



Country Partnership Strategy

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Sri Lanka
2012–2016

Asian Development Bank

CURRENCY EQUIVALENTS

(as of 22 September 2011)

Currency unit	–	Sri Lanka rupee/s (SLRe/SLRs)
SLRe1.00	=	\$0.01
\$1.00	=	SLRs111.13

ABBREVIATIONS

ADB	–	Asian Development Bank
ADF	–	Asian Development Fund
CPS	–	country partnership strategy
DPF	–	development policy framework
GDP	–	gross domestic product
IMF	–	International Monetary Fund
MDG	–	Millennium Development Goal
OCR	–	ordinary capital resources
PPP	–	public–private partnership
TA	–	technical assistance

NOTE

In this report, “\$” refers to US dollars.

Vice-President	X. Zhao, Operations 1
Director General	S.H. Rahman, South Asia Department (SARD)
Country Director	R.A. O'Sullivan, Sri Lanka Resident Mission (SLRM), SARD
Team leader	N. Rao, Lead Economist, SLRM, SARD
Team members	<p>M. Amerasinghe, Senior Project Officer, SLRM, SARD</p> <p>E.P. Araneta, Principal Operations Coordination Specialist, Private Sector Operations Department (PSOD)</p> <p>A. Cauchois, Senior Water Resources Specialist, SARD</p> <p>M. Fan, Urban Development Specialist, SARD</p> <p>N. Gunasekera, Senior Social Development Officer (Gender), SLRM, SARD</p> <p>A. Hussain, Lead Operations Coordination Specialist, SARD</p> <p>S. Jayakody, Senior Economics Assistant, SLRM, SARD</p> <p>M. Khaltarpurev, Procurement Specialist, Central Operations Services Office</p> <p>M. Khamudkhanov, Senior Energy Specialist, SARD</p> <p>T. Koike, Senior Investment Specialist, PSOD</p> <p>D.K. Lee, Senior Transport Specialist, SARD</p> <p>D.C.M. Margonsztern, Urban Development Specialist (Transport), SARD</p> <p>C. McDeigan, Senior Portfolio Management Specialist, SLRM, SARD</p> <p>T. Molligoda, Senior Finance and Administration Officer, SLRM, SARD</p> <p>S. Muthugala, Procurement Officer, SLRM, SARD</p> <p>A. Nanayakkara, Senior Project Officer, SLRM, SARD</p> <p>B. Panth, Principal Social Sector Specialist, SARD</p> <p>N. Saito, Senior Urban Development Specialist, SARD</p> <p>A. Salgado, Portfolio Management Officer, SLRM, SARD</p> <p>V. Samarasekara, Climate Change Specialist, INRM, SARD</p> <p>S. Sen, Principal Private Sector Development Specialist, SARD</p> <p>S. Shah, Senior Financial Sector Specialist, SARD</p> <p>K. Shin, Senior Financial Sector Economist, SARD</p> <p>K.M. Tilakaratne, Senior Project Officer, SLRM, SARD</p> <p>F. Tornieri, Senior Social Development Specialist (Gender and Development), SARD</p> <p>R. Van Dael, Social Sector Specialist, SARD</p> <p>H. Wickremasinghe, Senior Economics Officer, SLRM, SARD</p>
Peer reviewers	<p>S. Jha, Principal Economist, Economics and Research Department</p> <p>R. Loi, Lead Financing Partnerships Specialist, Office of Cofinancing Operations</p> <p>D. McCauley, Lead Climate Change Specialist, Regional and Sustainable Development Department</p> <p>G. Rauniyar, Senior Evaluation Specialist, Independent Evaluation Department</p> <p>C.C. Yu, Principal Results Management Specialist, Strategy and Policy Department</p>

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COUNTRY AT A GLANCE

Economic	2006	2007	2008	2009	2010
GDP (\$ billion, current)	28.3	32.4	40.7	42.0	49.5
GDP per capita (\$, current)	1421.0	1616.7	2014.0	2057.0	2,399.0
GDP growth (% in constant prices)	7.7	6.8	6.0	3.5	8.0
Agriculture	6.3	3.4	7.5	3.2	7.0
Industry	8.1	7.6	5.9	4.2	8.4
Services	7.7	7.1	5.6	3.3	8.0
Gross domestic investment (% of GDP)	28.0	28.0	27.6	24.4	27.8
Gross domestic saving (% of GDP)	17.0	17.6	13.9	17.9	18.7
Consumer price index (annual % change)	10.0	15.8	22.6	3.4	5.9
Liquidity (M2) (annual % change)	17.8	16.6	8.5	18.6	15.8
Overall fiscal surplus (deficit) (% of GDP)	(7.0)	(6.9)	(7.0)	(9.9)	(7.9)
Merchandise trade balance (% of GDP)	(11.9)	(11.3)	(14.7)	(7.4)	(10.5)
Current account balance (% of GDP)	(5.3)	(4.3)	(9.5)	(0.5)	(2.9)
External debt service (% of exports of goods and services)	12.7	13.1	15.1	19.0	15.2
External debt (% of GDP)	49.4	51.0	43.7	49.7	50.1

Poverty and Social	2001	2007	Latest
Population (million)	18.7	20.0	20.7 [2009]
Population growth (annual % change)	1.4	1.1	1.0 [2010]
Maternal mortality ratio (per 100,000 live births)	59.0 [2000]	45.0 [2005]	39.0 [2008]
Infant mortality rate (per 1,000 live births)	...	14.0	13.0 [2009]
Life expectancy at birth (years)	72.0	74.0	74.0 [2009]
Adult literacy (%)	91.0	91.0	91.0 [2008]
Primary school gross enrollment (%)	108.0	105.0	97.0 [2009]
Malnutrition prevalence, height for age (% of children under 5)	...	17.3	19.2 [2009]
Population with access to safe drinking water (%)	...	79.0 [2004]	87.3 [2010]
Improved sanitation facilities (% of population with access)	82.0 [2000]	88.0 [2005]	91.0 [2008]

Environment	2006	Latest
Carbon dioxide emissions (tons)	11.7	12.3 [2007]
Carbon dioxide emissions per capita (tons)	0.6	0.6 [2007]
Forest area (million hectares)	1.9	1.9 [2010]
Urban population (% of total population)	15.0	15.0 [2009]

ADB Portfolio (sovereign loans, as of 31 December 2010)	OCR	ADF	Total
Total number of loans			37
Net loan amount (\$ million, cumulative)			2101.32
Disbursements			
Total funds available for withdrawal (\$ million)	1211.29	1003.77	2215.07
Disbursed amount (\$ million, cumulative)	402.41	691.91	1094.31
Percentage disbursed (disbursed amount/total available)	33.22	68.93	49.40

... = not available, () = negative, [] = latest year for which data are available, ADB = Asian Development Bank, ADF = Asian Development Fund, GDP = gross domestic product, M2 = broad money, OCR = ordinary capital resources.

Sources: Asian Development Bank estimates; Central Bank of Sri Lanka. 2011. *Annual Report 2010*. Colombo; Food and Agriculture Organization of the United Nations. <http://www.fao.org/>; Government of Sri Lanka, Department of Census and Statistics. 2009. *MDG Indicators of Sri Lanka: A Midterm Review, 2008*. Colombo; International Union for Conservation of Nature and Natural Resources. <http://www.iucnredlist.org/>; UNDP. 2010. *Millennium Development Goals Country Report 2008/2009*. <http://www.undp.org> (prepared by the Institute of Policy Studies of Sri Lanka for the National Council for Economic Development); UNICEF; World Bank. World Development Indicators Online. <http://www.worldbank.org/> (accessed June 2011).

I. DEVELOPMENT TRENDS AND ISSUES

A. Country Background

1. With the end of the war and restoration of political and economic stability, Sri Lanka faces good prospects for rapid economic growth and development. The economy grew by 8% in 2010 and is expected to continue growing at about the same rate in the medium term. The International Monetary Fund (IMF) classified Sri Lanka as a middle-income country in 2010. The Government's ten-year development policy framework (DPF), 2007–2016 was updated in 2010 taking into account the changed and more favorable context.

2. Out of nine provinces in the country, the Western Province accounts for 45% of gross domestic product (GDP) while the contribution of five provinces is less than 10% each. Regional disparities are also reflected in sharp differences in per capita incomes across provinces.¹ Regional inequalities are visible in infrastructure development, quality of services, and capacity of institutions. Recognizing this, the government's development strategy places emphasis on equitable access to infrastructure and services for all, to promote inclusive growth.

3. The preliminary results of the household income and expenditure survey 2009/10 show that poverty dropped significantly from 23% in 2002 to 8.9% in 2010.² The rural and estate³ sectors have recorded remarkable reductions in poverty, with rural poverty falling from 15.7% in 2007 to 9.4% in 2010 and estate poverty falling from 32.0% in 2007 to 11.4% in 2010. Urban poverty is estimated at 5.3%. Sri Lanka's Gini coefficient is currently estimated at 0.47, dropping marginally from 0.49 in 2007.

4. While the government has resettled most of the war-affected internally displaced persons, economic prospects in the former conflict areas need to be revived to full potential. Sri Lanka's human development record has been historically high because of universal free education and health services. Sri Lanka is on track to meet most of the key targets of the Millennium Development Goals (MDGs).⁴ Of the 31 indicators, all but six targets are expected to be met.⁵

5. Sri Lanka has achieved gender parity (goal 3 of the MDGs), but gender-stereotyped sociocultural norms and practices, poverty, and the 30-year conflict have resulted in uneven development in women's quality of life. High numbers of war widows and single women with elderly dependents require more economic and psychosocial support. Expanding women's educational and technical training options to improve employment prospects, increasing women's participation in local (2%) and national (4%) governance structures,⁶ responding to the

¹ The per capita income was the highest in Western Province at \$3,981 in 2010 (\$1,491–\$2,231 in the other eight provinces). Western Province's per capita income in 2010 was 1.6 times the national average, while all other provinces had per capita incomes *below* the national average—the lowest being in the Northern and Sabaragamuwa provinces (only 60% of the national average).

² Estimated at the national poverty line of SLRs3,028 per person per month in 2009/10.

³ Communities attached to plantations on area of more than 20 acres and employing more than 10 residential laborers

⁴ Government of Sri Lanka, Department of Census and Statistics. 2009. *MDG Indicators of Sri Lanka: A Midterm Review*, 2008. Colombo.

⁵ The targets that are not likely to be met include increasing the share of national consumption of the poorest quintile, reducing the proportion of population below the minimum level of dietary consumption, increasing the share of women in wage employment in the nonagricultural sector, increasing the proportion of seats held by women in national parliament, and two environmental indicators.

⁶ ADB. 2008. *Country Gender Assessment: Sri Lanka*. Manila.

gender-based needs of an aging population, and addressing the social and economic needs of conflict-affected women are some of the key gender concerns in Sri Lanka.

B. Economic Assessment and Outlook

6. Sri Lanka's economy is expected to show strong growth of about 8% per annum in the medium term. The expected strong performance is underpinned by the end of the conflict, the resulting improvement in business confidence, and sustained growth in the Asia-Pacific region. Sustaining this level of economic growth would require an improved business climate and initiation of sector policy reforms, rapid development of infrastructure, fiscal consolidation, financial sector reforms, and prudent monetary and exchange rate management.

7. Historically, Sri Lanka's inflation has been high, averaging 13.7% during 2005–2008. Inflation fell in 2009 to 3.4% and remained at single-digit levels in 2010. Low inflation enabled the Central Bank of Sri Lanka to relax monetary policy, resulting in lower interest rates, which supported the recovery of domestic economic activity. Sri Lanka's fiscal accounts have been characterized by low revenue collection, high recurrent expenditure exceeding revenue collection, and high fiscal deficits. Sri Lanka aims to reduce the fiscal deficit from 7.9% of GDP in 2010 to 5% by 2013. This would require further reforms for closing loopholes in the tax system, improving efficiency in tax collection, broadening the tax base, and simplifying the tax regime. Expenditure rationalization needs to focus on reducing recurrent expenditure.

8. The debt–GDP ratio is high at about 84%. Since 2009, the foreign non-concessional debt component has increased sharply. With improved investor confidence in the economy, Sri Lanka raised \$1 billion each through international sovereign bond issues in September 2010 and July 2011 with a longer maturity period and at a yield rate substantially lower than the previous two occasions in 2007 and 2009.

9. Sri Lanka's exports are likely to recover fully in 2012 from the downturn in 2009. Rising global prices, especially of food and petroleum, and higher domestic demand will drive up imports. The trade deficit is likely to deteriorate over 2012–2014. Remittances have been resilient and are likely to continue the strong performance and moderate the effects of the rising trade deficit on the current account of the balance of payments. The reserve position is likely to remain strong, supported by reforms initiated under the ongoing IMF standby arrangement.

10. The rate of national savings (24.7% of GDP in 2010) and investment (27.9% of GDP in 2010) needs to increase to achieve the government's development goals. In particular, private investment needs to be scaled up substantially. This would require establishing an efficient system for facilitating business by strengthening institutions, building human resources capacity, and simplifying procedures. Financial sector development is important for achieving macro stability and increasing private savings and investment. Putting in place a sound regulatory framework, strengthening the legal framework, gradual consolidation in the banking sector, and development of the capital market are key elements in financial market development.

11. Sri Lanka was largely insulated from the effects of the 2008–2009 global financial crisis as its financial markets are not integrated with the global market. While risks from slow global recovery does not pose significant risks to the Asian Development Bank's (ADB's) country partnership strategy for Sri Lanka, the rise in international commodity prices and the resulting domestic inflationary pressures pose the risks of cost overruns in development projects, low private sector investment in a high interest rate environment, and pressures on counterpart funds resulting from fiscal tightening.

C. Highlights of Previous ADB Country Strategy

12. **Program overview: Responding to post-conflict needs.** The country partnership strategy (CPS), 2009–2011 was formulated at a time of considerable uncertainty as the internal war was still ongoing.⁷ The CPS time span was therefore relatively short at 3 years. It focused on two pillars identified in the government’s 10-year DPF: (i) strengthening the investment climate, and (ii) achieving socially inclusive development. The two crosscutting themes were (i) governance (including innovative capacity development), and (ii) private sector development through improvement in the investment climate. Under the first pillar, the strategy sought to improve private sector competitiveness and increase incentives for private sector investment by addressing two major bottlenecks—poor infrastructure and a volatile macroeconomic environment. Under the second pillar, the strategy aimed to provide expanded access to high-quality services in water supply, power, and transport; and to improve education in lagging regions.

13. Partnership with the government, development partners, and other stakeholders was a key modality in the effective implementation of the program. ADB maintained a close relationship with the government and the program was suitably altered to meet the urgent post-conflict needs of Northern and Eastern provinces. ADB’s programs were periodically discussed with the development partners. Several joint operations and cofinancing opportunities became feasible as a result of this close interaction.

14. The prolonged war caused major destruction to infrastructure, a majority of the people in the conflict-affected areas lost their livelihood, and a substantial number of people were internally displaced. The government requested ADB to reallocate resources for reconstruction and rehabilitation activities in the war-affected Northern and Eastern provinces. Soon after the war ended in 2009, ADB provided assistance for immediate reconstruction needs of Northern Province for restoring basic infrastructure requirements such as hospitals, schools, administrative buildings, and agriculture and livestock extension facilities. ADB’s 2010 program focused mainly on Northern Province. The Jaffna and Kilinochchi Water Supply and Sanitation Project⁸, Northern Road Connectivity Project, and the Sustainable Power Sector Support Project were either entirely focused on the war-affected regions or had substantial components in these areas. In addition, a \$150 million multisector Conflict-Affected Region Emergency Project was approved for meeting the reconstruction needs. Other interventions included the Fiscal Management Efficiency Project, aimed at more effective and transparent public financial management. The 2011 lending program is more diversified across sectors and regions: Sustainable Power Project, National Highways Sector Project (additional financing), Secondary Towns and Rural Community-Based Water Supply and Sanitation Project, and Lagging Local Authorities Infrastructure Development Project. The lending program over 2009–2011 aggregates to \$1.06 billion, averaging \$353 million per annum.

15. The nonlending program is assisting in several key areas, such as strengthening capacity for climate change adaptation, leading to the development of the first National Climate Change Adaptation Strategy, power sector regulation, providing rural households with electric connections, building the capacity of provincial road agencies which has improved project planning, design and supervision capacity, supporting fiscal management efficiency, investment

⁷ ADB. 2008. *Country Partnership Strategy: Sri Lanka, 2009–2011*. Manila.

⁸ Details of these TA projects and loans are in Country and Portfolio Indicators (accessible from the list of linked documents in Appendix 2).

climate improvement, and integrated urban transport development. The nonlending program aggregates to \$19.5 million over the CPS period, or \$6.48 million per annum.

16. **Portfolio performance.** The current portfolio contains 37 loans and six grants. Portfolio performance has improved on a number of indicators. ADB recorded its highest ever disbursements during 2010, exceeding \$300 million. The annual average net transfer of resources during 2009–2010 has improved significantly, recording \$142.5 million compared with \$105.6 million during 2004–2008. Continuous efforts have been made to resolve long-outstanding project implementation issues, resulting in only one project at risk (2.7% of the portfolio) at the end of 2010 compared with 4.9% at the end of 2008.

17. **Lessons.** The country partnership strategy final review, 2009–2011 was validated by the Independent Evaluation Department. The validation report⁹ concurred with the *successful* rating of the overall country program. The report noted that ADB's country program was *satisfactory* in strategic positioning, and it was *effective* in delivering the intended outputs and outcomes. The program was, however, *less efficient* and *less likely* sustainable. The report also observed that CPS interventions adapted well in the postwar phase and were aligned with the country's and ADB priorities. Sector selectivity was appropriate and helped to contribute to urgent development priorities. The report also acknowledges the key role played by the resident mission in projecting ADB's image and its lead role in key sectors of comparative advantage.

18. The validation report concurred with the key lessons noted in the final review: (i) government ownership to facilitate sector reforms in a sequenced manner; (ii) reliable funding for maintenance of infrastructure projects; (iii) partnerships with the government and development partners as key to effective implementation; and (iv) recognizing institutional capacity limitations. In addition, the report noted some further lessons: (i) policy dialogue should be conducted in a phased manner with broad stakeholder consultation; (ii) capacity building requires more focused intervention, better preparatory work for technical assistance (TA), and stakeholder consultation; and (iii) for ensuring sustainability, policy-level commitment for enhanced funding is required.

19. To improve the overall program effectiveness, efficiency, and sustainability, the validation report recommends the following: (i) pursue policy dialogue and reforms through a detailed pragmatic, consensus-driven approach, involving rigor, candidness, and transparency; (ii) continue the focus on conflict-affected areas and strive to improve the quality of life by empowering local bodies through decentralization; (iii) encourage public–private partnerships in infrastructure development and education by creating an incentive structure and an enabling environment; (iv) engage the major stakeholders and beneficiaries in capacity building initiatives; (v) give more emphasis to secondary and technical and vocational education; (vi) provide more effective technical support for managing for development results across government ministries; and (vii) ensure cost recovery mechanisms are in place, backed by political commitment. These lessons and recommendations will be built into program formulation and implementation.

⁹ ADB. 2011. Sri Lanka: Country Partnership Strategy, 2009–2011 Final Review Validation. Manila

II. THE COUNTRY STRATEGY

A. Government National Strategy

20. The end of the 26-year internal war in May 2009 was a defining moment for Sri Lanka. The war took a heavy toll on the economy and the social fabric of the country. With the return of peace and the gradual normalization of economic and social activities in the north and east of the country, economic prospects have improved considerably. The government's DPF aims to accelerate economic growth, improve social indicators, eradicate hard-core poverty, and improve the environment.¹⁰ The DPF thus aims for socially inclusive and environmentally sustainable economic growth. The private sector will play a central role, with private investment expected to increase from the current level of 21% of GDP to 26% of GDP by 2016 (i.e., all the incremental investment will come from the private sector). Public investment will remain constant at about 6%–7% of GDP. The DPF also envisages doubling foreign direct investment to 3% of GDP.

21. The DPF identifies inadequate and poor quality of infrastructure as a major constraint to sustaining rapid economic growth. Large infrastructure projects are therefore planned in transport, energy, water, sanitation, and irrigation. Since the government will not be able to finance all these investments, the DPF recommends private finance through public–private partnerships (PPPs) for investments that yield adequate returns over time. Private investments can be potentially viable in power, ports, telecommunications, public transport, and waste disposal. For these investments to materialize, the DPF envisages the adoption of a rational pricing mechanism and better financial and managerial discipline. Reforms will be introduced for reducing transmission losses and granting greater financial and managerial autonomy to public sector utilities. The DPF identifies a vibrant and well-regulated financial sector as a key catalyst for accelerating economic growth.

22. Regional cooperation will be strengthened as these arrangements are beneficial for Sri Lanka's exports, investment opportunities, and acquisition of technology. This has particularly been the case under existing free trade agreements with India and Pakistan, and other regional trade agreements (such as the Asia-Pacific Trade Agreement, the Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation, and the South Asian Free Trade Area) in which Sri Lanka actively participates.

B. ADB Country Strategy

23. The goals and objectives of the government's DPF and ADB's Strategy 2020 are very similar.¹¹ The proposed CPS builds on the priorities of government's DPF and ADB's Strategy 2020 and refines the focus of the CPS 2009–2011. The strategy has been developed in consultation with key development partners and complements their programs. The strategy aims to assist the government in addressing the major constraints for sustaining inclusive growth in post war Sri Lanka.

¹⁰ Department of National Planning, Ministry of Finance and Planning. 2010. *Sri Lanka, The Emerging Wonder of Asia: Mahinda Chintana—Vision for the Future*. Colombo. The government envisages that by 2016 hard-core poverty and hunger will be eradicated, secondary education will be universalized, and the malnutrition rate of children will be reduced from 33% to 12%–15%. The government aims to protect the environment by increasing forest coverage from 23% to 28%.

¹¹ Footnote 10 and ADB. 2008. *Strategy 2020: The Long-Term Strategic Framework of the Asian Development Bank, 2008–2020*. Manila.

24. The CPS 2012–2016 will focus on three pillars: (i) inclusive and sustainable economic growth, (ii) catalyzing private investment and enhancing the effectiveness of public investment, and (iii) human resource and knowledge development. Given the relatively small resource envelope, ADB's interventions will be strategically focused on a few sectors. Recognizing the magnitude of the needs in the former conflict areas, ADB will remain flexible to support critical interventions in these regions depending on the emerging needs. ADB's operations will also attempt to leverage its resources to attract private capital and will work with bilateral and multilateral development partners to improve coordination of the overall assistance package and to improve development effectiveness. The crosscutting themes of the strategy are also in line with the government's priorities and include the environment and climate change, gender, governance, and regional cooperation. To the extent feasible, all ADB interventions will attempt to incorporate components of crosscutting themes. The major departure of the proposed CPS from the earlier one is that there is greater certainty of the government's development goals and the modalities for achieving them in the postwar period. The government is also clearer on the gaps in infrastructure, especially in the lagging regions. A critical role has been assigned to the private sector, and skills development has been assigned high priority. This sharpens the focus of the CPS in addressing the critical development constraints facing the country.

1. Inclusive and Sustainable Economic Growth

25. ADB will support infrastructure development that improves connectivity and service delivery to lagging regions including the former conflict-affected regions of the country. These interventions will reduce regional disparities and expand employment opportunities, thereby promoting inclusive growth. ADB will also support nationally important strategic projects to promote long-term sustainable growth. The government's DPF identifies that substantial infrastructure investments are required in the transport, energy, water supply and sanitation, and urban sectors to promote inclusive and sustainable growth. ADB has been helping Sri Lanka in these sectors and has gained considerable experience in the design and implementation of projects. These sectors will be the focus of ADB's assistance.

26. **Transport.** The government's priorities include developing an expressway network with well-connected national and provincial roads, and expansion of the rural roads network that links to the major growth centers. ADB's assistance will focus on key arterial national road links, and improve provincial and rural roads, especially in the lagging areas. ADB will also assist in pursuing a more environmentally sustainable integrated strategy by developing viable multimodal transport systems, including railways and the public transport system. ADB will continue to assist in developing Sri Lanka's ports, which will contribute to regional cooperation, trade, and tourism. ADB will simultaneously enhance its focus on the sustainability of projects in line with the recommendations of the validation report.

27. **Energy.** The government's goal is to provide high-quality and reliable power supply to the entire population by 2012. ADB's assistance will focus on renewable energy development (including wind and other clean energy sources), energy efficiency improvement, the transmission and distribution system, and improving energy access for lagging regions. ADB will work with the government in reducing system losses through improved metering efficiency and better management systems. ADB will help the government in creating an enabling environment for clean power development, particularly through PPPs. ADB will pursue sector reforms, including accelerating ongoing initiatives toward unbundling and greater private sector participation.

28. **Water supply and sanitation.** ADB interventions in water supply and sanitation will focus on improving access to drinking water and sanitation, reducing water pollution, building resilience to climate change impacts, and expanding the coverage of urban sewerage to reduce environmental pollution. ADB will help the government in formulating sector reforms, especially in improving the cost recovery (reducing nonrevenue water supply) and regulatory mechanism, and in introducing innovative financing mechanisms for encouraging private sector involvement.

29. **Urban.** With an average growth of urbanization projected at 3%–4% per annum, the government is aiming to develop a systematic network of interlinked cities and settlements across the country to narrow the existing regional imbalances. ADB will continue to assist in building urban infrastructure and services including low cost housing, and consider embarking on integrated urban renewal initiatives. ADB's assistance will be aligned with the National Policy on Local Government 2009, which aims to strengthen local governance and build their capacities. ADB will explore a range of financing strategies to encourage private sector participation in urban infrastructure and services.

2. Catalyzing Private Investment and Enhancing the Effectiveness of Public Investment

30. The DPF places the private sector at the center of the development thrust. To accelerate the pace of private sector participation, Sri Lanka's financial sector needs to be developed to offer a wider range of financial products and services. ADB will assist in implementing capital market reforms to promote the development of equity and debt markets and induce higher savings and investment.

31. For increasing the effectiveness of public investment and catalyzing private investments, ADB will assist by institutionalizing PPPs through early and sustained engagement in (i) developing a suitable enabling environment for PPPs; (ii) early identification of PPP candidate projects, concept development, and pre-feasibility assessment; and (iii) project structuring by assessing commercial, technical, environmental, and financial viability. ADB will help the government strengthen the policy, legal, and regulatory framework for fostering PPPs, including improving the institutional framework. Constraints in the financial sector limit the potential to secure long-term domestic funding for private sector infrastructure projects. ADB will support stakeholder consultation and create public awareness on the benefits of PPP projects. ADB's involvement in viable PPP infrastructure will provide synergies between the first and second pillar of the CPS. ADB will also provide nonsovereign loans to reforming state-owned enterprises to expose them to alternate sources of finance.

32. ADB will explore cofinancing opportunities in all projects to channel additional resources and achieve greater leverage. Private investments will be catalyzed through cofinancing using ADB's credit enhancement products. These include guarantees for commercial and political risks, and syndication with other private financial entities, with ADB taking on the role of lender on record or guarantor on record. ADB will also explore providing loans in local currency to eliminate the exchange risk and deepening the domestic capital markets by issuing local currency bonds.

3. Human Resource and Knowledge Development

33. Human resources are likely to be a critical constraint as demand grows for an educated and skilled labor force. The government's Education Sector Development Framework and Program aims to increase equitable access to basic and secondary education, improve the

quality of education, and strengthen service delivery. The government emphasizes training of teachers to use modern methodologies and to accelerate skills creation. Curriculums are also being suitably revised, especially at the secondary level. The government is focusing on skills development and aims to double the number of students entering local universities by 2020. ADB will assist to improve the quality of secondary education and to provide equal access to education through the 1,000 school concept island-wide.¹² Quality of education will be improved through teacher training, curriculum development, greater use of information communication technology, and improvement in science and technology facilities. ADB will support the skills development program, with a focus on reducing gender disparities, by expanding and improving the quality of technical and vocational institutes and related infrastructure.

34. ADB will help build government capacity over a wide range of activities that are likely to be critical in the next phase of development. Inadequate capacity and training to implement development projects efficiently, especially government-financed infrastructure projects, is a weakness that needs to be addressed. ADB will work with the government in training executing and implementing agency staff in best practices across sectors and provinces, and assist in building institutional capacity for undertaking policy-oriented work.

35. Sri Lanka needs to reorient its planning and policy framework to suit the requirements of a middle-income country, drawing on the experiences of other Asian countries, and international best practices. Knowledge products and solutions will play a key role. ADB will enhance its assistance by helping the government to address major policy issues and institutional strengthening initiatives. As the economy becomes more integrated with the external economy, key macroeconomic and microeconomic management policy issues will need to be addressed over the CPS period. ADB will assist in enhancing understanding of the policy issues by undertaking joint analytical work, thereby simultaneously enhancing the capacity of local institutions.

4. Crosscutting Themes

36. Environmental sustainability will be improved by strengthening country safeguard systems, and through direct interventions to support climate change adaptation. ADB's planned initiatives of promoting multimodal transport systems will help ease the burden on a congested road network, reducing air pollution and carbon emissions. To address the impacts of climate change, ADB will build on the work completed under the TA for Strengthening Climate Change Adaptation,¹³ including improving the capacity of government institutions.¹⁴ Gender equity will be promoted by designing projects that are gender-inclusive and emphasize gender empowerment, especially in the education, health, water and sanitation, and infrastructure sectors. Improving governance will be a major thrust area during CPS implementation. Governance in public financial management and public procurement will be strengthened by introducing stringent anticorruption measures and mainstreaming accountability and transparency in ADB's operations. ADB will undertake comprehensive stakeholder consultations during project preparation, improve the capacity of the auditor general's office and executing agencies for undertaking financial and performance auditing, establish a formal accountability structural mechanism in project implementation, enhance capacity and transparency in public

¹² The government plans to develop 1,000 secondary schools, located throughout the island, into fully-fledged secondary schools, by upgrading the quality of physical infrastructure, teaching, and learning processes.

¹³ ADB. 2009. SRI: Strengthening Climate Change Adaptation. Manila.

¹⁴ The National Climate Change Adaptation Strategy developed under this TA has identified that Sri Lanka would need about \$430 million to finance adaptation interventions for 2011–2016. ADB will mainstream climate change concerns in proposed loan and TA projects, especially in urban, water, drainage, and sanitation.

procurement, strengthen legal provisions to enhance the role of the private sector, and work closely with the Commission to Investigate Allegations of Bribery and Corruption. Public sector financial management will be further strengthened through interventions that enhance fiscal management efficiency. ADB will also undertake a comprehensive country procurement assessment, especially focusing on enhancing the capacity of small contractors and key agencies to deliver infrastructure projects. Opportunities to foster regional cooperation will be explored in all interventions, especially in the transport and energy sectors, and in climate change initiatives. Regional cooperation activities will be aligned with the regional cooperation strategy for South Asia, and ADB will work with other development partners to explore opportunities for cooperation. Crosscutting themes will be addressed through a combination of lending and nonlending interventions.

III. STRATEGY IMPLEMENTATION

A. Indicative Resource Parameters

37. Over the next 3 years (2012–2014), Sri Lanka's total resource envelope will be about \$900 million, an annual average of about \$300 million (\$100 million from the Asian Development Fund and \$200 million from ordinary capital resources). ADB will attempt to catalyze additional private resources to complement its projects through PPPs and credit enhancement products. The cost-sharing ceilings and parameters will remain the same as under the CPS, 2009–2011 (90% for loans and 85% for TA). Cost-sharing ceilings for individual projects will be determined on a case-by-case basis. ADB will seek cofinancing opportunities from bilateral sources to expand the scope of proposed projects, especially in the urban and education sectors, and in climate change initiatives.

B. Program Overview

38. In the loan program, a substantial portion is expected to be absorbed by the transport, energy, and urban sectors. Most of the Asian Development Fund resources will be directed toward human resource development, water supply and sanitation projects, and in components of other projects in the lagging regions. The TA program will support the same sectors through project preparatory and capacity development TA, and areas such as policy research and knowledge products. ADB's private sector operations will explore potential projects in areas of renewable energy, thermal power, waste to energy, cargo handling and logistics, trade finance, housing, finance, leasing, and telecommunications.

IV. RESULTS MANAGEMENT

A. Monitoring

39. The Foreign Aid and Budget Monitoring Division of the Ministry of Finance and Planning is responsible for monitoring indicators related to attainment of targets. Sri Lanka has developed, with the active support and commitment of the government, target-related indicators in several sectors. The work needs to be refined and expanded. Development of indicators and institutionalizing the results-based approach was supported by ADB through regional TA on Mainstreaming Managing for Development Results.¹⁵

¹⁵ ADB. 2006. REG 6306: Mainstreaming Managing for Development Results (MfDR) in Support of Poverty Reduction in South Asia. Manila

40. The CPS results framework is based on country targets and indicators, which are specified in the DPF and monitored by the Foreign Aid and Budget Monitoring Division. These targets and indicators are included in the sector assessments and will be reflected in project design and monitoring frameworks during processing. Progress toward attaining these targets will be monitored by ADB and the government through regular portfolio reviews during CPS implementation. Increased delegation of responsibility and allocation of resources to the resident mission has resulted in better portfolio performance. ADB will continue to strengthen the resident mission to manage and monitor the portfolio. Development of indicators and strengthening of the monitoring function is a continuous learning and feedback process, which will be supported by ADB. Development effectiveness will be enhanced by conducting more rigorous impact evaluation, developing capacity in implementing agencies, better outcome monitoring, more systematic collection of outcome data, and improving the quality of projects at entry.

B. Risks

41. There are several important risks to the implementation of the CPS: (i) the reform agenda is not adequately elaborated in the government's DPF, (ii) the global economic situation could deteriorate and inadequate fiscal consolidation efforts could disrupt macroeconomic stability, (iii) social harmony could be disrupted as a result of inadequate attention to the needs of the war-affected population, and (iv) measures taken to strengthen public administration and improve institutional capacity could be inadequate.

42. While the government's DPF elaborates the sector investment program required to attain the development goals, it lacks a well-articulated assessment of complementary sector policy reforms. ADB has been involved in policy dialogue with the government in the sectors covered under the CPS. Policy issues will be further discussed and agreed upon with the government during the implementation stage. ADB will also improve the sequencing of the policy reform agenda. Deterioration in the global economic situation is beyond the control of the government, but it could affect the pace of project implementation if counterpart funds are in short supply on account of a widening fiscal deficit. Sri Lanka's management of the impact of the 2008-2009 global economic crisis shows that the government has the capacity to maintain macroeconomic stability. The capacity for undertaking policy changes has been strengthened under the IMF's ongoing standby arrangement. ADB's assistance for fiscal reforms and institutional strengthening has also enhanced the capacity of the government in fiscal management, and this work will continue during the CPS period. Disruption of social harmony resulting from inadequate attention to the requirements of the war-affected people remains a possible risk. The situation has been peaceful since the end of war and there is no evidence currently of the conflict reemerging. The government has successfully resettled most of the internally displaced persons and has allocated a high proportion of public investment for infrastructure development in the conflict-affected regions. Steps are being taken toward political reconciliation. ADB operations will take into account the specific needs of the people in conflict-affected regions, in coordination with other development partners. The capacity of public institutions in undertaking development work and in service delivery is currently weak. ADB will carefully assess institutional capacity in its operations and will take measures to strengthen capacity through judicious use of TA.

COUNTRY PARTNERSHIP STRATEGY RESULTS FRAMEWORK

Country Development Goals			
1. Accelerated economic growth (maintain 8% growth over the medium term) 2. Eradicate hard-core poverty and hunger by 2016 3. Protect the environment (increase forest cover from 23% in 2010 to 28% by 2016)			
Sectors Selected by ADB			
Government Sector Objectives	Sector Outcomes that ADB Contributes to and Indicators	ADB Areas of Intervention	ADB Indicative Resource Allocation in the Next Pipeline and Thematic Priorities
1. Transport (Strategy 2020 Core Area 1: Infrastructure)			
To establish a modern transport system that will enable acceleration of economic growth, with reduced travel time, cost, and improved safety.	Improved nationwide connectivity for the movement of people and goods: (i) The length of priority national highways with international roughness index above 5.5 reduces to 25% in 2016 (2011 baseline: 30%) (ii) Average travel speed on priority national roads increased to 49 kilometers per hour by 2016 (2011 baseline: 40 kilometers per hour)	National and provincial roads; road transport policies and reform	\$393 million from 2012 to 2014, 44% of CPS, of which: ENV = 100% GEN + EGM = 0% PSD = 20% RCI = 20%
2. Energy (Strategy 2020 Core Area 1: Infrastructure)			
Sustainable development of energy resources, conversion facilities, and delivery systems to enable access to and use of energy services by the entire population Safe, reliable delivery of such energy services at a regionally competitive price, through a commercially viable institution subjected to independent regulation	Improved provision of electricity: (i) System supply capacity increased to 3,470 MW by 2012 and 6,367 MW by 2020 (2010 baseline: 2,891 MW) (ii) Electrification ratio increased from 88% (2010) to 100% by 2012	Electrical power transmission; electrical power distribution; energy efficiency; Wind, solar, and hydro power generation	\$170 million from 2012 to 2014, 19% of CPS, of which: ENV = 100% GEN + EGM = 100% PSD = 100% RCI = 0%
3. Water Supply and Other Municipal Infrastructure and Services (Strategy 2020 Core Area 1: Infrastructure)			
Increasing population access to improved water supply facilities with sufficient water supply, and achieve service levels and quality of national standards Increasing access to adequate and improved sanitation facilities, and service levels and quality of (discharge) water to achieve national standards	Total population has improved access to drinking water and sanitation: (i) Safe water coverage: 100% by 2020 (2009 baseline: 85%) (ii) Pipe-borne sewerage coverage: 7.0% by 2020 (2009 baseline: 2.5%)	Drinking water systems; sanitation systems	\$102 million from 2012 to 2014, 11% of CPS, of which: ENV = 100% GEN + EGM = 33.3% PSD = 33.3% RCI = 0%

Sectors Selected by ADB			
Government Sector Objectives	Sector Outcomes that ADB Contributes to and Indicators	ADB Areas of Intervention	ADB Indicative Resource Allocation in the Next Pipeline and Thematic Priorities
4. Education (Strategy 2020 Core Area 5: Education)			
<p>Develop an education system that will provide the competencies and technological skills required for rapid economic and social development</p> <p>All children complete their primary and secondary education successfully</p>	<p>Increased attainment in secondary education</p> <p>(i) Lower secondary enrollment: 100% in 2020 (2010 baseline: 90%)</p> <p>(ii) General certificate of education Ordinary Level pass rate increased to 65% in 2020 (2009 baseline: 52%)</p> <p>(iii) General certificate of education advanced level pass rate increased to 75% in 2020 (2009 baseline: 60%)</p> <p>Priority technical skill requirements for emerging new economic sectors addressed</p> <p>(i) Add 300,000 trained workers suitable for high-end jobs in wide range of skills</p>	<p>School rehabilitation and building; curriculum development; teacher training; vocational training; formal skills development; informal skills and technical training; science development</p>	<p>\$150 million from 2012 to 2014, 17% of CPS, of which:</p> <p>ENV = 0%</p> <p>GEN + EGM = 100%</p> <p>PSD = 25%</p> <p>RCI = 0%</p>
5. Public Sector Management (Other Areas of Operations)			
<p>Equitable development through pro-poor, pro-growth, and pro-regional public spending</p>	<p>Greater sustainability of public investments through more effective public resource management</p> <p>(i) Increase in gross investment to GDP ratio to 34.0% by 2014 (2010 baseline: 27.8%)</p> <p>(ii) Increase private sector investments to 27.0% by 2014 (2010 baseline: 21.6%)</p> <p>(iii) Year-on-year decrease in total outstanding public debt stock to GDP ratio to 67.0% by 2014 (2010 baseline: 81.9%)</p>	<p>Public expenditure and fiscal management; revenue mobilization; accounting and auditing; civil service reforms and management; corporate governance</p>	<p>\$45 million from 2012 to 2014, 5% of CPS, of which:</p> <p>ENV = 0%</p> <p>GEN + EGM = 0%</p> <p>PSD = 0%</p> <p>RCI = 0%</p>

ADB = Asian Development Bank, CPS = country partnership strategy, EGM = effective gender mainstreaming, ENV = environmental sustainability, GDP = gross domestic product, GEN = gender equity, MW = megawatt, PSD = private sector development, RCI = regional cooperation and integration.

Source: ADB estimates.

LIST OF LINKED DOCUMENTS

<http://www.adb.org/Documents/CPS/?id=SRI-2012>

1. Economic Analysis (Summary)
2. Poverty Analysis (Summary)
3. Gender Analysis (Summary)
4. Environment Assessment
5. Private Sector Assessment (Summary)
6. Sector Assessment: Transport
7. Sector Assessment: Energy
8. Sector Assessment: Water Supply and Other Municipal Infrastructure and Services
9. Sector Assessment: Education
10. Sector Assessment: Public Resource Management
11. Risk Assessment and Risk Management Plan (Summary)
12. Country and Portfolio Indicators
13. Country Performance Assessment Ratings
14. Country Cost-Sharing Arrangements and Eligible Expenditure Financing Parameters
15. Country Partnership Strategy Formulation
16. Country Partnership Strategy Final Review
17. Country Operations Business Plan
18. Country Partnership Strategy Final Review Validation

Supplementary Documents

19. Government of Sri Lanka Development Policy Framework, 2010–2016
20. Asian Development Outlook 2011: Sri Lanka
21. Country Gender Assessment: Sri Lanka, 2008
22. Governance and Public Management: Sri Lanka, 2011
23. Country Poverty Assessment: Sri Lanka, 2011
24. List of Knowledge Management Products, 2010–2014