

THE WORLD BANK GROUP ARCHIVES

PUBLIC DISCLOSURE AUTHORIZED

Folder Title: Travel briefs, Sri Lanka 01

Folder ID: 1772863

ISAD(G) Reference Code: WB IBRD/IDA 03 EXC-10-4540S

Series: Travel briefings

Sub-Fonds: Records of President Robert S. McNamara

Fonds: Records of the Office of the President

Digitized: May 16, 2013

To cite materials from this archival folder, please follow the following format:
[Descriptive name of item], [Folder Title], Folder ID [Folder ID], ISAD(G) Reference Code [Reference Code], [Each Level Label as applicable], World Bank Group Archives, Washington, D.C., United States.

The records in this folder were created or received by The World Bank in the course of its business.

The records that were created by the staff of The World Bank are subject to the Bank's copyright.

Please refer to <http://www.worldbank.org/terms-of-use-earchives> for full copyright terms of use and disclaimers.



THE WORLD BANK
Washington, D.C.

© 2012 International Bank for Reconstruction and Development / International Development Association or
The World Bank
1818 H Street NW
Washington DC 20433
Telephone: 202-473-1000
Internet: www.worldbank.org

PUBLIC DISCLOSURE AUTHORIZED

McNamara Papers

Travel briefs -
Sept. 29 - Oct.

 **Archives**
Travel briefs, Sri Lanka 01
A1995-259 Other # 22 1772863 308703B

Folder 4 of 4

DECLASSIFIED
WBG Archives

SRI LANKA

MR. MCNAMARA'S BRIEF

Table of Contents

- A. Itinerary
- B. Airport Statement
- C. Map and State Department Notes
- D. List of Cabinet Members and Biographical Data
- E. Topics for Discussion
 - 1. President Jayawardene
 - 2. Prime Minister Premadasa
 - 3. Minister of Finance and Planning, Ronnie de Mel
 - 4. Minister of Lands and Land Development and of Mahaweli Development, Gamini Dissanayake
 - 5. Field Trip to Mahaweli Ganga Development Project Area and Tea Rehabilitation Project Area
- F. Reference Material
 - 1. Political Situation
 - 2. Economic Situation
 - 3. Foreign Assistance and Debts
 - 4. Annual Meeting Discussions
 - 5. Briefs on Special Issues
 - a. Medium Term Development Program
 - b. Mahaweli Ganga Development Program
 - c. Investment Promotion Zone
 - d. Greater Colombo Development Program
- G. Bank Group Operations
 - 1. Statement of Loans, Credits and IFC Operations
 - 2. Proposed Lending Program through FY 84
 - 3. Ongoing Projects
 - 4. Prospective Operations
 - 5. Memorandum of Conversation
- H. UNDP Activities
- I. News and Media
 - 1. Press Clippings
 - 2. Information Media
- J. Country Economic Memorandum

Sri Lanka

Day 1

Thursday, October 12

17:30 Arrive Colombo from Bombay by special plane provided by Government of India. (Accompanied by Mrs. McNamara, Messrs. Hopper, Clark, Narasimham and Koch-Weser)

18:00 Arrive Intercontinental Hotel

18:30 Meeting with the Minister of Finance and Planning, Mr. Ronnie de Mel. (Meeting subject to timely arrival of party from Bombay)

19:30 Official dinner hosted by President Jayawardene (President's House)

Day 2

Friday, October 13

08:00 Briefing on Mahaweli Ganga Development Program at the Operations Room, Central Bank of Ceylon. (Dress for field trip as party will leave directly from briefing for field trip).

08:45 Leave for Army Grounds, Colombo

09:00 Depart Army Grounds by helicopters. (Accompanied by Mr. Gamini Dissanayake, Minister of Lands and Land Development and of Mahaweli Development, Messrs Hopper, Clark, Narasimham, Shibusawa and Koch-Weser.) Fly over Kotmale.

10:00 Arrive Dickoya Sports Club Grounds. Brief inspection of Tea Rehabilitation area at Maskeliya and meeting with planters and estate work-force.

11:00 Depart Dickoya by helicopters. Fly over Polgolla, Victoria, Randenigalla, Maduru Oya and Polonnaruwa

12:00 Arrive Anuradhapura

12:30 Lunch at Miridiya Hotel, Anuradhapura, hosted by Mr. Gamini Dissanayake, Minister of Land, Land Development and Mahaweli Development.

14:00 Leave Anuradhapura by helicopters for Maha Illupallama Research Station.

14:20 Visit by road transport homesteads in the IDA assisted Mahaweli Ganga Development Project II area.

16:00 Depart Maha Illupallama by helicopters for Colombo

17:00 Arrive Colombo (Army Grounds).

17:30 Arrive Hotel.

19:30 Official dinner hosted by Mr. Ronnie de Mel, Minister of Finance and Planning, at Hotel Intercontinental

23:30 Leave Hotel for Katunayake International Airport

Day 3

Saturday, October 14

01:35 Depart for London by BA34

B. Airport
Statement

Airport Arrival Statement

Sri Lanka

I am delighted to be in Sri Lanka, and greatly appreciate the kind invitation to visit your beautiful and interesting country. I am particularly looking forward to meeting your leaders. From these discussions, I hope to acquire a deeper understanding of your problems and prospects, and of the policies you are adopting to stimulate the economic and social progress of your people.

The remarkable progress Sri Lanka has made in the social field and the quality of life it has provided to its citizens through free education, health care and social services, has made this country almost unique in the developing world. We in the World Bank are greatly impressed by your achievements in this field.

World Bank lending to Sri Lanka has been increasing in recent years. Over the last three years, IDA has provided \$92 million out of a total of about \$220 million provided to date by the Bank and IDA for projects relating to agriculture, power, water supply and industry. I am especially pleased that this trip will include a visit to Mahaweli Project in which we have been closely involved in the past and which will continue to receive our attention in the future. I am looking forward to the opportunity of learning more about your farmers, whose efforts will be of crucial importance in building a better future for your country.

As you know, the bulk of the resources -- human and material -- for development comes from within the developing countries themselves. In line with your readiness to implement the necessary and often difficult measures that constitute the basis of any serious development effort, we are prepared to assist projects of high priority within the framework of Sri Lanka's development program.

In providing assistance, our aim is to help the people of Sri Lanka to achieve the goals that they themselves have chosen. Your country has the potential for rapid as well as equitable growth, and we in the World Bank are ready to assist in any way we can.

C. Map and State
Dept. Notes

Sri Lanka

State Department Notes

The attached State Department briefing has been overtaken by events, particularly since it was prepared before the August 1977 elections. For:

- an analysis of the political situation,
see Section F-1.
- an analysis of the economic situation,
see Section F-2.
- a list of Government officials,
see Section D.

department of state * december 1976

OFFICIAL NAME: Republic of Sri Lanka

GEOGRAPHY

The Republic of Sri Lanka is a pear-shaped island located in the Indian Ocean southeast of India, from which it is separated at the closest point by only 18 miles (29 km.). It has an area of 25,332 square miles (65,610 sq. km.), about the size of West Virginia. A plain only slightly above sea level makes up the entire northern half of the island and continues around the coast of the southern half. The south-central part is hilly and mountainous, ranging from 3,000 feet

to more than 7,000 feet (914-2,133 m.) above sea level in the Central and Uva Provinces, where Sri Lanka's best quality high-grown tea is produced.

Sri Lanka has a generally uniform tropical climate. The south-central mountains offer some relief from the tropical heat. Throughout the year the humidity is rather high—more than 75 percent—and the temperature averages 80°F (27°C), with little variation daily or seasonally. Average annual rainfall ranges from about 50 inches (127 cm.) in the northeast section to about 200 inches (508 cm.) in the

southwest, the distribution being determined largely by the monsoon and the island's topographical features. The heaviest rainfall occurs during the southwest monsoon period in the early summer.

(Sri Lanka is 10½ hours ahead of eastern standard time.)

PEOPLE

Sri Lanka's population is about 13.4 million. Population density is greatest in the southwest quarter of

PROFILE**Geography**

AREA: 25,332 sq. mi. (65,610 sq. km.), compares in size with W.Va. CAPITAL: Colombo (pop. 890,000). OTHER CITIES: Jaffna (110,000), Kandy (91,942), Galle (72,720).

People

POPULATION: 13.4 million (1973 est.). ANNUAL GROWTH RATE: 1.7%. DENSITY: 529 per sq. mi. (204 per sq. km.). ETHNIC GROUPS: Sinhalese 68%, Tamils 22%, Moors 8%, Burghers, Malays, Veddahs. RELIGIONS: Buddhist, Hindu, Islamic, Christian. LANGUAGES: Sinhala (official), Tamil, English. LITERACY: 85% (percentage of age group completing elementary school: 80%). LIFE EXPECTANCY: 67 years.

Government

TYPE: Republic. INDEPENDENCE: February 4, 1948. DATE OF CONSTITUTION: May 22, 1972.

BRANCHES: Executive—President (Chief of State, appointed to 4-yr. term);

Prime Minister (Head of Government). Legislative—National State Assembly (151 members elected to 6-yr. terms, 6 appointed members). Judicial—Constitutional Court, Supreme Court, Commissioners of Assize, Criminal Court of Appeals.

POLITICAL PARTIES: Sri Lanka Freedom Party (SLFP), United National Party (UNP), Lanka Sama Samaja Party (LSSP), Communist Party (Moscow, CP/M), Tamil United Liberation Front (TULF). SUFFRAGE: Universal adult. ADMINISTRATIVE SUBDIVISIONS: 9 Provinces.

FLAG: Background is yellow. A red stripe and a green stripe run up the staff side. On the remaining two-thirds is a yellow lion holding up a sword centered in a red square.

Economy

GDP: \$2.93 billion (1974). ANNUAL GROWTH RATE: 3.5%. PER CAPITA INCOME: \$217. PER CAPITA GROWTH RATE: 1.7%.

AGRICULTURE: Cultivated land 39%. Labor 45%. Products—tea, coconuts, rubber, rice, spices.

INDUSTRY: Labor 3%. Products—consumer goods, textiles, chemicals and

chemical products, milling, light engineering, paper, and paper products.

NATURAL RESOURCES: Limestone, graphite, mineral sands, gems.

TRADE: Exports—\$519 million (1974): tea \$203 million, rubber \$110 million. Partners—UK \$45 million (1973), US \$46.5 million (1975), Communist countries \$47 million (1973). Imports—\$688 million (1974): food \$287 million, petroleum \$141 million, fertilizer \$75 million. Partners—Iraq, China, US, UK, Germany, USSR, Japan, India.

LEGAL EXCHANGE RATES: 8.6 Rupees=US\$1, official (floating). Export promotion/tourist (locally called FEEC)—14-25 Rupees=US\$1 (1976).

ECONOMIC AID RECEIVED: Total—\$761 million, 1974. IBRD—\$150 million; OPEC countries, \$68 million; short-term bank credits, na. US only (1946-1974)—loans and grants \$120 million, PL 480 (Food for Peace) \$168 million, Peace Corps \$1 million, EXIM Bank \$3 million.

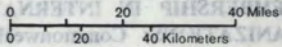
MEMBERSHIP IN INTERNATIONAL ORGANIZATIONS: Commonwealth, UN, IBRD, IMF, ADB, Colombo Plan, Group of 77, nonaligned group of nations.

(Either "Sri Lanka" or "Ceylonese" is an appropriate adjective.)



Sri Lanka

- ⊙ National capital
- +— Railroad
- Road
- ✈ International airport



the island, where agricultural conditions are most favorable. Greater Colombo has about 900,000 inhabitants.

The island's population increased for many years at an average annual rate of 2.4 percent, resulting in its doubling in 25 years. Fertility rates have begun to decline (to 1.7 percent in 1976), but development programs undertaken in the country continue to be offset by population growth, and an already relatively low living standard threatens to be even further depressed. The government has devoted much attention to this problem in recent years and has stepped up considerably the availability of family-planning services. It has been aided by a substantial U.N. assistance, which is reinforced by active private programs and by bilateral aid from Sweden.

Ethnically about 70 percent of the people are Sinhalese and 22 percent are Tamil (people of south Indian origins). About half of the Tamil population are "Ceylon Tamils" (Ceylonese citizens whose ancestors have lived in Sri Lanka for many generations and who have full voting rights). Ceylon Tamils live predominantly in the Northern and Eastern Provinces.

The other half of the Tamil population are the so-called "Indian Tamils," whose forebears were brought to Sri Lanka from south India in the latter half of the 19th century to work on the tea and rubber plantations. About nine-tenths of them were disenfranchised as a result of legislation passed in 1948. As India also refused to recognize these people as its citizens, they were in effect stateless.

Their presence has constituted a major population growth problem which becomes increasingly acute each year. The estates on which the 1 million Indian Tamils live cannot provide work for all the young people entering the labor force, and it is virtually impossible for them to obtain outside employment.

In an effort to settle this long-standing issue, an agreement between Sri Lanka and India was concluded on October 30, 1964. The agreement provided that India would accept 525,000 of the Indian Tamils, with their natural increase, over a period of 15 years; Sri Lanka would grant citizenship to 300,000 during the same

TRAVEL NOTES

Climate and Clothing—The climate of Sri Lanka is tropical. Clothing worn during a hot American summer is suitable for year-round use in Sri Lanka. Wash and wear clothing is advised; there are few dry-cleaning facilities. Toiletries, cosmetics, home medicines, and photographic items, including film, should also be brought, as these are difficult to obtain.

Customs—US citizens do not need visas to enter Sri Lanka for a 30-day period. All visitors do need a valid smallpox and cholera certificate, however. A physician should be consulted for additional recommended inoculations (e.g., gamma globulin). Foreign currency, including travelers checks, must be declared upon entry, because travelers are required on departure to show evidence of having changed their money through authorized agents. Foreign visitors currently are entitled to exchange their money at a favorable rate of exchange (known as the FEEC rate).

Health—Public health facilities in Sri Lanka are good. The US Embassy maintains a list of private physicians who may be consulted in cases of emergency. Medical supplies are scarce, so it is best to bring along any special drugs required. Avoid drinking unboiled water and eating unpeeled or uncooked fruits and vegetables.

Telecommunications—Telephones are found in virtually all hotels, and telephone service within the country is good. Long-distance service to and from

Sri Lanka is good and direct but must be booked through an operator in advance. Telegraph and cable service is excellent and is available 24 hours in Colombo. International mail service is good, with 1-week service to the US. Registered airmail service is reliable. Seamail service is slow and sometimes erratic.

Transportation—Colombo is well served by many international airlines, though no US carriers transit Sri Lanka. All parts of the island may easily be reached either by rail or by bus, though most foreign visitors hire a vehicle to travel outside Colombo. Rates are reasonable. Metered, inexpensive taxi service is readily available in Colombo. Air Ceylon offers service to the east coast and northern towns.

Tourism—The Ceylon Travel Board in Colombo and numerous travel agencies in Sri Lanka can easily arrange for inexpensive and comfortable travel to points of archaeological interest such as Anuradhapura and Pollonaruwa as well as to such popular towns as Kandy, Galle, Nuwara Eliya, and Trincomalee. Hotels in Sri Lanka are numerous, inexpensive, and of good quality. There is an interesting national museum in Colombo and a smaller collection in Kandy. The latter town is Sri Lanka's religious and cultural center, where the island's main Buddhist shrine, the Temple of the Tooth, is located and where the famous Perahera procession is held nightly for about 2 weeks in August. Kandy, about 70 miles (112 km.) from Colombo, is also the site of the Peradeniya campus of the University of Sri Lanka and of the splendid Royal Botanical Gardens.

period; and the future of the remainder (approximately 150,000) would be considered later. A significant breakthrough was achieved in April 1973; following negotiations between India and Sri Lanka in which both countries agreed to progressively increase repatriation by 10 percent each year over the flow of 35,000 persons agreed to in 1964, while the granting of Sri Lankan citizenship was to be substantially accelerated. In February 1974 the two countries agreed to divide equally the remaining 150,000 persons, whose status had been left open by the 1964 pact. Implementation is expected to be completed by the early 1980's. Other minority groups in Sri Lanka include

the Moors (as the Muslim community is known)—about 8 percent of the population, and the much smaller communities of the Burghers (descendants of Portuguese and Dutch colonists), Eurasians, Malays, and a small number of Veddahs, the earliest known inhabitants of the island.

Buddhism, in its Theravada form, is the religion of most of the Sinhalese; Hinduism, that of the Tamils; and Islam, that of the Moors and Malays. Christianity cuts across ethnic lines with some 900,000 followers, most of whom are Roman Catholics.

Sinhala is the official language of Sri Lanka. English, however, is widely spoken. The literacy rate is about 85 percent.

READING LIST

These titles are provided as a general indication of the material published on this country. The Department of State does not endorse the specific views in unofficial publications as representing the position of the U.S. Government.

- Most important English-language newspaper: *Ceylon Daily News*. Arasaratnam, S. *Ceylon*. Englewood Cliffs, N.J.: Prentice - Hall, 1964.
- Beny, Roloff. *Island Ceylon*. New York: Viking Press, 1972.
- Codrington, Humphrey William. *A Short History of Ceylon*. New York: Macmillan, 1947.
- Foreign Area Studies. *Area Handbook for Ceylon*. Washington, 1971.
- Goonetilleke, H.A.I. *Images of Sri Lanka Through American Eyes: Travellers in Ceylon in the 19th and 20th Centuries*. Colombo, 1976.
- Grosvenor, Gilbert M. and Donna K. "Ceylon." *National Geographic*, April 1966.
- Kearney, Robert N. *The Politics of Ceylon (Sri Lanka)*. Ithaca, N.Y.: Cornell University Press, 1973.
- Ludowyk, E.F.C. *The Story of Ceylon*. London: Faber and Faber, 1962.
- Singer, Marshall R. *The Emerging Elite: A Study of Political Leadership in Ceylon*. Cambridge: Massachusetts Institute of Technology Press, 1964.
- Smith, Donald E. *South Asian Politics and Religion*. Princeton: Princeton University Press, 1966.
- Woodward, Calvin A. *The Growth of a Party System in Ceylon*. Providence: Brown University Press, 1969.

HISTORY

The earliest known inhabitants of Sri Lanka were the Veddahs, some of whose descendants still live in the jungle regions of Sri Lanka. They and the other primitive peoples of Sri Lanka were subjugated and largely assimilated by Aryan invaders, the Sinhalese, who came from northern India to Sri Lanka in about the 6th century B.C.

The early settlers from India occupied the dry north-central area and constructed elaborate irrigation works to insure a supply of water for the principal food, rice. (Efforts were made under British rule and are continuing now to reconstruct these works and resettle the area.) In the 3rd century B.C., with the coming of Buddhism to Sri Lanka from India, Sinhalese civilization flowered, and the Buddhist religion spread rapidly. The architectural and irrigational ruins at Anuradhapura, the first capital (3rd century B.C.-9th century A.D.), and Polonnaruwa further east (9th through 12th centuries A.D.), testify to the high culture reached by the Sinhalese during this early period.

Throughout these centuries the Sinhalese were in frequent conflict with invaders from southern India. The most notable invasion was of the Chola Kingdom in the 11th century A.D., which made Sri Lanka, for the first time since the Aryan conquest, a dependent kingdom tributary to an Indian empire. Chola rule did not last long, but under constant pressure the focus of Sinhalese political power gradually was forced to the center and south of the island, eventually concentrating around the Kingdom of Kandy and around Colombo. Sinhalese self-consciousness rests in large measure on a still-vivid historical awareness which stretches back over many centuries as well as on a commitment among many to the survival of Buddhism and the special role of the Sinhalese language. The Tamils, who settled in northern Sri Lanka, did not adopt Buddhism but clung instead to the Hindu religion, which they follow to this day. In the 12th century, Muslims (called Moors) from the Persian Gulf were building a profitable trade with Ceylon, where some of them settled.

European Settlement and Independence

The Portuguese, the first Europeans to come to Sri Lanka, were attracted by the spice trade, Sri Lanka then being the sole producer of a fine grade of cinnamon. Beginning in 1505 they gradually gained control of the western maritime provinces and established themselves in the north as well. They were able to maintain control over coastal Sri Lanka for nearly 150 years.

It was during this period that Christianity was introduced to the island.

In 1638 the Dutch East India Company, motivated by a desire to control the profitable cinnamon trade, entered Sri Lanka and, with the aid of the King of Kandy, succeeded after 20 years in supplanting the Portuguese. The Dutch were interested primarily in increasing trade, and most of their activities in Sri Lanka were devoted to this end. The major permanent heritage left by the Dutch was a foundation for a system of civil law.

The Dutch, in turn, were supplanted by the British, following a military expedition in 1796. Whereas the Portuguese and Dutch never succeeded in bringing the interior of the island under their control, the British, aided by a group of dissatisfied Kandyan nobles, finally succeeded in doing so in 1815, a key time in Ceylonese history. Sri Lanka remained a British Crown Colony and received periodic extensions of democratic participation in the government until 1931. In that year, the Donoughmore constitution enfranchised Ceylonese adults and gave them an opportunity for limited self-government.

The British period was also notable for the establishment of a plantation economy based on the export of tea, rubber, and coconut; the widespread dissemination of English language education; the rise of an anglicized Ceylonese elite; and, in the 20th century, the growth of nationalist sentiment and the emergence of political groups and parties prepared to assume power. In 1946 the Donoughmore constitution was replaced by the Soulbury constitution, which granted the island a parliamentary form of government. The following year the Ceylon Independence Act was passed, and Sri Lanka became fully independent and a member of the British Commonwealth on February 4, 1948.

Postindependence

Sri Lanka's first parliamentary elections were held in September 1947. The moderate United National Party (UNP) won these elections, as well as those held in 1952, by comfortable margins. However, in general elections held 4 years later, the UNP was defeated by the Sri Lanka Freedom Party (SLFP), whose campaign em-

phasized Buddhism, nationalism, "democratic socialism" in Sri Lanka, and nonalignment in international affairs. Also growing in influence during this period, due to their active involvement in the urban trade union movement, were Sri Lanka's two main Marxist parties, the Lanka Sama Samaja Party (LSSP)—a Trotskyite group—and the Communist Party of Sri Lanka. SLFP leader Solomon W.R.D. Bandaranaike was assassinated in September 1959, and his coalition government fell the following December. The UNP formed a shaky minority government following the March 1960 general elections, but it fell too a few months later, after receiving a vote of "no confidence."

In July 1960 the SLFP, under the leadership of Mrs. Sirimavo Bandaranaike, widow of the late Prime Minister, won a near majority of parliamentary seats and was able to form a wholly SLFP government. To bolster its faltering parliamentary strength, the SLFP formed a coalition in June 1964 with the Lanka Sama Samaja Party (LSSP), but it fell in December, when 14 SLFP Members of Parliament left the party because of economic stagnation, the increasing influence of leftist elements in the coalition, and the government's plans to nationalize the press.

In the March 1965 general elections the UNP, with the support of other parties that had opposed Mrs. Bandaranaike's government, was able to form a coalition government. UNP leader Dudley Senanayake, who had headed previous UNP governments, again became Prime Minister.

GOVERNMENT

On May 22, 1972, the Ceylonese adopted a new Constitution, which declared Ceylon to be the Republic of Sri Lanka. Prior to this date, Ceylon had been a completely self-governing Dominion in the Commonwealth, with Queen Elizabeth II as Head of State. Under the Constitution, the Head of State is a President appointed by the Prime Minister. This position is largely ceremonial, and the Constitution requires the President to act upon the advice of the Prime Minister in most matters. Sri Lanka continues to remain

within the Commonwealth in spite of the change in its Constitution.

Legislative power rests in the National State Assembly (formerly Parliament), with 157 members. It is a unicameral legislature composed of 151 members elected by universal suffrage for a maximum 6-year term; the remaining 6 members are appointed by the Council of Ministers. The members of the first Assembly will have 5-year terms, with new elections mandatory by May 22, 1977.

The general direction and control of the government is given to the Prime Minister, who is the Head of Government, and the Council of Ministers, which the Prime Minister appoints. The leader of the dominant party in the Assembly would normally be named Prime Minister by the President. The Council of Ministers has wide governing power, including control over the civil service and the judiciary. Sri Lanka is divided into 22 Districts administered by government agents who are members of the Ceylon Administrative Service.

Sri Lanka's judiciary consists of a Constitutional Court, a Supreme Court, Commissioners of Assize, a Criminal Court of Appeals, and a number of subordinate courts. The National State Assembly is empowered to create additional courts if it feels they are needed. The Supreme Court, composed of a Chief Justice and 10 Puisne Justices, has appellate jurisdiction in civil cases, original jurisdiction in criminal cases, and exclusive jurisdiction in the more serious criminal offenses. It is the highest court with regard to civil cases, but its decisions on criminal cases may be appealed to the Criminal Court of Appeals. Commissioners of Assize are judicial officers appointed to hold any criminal session or part thereof of the Supreme Court. The constitutionality of legislation passed by the National State Assembly cannot be challenged in the courts. Proposed legislation may be challenged and referred to the Constitutional Court prior to passage by the Assembly to determine whether it is inconsistent with the Constitution. If a proposed law is considered inconsistent, it may not be passed except by a vote of two-thirds of the members of the Assembly.

Principal Government Officials

President—William Gopallawa
 Prime Minister; Minister of Defense and Foreign Affairs; Minister of Planning and Employment—Mrs. Sirimavo Bandaranaike
 Minister of Irrigation, Power, and Highways—Maithripala Senanayake
 Minister of Foreign and Internal Trade; Minister of Public Administration, Local Government and Home Affairs—T.B. Ilangaratne
 Minister of Shipping and Tourism—P.G.B. Kalugalle
 Minister of Industries and Scientific Affairs—T.B. Subasinghe
 Minister of Finance; Minister of Justice—Felix Dias Bandaranaike
 Minister of Parliamentary Affairs; Minister of Sports; Minister of Transport—K.B. Ratnayake
 Chief Justice of the Supreme Court—Victor Tennekoon
 Ambassador to the U.S.—Neville Kanakaratne
 Ambassador to the U.N.—H. Shirley Amerasinghe

Sri Lanka maintains an Embassy in the U.S. at 2148 Wyoming Ave., NW., Washington, D.C. 20008 (tel. 202-483-4025).

POLITICAL CONDITIONS

Sri Lanka has maintained a strong democratic tradition since independence in 1948, with control of the government changing hands five times through peaceful democratic elections. In elections held on May 27, 1970, the SLFP, led by Mrs. Bandaranaike, and its coalition partners, the LSSP and the pro-Moscow Communists (CP/M), were elected in a landslide victory. The SLFP won 91 parliamentary seats and also gained the six appointive seats which were assigned to SLFP supporters. The LSSP and the CP/M won 19 and 6 seats, respectively.

Despite the lopsided number of parliamentary seats won by the SLFP in 1970, the UNP and SLFP were almost evenly balanced in competing for the popular vote, both of them deriving their support from the Sinhalese Buddhist majority, while also attracting considerable Christian and Muslim backing. Two Tamil parties, the Federal Party and the

RI
inc
thi
do
un
th
M
A
B
C
F
G
G
K
L
S
S
V
H
S
w
ju
th
L
as
S
In
c

Tamil Congress, represented the interests of the Ceylon Tamils in the Northern and Eastern Provinces of Sri Lanka in 1970. In 1972, however, these and other Tamil groups banded together to form the Tamil United Liberation Front (TULF) to promote Tamil interests and agitate for official status for the Tamil language.

More recently, militant Tamil youths have urged formation of a "separate" Tamil state in Sri Lanka, claiming that there exists little opportunity for Tamils in the face of Sinhalese preponderance. Although the leadership of the TULF has called for nonviolent protest, there have been some incidents of violence in the Jaffna Peninsula, where most of the Ceylon Tamils live.

The backbone of the Marxist parties are urban labor unions, and their support is mainly in the Western and Southern Provinces. The impact of the Marxist parties on Sri Lanka's political and economic life is greater than their overall popular following would indicate. The leftist leaders have a consistent record of "anti-imperialism" and they cater to popular mass aspirations. They control most of the larger urban trade unions and are able, by raising demands on behalf of labor, to cause any government serious economic difficulties.

Although organized labor in Sri Lanka accounts for about 1.5 million members of the total labor force (estimated at nearly 4 million), it is fragmented into more than a thousand unions. Moreover, three large unions of agricultural workers of the tea, rubber, and coconut estates comprise nearly half the organized workers. White-collar employees, particularly in government ranks, are union members to a much greater degree than in the United States. The bulk of the unorganized labor force consists of small farmers.

Those unions which have been openly associated with the SLFP and the Ceylon Communist Parties (Moscow and Peking) are affiliates of the World Federation of Trade Unions (Communist). The Ceylon Workers Congress, the largest union of estate workers and by far the largest union in Sri Lanka, is an affiliate of the International Confederation of Free Trade Unions.

Sri Lanka's democratic tradition received its most severe challenge in April 1971, when an attempt was made to carry out an overnight revolution through well-coordinated and widespread attacks on police stations and other government facilities. These attacks, made by a group calling itself the *Janatha Vimukti Peramuna* (JVP, People's Liberation Front), very nearly succeeded in overthrowing the government. Sinhalese Buddhist youths from rural areas who had been indoctrinated with "Maoist" ideology made up the rank and file of this group. Most of the Ceylonese did not support the uprising, and the government was able to restore order within a few weeks. However, what are believed to be the underlying causes of the uprising—unemployment and limited economic opportunity, particularly for educated rural youth—continue to plague the country.

In September 1975, following many months of growing differences between the SLFP and the LSSP, the latter party was expelled from the coalition and moved into the opposition. Mrs. Bandaranaike's party continues to maintain overwhelming control of the National State Assembly, with 98 of 157 seats. The UNP, which had ruled from 1965 to 1970 and which became the main opposition in 1970, won only 17 seats. By-election results have slightly altered that number. The UNP is headed by veteran politician J.R. Jayewardene, who holds the office of Leader of the Opposition. Under the Constitution, elections for a new Parliament must be held within 3 months after Parliament is dissolved, which can be no later than May 1977.

ECONOMY

Sri Lanka's economy is predominantly agricultural, with manufacturing accounting for only 15 percent of the gross national product (GNP). In 1974, GNP was about \$2.93 billion and per capita GNP was \$217, both at current prices. Restrictions on the importation of foreign goods have stimulated manufacturing in recent years, but the scarcity of foreign exchange and of minerals and other natural resources probably will inhibit

any large-scale industrialization in the foreseeable future.

Tea, rubber, and coconut are Sri Lanka's most important export products. They account for 70 percent of its foreign exchange earnings, bring in 30 percent of the national income, and provide employment for about 20 percent of the total work force. Tea alone accounts for 40 percent of the value of all exports and about 12 percent of the GNP.

Sri Lanka has traditionally depended on exports to finance not only importation of manufactured goods but also a large share of its more basic needs, including about 50 percent of the food consumed on the island. Until quite recently this system worked well, and the average Ceylonese enjoyed a living standard which, although low by Western standards, was appreciably higher than that of most Asians.

Government policies have systematically focused on improving the conditions of the bottom half of the population. There has been a significant transfer of resources by way of education, health, and food and other subsidies. Notable consequences of this social framework have been an increase in life expectancy by 15 years, reduction in infant mortality by 50 percent, and a high literacy rate. A stabilization of population in rural areas has also been achieved. Finally, there has been a significant transfer of power from the English-speaking urban groups to a much broader spectrum of society.

These achievements, initiated and pursued through the fifties and sixties, helped orient Mrs. Bandaranaike's coalition government in 1970 to a program which would consolidate a Socialist, welfare-state economy and society. There was some nationalization of foreign and domestic private assets, backed by new laws giving the government considerable latitude in controlling the economy. Extensive land reform in the plantation sector occurred between 1972 and 1975, with most large estates, both foreign and locally owned, having been acquired by the state.

Domestic production, however, has not grown as rapidly as necessary to absorb a rising population and to permit the further extension of ben-

efits. Drought, curtailed industrial imports, and inadequate incentives were, in part, responsible. In addition, the earnings of Sri Lanka's main exports lagged behind the rising prices of its imports.

The fundamental weakness of the Ceylonese economy has been the failure to achieve food self-sufficiency. The result has been a dependence on food imports consuming up to 75 percent of Sri Lanka's export earnings. This problem has existed for many decades, but until recently, high prices abroad for Sri Lanka's main export products permitted large food imports and the support of a relatively high standard of living. Beginning in the late fifties, export earnings began first to falter and then to stagnate, as the prices for Ceylonese products failed to keep pace with the rising cost of imported goods.

These problems were enormously compounded by the sudden increase in commodity and fuel prices in 1974 and 1975. Sri Lanka's trade deficit rose from \$4 million in August 1973 to \$112 million a year later. The huge expansion in the trade deficit has forced very substantial dependence on short-term credits and foreign assistance in support of Sri Lanka's balance-of-payments position. Credit from U.S. and European banks has expanded rapidly as has aid from the World Bank-led Western Aid Group, which includes the United States, and the International Monetary Fund (IMF).

Foreign aid has helped the Ceylonese in coping with their foreign exchange problems and in development investment activities. Since independence, Sri Lanka has received approximately \$1 billion in external economic assistance, mostly in the form of long-term loans and food sales on concessional terms. The International Bank for Reconstruction and Development and the IMF have taken the lead in organizing an aid effort by a number of developed countries, including the United States. This Aid Sri Lanka group has been active since 1965 but has greatly stepped up its annual aid levels since 1974, in recognition of the magnitude of Sri Lanka's problems, particularly its trade deficit. Current pledges and commitments by this aid consortium have

averaged \$150-\$200 million a year. The Asian Development Bank has also provided significant assistance in the last few years, and some Middle Eastern oil-producing countries have also been important sources of aid.

In addition to seeking foreign aid, the government has moved to cut back on (but not eliminate) welfare benefits, including subsidized foodstuffs and social services, while also vigorously promoting local food production, especially by giving greater incentives to domestic producers and improving the local investment climate. Nevertheless, the classification of Sri Lanka by the United Nations in 1974 as a "most seriously affected nation" in the wake of the global economic upheaval underscores its vulnerability to external forces.

In an effort to diversify Sri Lanka's trade patterns, as well as to open new markets for its products, the SLFP has pursued broader trade and aid relations with Communist countries. A 1952 rubber-rice barter agreement between the People's Republic of China (P.R.C.) and Sri Lanka, under which Sri Lanka exchanges its rubber at favorable rates for rice, which is also provided at advantageous terms, is still in effect. Barter agreements were also signed with other Communist countries and were significant in the sixties but have since been largely abandoned. In fact, trade with Communist countries other than the P.R.C. amounts to only 5 percent of Sri Lanka's total imports and exports. Middle Eastern countries and Pakistan have emerged as major purchasers of Ceylonese tea in the last 3 to 4 years.

Since 1957 the P.R.C. has made available approximately \$75 million for economic aid and is by far the largest Communist aid donor. By contrast, there has been relatively little Soviet aid to Sri Lanka. An aid agreement with the Soviet Union signed in 1958 provided a line of credit amounting to about \$30 million, which has still not been fully drawn down. Much more significant to Sri Lanka in coping with its burgeoning trade deficit has been the great expansion in credit from European and American banks since 1974, a major impact of which has been to increase Sri Lanka's short-term external indebtedness.

FOREIGN RELATIONS

Sri Lanka follows a nonaligned policy characterized by balanced relations with all of the major powers, while seeking to promote its sovereignty and interests through its active role as a Third World spokesman, particularly in the nonaligned movement. Sri Lanka hosted the 85-nation fifth nonaligned summit conference in August 1976 and is serving as chairman of the nonaligned movement, succeeding Algeria, until the next summit in 1979. Sri Lanka is also active in the Commonwealth and in other international fora, especially the United Nations and its agencies, where the Ceylonese have long played a disproportionately influential role. Ceylonese governments have seen this path as the means both of maintaining an independent foreign policy and of promoting Sri Lanka's international interests.

Sri Lanka introduced and continues to promote actively the concept of an Indian Ocean peace zone, perhaps its best-known diplomatic initiative. The two longstanding problems in its relations with its great neighbor, India—the repatriation of Tamil laborers (see PEOPLE) and a territorial dispute regarding the small island of Kachchaitivu in the Palk Strait—were successfully resolved in 1973 and 1974. Sri Lanka has no outstanding bilateral disputes with other countries.

U.S.-SRI LANKA RELATIONS

The United States presently enjoys very friendly relations with Sri Lanka and hopes to encourage them through trade, economic assistance programs, and cultural exchanges.

There have previously been periods when there were problems in our relations. The expropriation of the distribution facilities of two U.S. oil companies in 1962 led to difficulties. When the Ceylonese Government failed to take appropriate steps to pay compensation as required by the Hickenlooper amendment to the Foreign Assistance Act of 1961, the United States suspended economic assistance to Sri Lanka in February 1963. In June 1965 the Ceylonese Government and the two U.S. oil companies signed compensation agreements, and the suspension of eco-

conomic assistance was lifted on July 3, 1965.

In 1970, the present government took some actions which appeared to be directed against the United States. These included the termination of the Peace Corps and Asia Foundation programs and anti-American public statements by some members of the government. Actions of this kind soon ceased, however, and our relations have had satisfactory development since. The United States responded positively to a request addressed to many countries for assistance at the time of the 1971 insurgency in Sri Lanka. In addition, for the last several years the United States has actively supported Sri Lanka's development efforts, while also being mindful of the special affinity existing between the two countries arising out of a common commitment to democratic government.

U.S. policy toward Sri Lanka is based on respect for its independence and sovereignty and acceptance of its nonaligned policy. The United States does not seek a special position in Sri Lanka and appreciates the Ceylonese commitment to good and balanced

relations with all countries. Today, our relations are based on mutual trust and respect and the conviction that our common interests transcend whatever differences we may have.

Commercial Relations

The United States is a good customer for Sri Lanka's tea, rubber, and graphite. Total exports to the United States in 1975 amounted to \$46.5 million, while imports from the United States were \$38 million (including AID-financed commodities). U.S. investment in Sri Lanka is very small, estimated at about \$9 million. Import duties and import controls and restrictions during recent years have seriously limited the market for American consumer goods. While there is a market for capital goods, this has been shrinking due to the lack of foreign exchange. Also, distance, U.S. prices, shipping costs, and credit terms often militate against such sales because of competition from other sources.

U.S. Aid

Since 1974 U.S. aid to Sri Lanka has been provided at a level of ap-

proximately \$32 million a year, about \$22 million of which is in dollar-repayable P.L. 480 (Food for Peace) loans. There has also long existed a people-to-people P.L. 480 program of food for school lunches and expectant mothers, which is operated by CARE. Finally, there are development loans in the field of agricultural development which are used to finance the purchases of commodities from the United States.

Principal U.S. Officials

- Ambassador—John H. Reed
- Deputy Chief of Mission—Raymond L. Perkins
- Defense Attache—Cmdr. Paul Cutcheon, USN
- AID Representative—Thomas Arndt
- Public Affairs Officer (USIS)—Richard von Glotz
- Chief, Political Section—Leroy Debold
- Chief, Economic/Commercial Section—John P. Spillane

The U.S. Embassy in Sri Lanka is located at 44 Galle Road, Colombo 3 (tel. 26211 through 26216).

DEPARTMENT OF STATE PUBLICATION 7757, Released December 1976
Office of Media Services, Bureau of Public Affairs

☆ U.S. Government Printing Office: 1977—241-101/2359

For sale by the Superintendent of Documents, U.S. Government Printing Office, Washington, D.C. 20402
Price 35 cents (single copy). Subscription price: \$23.10 per year; \$5.80 additional for foreign mailing.

**UNITED STATES
GOVERNMENT PRINTING OFFICE**
PUBLIC DOCUMENTS DEPARTMENT
WASHINGTON, D.C. 20402
OFFICIAL BUSINESS

POSTAGE AND FEES PAID
DEPARTMENT OF STATE
STA-501



Third Class

D. List Cabinet
and Bio-data

Sri Lankan Government Officials

- * President -- Mr. J. R. Jayawardene
- *** Prime Minister -- Mr. R. Premadasa
- * Minister of Finance and Planning -- Mr. Ronnie de Mel
- Minister of Plan Implementation -- Mr. J. R. Jayawardene
- Minister of Defense -- Mr. J. R. Jayawardene
- Minister of Local Government, Housing and Construction -- Mr. R. Premadasa
- Minister of Public Administration and Home Affairs -- Major Montague Jayawickreme
- Minister of Education -- Mr. Nissanka Wijeyeratne
- Minister of Higher Education -- Mr. Nissanka Wijeyeratne
- Minister of Cultural Affairs -- Mr. E.L.B. Hurulle
- ** Minister of Agricultural Development and Research -- Mr. E.L. Senanayake
- Minister of Fisheries -- Mr. Festus Perera
- Minister of Food and Cooperatives -- Mr. S.B. Herat
- Minister of Foreign Affairs -- Mr. A.C.S. Hameed
- Minister of Health -- Mr. Gamini Jayasuriya
- Minister of Industries and Scientific Affairs -- Mr. Cyril Mathew
- Minister of Power and Highways -- Mr. D.B. Wijetunga
- Minister of Posts and Telecommunications -- Mr. D.B. Wijetunga
- Minister of Justice -- Mr. E.W. Devanayagam
- Minister of Labour -- Capt. C.P. Seneviratne
- Minister of Parliamentary Affairs and Sports -- Mr. Vincent Perera
- ** Minister of Plantation Industries -- Mr. M.D.H. Jayawardane
- Minister of Social Services -- Mr. Asoka Karunaratne
- Minister of Textile Industries -- Mr. Wijeyepala Mendis
- ** Minister of Trade and Shipping -- Mr. Lalith Athulathmudali
- Minister of Transport -- Mr. M. Mohamed
- ** Minister of Rural Development -- Mrs. Wimala Kannangara
- * Minister of Lands and Land Development -- Mr. Gamini Dissanayake

* Minister of Mahaweli Development --- Mr. Gamini Dissanayake
Minister of Rural Industrial Development --- Mr. S. Thondaman
Minister of Youth Affairs and Employment --- Mr. Ranil Wickremasinghe
Minister of State for Tourism, Information and Broadcasting --- Mr. Anandatissa
de Alwis

- * Officials with whom you are likely to have a formal meeting. Biographical sketches are attached.
- ** Officials who may be present in formal meetings or in part of the field trip. Biographical sketches are attached.
- *** Officials who may like to have substantive discussions with you even though not scheduled. Biographical sketches are attached.

BIOGRAPHICAL SKETCHES

1. Junius Richard Jayawardene, President and Minister of Defense and of Plan Implementation.

Born on September 17, 1906. He attended the Royal College, Colombo and Ceylon University College and graduated from Ceylon Law College as an advocate. Mr. Jayawardene practiced as an advocate of the Supreme Court of Ceylon for a few years before entering politics. He joined the Ceylon National Congress and was Secretary of the Congress from 1940 to 1947. Mr. Jayawardene entered the Ceylon State Council in 1943 when he was elected as the member for Kelaniya in a by-election. When Ceylon's Parliament was formed in 1947, he was re-elected by the Kelaniya constituency. He was a member of the Parliament, representing Kelaniya from 1947 to 1956 and again in March 1960. Since the July 1960 Elections, Mr. Jayawardene has held seats representing the constituencies of Colombo South and Colombo West. In the 1977 Elections, he won by a resounding majority.

President Jayawardene has held key positions in several governments since 1947 when he was appointed Minister of Finance in the First Parliament, a position he held until October 1953. He was Minister of Agriculture and Food from 1953 to April 1956. When the UNP briefly returned to power from March to July 1960, he was again appointed Minister of Finance. In the National Government formed by Mr. Dudley Senanayake after the March 1965 Elections, Mr. Jayawardene was appointed Minister of State and Parliamentary Secretary to the Prime Minister and Minister of Defense and External Affairs. After the General Elections of 1970, Mr. Jayawardene became a leader of the opposition. With the death of Mr. Senanayake in April 1973, Mr. Jayawardene assumed the leadership of the United National Party. In the international field, Mr. Jayawardene is perhaps best known as the co-author (with Mr. Percy Spender, the Australian Foreign Minister) of the Colombo Plan.

Appointed Prime Minister after the 1977 election victory, he became President with full executive powers in February, 1978, through a constitutional amendment.

2. Ranasinghe Premadasa, Prime Minister and Minister of Local Government, Housing and Construction.

Mr. Premadasa, 54, was educated at St. Joseph's College, Colombo, and began his political career as a member of the Ceylon Labour Party. He was elected to the Colombo Municipal Council in March 1950 and was Colombo's Deputy Mayor in 1955. Joining the UNP, Mr. Premadasa took a keen interest in the party trade union activities and played a major role in winning working class support for the party. He was first elected the Third MP for Colombo Central in March 1960 but was defeated at the next elections in July the same year. He was, however, elected the Second MP in 1965 and became the First MP in 1970. He was appointed Parliamentary Secretary to the Minister of Local Government and to the Minister of Broadcasting and Information in 1965. He was appointed Minister of Local Government in 1968. He was also the Chief Government Whip during the term of the Sixth Parliament. He was appointed Deputy to the Leader of the UNP in 1976. He has also earned a name for himself as a popular Sinhala novelist.

3. Ronnie de Mel, Minister of Finance and Planning.

Born April 11, 1925, Mr. de Mel received his education mainly in Sri Lanka obtaining an Honour's degree in History from the University of Sri Lanka in 1947. He entered the Ceylon Civil Service in 1948 and subsequently served as Commissioner of Co-operative Development and Director General of Broadcasting in Sri Lanka. Resigning from the Civil Service he joined the SLFP party and unsuccessfully contested a seat in Parliament in 1965 but managed to enter Parliament in a by-election in 1967. In the 1970 elections he retained the seat by a majority of over 6,000 votes. Until he left the SLFP to join the UNP in 1975 Mr. de Mel was an advocate of SLFP policy serving on the Parliamentary Committees on Company Law Reform and Land Reform. Not receiving a Ministry in the SLFP is thought to be the reason for his "crossing the floor" to the UNP. Mr. de Mel has also served as a member of the Board of Directors of several private sector firms and was a member of the Sri Lankan delegation to the Meeting of the Inter-Parliamentary Union on World Production and Trade.

In the 1977 Elections, he won a majority of over 9,000 votes, while receiving about 56% of all votes in Devinuwara. He is especially known as a skillful speaker.

4. Gamini Dissanayake, Minister of Lands and Land Development and of Mahaweli Development.

The UNP discovery of the 1970 General Election, Mr. Dissanayake, 36, was a prominent figure on the opposition benches of the last Parliament. The son of Mr. Andrew Dissanayake, a SLFP Member of Parliament and Parliamentary Secretary of the First Bandaranaike Government, he was educated at Trinity College, Kandy, and is a lawyer by profession. One of the few UNP candidates to win at the 1970 polls, Mr. Dissanayake proved himself a seasoned campaigner when he retained the Nuwara Eliya seat at a subsequent by-election. He is a trade union and youth league worker and represents the Nuwara Eliya - Maskeliya constituency.

5. Mahabalage Don Henry Jayawardane, Minister of Plantation Industries.

A seasoned UNP member, Mr. Jayawardane was Junior Minister of Finance in the late Mr. Dudley Senanayake's first Government when he was elected MP for Horana. He has held a series of cabinet posts since 1954 when he was made Minister of Finance in Sir John Kotelawala's cabinet. Since 1956, Mr. Jayawardane has had a chequered career having lost the Horana seat in 1956 and March, 1960, and the Kottawa seat in July, 1960. In March, 1965, Mr. Jayawardane returned to the legislature and became Minister of Scientific Research and Housing. He was Joint Secretary of the UNP in the 1965 polls.

6. Edward Lionel Senanayake, Minister of Agricultural Development and Research.

Mr. Senanayake, 58, was educated at Trinity College, Kandy and later at the Ceylon University College where he obtained a degree in Economics. He later embarked on a planting career. He took to local government politics quite early in his life and was elected to the Kandy Municipal Council in 1943. He was elected Deputy Mayor of Kandy in 1946 and became the youngest Mayor in Sri Lanka in 1950. He held this office on several later occasions too.

Mr. Senanayake was first elected to Parliament from Kandy in 1952 but was unseated by an election judge. Following an unsuccessful effort in 1956, he has represented Kandy continuously since March, 1960. He was also the Minister of Health from 1968 to 1970. He has represented Sri Lanka at the UN General Assembly Sessions and at Inter-Parliamentary Union Conferences.

7. Lalith Athulathmudali, Minister of Trade and Shipping.

Mr. Athulathmudali, 42, who won the Ratmalana seat in his maiden attempt, had an illustrious academic career. He is an alumnus of Oxford University's Jesus College, where he obtained his B.A. in Jurisprudence and also his M.A. degree. At the age of 22 he was called to the Bar. From Gray's Inn, he won a scholarship to Harvard University. He is well known as a powerful speaker. At Oxford University, he was the President of the Union. He is also an advocate at the Supreme Court of Sri Lanka and a Barrister of the Australian Bar. Mr. Athulathmudali has been a guest lecturer in Law at several Universities including Edinburgh. He was among the jurists chosen to start the Faculty of Law at the University of Singapore. A public school athlete, he was the all-island athletic champion.

8. Wimala Kannangara, Minister of Rural Development

Mrs. Kannangara commenced her political career at village committee level and was the chairman of two village councils, i.e., Panakawa and Gamaldolahapattu. In 1956 she contested the Dedigama seat, which was vacated by Mr. Dudley Senanayake (Mr. Senanayake did not contest in the 1956 election), but was defeated. In March 1956, she contested the Galigamuwa seat and won. In the 1960 and March 1965 elections, she again returned to the Galigamuwa seat. She became Deputy Minister of Health in Mr. Dudley Senanayake's Government in 1965.

9. Dr. W.M. Tilakaratna, Secretary, Ministry of Finance and Planning.

Born in 1927, he received a B.A. in Economics with honours from the University of Ceylon in 1949 and a Ph.D. from the London School of Economics in 1957. He has had a long career with the Central Bank of Ceylon which he joined in 1953 and was appointed its Senior Deputy Governor in 1972. From November, 1972, to June, 1976, he served as Alternate Executive Director of the IMF. Thereafter, he resumed his duties as Senior Deputy Governor of the Central Bank of Ceylon. He was appointed Secretary, Ministry of Finance and Planning, in early 1978.

E. Topics for
Discussion

Sri Lanka - Topics for Discussion

Background

1. Your program provides the following opportunities for substantive discussion with:

- (i) Mr. J.R. Jayawardene, President of Sri Lanka, on the Government's strategy for development over the next five years;
- (ii) Mr. Ronnie de Mel, Minister of Finance and Planning, on the more detailed aspects of Sri Lanka's Development Program; and
- (iii) Mr. Gamini Dissanayake, Minister of Lands and Land Development and of Mahaweli Development, on the Accelerated Mahaweli Development Program.

In addition Mr. Premadasa, the Prime Minister, may seek an opportunity to raise with you the question of Bank assistance for Urban Development in the Greater Colombo Area. Points which you may wish to address during these discussions follow. Biographical information on the above persons is given in Section D of this briefing.

2. In all your discussions with Government officials, you may wish to emphasize the two basic requirements facing the Government if economic activity is to be revived in Sri Lanka: (i) more efficient use of resources; and (ii) an increased level of investment, both public and private. The new Government under President J.R. Jayawardene is making impressive progress with the first of these requirements. A comprehensive reform program has been initiated which is designed to dismantle administrative controls over resource allocation, restore realistic relative prices and provide greater encouragement for extended private sector activity. Under the program, Government has already liberalized the external trade and payments system, lifted many domestic price controls, and revamped the tariff and domestic indirect tax structure.

3. To strengthen its capacity to finance an increased volume of investment, the Government has limited food subsidies to only the poorest half of the population and reduced subsidy rates for fertilizer, flour and public bus transport. However, the total burden of resource transfers and subsidies (including a recently-instituted unemployment dole) remain large relative to Government spending.

4. Alongside the above policy reforms, a Medium-term Development Program for 1979-83 is in the course of preparation with investment targetted to rise substantially from the levels under the previous Government. In aggregate, investment in 1971-76 was, in real terms, below that of a decade earlier. Within the Program, the Government has so far identified three large projects on which it intends to place major emphasis: (i) the accelerated Mahaweli Ganga Development Program; (ii) development of an export processing zone; and (iii) the Greater Colombo urban renewal and housing schemes.

5. In summary, the progress made by the Government so far is clearly encouraging. In support of the Government's initiatives, the Aid Group at its last annual meeting in May increased total aid indications by 53%, from US\$246 million in 1977 to US\$377 million in 1978. Nevertheless, major additional steps are needed.

September 20, 1978

I. President
Jayawardene

Commendable extraordinary pol + econ changes in 15 mos

Changed Consti
Replanning local govt
Changed leadership of public sector
Liberalized controls
Lifted price controls
Unified exchange
Reduced subsidies

Sri Lanka - Topics for Discussion

Mr. McNamara's Dinner Meeting with President J.R. Jayawardene

(7:30 p.m., Thursday, October 12)

Time constraints on both your schedule and Mr. Jayawardene's schedule have at this time limited your meeting with the President to a dinner on the night of your arrival.

1. Resource mobilization
What are their plans
How to further cut subsidies
to minimize criticism in West:
upward bias
stabilizing prices
inc. foreign
What are their plans

2. There are a number of important issues which the Government must resolve in preparing and implementing its development strategy. Although some of these issues may have been discussed during the Annual Meeting, it is important that your discussions with him focus on these issues, since decisions lie to a substantial extent with the President himself.

2. subsidies
need to support but just decision
focus on sales with only
long-term benefit could have
negative impact

Resource Mobilization

3. A major need in the implementation of the Medium-term Development Program will be to step up resource mobilization over and above the measures already undertaken. It would be useful to explore with the President the extent to which the Government would in fact move in this direction. The task before the Government is complicated by the likely deterioration of the terms of trade for tree crops, particularly tea, which will have a depressing effect on export taxes, which amount to more than half of total Government revenue, which in turn accounts for a high 21% of GNP at market prices. Thus, the Government must face the major issue of how to effect further cuts in subsidies and transfers (33% of total revenue), of which net food subsidies are the largest (19% of revenue), without eroding the considerable social gains which it has achieved and generating political unrest.

3. concerned re 5% devaluing
R 112 (current price)
3. How will prepare program with
early benefits to other sectors
com. finance

4. It is our assessment that the necessary further cuts can be effected with minimum political risk if the Government is seen at the same time to be succeeding in expanding production, stabilizing prices and improving the employment situation. You may wish, therefore, to emphasize the importance of such tangible progress being made in the short run. Also, although the new Government has been in power only about one year, you may wish to inquire of the President his views on the progress so far and what further steps the Government intends to take in the immediate future.

4. How will medium term Dev. Program
stimulate private inv. + growth

Sectoral Balance

5. Given the need to dramatize Government commitment towards significant improvement being made, the major appeal of projects such as those included in the Mahaweli Program is their high visibility. Less appreciated, however, is the fact that the full benefits from such projects can only be expected beyond the medium term. You may wish to commend the Government on its recognition of the need to ensure that the level of resources allocated to the Government's high priority, but long gestating programs must be balanced with the competing claims of projects designed to rehabilitate and revitalize the economy in the intervening period. It would be useful, however, to express our concern to the President on the urgent need to strengthen the machinery for identification and preparation of new projects which ensure an early flow of benefits in terms of both output and employment.

5. How to meet brain-drain
technical skills

6. Can be with social services
in form of research + other
invest plans -

24-28 6.
69-73 76.
74-78 140.
79-83 369.
76 75
77 33
78 33
79 55
80 99

6. With respect to the Mahaweli Program (for details see F-5-b) itself, you may wish to commend the President for adopting the principle that, given its absorptive capacity, expenditures on the Program during the next five years will not exceed a ceiling of Rs 8 billion in 1978 prices or Rs 11 billion in current prices.

Private Sector

7. Given the dominance that the public sector has enjoyed in recent years, the increased role which the new Government envisages for the private sector will require that the policy environment for the purpose be explicitly established. It would be useful to ascertain from the President his views on how the Medium-term Development Program will address this need. In this connection the President may refer to his plans for the Greater Colombo Economic Commission information on which is provided in F-5-c. Although Bank assistance may be requested on this program, we have not taken any position pending a full review both within the Bank and with the Government of the findings of our recent Industrial Sector Mission Report.

Proposed Resident Mission

8. Attached please find a copy of Mr. Hopper's September 27 memorandum to you concerning the Government's request that we establish a Resident Mission in Sri Lanka. President Jayawardene is very likely to raise this subject with you.

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara, President

DATE: September 27, 1978

FROM: W. David Hopper, Vice President, ASNVP *WDH*SUBJECT: SRI LANKA - Proposal to Establish a Resident Mission

1. Upon return from my mission to Sri Lanka in March, I reported to you that President Jayawardene had requested that we establish a Resident Mission in Colombo in order to provide the on-the-spot liaison needed to support the many development activities that the Bank and other donors have underway or in the planning stage, some of which the Bank has been asked to provide coordination. At the time, I recommended to you that we weigh the request carefully. Now, having reviewed the developments in Sri Lanka and extended our conversations with other donors, I am writing to recommend that we open an office in Colombo staffed with one person.
2. The new Government, which came to power in July 1977 with an unprecedented majority, inherited an economy which had become nearly stagnant. The productive sectors had been severely neglected and resource misallocation was pervasive--the result of price distortions, a dual exchange rate, and import and exchange controls. At the same time, welfare expenditures, subsidies and transfers were being financed on a scale that left little public money for productive uses. A corollary of this poor performance was the failure to generate adequate employment opportunities---a severe problem in itself, but compounded by inflationary pressures fueled by excessive deficit financing.
3. The new Government moved quickly, not only to generate solutions to immediate problems, but also to begin the resuscitation of the economy and lay the foundation for sustained growth. It has gone about the task impressively. Indeed, what struck me most strongly during my visit was the enthusiasm, energy and earnestness of purpose that President Jayawardene has brought to bear on the range of problems his country faces. Within two to three months after taking office, a number of important policy changes were initiated in concert with the IMF which effectively recast the basic ground rules on which the economy runs--changes which only a short while before would have been regarded as political suicide. These changes included widespread dismantling of controls over resource allocation, reform of the external trade and payments system, unification of the exchange rate (reflecting an effective devaluation of 46% over the official rate), reduction by half of those eligible for food subsidies, and an increased role for the private sector. The response of the economy to date has been encouraging, and the Government expects a major improvement in the budgetary current account surplus in 1978, thus enabling a sizable increase in the allocations to this year's capital budget.
4. Alongside these initiatives, the Government began work recently, in consultation with the Bank, on a Medium-term Development Program--an exercise to be completed over the next 12-15 months in concert with the results of a number of major sector surveys. A principal objective of this work is to determine the resource mobilization effort required for the Government's priority investments over the next five years. An equally important objective is to establish the proper balance of expenditures between high-priority, long-gestation programs, and other important projects both for generating immediate

employment and production increases, and for maintaining and rehabilitating existing works. At the same time, and without pre-empting the outcome of the Medium-term Development Program's preparation, the Government initiated action on its highest priority investment--the accelerated implementation of the Mahaweli Ganga Development Program, an ambitious irrigation/settlement scheme.

5. In sum, while many additional measures remain to be taken to confront adequately the many problems still before the Government, we are encouraged by the bold actions it has taken so far--a view shared by other members of the Aid Group who responded to the Government's initiatives last May by increasing their aid indications by 53%, up from US\$246 million equivalent in 1977 to US\$377 million in 1978. And we are now engaged with the Government in a far-reaching program of sector studies and assistance in medium-term development planning that should establish the foundation for Government economic action over the next several years.

Efforts for Increased Bank Group Assistance

6. Although the preparation of the Medium-term Development Program is still at an early stage, it is certain that, if the Government's development efforts are to be successful, there will be a critical need for larger resource mobilization, both from local sources as well as from abroad. Recognizing the practical constraints the Government faces in mobilizing domestic resources, President Jayawardene has requested the Bank Group to take the lead in securing the necessary funds. Within the resources available to us, we have responded to this request. Our Economic and Sector Work Program was recently expanded to permit us to enlarge our advisory capacity. In May/June, an investment program mission visited Sri Lanka to consult with the Government in the preparation of the Medium-term Development Program. An economic mission is scheduled for June 1979. To assist critical sectors, an industrial sector mission visited Sri Lanka in March/April, and a comprehensive survey of the agricultural sector is scheduled for early 1979. In order to assist in expanding the project pipeline, a Multi-Sector Programme of Project Preparation (Umbrella) grant was approved by the UNDP in April for execution by the Bank Group. While other sources of external aid (e.g. CIDA and ODM) are also providing significant assistance in this area, we are, in our capacity as Chairman of the Aid Group, actively meeting our mandate to coordinate external activities. To discharge our full responsibility will require a strengthening of our capacity to support these many endeavours. Indeed, even greater efforts on our part will be required in the future to handle an increased burden of economic and sector work, project preparation and supervision, technical assistance, together with Aid Group work and co-financing activities.

The Mahaweli Ganga Development

7. The need to strengthen our support capacity is also being increasingly heightened by our agreement with the Government and aid donors to serve in a coordinating role for the accelerated Mahaweli Program. This Program now includes six major irrigation/settlement projects (out of a total of 12) which will irrigate about 340,000 ac of new land, generate nearly 400 MW of hydro-power

and settle over 500,000 people on irrigated farm land. The projects are to be implemented concurrently, in as short a time as possible, with financial and technical assistance from as many as ten external aid agencies. President Jayawardene has staked a good deal of his personal and of his party's reputation on the acceleration of the Program (originally to be phased over 30 years), and many parts of his Government have been mobilized around its implementation. When I arrived in Sri Lanka in March, I found the Government in the midst of a flurry of negotiations for assistance with several potential donors.

8. In my association with the Mahaweli Program over the last nine months, it has become increasingly clear that we will have to run fast to catch up to and stay with this very energetic Government. As a start, we have engaged a French consulting firm (SOGREAH) with UNDP funds to serve in Colombo as our liaison, as well as to provide the Government with highly specialized technical assistance. In addition, we are planning to hold meetings regularly in Sri Lanka (every 4 to 6 months) consisting of Government officials and donor country representatives, and their respective consultants, to exchange information about the status of their activities in the several projects. The first such meeting, which took place in July, was considered a success by all participants. To reinforce these local meetings, we are planning to hold a separate meeting on the Mahaweli Program in conjunction with the next Aid Group meeting in early 1979. In the interim, as I reported to you in my memorandum of July 21, we have arranged for a Bank staff member to visit Sri Lanka on mission status during October-January to provide the on-the-spot support we feel is required for the Mahaweli Program, as well as our other operations.

Conclusions and Recommendation

9. After re-examining the implications these activities have had on our present staff capacity, as well as the implications of the level of activity we would like to achieve, I have concluded that we are rapidly reaching the limit in the amount of assistance we are able to provide operating from Washington, D.C., only. Although the number of missions to Sri Lanka doubled in FY78 to 45 (up from an annual average of 22 during FY74-77), my colleagues and I believe our support capacity still falls short of being adequate. After carefully reviewing our obligations and the Government's needs, I do not feel an increase in our headquarters' staff would necessarily provide the type of coverage we need. Instead, I feel that one man in residence would be enormously helpful in providing the continuity of information and the daily contacts necessary for expanding our operations in Sri Lanka and for discharging more fully our responsibility as Chairman of the Aid Group, and Coordinator of the accelerated Mahaweli Program.

10. Although a direct parallel between Sri Lanka and Nepal cannot be drawn, our experience in Nepal clearly indicates that an energetic and mature Resident Representative, who can win the confidence of the Government's senior administration, can contribute substantially towards achieving our objectives. Prior to FY74, after five years of lending to Nepal, the Bank Group had achieved a commitment level of only US\$20 million, with annual disbursements averaging about US\$300,000. Five years later, after establishing a one-man Resident Mission in 1974, our commitments stood at US\$163 million, with disbursements reaching US\$11 million in FY78 alone, or nearly the total of all previous years. Moreover, there is now a reasonably firm pipeline of projects suitable for Bank financing

of about US\$200 million over the next three years, considerably in excess of the likely allocation of IDA funds for Nepal. A feature of these achievements is that the cost of maintaining the Mission was only about US\$100,000 p.a., which my staff and I believe was more than offset by time savings attributable to increased mission efficiency arising from the preparatory work of the Resident Representative. Based on this record, I think the most efficacious means for making similar achievements in Sri Lanka would be to establish a Resident Mission in Colombo as soon as possible.

11. The above program management factors weigh heavily in favor of establishing a Resident Mission in Colombo. However, there is perhaps an even more important, although less tangible consideration. It concerns the need to demonstrate the Bank Group's support for the Herculean efforts that the new Government is undertaking at this time. While Sri Lanka has long been admired for its successes in the social sectors, there has been concern that its poor performance in the productive sectors would eventually erode the social gains it has achieved. In the face of enormous political constraints, the new Government has precious little time to show results in its efforts to revitalize the economy. Failure to do so would surely return the country to the dismal policy environment of the early 1970's and, regrettably, reinforce the argument of those who say that growth and equity are mutually incompatible. In this context, it should be recalled that, at the last CPP Review, it was agreed that if the Government of Sri Lanka should implement needed economic reforms, then IDA would be prepared to reconsider its lending program with a view toward expanding its assistance. Establishing a Resident Mission would be a meaningful gesture symbolizing the Bank Group's support for the new Government's policy endeavors, while, at the same time, providing tangible technical assistance for Sri Lanka.

12. In light of the above arguments, I recommend that: (i) the Bank Group establish a Resident Mission in Sri Lanka, effective January 1, 1979; (ii) one additional professional staff position be made available to the South Asia Programs Department in order for it to fill the new position by January 1, 1979; and (iii) an FY79 budget supplement in the amount of US\$70,000 be added to the Department's budget so that it can establish the Mission and operate it during the second half of this fiscal year.

cc: Messrs. E. Stern, VPO
J. M. Kearns, L. H. Berlin, OPD
K. G. Gabriel, PAB
R. A. Clarke, PER
Picciotto, ASP
Dunn, Shibusawa, ASA
Street, ASNVP

GAMcBride/WDHopper:jet

2. Prime Minister
Premadasa

Sri Lanka - Topics for Discussion

Mr. McNamara's Meeting with Prime Minister, Mr. R. Premadasa

(7:30 p.m., Thursday, October 12)

Although no meeting has been arranged between you and Mr. Premadasa, it is almost certain that he will seek you out and press his case for Bank assistance for the Greater Colombo Urban Renewal and Housing Schemes. In this case you may wish to point out that IDA is already assisting an ongoing Water Supply Project in the Greater Colombo area, and a Sewerage Project is being prepared under that Credit. In addition, an appraisal will have just been completed for a proposed Road Maintenance and Road Transport Project, part of which will support bus transport in the Colombo area. We have declined further assistance because of: (i) the need for Sri Lanka itself to apply its limited resources to the development of its productive sectors, particularly agriculture, as well as directly supporting infrastructure, and (ii) the relative lack of major urban problems in Sri Lanka. Further details on this issue are provided in F-5-d.

Review of meeting with -
Full list of work & prior capacity -
Main new proj: Mahaweli: 5 yrs: 50000 acres with 450000 head of cattle, rubber, coconut, rubber families
rehab & replanting of tea, coconut, rubber
diversify: part of tea
plus hydro-pow: 400 MW
guess on Kotmale: 1 CB + South India (+ WB?) (or Sweden)
or Sweden
The pol life of their govt is tied up with the speed of the proj
The other priority proj considered by Combank -
1. Free trade zone
2. Housing Proj (100000 houses in 5 yrs)
3. Greater Colombo Scheme
will approve loan to finance
4) Shift Port etc to new effects
5. Fisheries
6. Telecommunication
7. Water supply + sewerage
8. Transportation
9. Integrated rural devel

3. Min. of Fin.
& Plan

Comment for:

Sri Lanka - Topics for Discussion

Mr. McNamara's Meeting with the Finance Minister Mr. Ronnie de Mel

(6:30 p.m., Thursday, October 12)

(Meeting subject to timely arrival of party from Bombay)

1. In anticipation of the points you will raise with the President you may wish to spend some time reviewing in some detail the major issues concerning the Medium-term Development Program (for details see: F-5-a).

- (a) Resource Mobilization, - increase by reducing sub + make available by off-hand prod, state power, + inc. supply
 - (b) Sectoral Balance, -
 - (c) Private Sector Revitalization. - what plans for
- 2. inc. of sub + make available by off-hand prod, state power, + inc. supply*
+ prof. of new, but return prog.

2. In addition, you may wish to raise with the Minister the question of how the Government plans to overcome the serious shortage of trained manpower; a shortage which is critically affecting the Government's ability to execute its overall development program. This shortage partly reflects inadequate training programs and partly, the accelerating migration of skilled and educated manpower to Africa and the Middle East.

3. Within the Government, existing capacity is especially inadequate for effective project preparation, coordination and implementation. At the center, the Ministry of Finance and Planning suffers from a severe overall shortage of professional staff in its planning wing, and in the External Resources Department which deals directly with aid donors and financing institutions. We should emphasize the importance of augmenting the planning capacity of the Ministry of Finance and Planning, and strengthening the project preparation units in the key operational Ministries.

4. The Government is fully aware of the efforts it must make to improve its absorptive capacity, but points out that significant improvement cannot be expected in the short run because of its severe shortage of experienced staff. In response to this argument, you may wish to stress that:

- (a) surely there must be a surfeit of experienced staff previously engaged in the administration of the former Government's economic control programs who could now be redeployed to more productive development functions;
- (b) an examination of the tasks of key operational Ministries should indicate possibilities for hiving off major pieces of work to private consultants and contractors; and
- (c) it appears that more effective use could be made of technical assistance staff already in position, as well as greater use of currently under-utilized UNDP, CIDA and ODM technical assistance funds.

4. Min. of Land
& Dev. & Mahaweli

1. How well they settle the newly arriving lands

SRI LANKA: TOPICS FOR DISCUSSION

Mr. McNamara's Meeting with Mr. Gamini Dissanayake,
the Minister of Lands and Land Development
and of Mahaweli Development

(8:00 a.m. - 5:00 p.m., Friday, October 13)

You will have an extended opportunity to discuss the Accelerated Mahaweli Ganga Development Program with Mr. Dissanayake, who is expected to accompany you on your field trip.

The issue of the balance to be struck between the Mahaweli Program and other priorities has been outlined in the briefs provided for your discussions with the President and the Minister of Finance. A detailed background note on the program itself is provided in F-5-b.

You may wish to raise the following specific issues with Mr. Dissanayake:

(a) Cost Recovery - As you know, we have been discussing this issue with the Government since the mid-1960s. Until recently, the Government had not complied with existing agreements on cost recovery in conjunction with three ongoing IDA credits -- the Mahaweli Ganga Development Projects I and II and the Tank Irrigation Project I. In August, we learned that the Government had issued an instruction to levy water charges under the existing Irrigation Ordinance. The charges are in accordance with the schedules as documented in the agreements for the above projects. The charges are low, however, representing only about 25% of what the Government should be spending on the operation and maintenance of its irrigation systems. You may wish to inquire about (i) the Government's schedule for the actual collection of water charges, and (ii) the Government's intentions for increasing the water charges in the near term.

(b) Kotmale Project - The feasibility study for this predominantly hydroelectric power project is more advanced than for most other projects in the Mahaweli Program. Thus, for political reasons, the Government wishes to demonstrate early results and proceed immediately with the construction. The Government has requested Sweden to provide financing for the project. Sweden has responded by allowing Sri Lanka to use its normal commodity grant funds for the civil works construction (about US\$47 million equivalent during 1978-80), with the prospect of slight increases in Swedish Aid resulting from annual reviews of its 3-year allocations.

In mid-September, SKANSKA, a Swedish hydropower contractor and member of the Swedish Hydropower Group, submitted a proposal to the Government of Sri Lanka which would permit construction of preliminary works (access roads, bridges, campsite, etc.) to start by January, 1979, followed by the construction of the main civil works (dam and underground power plant). SKANSKA feels sufficient documentation exists for making cost estimates, and that final designs and specifications for the dam, power plant, turbines, generators, etc. would be completed during the construction by the Government assisted by Swedish consultants. One hydroelectric unit of 50MW would be functioning by 1983, with remaining two

units in 1984. Contractual arrangements would be negotiated on a cost plus fee basis, with a bonus if the final cost and construction time are lower and a reduction if the cost and time are higher.

We have several concerns with this situation which have been conveyed to the Government and which you may wish to raise with Mr. Dissanayake.

- The Swedish aid arrangements breach the agreement at the May Aid Group Meeting that donors' assistance for the Mahaweli Program should be in addition to their normal aid flows.
- The amount of aid that Sweden can be expected to provide out of its 1978-80 grant allocation (US\$47 million), is less than half of what is required for the civil works construction (US\$105 million)-- and then US\$55 million will be needed for electro/mechanical equipment. Regarding the possibility of cofinancing, it will be extremely difficult to secure such financing from a non-commercial external aid agency since the project would already be identified with Sweden without competitive bidding.
- Our overriding concern with the Government's intention to negotiate a contract with SKANSKA is that the final design, specifications and tender documents are not yet available. Without these documents, and without competitive bidding, our experience in such cases is that there is a strong tendency for the contractor to quote high rates and prices, which in turn, leads to a higher construction cost than otherwise expected, and that, under these conditions, the contractor has the upper hand. Moreover, our experience is that contracts negotiated with insufficiently prepared documents and under non-competitive conditions leave the door open for subsequent litigation and protracted delays.

We have called the Government's attention to these concerns. In addition, we would urge you to stress the importance of Sri Lanka moving cautiously in this matter, keeping in mind (i) the Swedish grants will be available in any case, whether or not SKANSKA is involved and these grants might better be used for commodity imports which would provide the Government flexibility in managing its balance of payments, and (ii) it would be easier to obtain additional funds for the Kotmale Project through cofinancing arrangements if the design, tender documents and specifications are prepared and put up for international competitive bidding.

(c) Implementation of Mahaweli Project II - A mission visited Sri Lanka in August/September 1978, to supervise this Project. The mission, which included representatives from the cofinancing countries (Canada, Netherlands, U.K. and U.S.), found that in keeping with the Government's decision to significantly accelerate the implementation of the Mahaweli Program, the Government had decided to reduce the implementation period for this Project from five years to two. As a result, the implementing agencies are moving with breakneck speed.

The mission found that the quality of work in the Project has been adversely affected by the acceleration. The Project is being carried out without adequate planning, supervision and coordination, and the lack of sufficient equipment and experienced technical personnel (drawn off for the preparation of other projects in the Mahaweli Program), are resulting in poor construction techniques and low quality of work (e.g., poor compaction in backfilling canals, inadequate equipment maintenance, and no ripping in land clearing, thus rapid regrowth). Other problems uncovered by the mission included (i) large civil works contracts are being negotiated (rather than let by local competitive bidding as agreed), (ii) the position of Resident Project Manager is vacant, (iii) inattention to efforts to improve water management practices and conservation, (iv) premature settlement without sufficient social infrastructure and agricultural support and extension services, and (v) crop losses due to construction are not being compensated.

The Mission discussed this situation in detail with Government officials and left its comments and recommendations with the Government in writing (attached). In addition, the Government wrote a letter to the Mission explaining the remedial actions it proposes to take. Whereas we feel the Government intends to squarely address the situation, you may wish to discuss these problems again with the Minister, emphasizing that, unless a more orderly and considered approach to project implementation is adopted, the Government's credibility with its cofinanciers could be seriously jeopardized.

SRI LANKA
MAHAWELI GANGA DEVELOPMENT PROJECT II

Comments and Recommendations of the August/September 1978 Review Mission

At the September 14, 1978 meeting in the office of the Director General, Mahaweli Ganga Development Authority to discuss the IDA/co-financing countries review of the project, Mr Panditharatne requested that the Mission's views and recommendations on project implementation progress and work quality be submitted in written form for review and guidance on future work. With the concurrence of Mr Shibusawa, Chief Programs Division (IDA), the following observations and recommendations are made:

Observations:

1. Since the project was formulated with the view that it would serve as a model to be replicated in other command areas to be developed in the Mahaweli Ganga Program, the project works should be well planned and constructed to ensure successful development. The Mission's field review did not substantiate that this is being done. It is the Mission's view that vital planning has not taken place and work activities are not being properly coordinated, resulting in work being poorly constructed and improperly timed. Some work is not being done and modifications are being made which are detrimental to the project plan.

Systematic planning has only recently been started and is far behind construction activities. However, this planning as now being done will provide the basis for sound management and proper scheduling of the work and additional staff for the Planning and Evaluation Unit should be provided.

2. Quality control of all canal construction work is needed to ensure that canal operation and seepage losses are minimized and that maintenance costs of the irrigation system will not be excessively high. Also, plans are being made to settle farmers on the farms without the necessary social infrastructure (including the hamlets and village centers) being undertaken and without ploughing to assist in conservation bund construction and land development.
3. The Mission believes one of the most serious detriments to successful quality control and project coordination is the lack of centralized control of work in the project area. A Senior Resident Project Manager with the power to enforce proper work scheduling and adequate construction quality from all participating agencies is urgently needed. This post is now vacant. The position of Resident Project Manager was mutually agreed at the time of negotiations and is reflected in the credit agreement. The RVDB has undertaken development in about one half of the project area with seemingly complete autonomy from MDB. The RVDB and the Army are

working without written contracts (which should have been submitted to IDA for review before such contracts were awarded). There also appears to be a serious lack of control at the field level in accounting for work progress and expenditures for all contracts.

4. The Mission noted the lack of inspection staff, particularly staff with authority to enforce work standards and quality control. There also is a lack of coordination of equipment orders with project needs. (Chain saws, air shipped by CIDA for use in clearing work have lain idle in Colombo for 3 months and farm tractors have been ordered without implements.)
5. Public relations with the farmers should be improved and problems exist in the flow of information from the MDB head office to the field and the feedback up the chain of command.

Recommendations:

A) Top Priority Actions Recommended

- 1) All work should be put under the direct responsibility of MDB and MDB should have power to enforce the scheduling of work, quality control and progress for all participating agencies. A senior project administrator or engineer should be appointed as Resident Project Manager and delegated with the necessary authority to properly control and coordinate work actions in the field and to enforce work standards.
- 2) A quality control unit should be set up within MDB and properly staffed to inspect all works under construction and to enforce quality standards. The unit should be headed by a senior engineer, with the assistance of a chief materials engineer and a head surveyor and lower level inspectors throughout the project area. The unit should conduct a quality control workshop and training program for all MDB field staff.
- 3) Written contracts should be made by MDB with the RVDB, Army and any other agencies performing work in the project area and these contracts should be furnished to IDA for review. (This was mutually agreed at the time of negotiations and is reflected in the credit agreement). A list of all construction contracts and expenditures to date also should be provided to IDA. MDB should certify the quantity and quality of all work completed.
- 4) A realistic project implementation schedule should be prepared by MDB for each block, properly coordinating all required work and settlement actions for each area. Systematic planning should precede construction work wherever possible.

B) Other Recommendations:

Among other improvements needed are the full staffing of the extension service and initiation of the Training and Visiting system, assistance in providing the necessary agricultural inputs required for successful agricultural production, improved public relations in all areas affected by the project and encouraging lower level field staff to discuss frankly with supervisors problems arising in the field so that the head office can take appropriate action. Finally, in view of MDB's plan to complete field channel construction and on-farm development by the settlers themselves, ripping should be completed in areas required before work in these areas is undertaken.

Agreement with MDB has already been reached on many of the foregoing recommendations. A letter of intent of actions to be taken to improve MDB operations (copy attached) has been received from MDB by the Mission.

S.J. Baker

September 15, 1978

සභාපති
தலைவர் } 83069
Chairman

සාමාන්‍ය
பிர. முகாமையாளர் } 84501
General Manager

කාර්යාල
அலுவலகம் } 83060
Office } 83071



මගේ අංකය
எனது இல. } CH/DL/1BRD
My No.

ඔබේ අංකය
உமது இல. }
Your No.

මහවැලි සංවර්ධන මණ්ඩලය

மகாவலி அபிவிருத்தி சபை
MAHAWELI DEVELOPMENT BOARD

දිනය
திகதி } 13th Sept. 1978.
Date

ක. ප. ප. } 1667
த. பெ. }
P. O. Box

විදුලි පණිවුඩ
தந்தி } மாவலி
Telegrams } Mahaweli

11, Jawatte Road, Colombo-5.

11, ජාවත්ත පාර, කොළඹ - 5.

11, யாவத்தை வீதி, கொழும்பு-5.

Mr. Stanley Baker,
Leader, World Bank Review Team.

Dear Stan,

The supervision mission conducted during the last two weeks by the World Bank and other donor countries of work progress in Area H of the Mahaweli Development Project has included an inspection of the area and comments to the MDB staff. As you know, MDB has attempted to implement the program on an accelerated schedule consistent with National Objectives. We are also aware of the need to plan and construct the facilities, and provide the required agricultural and social support, in a manner that will assure the successful completion and operation of the project.

The World Bank Review Team has suggested the need for certain improvements in the program. In an effort to clarify and improve our operations, we intend to proceed with the following program :

1. A revised, more complete, and realistic implementation plan will be submitted by November 1st 1978.
2. A written plan for assuring construction quality in the H4 and H5 areas will be completed by September, 29th.
3. A revised cost estimate, a more complete plan for financial control and a schedule of financial requirements will be completed by October 13th.
4. A written plan for co-ordinating the settlement schedule in H4 and H5 with the completion of construction, providing on-farm development, and the furnishing of agricultural production support and social infrastructure will be completed by October 13th.
5. A check list of specific comments by the World Bank team and a list of specific actions required by the Loan Agreement will be prepared and assignments made for action.
6. A written plan for water monitoring and water management will be completed by October 13th.

contd...

සාමාන්‍ය
தலைவர் } 83069
Chairman

සාමාන්‍ය
பிர. முகாமையாளர் } 84501
General Manager

කාර්යාල
அலுவலகம் } 83060
Office } 83071



මගේ අංකය
எனது இல. }
My No.

ඔබේ අංකය
உமது இல. }
Your No.

දිනය
திகதி }
Date

මහවැලි සංවර්ධන මණ්ඩලය

மகாவலி அபிவிருத்தி சபை
MAHAWELI DEVELOPMENT BOARD

ක. පෙ.
த. பெ. } 1667
P. O. Box

විදුලි පණිවුඩ
தந்தி }
Telegrams }
මහවැලි
மகாவலி
Mahaweli

11, Jawatte Road, Colombo-5.

11, ජාවත්ත පාර, කොළඹ - 5.

11, யாவத்தை வீதி, கொழும்பு-5.

Page 2.

7. A program will be developed to improve the management of MDB with emphasis on team effort.

In our plans for continuing the development of the H4 and H5 areas, we want to make it clear that we intend to call on the prospective farmers to provide labour for constructing field channels and preparing the land for cultivation. Our proposals regarding this may not have been fully understood. The prospective farmers will be shown their allotments, and then will be paid for their work in the construction of field channels and doing part or all of the land preparation (machines will be used to the extent needed and available). Under this approach, labour will be made available to complete the system, and the prospective farmers will have a source of income, pending their settlement, and cultivation of their land.

Your frank comments have been helpful in identifying areas in which we can improve our work. It is our desire and intention to continue with the program in Areas H on a basis that will meet the needs of and be acceptable to both Sri Lanka and the World Bank and other donor countries. Your continued cooperation is appreciated.

With regards,

Yours sincerely,

D. V. P. Ladduwahetty
D. V. P. Ladduwahetty
Chairman

Mahaweli Development Board.

5. Field Trip

FIELD TRIP - TOUR OF TEA REHABILITATION AREA AT MASKELIYA AND

MAHAWELI GANGA DEVELOPMENT PROJECT AREA

(8:00 a.m. - 5:00 p.m. Friday, October 13)

1. After a briefing on Mahaweli Ganga Development Program at the Operations Room, Central Bank of Ceylon, Colombo, you and your party will be on an all-day field trip by helicopter and road transport to visit the Mahaweli Ganga Development Project area and the Tea Rehabilitation Project area at Maskeliya. En route you will have an opportunity to engage in informal discussions with Mr. Gamini Dissanayake, Minister of Lands and Land Development and of Mahaweli Development, who will accompany you throughout the trip. (For background and discussion, see attached briefing material on Mahaweli Ganga Development Program: Tab F-5-b and Topics for Discussion: Tab E-4).
2. Kotmale. Around 9:30 a.m. you will be flying over Kotmale. The Kotmale Reservoir, one of the six projects to be included in the Accelerated Mahaweli Ganga Development Program will include a dam and a 4-mile tunnel and underground power plant (150 MW). Its purpose is to provide storage, regulation of flow and hydroelectric power. (For further information, see para 4.09 of Section F-5-b).
3. Maskeliya. After arriving at Dickoya Sports Club Grounds at about 10:00 a.m., you will be able to briefly inspect a portion of the IDA assisted project area of the Tree Crops Rehabilitation Project (Tea) and have a chance to meet planters and estate work force. The project area is located about 80 km east of Colombo, in the planting districts of Maskeliya and Upper and Lower Dickoya in the northwestern part of the administrative district of Nuwara Eliya. The project area includes about 18,000 ha of tea, managed by the State Plantations Corporation (10,000 ha in 30 estates), Janatha Estates Development Board (7,600 ha in 29 estates) and by small-scale producers (300 ha owned by 183 individuals). The economy of the project area is almost entirely dependent on tea. There are few of the traditional village settlements which characterize the mid and low country tea areas, and the majority of the area's population, mostly Tamil (mainly non-citizen Tamils of Indian origin), lives on tea estates. This population is declining, because of GOSL's Tamil repatriation program, causing labour shortages at times of peak demand. Typical accommodation for an estate laborer's family consists of a tiny (20 m²), two-room row house. Poor housing is a major factor in the sub-standard health of estate labor and is a major impediment to attracting Sinhalese labor into the tea industry to replace the traditional Tamil labor. The quality of estate schools is below the national average. Overall mortality is about 50% above the national average. (For information about the project, see attached Annex I).
4. The Mahaweli Ganga Development Project Area. After leaving Dickoya, you will be flying over the Mahaweli Ganga Development Project Area. The Mahaweli Ganga is Sri Lanka's largest river, draining an area of about 4,000 square miles (see Map in Section F-5-b). It rises in the mountainous south-central part of the island, which receives an annual rainfall of 175-200 inches, and discharges an average of about 7 million acre-feet annually into the Bay of Bengal. It is the principal source of water for irrigation in the Dry Zone.

(a) Polgolla. The construction of diversion headworks and a 40 MW hydro-power plant at Polgolla was part of the Mahaweli Ganga Development Project I, begun in 1970 with financial assistance from the World Bank and is now in full operation. (For further information see para 1.02 of Section F-5-b).

(b) Victoria. One of six new projects under the Mahaweli Program, the Victoria Reservoir Project includes a dam, power plant (120 MW), the Minipe Diversion Complex and the development of irrigation works and infrastructure on the Mahaweli Basin right bank area of 74,000 acres. (For further information, see para 4.05 of Section F-5-b).

(c) Randenigalla. The proposed Randenigalla Reservoir will be located about 13 miles below the Victoria Reservoir, and operate in cascade with it, and will include the dam, power plant (75 MW), and irrigation works and infrastructure. Its purpose is to provide long-term regulation of flow, generate hydroelectric power and reduce peak flood flows. (For further information, see para 4.06 of Section F-5-b).

(d) Maduru Oya. The proposed Maduru Oya Reservoir Project includes the Ulhitiya - Maduru Oya tunnel (4.5 miles), Maduru Oya dam, power plant (5 MW), and irrigation system and infrastructure for the development of about 125,000 acres in the Maduru Oya Basin, of which 118,000 acres will be new land. (For further information, see para 4.07 of Section F-5-b).

5. Polonnaruwa. One of the most important historical sites in Sri Lanka, Polonnaruwa was, next to Anuradhapura, the most important of Ceylon's medieval capitals and has extensive remains still standing. The variations in architectural style and the preponderance of brick over stone are especially noteworthy.

6. Anuradhapura. You and your party will arrive at Anuradhapura at noon and will have lunch there. Anuradhapura is the most important historical city in Sri Lanka and is thought to be the site where Buddhism arrived in Sri Lanka. The ancient city thus became a Holy City to Buddhism in the sense that Jerusalem is to the Jew and Christian or Benares to the Hindu. This single fact determined its structure, imbued its atmosphere and explains its sacredness to the Sri Lankans of today. Anuradhapura has some of Sri Lanka's most famous "dagabas," or "stupas," a sepulchral mound built over sacred relics. Anuradhapura was the national capital for about six hundred years during the ancient kingdoms. The ruins of the city are a great tourist attraction.

7. Mahaweli Ganga Development Project II Area. After leaving Anuradhapura and arriving at Maha Illupallama Research Station, you and your party will be visiting by road transport some homesteads in a portion of the IDA-assisted Mahaweli Ganga Development Project II area. At issue in this project is the adverse impact on quality of work resulting from the Government's haste in implementing the Accelerated Mahaweli Development Program. (See Tab. E-4: Topics for Discussion with Mr. Dissanayake and Tab. G-3: Ongoing Projects, Mahaweli Development Project II.) For further

information on this project, see also the attached Annex 2.

Attachments:

Annex 1 - Tree Crop Rehabilitation (Tea) Project
Annex 2 - Mahaweli Ganga Development Project II

SRI LANKA

TREE CROP REHABILITATION (TEA) PROJECT

Credit and Project Summary

Borrower: Government of Sri Lanka.

Beneficiaries: State Plantation Corporation (SPC)
Janatha Estates Development Board (JEDB)
Private estate owners
About 180 small-holders
Private transporters.

Amount: US\$21.0 million

Terms: Standard

Relending Terms: Government through the Central Bank will on-lend up to US\$17.2 M of the credit to the Bank of Ceylon (BOC) at a rate of interest of: (i) 8.5% per annum, to be on-lent for project purposes at 12% per annum to SPC, JEDB, private truck operators, private growers, and factory owners; and (ii) 6.5% per annum, to be on-lent to SPC, JEDB, and private growers at 10% per annum for estate labor housing expenditure. Maturities would be: factory machinery, 10 years; vehicles, 5 years; field development, 15 years, with one year of grace; and estate labor housing, 15 years, and 5 years of grace. The Bank of Ceylon shall repay its loans from the Central Bank within the same term as the relevant sub-loans.

Project Description: The project would assist the Government of Sri Lanka in improving the economic efficiency of the tea industry by lowering production costs and improving tea quality in the project area, as well as in stemming the decline in output of tea through: expanded programs of tea replanting and infilling; strengthening the two major Government corporations involved in estate management; reduction in total number of factories, and expansion and rehabilitation of the remainder; provision of vehicles for personnel, green leaf and made-tea transport; and rehabilitation of soil conservation works. The project would also assist private estate owners and approximately 180 small-holder producers, and would provide improved housing and medical facilities for estate laborers. The project faces no special risks, but realization of full benefits will depend mainly upon the management performance of the two Government corporations involved.

Estimated Cost:

The table below summarizes the total cost of the project. (Numbers may not add due to rounding.)

	<u>US\$ Million Equivalent</u>		
	<u>Local</u>	<u>Foreign</u>	<u>Total</u>
Field works	3.6	1.2	4.8
Field and Nursery			
Equipment	.4	.3	.7
Vehicles	1.1	2.0	3.1
Housing	6.3	2.1	8.4
Factory Equipment	2.6	1.7	4.3
Medical	.2	.2	.4
Training	-	.2	.2
Support	.1	.1	.2
<u>Total Base Costs</u>	<u>14.2</u>	<u>7.7</u>	<u>22.0</u>
Physical Contingencies	.7	.4	1.1
Price Contingencies	6.2	1.5	7.7
<u>Total Costs</u>	<u>21.1</u>	<u>9.7</u>	<u>30.8</u>

Financing Plan:

	<u>US\$ Million Equivalent</u>		
	<u>Local</u>	<u>Foreign</u>	<u>Total</u>
IDA	11.3	9.7	21.0
SPC and JEDB	7.1	-	7.1
Bank of Ceylon	1.9	-	1.9
Private Operators	.4	-	.4
GOSL	.4	-	.4
<u>Total</u>	<u>21.1</u>	<u>9.7</u>	<u>30.8</u>

Estimated Disbursements:

Bank Fiscal Year	<u>\$ Million</u>					
	<u>1980</u>	<u>1981</u>	<u>1982</u>	<u>1983</u>	<u>1984</u>	<u>1985</u>
Annual	3.0	4.5	4.5	3.5	4.5	1.0
Cumulative	3.0	7.5	12.0	15.5	20.0	21.0

Rate of Return:

25%

Staff Appraisal Report:

No. 1892-CE, dated May 12, 1978

SRI LANKA - MAHAWELI GANGA DEVELOPMENT PROJECT II

CREDIT & PROJECT SUMMARY

- Borrower: Republic of Sri Lanka (GOSL).
- Amount: \$19.0 million.
- Terms: Standard.
- Cofinanciers: Canada - US\$6.0 million equivalent with no interest or service charge, repayment period of 50 years (including 10 years' grace). Procurement tied to goods and services produced in Canada.
- The Netherlands - US\$5.0 million equivalent at 2-1/2% interest, repayment period of 30 years (including 8 years' grace). Procurement untied, joint financing with IDA under international competitive bidding.
- United Kingdom - US\$7.2 million equivalent on grant basis. Procurement tied to goods and services produced in the U.K.
- United States - US\$5.0 million equivalent at 2% interest during grace period (10 years) and 3% interest thereafter, repayment period of 40 years. Procurement tied to goods and services produced in the U.S.

Project

Description:

The Project would be the first major development of new lands located in Sri Lanka's north-central dry zone, covered by the Government's Mahaweli Master Plan. The Project builds on experience gained from ongoing irrigation/settlement works in the area, as well as previous schemes elsewhere in Sri Lanka, and is designed with the view to replication in the future. It provides for irrigation works and land development, agricultural production support, and social infrastructure required for completing Stage II of the Government's Plan. The details of the Project are given below.

Project

Components: I. Irrigation Infrastructure (and Land)

- (a) Completion of reconstruction of existing Kalawewa Main Canal (10 mi), with control structure;
- (b) Improvement of four large tanks along Main Canal to serve as equalizing reservoirs to reduce operational losses;
- (c) Construction of 250 mi of distributary canals, with control structures, and 400 mi of field channels;
- (d) Construction of operation and maintenance (O&M) roadways along main, branch and distributary canals; and
- (e) Improvement of main drains (10 mi) and construction of secondary and tertiary drains (100 mi and 110 mi, respectively).

II. On-Farm Development

- (a) Cleaning of trees and brush and cross-ripping by heavy tractors;
- (b) Plowing of cultivation areas to assist settlers in leveling, grading and constructing soil conservation bunds; and
- (c) construction of 1,500 mi of farm ditches and drains to provide farm-level water distribution and drainage.

III. Equipment, Vehicles and Facilities

- (a) Provision of equipment and vehicles for construction of civil works; and
- (b) Construction of workshop (with equipment, offices and staff quarters) and equipment to support the O&M of irrigation works.

IV. Agricultural Extension and Research

- (a) Reorganization and strengthening of agricultural extension services in the area, and provision of vehicles for increased staff mobility, staff quarters, and demonstration equipment;
- (b) Provision of equipment, teaching aids, staff quarters and dormitories for the Regional Agricultural Training Center at Maha Illuppallama; and
- (c) Provision of equipment and staff housing for new Irrigation and Water Management Pilot Project jointly sponsored by the Mahaweli Development Board and Irrigation and Agricultural Departments.

V. Farm Equipment

- (a) Provision of 300 four-wheel and 1,200 two-wheel tractors, with implements; and
- (b) Provision of 50 power sprayers and 1,300 hand sprayers for improved plant protection.

VI. Storage, Marketing and Processing

- (a) Construction of storage facilities for fertilizer, seed and paddy in 50 village centers;
- (b) Construction of three primary cooperatives and 24 branch cooperatives, renovation of 26 branch buildings, and vehicles and minor equipment for the three primary cooperatives; and
- (c) Provision of buildings, plant and equipment for the Paddy Marketing Board's processing complex, and 50 rice hullers and 25 thresher/winnowers for the Cultivation Committees in the project area.

VII. Market Roads

- (a) Construction of 25 mi of new link roads and improvement of 50 existing link roads to provide all-weather access throughout the project area.

VIII. Schools and Medical and Community Development Facilities

- (a) Construction of 600 classrooms in primary schools and 20 classrooms in secondary schools, together with laboratories, playgrounds, and quarters for school principals;
- (b) Construction of two rural hospitals and two central dispensaries, with maternity wards, together with vehicles, equipment and staff quarters;
- (c) Construction of small community halls for each village center and provision of vehicles and staff housing.

IX. Village Wells and Roads

- (a) Construction of 1,235 wells (one per 20 families) in the hamlets; and
- (b) Construction of 200 mi roads in the hamlets and villages, including drains and culverting.

X. Assistance to Settlers

- (a) Provision to each settler materials for a temporary hut, seeds and planting material for the first crop, field tools, and a subsistence allowance of Rs 50 per month for five months, totalling about Rs 680 per family; and
- (b) Provision to each family free food rations for one year from the World Food Program.

XI. Technical Assistance and Monitoring

- (a) Provision of an Implementation Advisor and On-Farm Development Specialist for three years each; and
- (b) Provision of buildings, equipment and vehicles, consultant's services to support a program to monitor irrigation efficiencies and to assess the agricultural, economic and social impact of the project.

Cost Estimates: 1/

	US\$ Millions		
	Local	Foreign	Total
<u>I. Irrigation and Land Development</u>			
Land Acquisition	0.4	0.0	0.4
Irrigation Infrastructure	10.0	3.1	13.1
On-Farm Development Works	12.2	3.4	15.6
Construction Equipment, Vehicles	4.4	5.4	9.8
O&M Facilities and Equipment	<u>1.4</u>	<u>1.5</u>	<u>2.9</u>
Sub-total	28.4	13.4	41.8
<u>II. Agricultural Production Support</u>			
Agricultural Extension, Research	1.1	0.8	1.9
Farm Equipment	3.7	6.0	9.7
Storage, Marketing, Processing	2.0	1.4	3.4
Market Roads	<u>0.4</u>	<u>0.1</u>	<u>0.5</u>
Sub-total	7.2	8.3	15.5
<u>III. Social Infrastructure</u>			
Schools, Medical and Community Development Facilities	3.3	0.9	4.2
Village Wells and Roads	<u>1.6</u>	<u>0.5</u>	<u>2.1</u>
Sub-total	4.9	1.4	6.3
IV. <u>Settlement</u>	1.8	0.5	2.3
V. <u>Technical Assistance/Monitoring</u>	0.4	0.7	1.1
VI. <u>Engineering, Supervision, Administration</u>	<u>4.5</u>	<u>0.0</u>	<u>4.5</u>
Base Project Cost	<u>47.2</u>	<u>24.3</u>	<u>71.5</u>
VII. <u>Physical Contingencies</u>	<u>5.3</u>	<u>1.5</u>	<u>6.8</u>
Sub-total	52.5	25.8	78.3
VIII. <u>Price Contingencies</u>	<u>15.4</u>	<u>6.8</u>	<u>22.2</u>
Total Project Cost	<u>67.9</u>	<u>32.6</u>	<u>100.5</u>

1/ Including Taxes and Duties (US\$20.5 M equivalent).

Financing Plan:

	US\$ Millions		
	Local	Foreign	Total
(a) <u>Components Net of Taxes</u>			
IDA Credit	4.7	14.3	19.0
Canada	1.2	4.8	6.0
The Netherlands	1.3	3.7	5.0
United Kingdom	1.4	5.8	7.2
United States	1.0	4.0	5.0
Government of Sri Lanka	28.1	-	28.1
Commercial Banks/Private Sector	9.7	-	9.7
Sub-total	47.4	32.6	80.0
(b) Taxes	20.5	-	20.5
TOTAL	67.9	32.6	100.5

Estimated Disbursements:

IDA Fiscal Year	US\$ Millions	
	Annual	Cumulative
1978	1.6	1.6
1979	4.8	6.4
1980	6.2	12.6
1981	4.0	16.6
1982	2.4	19.0
TOTAL	19.0	

Procurement

Arrangements:

International competitive bidding (ICB) under IDA guidelines (with a 15% preference margin, or prevailing custom duties if lower, for local manufacturers) for equipment and vehicles financed by IDA and The Netherlands; tied procurement under Canadian, U.K. and U.S. guidelines for equipment and vehicles financed by Canada, U.K. and U.S., respectively; for civil works, local competitive bidding (LCB) for private contractors; negotiated contracts for public agencies, and a small amount under force account, all under usual Government procedures which are acceptable to IDA; normal trade channels for small off-the-shelf items costing less than US\$10,000 each and aggregating less than a total of US\$250,000.

Technical Assistance/
Monitoring:

One Implementation Advisor for about three years to serve as a non-voting member of the Mahaweli Coordinating Committee (MCC) and to assist the Chairman of the Mahaweli Development Board (MDB) in planning, scheduling and management of all aspects of the project, as well as preparation of the next stages of the Mahaweli Development Scheme; one On-Farm Development Specialist for about three years to assist in planning the irrigation of up-land crops, developing suitable farm layout models, and establishing operational criteria for the irrigation system; and funds for a program for monitoring irrigation efficiencies and the agricultural, economic and social impacts of the project, including recording stations, equipment and vehicles, services of a short-term hydrologist (12 man-months), and agro-economic surveys to be carried out by the Agrarian Research and Training Institute (ARTI), an independent local organization.

Economic Rate of Return:

The economic rate of return is estimated at 21 percent.

Appraisal Report:

No. 1487-CE of March 31, 1977

F. Reference
Material

Sri Lanka

Political Situation

Election Results

1. In the July 1977 elections, Mr. J. R. Jayawardene's United National Party (UNP), won by an overwhelming majority--140 of parliament's 168 seats. The Tamil United Liberation Front (TULF), a coalition of the Federal Party, the Tamil Congress and the Ceylon Workers' Congress, won 18 out of the 26 seats it contested, mainly in the northern and eastern provinces, and became the main opposition party. Mrs. Sirimavo Bandaranaike, widow of the founder of the Sri Lanka Freedom Party (SLFP), who had led a coalition of left parties to a landslide victory at the 1970 elections, was routed, winning only 8 seats. The SLFP's former coalition partners, the Trotskyite Lanka Sama Samaja Party and the Moscow-oriented Communist Party, which, together with other defectors from Mrs. Bandaranaike's camp, contested the election under the banner of the United Left Front (ULF), fared even worse, losing all the seats they contested.

2. Mrs. Bandaranaike's defeat after seven years in power (a five year term extended by two years under the Republican Constitution introduced in 1972) was in keeping with a well established tradition of post-independence politics. In six successive elections the party in power has been defeated. Given a clear choice, Sri Lanka's sophisticated electorate has always opted for change. The two political parties that have dominated Sri Lanka's politics since 1947 have offered such a choice: the SLFP representing populist left center views, and the UNP, till recently, right of center. Other factors of importance in the election were inflation, unemployment, corruption and nepotism and the erosion of fundamental freedoms under the State of Emergency declared after the 1971 insurrection. During this period, the independence of the Judiciary had been restricted, the freedom of the press curtailed and freedom of association curbed. Mr. Jayawardene rode to power on pledges of a clean administration, immediate economic relief for the people, and the restoration of basic rights.

3. The UNP had its origins in the Senanayake family--which, with the Bandaranaike family, has governed Sri Lanka alternately since Independence. Mr. Jayawardene took over the leadership in 1973 after the death of Mr. Dudley Senanayake and widened the party's appeal beyond the influential Colombo-based squirearchy and commercial interests with which it was traditionally associated. The party now is pledged to a policy of pragmatic moderate socialism. He also brought in younger people from different walks of life into the party. This shift in image, accompanied by a significant change in the class composition of UNP candidates (in favor of the working and lower middle class) was a major factor in the size of the UNP victory. In its Manifesto for the 1977 elections, the UNP stressed its commitment to democracy and socialism and its desire "to expand individual participation within a socialist framework". In a policy statement presented to the State Assembly on August 4, 1977, the new Government pledged the creation of: a

new and more moral society based on traditional Buddhist values; priority for a cultural renaissance; reducing the cost of living; self-sufficiency; agrarian reforms; the revamping of education; establishment of a free trade zone and a "people's sector"; 1/ ensuring public participation in administration through district development councils; resolution of the Tamil minority issue and the introduction of a Presidential system of government.

The Political Inheritance

4. In the three decades since Independence, Sri Lanka has successfully conducted as many as eight general elections; in six of them the party in power has been defeated. With each election, voter participation has risen; in the July 1977 election, 87% of the electorate exercised its franchise. After each election, there has been a peaceful transition, and on the surface at least, the record appears to be one of impressive political stability. This remarkable political performance contrasts starkly with a relatively poor economic record. Economic growth has been modest, (see F-2 - Economic Situation) and growth in employment has been well below the rate of growth of the labor force, resulting in open unemployment of over 20% of the labor force (or 1 million).

5. There is in this a paradox awaiting resolution. While Sri Lanka has demonstrated a high level of political development and impressive political stability, its political system has been experiencing increasing difficulties in stimulating economic growth, generating employment and meeting the demands arising from the rapid increase in popular aspirations. This apparent paradox, however, is partially resolved when one takes into account Sri Lanka's social achievements. These impressive social gains, which have been well documented elsewhere, 2/ are not caught in the traditional yardsticks that measure economic performance. And yet, the gains in nutrition, health and education are clearly a major explanation for the record of political and social stability, reflecting the fact that successive governments have in fact proved extremely responsive to the rising aspirations of the electorate through the comprehensive welfare programs for which Sri Lanka has justifiably won international repute.

6. However, Sri Lanka's ability to sustain these welfare programs has in recent years increasingly come into question. First, the substantial surpluses generated by tea and rubber estates in the 1950's and early 1960's which provided the revenues and foreign exchange needed to support the welfare programs, have been eroded over time by the neglect of these crops and declining terms of trade. Second, slow economic growth, combined in the 1970's with rapid inflation, has also eaten into these gains. Expenditures on social

1/ A euphemism for a reformed private sector, consisting predominately of small enterprises a la Disraeli's "acre and a cow".

2/ See "Development in Sri Lanka: Issues and Prospects" World Bank Report No. 1937 CE. March 1978.

services as a percentage of total current expenditures or GDP have been declining steadily, with the pace of deterioration accelerating in the 1970's. There has been a serious deterioration in health services, in terms of per capita expenditures, personnel and equipment. The recorded improvement in income distribution may also have been eroded by inflation in the 1970's. Third, the gains in education have had negative returns in the form of a politically explosive expansion of the numbers of educated unemployed and the unsatisfied aspirations of an even larger group of the educated employed. These have posed a challenge to the established political order and continue to be a source of instability.

7. The outer appearance of political stability has traditionally been accompanied in the post-Independence period by an established tradition of extra-parliamentary pressure and political violence. Such pressure has on occasion taken extreme forms, as in the Tamil-Sinhalese riots of 1958 and 1977, and the more dramatic Insurgency of 1971. These eruptions reflect the thin line between stability and unrest in most developing countries. The traditional political response to this ever present threat to stability represented by unsatisfied economic and social demands has been one of short run expediency. Successive governments have resorted to palliatives rather than cures. Parties have tended to compete with each other to bid up what each offers in short-term give aways. As a consequence, explicit and implicit subsidies emerged throughout the economy, and, with the recent spread of price controls, their burden has grown markedly. This process has meant that efforts to reduce the enormous budgetary burden of transfers and subsidies and divert resources for development have more often than not been reversed. A populist environment has served to inhibit private investment, and spawned a vast, inefficient public sector.

The New Government's Response

8. The unenviable economic inheritance of the new government combined with the high expectations arising from the size of its election victory has influenced the nature of its political response. The UNP's programs and policies were fashioned during the long spell in opposition by the man who knew where he wanted his country and his party to go. "JR" as the President is commonly known, carefully nurtured the UNP back to health from the debacle of the 1970 elections, changing the party's image, and infusing new talent, while keeping a tight control over policies and party affairs. A strong disciplinarian, JR does not brook factionalism or indiscipline in the party. In sheer ability, personality and personal popularity, JR has no rival and owes no one any favors. However, at the age of 72, he knows that time is not on his side. He is, therefore, a man very much in a hurry. This partially accounts for the speed with which the new government has moved to introduce a staggering range of political, constitutional and economic reforms.

9. One of Mr. Jayawardene's first acts on coming to power was to use his two-thirds majority in the Assembly to introduce a Presidential system of government. He was sworn in as Sri Lanka's first Executive President on February 4, 1978 under the new constitution, which came into effect in September 1978. He is now both head of state and of government, able to dissolve

Parliament but not to be dismissed by it. He has thus set aside the Westminster parliamentary system with which Sri Lanka has lived since Independence, and replaced it with a presidential system whose inspiration is clearly drawn from Gaullist France. By also introducing proportional representation, he has made it extremely unlikely that any new government will have the majority to reverse this change. The primary objective appears to be to insulate the executive branch of the government from the vicissitudes and populist pressures that inevitably emanate from the legislative branch of any democratic government, and to give the executive greater powers vis a vis the legislature. In addition, the new constitution revised the judicial system making it independent of the legislature.

10. The shift to proportional representation will also ensure that the political composition of the legislative assembly does not experience the kind of dramatic changes after each election that have characterized the past. JR clearly hopes that the new constitution will provide the degree of stability needed to ensure that development activity can proceed relatively unimpeded by political changes. Whether the experiment will succeed remains to be seen, particularly since it is not clear what will happen if the political parties dominating the legislature are different from the party affiliation of the President. Nevertheless, the enhanced powers of the executive branch of government, and the concentration of powers in the President greatly facilitates the decision making process. This can already be seen in the unprecedented speed with which decisions are being taken in Sri Lanka.

Major Political Problems

11. The main political dilemma facing the new government is that while it is committed to providing early benefits to the people through enhanced economic growth and increased employment opportunities, there are no instant remedies for low growth and high unemployment. Any benefits flowing from the major economic reforms introduced last year (see F-2 - Economic Situation) will necessarily take time to make a dent in the level of unemployment. Moreover, the reforms themselves require substantial sacrifices as they entail an erosion of welfare benefits through reduced subsidies and transfers. These could prove enormously unpopular if the benefits to flow from such cuts are not immediately obvious. The government has, therefore, to choose between (i) a strategy that would take advantage of the political popularity it currently enjoys to push through all the unpalatable measures needed to raise resources for development in the hope that the benefits will begin to flow before the next elections (due 1983) and (ii) a strategy that would proceed more cautiously, timing the unpopular measures to coincide with the benefits flowing from economic reforms and relying more heavily initially on external assistance. While the government appears inclined towards the latter tactic, only the budget of 1979 will provide a clear indication of the choice it has made.

12. The task of development is made more difficult by the decimation of the SLFP and the "left" in the last elections. The absence of an effective Sinhalese parliamentary opposition could increase the attractiveness of

militant extra-parliamentary activities to parties of the left. The SLFP and the left feels further threatened by the constitutional changes which they have already denounced as introducing a dictatorship by reducing the powers of the National Assembly vis a vis the Executive. Mr. Keuneman, head of the Communist party, has also warned of the danger of driving the left underground. The Insurrection of 1971, led by Marxist youths, is still fresh in the memory of politicians. That it was skillfully organized and that the leaders were given the advantage of drawing lessons from their failure by being confined together in prison, is a source of concern. The leader of that insurrection, Mr. Rohan Wijeweera, has been released from prison by the UNP. His Jathika Vimukthi Peramune (JVP) remains the strongest of some 25 left youth movements, appealing mainly to the vast body of the educated unemployed in town and country. Mr. Wijeweera has so far been preoccupied with discrediting the defeated left wing parties. The JVP claims it is not interested in overthrowing the Government, merely "the system". But the movement will be quick to exploit any failure of the UNP to deliver results. Student unrest remains a serious problem in schools and universities, where there have already been a number of clashes between Marxists and UNP followers. The Government has tended to respond by sending students home in the belief that angry parents will force their children to go back to studies and leave politics alone.

13. A second source of unrest could be organized labor. This group is the worst affected by the withdrawal of the rice ration and increases in the price of flour. Control of the left parties over the trade unions is also being threatened by the ban on political strikes and the Government's commitment to depoliticize the trade unions. Although strong trade union pressure has forced the government to withdraw its radical industrial relations bill that sought to limit trade union powers and introduce a one-industry, one-union principle, some modified bill is likely to be reintroduced with the same objective. How serious an obstacle the trade unions will prove depends on the success the UNP enjoys in increasing its support among the unions. If, as appears likely, the UNP expands its hold over the trade union movement, this may, itself prove a constraint on how far the government can move either in the area of limiting political competition among organized labor or in introducing measures that hurt organized labor's short-term economic interests, such as further cuts in consumer subsidies.

14. The third, and most worrying political problem for the government is the Tamil problem. This surfaced shortly after the July 1977 elections when communal disturbances erupted, the worst since 1958, following an innocuous incident at a carnival in Jaffna, the largest northern city which is inhabited preponderantly by the minority Tamils. About 140 deaths were officially recorded in the subsequent riots and incidents in which Tamil business establishments and homes in several areas across the country were attacked and burned. The government handled the riots with firmness and cool confidence. A fortnight's dusk-to-dawn curfew and some 5,000 arrests quelled the disturbances. That it took so long to bring the situation under control reflects the thinness of the military, para-military and police forces in Sri Lanka. Moreover, the Sinhalese dominated police appeared far from neutral, since they were a party to the incident that sparked off the riots. Not surprisingly, it has taken months to persuade the thousands of displaced Tamil-speaking citizens to return to their homes and jobs.

15. The situation is greatly complicated by the fact that a frankly separatist Tamil party has emerged as the main opposition party in Sri Lanka. The riots of August 1977 were indirectly caused by the Tamil United Liberation Front's somewhat disputable claim that the election results were a mandate from the island's two million Tamils for the creation of "Tamil Eelam". This aroused Sinhalese ire, which the UNP claims was exploited by frustrated SLFP and left party politicians in an attempt to embarrass the victorious UNP. JR has tried to reassure the Tamil minority that there would be no more discrimination. He said he was President of the entire country, including Tamils. In an attempt to win Tamil goodwill, he has removed "standardization" from public examinations, a mechanism that had been used to reduce the number of Tamil entrants to university. He also pledged equal rights in the use of language, education and employment and to stop the colonization of traditional Tamil areas with Sinhalese families. These pledges have been enshrined in the new constitution; but the TULF is still dissatisfied, choosing to boycott the vote in the Assembly on the constitution. This must partly reflect its concern at being outflanked by more extremist Tamil youth organizations. An organization called the Liberation Tigers of Tamil Eelam has already emerged and claims responsibility for 11 murders, including five police officers. Government has taken extreme measures to suppress this movement; but the whole Tamil question remains potentially a serious threat to the government's development programs. To the extent that Tamil-speaking Indian nationals on tea estates feel threatened by these developments, as they undoubtedly do, there could also be a severe adverse effect on tea production from an acceleration in the migration of these workers to India, particularly since it is apparently difficult to persuade Sinhalese workers to work in the arduous physical and climatic conditions prevailing on the tea estates.

16. Underlying all these uncertainties is the extraordinary dependence of the UNP on JR. The party has been appropriately described as a "fragile coalition of interest groups held together by the personality of the President". JR towers over his colleagues, and there appears to be no one else in the party who could take the reins of office and command the same degree of loyalty in the party and the country. This makes the UNP, and the country, enormously vulnerable, should anything happen to JR. This is the first government Sri Lanka has had in several years which is trying to address seriously the problems of development the country is facing. While the political task is even more difficult than the economic, the key question is whether the vision JR brings to both tasks will fire the people's imagination sufficiently to enable Sri Lanka to successfully attain the balance between growth and welfare objectives that has so far eluded the country.

SRI LANKA

THE ECONOMIC SITUATION

1. Sri Lanka has achieved social progress far beyond that of other countries with comparably low per capita incomes. Literacy, health, and life expectancy are high; nutrition is adequate, and mortality and population growth rates have been declining. These impressive gains have been achieved despite generally low output and employment growth. Per capita GDP growth was only 0.9% per annum in the 1948-60 period; it accelerated to 2.1% in the 1960s and then declined to 1.3% per annum in the 1970s. Throughout the 1960s and the 1970s, these modest output gains were eroded by adverse terms of trade trends. This disappointing performance has been accompanied by a disturbing increase in the level of open unemployment. In the 1970s, while the labor force has been growing at about 125,000 per year, employment has been rising by about 85,000, much of it unproductive jobs. The number of unemployed has, therefore, been rising, and open unemployment is estimated at over one million or 20% of the labor force.

2. The gains in the social field were made possible by favorable initial conditions. Compulsory primary education had been introduced as early as 1901. The food ration was introduced in 1942. Thus, at the time of Independence in 1948, Sri Lanka already enjoyed high levels of adult literacy and life expectancy. These initial gains were consolidated and expanded in the post-Independence period through large expenditures on social services and the food subsidy, which have accounted for two-fifths to one-half of government revenues in the 1960s and 1970s. These expenditures have been financed by harnessing the surpluses of Sri Lanka's three major tree crops, tea, rubber, and coconut, which provided the Government with both an easy revenue source and the foreign exchange earnings needed to pay for food imports required to meet consumption requirements.

3. There are both measurable and non-measurable economic benefits flowing from these improvements in health, nutrition, and education. Of these, the most important ones are the decline in fertility and the relatively low rate of urbanization. At the same time, there have been some significant costs arising from the firm commitment of successive governments to maintaining these social gains. The fiscal burden of these expenditures has imposed a high degree of inflexibility on Sri Lanka's policymakers in their attempts to accelerate long-term growth. That inflexibility has increased over time as growth slowed down and, in particular, the ability of the tree crop subsector to provide resources weakened as commodity prices kept falling and productivity suffered due to inadequate incentives. Moreover, the gains in education have had a negative impact in the form of large numbers of educated unemployed who have posed a challenge to the established political order. With political parties competing against each other to offer inducements to the electorate, it has proved difficult for governments to focus social expenditure programs more narrowly on specific groups living in poverty.

4. In the 1960-77 period, gross domestic product at constant prices rose by 3.8% per annum, slightly above the 3.5% per annum recorded in the first 12 years after Independence. This impressive performance masks a marked deceleration in the growth of the productive sectors of the economy between the 1960s and the 1970s. GDP growth slowed down from 4.4% per annum in the 1960s to 3.0% in the 1970-77 period. Growth fell from 3.4% to 1.9% in agriculture; from 6.2% to 2.3% in manufacturing.

5. The key to the slowdown in GDP growth lies largely in the slow growth of agriculture, which accounts for over one-third of GDP and four-fifths of export earnings. Tea and coconut output has been declining steadily from the mid 1960s; rubber, after showing a rapid increase in the 1960s, stagnated in the 1970s. Poor weather, declining commodity prices, a rising effective tax burden, and low producer returns combined with the uncertainties caused by a long, drawn-out land reform (1972-75) depressed producer incentives and, hence, investment and production, to new lows. These problems were aggravated by a dual exchange rate, introduced in 1968, which discriminated against traditional exports and in favor of food imports.

6. Paddy production, which grew at 7.4% per annum in the 1964-70 period, slowed down to 0.7% per annum in the 1970-77 period. The decline in yields and cropping intensities that this reflected is attributable to a series of droughts and a sharp deterioration in the institutional support for production programs. The only bright spot on the agricultural scene has been the rapid increase in output of subsidiary food crops in the 1970s. This represents gains in acreage rather than yields, and is in response to the improved incentives arising from a ban on imports of this foodstuff, introduced in 1970.

7. The slowdown in manufacturing output in the 1970s was due to the cumulative impact of declining investment levels, severe foreign exchange shortages that necessitated import rationing (with serious consequences for a sector in which imported raw materials account for 70% of the value of raw materials used), the exhaustion of import substitution possibilities, and inefficiencies in management of the public sector, which now accounts for 66% of the gross value of production in organized industry.

8. In general, economic growth was constrained by a persistent foreign exchange shortage throughout the 1960s and 1970s, inadequate levels of saving and investment, and the low efficiency of resource use. Sri Lanka's terms of trade have deteriorated steadily since the early 1960s and worsened sharply in the mid 1970s following increases in the price of imported food, fertilizer and petroleum. The share of these three items in Sri Lanka's total imports jumped from about 50% in 1972 to 70% in 1975. This sharp increase has, to some extent, offset the improvement in export prices (particularly of tea) since 1973. Trade policies that discriminated against exports and encouraged import substitution caused a slow growth in exports of 2.5% per annum between 1960 and 1976, which acted as a significant constraint on growth for an economy in which exports accounted for 30% of GDP in 1960, and at 22%, are still substantial today.

9. The share of consumption in GDP has remained relatively stable and high (at 86%) over the last decade and a half. Domestic savings, when adjusted for the dual exchange rate, fell from 11.5% of GDP in 1966-77 to 9% in 1971-76. This deterioration in savings performance is largely explained by a decline in public savings. Public savings averaged a mere 1% of GDP in the 1960s, shrinking rapidly in the 1970s, and eventually becoming negative. This poor performance is attributable to the large and growing burden of subsidies and transfers, which worsened in the 1970s, because of the increasing disparity between import and officially determined prices. Savings levels were also adversely affected by the large hidden subsidy burden implicit in the failure to recover costs from beneficiaries of irrigation and other infrastructure projects. Private savings were adversely affected in the 1970s by political uncertainties, a confiscatory tax burden, and falling real interest rates.

10. Gross investment has averaged 16% of GDP at current market prices in the 1960-1976 period. In real terms, investment has been declining, and there has been persistent failure throughout this period to raise the level of public investment (around 6-7% of GDP) while private investment in productive activities was, on the whole, not being given much encouragement. The efficiency of investment has also been rather low due to both a misdirection of investment and a failure to exploit the full potential of past investments. Thus, much of the investment in agriculture has been directed to paddy, to the neglect of replanting in the tree crop sub-sector, resulting in an erosion of the latter's production base. Even within paddy, the strategy pursued emphasized costlier, more visible extensive development of the Dry Zone to the neglect of cheaper, but less intensive development. In the manufacturing sector, capital-intensive import substitution was pursued to the neglect of labor-intensive export-oriented production. Utilization of the potential already established is uniformly low. This is reflected in low cropping intensities and yields in the agricultural sector, and low-capacity utilization in manufacturing.

11. In the elections of July 1977, the eighth since Independence, the United National Party won a large majority. In the relatively short period it has been in office, it has embarked on a number of changes in the structure of Government and economic policies. The Budget for 1978, introduced on November 15, 1977, contains a number of policy initiatives designed to "provide a basis for strong and sustained growth." The explicit objectives identified by the Government are a revival and resuscitation of the economy, increased capacity utilization in the productive sectors, increased employment opportunities, the stimulation of savings and investment, and an improvement in the balance of payments over the medium term. These objectives are to be achieved through a shift in emphasis from direct controls to reliance on the price mechanism, together with a restructuring of relative prices, and an increased role for the private sector.

12. The main thrust of the comprehensive economic reforms, in support of which the IMF granted, in December 1977, a Stand-by Arrangement in the amount of SDR 93 million, is to dismantle administrative controls over the allocation of resources and to set realistic relative prices. On the external front, this involved a major liberalization and restructuring of the external trade and payments system supported by a reform of the exchange rate. Most public sector monopolies in imports (with the exception of food and refined petroleum) have been terminated. Prior licensing of imports has been reduced to a short list of items. Most exchange controls over invisibles transactions have been relaxed. In order to ease the task of managing the external payments position and reduce the bias against tree crop exports and in favor of food imports, the exchange rate has been unified and allowed to float, on the basis of underlying market forces, at an initial level of Rs 16 = US\$1.00.

13. Import liberalization and the reform of the exchange rate required corresponding adjustments of indirect taxes. A new import tariff structure has been introduced. The Business Turnover Tax rates have been substantially lowered and rationalized to be consistent with the new import tariff and exchange rate. Export duties on traditional tree crops have been increased to mop up the bulk of the additional receipts flowing to this sector as a result of the unification of the exchange rate.

14. In order to reduce the drain on resources caused by the sharp increase in the cost to the budget of the food subsidy following the unification of the exchange rate, the rice subsidy has been confined to households with a monthly income of Rs 300 (\$19). This implies that roughly half the population will no longer be entitled to the ration and will have to rely on the open market. To compensate those adversely affected, wages and salaries have been increased, provision was made for a dole of Rs 50 per month for the unemployed, expected to benefit about 350,000 unemployed, and the procurement price of paddy has been raised by 21%. Further, price adjustments arising from the new exchange rate and wage increases were deferred in the case of wheat flour, fertilizer, petroleum, public transport, and infants' milk food. However, price controls have ended for most commodities, and public corporations are to be allowed more autonomy in pricing and distribution policies.

15. The reform of the exchange rate, combined with corresponding adjustments in import and export tax rates, is expected to result in a substantial increase by 75%, in Government revenues in 1978 over 1977 levels. Expenditures have also risen partly due to the exchange rate unification and to increased subsidies and transfers designed to cushion consumers from the impact of the increases in prices resulting from the exchange reform, the reduction in scope of the rice subsidies, and the removal of price controls over a wide range of goods. The combined impact of the various budgetary measures has resulted in a current account surplus of about Rs 650 million, permitting the Government to increase allocations to the capital budget.

16. An adequate response of investment, production, exports, and employment to the major realignment of relative prices introduced in the Budget of 1978 is contingent on a well-thought-out medium-term development strategy. This is recognized by the Government which is beginning the process of identifying the steps necessary to tackle the constraints facing agricultural output, industrial efficiency and exports. The capital budget for 1978 represents a determined effort to raise the level of public investment. Although the sectoral allocations in the budget mainly reflect the momentum of continuation works, the process of allocating financial and manpower resources to three new key programs has already begun. These are: (i) a significant acceleration in the pace of implementation of the Mahaweli Ganga River Development Master Plan (see F-5-b), (ii) a new export processing zone north of Colombo (see F-5-c), and (iii) urban renewal for the Greater Colombo Metropolitan Area (see F-5-d).

17. The Government has also begun the process of integrating these policies and programs into a medium-term investment program (see F-5-a). In order to streamline the machinery for planning, the Ministry of Planning and Economic Affairs has been merged with the Ministry of Finance. The enlarged Ministry has been entrusted with the task of preparing a medium-term investment program by the autumn of 1978. A review of sector programs and policies is also under way. Project preparation capabilities, which have been a major weakness in the past, are to be bolstered by a new UNDP technical assistance Umbrella Project with IDA as Executing Agency. There are a number of parallel bilateral programs involved in similar efforts.

18. The ability of the Government to manage this period of transition in economic policies is greatly enhanced by a relatively strong short-term economic situation. The economy showed signs of recovery in 1977. GDP

rose by 4.3%. This was due mainly to a 7% increase in agricultural output and a 3% increase in manufacturing and services. Paddy production reached a record high of 82 million bushels (1.16 million metric tons) due to favorable weather conditions. Tea production recovered from a low of 433 million lbs in 1976 to 460 million lbs in 1977. Rubber production fell from 345 million lbs to 322 million lbs. Coconut output fell in 1977, reflecting the delayed impact of drought in 1976. With money supply expanding rapidly (29% annual growth in 1977); prices have remained under pressure despite the improvement in supplies. However, there has been a substantial improvement in the external accounts. Export earnings in 1977 rose by a record 37%. This was due in the main to a 69% increase in earnings from tea, brought about by record tea prices. Rubber and coconut exports also benefited from higher unit values, and there was a further encouraging growth in non-traditional exports. Despite various import-inducing policies, such as the March 1977 revaluation and record food imports, imports grew much more slowly. As a result, a current account surplus emerged for the first time since 1965. With a substantial net foreign exchange inflow, gross foreign exchange reserves have risen sizably from \$92 million at the end of 1976 to \$292 million at the end of December 1977. Part of this reserve build-up represents a \$64 million drawing against the SDR 93 million IMF Stand-by Arrangement.

19. This relatively strong performance has been sustained in 1978. Highly tentative estimates place GDP growth over 4%, due once again, to an improved agricultural performance. Paddy production in the Maha (winter) crop (1977/78) is 7% up over 1976/77 levels. The Yala (summer) crop 1978 is likely to be poorer; total paddy production is likely to be around 85 million bushels (1.21 million metric tons), enabling rice imports to be slashed from 534,000 bushels in 1977 to 173,000 bushels in 1978. Tea production is estimated at the 1977 level of 460 million lbs; rubber production at 330 million lbs, and coconuts at 2000 million nuts, will record modest gains over 1977 levels. Industrial production should improve over 1977 levels following import liberalization. But money supply continues to expand rapidly, at an annual rate of 26% through April 1978. The increases in rice and flour prices and wage adjustments announced during the early months of 1978 will also exert pressure on prices; the various official indices still show inflation rates below double digits. The balance of payments situation is likely to undergo a sharp deterioration following import liberalization. But the estimated current account deficit of \$200 million will be more than offset by capital flows, and a further increase in reserves appears likely. At the end of July 1978, gross reserves stood at \$333 million, or approximately four months of imports.

20. The task of external management will be greatly eased in the short-term by the buildup in reserves and the relatively favorable prices for traditional exports. However, Sri Lanka's current account deficit is likely to widen sharply in the coming years for four reasons. First, the new policy of import liberalization will permit industry and trade to replenish depleted stocks and meet some of the large unsatisfied demand for imports of consumer goods intermediates and spare parts. Second, the substantial rehabilitation requirements of the economy will gradually begin to be addressed. Third, as the Government implements its medium-term investment program, major new investment efforts will place an additional burden on the balance of payments. Finally, the increased volume of imports will be set within a background of deteriorating terms of trade in the medium term, as tea prices decline in real terms and foodgrain import costs rise. The success of the program of economic reforms instituted in

November 1977, thus depends heavily on an increase in aid flows. Such an increase will help discourage excessive speculative imports, by strengthening in the eyes of speculators, the Government's ability to persist with its import liberalization policy. It will also enable the Government to desist from more costly forms of borrowings. Most important, increased concessional aid will be needed to supplement the Government's efforts at domestic and external resource mobilization in support of higher levels of investment spending. In this context, local financing will be needed to support this effort, particularly in the early years, when domestic resource mobilization efforts begin to gather momentum.

3. Foreign Asst.
and Debts.

SRI LANKA

Balance of Payments, Debt and Aid.

Balance of Payments Prospects

1. Exports in 1977 were 37% higher than in 1976, largely because of a 60% increase in world tea prices. Exports almost covered imports, and as a result of a surplus on invisibles there was a \$40 million current account surplus, Sri Lanka's first since 1965. Disbursements on foreign aid also increased, and \$64 million was drawn from a Standby-Agreement with the Fund in anticipation of increased imports following the liberalization of November 1977. At the end of 1977, Sri Lanka's external reserves stood at \$292 million (gross), \$200 million higher than a year earlier, and at about 4-6 months worth of imports.

2. The Government was thus in a comparatively good position to absorb the effects of the import liberalization of November 1977. Although the initial impact was weaker than anticipated (there was still a surplus on current account of \$12 million and an overall surplus of \$40 million in the first quarter of 1978), indications are that imports are picking up rapidly. Through May 1978, \$575 million in Letters of Credit had been opened, suggesting total imports for 1978 will be about \$1000 million, some 32% higher than in 1977. Investment goods comprised an unexpectedly high 28% of these LC's while consumer imports were surprisingly low. Exports are showing little growth, as increased prices for rubber and coconut are being negated by the decline in tea prices. In light of these developments, it now appears there will be a current account deficit of about \$200 million in 1978. But this will be offset by increased aid disbursements and capital flows (including \$51 million IMF Trust Fund Drawings), resulting in overall balance-of-payments surplus for the third consecutive year.

3. The medium-term trade prospects for Sri Lanka are, however, not particularly good.

Export prospects are not good, principally because of the anticipated decline in tea prices, as the following table illustrates,

Table 1: Export Current Price Prospects 1978-1985 (1977 = 100)

	Percent of total Merchandise Exports 1975-77	1977	1978	1979	1980	1981	1982	1985	1985*
Tea	46.9	100	78	75	73	77	80	91	57
Rubber	16.1	100	103	113	126	126	135	173	107
Coconut	7.3	100	96	118	116	116	147	174	107
All Tree Crops	70.3	100	86	88	90	92	100	118	74

* In 1977 constant prices.

Source: IBRD, Commodity Price Forecasts, May 1978.

As a result of the expected decline in tea prices in both constant and current prices over 1977, Sri Lanka's terms of trade are likely to deteriorate by well in excess of 25% in the medium-term.

4. In response to the economic liberalization, imports by the private sector are expected to continue the growth they are now beginning to show, while imports of development goods in the public sector should grow rapidly in response to Government's ambitious development programs. There is, however, considerable scope for cutting food imports (35% of total imports) because of the present rice surplus, which should reduce the need to import not only rice but also flour over the next few years, if the proper policy measures are adopted.

5. Nevertheless, mainly because large oil crisis borrowings are maturing, the medium-term debt service burden should decline. The following table summarizes the expected debt service trend.

Table 2: Medium-Term Debt Service Projections (December 1977)

	<u>1977</u>	<u>1978</u>	<u>1979</u>	<u>1980</u>	<u>1981</u>	<u>1982</u>
Debt Service US\$ Million	113	120	83	82	81	75
Debt Service Ratio (%)	13.1	13.6	8.6	8.0	7.1	6.1

III. Aid Prospects

6. Sri Lanka's dependence on foreign aid has risen substantially in recent years. Net aid transfers have gone up from about \$40 million in 1970 to \$139 million in 1977, with gross aid rising from \$63 million to \$199 million. About four-fifths of net aid comes from member countries and institutions of the Sri Lanka Aid Group.

7. Aid prospects in general are good, as the Aid Group has shown strong, decisive support for the Government's economic initiatives. Aid indications at the May 1978 Aid Group meeting amounted to \$380 million, 57% higher than those at the 1977 meeting and about 25% higher than the Bank's recommendation. The following table summarizes the Aid Group's response (exclusive of Mahaweli, which, it was agreed, would be additional).

Table 3: Aid Indications by Aid Group Members 1977-1978
(\$ million)

	<u>1977</u>	<u>1978</u>
Bilateral	161	279
Multilateral	86	98
of which IDA	<u>(46)</u>	<u>(45)</u>
<u>Total</u>	247	377
Project Aid	120	114
Grant Aid (%)	32%	34%

8. Donors indicated continued strong assistance in future, but some donors did state that they might be forced to reassess their food-aid component if Government failed to undertake greater initiatives to increase domestic food production. Particular concern was expressed over flour imports, which were not only a drain on foreign resources and the budget, but also a disincentive to increased domestic foodgrains production

9. Sri Lanka's outstanding debt as of December 31, 1977 is shown below:

TABLE 1 - SRI LANKA

EXTERNAL PUBLIC DEBT OUTSTANDING INCLUDING UNDISBURSED AS OF DEC. 31, 1977
DEBT REPAYABLE IN FOREIGN CURRENCY AND GOODS
(IN THOUSANDS OF U.S. DOLLARS)

TYPE OF CREDITOR CREDITOR COUNTRY	DEBT OUTSTANDING : IN ARREARS				
	DISBURSED	UNDISBURSED	TOTAL	PRINCIPAL	INTEREST
SUPPLIERS CREDITS					
BAHAMAS	1,252	-	1,252	-	-
BELGIUM	2,466	-	2,466	-	-
BERMUDA	2,576	-	2,576	-	-
CANADA	433	-	433	-	-
CZECHOSLOVAKIA	1,304	-	1,304	-	-
FRANCE	17,202	111	17,313	-	-
GERMAN DEM. REP.	116	19	135	17	-
GERMANY, FED.REP. OF	5,783	-	5,783	-	-
HONG KONG	295	-	295	-	-
INDIA	3,445	-	3,445	-	-
ITALY	4,581	227	4,808	-	-
JAPAN	15,949	-	15,949	-	-
KUWAIT	1,114	-	1,114	-	-
NETHERLANDS	2,866	-	2,866	-	-
NORWAY	-	7,102	7,102	-	-
ROMANIA	14,445	-	14,445	-	-
UNITED KINGDOM	1,206	-	1,206	-	-
UNITED STATES	1,553	-	1,553	-	-
USSR	1,845	6	1,851	2	-
YUGOSLAVIA	776	13	789	-	-
TOTAL SUPPLIERS CREDITS	79,207	7,478	86,685	19	-
FINANCIAL INSTITUTIONS					
UNITED KINGDOM	142	-	142	-	-
TOTAL FINANCIAL INSTITUTIONS	142	-	142	-	-
MULTILATERAL LOANS					
ASIAN DEV. BANK	35,692	75,117	110,809	-	-
IBRD	34,327	5,770	40,097	-	-
IDA	54,692	67,054	121,746	-	-
OPEC SPECIAL FUND	8,100	3,150	11,250	-	-
TOTAL MULTILATERAL LOANS	132,811	151,091	283,902	-	-
BILATERAL LOANS					
ABU DHABI	-	5,131	5,131	-	-
CANADA	36,088	20,551	56,639	-	-
CHINA, P.R. OF	32,437	8,229	40,666	-	-
DENMARK	6,916	3,087	10,003	-	-
FRANCE	16,626	6,547	23,173	-	-
GERMAN DEM. REP.	5,443	8,548	13,991	-	-
GERMANY, FED.REP. OF	87,719	29,816	117,535	-	-
HUNGARY	518	7,003	7,521	-	-
INDIA	20,299	20,417	40,716	-	-

TABLE 1 - SRI LANKA

EXTERNAL PUBLIC DEBT OUTSTANDING INCLUDING UNDISBURSED AS OF DEC. 31, 1977
DEBT REPAYABLE IN FOREIGN CURRENCY AND GOODS
(IN THOUSANDS OF U.S. DOLLARS)

TYPE OF CREDITOR CREDITOR COUNTRY	DEBT OUTSTANDING : IN ARREARS				
	DISBURSED	UNDISBURSED	TOTAL	PRINCIPAL	INTEREST
IRAQ	-	19,000	19,000	-	-
ITALY	1,240	142	1,382	-	-
JAPAN	94,382	31,141	125,523	-	-
KUWAIT	14,106	12,671	26,777	-	-
LIBYA	15,000	-	15,000	-	-
NETHERLANDS	5,352	22,718	28,070	-	-
UNITED ARAB EMIRATES	12,265	-	12,265	-	-
UNITED KINGDOM	49,615	279	49,894	-	-
UNITED STATES	162,421	14,593	177,014	-	-
USSR	14,428	62,468	76,896	-	-
TOTAL BILATERAL LOANS	574,855	272,341	847,196	-	-
TOTAL EXTERNAL PUBLIC DEBT	787,015	430,910	1,217,925	19	-

NOTES: (1) ONLY DEBTS WITH AN ORIGINAL OR EXTENDED MATURITY OF OVER ONE YEAR ARE INCLUDED IN THIS TABLE.
(2) DEBT OUTSTANDING INCLUDES PRINCIPAL IN ARREARS BUT EXCLUDES INTEREST IN ARREARS.
(3) THE FOLLOWING UNCOMMITTED PARTS OF FRAME AGREEMENTS AND STANDBYS ARE NOT INCLUDED IN THIS TABLE.

BILATERAL LOANS	
CHINA, P.R. OF	46,366
CZECHOSLOVAKIA	5,718
GERMAN DEM. REP.	5,857
KOREA, D.P.R. OF	1,000
POLAND	4,193
USSR	12,041
YUGOSLAVIA	10,845
TOTAL	86,020
TOTAL UNCOMMITTED FRAME AGREEMENTS AND STANDBYS	86,020

EXTERNAL DEBT DIVISION
ECONOMIC ANALYSIS AND PROJECTIONS DEPARTMENT

4. Annual Meeting
Discussions

OFFICE MEMORANDUM

TO: Files

DATE: September 29, 1978

FROM: K. Sarwar Lateef, ASADC *K. Sarwar Lateef*SUBJECT: SRI LANKA: Minutes of Meeting of September 26, 1978
with the Sri Lanka Delegation to Annual Meetings

1. A meeting was held between the South Asia Region and the Sri Lankan delegation to the Annual Meetings at 9:30 a.m. on September 26, 1978 at the Sheraton Park Hotel. The Sri Lanka delegation consisted of Mr. Ronnie de Mel, Minister of Finance and Planning; Dr. W. M. Tilakaratna, Secretary, Ministry of Finance and Planning; Mr. H. E. Tennekoon, Governor of the Central Bank; Dr. W. S. Karunaratne, Ambassador of Sri Lanka to the United States, and Mr. W. Rasaputram, Alternate Executive Director for Sri Lanka, IMF. The Bank was represented by Mr. David Hopper, Mr. R. Picciotto, Mr. David Dunn, Mr. Bevan Waide, Mr. A. H. Shibusawa, Mr. G. A. McBride, Mr. C. L. Robless and Mr. K. S. Lateef.
2. Mr. Hopper began the meeting by commending the Sri Lanka delegation on the draft Medium Term Development Program. Although Bank staff had not had an opportunity to review the program in detail, their preliminary assessment had been positive. Mr. Hopper requested Dr. Tilakaratna, Secretary, Ministry of Finance and Planning, to stay on next week for more detailed discussions with Bank staff on the program and the latter agreed to do so. Mr. Hopper asked if the program had received Cabinet clearance. The Minister of Finance and Planning, Mr. Ronnie de Mel, replied that the document was still only a draft. On his return to Sri Lanka, he would submit it to the Cabinet together with his draft budgetary proposals. The 1979 outlays for the capital budget shown in the draft had been negotiated with the ministries and were fairly firm. It was, however, difficult to commit ministries to the outlays for the 1980-83 period.
3. Responding to a query from Mr. Hopper on the proposed transfers from current to capital account in the Development Program, the Sri Lanka delegation explained that the Treasury was considering proposals to reduce losses in the four major loss making public corporations (Petroleum, Fertilizer, Milk Board and CTB) as well as further reductions in subsidies. No decisions had, as yet, been made on how far these cuts would go. Very roughly, revenue mobilization efforts in the medium term were likely to be offset by increases in recurrent expenditures and civil servant emoluments. Thus, the bulk of the transfers from current to capital account would have to come from cuts in subsidies and transfers.
4. The Sri Lanka delegation reviewed progress in the economy since the reforms were introduced. Inflation had been kept under control, and prices of some commodities, notably rice, clothes, onions and textiles had come down. Money supply growth had abated. GNP growth in 1978 was estimated at 5.7% per annum. Tea production had fallen slightly, but the hope was expressed that in two or three years the plantations would be put on a sound footing. There had been a record rice harvest. Although information on private sector

industrial output was not readily available, the letters of credit issued for imports of raw materials and machinery suggested a major increase in activity. Electricity consumption was rising at an annual rate of 13%, cement by 38%. The balance of payments situation remained under control. Despite liberalization, reserves continued to rise, and were currently at Rs 6,500 million. The government had begun moving in a number of areas. The Greater Colombo Economic Commission had been established; 100 applications had been received. The government was not encouraging fly-by-night operators. Applicants were being carefully screened and only 25 had been approved. The Ministry of Housing and Local government's program to build 100,000 houses had got off the ground. The redevelopment of the Colombo area, which envisaged property development along the Hong Kong pattern, was still to be undertaken.

5. On the question of tea margins, the Sri Lanka delegation noted that average Colombo auction prices for medium grown had fallen, partly due to a softening in demand (particularly a decline in purchases from Pakistan), but mainly on account of a drop in quality. Mr. Hopper endorsed the Fund's concern on tea margins, and stated that this was an issue on which Bank staff would hold further discussions with Dr. Tilakaratna next week.

6. Mr. Bevan Waide expressed the Bank's concern on the need to strengthen the machinery for planning and aid coordination. The Minister conceded that the planning section of his Ministry could be strengthened. He was, however, unable to find the right people to fill the many vacancies that existed. With some difficulty, he had secured the services of someone from the private sector to coordinate aid for Mahaweli under Mr. Velayutham. Dr. Tilakaratna said that technical assistance was not easy to use when counterpart staff were not adequate.

7. Mr. Hopper expressed concern over Sri Lanka's decision to borrow money in the Euro-dollar market. He said that in the Bank's assessment such commercial borrowing did not seem necessary or desirable, particularly in the context of efforts being made to mobilize external resources through the Aid Group and from the IMF. The Finance Minister replied that at the present stage the government was only making a feeler. There were two considerations behind such a move. First, Sri Lanka might be able to establish a credit rating at a time when its credit was good. If Sri Lanka became well known, it would find it easier to borrow on the Euro-dollar market in the future if this were to prove necessary. Second, the capital markets are highly liquid at present and the spread over LIBOR was likely to be quite small. Mr. Hopper cautioned against the high interest rates attached to such credits, and, he felt Sri Lanka's eligibility for credit with the IMF was good. There was, therefore, no need for such short term borrowing. He also felt that such borrowing might be questioned at the Aid Group. If this was the first of many such credits it would be difficult to hold down the debt-service ratio that had recently shown a major improvement. The Minister of Finance said that he had noted the Bank's concern. Sri Lanka would not rush headlong into such credits, and, in any case, would observe any limits set on such borrowings by the Fund.

8. The meeting reviewed progress on the accelerated Mahaweli program. The Minister outlined the organizational changes made in Sri Lanka to ensure effective implementation of the project. He felt that an adequate organization had now been established at the center, but there was scope for improving implementation machinery in the field. He asked whether the Mahaweli meeting would be held as scheduled in January. Mr. Hopper said that he did not think the meeting should be held prematurely. The Bank would assess the NEDECO report when it became available in November and would consult with other donors. It was necessary to await the findings of some of the feasibility studies now underway so that we might have a better view of cost and project phasings and how much each donor was prepared to finance. He felt that it was important that we should go into the meeting knowing what would come out of it.

9. Responding to a question from the Minister as to whether additionality with respect to Mahaweli was accepted by all donors, Mr. Hopper said that, with the exception of Sweden, all donors had accepted this in principle. It had also been agreed that resource flows into the economy in non-Mahaweli activities should not be interrupted. The Scandinavians were particularly concerned that Sri Lanka should not cut back social programs in order to provide resources for Mahaweli. Mr. Hopper thought that Canada might find it difficult to maintain additionality following the substantial cuts in the Canadian aid allocations. However, Canada was discussing possible cooperation with the United States on Madura Oya and it might be possible in the longer term to hold Canada to additionality.

10. The problems pertaining to Mahaweli II were briefly discussed. Mr. Shibusawa briefly outlined the findings of the recent supervision mission and expressed concern that the difficulties being experienced in implementation of Mahaweli II would weaken the case for substantial support to the accelerated program since those who were co-financing Mahaweli II were also involved in assisting the accelerated program.

11. The status of the Kotmale project was reviewed. Mr. Hopper noted that Sweden had made it clear that it was unable to accept additionality. He questioned the wisdom of tying the project to Swedish commercial contractors since this foreclosed financing by other donors. If SIDA itself could be persuaded to underwrite the project, the problem of a shortfall in financing may be overcome. Dr. Tilakaratna stated that the Treasury shared the Bank's reservations about the financing of Kotmale. He felt that it would be unwise to use up the Swedish resources that would in any case be available to Sri Lanka. The Treasury had instead proposed that the government call for international bids and seek co-financing. Mr. Hopper said that another approach would be to delink Kotmale altogether from the cluster of Mahaweli projects, treating it as purely a power project that could be financed outside the accelerated program. The key question then would be whether Kotmale was the most rational next step in meeting Sri Lanka's power needs. Mr. Ronnie de Mel suggested that Mr. Hopper might discuss this idea with the Sri Lanka President when he met him in October.

12. The problem of water charges was discussed. Mr. Hopper expressed pleasure that this thorn was about to be removed. The Sri Lankan delegation revealed that circulars had been issued to government agents to prepare

registers so that recovery would begin in 1979. Bank staff noted that the amount to be recovered did not fully cover O and M costs.

13. Mr. Picciotto raised the issue of the dairy development project. Government pricing policies had led to a situation where farmers found it more profitable to slaughter their cattle, thus reducing the supply of milk. Dr. Tilakaratna said that the government was actively examining the possibility of increasing the price of milk bought from farmers from Rs 0.90 to Rs 1.40 a lb. Since this was likely to result in an increase in the budgetary subsidies, the Treasury was examining the possibility of increasing the price of milk products to the consumer. A Cabinet paper was under preparation.

14. Mr. McNamara's visit to Sri Lanka on October 12/13 was reviewed and the program for Mr. and Mrs. McNamara was approved.

15. In conclusion, the Minister asked what the Bank's financial contribution to the accelerated Mahaweli program would be. Mr. Hopper explained that it would be difficult to apply the concept of additionality in the case of IDA because of the mechanism used to determine country allocations. Much also depended on the progress with the sixth IDA replenishment. The Bank would review the gaps in financing of all the different Mahaweli projects. It could also look at Kotmale. The Bank looked forward to a dialogue with the Government of Sri Lanka on what would be the most optimum use for its resources in Sri Lanka in the context of the Government's Medium Term Development Program.

CC

cc: Messrs. Hopper, Picciotto, Dunn, Waide, Pilvin, Shibusawa, McBride, Robless and Lateef

5. Briefs on
Special Issues

SRI LANKA

MEDIUM TERM DEVELOPMENT PROGRAM

I. BACKGROUND

1. As an integral part of the policy reforms being undertaken to stimulate economic development, the Government decided, with World Bank and IMF encouragement, to prepare a Medium Term Development Program. Preliminary work was undertaken in early 1978--by May a draft macro-economic framework had been prepared and most of the ministries had submitted investment programs and strategy statements, and a general statement of strategy and policies was presented to the Aid Group at the May 1978 meeting. In addition, some institutional changes were made: the treasury and planning functions were brought together in the new Ministry of Finance and Planning and the regular meetings of Secretaries of development ministries were reinstated. Further, in September 1978, the Ministry of Irrigation, Power and Highways and the Ministry of Agriculture and Lands were recombined* to better administer the ambitious irrigation development and settlement programs. The Department of Irrigation was combined with the Department of Lands to create the new Ministry of Lands and Lands Development and a separate Ministry of Mahaweli Development was established. The Department of Agriculture was renamed the Ministry of Agricultural Development and Research, and the Departments of Power and Highways became the new Ministry of Power and Highways.

2. At the request of the Government, the World Bank has played an advisory role in the preparations for the Medium Term Development Program. A one-man mission visited the country in February 1978, and in June, once the first round of the exercise had been completed, a three-man mission returned to discuss how preparation might best continue. Although the Government's original intention had been to complete the preparation of the Medium Term Development Program by September 1978, it became apparent during the June mission that this was no longer realistic or indeed desirable:

- The basis for major decisions concerning investments in several key sectors, especially agriculture, had only recently begun to be established. Several key investment-oriented studies (including a Tea Master Plan, a major fertilizer distribution study, and the Mahaweli Implementation Strategy Study) would not be completed and assessed by September 1978. Also, the investment required for the Government's three major programs (Mahaweli Development, Export Processing Zone, and housing and urban redevelopment) would not have been clearly determined by that date, as detailed feasibility studies had still to be undertaken.

- Considerable work was still required to ensure that proposed investments were consistent with sectoral priorities and objectives.
- Initial investment proposals far exceeded resource projections; considerable work was needed to reconcile competing claims, and establish reasonable intersectoral balance.

The mission therefore suggested and Government concurred, that a two-stage approach to develop the Medium Term Development Plan be undertaken. Stage I, which would be completed by November 1978, would entail revision of the macro-framework on the basis of more up-to-date domestic and external resource projections, the determination of intersectoral priorities, and the establishment of macro and sectoral policies, with the priorities and policies so determined to be incorporated into the 1979 budget. Stage II would be completed by September 1979 as the various studies referred to above are completed and assessed. It would include the detailed investment program and a comprehensive list of projects. A draft document incorporating the major components of Stage I has been prepared. While we have not had an opportunity to carefully review this document, the major issues relating to the medium term are outlined below.

II. MACROECONOMIC ISSUES

3. To achieve its target rate of growth of real GNP of 5.5% per year, the Government has estimated that investment would have to total Rs. 77.6 billion for 1979-83 in current prices. If achieved, the investment to GNP ratio would rise from the 1971-76 average of 16.0% to 25.8% by 1982. Both the public and private sectors are expected to assume major responsibilities, the public sector accounting for Rs. 46.8 billion or 60.3% of the total investment, and the private sector, the remainder. In both sectors, there are major macroeconomic issues that must be addressed.

A. The Public Sector

4. The effectiveness with which the public sector fulfills the key role assigned to it will depend upon the amount of resources it can generate and the composition of its investment program.

5. Resource mobilization. In order to meet the public sector investment target as well as allow for increasing current expenditures, which must not only increase with development expenditure, but must also be raised to provide for much needed salary increases and higher maintenance outlays, the resource mobilization effort will have to be intensified. It will be difficult to do this by new revenue measures alone, as the Sri Lankan economy is already highly taxed by developing country standards (17.9% of GNP in 1977), and tea export duty revenues, the largest single source of revenue (38% of 1978 revenues), are likely to decline with the falling price of tea (especially if tax rates are adjusted--as they must be--to maintain tea producer margins). Hence, increased cuts in government subsidies and transfers will have to play a key role in increasing resources for investment. The Government is

committed in general to reducing subsidies and transfers (which comprise about 36% of the current budget) to the extent possible; however, it finds itself constrained by possible political unrest and the desire not to erode Sri Lanka's social gains. The draft development program envisages an increase in the resource transfer from current to capital budget over and above any revenue raising measure from 2.1% of GNP in 1979 to 4.5% of GNP in 1983. But the Government has yet to spell out precisely how this is to be accomplished.

6. Despite the assumed increase in the current account surplus over the medium term, which, if it is to materialize, would require unprecedented political courage and fiscal discipline, and expanded recourse to domestic borrowing, the bulk of public capital expenditures are to be financed by external assistance (67% of the total). The external aid flows appear, on a preliminary assessment, to be reasonable, in the light of the aid indications received at the May 1978 Aid Group, provided that assistance for the accelerated Mahaweli is entirely additional to regular aid flows, and efforts are made to significantly step up the pace of disbursements.

Table 1: Financing of Public Investment Program
(Rs million, at current market prices)

	<u>1978</u>	<u>1979</u>	<u>1983</u>	<u>1979-83</u>
Public investment	4,862	5,834	12,536	46,764
<u>Financed by:</u>				
Public Savings	686	538	1,735	5,953
Non-Bank Domestic Borrowings	1,127	1,482	1,968	8,710
Foreign Aid (net)	3,049	3,814	8,833	32,101

7. Investment Balance. A second key issue that the Government faces is the balance to be struck between its three long-gestating priority projects on the one hand, and other equally important new projects as well as ongoing projects on the other. The first benefits from the Rs 11 billion accelerated Mahaweli program will not begin to flow until 1983; investment by the Greater Colombo Economic Commission is primarily in supportive infrastructure for the proposed investment promotion zones; and the largest component of the Rs 4.0 billion Housing and Urban Redevelopment Program is the construction of 100,000 low-cost homes at a cost of Rs 2.4 billion. Clearly, unless investment in these priority projects is balanced with quicker-gestation production-oriented projects, the Government runs the political danger of not being able to demonstrate tangible economic progress while awaiting the results of its priority projects, and the economic danger of inflation and balance of payments deterioration as demand for consumption goods swells during the peak Mahaweli investment years of the early 1980s.

8. The Government recognizes the need for such balance. In its draft program it has tentatively budgeted about 32% of public investment for its three priority programs, another 29% for continuation and replacement works and 39% for new projects. This balance appears appropriate, although we are

concerned that the housing and urban renewal investment will absorb a disproportionate amount of resources whose benefits will not accrue primarily to the poorest sections of society. The program is, however, predicated on:

- (i) success in mobilizing the sizable domestic and external resources that will be needed to finance this unprecedented high level of investment;
- (ii) appropriate phasing of investment during the 1980-83 period, which has yet to be specified;
- (iii) a detailed screening of ongoing projects to ensure their consistency with and contribution to the revised policy objectives and
- (iv) identification and preparation of new projects that have the potential for bringing about an early flow of benefits.

At this time, we have not been able to scrutinize the tentative list of old and new projects identified in the development program to examine whether these are consistent with government objectives.

B. The Private Sector

9. About 40% of total investment in the Medium Term Development Program is to be generated by the private sector. Because their investments would be less capital-intensive, they would help in increasing employment and production in the short term.

10. The climate for private investment has improved greatly with the economic reforms undertaken by the new Government, including: the liberalization of imports, unification of the exchange rate, establishment of the GCEC, and reduction of price controls. Growth in imports of investment, maintenance, and intermediate goods are encouraging signs that private sector investment and production is picking up. But in view of the significant role that the private sector is expected to play in achieving the objectives of the Medium Term Development Program, the Government recognizes that it will have to ensure that continuous attention is given to the incentives and promotion facilities that a thriving private sector will require.

III. GENERAL SECTORAL ISSUES

11. The following key sectoral issues need to be addressed to create a favorable policy environment for the Medium Term Development Program. Four major themes that cut across sectors stand out: the need to expand non-traditional exports, the role of the public sector corporations, the manpower situation, and the question of agricultural price incentives.

12. Exports of manufactured goods, exclusive of tea and rubber products, are extremely small, even for a country at Sri Lanka's stage of industrial development. Given the import liberalization measures of November 1977, and the generally unfavorable prospects for tree crop exports in the medium term, it is imperative that Sri Lanka expand non-traditional exports if a strong balance of trade deterioration is not to

occur. A major initiative of the Government in this connection is the establishment of the Greater Colombo Economic Commission (for details, see F-5-C). Additional major policy initiatives, however, are also required. The experience of other developing countries suggests that a successful export promotion program requires deliberate policy measures to reduce the bias against exporting, resulting from high tariff protection afforded to domestic production activities. The introduction of direct cash subsidies or tax concessions on export income deserves serious consideration. Another important component of a successful promotion strategy is the institutional framework which, despite various formal mechanisms, remains weak. The Export Promotion Council of Ministers and the Export Promotion Advisory Committee of Secretaries need to be revived. The Export Promotion Secretariat needs to be strengthened in staff and financial resources and overseas representation in major trade centers needs to be considered.

13. Public sector corporations in Sri Lanka account for 60% of the gross value of production in the organized industrial sector; they also control 60% of the tea land, 32% of acreage under rubber and 10% of land under coconuts. With little exception, however, the performance of public sector units leaves much to be desired. Capacity utilization remains low at about 50-60%; financial performance has deteriorated to a point where net profits for many have become negative. Given that they pre-empt so much resources (25% of total expenditure in 1977), a comprehensive program needs to be developed to improve the performance of this critical sector. Such a program should include:

- (1) an effective organizational set-up for public enterprises;
- (2) specific rules guaranteeing greater autonomy in management;
- (3) incentive bonus schemes for managers and workers, based on their performance;
- (4) effective devices for monitoring their performance.

Furthermore, a detailed program to improve production efficiency needs to be formulated and implemented on a priority basis for a few selected industries/enterprises.

14. One of the most critical development constraints the country faces is the acute shortage of trained and skilled and semi-skilled manpower in key areas. While this reflects inadequate training programs, the problem has been exacerbated by the rapidly increasing rate of migration to the Middle East and the accelerating "brain drain" of manpower, such as engineers. In the preparation of the Medium Term Investment Program, we have therefore recommended that the Government pay particular attention to the need for:

- (i) careful evaluation of the manpower implications of all major projects in the Investment Program;
- (ii) thorough review of the uses to which Government's current manpower is being put, with a view to redeploying them more purposefully;

- (iii) strengthening training programs;
- (iv) more effective use of contractual and consultancy services in the private sector; and
- (v) greater recourse to technical assistance for project planning and implementation.

15. Although the Government has made encouraging progress on a number of fronts towards relaxing price controls and permitting the price mechanism to allocate resources (e.g. import liberalization, reduction of the rice and transport subsidies), there are still important areas for further progress. One of the most crucial is the maintenance of strong agricultural price incentives. In field crop agriculture, further upward revisions in the flour price are warranted. Not only is consumer preference shifting away from rice to the relatively cheaper flour, with the result that Sri Lanka has built up a larger rice surplus than it can properly store, but cheap imported flour is also proving a disincentive to the production of foodgrains, especially coarse grains for which flour is a substitute. Since lowering the price from Rs. 0.80 to Rs. 0.60/lb. after the elections, the price has again been raised to Rs. 1.12/lb. However, this is still below the international price. Measures are also needed to ensure that adequate tea producer incentives are maintained which allow sufficient margin to enable investment needs to be met from producers' resources. Currently, producers are bearing the entire burden of falling prices with the consequence that margins are declining to the point that investment needs can no longer be met from internal resources. In view of this, there is an urgent need to review the system of tea exports taxation so as to maintain adequate producer margins.

b. Mahaveji Ganga
Dev. Pro.

SRI LANKA

MAHAWELI GANGA DEVELOPMENT PROGRAM

I. Introduction

1.01 In an effort to increase agricultural production, create jobs for the unemployed, and stimulate economic development, the new Government of Sri Lanka, under the leadership of President J. R. Jayawardene, has given top priority to the implementation of the Mahaweli Ganga Development Program in as short a time as possible. The Program, the largest multi-purpose river basin development ever undertaken in Sri Lanka, is based on a Master Plan prepared jointly by a UNDP/FAO team and Sri Lanka engineers in 1965-68. The Plan envisaged development of about 900,000 acres of irrigable land in the dry zone, as well as of about 500 MW of hydropower. It was divided into three phases, each including several projects, for stepwise implementation over a 30-year period.

1.02 The initial construction (under the Mahaweli Ganga Development Project I (Credit 174/Loan 653) began in 1970 on diversion headworks at Polgolla on the Mahaweli Ganga and at Bowatenna on the Amban Ganga, including a 40 MW hydropower plant at Polgolla. These works, constructed with financial assistance from the World Bank, are now in full operation, and a second 40 MW hydropower plant at Bowatenna is under construction with assistance from the Asian Development Bank. These headworks provide an improved water supply to about 130,000 acres of existing irrigated land and a full irrigation supply to about 90,000 acres of new land. Work on the Mahaweli Ganga Development Project II (Credit 701) for development of irrigation systems, construction of infrastructure for settlement, and provisions for agricultural extension and support services are underway with assistance from the Bank in collaboration with Canada, the Netherlands, U.K. and U.S.A.

1.03 Whereas these works represent a significant start in the implementation of the Program, the Government now realizes that, at the present rate of construction, and given the current rate of population growth, the Program will not have much impact on the country's economy in terms of meeting the serious food shortage and unemployment problems. Accordingly, the Government has consolidated the remaining works into twelve projects, with a view to construct them in as short a time as possible.

1.04 General agreement on the desirability of accelerating the implementation of the Plan was reached between the Government and the Bank during a meeting between Mr. McNamara and Mr. R. Coomaraswamy, Advisor to President Jayawardene, on November 29, 1977 in Washington, D.C. The agreed approach, which emerged during subsequent discussions in the Bank, called for an Implementation Strategy Study, which is presently being carried out by Netherlands-financed consultants (NEDECO). The principal objective of the study is to review the UNDP/FAO Master Plan, examine the implications of various alternative phasings of the twelve projects, and recommend a specific Action Plan taking into account technical, financial, economic, institution and manpower aspects. It was also agreed that the Study need not hold up progress of on-going work, and should, in fact, proceed simultaneously with the execution of readily implementable projects for which the technical and economic viability has been clearly established.

II. Accelerated Program and Costs

2.01 During the early months of 1978, the Government of Sri Lanka contacted several prospective donor agencies for assistance. Based upon these discussions, the Government decided to launch an accelerated Mahaweli Program, including the construction of six major reservoirs with canal systems to irrigate about 340,000 acres of new land (see Map) and five hydroelectric power plants. These six projects are:

- (a) Victoria Reservoir-Minipe Diversion Complex, including Victoria Dam, power plant, Right Bank transbasin canal, and Ulhitiya Dam;
- (b) Randenigala Reservoir and power plant, designed to operate in cascade with the Victoria Reservoir;
- (c) Maduru Oya Reservoir, augmented by releases made possible by the Victoria and Randenigala Reservoirs;
- (d) Rotalawela Reservoir;
- (e) Maragahakanda Reservoir and power plants; and
- (f) Kotmale Reservoir and power plant.

Included in these works would be the irrigation systems, land development, social infrastructure, settlement, and agricultural extension and support services for the benefitted areas in Systems C (74,000 acres) and B (118,000 acres) in the right bank of the Mahaweli Basin, System A (100,000 acres) in the Maduru Oya Basin, and System D (46,000 acres) in the left bank of the Mahaweli Basin. In addition to employment for hundreds of thousands during the construction, these projects will provide an estimated 140,000 farm families with gainful employment in agriculture and allied pursuits. They will also provide about 390 MW of hydropower (Victoria Dam - 120 MW, Randenigala Dam - 75 MW, Maduru Oya Dam - 5 MW, Moragahakanda Dam - 40 MW, and Kotmale Dam - 150 MW). Details of these works are contained in Attachment I.

2.02 Based upon preliminary estimates of available resources, both domestic and foreign, the Government has tentatively earmarked about Rs 8.0 billion (US\$533m equivalent) in 1978 prices, or Rs 11.0 billion (US\$733m equivalent) in current prices, for these projects over the next 5-6 years. This amount would permit the Government to substantially complete these projects by end 1983, as planned. It also appears to be manageable in relation to projected domestic resource availability over the 1979-83 period.

III. Organization for Implementation

A. Policy and Overall Coordination

3.01 The determination of policies relating to the implementation of the accelerated Program is vested in the Cabinet Sub-Committee on the Mahaweli Ganga Development Program. The Sub-Committee is chaired by the President, and includes the

Minister for Finance and Planning and the Minister for Irrigation, Power and Highways. 1/ It meets weekly to consider policy matters put before it, and it acts with the full authority and power of the Cabinet. The meetings are attended by the Chairman Designate of the proposed Mahaweli Development Authority, the Secretary to the Cabinet, the Secretary for Finance and Planning, and the Secretary for Irrigation, Power and Highways. 1/

3.02 The Government is in the process of setting up the proposed Mahaweli Development Authority under special legislation. The Authority will be in sole charge of the implementation of the Mahaweli Program. The functions of the Authority will be wide in scope, covering all aspects of the Program. As the chief planning, financing, executing and coordinating body, the Authority would direct the activities of the different implementing agencies, including the Mahaweli Development Board, Central Engineering Consultancy Bureau, Irrigation Department, and the River Valleys Development Board. All financial requirements of the Program will be channeled through the Authority to these agencies. The legislation for the Authority would include provision for the Minister for Irrigation, Power and Highways, 1/ to establish additional implementing agencies as required. The actual establishment of the Authority is imminent.

B. Program Implementation

3.03 The Mahaweli Development Board (MDB), established in 1969 is responsible for the execution of all irrigation systems and infrastructure in the Program, except the storage dams and headworks. At present, the Board is being reorganized with separate units under Project Managers to carry out the development works in the ongoing Mahaweli Project II area and the areas to be irrigated by the Victoria, Randenigala, Maduru Oya and Moragahakanda Reservoirs. In addition to its engineering staff, the MDB has the full range of expertise required for carrying out its multi-sectoral responsibilities.

3.04 The Central Engineering Consultancy Bureau (CECB) was established in 1973 to provide engineering services for several Government Departments and agencies concerned with development. It now provides such services primarily for the Mahaweli Development Program. Specifically, the CECB is responsible for the preparation of feasibility reports, plans, designs and construction supervision for the dams and headworks in the Program. In addition, it is planning the access roads, construction camps and other preparatory works in order that construction on the dams could start early.

3.05 Although the CECB has about 200 engineers, very few are senior engineers with experience. Over the last two years there has been an exodus of senior- and middle-grade irrigation engineers for more lucrative positions overseas. To meet this situation, the Government has recently instituted an incentive program designed to stem the flow abroad of experienced engineers. It is also trying to persuade some senior engineers, who left during the last few years, to return. In addition,

1/ At the time of preparation of this brief, the Government of Sri Lanka informed that the Ministry of Irrigation, Power and Highways has been split into three Ministries, namely (a) Ministry of Power and Highways, (b) Ministry of Lands and Land Development, and (c) Ministry of Mahaweli Development. Further information is awaited.

the CECB has recently engaged the services of a few specialists from India, each with 20-30 years' experience to provide technical assistance in water resources planning, engineering geology, power plant design, electrical and mechanical engineering and hydrology.

3.06 The Irrigation Department (ID) is an old and well-established department with experience in the construction and operation and maintenance of dams and irrigation and drainage systems throughout the country. At present, the ID is carrying out geological investigations survey of construction material, soil testing, and hydrological studies for the Victoria, Randenigala, Maduru Oya, and Moragahakanda dams. In addition, the ID will be responsible for the design and implementation of the Minipe Anicut, Right Bank transbasin canal, and Ulhitiya Reservoir, including the irrigation system in the southern part of System C. During the recent years, the Department as a whole, suffers from the shortage of middle-grade engineers; about 50 engineers left for jobs abroad during the last two years.

3.07 The River Valleys Development Board (RVDB) acts as a contractor. Along with other local contractors, the RVDB will carry out medium and minor irrigation works in the Program. Other works, such as land clearing and levelling, drainage systems, and social infrastructure, will be contracted out to private contractors, State Construction Corporations, and Army Corps of Engineers. The Government expects foreign contractors to construct the major dams on a turnkey basis through International Competitive Bidding (ICB).

IV. External Assistance

4.01 Included in the Government's Rs 11.0 billion (current prices) budget is a foreign exchange component estimated at about one-half the total cost, or about Rs 5.5 billion (US \$367 million). In light of the magnitude of this investment, the Government has sought technical and financial assistance from several multilateral and bilateral aid agencies, with a view to covering the foreign exchange expenditures and a substantial part of the local costs. At the Government's request, the Bank has agreed to assist in mobilizing and coordinating the external assistance required.

4.02 At the Aid Group meeting in May, the implementation of the accelerated Mahaweli Program was discussed as a special item on the agenda, during which three important principles concerned with external assistance were agreed: (i) the investment in the Program for the 1979/1983 period should be kept to about Rs 8.0 billion in 1978 prices, or Rs 11.0 billion in current prices, so as not to neglect the requirements of other priority projects for generating short-term outputs, as well as for the maintenance and rehabilitation of existing works; (ii) donors should treat the Program as additional to their regular aid effort; and (iii) external financing for the Program should be entirely on concessionary terms.

4.03 The Netherlands-financed Consulting firm, NEDECO, who began work in Sri Lanka in early April, is carrying out the Implementation Strategy Study (para 1.04). Upon completion of this work, it will recommend a specific Action Plan taking into account the Government's interest in taking up, as a matter of urgency, the construction of the six major projects included in the accelerated

Mahaweli Program. It is expected that, by mid-November 1978, the consultants will be in a position to recommend with a reasonable degree of certainty the optimal sizes of the reservoirs and the sequence of implementation of the individual projects. The work will involve about 130 man-months of consultant's time about 200 man-months of Sri Lankan counterpart time, carried out over a 15-month period ending in June 1979.

4.04 To serve as General Consultants, the Bank has engaged a French engineering consulting firm, SOGREAH, using available UNDP funds. SOGREAH has been associated with the Mahaweli Program since 1970 as consultants for the supervision of the Mahaweli Ganga Development Project I and for the preparation of the Mahaweli Ganga Development Project II, both assisted by the Bank. The General Consultants are assisting the Government by providing specialists to carry out services related to the preparation of feasibility studies, designs and tender documents for the projects in the Program as requested by the Government. In addition, the consultants are reviewing and assessing on a continual basis, the feasibility and design works being carried out by bilateral-financed consultants and advising the Government on their adequacy. The consultants are also liaising regularly with the Bank so as to assist it in carrying out its coordinating role. The consultants began work in Colombo in June.

4.05 The Victoria Project includes the dam, power plant (120 MW), Minipe Diversion Complex and the development of irrigation works and infrastructure on the Mahaweli Basin right bank area of 74,000 acres (System C). With the high priority already established by UNDP/FAO and the Government for the Victoria Reservoir, the Government is trying to move ahead with its implementation. At the Government's request, the U.K. engaged and is financing consultants to assist in updating the UNDP/FAO feasibility study (1968/69) and preparing the final design and tender documents. The consultants began the feasibility work in Colombo in early June and will begin final design and preparation of tender documents by January, by which time the NEDECO team would have completed their preliminary study on reservoir sizes and be able to determine vital features of the dam and reservoir.

4.06 The Randenigala Project, located about 13 mi. below the Victoria Reservoir, and operating in cascade with it, includes the dam, power plant (75 MW), and irrigation works and infrastructures. Its purpose is to provide long-term regulation of flow, generate hydro-electric power, and reduce peak flood flows. In addition, Victoria and Randenigala will provide irrigation water for System B (125,000 acres) in the Maduru Oya Basin via the Right Bank canal, Ulhitiya Oya Reservoir and 4.5 mi. tunnel to the proposed Maduru Oya Reservoir. The Government has requested the Republic of Germany to engage and finance consultants to prepare a feasibility study for the reservoir. Germany has agreed to do so and expects the consultants to commence work in Sri Lanka by November of this year. The Government hopes that Germany will also agree to finance the final design and tender documents, and eventually the construction of the project.

4.07 The Maduru Oya Project includes the Ulhitiya-Maduru Oya tunnel (4.5 mi.), Maduru Oya dam, power plant (5 MW), and irrigation system and infrastructure for the development of about 125,000 acres in the Maduru Oya Basin (System B), of which 118,000 acres will be new land. Its irrigation waters will be augmented by releases from the Randenigala Reservoir. The feasibility study, final design and

tender documents for the reservoir are being prepared by the CECB assisted by SOGREA. A Canadian-financed team of consultants will oversee this work with a view to ensuring that it meets standards suitable for Canada to consider financing the construction. In addition, the Government of Sri Lanka has engaged and is financing a Canadian consulting firm (Acres) to carry out a feasibility study for the project. The Government hopes that Canada will assist in the financing of the Project.

4.08 The Moragahakanda Project includes the dam across the Amban Ganga (largest left bank tributary of the Mahaweli Ganga), the power plant (40 MW), and irrigation works and infrastructure for the development of about 46,000 acres in several areas located in the Mahaweli Basin left bank. The regulated flow from the Amban Ganga catchment area, together with supplemented Mahaweli flows diverted at Polgolla (completed works), will be utilized for irrigation and hydroelectric purposes. To expedite the implementation of the project, the Government has requested Japan to engage and finance a consulting firm to prepare a feasibility study, final design and tender documents. Japan responded to this request by sending a mission in May to inspect the dam site, review the project, and prepare terms of reference for the consulting firm. The mission reported favorably and consultants are scheduled to begin the feasibility work in Sri Lanka by end October this year, followed by design work and tender documents beginning in March 1979. After this work, the Government hopes that Japan would assist in financing the construction of the project.

4.09 The Kotmale Project includes the dam and a 4-mile tunnel and underground power plant (150 MW). Its purpose is to provide storage, regulation of flow for hydroelectric power and irrigation. The feasibility study for the project was prepared by the Water and Power Development Consultancy Services (India) Ltd., under technical assistance from the Government of India. The Government of Sri Lanka has requested the Government of Sweden to assist in the financing of the project. A Swedish contractor (SKANSKA), a member of the Swedish Hydropower Group, has reviewed the feasibility study and has proposed to the Government that the final design and tender documents be completed during construction by the CECB assisted by SWECO (group of Swedish consulting firms). SKANSKA would expect to start construction of preliminary works by January 1979 (access roads, bridges, campsite, etc.), followed by construction of the dam and power plant, with project completion by 1984. The Government is considering the proposal at present and negotiations are currently in progress with the Government of Sweden with a view to ensuring that Swedish assistance to the project would be additional to Sweden's normal aid flows.

4.10 Other external assistance included an agreement by the Government of Canada to finance feasibility studies for all other projects in the UNDP/FAO Plan. A Canadian firm of consultants is at present reviewing the available data and information needed for drawing up consultants' terms of reference. In addition, the USAID has indicated that it would consider the financing of irrigation systems, on-farm development and infrastructure (village centers, roads, health facilities, schools, markets, etc.) for the projects in the Program. The USAID is also considering financing an in-depth study of the impact of the Program on the environment.

SUMMARY OF PRIORITY PROJECTS SELECTED FOR IMPLEMENTATION AND THEIR CURRENT STATUS ^{1/}

<u>Project</u>	<u>Data</u>	<u>Active Reservoir Capacity</u>	<u>Est. Hydropower Installed Capacity</u>	<u>Estimated Area to be Irrigated</u>	<u>Estimated Cost</u> ^{2/}	<u>Current Status</u>
Victoria (including Right Bank Canal; new Minipe weir and Ulhitiya Reservoir).	Gravity arch 250 ft high, 1100 ft long.	130,000 ac ft.	120 MW	3,000 ac and 16,000 ac of existing irrigation areas in System C and E, and 74,000 ac of new land in System C.	Victoria Complex \$130 M; Total project: \$220 M.	Updating of feasibility study is underway by consultants provided under bilateral assistance from U.K. Final design specifications and tender documents of Victoria Dam will start in November.
Randenigala	Concrete gravity or rockfill or earthfill, 290 ft high, 1800 ft long.	370,000 ac ft.	75 MW	Together with Victoria and Maduru Oya Projects, it will irrigate 118,000 ac of new land in System B.	Randenigala Complex \$120 M.	Consulting firm has been selected by Fed. Rep. of Germany. Feasibility study will be started by the firm in November under FRG's technical assistance program.
Maduru Oya	Earthfill, 150 ft high, 1800 ft long.	290,000 ac ft.	5 MW	7,000 ac of existing area in System B, and 118,000 ac of new land, also in System B (with Randenigala Reservoir).	Maduru Oya Dam and Tunnel \$45 M; Total Project: \$180 M.	Geophysical investigations of the dam site and Ulhitiya - Maduru Oya tunnel will begin in October this year. Final design of the dam is being carried out by CECB assisted by SOGREA. Consultants (Acres of Canada) have been engaged by GOSL for feasibility study of whole project.
Moragahakanda	Composite - concrete, rockfill and earthfill; concrete - 230 ft high, 1700 ft long; rockfill 170 ft high, 1300 ft long; earthfill 70 ft high, 2100 ft long.	470,000 ac ft.	40 MW	46,000 ac of new land in System D.	Moragahakanda Dam \$90 M; Total Project \$140 M.	Mission from Japan conducted pre-feasibility study and concluded that the project is favorable. Consulting firm selected by Japan will start the feasibility study under Japan's technical assistance program by end October this year.
Kotmale	Rockfill 360 ft high, 1930 ft long.	297,000 ac ft.	150 MW	To increase water supply diverted at Polgolla by 250,000 ac ft annually for irrigation.	Total project cost: \$160 M	Feasibility completed. Final design, specifications and tender documents are under preparation by CECB. Negotiations with SKANSKA, Swedish Contractor, are underway for construction of project.
Rotalawela	Earthfill, 80 ft high, 6700 ft long.	184,000 ac ft.	None	14,000 ac of existing area and 100,000 ac of new land in System A.	Rotalawela Complex \$35 M; Total Project: \$140 M.	No activity yet.

^{1/} All figures mentioned hereunder are rough estimates.

^{2/} Costs are at estimated current prices, calculated basing on UNDP/FAO Master Plan costs (1968) multiplied by inflation factors.

Countries and Organizations Interested in Assisting Sri Lanka
in Mahaweli Ganga Development Program

<u>Country</u>	<u>Assistance For</u>
Netherlands	Implementation Strategy Study (underway by NEDECO).
United Kingdom	Updating the feasibility study and preparation of design and tender documents for Victoria Project (incl. dam, hydro-power plant, irrigation system and social infrastructures in project area), and possible implementation of the project.
Federal Republic of Germany	Feasibility study of Randenigala Project (incl. dam, hydropower plant, irrigation system and social infrastructure), and possible implementation of the project.
Japan	Feasibility studies of Moragahakanda Project (incl. dam, hydropower plant, irrigation system and social infrastructure) and possible implementation of the project.
Canada	Feasibility studies for other projects in the Mahaweli Ganga Development Program and possible implementation of Madura Oya Project.
Sweden	Possible implementation of Kotmale Project (dam and underground power plant). Discussions between GOSL and Sweden are ongoing.
United States	Study on the impact of the Mahaweli Ganga Development Program on environment. Initially the planning and design of irrigation systems, land development and development of social infrastructures for projects under the Program, and possible implementation of these project components.
Asian Development Bank	Particulars to be determined.
United Nations Development Program	Technical assistance for the Program as requested by the Government. Initial assistance, estimated at US\$1 million, is provided under the UNDP-financed Umbrella Program for Sri Lanka for financing Consultants (SOGREAH).
World Bank	Execution of the above UNDP-financed Umbrella Program and acting as Co-ordinator for the Mahaweli Ganga Development Program. Other assistance, technical and financial, will be determined as appropriate.

SRI LANKA
MAHAWELI GANGA DEVELOPMENT PROJECT II

Comments and Recommendations of the August/September 1978 Review Mission

At the September 14, 1978 meeting in the office of the Director General, Mahaweli Ganga Development Authority to discuss the IDA/co-financing countries review of the project, Mr Panditharatne requested that the Mission's views and recommendations on project implementation progress and work quality be submitted in written form for review and guidance on future work. With the concurrence of Mr Shibusawa, Chief Programs Division (IDA), the following observations and recommendations are made:

Observations:

1. Since the project was formulated with the view that it would serve as a model to be replicated in other command areas to be developed in the Mahaweli Ganga Program, the project works should be well planned and constructed to ensure successful development. The Mission's field review did not substantiate that this is being done. It is the Mission's view that vital planning has not taken place and work activities are not being properly coordinated, resulting in work being poorly constructed and improperly timed. Some work is not being done and modifications are being made which are detrimental to the project plan.

Systematic planning has only recently been started and is far behind construction activities. However, this planning as now being done will provide the basis for sound management and proper scheduling of the work and additional staff for the Planning and Evaluation Unit should be provided.

2. Quality control of all canal construction work is needed to ensure that canal operation and seepage losses are minimized and that maintenance costs of the irrigation system will not be excessively high. Also, plans are being made to settle farmers on the farms without the necessary social infrastructure (including the hamlets and village centers) being undertaken and without ploughing to assist in conservation bund construction and land development.
3. The Mission believes one of the most serious detriments to successful quality control and project coordination is the lack of centralized control of work in the project area. A Senior Resident Project Manager with the power to enforce proper work scheduling and adequate construction quality from all participating agencies is urgently needed. This post is now vacant. The position of Resident Project Manager was mutually agreed at the time of negotiations and is reflected in the credit agreement. The RVDB has undertaken development in about one half of the project area with seemingly complete autonomy from MDB. The RVDB and the Army are

working without written contracts (which should have been submitted to IDA for review before such contracts were awarded). There also appears to be a serious lack of control at the field level in accounting for work progress and expenditures for all contracts.

4. The Mission noted the lack of inspection staff, particularly staff with authority to enforce work standards and quality control. There also is a lack of coordination of equipment orders with project needs. (Chain saws, air shipped by CIDA for use in clearing work have lain idle in Colombo for 3 months and farm tractors have been ordered without implements.)
5. Public relations with the farmers should be improved and problems exist in the flow of information from the MDB head office to the field and the feedback up the chain of command.

Recommendations:

A) Top Priority Actions Recommended

- 1) All work should be put under the direct responsibility of MDB and MDB should have power to enforce the scheduling of work, quality control and progress for all participating agencies. A senior project administrator or engineer should be appointed as Resident Project Manager and delegated with the necessary authority to properly control and coordinate work actions in the field and to enforce work standards.
- 2) A quality control unit should be set up within MDB and properly staffed to inspect all works under construction and to enforce quality standards. The unit should be headed by a senior engineer, with the assistance of a chief materials engineer and a head surveyor and lower level inspectors throughout the project area. The unit should conduct a quality control workshop and training program for all MDB field staff.
- 3) Written contracts should be made by MDB with the RVDB, Army and any other agencies performing work in the project area and these contracts should be furnished to IDA for review. (This was mutually agreed at the time of negotiations and is reflected in the credit agreement). A list of all construction contracts and expenditures to date also should be provided to IDA. MDB should certify the quantity and quality of all work completed.
- 4) A realistic project implementation schedule should be prepared by MDB for each block, properly coordinating all required work and settlement actions for each area. Systematic planning should precede construction work wherever possible.

B) Other Recommendations:

Among other improvements needed are the full staffing of the extension service and initiation of the Training and Visiting system, assistance in providing the necessary agricultural inputs required for successful agricultural production, improved public relations in all areas affected by the project and encouraging lower level field staff to discuss frankly with supervisors problems arising in the field so that the head office can take appropriate action. Finally, in view of MDB's plan to complete field channel construction and on-farm development by the settlers themselves, ripping should be completed in areas required before work in these areas is undertaken.

Agreement with MDB has already been reached on many of the foregoing recommendations. A letter of intent of actions to be taken to improve MDB operations (copy attached) has been received from MDB by the Mission.

S.J. Baker

September 15, 1978

සභාපති
தலைவர்
Chairman } 83069

සාමාන්‍යාධිකාරී
பிர. முகாமைப்பாளர்
General Manager } 84501

කාර්යාල
அலுவலகம்
Office } 83060
83071



මගේ අංකය
எனது இல.
My No. } CH/DL/1BRD

ඔබේ අංකය
உமது இல.
Your No. }

මහවැලි සංවර්ධන මණ්ඩලය

மகாவலி அபிவிருத்தி சபை
MAHAWELI DEVELOPMENT BOARD

දිනය
திகதி
Date } 13th Sept. 1978.

ක. ප. ප.
த. பெ.
P. O. Box } 1667

විදුලි පණිවුඩ
தந்தி
Telegrams }
මහවැලි
மகாவலி
Mahaweli

11, Jawatte Road, Colombo-5.

11, ජාවත්ත පාර, කොළඹ - 5.

11, யாவத்த வீதி, கொழும்பு-5.

Mr. Stanley Baker,
Leader, World Bank Review Team.

Dear Stan,

The supervision mission conducted during the last two weeks by the World Bank and other donor countries of work progress in Area H of the Mahaweli Development Project has included an inspection of the area and comments to the MDB staff. As you know, MDB has attempted to implement the program on an accelerated schedule consistent with National Objectives. We are also aware of the need to plan and construct the facilities, and provide the required agricultural and social support, in a manner that will assure the successful completion and operation of the project.

The World Bank Review Team has suggested the need for certain improvements in the program. In an effort to clarify and improve our operations, we intend to proceed with the following program :

1. A revised, more complete, and realistic implementation plan will be submitted by November 1st 1978.
2. A written plan for assuring construction quality in the H4 and H5 areas will be completed by September, 29th.
3. A revised cost estimate, a more complete plan for financial control and a schedule of financial requirements will be completed by October 13th.
4. A written plan for co-ordinating the settlement schedule in H4 and H5 with the completion of construction, providing on-farm development, and the furnishing of agricultural production support and social infrastructure will be completed by October 13th.
5. A check list of specific comments by the World Bank team and a list of specific actions required by the Loan Agreement will be prepared and assignments made for action.
6. A written plan for water monitoring and water management will be completed by October 13th.

contd...

දුරකථන/தொலைபேசி/Telephone

සාමාන්‍ය
தலைவர் } 83069
Chairman

සාමාන්‍ය
பிர. முகாமையாளர் } 84501
General Manager

කාර්යාල
அலுவலகம் } 83060
Office } 83071



මගේ අංකය
எனது இல. }
My No.

ඔබේ අංකය
உமது இல. }
Your No.

දිනය
திகதி }
Date

මහවැලි සංවර්ධන මණ්ඩලය

மகாவலி அபிவிருத்தி சபை
MAHAWELI DEVELOPMENT BOARD

ත. ප. ප.
த. பெ. ப. } 1667
P. O. Box

විදුලි පණිවුඩ
தந்தி }
Telegrams }
මහවැලි
மகாவலி
Mahaweli

11, Jawatte Road, Colombo-5.

11, ජාවත්ත පාර, කොළඹ - 5.

11, யாவத்தை வீதி, கொழும்பு-5.

Page 2.

7. A program will be developed to improve the management of MDB with emphasis on team effort.

In our plans for continuing the development of the H4 and H5 areas, we want to make it clear that we intend to call on the prospective farmers to provide labour for constructing field channels and preparing the land for cultivation. Our proposals regarding this may not have been fully understood. The prospective farmers will be shown their allotments, and then will be paid for their work in the construction of field channels and doing part or all of the land preparation (machines will be used to the extent needed and available). Under this approach, labour will be made available to complete the system, and the prospective farmers will have a source of income, pending their settlement, and cultivation of their land.

Your frank comments have been helpful in identifying areas in which we can improve our work. It is our desire and intention to continue with the program in Areas H on a basis that will meet the needs of and be acceptable to both Sri Lanka and the World Bank and other donor countries. Your continued cooperation is appreciated.

With regards,

Yours sincerely,

D. V. P. Ladduwahetty
D. V. P. Ladduwahetty
Chairman

Mahaweli Development Board.

c. Investment
Promotion Zone

The Investment Promotion Zone

Concept

1. The concept of an investment promotion zone or export processing zone for Sri Lanka had been discussed from the late 1960's and a brief mention was made of its possibilities in the ILO report on employment (1971). However, the detailed planning work for an export processing zone or export processing industrial estates followed from a cabinet decision in 1974, which appointed a committee to examine the concept of export oriented industrial estates at Pallekelle and Trincomalee. The committee reported in detail in October 1974 and recommended the development of an Export Processing Industrial Estate at Katunayake and Boosa. However, the concept of export processing was rejected after severe political disagreements in Mrs. Bandaranaike's cabinet.
2. The idea of a free trade zone was one of the key elements of the election manifesto of the present ruling party. As announced by the Government, the private sector is expected to play a major role in expanding industrial production during 1978-82. Accordingly, specific policy measures have already been adopted with a view to attracting private investment, both foreign and local. In keeping with the declared policy of encouraging foreign investment, the government created the Greater Colombo Economic Commission (GCEC) through Law No. 4 of 1978 (ratified on January 31, 1978). The Commission has been assigned broad objectives related to generating economic development, broadening the base of the economy, promoting foreign investment and increasing export earnings. The Commission has been given responsibility for administering the affairs of an "Area of Authority" which is an area of about 180 square miles located north of the city of Colombo. Within this area, export-oriented industries, both local and foreign, are to be attracted into several Investment Promotion Zones. The first of such Zones is 600 acres in extent and is being located adjacent to Sri Lanka's International Airport at Katunayake. The Zone has become one of the key projects in the Government's development plan. A great deal appears to depend on its success since the plans and commitments publicly announced leave little doubt as to the great hopes that are held for it.
3. The idea behind the IPZ is to diversify Sri Lanka's economy away from dependence on relatively few products such as tea, rubber and coconut, and less well known products such as batiks, ready-made garments, gems and curios, in which it nevertheless has a sizeable trade with Asia, Europe and the Middle East. There will also be other advantages such as provision of training and skills, backward linkages, financial returns to the Government through increased port revenues and a demonstration effect for the domestic industry to exploit export potential.

Incentives

4. A wide range of infrastructure facilities such as an air cargo terminal, containerized shipping, modern telecommunication facilities and additional housing are to be provided. Security of investment is guaranteed by legislation already enacted, and a wide range of tax incentives has been

offered by the GCEC. These are:

- a tax holiday period averaging five years from the date of commencement of commercial production;
- after the expiry of a tax holiday period, income tax on the turnover at a rate of 2% on sales to countries outside Sri Lanka, and 5% on local sales;
- 10% withholding tax on all remittances of royalty and technical service payments, after the tax holiday period;
- all foreign personnel attached to projects licensed by GCEC would be exempted from taxes for the period of the tax holiday for the particular project;
- all dividends paid to non-resident shareholders of the licensed area projects would be free from any further taxes and from any exchange control.

5. Further, all imports of equipment, construction materials and inputs for industry in the Zone would be free of import duty and both imports and exports would be free from administrative controls. Facilities for off-shore banking, warehousing and trans-shipment will be available in this area. Banking institutions will also be entitled to the five-year tax holiday. The Commission has authority to increase and extend concessions enjoyed in the Zone to export-oriented industries whose major activities are located outside the Zone.

6. The implications for the incentive structure for enterprises located outside the Zone are not as yet clear. As presently conceived, firms located in the zone will receive far greater incentives. The decision to permit these firms to sell a part of their output in the domestic market implies that there will be a differential incentive structure for firms competing in the domestic market which could well threaten relatively inefficient firms located outside the zone, leading to closures and unemployment if the zone is less than fully leak-proof.

Present Status

7. The progress of the IPZ has been rather uneven. The response from foreign investors has been slow and so far agreements have been reached with approximately 12 companies to locate in the zone.

8. At the present time, through the assistance of the Shannon Free Airport Development Corporation (SFADCO) team, financed by the UNDP, progress has been made on the topographic survey and preliminary tests of soil load-bearing properties, plus some thinking about a water supply system. No work apparently has yet been done on drainage or land levelling problems. It is yet to be confirmed whether electrical power will be adequately supplied by the national grid. Similar questions arise on provision of access roads and transportation for labor.

9. The Commission is largely operating without a staff. The SFADCO team has supplied assistance in defining an organization structure and helping prepare job descriptions for key personnel.

10. The infrastructure and related facilities will be financed by the Government and buildings will be financed by the enterprises. So far as is known, there are no estimates of costs nor of potential revenues, and hence no estimates of the financial viability of the IPZ. In short, almost no financial planning has apparently been done.

11. The total expenditure on the construction of infrastructure is expected to be only about Rs. 50 million in 1978 out of a total expected investment of about Rs. 1 billion over five years. It has also not yet been decided whether the IPZ will operate as a separate "profit centre" within the Commission's more general responsibilities for development.

12. The GCEC has indicated a wide range of industries suitable for the IPZ. Among the industries for which the GCEC is trying to attract both foreign and local capital are electronic goods, light engineering and light electrical engineering, small metal articles, fine machines, household equipment, photographic and optical equipment, tea-based products, rubber-based products, coconut-based products, precious stones, leather products, wooden products, garment manufacturing, cosmetics and pharmaceuticals, food processing, fiberglass boats, computer applications and also for insurance and banking. The list of industries mentioned above is not exhaustive and the GCEC would consider any investment which meets its objectives.

Employment and Foreign Exchange Gains

13. The potential gains in terms of employment and foreign exchange earnings from IPZ should not be exaggerated. The experience of similar free trade zones in some other developing countries should be carefully evaluated. For example, the export processing zones in Mauritius have developed many difficulties in the last two years and employment is now actually falling. Based on the experience of export zones in a number of other countries, it is estimated that on average, about 40 to 60 jobs per acre would be created after the zone is fully occupied and the plants are in full operation. This is for single storey factories; in some places, such as Jurong (Singapore), which has up to seven-level flatted factories, employment per unit area is of course much higher. If Sri Lanka's experience is approximately average, the first investment promotion zone might be expected to generate roughly 25,000 jobs after a certain period, say 5 years. The volume of open unemployment is high in Sri Lanka and even under the most favorable circumstances the IPZ cannot be expected to make a large contribution to alleviating unemployment. The employment effects may be multiplied if enterprises in the zone are able to purchase a large part of their raw materials and intermediate goods from domestic firms located elsewhere in the country. For example, the Santa Cruz electronic export processing zone near Bombay enjoyed net foreign exchange earnings in 1976 of about 60% of gross sales which reflected the high level of local procurement of inputs. In Sri Lanka it is almost certainly true that the majority of inputs will have to be imported and the net foreign exchange earnings are unlikely to be more than 20%.

Conclusion

14. Sri Lanka will certainly benefit from Japanese, Hong Kong and Singaporean investors switching labor-intensive production to the lower labor cost IPZ near Colombo, but even if clear legislation, excellent implementation and efficient administration for the zone is achieved by the end of 1978, the build-up of new factories (and jobs) will be a slow process in present world economic conditions.

15. It is not possible at this point to try to estimate the net foreign exchange earnings that might ultimately flow from the zone. It is, however, important to note that no country has depended upon export processing zones to supply the majority of exports. Taiwan, which has perhaps the most extensive industrial estates and export zones, obtains only about 20% of its exports from the zones. In every case, the countries get the majority of their exports from firms not located in export processing zones and the experience of Sri Lanka will probably be the same. Export zones are a useful institutional device to attract entrepreneurs, both foreign and domestic, and to help focus attention on export promotion. They are not a substitute for a broadly based export program for all of industry. The Government should continue to foster the development of the IPZ within the framework of the total export promotion program, but it would not be prudent to rely on the IPZ to supply the major increase in exports over the next five to ten years.

d. Greater
Colombo Dev.

SRI LANKA

Proposed Urban Development Project
for Metropolitan Colombo

1. During the course of your visit, the Government may wish to discuss the possibility of IDA involvement in the Greater Colombo Development Program, particularly IDA financing for the above proposed project. While we would not encourage such a discussion, the following paragraphs provide you with some background in the event the Government brings the subject up.

2. The Government attaches high priority to the Greater Colombo Development Program, along with the Mahaweli Ganga Development Program and the Free Trade Zone project. The portfolio for the responsible ministry--the Ministry of local Government, Housing and Construction--is held by Prime Minister R. Premadasa, who, along with President J. R. Jayawardene, has a high political stake in central Colombo. The Prime Minister takes great pride in having emerged from a poor area in Colombo and views the Greater Colombo Development Program as a means for personally dealing with the problems of his constituency.

3. The Government first indicated its interest in IDA involvement in the Program at last year's Annual Meeting. The matter arose again in a discussion in late February 1978 between officials of the Ministry and a Bank staff member who was in Sri Lanka to assist in the preparation of the estate housing component in the Tree Crops Rehabilitation Project. In May, the Government submitted a formal request for IDA to assist in the financing of the proposed Urban Development Project for Metropolitan Project. The request included the following:

a. Slum and Shanty Upgrading	Rs 175m
b. Housing (semi-urban, rural)	300
c. Land Reclamation and Drainage	100
d. Sanitary Sewerage	400
e. Water Supply (separate IDA financing)	-
f. Public Transport	300
g. Streets and Highways	75
h. Education	<u>280</u>
Subtotal	Rs 1,630m
Research and Management (5%)	<u>82</u>
Total in Rupees	Rs 1,712m
Total in US Dollars	US\$ 114m

4. The request is part of the outcome of the UNDP-financed Colombo Master Plan Project initiated in late 1974. Although the project got off to a slow start (the Project Director was replaced about two years ago), it now seems to be producing some useful output. A number of subsector studies are underway, and the Government will soon initiate investments in slum and shanty upgrading and central area development. Although it is too early to evaluate, it would appear that largely as a result of the UNDP project, the necessary institutional structure will soon be in place--i.e., land development and management policy, policies addressed to the major urban problems, identified priority programs and projects, metropolitan governmental machinery, and trained personnel for implementation. Shortly, an Urban Development Authority is expected to be created.

5. In the past, we have argued against our getting directly involved in a major urban renewal program in light of (i) our investment strategy geared primarily toward agriculture, (ii) the relative lack of major urban problems in Sri Lanka, and (iii) inadvisability of introducing an urban/rural distinction in the Sri Lanka content. However, we are already involved, or plan to be involved, in activities that relate to the urban sector. A first Water Supply Project that will benefit the greater Colombo area was approved in FY77. As part of this project, design work is being undertaken for a follow-up water supply and sewerage project, tentatively scheduled for FY80, but which could, in view of the urgency the Government attaches to their program, be brought forward provided the first project makes satisfactory progress. In the public transport sector, a mission is presently in Sri Lanka appraising the proposed Road Maintenance and Road Transport Project, which includes a public transport component. The project could also include a small component for improved access between the Port of Colombo and the Free Trade Zone, together with necessary road improvements to accommodate the increased bus fleet.

6. Thus, we are now or could be directly addressing over half of the proposed capital expenditures in paragraph 3 above. Although a review of the Bank's lending program to Sri Lanka in the context of the Government's new policies is currently underway, a priori, it would appear highly likely that such a review would reinforce our current strategy to devote the bulk of our resources to the considerable rehabilitation requirements of the productive sectors of the economy.

THE STATUS OF BANK GROUP OPERATIONS IN SRI LANKA

A. STATEMENT OF BANK LOANS AND IDA CREDITS (as of August 31, 1978)

Loan or Credit No.	Year	Borrower	Purpose	US\$ Million		
				Bank	IDA	Undisbursed
Six loans and five credits fully disbursed				42.4	34.6	
636	1969	Ceylon Electricity Board	Power	16.5		0.5
653	1970	Sri Lanka	Mahaweli Ganga Development	14.5		3.0
372	1973	Sri Lanka	Power Transm.		6.0	0.4
504	1974	Sri Lanka	Dairy Development		9.0	7.7
566	1975	Sri Lanka	DFC - Industrial		4.5	1.0
595	1975	Sri Lanka	Agricultural Development		25.0	8.6
666	1976	Sri Lanka	Tank Irrigation		5.0	4.7
701	1977	Sri Lanka	Mahaweli Ganga Development II		19.0	19.0
709	1977	Sri Lanka	Water Supply		9.2	9.2
742	1977	Sri Lanka	DFC - Industrial		8.0	7.9
818	1978	Sri Lanka	Tree Crop Reha- bilitation (Tea)		21.0	21.0*
819	1978	Sri Lanka	Tree Crop Diver- sification (Tea)		4.5	4.5*
Total,				73.4	145.8	87.5
of which has been repaid				35.8		
Total now outstanding				34.1	61.8	
Amount sold,						
of which has been repaid				3.6		
Total now held by Bank and IDA				34.1	61.8	
Total undisbursed				3.5	84.0	87.5

B. STATEMENT OF IFC INVESTMENTS (as of August 31, 1978)

Year	Obligor	Type of Business	Amount of US\$ Million		
			Loan	Equity	Total
1977	The Development Finance Corporation of Ceylon	Development Banking	-	0.1	0.1
1978	Bank of Ceylon	Development Banking	2.0	-	2.0
Total Commitment now held by IFC			2.0	0.1	2.1

*Credit not yet effective

SRI LANKA

Proposed Lending Program Through FY84

(All IDA Credits)

	FY78	FY79	FY80	FY81	FY82	FY83	FY84
<u>Agriculture - Irrigation</u>							
Irrigation and Drainage		15.0(R)					
Mahaweli Irrigation III			30.0				
Mahaweli Irrigation IV				30.0			
Mahaweli Irrigation V						45.0	
<u>Agriculture - Rural Development</u>							
Rural Development I		20.0					
Rural Development II					20.0		
<u>Agriculture - Tree Crops</u>							
Tree Crop Rehab. (Tea)	21.0						
Tree Crop Rehab. II (Rubber)				-15.0(S)			
Tree Crop Rehab. III						15.0	
Tree Crop Diver. (Tea)	4.5						
Tree Crop Diver. II					15.0(S)		
Tree Crop Diver. III							20.0
<u>Agriculture - General</u>							
Extension & Research			12.0				
Rainfed Farming (Sugar)			35.0(S)				
Rainfed Farming II				17.0(R)			
Fisheries			17.0(R)				
Rainfed Farming III							22.0
<u>Agriculture - Industry</u>							
Forest Industries				25.0(R)			
<u>Industry</u>							
DFCC IV	8.0						
Industrial Exp. Dev. I					10.0(R)		
Industrial Exp. Dev. II							23.0
Program Credit II			30.0(R)				
<u>Infrastructure</u>							
Power Transmission II				20.0			
Transport II (Road Maintenance)		35.0					
Transport III					25.0		
Water Supply II			22.0				
Water Supply III						30.0	
Water Supply IV							20.0
TOTAL (number)	33.5(3)	55.0(2)	99.0(4)	65.0(3)	60.0(3)	90.0(3)	85.0(4)

R - Reserve

S - Standby

3. Ongoing
Projects

SRI LANKA: 1978 BRIEFING PAPER

Ongoing Projects

1. Loan No. 636 - Maskeliya Oya Power Project

Although physical implementation is proceeding without problem, the Borrower has not met all the financial covenants included in the project agreement. (See Credit No. 372 below.)

Amount:	\$16.5 million
Date of Signing:	July 28, 1969
Original Closing Date:	September 30, 1973
Revised Closing Date:	December 31, 1978
Undisbursed Balance: (August 31, 1978)	\$0.5 million

The loan was made to cover the foreign exchange costs of the second state 90 MW hydroelectric development of the Maskeliya Oya and associated transmission facilities, and of a 25 MW gas turbine generating unit near Colombo.

The project is virtually completed. The first unit of 50 MW was commissioned in February, 1974, about 1-1/2 years later than originally estimated. The second unit was commissioned in July, 1974. The gas turbine unit was cancelled upon the request of the Ceylon Electricity Board (CEB). Delays were caused mainly by problems associated with the appointment of acceptable consultants, landslides in the penstock area and various strikes in manufacturers' factories. Site work has in general been carried out satisfactorily. The only remaining work, the extension of the Polpitiya switching station, is expected to be completed during 1978. The Closing Date of the loan has been extended to December 31, 1978, to allow for completion of the Polpitiya switching station, and the use of foreign exchange savings of about \$1.7 million to cover the cost overrun on the Power Transmission and Distribution Project (Credit 372).

2. Loan No. 653 - Mahaweli Ganga Development Project I

No major problems affecting progress.

Amount:	\$14.5 million
Date of Signing:	January 30, 1970
Original Closing Date:	June 30, 1976
Revised Closing Date:	July 31, 1979
Undisbursed Balance: (August 31, 1978)	\$3.0 million

The project is the first stage of the multi-phase Mahaweli Ganga Development Project and includes the provision of supplemental irrigation water for about 127,000 acres in the Dry Zone and the installation of 40 MW of hydro power generating capacity. With the completion of the project, rice production is expected to increase by about 83,000 metric tons and sugar production by about 10,000 metric tons.

The project, now complete, is about two years behind appraisal target. Delays were due mainly to foundation problems at Polgolla power house and a slow start at Bowatenna diversion dam. After overcoming these problems, the construction progressed satisfactorily. Good progress has been recorded to date on agricultural extension and research in the project area. The Credit (174-CE) associated with this project has been fully disbursed. However, an undisbursed amount of \$3.0 million remains in the loan which the Government wants to utilize for the procurement of badly needed vehicles and equipment for the operation and maintenance of project works and for other urgent works associated with the further implementation of the Mahaweli Ganga Development Program. The closing date of the loan has accordingly been extended to July 31, 1979.

3. Credit No. 372 - Power Transmission and Distribution

Although physical implementation is proceeding without problem, the Borrower has not met all the financial covenants included in the project agreement.

Amount:	\$6.0 million
Date of Signing:	April 18, 1973
Original Closing Date:	December 31, 1976
Revised Closing Date:	December 31, 1978
Undisbursed Balance: (August 31, 1978)	\$0.4 million

The project is for construction of 490 miles of transmission and distribution lines and associated sub-stations, extending the utilization of power generated under the Maskeliya Oya (Loan 636) and the Mahaweli Ganga (Loan 653 - Credit 174) projects.

Although the causes and possible solutions are largely out of the control of the Ceylon Electricity Board, it has not met the following financial covenants: the CEB has not over the past three years achieved the agreed (8% on revalued assets) rate of return; total accounts receivable by the CEB at end calendar 1977 exceeded the agreed limit of three months' billings with Government and local authorities having the largest accounts outstanding; and the CEB has paid contributions to the Government even though it had not satisfied the agreed condition of generating internal funds sufficient to finance not less than 30% of its annual capital expenditures before paying dividends or contributions to the Government. However, the CEB has recently submitted a proposal to the Government to increase electricity tariffs so as to enable the CEB to achieve an 8% return on revalued assets and finance at least 30% of its planned capital investment over the next five years. The proposal is under serious consideration by the Government.

Procurement of equipment and material for the project is practically completed. Route survey and right-of-way acquisition are progressing satisfactorily. Inflation since the signing of the Credit has increased foreign exchange costs by some 30% and we have agreed to cover the cost overruns from savings under Loan 636-CE above. Although actual physical completion of the project will not be until late 1979, disbursements from this Credit and the US\$1.7 million from Loan 636-CE, are expected to be completed by the Revised Closing Date.

4. Credit No. 504 - Dairy Development

The reformulated project is under discussion with the Government (See below).

Amount:	\$9.0 million
Date of Signing:	August 9, 1974
Closing Date:	December 31, 1980
Undisbursed Balance: (August 31, 1978)	\$7.7 million

The original project, as appraised in 1973, was designed to increase milk production on about 2,400 dairy farms covering 42,000 acres in the Coconut Triangle and Mid Country of Sri Lanka by providing credit, technical assistance and a strengthened milk collection, transport and marketing system. Complementary objectives were to establish pilot units for commercial calf rearing and pasture management systems; and provide processing equipment to the National Milk Board. However, progress was severely constrained by the poor supply of cattle available for onlending to project borrowers. The poor supply of cattle was due to import problems and an over-estimation of the national herd at appraisal stemming from unreliable Government statistics. Moreover, unrestricted slaughter of cattle was stimulated by a rapid increase in concentrate feed prices which made milk production unattractive plus the relatively high consumer price of fish and poultry meat. It, therefore, became necessary to reformulate the project. The revised project, still under discussion with the Government, would focus on what was a small component of the original project - support to dairy cooperatives. Under this component, dairy farmers would be organized in a manner similar to the successful Anand pattern of Dairy Cooperatives in India. The Government has requested the National Dairy Development Board (India) to help evaluate the potential of such an approach. Consequently, the supply of inputs and services would become key activities of the revised project, which would include provision of technical assistance and credit to farmers and support for milk collection, transport and marketing. Preliminary proposals have already been received to expand the successful ongoing calf/heifer rearing and pilot pasture programs. The number of beneficiary farm families would be substantially increased (current estimate approximately 10,000 vs. 2,400 in the original project) and the project would contribute to a considerable increase in income of existing landless and small farmer dairy producers. A September 1978 mission discussed the preliminary proposals, as well as the next phase of project reformulation. A clear statement of Government's policy regarding the price structure in the dairy sector has not yet been received. An increase in the producer price of milk is central to IDA's acceptance of a reformulated project.

5. Credit 566 - Third DFCC

No major problems currently affecting progress.

Amount:	\$4.5 million
Date of Signing:	June 27, 1975
Closing Date:	September 30, 1979
Undisbursed Balance: (August 31, 1978)	\$1.0 million

The credit was designed to help meet the estimated foreign exchange requirements of the Development Finance Corporation of Ceylon (DFCC) for lending mainly to export industries and tourism. The Credit is likely to be fully disbursed by the Closing Date.

6. Credit 595 - Agricultural Development Project

No major problems currently affecting progress.

Amount:	\$25.0 million
Date of Signing:	December 24, 1975
Original Closing Date:	June 30, 1978
Revised Closing Date:	June 30, 1979
Undisbursed Balance: (August 31, 1978)	\$8.6 million

The project is expected to result in estimated agricultural production increases after year six of 150,000 tons of rice, 15,000 tons of cereals and pulses, and 11,500 tons of sugar. The approximate value of these commodities at projected world market prices in constant dollars would be about \$40 million per annum. In addition, it would improve transport, processing, research and extension in the tree crops sector, thereby maintaining output and quality of end-products.

The Credit helps meet capital requirements in the agricultural sector. Project implementation and disbursements have fallen behind schedule because of initial delays in finalizing complementary UNDP Projects, late appointment by Government of one key consultant, inadequacies in local overall project coordination and slow procurement throughout the project life to date. Disbursements were only \$15.4 million on June 30, 1978, the initial closing date. In order to complete the vehicle repair program and procurement of spare parts for the Department of Agriculture, procurement of equipment for the Sugar Corporation, and to allow the procurement of additional trucks for the plantation sector and tractors for Dry Zone farm power, the closing date has been extended to June 30, 1979. It now appears likely that part of the credit amount will remain undisbursed on that date.

7. Credit 666 - Tank Irrigation Modernization Project

No major problems currently affecting progress.

Amount:	\$5.0 million
Date of Signing:	January 12, 1977
Closing Date:	June 30, 1981
Undisbursed Balance: (August 31, 1978)	\$4.7 million

The project covers five tank areas, serving a total cultivated area of 31,500 acres. The project includes: (a) construction works for improving irrigation and drainage facilities; (b) improvement of farm roads, (c) provision of farm equipment for land preparation and plant protection; (d) strengthening of agricultural supporting services, particularly extension; and (e) technical assistance for improving the operation and maintenance of the irrigation systems. At full development by 1985, annual food grain production in the five tank areas is expected to reach 46,000 tons compared to a projected 23,700 tons without the project. It would directly benefit some 10,000 farm families operating mostly about 3 acres each.

The construction program is behind schedule by about one year due to delays in procurement of construction equipment, civil disturbances in 1977, and shortages of experienced staff for surveys, designs, and supervision. Practically all construction equipment has now been procured and is available at work sites. The Government has also introduced special incentives to stem the exodus of experienced technical staff for better paid jobs abroad. Implementation is expected to pick up significantly from this year. However, project completion is likely to be delayed by about one year. Procurement and distribution of farm equipment is proceeding on schedule. Introduction of the Training and Visits system of agricultural extension is also proceeding satisfactorily. Due to changes in the exchange rate, as well as refinement of quantities for various civil works, revised project costs (net of taxes and duties) are expected to be about 30% lower than those estimated at appraisal.

8. Credit 701 - Mahaweli Ganga Development Project II

Problems emerging due to crash implementation program.

Amount:	\$19.0 million
Date of Signing:	April 21, 1977
Closing Date:	June 30, 1983
Undisbursed Balance: (August 31, 1978)	\$19.0 million

The Credit will help finance construction of irrigation and drainage schemes on 40,000 acres of new land in Mahaweli Ganga in dry zone, together with providing O&M facilities and equipment, production support in the form of necessary tilling power and implements, marketing, transport and processing facilities for 71,000 acres and improved agricultural extension services for 106,000 acres. Cofinancing arrangements have been made with Canada, the Netherlands, the United Kingdom and the United States.

The new Government, which came into office in July 1977, has chosen to make the Mahaweli Ganga Development Program the focus of its development effort in order to meet its priority objectives of increased agricultural production and job generation for the unemployed. Accordingly, the Government has decided to greatly accelerate the implementation of Mahaweli Ganga Development Project II and reduce the implementation period from five years to two.

A mission visited Sri Lanka in August/September, 1978, to supervise this project. The mission, which included representatives from the four cofinancing countries, found that, in keeping with the Government's decision to accelerate the project, the implementing agencies are moving at a breakneck speed. At time of writing, the mission had not yet returned from the field. However, initial indications are that the quality of work in the Project has been adversely affected by this acceleration. The matter is currently being critically reviewed and will be discussed at the Annual Meeting.

9. Credit 709 - Water Supply Project

No major problems currently affecting progress.

Amount:	\$9.2 million
Date of Signing:	May 10, 1977
Closing Date:	March 31, 1982
Undisbursed Balance: (August 31, 1978)	\$9.2 million

This credit will help finance improvement of existing piped water supplies to Colombo and five adjacent towns south of Colombo. In addition, the project will provide piped water to five adjacent towns north of Colombo and Ambalangoda and Lakutara on the southwest coast of Sri Lanka; it also includes provision for expenditures on spare parts and equipment, technical assistance and training. An additional credit of Canadian \$5.0 million from Canadian funds administered by IDA, will also assist in financing this project.

Because of a change of Government in July, 1977, and post-election civil disturbances, the new Government's consideration and review of its obligations under the credit agreement was delayed. As a consequence, at the time of the scheduled effectiveness date, the Government and WDB had not complied with agreed upon rate increases for bulk water and other covenants. The Government indicated its intention to comply with this covenant by January 31, 1978, and the effectiveness date was changed to February 15, 1978. The Government subsequently fulfilled all necessary covenants for the credit to become effective including the rate increase for bulk water, and the credit was declared effective on February 9, 1978.

10. Credit 742 - Fourth DFCC

No major problems currently affecting progress.

Amount:	\$8.0 million
Date of Signing:	September 30, 1977
Closing Date:	December 31, 1981
Undisbursed Balance: (August 31, 1978)	\$7.9 million

This credit will meet a substantial portion of DFCC's estimated foreign exchange requirements over a two-year period for lending to private sector industrial projects and tourism. Although implementation is progressing satisfactorily, an ongoing internal management power struggle between the Chairman of the Board and the General Manager of the DFCC has adversely affected staff productivity and morale. The conflict is expected to be resolved at a scheduled Board meeting on October 3, 1978.

11. Credit 818 - Tree Crop Rehabilitation (Tea)

Credit scheduled to become effective on October 12, 1978.

Amount:	\$21.0 million
Date of Signing:	July 12, 1978
Closing Date:	December 31, 1984

This credit would assist the Government in improving the economic efficiency of the tea industry by lowering production costs and improving tea quality in the project area, as well as in stemming the decline in output of tea through: expanded programs of tea replanting (550 ha) and in-filling (6,500 ha); strengthening the two major Government corporations involved in estate management; reduction in total number of factories (15 factories to be closed down) and expansion and rehabilitation of the remaining 42 factories; provision of vehicles for personnel, green leaf and made-tea transport; and rehabilitation of soil conservation works. The project would also assist private estate owners and approximately 180 small-holder producers and would provide improved housing and medical facilities for estate laborers.

12. Credit 819 - Tree Crop Diversification (Tea)

Credit scheduled to become effective on October 12, 1978.

Amount:	\$4.5 million
Date of Signing:	July 12, 1978
Closing Date:	June 30, 1983

This credit would help the Government in its initial effort in a long-term program to rehabilitate, diversify and settle degraded mid-country lands, mainly nationalized tea estates. It would provide financing for diversification of about 11,500 ha of marginal tea land, scrub land, or degraded forest, and would include establishment of about 4,500 small farms based on mixed minor tree crops, mainly spices; some 1,300 of these farms would be provided with dairy cows subject to satisfactory input supply and marketing arrangements. The project would provide the 27,000 settlers with both regularly paid work opportunities in land development and about 5,700 ha of developed homesteads, with garden plots and farms. Necessary social infrastructure, including housing, water supply and access roads would be provided at low cost. Project beneficiaries would be displaced estate workers, landless laborers and unemployed youth with a current average per capita income of less than US\$60 equivalent per annum.

SRI LANKA: 1978 BRIEFING PAPER

Prospective Operations

1. Kurunegala Rural Development (FY79 - \$20 Million)

The Government has given high priority to an integrated area development project for the Kurunegala District. The project would assist the Government in evolving a replicable model of regional development for raising productivity, employment, incomes and living standards of the rural population through a package of critically needed investments and institutional improvements. The project would include: coconut development; strengthening agricultural extension; development of tank irrigation; groundwater exploration; provision of agricultural inputs and credit; improvement of irrigation water management; construction and rehabilitation of rural roads; provision of rural electricity, rural water supply and education and health facilities; and technical assistance.

The project was appraised in March/April, 1978, and a follow-up mission visited Sri Lanka in August, 1978. The yellow cover staff appraisal report is scheduled for November 20, 1978.

2. Highway Maintenance and Road Transport (FY79 - \$35 Million)

The project is expected to have two components to be executed respectively by the Department of Highways (DOH) and the Ceylon Transport Board (CTB). The DOH component would focus on improved highway maintenance and rehabilitation with the specific objective of preparatory work for a comprehensive maintenance program for the existing highway network. The objectives of this component would be to: prepare the highway system for resealing or resurfacing; commence reconstruction of those sections which have failed or are about to fail; strengthen or replace structurally unsound bridges on main routes; provide equipment for the work proposed and for training in resealing and resurfacing; and provide technical assistance for implementation of improved maintenance in a selected pilot area, training aids and assistance with preparation of a possible further project.

The objectives of the CTB component would be to: contain the increasing operating cost of CTB buses by providing assistance to increase the reclamation of spare parts, increase the domestic production of springs to about 40,000 sets per annum and improve provincial workshops and depots; assist in the replacement of buses by providing materials for bus body building and assembly; and improve the financial situation of CTB.

The appraisal mission will be in Sri Lanka from September 20 to about October 16, 1978.

3. Rainfed Farming (Sugar) (FY80S - \$35 Million)

Located in the Moneragala District, the project would have two components. The main component would include a 2,500 tons cane per day sugar mill and arrangements for its cane supply. Approximately 15,000 acres of

mainly unused land surrounding the mill site would be developed for cane production comprising a 5,000 acres nucleus estate surrounded by 2,250 settlers growing 9,000 acres of cane. The project would finance: farm machinery and cane collection equipment for the estate and settlers; road-making equipment; settlement and social infrastructure costs; research; extension; training; evaluation and monitoring; and working capital. A pilot component would establish four small-scale processing (Khandsari) units, each with a capacity of 290 tons cane per day. The objective would be to determine the viability of labor-intensive versus capital-intensive technology. As a result of the project, crystalline sugar output would be increased by some 58,000 tons/year.

The project preparation report has been received from FAO/CP and is under review. Subject to satisfactory review, an appraisal mission will be scheduled for October/November. Total project costs will be about US\$120 million including contingencies. Cofinancing will, therefore, be needed. Project implementation should be undertaken under contract by an appropriate international company or organization which could be encouraged to take a minority shareholding and given a profit-sharing management contract for the initial period of project life.

4. Mahaweli Ganga Development Project III (FY80 - \$30 Million)

The proposed project, which will further Bank Group involvement in the Mahaweli Ganga Development Program, has not yet been identified. The consultants' feasibility and design work for the six irrigation/settlement sub-projects included in the program is progressing. It is expected that the Bank Group will participate in one of the sub-projects on a cofinancing basis. Meanwhile, the Bank is serving as Executing Agency for consultants financed by the UNDP to serve as general consultants to the Government of Sri Lanka and as a liaison for the Bank. In addition, as Chairman of the Aid Group, the Bank is helping the Government in coordinating the necessary external financial and technical assistance for the Program.

5. Water and Sewerage II (FY80 - \$22 Million)

The project has not yet been identified. It will be based on a sewerage study for which the Government has appointed consultants and with whom a contract is to be signed shortly. The consultants are expected to begin their study at the end of September.

6. National Extension and Research (FY80 - \$12 Million)

The proposed project, covering all the 22 districts in a national program of five years' duration, aims to increase the productivity and incomes of existing and newly-settled agricultural lands, cultivated mainly by small farmers; to raise the levels of output of paddy and other farm crops and to encourage associated livestock development. This would be achieved through a well-organized and disciplined extension drive intended to communicate improved practices suited to the farmers' specific agro-climatic and socio-economic conditions. The proposed project would strengthen the existing Extension, Education and Research Divisions of the Department of Agriculture.

In addition to the adoption of the T & V Extension System on a national basis, additional adaptive research facilities are also proposed to augment existing research institutions and to adapt research information to the farmers' needs under various agro-ecological conditions.

5. Memo of
Conversation

UNDP Activities in Sri Lanka

A. UNDP Country Program

The level of UNDP technical and pre-investment assistance to Sri Lanka has increased over the years. UNDP's first Indicative Planning Figure (IPF) for Sri Lanka was \$15 million for 1972-76 period. The second IPF for 1977-81 increased to \$31.5 million; or an increase of about 110% over the previous five years. While the project deliveries in the 1972-76 cycle amounted to \$17.8 million (against the \$15 million allocation), the following expenditure ceilings have been established for the current five year cycle:

1977	\$5.25 million
1978	\$5.21 million
1979	\$5.17 million
1980	\$5.13 million
1981	\$5.10 million

This ceiling has been established against the total 1972-81 allocation of \$46.5 million.

In the 1972-76 period, over 46% of the expenditure was for agriculture and fisheries, about 6% for education, 15% for transport and telecommunication, 8% for industries, 3% for health, 9% for labor, management and employment, and 13% for general economic and social policy and planning.

As of June 30, 1977, Sri Lanka was receiving UNDP assistance through 201 ongoing projects for a total amount of US\$28.559 million, while the Government of Sri Lanka had contributed the equivalent of US\$13.588 million bringing the total estimated cost of UNDP-supported Program since the inception of the first IPF cycle in 1972 to US\$42.147 million.

B. Bank and UNDP

The interdependency of IBRD and UNDP activities in Sri Lanka is significant. The most important cooperation between UNDP and the Bank will be seen in the "Umbrella Project" (a program of pre-investment and investment assistance). This is a UNDP-financed project for which the Bank is Executing Agency. The Project Document was signed in April 1978, with a UNDP contribution of \$2 million. This is a program designed to improve the data base in selected sectors, to identify priority projects for investment, to undertake feasibility studies and carry out project preparation. The project follows a similar effort undertaken by the Bank and UNDP for Burma in 1975 as an experiment to synchronize pre-investment and investment activities by aid agencies (particularly UNDP and the World Bank) and thus minimizing loss of time and funds. The Umbrella Project is getting excellent support from both the Sri Lankan Government and UNDP Resident Representative's office and the implementation so far has been very satisfactory.

I.
News and
Media

1. Press
Clippings

Flirting With Capitalism

Socialist Sri Lanka Acts to Curb Welfare Outlays, Welcome Back Foreign Firms to Lift Growth Rate

By BARRY KRAMER

Staff Reporter of THE WALL STREET JOURNAL

COLOMBO, Sri Lanka—Most of the 14 million people of this verdant island nation—once called Ceylon—live off the land by growing tea, rubber, coconut and rice. Sri Lanka is beautiful, but with annual gross national product equivalent to less than \$160 a person, it isn't paradise.

Nevertheless, broad social-welfare programs, instituted by successive socialist governments dating back to the British grant of independence in 1948, give Sri Lankans the best "quality of life" in South Asia. Take these examples: Medical care is largely free and widely available, and basic foods are subsidized; as one result, the average life span is 67 years—22 years more than in other developing countries of similar wealth. Education is free through the university level—part of the reason for a literacy rate of more than 80%, two or three times what might be anticipated.

With such advantages, outsiders might wonder why Sri Lankans last year turned out of office their most socialist government to date. The new government received an overwhelming electoral mandate—140 of parliament's 168 seats—after promising to curtail sharply state welfare programs and to welcome back foreign capitalists in a way that wouldn't endanger the economy's basic socialism.

Key Election Issues

There were distinctly Sri Lankan reasons why the voters tossed out of power a coalition of Communists, Trotskyites and the middle-to-left Freedom Party headed by Mrs. Sirimavo Bandaranaike, which had ruled the country since 1970. The voters chose instead the United National Party, headed by Junius R. Jayewardene, the long-time opposition leader whom the Communists used to call "the high priest of capitalism." Two major issues in the voting were government corruption and inflation.

But the political change here also reflects similar dissatisfaction with the poor performance of socialist economic systems in several Asian countries. Although none of these countries are abandoning socialism or communism, they are flirting with injections of capitalism and free-enterprise methods in a way unthinkable a few years ago.

For example, China, decrying its economic and technological backwardness, says it will try to catch up by playing down the rigid ideology of the Mao Tse-tung era and by emphasizing technical professionalism in industry, education and science. Industrial bonuses and wage increases have been widely introduced to spur production, and China is said to be contemplating direct foreign loans and limited joint ventures with foreign companies.

Vietnam also is seeking foreign investments. North Korea went heavily in debt to foreign banks in order to make multibillion-dollar purchases of capitalist technology and equipment. And even xenophobic Burma, whose strange brand of socialism has proved unworkable, says it may grant "mutually beneficial economic opportunities" to foreign corporations.

Just how far, and how successfully, such changes will be pressed can't be predicted with any assurance, of course. In the case of Sri Lanka, many observers doubt that Mr. Jayewardene can carry out a pledge to dissolve unprofitable government corporations, for example. He will have to battle bureaucratic inertia as well as the corporations themselves; besides, the country's recent history bodes ill for the new government's officials.

"Overall, they've got good policies," a foreign diplomat says. "But historically, implementation has been their great failure. I don't see that this government is going to be significantly better."

The Sri Lankan government does have one advantage that can't be claimed by many neighboring regimes, however: Only here are the changes coming about through free elections. In all probability, it is true, few voters in the July 1977 balloting saw their choice as lying between more socialism or less. But voters knew well the shortcomings of Sri Lanka's socialist economy—surging prices and extremely high unemployment, for example. More than one million of the work force of five million are jobless, and perhaps another 600,000 are underemployed. Many high-school and college graduates prefer to remain idle rather than accept a position that they consider beneath their skills.

The previous government of Mrs. Bandaranaike had pushed nationalization;

banks, the important tea estates (which provide more than half of the country's export earnings) and other enterprises fell under state ownership. But many state corporations, lacking incentives and managerial talent, operated at a loss. Indeed, some of them were required for social reasons to keep their prices low. So rather than helping pay for the burgeoning welfare programs, the corporations themselves are draining the national treasury.

On the tea plantations, the use of fertilizer declined, and old, less productive tea bushes weren't replaced on schedule. Production dropped. The problems were aggravated by the departure of the former British managers of the sprawling mountaintop estates.

At one such nationalized estate near Nuwara Eliya, the Sri Lankan manager concedes that present management can't persuade the women pickers to gather only the tiny leaves essential to making top-quality tea. With wages determined by the weight of what is gathered, the women pick anything they can, including leathery old leaves and twigs. This trash must be winnowed out at the factory—raising costs and lowering quality. "That wouldn't have happened when British management was here," the new manager comments.

Lagging Growth

Meanwhile, private industry, severely restricted on the import of raw materials and equipment and by government antagonism, became less and less productive. For most of this decade, the economy has limped along at an annual growth rate of only slightly more than 1%.

While government revenues declined, social-welfare spending increased. By the time of the elections, practically every Sri Lankan received each week a pound of rice free and three more at subsidized prices. Wheat flour, which is entirely imported, and sugar also were sold at subsidized prices to much of the population.

The social-welfare programs are believed to sop up as much as one-third of the government budget. Although these programs have reduced the disparity of income between rich and poor to a far narrower range than that in much of the underdeveloped world, they also have diverted much of Sri Lanka's income to current consumption and away from investment for future develop-

ment.

In the mid-1970s, the real crunch came, with the surge in world petroleum prices, a drought in Sri Lanka and a decline in the prices that Sri Lanka got for its tea, coconut and rubber exports. Mrs. Bandaranaike could do little about those calamities, and neither could the inefficient state corporations adapt to the new situation.

After winning the election, Mr. Jayewardene moved to pull Sri Lanka out of the doldrums. He quickly announced a step-up in the country's biggest development project, a program to build 12 dams and reservoirs on the Mahaweli River, install more than 500 megawatts of hydroelectric capacity and irrigate 900,000 acres of new farmland. He proposed that the 30-year project, which had been limping along since 1970, be condensed into the next six years.

Later, the overly ambitious plan was scaled down when the government realized that the economy couldn't absorb the necessary foreign funds in six years, that ports couldn't handle the sudden influx of construction equipment and that that equipment would have used up the country's entire imports of gasoline. Now, only six dams, producing less than 300 megawatts and irrigating 358,000 acres, are planned. So far, only two small dams and hydroelectric plants have been built.

Then, although previous governments had foundered when they tried to cut food subsidies, Mr. Jayewardene ordered the rice and sugar rations slashed. The better-off half of the population lost the free rice, and 82% lost the sugar entitlement. The government also has raised the price of wheat flour in two steps, the latest just recently, to about 7.1 cents a pound, although the government says that it still is paying a subsidy of 4.5 cents a pound.

Before the latest 1.7-cent-a-pound price rise, the flour subsidy had totaled almost \$80 million a year, and subsidies in infant milk formula, transportation, petroleum and fertilizer remain. So far, there hasn't been any popular opposition to the subsidy changes, but many people grumble about inflation. Wholesale prices rose 31% last year (retail figures aren't reliable), and inflation is believed to be even worse this year.

Mr. Jayewardene's third major move is the promotion of a 200-square-mile free-trade zone—a clear signal that private capital is again welcome. (He has been quoted as saying, "Let the robber barons come," but he also has told the nation's legislators that foreign investors would be welcome "not for good but for 10 to 15 years. After that, the whole thing comes into our socialist economy.")

To companies establishing operations in

the free-trade zone, the government offers—in addition to literate, low-paid workers—tax holidays and exemption from many of its tough labor laws, which make it almost impossible to fire anyone. Indeed, government officials say Mr. Jayewardene wants to restrict labor-union power; in the past, the predominantly Marxist unions often have struck for political reasons, including ideological causes in other countries. A proposed labor code would require that industrial disputes go to arbitration and would ban most strikes.

But the free-trade zone, located north of Colombo, lacks many basic facilities, such as good roads, port facilities and electrification. So, except for about five Hong Kong garment manufacturers and a sailmaker, the response from foreign companies has been meager.

Impressed by Mr. Jayewardene's initiatives, however, Western nations have promised major increases in aid, and the Soviet Union and China, both longtime friends of nonaligned Sri Lanka, also are adding projects. Last May in Paris, a Western aid consortium pledged \$380 million, some of it for the Mahaweli project; the total is up from \$260 million the year before and \$180 million the year before that. Next January, hundreds of millions more are expected to be pledged for the Mahaweli project, which will cost \$800 million over the next six years.

There are plenty of reasons for Mr. Jayewardene's haste. Unrest among the nation's Tamil minority, communal conflict between the majority Sinhalese and the Tamils, or student upheavals might disrupt economic development. And Mr. Jayewardene knows that he has only five years more to show progress before another election and that no previous government has won a second consecutive term. "There's a feeling that the next time the left gets in, they'll change things permanently their way," a political observer says.

SRI LANKA**More power to the President**

The hidden dangers in rewriting a country's constitution, however well-intentioned

By *B. H. S. Jayewardene*

Colombo: While much of the new draft constitution soon to be debated in Sri Lanka's National State Assembly (NSA) is obviously intended to break new ground and speed up progress, some provisions are being viewed with real alarm by the Opposition, and not just for reasons of self-interest.

Sri Lanka's 1972 Constitution placed power firmly in the hands of the legislature, with a 1977 amendment creating the post of Executive President, elected directly by the people and given powers which made inroads into the NSA's authority. First into the new presidential hot seat was the then Prime Minister, Junius Jayewardene, in February this year. One of the main arguments for Jayewardene's concept of an independent presidency was that it would provide political stability, and would not be swayed by the whims of the NSA (REVIEW, Oct. '77).

The new draft constitution was expected to concentrate on the detailed changes made necessary by the grafting of the presidency on to the 1972 Constitution, but the result is a startling document which combines a declaration

of intended progress with a further concentration of presidential power, as well as providing for stability to such an extent that further amendments may become virtually impossible. Major innovations are:

- ▶ the appointment of an ombudsman in an attempt to check corruption, which is now almost a way of public life;
- ▶ the promise of a definite role for the private sector after nearly 25 years of nationalisation strangling private enterprise;
- ▶ proportional representation in parliamentary elections, replacing the conventional British Commonwealth model of the majority taking the seat;
- ▶ the use of a national referendum by the president when issues of national interest are blocked in Parliament;
- ▶ total protection for all presidential actions whether taken in public or private life.

The ombudsman, designated Parliamentary Commissioner of Administration, will investigate and report on complaints or allegations of malpractice and violations of fundamental rights by public officers. The ombudsman may be removed by the president through a resolution approved by Parliament. Yet another innovation is the effort to check the use of influence in appointments to the public service. Sri Lanka has been notorious for the "pulling of strings," notably by politicians to get

appointments for their favourites.

Theoretically, all appointments to executive positions in the administration have required the approval of the Public Services Commission. In the past, its members have been subject to discreet persuasion, especially by ministers and influential politicians. The new constitution would prescribe that any person who influences or attempts to influence the decision of the commission could be imprisoned for up to a year or fined as well as imprisoned.

The private sector is strengthened indirectly through a clause in the draft constitution which makes it an objective of national policy to eliminate the concentration of economic power in the state or state agencies.

A major departure from tradition is the introduction of a system of proportional representation to replace the awarding of a parliamentary seat to the candidate who gets a simple majority of votes cast. The effect of the "British system" is that it denies adequate parliamentary representation to those who voted for the opposition. Landslide victories in terms of seats won have been achieved in Sri Lanka's elections by parties which have received far less than half the total votes polled in all the constituencies.

In the new system, each party will be



Jayewardene: Just his cup of tea.

allotted seats in proportion to the number of votes cast for its list of candidates. Critics say it will make for parliamentary instability in that no single party will ever be able to get the two-thirds majority which is required for the passage of certain bills. This could in turn lead to a further build-up of the power of the president, through the authority given to him to refer to a public referendum bills that have been defeated in Parliament, if he considers them to be of "national importance."

The president is further empowered to grant a pardon to any convicted offender, while he himself is immune from prosecution for any offence committed while in office — this includes action taken by him in both official or private capacities.

An effort is also being made in the draft constitution to eliminate the grievances of the largest ethnic minority, the Tamils, which have over the last quarter of a century provoked them into riots and other acts of civil disobedience, and obliged them in their frustration to seek a separate state in the north of the island republic. While Sinhala, the language of the majority, remains the official language, Tamil has been declared a national language with provision for its use in Parliament, in the administration and in the law

courts in the northern and eastern provinces of Sri Lanka where Tamils form a majority. Provision is also made in the draft constitution for the official translation of all laws into English, which until around 1958 was the language of administration in this former British colony.

Although the draft provides that the constitution can be amended only by a two-thirds majority, the Opposition Sri Lanka Freedom Party has threatened it will change the constitution should it get a mandate to do so from the voters at the next election. The problem might be how to establish legally such a mandate, since — in its draft form at least — the new constitution appears to be self-sustaining in all but the most idealistic circumstances. ■

SRI LANKA



Mrs Bandaranaike: Little headway; Jayewardene: Standing firm.

Shades of rural revolution

By B. H. S. Jayewardene

Colombo: Wall-posters scrawled in red are again appearing here. They denounce capitalists, the taking away of trade union rights and demand the restoration of the "standardisation of marks" system for university admission. Almost simultaneously the press reported two daring jailbreaks, which, it speculated, had the flavour of the 1971 insurrection.

Colombo's citizens have inevitably begun to wonder if these are rumblings of yet another youthful onslaught. The 1971 insurrection, it is now accepted, sprang mainly from the demand of rural youth for a greater share of the national cake. Today's rumblings confirm that the demand has not yet been heeded.

The Bandaranaike government, which was booted out of office last July, made little headway in its attempts to handle the youth question. Analysts agree that the youth vote had a lot to do with the unprecedented swing of the electorate towards the Junius Jayewardene-led United National Party (UNP).

Mrs Bandaranaike's United Front coalition — till 1975 — and the non-coalition Sri Lanka Freedom Party (SLFP) government of 1975-77 gave priority to solving the youth problem. On paper the measures would seem impressive. The Bandaranaike government introduced the standardisation of marks, which gave Sinhala youth a better chance of a university place — a measure which politicians of the north and east said was unfair to Tamil youth. The government set up a network of youth farms. The MPs' chit system to help youth find jobs was also encouraged, although with disastrous consequences.

None of these steps appeased the swelling ranks of jobless youth and the

new-look United National Party pounced on this situation when electioneering last July. It even promised a ministry to handle youth affairs. After the party swept to power it revoked the obnoxious Criminal Justice Commission laws under which insurgent youth leaders had been jailed.

Jayewardene was, in effect, pardoning those guilty of participating in the 1971 troubles and inviting them to be useful members of society. In the past few months, however, a spate of daring robberies — of provincial banks, of co-operative stores and of bus passengers — has resulted in the police keeping extra vigil on those who had been connected with the 1971 troubles.

Why should youth be in ferment in Sri Lanka today? The answer goes back many years. Before independence, the British favoured Tamils and Christians, who imitated the language and the habits of the ruler. The country was divided into two — an English-speaking elite and the larger Sinhala-speaking "nation."

The first post-independence UNP government segregated students into three language streams — English, Sinhala and Tamil. With the benefit of hindsight this, too, is seen today as a cause of the growth of communalism. However much successive governments have tried to justify the system, it was obvious that the non-English stream student was destined to be a second-class citizen. Free education introduced in the 1940s no doubt widened opportunities and gave the country the highest literacy rate in Asia — 80%. But the way it has been operated created serious anomalies.

The frustrations of the Sinhala-educated youth found an outlet in the formation of the ultra-radical People's

Liberation Front (JVP) in 1965 when³¹ Dudley Senanayake's UNP came to power. The years immediately preceding this had been eventful. SLFP's founder, Solomon Bandaranaike had been assassinated. His widow who succeeded him had escaped a coup attempt; defections from her ranks had maimed her party, and a coalition with the Trotskyist Lanka Sama Samaja Party did not prevent the return of the UNP.

Young men and women fired by a need for social and political changes and frustrated by their hopeless position — the educated unemployed at the time was estimated at around 600,000 — joined the JVP. In the villages they spoke of the correctness of Marxist-Leninist ideology and the way the country was exploited by American and British imperialists. Because the UNP had always been associated with the imperialist West, the first step was to secure the return of the SLFP which was closer to the aspirations of the people.

Their campaign succeeded and saw Mrs Bandaranaike triumph in 1970. But their impatience at the tardiness with which the United Front was tackling the country's problems soon boiled over in the insurgency. Of the 18,000 who were taken into custody during the insurgency, 80% were aged 20-25, the products of the post-1956 education system.

OLD IDEALS: Until the JVP-initiated upheaval of 1971, the establishment had accepted the revolutionary as almost a part of itself. The revolutionary was English-speaking, trousered, middle-class and respectable. He had the same background as any conventional politician — coming from an affluent home, educated at a foreign university and with little contact with the masses. The new radicals came from the rural middle-class and peasantry and had had their education in a provincial school. They reflected on how the ideals of the older generation — indigenous culture, national languages, severing of links with the colonialists — had led them up a blind alley.

The standardisation of marks was a sop that the Bandaranaike government offered to Sinhala youth. But although it appeased the Sinhala Buddhist extremists, this measure resulted in a decline in the number of Tamil students admitted to university. In 1969, 40.8% of students admitted were Tamils. In 1974 the number had gone down to 16.3%. There were also fewer jobs for Tamils.

Around 1971 a shadowy underground of young terrorists made its appearance among the Tamils in the north. At first they claimed to be saviours of the oppressed minority. Today they terrorise those sections of the Tamil community who are unwilling to shout ex-



Sri Lankan youth: Fewer students, fewer jobs.

tremist slogans about *eelam* (separation).

As a conciliatory gesture towards the Tamils, Jayewardene scrapped the standardisation policy, and almost immediately was rewarded by an outcry from Sinhala Buddhist extremists. President Jayewardene has so far stood firm by his decision.

Meanwhile, there is little prospect of any marked change in urban-rural education patterns. The glaring disparities between these sectors are perpetuated by the scarcity of resources including teachers, laboratories and libraries. In the National State Assembly recently an MP disclosed that a school in his constituency had been closed for a month for

want of teachers. Another MP warned that unless early action was taken to improve educational standards in rural schools the economic development of the country would be ruined.

In all this confusion the Education Minister has made a decision that could have far-reaching consequences. He has stated that in future teachers should have served in outstation schools from 10-15 years to be eligible for promotion. He believes, he said, the village is "the initial environment from which stems an awareness to meet shortcomings." Perhaps a new type of teacher in the rural areas could be a step closer to the dream of a better deal for rural youth.

The Left tries to get it right

By Mervyn de Silva

Colombo: An unusual essay in self-criticism produced by the pro-Moscow Communist Party of Sri Lanka (CP) reflects the extraordinary state of mind in which the Left as a whole finds itself and the exceptional importance it attached to the conferences held this month by the CP and the other major Marxist party, the Lanka Sama Samaja Party (LSSP).

The two parties, bitter foes when the LSSP flaunted a Trotskyist banner, belong to the 1977 United Left Front (ULF), a triple alliance which failed to win a seat in the July general election. The flurry of excitement surrounding each party's first post-election conference indicated that more than routine re-appraisals were being undertaken.

Both agree that the "new political situation" represents "a critical phase" in Sri Lanka's mass movement, and that "today's tasks" cannot be undertaken without a thorough analysis of recent events.

The ULF desperately needs a spokesman in the National State Assembly. The desperation is easy to understand: the established Left is caught between three forces, which reinforces the public image of the ULF's isolation.

Firstly, there is the conservative, middle-class United National Party (UNP) supporter who was often given to an exaggerated awe of these "Marxist masterminds" and "rabid revolutionaries." Now he gloats over the fact that the "downtrodden masses" have banished them from the parliamentary arena.

Next, the Sri Lanka Freedom Party (SLFP), finding that the UNP's fire is aimed more in its direction than at the ULF, talks openly of a "secret understanding" between the UNP and the LSSP leaders.

Finally, a spirited, if ill-organised "new" Left makes no effort to conceal its malicious glee over the fate of its once respected gurus. "Our learned leaders tried Eurocommunism in the middle of the Indian Ocean and see how they are drowning in their own parliamentary reformism and opportunism," writes a Politburo member of the newly-formed "rebel" LSSP.

Parliament is at the core of the debate. Both parties agree that the parliamentary path to socialism was right in the Sri Lankan situation. But they also agree that there is need for discussion on tactics. The issues include:

► an evaluation of the United Front

line, first put forward by the CP at its 4th Congress in 1950.

► The Left's hostile reaction to the 1971 youth insurrection. (An intellectual snobbery and a prissy disgust for these boorish village lads trying to play Lenin and Guevara seems to have prevented the Westernised, Colombo-centred Lef leaders from coming to grips with a new social force in the form of rural petit-bourgeois educated youth.)

► The Left's attitude to racial minorities, notably the Tamils, whose disaffection has driven even their essentially conservative leaders to form "liberation fronts" and demand a separate state.

The CP discussion has been based on a central committee "draft thesis," itself based on a document sent to members in January. It is more genuinely self-critical and lively than the "political resolution" drafted by the LSSP leadership and discussed by branches last month before the conference. The CP document discusses the party's stand on the issue of Tamil language regulations introduced by the Dudley Senanayake (UNP) government in 1966. This CP admission is particularly significant in the light of the current SLFP propaganda on university admissions and standardisation of marks.

TRIBAL DRUM: Since communalism is the first refuge of the electorally vanquished, Mrs Bandaranaike beat the tribal drum in 1965-66, when Senanayake tried to grant similar concessions. Trailing behind her (in the interests of the United Front), the LSSP and CP placed race before class. The CP is now shamefaced, whereas the LSSP resolution shows no trace of guilt over its lapse into crude communalism.

In the past the CP line was predictable. Working within the parameters of Soviet foreign policy, it saved itself the bother of needless celebration by simply adding a little local colour to the Indian communist party line. With its proud Trotskyist lineage, the LSSP welcomed democratic debate and made almost a fetish of its independent thinking on domestic issues and its Titoist freelancing on international questions.

External and local events have contrived to reverse roles. Moscow's special relationship with the "progressive" Mrs Gandhi and her "non-capitalist path of development," and the ultimate fate of a supine Indian communist party that remained silent even on the worst excesses of Emergency rule, have obvious lessons for a CP which went one step further and accepted ministerial office in Mrs Bandaranaike's government.

Paradoxically, this identification with the SLFP aggravated internal CP conflicts, which thrust themselves to the surface soon after the 1971 insurrection. Three out of the CP's six MPs quit

the United Front in an act of brave defiance over the introduction of the (now repealed) draconian Criminal Justice Commission Act.

The three defectors were Dr S. A. Wickremasinghe, Aelian Nanayakkara and Sarath Muttetuwegama. Since many of the top cadres of the insurgent People's Liberation Front had roots in the south, Wickremasinghe and Nanayakkara, two southerners, were more than merely conscience-stricken by the ferocity of the repression. As for the young Muttetuwegama, he had his eye on what is certainly a bright future in the party and responded to the indignant outcry of the CP's youth league and student wing.

It took the CP, with some friendly persuasion from Moscow, less than two years to patch up the split. So these critics and young militants are still within the party fold, able to voice their views even more confidently. This "tendency" finds expression in the memo which preceded the central committee's draft thesis and whose authorship is unclear. The author of the official thesis, in which criticism is generalised and modulated, is party secretary Pieter Keuneman, the only CP minister in the Bandaranaike cabinet.

A "bureaucratic barrier" was gradually erected, observes the memo, between minister and party centre, with the minister more occupied with his ministerial duties than his party responsibilities. While this point is conspicuously absent in the thesis, many lessons for a CP which has accepted ministerial office in a coalition dominated by a bourgeois party have been deftly incorporated. In party circles, the literary skills of Keuneman, who has retained his post from the Stalin era to the Brezhnev decade, are legendary.

MOVING TARGET: When the memo was still a secret, a party intellectual told this correspondent: "The target is Pieter, but he is a fast-moving target. He will find the formula and the right words to satisfy all groups, probably reconciling even the irreconcilable ... Cambridge University English helps, you know."

But the basic errors are acknowledged:

► the United Front tactic of completing the anti-imperialist and national-democratic stage was correct, but the defeat of the UNP and the maintenance of the Front should not have been the priority at all stages.

► One-sided misapplication of the tactic of "unity and struggle" vis-à-vis the SLFP.

► The CP's independent identity was insufficiently stressed and the SLFP's right-wing policies, anti-democratic acts and unpopular measures were not adequately exposed.



Senanayake: Conserver.



Wickremasinghe: Defector.



Keuneman: Survivor.

► The shifting character of the national bourgeoisie was not fully grasped.

► There was insufficient awareness of ultra-leftism, once a mere projection of ideological controversies abroad but subsequently a clear trend in local Left politics.

The CP's new position shows a leftward shift. The LSSP, on the other hand, is modest enough to admit mistakes, but the self-criticism is largely

ceremonial. It can afford such self-indulgence for its left wing, unlike that of the CP, has been expelled. Vasudeva Nanayakkara and the LSSP's young rebels have formed their own party, leaving the LSSP's priestly theoreticians, frightened out of their wits by the bloody 1971 insurrection, to brand them "ultra-Left adventurers."

RIGHT MOVE: As the bourgeoisie increasingly imposed its will on the SLFP, the SLFP's right wing assumed command. The class interests of a national bourgeoisie which was nurtured by import substitution, protectionism and State patronage have now radically changed. Low technological levels, the narrowness of the domestic market and World Bank-decreed economic policies, runs the Marxist argument, have forced this class to seek collaboration with international capital and neo-colonial agencies.

So the LSSP and CP can no longer have any understanding with the SLFP on a programmatic basis. The CP, however, leaves the door slightly open by identifying "many social forces" within the SLFP that can be drawn into the "struggle against the UNP and neo-colonialism."

Both parties also agreed that the UNP's economic strategy is a logical, if more clearly conceived and thorough, extension of the policies adopted by the SLFP after the expulsion of the LSSP from the UF in 1975.

Both also see the spectre of right-wing repression in what they regard as the devaluation of Parliament and the centralisation of authority in an executive President; the extension of control over the media, and the amendment to the Parliamentary Privileges Act; the ban on demonstrations; the formation of a special police reserve; victimisation of political opponents and trade union activists; and a proposed labour law which will reduce workers' rights and depoliticise the unions.

More apprehensive of the future than the CP, the LSSP is caught looking over its left shoulder at the "ultras" who by their adventurism "may quicken the pace of repression." Parliament, says the LSSP, should remain the main focus of the ULF's efforts. The CP enumerates various types of extra-parliamentary action as a means of mobilising mass opinion in support of a "socialist alternative" (LSSP) and "socialist-oriented development" (CP).

Since both agree that there cannot be any autonomous development of capitalism at the periphery (in other words, that capitalism in the Third World is essentially dependent), there is no mention of a "non-capitalist path of development," the theoretical justification for the Soviet Union's special relationships with "progressive" governments from Egypt to India.

2. Information
Media

SRI LANKA

Population 12 760 000
Area 65 610 sq. km.

PRESS

Newspapers Dailies 17, Non-dailies 17
Total circulation Dailies 612 000, Non-dailies 1 058 000
Copies per 1000 people Dailies 48, Non-dailies 83

RADIO

Transmitters Long/medium-wave 9, Short-wave 12, VHF-FM 8
Total receivers 846 000
Receivers per 1000 people 66

FILM

Cinemas Fixed 303
Total seating capacity 128 544
Seats per 1000 people 10
Total annual attendance 98 135 800
Annual visits per capita 8

PRESS

The daily press – 10 morning and 7 evening newspapers – is entirely based in the capital, Colombo, though most papers have a much wider readership, in one or other of the three main publishing languages: Sinhalese, with 5 newspapers circulating a total of 374 568 copies daily, Tamil, with 6 newspapers (111 675 copies) and English, 6 newspapers (12 588 copies).

Non-daily general interest newspapers, mostly weekend or weekly papers, are also published in Colombo; 9 in Sinhalese, 5 in Tamil and 3 in English. In addition, there are many periodical publications dealing with political, cultural or religious affairs, women's and children's interests, industry and commerce, annual surveys, etc.

NEWS AGENCIES

The national agency is the Press Trust of Ceylon (Sri Lanka) Ltd (Newstrust), a private company founded in 1951 and dealing only in foreign news, which it receives from Reuters (London) and the Press Trust of India. It distributes 35 000 words a day, in English, to its 12 subscribers in Sri Lanka (11 newspapers belonging to the four main groups and government radio stations). Newstrust has its permanent bureau in Colombo with a staff of 15, but employs no local or foreign correspondents.

Most of the world's leading agencies have either permanent or part-time correspondents in Colombo.

RADIO

The Sri Lanka (Ceylon) Broadcasting Corporation, formerly Radio Ceylon, was

established as a public corporation under the Ministry of Information in 1967. In addition to government subsidies, it is financed by listeners' licence fees and commercial advertising revenue. There were 466 000 licences in 1972 (each licence may cover more than one receiver).

The corporation operates 9 medium-wave transmitters (including three of 50kW), 8 FM transmitters (totalling 2kW) at various points on the island, and 12 short-wave transmitters (including three of 100kW) all at Ekala.

The national service has three language programmes. in Sinhalese (74 hours a week), Tamil (72 hours) and English (45 hours) which, with the alternative light programme in Sinhala -- Radio Sandhaya (31 hours) -- brings the total broadcasting time to 222 hours a week. Main programme categories are: light entertainment (75 hours), broadcasts for special audiences (59 hours), artistic and cultural (37 hours), news and information (17 hours), educational (15 hours), broadcasts for ethnic minorities (7 hours) and advertising (7 hours). A highly successful innovation is the education programme, replacing the former day-time schools service, which is broadcast nightly for 1¾ hours and is designed not only to supplement school curricula but to prepare secondary-level students for recognized examinations.

The commercial service consists of a domestic network which is on the air 192 hours a week in Sinhalese (79 hours), English (69 hours) and Tamil (44 hours), and an overseas service beamed to south-east Asia and broadcasting in Hindi (52 hours), English (46 hours) and Tamil (18 hours a week).

A commercial rediffusion company under government contract and with government participation operates a four-channel wired network rebroadcasting the national service programmes in Sinhala, Tamil, English and Hindi to over 22 250 subscribers (in 1969) in Colombo and district, and the inland city of Kandy.

The Voice of America has a station in Colombo with four 35kW short-wave transmitters broadcasting VOA programmes in English, Urdu and Hindi.

TELEVISION

There is no television but preliminary planning for its introduction is under way.

FILM

Local film companies produced 25 feature films and 8 short films in 1971. Apart from its weekly newsreel, the government film unit's annual production of 53 short films in 1970 included 49 educational and instructional titles.

A national film institute, set up under government auspices in 1970, deals with film imports and distribution. the operation of a government film studio for local producers and the production of educational, cultural and children's films.

Annual imports in 1971 included 198 feature films from the USA (107), India (55), the UK (14), Italy (10), France (6) and the USSR (4). Annual cinema attendances have more than trebled over the last ten years. In addition, non-commercial exhibition of educational and cultural films, mainly by mobile units, attracts large audiences.

SPACE COMMUNICATIONS

An Indian Ocean Intelsat earth station is planned to be built at Mirigama in 1974.

J. Country Econ.
Memo.