

Sri Lanka

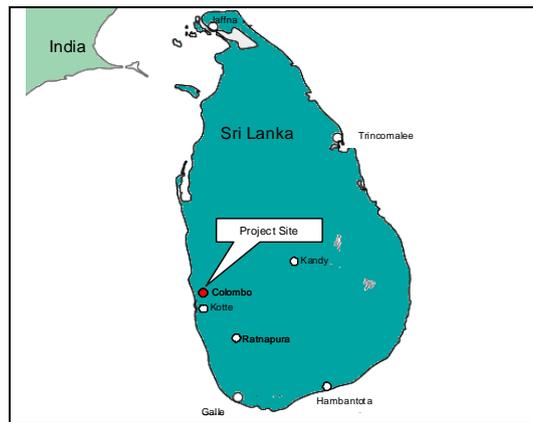
Ex-Post Evaluation of Japanese ODA Loan Project
“Power Sector Restructuring Program”

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Field Survey: October 2008

1. Project Profile and Japan’s ODA Loan



Location of the project site

1.1 Background

In Sri Lanka, electricity demand grew at a rate of 8% per annum on average in the 1990s. The government of Sri Lanka promoted the development of electric power resources, with focus on hydroelectric power, to deal with such expanding demand. As a result, the electricity output structurally depends heavily upon rainfall, and it has been recognized that focus needs to be shifted to the development of thermoelectric power in the future. However, delay in the development of power resources had posed a very serious problem. At the same time, investment has been directed primarily to power generation facilities, which has slowed down the development of power transmission systems. That is, the country is faced with problems such as inadequate capacity of power transmission systems, large transmission losses, and dwindling reliability of power supply.

In Sri Lanka, the Ceylon Electricity Board (CEB) under the jurisdiction of the Ministry of Electric Power has assumed sole responsibility for power generation, transmission, and distribution operations in the power sector as a vertically integrated public corporation for electricity. However, the government of Sri Lanka announced in the “Government’s Policy Principle for the Power Sector” that it would separate the three operations, power generation, power transmission, and power distribution, carried out by the CEB from the standpoints of

enhancing the efficiency and strengthening the finance and management of the whole power sector. The government was working out a detailed plan up to the time of appraisal under the aegis of the World Bank (WB) and the Asian Development Bank (ADB).

Since 1993, the power rate has been revised step by step with the policy advice of the ADB, whereby the profits of the CEB have grown satisfactorily. However, due to an increased volume of emergency purchase of electricity to address the problem of drought and a hike in fuel costs during the period from 1999 to 2000, the finances of the CEB worsened drastically. That is, it slipped into the red in October 2000 and the return on asset dropped to -2.28% at the end of 2000 from 3.0% at the end of 1998.

1.2 Objective

The objectives of this project are, through extending assistance to power sector reforms carried out by the government of Sri Lanka, to enhance the efficiency of the power sector by promoting competition and commercialization, to introduce a transparent and independent mechanism to set a power rate that reflects costs, to invite private funds by developing a transparent management environment, and to recover the sound finances of the CEB that will be instrumental in the stabilization of the macro-economy, and thereby contribute to a stable supply of high-quality electricity at reasonable prices for a long period of time.

1.3 Borrower/Executing Agency

Borrower: Government of the Democratic Socialist Republic of Sri Lanka

Executing agency: Ministry of Finance, Government of Sri Lanka

1.4 Outline of Loan Agreement

Approved Amount/ Disbursed Amount	7,440 million yen / 3,720 million yen
End Notes Exchange Notes/ Loan Agreement Signing Date	March 2003 / March 2003
Terms and Conditions	Interest rate: 2.2% Repayment period: 30 years (Grace period: 10 years) Procurement: General untied
Final Disbursement Date	January, 2006
Main Contractor (Over 1 billion yen)	None
Main Consultant (Over 100 million yen)	None
Feasibility Studies, etc.	None

2. Evaluation Result

2.1 Relevance

This project has been highly relevant with Sri Lanka's national policies and development needs at the times of both appraisal and ex-post evaluation.

2.1.1 Relevance at Appraisal

The government of Sri Lanka formulated the "Government's Policy Principle for the Power Sector" in 1997 and had been promoting reforms in the power sector. In the Policy Principle, the government clearly stated that power resources would be developed by inviting private investments and that the three operations, i.e., power generation, transmission, and distribution, which were under the control of CEB, would be separated.

The objectives (i.e., outcomes) of this project are "to enhance the efficiency of the power sector by promoting competition and commercialization," "to introduce a transparent and independent mechanism to set a power rate that reflects costs," "to invite private funds by developing a transparent management environment," and "to recover the sound finances of the CEB that will be instrumental in stabilizing the macro-economy." In particular, to "enhance the efficiency of the power sector by promoting competition and commercialization" is nothing but the "separation of the operations of power generation, transmission, and distribution of the CEB" as stated in the "Government's Policy Principle for the Power Sector."¹ Likewise, "to

¹ The project appraisal documents did not indicate whether or not such separation of the CEB's operations of power generation, transmission and distribution, that is, so-called "unbundling," was the best approach under the national circumstances of Sri Lanka. At the same time, they neither fully analyzed nor explained what effects could be perceived. However, according to the appraisal report of the ADB that provided a syndicated loan simultaneously

invite private funds by developing a transparent management environment” in fact embodies the development of power resources through inviting private investors as stated in the Policy Principle.

The other two objectives (outcomes) are also well grounded as discussed below. Thus, we believe that the relevance of such objectives was high.

- “To introduce a transparent and independent mechanism to set a power rate that reflects costs”: It was obvious that the power generation, transmission, and distribution costs had not been reflected in the power rate. Hence, there was a strong need to improve the mechanism for setting the power rate.
- “To recover the sound finances of the CEB that will be instrumental in the stabilization of the macro-economy”: As discussed in section “1.1 Background,” since 2000, the finances of the CEB have taken a drastic downward turn. It was indeed important from the perspective of appropriate distribution of resources to restructure the overblown public sector, particularly the power sector that had a fragile financial structure, and establish a transparent and efficient sector. On the other hand, it was difficult to allocate funds to the reforms from domestic funds in the light of fragile primary balance.

2.1.2 Relevance at Ex-post Evaluation

Around the time of ex-post evaluation, the “Mahinda Chintana: Vision for a New Sri Lanka (policy framework for the period from 2006 to 2016)” was announced, in which eight major issues were picked up for the energy sector. The Vision includes some issues that are related to this project: “diffusion of electricity,” “formulation of independent regulations for the Public Utilities Commission (PUC),” “optimization of the power rate,” “diversification of power sector fuels and development of electric power resources,” and “improvement of power transmission and distribution systems.” These issues are closely associated with the outcomes of this project as well as with its impact, “a stable supply of high-quality electricity at low prices.”

Next, in terms of measures, the “National Energy Policy and Strategies of Sri Lanka” released in May 2008 announced nine policy measures, which included “fulfillment of basic energy demand” and “introduction of a proper price policy.” Separately from the nine policy measures, it contains a section on “overall strategies.” This section discusses the issue of reorganization (that is, unbundling) of the CEB and the application of regulations by the PUC. Therefore, the National Energy Policy and Strategies of Sri Lanka are tightly connected with the outcomes and impact of this project.

The government of Sri Lanka tried to establish an electricity reform act as an important move

with this project and interviews with relevant persons in the CEB, a number of options were discussed at the formulation stage of this project. It is therefore surmised that the final decision was made with the full consent of the Sri Lanka side.

in power sector restructuring in Sri Lanka. First, in 2002, the Electricity Reform Act was formulated and approved by parliament. However, the minister for electric power refused to sign the bill in the end. Thus, the act failed to enter force. Subsequently, there was a move to revise the act and a new electricity act was formulated in 2007. It passed parliament on March 3, 2009. This new act is characterized by deletion of the provision concerning the separation of the CEB's operations that was included in the 2002 Electricity Reform Act. This means that the act approves the current system of the strategic business unit (SBU). On the other hand, the function of an independent regulatory agency concerning setting the power rate, another major pillar of the 2002 Electricity Reform Act, is maintained in the new act.

The problems that lay in the background at the time of appraisal did not change much at the time of ex-post evaluation. That is, the objectives of this project posed important challenges in the power sector in Sri Lanka even at the time of ex-post evaluation. These problems still remain because this project was put on hold² without fulfilling the second conditionality³ that in fact served as an action plan to achieve these objectives.

In this evaluation, we confirmed the issues pertaining to the entire power sector from the time of appraisal in the late 1990s to the early 2000s. The main issues during that period were located in the "quantitative problem of power supply" (that is, the problem that electricity had not been supplied sufficiently nationwide) and the "qualitative problem of power supply" (that is, the problem that the power supply had not been stable in terms of power failure and voltage). Furthermore, these issues were caused by major problems such as "shortage of power generation," "high generation costs," "a problem with setting the power rate" (that is, the problem that costs had not been fully reflected), "underdevelopment of transmission networks," and "underdevelopment of power distribution networks." This project was related to solving or alleviating the multiple causes of these problems. In particular, it directly addressed the problem of establishing a power rate.

2.2 Efficiency

This project was designed as a separate program-type loan project to which JICA's own conditionality was added based on the conditionality (terms and conditions of loan) of the Power Sector Development Program (PSDP)⁴ to which the ADB provided loans. The conditionality is stipulated separately for the first tranche and the second tranche (amount of disbursement). The first tranche conditionality primarily pertains to creating a framework for sector restructuring, whereas the second tranche conditionality is a concrete action towards

² Details on this issue are discussed in section "2.2.2 Period." To put it in a few words here, this project was shelved after the disbursement period had been extended twice, and only a half of the scheduled loan was disbursed.

³ Conditionality means the terms and conditions of loan. The second conditionality is discussed in section "2.2 Efficiency."

⁴ This is the name of the sector funding program that is a coordinated loan project with this loan project.

sector restructuring premised on the first tranche conditionality. (Refer to the following table for details.)

The first tranche would be released after the L/A⁵ had taken effect and the second tranche would have been released when the second tranche conditionality had been fulfilled on December 2003.

Table 1: Conditionality of this project

(First tranche conditionality)

Measures for restructuring	Specific measures and means of confirmation
A. Power sector restructuring	
1.1 Agreement with the IMF on the framework of macro policies	<ul style="list-style-type: none"> • Detailed plan • Agreement with the IMF
2.1 Establishment of a steering committee for power sector restructuring	<ul style="list-style-type: none"> • Establishment of the committee (instituted on February 26,1999).
2.2 Establishment of an energy supply commission	<ul style="list-style-type: none"> • Establishment of the commission (instituted based upon the Electricity Supply Act of 2002)
2.3 The Steering Committee for Power Sector Restructuring will be transferred to the Energy Supply Commission and decisions by the Commission will be approved and adopted.	<ul style="list-style-type: none"> • Related minutes
2.4 The Energy Supply Commission will formulate the CEB's financial restructuring plan, financial improvement plan, enforcement plan of the reforms, and personnel allocation plan.	<ul style="list-style-type: none"> • Various plans
2.5 Approval and public release of the power sector policies	<ul style="list-style-type: none"> • Policy documents • Bringing an electricity bill to parliament
2.6 Setting up a reform office that deals with daily works related to the reforms	<ul style="list-style-type: none"> • Documents concerning establishment (Established in August 2000)
2.7 Approval of a restructuring plan that sketches a future vision of the power sector	<ul style="list-style-type: none"> • Minutes to show approval
2.8 Establishment of an organizational structure and preparation of a work schedule towards the reforms	<ul style="list-style-type: none"> • Report containing the content described on the left
3.1 Formulation of a bill for a public utilities commission that serves as a regulatory agency	<ul style="list-style-type: none"> • Introduction of the bill for a public utilities commission in parliament
3.2 Formulation of a bill for electricity reforms and introduction of the bill in parliament	<ul style="list-style-type: none"> • Bringing the bill for an electricity reform act to parliament
3.3 Parliament passes the bill for a public utilities commission and the bill for an electricity reform act	<ul style="list-style-type: none"> • Parliament passes the bill for an electricity reform act.
B. Financial reforms of the CEB	
1.1 The government formulates and approves a financial restructuring plan and a financial improvement plan.	<ul style="list-style-type: none"> • The financial restructuring plan is approved by March 2002. • The financial improvement plan will be approved by the Energy Supply Commission.
1.3.1 Repayment of delinquent debts created by the public sector in the CEB amounting to 8 million rupees	<ul style="list-style-type: none"> • Documents to indicate payments

⁵ That is, Loan Agreement

2.1 The government's warranty to compensate for the cash shortage during the restructuring period of the CEB	<ul style="list-style-type: none"> • Loan agreement
(Second tranche conditionality)	
Policy measures	Specific measures and means of confirmation
A. Power sector restructuring	
4.0 Government's request to the Constitution Committee to approve the members appointed for the Public Utilities Commission	<ul style="list-style-type: none"> • Written request
4.1 Appointment of members of the Public Utilities Commission	<ul style="list-style-type: none"> • Official documents to confirm its establishment
4.2 Formulation of guidelines for setting the power rate	<ul style="list-style-type: none"> • Guidelines
4.3 Grant of a license to a new power producer certified under the reform program	<ul style="list-style-type: none"> • Confirmation of the issuance of licenses
4.4 Issuance of the management standards of the power sector by the Public Utilities Commission	<ul style="list-style-type: none"> • Performance standards
5.1 Completion of the separation of the CEB's power generation section	<ul style="list-style-type: none"> • Documents to endorse separation; Inauguration of the Board of Directors; Provision of resources; Employment of staff members; Etc.
5.2 Completion of the separation of the CEB's power transmission section	<ul style="list-style-type: none"> • Documents to endorse separation; Inauguration of the Board of Directors; Provision of resources; Employment of staff members; Etc.
5.3 Completion of the separation of the CEB's power distribution section	<ul style="list-style-type: none"> • Documents to endorse separation; Inauguration of the Board of Directors; Provision of resources; Employment of staff members; Etc.
5.4 The government receives an agreement from major financial institutions as to reorganization.	<ul style="list-style-type: none"> • Agreements
5.5 Each separated corporation formulates its own procurement guidelines.	<ul style="list-style-type: none"> • Procurement guidelines
6 Development of an environment that will enable private enterprises to participate	<ul style="list-style-type: none"> • A new power transmission company formulates a project plan as IPP project manager.* • A new power transmission company formulates a model project contract. • The government formulates guidelines for assisting IPP projects. • A new power transmission company formulates guidelines for efficient bidding. • Standardization of the process of environmental impact assessment
B. Financial reforms in the CEB	
1.2 The government assists the CEB with ensuring its liquidity, for instance, by curbing the CEB's net receivables to 2.5 months of its sales.	<ul style="list-style-type: none"> • Report to show improved liquidity
1.3.2 The government pays the unpaid costs of street lighting and develops a payment scheme for the future.	<ul style="list-style-type: none"> • Document to show the payment of payables • Cabinet's written approval for the scheme
1.3.3 Payment of the unsettled tax returns for in-house power generation	<ul style="list-style-type: none"> • Document to show payment
1.3.4 A new power transmission company develops and manages an emergency electricity purchase system including in-house power generation and lease of power generators.	<ul style="list-style-type: none"> • Guidelines concerning the system described on the left

1.4 The government tries to curb the debts of electricity costs (payables) of the public sector to 2.5 months or below.	• Quarterly report
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*Note: IPP stands for an independent power producer.

The plan was that the fund loaned under this project would settle the import expenses for general goods and also be deposited in a special account for the counterpart fund that would be opened in the Central Bank of Sri Lanka. It was further planned that the counterpart fund would be appropriated for the following purposes.

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| <ol style="list-style-type: none"> 1. Payment of unpaid electricity charges by governments and state-owned agencies 2. Payment of unpaid costs for street lighting by the government (by the end of 2002) 3. Payment of unsettled tax returns for in-house power generation by the government* 4. Repayment of the official debts of the CEB 5. Premium on retirement benefits 6. Equipment costs incurred in organizational reforms 7. Awareness campaign costs as to organizational reforms 8. Payment of past service liability (pension liability) |
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*Note: The CEB was allowed exemptions from taxation on purchasing power fuels. At the time of serious drought from 1999 to 2001, the CEB dealt with the pressure of power demand by purchasing surplus electricity of in-house power generation from factories. The fuels that such factories had purchased included taxes. Thus, the CEB requested that the government return the amount equivalent to the taxes and the government had agreed to pay it.

In the evaluation of this project, we conceived that the conditionality of lending would be virtually equal to the outputs of the project. To put it another way, the second tranche conditionality (hereinafter referred to as “the second conditionality”) was defined to be major outputs and it was deemed that the first tranche conditionality was the precondition to realize the second conditionality. (All of the first tranche conditionality was realized.)

As a result, the outputs of the project were only partially materialized. The project period was longer than planned. Therefore, the evaluation for efficiency is low.

2.2.1 Project Outputs

The following table outlines how each item of the second conditionality has been achieved and the cause of non-achievement as to the four objectives (outcomes) of the project.

Table 2: Achievement of the second conditionality

*The meanings of the abbreviations are: R: Realized; N: Not realized.

Item of conditionality	Situation in November 2005*	Reasons for non-achievement
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A. Power sector restructuring		
Items for the project's objective "to introduce a transparent and independent mechanism to set a power rate that reflects costs"		
4.0 The government requests the Constitution Commission to agree on the members appointed for the Public Utilities Commission.	R	—
4.1 Appointment of members of the Public Utilities Commission	R	—
4.2 Formulation of guidelines for setting the power rate	N	Draft guidelines were formulated, but no new applicable companies were founded. Thus, no license has been issued.
4.3 Formulation of guidelines concerning the sanction of new enterprises	N	Same as the above
4.4 Sanctioning of new enterprises acknowledged in the reform program	N	Same as the above
4.5 Formulation of guidelines for setting the power rate for low-income people	N	No action plan was formulated as planned.
Items for the project's objective "to enhance efficiency of the power sector by promoting competition and commercialization"		
5.1-5.3 Completion of the separation of the CEB's operations: power generation, power transmission, and power distribution	N	There are two factors that have hindered the objective from being realized, one at the policy level and the other at the organizational level. At the organizational level, a major cause was that some labor unions strongly opposed. At the policy level, commitment to reforms was not necessarily strong. However, it is believed that under a strong push of the donors (JICA and ADB), the reorganization of the CEB was pressed forward, thereby eventually leading to the introduction of SBU.
5.4 The government receives an agreement as to the reorganization of the CEB from major financial institutions.	N	
5.5 Each separated corporation formulates its own guidelines for procurement.	N	
Items for the project's objective "to invite private funds by developing a transparent management environment"		
6 Improvement of the environment for enabling private companies to participate	N	Not realized because the issue is premised on the above-stated separation of the CEB's operations.
Items for the project's objective "to recover the sound finances of the CEB that will be instrumental in the stabilization of the macro-economy"		
B. The CEB's financial reforms		
1.2 The government assists the CEB with ensuring its liquidity, for instance, by restricting the CEB's net accounts receivable to 2.5 months of its sales.	R	—
1.3.2 The government pays unpaid costs for street lighting and draws up a payment scheme for the future.	R	—
1.3.3 The government pays unsettled tax returns for in-house power generation.	R	—
1.3.4 A new power transmission corporation develops and manages an emergency power purchase system including in-house power generation and lease of power generators.	N	Not realized because the issue is premised upon the abovementioned separation of the CEB's operations.
1.4 The government tries to curb the power cost debts (accounts payable) of the public sector to 2.5 months or less.	R	—

As indicated in the above table, the degree of achievement of the output, that is, the second tranche conditionality, is low. The following section looks into the causes of the low degree of achievement.

The core conditionality that has not been fulfilled is the “separation of the CEB’s operations—power generation, transmission, and distribution.” The reason that the separation had not been realized lay in the fact that the Electricity Reform Act (2002) that contained the clause for separation failed to enter force. The reasons that the act could not take effect were that the CEB had a strong opposing force, i.e., internal labor unions,⁶ and that the minister for electric power refused to sign the bill (although parliament approved the bill).

Under this project, three review missions (i.e., joint missions with the ADB) were dispatched (in September 2004, December 2004, and October 2005). For instance, in the mission of September 2004, the Ministry of Electric Power in Sri Lanka had discussions with the mission and agreed that the cabinet of a new administration would approve the reorganization scheme required for the separation of the CEB’s operations, and that the separation would be completed by February 28, 2005. (There is a memo submitted by the ADB and the former JBIC to the government of Sri Lanka.)

Therefore, it does not appear that the input of resources by JICA has been insufficient. Likewise, in light of the fact that the main actors who were in opposition to the act were labor unions, it might have been possible, as one approach, to inject persons who would have been able to mediate between labor and management. However, since those who were opposed to the act were not limited only to labor unions, there remained some doubts about how effective the input of such mediators might have been under the complicated political circumstances of Sri Lanka. We surmise that it would not have been easy to predict the suspension of the project in advance because due procedures had been taken for signing the loan agreement with the government of Sri Lanka.

2.2.2 Project Period

The project was planned for a period of two years after the loan agreement took effect. (The disbursement due date was initially set on June 30, 2005.) The first tranche was completed in March 2003. Against the background discussed above, however, the second tranche was not released although the disbursement period had been prolonged twice. Disbursement was suspended on January 4, 2006 (the termination of the project).

⁶ There are multiple labor unions in the CEB. The most powerful unions are the Technological Engineers’ Union (with 300 members) and the Store Keepers’ Union (with 150 members), both of which were strongly opposed to the stipulations of the Electricity Reform Act (2002). The representative of the Store Keepers’ Union concurrently represents the federated organization of the CEB’s labor unions. Thus, the union has much influence over the entire organization.

2.2.3 Project Cost

The initial project cost was estimated at 7,440 million yen, whereas the actual cost was 3,720 million yen (only for the first tranche), which was 50% of the planned cost.

2.3 Effectiveness

As a result of the following analysis, this project has produced limited effects, and its effectiveness is low.

Under this project, there were no standard indicators that could be applied for operation and effect. Thus, we confirmed the degree of achievement of each item of the objectives (outcomes) that had been set for this project as follows.

First, each conditionality of this project was directly associated with each item of the project's objectives (outcomes), as discussed in the section on "Relevance." We believe that the conditionality was correctly set. We discuss below the degree of achievement of each item and its backdrop.

1) To enhance the efficiency of the power sector by promoting competition and commercialization: System loss decreased from 19.5% in 2002 to 15.7% in 2007, thus indicating that efficiency had been enhanced. Nonetheless, as for the profitability of the CEB, it has suffered deficits for the last few years. Thus, we cannot assert that the CEB has been effectively managed.

As for this item, the objective itself has not been realized. This is because the project, that is, conditionality, has not been fully fulfilled. Thus, the objective that is a direct effect of this project has been realized only to a low extent.

2) To introduce a transparent and independent mechanism to set a power rate that reflects costs: An independent regulatory agency was instituted. However, it has not shown its function to enforce regulations until now, thus failing to realize improvement of transparency in setting the power rate.

As for this item as well, this project, that is, conditionality, has been inadequately achieved. That is why the objective, i.e., a direct effect, of this project has been realized only to a low extent. The reason that the independent regulatory agency has not been able to carry out its regulatory function lies in the failure to establish and put the act into force for restructuring the power sector that stipulates the functions of the agency. Under the current circumstances, a set of power rate is prepared by the CEB and presented at a cabinet conference through the Ministry

of Electric Power. However, it is often the case that political considerations such as impact on elections are made and the cabinet opts for a lower-level power rate that does not reflect actual costs.⁷

3) To invite private capital by developing a transparent management environment: In Sri Lanka, there were five thermal power-generating plants operated by independent power producers (IPPs) and 23 small power producers⁸ (SPPs) by 2002. These plants produced 19.7% of the total electricity generated in Sri Lanka. By the year 2007, the number increased to eight IPPs and 64 SPPs, which in total generate 39.5% of the total power.

As for this item, there is a certain progress as shown above. Nonetheless, the conditionality to address the issue of improvement an environment for inviting private producers has not been realized. Therefore, the project itself has not contributed to the realization of the effect under this item.

4) To recover the sound finances of the CEB that will be instrumental in the stabilization of the macro-economy: The finances of the CEB have improved to a certain degree by using the counterpart fund. The funds from the former JBIC and ADB (the first tranche) satisfied 53.2% of the amount required for four items out of the eight that had been initially planned. (JICA's fund alone satisfied 27.3%.) The details are outlined in the table below.

Table 3: Use of the counterpart fund

Item	How the counterpart fund was used	Necessary budget *1	Performance *2	
			ADB's portion	JICA's portion
1	Payment of unpaid electricity charges by government and state-owned organizations	889	2,898.6	3,047.0
2	Payment of unpaid costs for street lighting by the government (by the end of 2002)	896		
3	Payment of unsettled tax returns for in-house power generation by the government	452		
4	Repayment of official debts of the CEB	8,934	-	-
5	Premiums on retirement benefits	650	-	-
6	Equipment purchase costs incurred in organizational reforms	2,925	-	-
7	Awareness campaign as to organizational reforms	96	-	-
8	Payment of past service liability (pension liability)	804	-	-
	Total	15,646	2,898.6	3,047.0

⁷ At the time of the second field survey (February 2009), the Electricity Act was established in parliament on March 3.

⁸ This means small-scale hydropower and biomass power generation plants.

*1. Source: Minutes of the discussion (Dec. 20, 2002), ANNEX III

*2. Source: CEB

2.4 Impact

The impact of this project is “a stable supply of high-quality electricity at low prices.” We analyze how this objective has been achieved and its background.

1) When the prices of electricity in Sri Lanka are compared to the international standards, they are higher than those in its neighboring countries despite the fact they are priced lower than the actual total costs of power generation and transmission. For instance, when compared with those in Thailand, the power rate in Sri Lanka is higher in all of the individual, commercial, and industrial categories than that in Thailand⁹ (as of January 2007).

A reason that it was difficult to set a low power rate stems from the fact that power generation costs were relatively high in recent years. However, as of now, the power rate is set below the total costs of power supply. Hence, there is concern that the optimization of the power rate may hinder the supply of electricity at “low prices.”

2) Viewed from the supply side of electricity, the electrification rate has steadily grown in the 2000s. That is, the electrification rate of households was 66.4% in 2001 and increased to 80.0% in 2007.

Thus, the electrification rate has been on the increase, but we cannot assert that this project has directly contributed to improving the indicator in particular. It is related to one objective of this project, that is, “to invite private funds by developing a transparent management environment.” As stated above, however, this project itself has not contributed to the enhancement of inviting private funds. To put it another way, a quantitative impact in particular in power supply has manifested itself through contributions made by other projects than this project and the projects of the recipient country. Specifically speaking, in alignment with the “Government’s Policy Principle for the Power Sector” (2002) that clearly states the promotion of local electrification, many electrification projects have been implemented with assistance from donors. For instance, projects whose completion dates were in the 2000s include two by the ADB, one by the Swedish International Development Cooperation Agency (SIDA), one by Kuwait, and one by China.

3) From the perspective of high-quality power supply, for instance, reliability indicators such as the frequency of blackouts and the number of hours of blackout greatly improved in 2007 in comparison to 2002 in 132-kV and 220-kV transmission networks, after repeated

⁹ Sri Lanka Country Assistance Program Evaluation: Power Sector (August 2007, ADB)

increases and decreases, as indicated in the following table.

Table 4: Changes in the frequency of blackouts and the number of hours

Fiscal year	2002	2003	2004	2005	2006	2007
132kV: Hours of blackout	38,392	20,631	13,221	17,849	19,642	19,679
132kV: Frequency of blackouts	464	337	200	233	290	222
220kV: Hours of blackout	5,220	3,903	1,094	8,327	1,981	2,827
220kV: Frequency of blackouts	39	30	28	38	30	20

Source: CEB

As for the qualitative improvement of power supply, reliability has been on an upward trend. This is due primarily to other projects including a power transmission project separately assisted by the former JBIC and measures taken by the CEB. That is, this project has made no particular contribution to the improvement of the indicators.

2.5 Sustainability

In case of sector loans, as long as a development component is included, sustainability can be validated from the project's organization, technique, and finance. This project contains no development project in particular. Hence, we diagnosed the sustainability of the "second conditionality" (i.e., the second tranche conditionality), which were planned outputs, and the financial sustainability of the entire organization.

First, the conditionalities that have been realized are limited in number such as "appointment of members of the Public Utilities Commission" and "curbing net receivables to the government to 2.5 months or less," but in all likelihood, these achievements will be sustained in the future. Second, as for the conditionality that has not been realized, i.e., "completion of the separation of the CEB's operations of power generation, power transmission, and power distribution," in response to the enactment of the Electricity Act in March 2009, there is a possibility that certain similar effects may be attained in the strategic business unit (SBU), a form of management that was not initially planned. In fact, the top management of the CEB aims for financial improvement of the whole organization by elucidating financial conditions through introducing an SBU-based accounting system (balance sheet and statement of income and expense).

The following table summarizes the balance of income and expense of the CEB since 2003 including those from 2007 on. As can be seen, loss before tax was once inflated to approximately 39 billion rupees in 2008, but it is predicted that it will shrink to about 2.1 billion rupees in 2009. In the background, there are the following factors; sale has increased through

growth of power consumption and raising of sale prices, whereas power generation costs have dropped due to the falling prices of crude oil. In addition, it is expected that power generation costs will decline further through an increase in relatively cheaper thermal electricity by starting the operation of a new thermal power generation plant.¹⁰

Table 5: Statement of income and expense

Fiscal year	In one million rupees						
	2009 (Estimated)	2008 (Tentative)	2007	2006	2005	2004	2003
Gross sales	115,492	115,653	87,574	69,941	55,978	51,119	47,719
Direct expense	116,199	155,236	112,754	81,733	71,027	61,564	48,363
Gross profit from sales	-707	-39,583	-23,477	-11,792	-15,049	-10,445	-644
Operation and management expense	4,063	1,415	1,379	2,383	2,518	634	2,347
Operating profit or loss	-4,770	-40,998	-24,856	-14,175	-17,567	-11,079	-2,991
Other revenue *1	4,248	3,562	11,748	9,572	16,348	2,017	5,440
Payment of interest	1,560	1,600	1,703	1,521	5,634	6,645	6,199
Profit or loss before tax	-2,082	-39,036	-14,811	-6,125	-6,852	-15,707	-3,750

Source: Annual report (2006) by the Department of Finance of the CEB

Note =1: "Other revenues" include the government's subsidies: 11.3 billion rupees in FY 2005; 5 billion rupees in FY 2006 and FY2007, respectively.

Obviously, the overall finances of the CEB have definitely been on the way to improvement when these conditions are studied comprehensively. Nonetheless, it is almost certain that the deficits will remain to the year 2009. In the background of financial improvement lies in a temporary external factor, i.e., a rapid drop in crude oil price. Hence, it is necessary for the CEB to maintain financial soundness by effective cost management through grasping the profit and loss conditions of each operational section in the future.

2.6 Supplementary analysis of the suspended project

2.6.1 Impact had the project not been suspended (hypothetical)

Suppose that the project had not been terminated on January 4, 2006 (even if it had become obvious that the separation of the CEB's operations would be impossible), project management costs, albeit in small amounts, would be continually incurred. Likewise, that the situation without suspending the project would have continued means that the government of Japan lacks so-called "discipline," which would have had an adverse effect on any policy dialogue or negotiation with the government of the recipient

¹⁰ The general manager and the director of the Department of Finance of the CEB explains as follows: "The problem with the finances of the CEB is only with the power generation sector. In particular, the problem is that the price of fuel oil has been on the rise. However, it is anticipated that power generation costs will decrease because 1) The president announced that the sale price of oil by Ceylon Petroleum Corporation (CPC) to the CEB would be reduced to 45 rupees from 71 rupees per liter and 2) the operation of a thermal power generation plant that uses coal will be started in 2011 with assistance from the government of China (accounting for approximately 20% of power generation)."

country in the future.

2.6.2 Timing of suspension of the project

We conclude that the timing of suspension was opportune. When the deadline for the first disbursement (March 28, 2005) had come, it would have been rather difficult to make an instant decision on suspension of the project because there was a possibility that the government of the recipient country might save the situation through collecting information from relevant parties.¹¹ After the extension of the period that was set for March 2005, a special committee was established to discuss the final reform bill to refer it to a cabinet conference. However, when the second disbursement period (June 30, 2005) arrived, the committee failed to draw a conclusion. Then, the government of Sri Lanka requested that the disbursement period be extended again. It is surmised that prudence in discerning the situation worked at that time as well and the period was prolonged up to December 31, 2005. However, in the third joint review mission with the ADB (in October 2005), it was assumed that fulfillment of the conditionality was no longer possible.¹² The decision was made when the third disbursement period (December 21, 2005) had elapsed not to extend the period for a third time.

The timing of making a decision on suspension of the project was neither too late nor too early. That is, it was appropriate.

3. Conclusion, Lessons Learned and Recommendations

3.1 Conclusion

The relevance of this project is high. It was not possible to reverse the decision on the implementation of this project by predicting in advance the causes that led to suspension of this project. The timing of the suspension of the project was good. Had the decision on the project's

¹¹ According to a document dated March 28, 2005 prepared by Team 3 of Development Department 2 of the former JBIC, a discussion was held at the end of February 2005 as to sector reforms between the president of Sri Lanka and the CEB unions that opposed the separation. It was decided in the discussion that the policy on sector reforms based on exchange of opinions with the unions would be decided in the cabinet. A sector reform bill was presented jointly by the president, the minister for finance, and the minister for electric power, and an official request to extend the period was presented by the government of Sri Lanka. The sector reform bill ① was based on the policy of sector reforms that had been agreed between the ADB and JBIC and ② declared that the CEB's operations would be separated by June 1, 2005. It is expected that cabinet approval will be given in the very near future as to the separation of the CEB's operations that had been considered impossible due to strong opposition of the unions. Similarly, in all likelihood, the possibility of achieving the second tranche conditionality by the end of June 2005 has grown greater.

¹² It was revealed through this joint review that opinions did not converge concerning a revised sector reform bill (approved by the cabinet in July). For instance, the representatives of CEB unions and some members of the Steering Committee for Power Sector Restructuring refused to sign the bill. Furthermore, a problem regarding the content of the bill was also exposed whereby there was concern over the low degree of independence of a new company because it would be founded based on the Public Corporation Act instead of the Companies Act.

suspension been made later, it might have had a negative effect. Therefore, I conclude that the decision on implementation and suspension of the project was proper. It should be noted that the project has produced effects, albeit partial, despite its suspension.

3.2 Lessons Learned

- Lessons to prevent a situation in which a project is suspended: I do not believe that there was any particularly serious flaw at the time of appraisal. Therefore, there is little need to offer any lessons in particular. However, we should note the necessity of thoroughly discerning how clearly a roadmap towards reforms is prepared for a project, for instance, in the field of sector reforms. In the future, when a project is implemented in Sri Lanka, based on the political situation particular to this country in which the left-wing party is powerful, it is essential to proceed with a state-managed project or privatization with extreme care when it is not supported by unions.
- The best way to suspend a project when compelled to do so: As done in this project, a review mission should be dispatched at a key point to identify major stakeholders with whom opinions are exchanged and information should be analyzed.

3.3 Recommendations

I conclude within the scope of this field survey that the possibility of separating the CEB's operations in the power sector in Sri Lanka is not necessarily promising. The ADB has already set forth its policy that it will respect the initiative of the Sri Lanka side and provide its assistance without adhering to the conditionality of the former project (i.e., separation) based on the idea that reforms will not be pushed forward with a sense of ownership if the donor's intention is too strong. It is recommended that JICA also take a more realistic approach in which sector reforms will be pushed forward premised upon the present SBU. Currently, the CEB is interested in making a financial statement for each operation (SBU), i.e., power generation, power transmission, and power distribution. For instance, the promotion of this attempt with technical assistance may contribute to improving the profits of the CEB in the future.