported the bank's expansion into other countries in the region. Contrary to intentions stated in the FY03 CAS, however, IFC was not able to realize any investments in housing finance or support the growth of contractual savings institutions. Although partly fueled by expansionary monetary policies, the banking sector saw significant growth over the CAS period, with private sector credit rising from 29.5 percent of GDP in 2003 to 34.5 percent in 2006. The gross non-performing loan ratio in the banking sector also decreased substantially from 12.3 percent in 2003 to 5.7 percent in 2006. However, with real interest

rates very low or negative, credit growth has outpaced deposit growth, creating risks to stability in the banking system (IMF).

**Private provision of infrastructure services.** IFC's invested in the leading mobile telephone company in the country, which expanded and upgraded its GSM network, particularly outside Colombo. At the time IFC made its investment in 2003, Sri Lanka's mobile phone penetration was only 4%, with the company having about 52 percent of the market share. By 2007, mobile penetration had increased to 27 percent, with the company's market share increasing to 60 percent. With no other investments, however, IFC did not make a contribution in any of the other potential infrastructure areas that it had identified in the CAS, such as power, ports, and water.

**Growth of export-oriented manufacturing and service companies.** IFC was not able to realize any investments in the manufacturing or service sectors during the CAS period and did not contribute to this objective. It did, however, set the stage for potential future contributions by financing a value chain analyses in the business/knowledge process outsourcing sector and developing a strategy to support the IT sector.

**Privatization.** IFC did not contribute to this objective. Progress on the privatization agenda stalled during the CAS period. Although the WB intended to support the privatization program through a series of three additional PRSCs, these did not take place.

**Growth of small and medium enterprises (SMEs).** IFC made a contribution to this broad objective by assisting the leading private sector commercial bank in Sri Lanka expand its services to SMEs.

**Tourism.** An IFC AS operation helped connect SME hotel operators with an international e-market place. However, tourism has been the hardest hit sector in the prevailing security environment and contracted by 40 percent during the course of the CAS period.

## **7. Lessons and Challenges from Experience**

- The CASCR draws a "key lesson" on the value of IFC's advisory services. Between FY03-06, IFC did not have an advisory services program in place in Sri Lanka and only after establishment of SEDF in 2006 did it undertake significant AS work. It was found that AS and investment operations "are very complementary, both in terms of improving potential client relationships and business development work, but also in terms of developmental impact from investments." IEG agrees that this is an important and relevant lesson.
- IEG also draws the following lesson: In a difficult setting, a strong on-the-ground IFC team is needed to identify opportunities and assist entrepreneurs develop viable, bankable projects. During the CAS period, IFC strengthened its country team, and deepened its understanding of the complex and challenging country context and as a result, the current pipeline of projects is strong.