



1. Project Data:		Date Posted : 09/20/2004	
PROJ ID: P081718		Appraisal	Actual
Project Name: PRSC	Project Costs (US\$M)	125	125
Country: Sri Lanka	Loan/Credit (US\$M)	125	125
Sector(s): Board: PO - General agriculture fishing and forestry sector (20%), Central government administration (20%), General finance sector (20%), Other social services (20%), General industry and trade sector (20%)	Cofinancing (US\$M)		
L/C Number: C3785			
	Board Approval (FY)		03
Partners involved :	Closing Date	12/31/2003	12/31/2003

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2. Project Objectives and Components

a. Objectives

1. Accelerate economic growth and support private sector development; and
2. Strengthen governance in the public sector and improve the welfare system .

b. Components

1. Stable macroeconomic framework.
2. For the objective of accelerating growth and supporting private sector development, project components consisted of reforms in : (a) *labor market* to address costly labor regulations; (b) *agricultural land market* to remove restrictions on sale, mortgage, lease and transfer of land permits; (c) *financial sector* to restructure and privatize the two large state-owned banks; and (d) *power sector* to make it efficient, facilitate private sector investment and reduce and eliminate claims on the state budget from energy utilities
3. For the objective of strengthening governance in the public sector and improving the welfare system, the project components consisted of: (a) civil service and administrative reform; (b) public expenditure management and (c) reform of the welfare system by better targeting the Samurdhi transfer scheme .

c. Comments on Project Cost, Financing and Dates

The project cost US\$ 125 million financed by an IDA credit of US\$ 125 million in one tranche. The project was appraised in April, 2003, approved by the Board on June 17, 2003, made effective on June 26, 2003, and closed on schedule on December 31, 2003.

3. Achievement of Relevant Objectives:

1. *Accelerate economic growth and support private sector development* . The economy grew faster in 2003 and the government took steps that should help achieve the medium term objectives of the project . In particular, in (a) *macroeconomic management* the Government enacted the Fiscal Management Responsibly Act which sets medium term limits on the budget deficit (5 percent of GDP) and public debt (85 percent of GDP); (b) *labor market*, reforms were made to: (i) the rules governing the termination of employees under the Workmen act, (ii) the Industrial Disputes Bill (Hearings and Determination of Proceedings); and (iii) the Industrial Disputes Act; and (iv) how the Labor Commissioner set the compensation formula at retrenchment, binding it to a predetermined formula;
- (c) *land market*, the government enacted the Survey Act, appointed the Registrar General Land as the Registrar General of Titles, and announced its decision to convert to full private ownership the restricted land grants under the Land Development Ordinance and the Land Grants Act;
- (d) *financial sector*, the government enacted amendments to the Monetary Law Act, privatized the Sri Lanka

Insurance Corporation, established an insurance regulatory authority and liberalized the sector to reduce constraints on foreign ownership, and initiated the commercialization of the state-owned People's Bank,
 (e) *power sector* the government established a multi-sector regulator, enacted the Electricity Reforms Act which unbundles the Ceylon Electricity Board, and increased electricity tariffs to reflect cost recovery .

2. *Governance in public sector and welfare reform* . The government reduced the fiscal deficit and its domestic financing needs in 2003, and took steps that should help it have better governance and an effective safety net system. Main steps taken are:

(a) on *welfare reform* the government enacted the Welfare Benefits Act to provide an improved legal and institutional framework for reform, and formed a steering committee to oversee implementation, and completed the technical work for introducing a new targeting system for Samurdhi;

(b) on *governance* the government reestablished the independent Public Services Commission to depoliticize the civil service, and introduced strict time limits for the submission of annual accounts and performance reports by the line ministries and the state owned enterprises .

4. Significant Outcomes/Impacts:

GDP growth accelerated from 4 percent to 5.9 percent in 2003, inflation was reduced to 6.3 percent, and unemployment decreased from 8.8 percent in 2002 to 7.8 percent in 2003.

5. Significant Shortcomings (including non-compliance with safeguard policies):

The PRGF program has been suspended because of fiscal imbalances . FDI was only US\$229 million during 2003, below the US\$300 million expected before elections were called .

The anticipate growth of 6 percent in 2004 is unlikely to materialize, a result of the drought but also of the lower investment levels linked to the uncertain political and economic environment .

With elections, political power transferred from the party which proposed reforms supported by the PRSC to a coalition of parties which seem less favorable to reform . The new government appears much more likely to restructure rather than privatize the two large state-owned banks; in the meantime, the financial position of the People's Bank has deteriorated substantially .

The Supreme Court ruled that the land ownership bill, presented to Parliament in November 2003, violates the 13th Amendment of the Constitution, thereby undermining the efforts to remove the restrictions for transactions on land .

6. Ratings:	ICR	OED Review	Reason for Disagreement /Comments
<p>Outcome:</p>	<p>Satisfactory</p>	<p>Moderately Satisfactory</p>	<p>Note: These ratings are based on the Simplified ICR and as such are tentative until a more comprehensive review can be made on the basis of a final ICR to be done at the end of the series of programmatic loans.</p> <p>While the project was approved on the basis of upfront actions which were fully achieved, its outcome rating depends on how well the program achieves its objectives. Although the project achieved a number of its relevant objectives noted in Section 3 above, OED rates the outcome only moderately satisfactory . The fiscal revenue shortfalls in 2003 are of some concern as is the failure of the government to adhere to the deficit ceiling and the related delay in the first review under the IMF PRGF/EFF, as well as the ICR's forecast that the fiscal deficit is expected to widen in 2004 owing to further revenue shortfalls linked to delays in implementing revenue measures .</p> <p>Note also that an Outcome Rating of "Moderately Satisfactory" is not available for the ICR.</p>

Institutional Dev .:	Modest	Modest	
Sustainability :	Likely	Likely	
Bank Performance :	Satisfactory	Satisfactory	
Borrower Perf .:	Satisfactory	Satisfactory	
Quality of ICR :		Satisfactory	

NOTE: ICR rating values flagged with "*" don't comply with OP/BP 13.55, but are listed for completeness.

7. Lessons of Broad Applicability:

1. Programmatic loans should be based on up-front actions, especially in circumstances of political uncertainty as in this case. 2. An effective communications strategy to the general public is essential to gain support for reforms and increase the likelihood that they will be maintained. 3. PRSC operations that neglect fiscal problems tend to produce mediocre results, which calls for linking more future PRSCs with budget plans and outcomes.

8. Assessment Recommended? Yes No

Why? Since only a Simplified ICR is available, and a full ICR will only be available at the end of the series of programmatic adjustment credits, it will be important to implement a PPAR to fully evaluate each of the projects in this series.

9. Comments on Quality of ICR:

The ICR meets the guideline requirements for a Simplified ICR and frankly presents the political difficulties facing continued implementation of the program. The main text could have used the list of actions presented in Annex I to explain better what was achieved under the PRSC I, the problems faced in continuing with a PRSC II, and separate achievements and shortcomings of credit from those of the entire PRS program. As it is, the reader can hardly differentiate achievements of one and other; moreover, section 4 on achievements of objectives and outcomes could be interpreted that the credit had a negligible impact.