

PN-ACC-391

***USAID/SRI LANKA***

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***REVISED COUNTRY PROGRAM  
STRATEGY  
1998 - 2000***

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# COLOMBO - APRIL 1998

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## INTRODUCTION

The Sri Lankan economy has largely recovered from its poor performance in 1996. Future prospects, however, remain uncertain. The prolonged ethnic conflict in the north and east continues to place a heavy strain on the government's budget and limits its ability to make further reductions in the fiscal deficit. With the renewed military offensive begun in 1997, the conflict continues to exact a heavy toll on human resources, not only in terms of lives lost and the casualty rate, but also in the psycho-social impact on children and communities.

An end to the ethnic conflict may well produce an initial positive response in investment in Sri Lanka. However, continued need for reform in a wide range of areas important to investors will more likely impede any significant or sustainable "peace dividend."

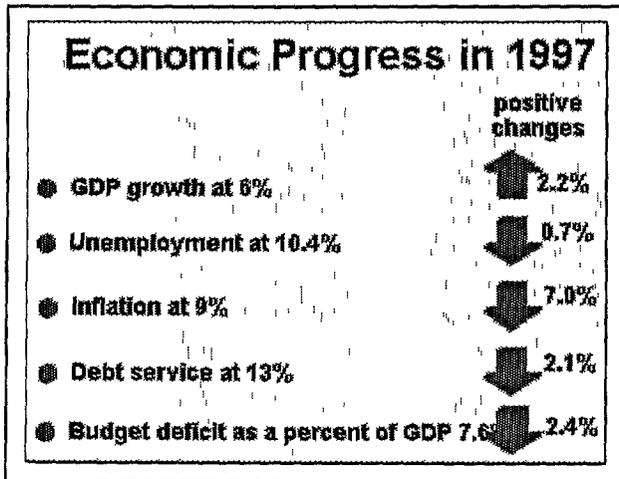
The current USAID 1997-2000 strategy for Sri Lanka focuses on employment and income generation, with a special objective to improve the quality of life of the disadvantaged. With the recent reductions in program resources, USAID believes that individual, firm-level assistance will not have a significant impact on economic growth. Although some gains in employment and income can be demonstrated, the impact on the overall employment rate is marginal. A more systemic approach is required which affects national and sectoral factors contributing to growth and competitiveness.

This document requests approval to modify the strategy for the remainder of the strategy period. It proposes a strategic objective of improving the enabling environment for trade and investment, and two special objectives, one to ensure better protection of citizens rights in law and practice, and one for enhanced economic and social opportunities for disadvantaged groups. The revised strategy would bring the program directly in line with the three key foreign policy interests of the United States: (1) promotion of a peaceful, democratic resolution of the ongoing civil conflict, including strengthening democratic institutions, particularly an efficient, non-partisan judiciary, (2) promotion of continued expansion and liberalization of the Sri Lankan economy, and (3) promotion of recognition and respect for human rights.

## 1.0 ANALYSIS OF THE ASSISTANCE ENVIRONMENT

### 1.1 The Development Setting

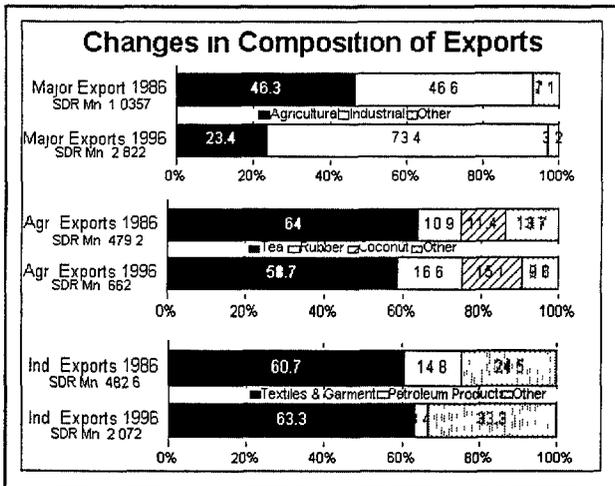
The primary development constraint for Sri Lanka is the 14 year old ethnic conflict in the northern and eastern provinces, which remains a drag on the economy. At the November 1996 World Bank Consultative Group meeting on Sri Lanka, the Government of Sri Lanka (GSL) stated that it recognized the broader political implications of sound economic growth as an essential element of a strategy to facilitate the resolution of the conflict in the North and East. Therefore, economic growth and stability are essential components of the political environment required to resolve issues that must be addressed to end the conflict.



Despite the war and the financial crisis of Eastern Asia, the Sri Lankan economy did remarkably well in 1997. After a decade where GDP growth averaged about 4%, the GDP growth in 1997 is estimated at 6% compared to 3.8% in 1996. Unemployment dropped from 11.1% in 1996 to 10.4% in 1997 and inflation dropped from 16% to 9% during the same period. The debt service ratio in 1997 is estimated at 13.0%, down from 15.1% in 1996 and the budget deficit as a percentage of GDP dropped to 7.6% in 1997 from its average of about 10% in the early 90's. Despite the ongoing ethnic

conflict and recent terrorist activities, tourism is up 22% over 1996 levels.

There were strong signals of the GSL's re-commitment to privatization as the proceeds raised exceeded Rs 23 billion during 1997. Apart from divestment in the plantation sector, the GSL successfully divested 35% of Sri Lanka Telecom and also divested its holdings in the National Development Bank. The increased capital inflow from the privatizations resulted in the capital account offsetting the trade and current account deficit to register an estimated balance of payments surplus of US\$ 400 million for 1997. Even with these positive trends described above, significant constraints to Sri Lanka's entry into the global market place remain. The overall trade balance is still negative (approximately \$1.2 billion) despite recent improvements in some export sectors. The United States is Sri Lanka's principal trading partner, with exports to the U.S. reaching almost \$1.4 billion (34.1% of all exports) and imports from the U.S. at \$211 million. The European Union is second and accounts for about 29% of the country's total exports.



The Sri Lankan economy is dominated by garments and plantation crops (tea, rubber and coconut) which currently account for 66% of all exports, revealing the country's heavy reliance on these two sectors. Although total exports are estimated to be up by 14% in 1997, this is partly due to higher tea prices which is likely a temporary phenomenon. The elimination of textile and garment quotas over the next few years, the volatility of tea and rubber prices, and the devaluation of many East Asian currencies raise doubts about the country's prospects for 1998 and beyond. Although, there is evidence

that exporters with up-market high quality products will remain unaffected, the Sri Lankan economy clearly must be redirected to focus on quality and high-value added products if sustainable growth is to be achieved.

Policy and regulatory impediments still exist which create disincentives to both investors and producers. Macro and sectoral policy and regulatory reforms, as well as programs to improve practices are needed in order to strengthen financial markets and to liberalize the economy. Policies that will contribute to increased efficiency, a better regulatory and oversight system and increased transparency are required in order to attract investment. The 1998 budget proposals affirmed the government's commitment to a private sector led growth strategy. Proposals include several major policy reforms, primarily dealing with business sector taxes and tariffs. In some cases, tariffs on capital and intermediate goods imports have been eliminated and in other cases the duties have been dramatically reduced. The new budget also provides tax incentives for investors and liberalizes regulations dealing with foreign investment. The proposals also allow for release of statutory pension funds into the equity market. A release of even 5% to 10% of these funds will boost domestic liquidity in the stock market significantly.

Sri Lanka has a long standing democracy with an active multiparty system, an independent judiciary, and an active print and electronic media. Constitutional power is shared between the popularly elected President and the 225 member parliament. The strong, long-standing democratic values and institutions in the island have deteriorated due to the ethnic conflict. The government generally respects human rights of its citizens in areas not affected by the conflict. However, human rights abuses, including extrajudicial killings, illegal detention, and torture continue to occur in the areas affected by the conflict. Although the human rights protection guaranteed by the Sri Lankan constitution is comparable with any western democracy, and the mechanisms for reporting violations are well entrenched in the legal system, victims rarely report violations due to fear and a lack of awareness of their rights and reporting mechanisms. Other serious impediments include the high cost of litigation, delays and weak case management by the judiciary. Although there are some organizations providing legal aid, current efforts are

insufficient and Sri Lanka has not yet developed a system of court appointed lawyers. The Human Rights Commission (HRC) has established field offices throughout the country, but HRC field staff lack the necessary training and expertise to be effective.

The north-east conflict has caused the displacement of thousands of people. Over half a million persons remained displaced during 1997, living in basic conditions and undergoing considerable physical and psychological hardship. A recent survey revealed approximately 170,000 - 190,000 displaced children live in parts of the northern province alone. Thousands of children displaced by the conflict suffer from constant exposure to a war environment and the resulting trauma of growing up in a war zone. Although the civilian population has generally been able to move away from areas of direct military confrontation, civilian casualties continue to occur in the north and east from artillery and mortar fire, from mine incidents, from direct attacks on villagers and related incidents. The conflict continues to produce around 1500 amputees yearly.

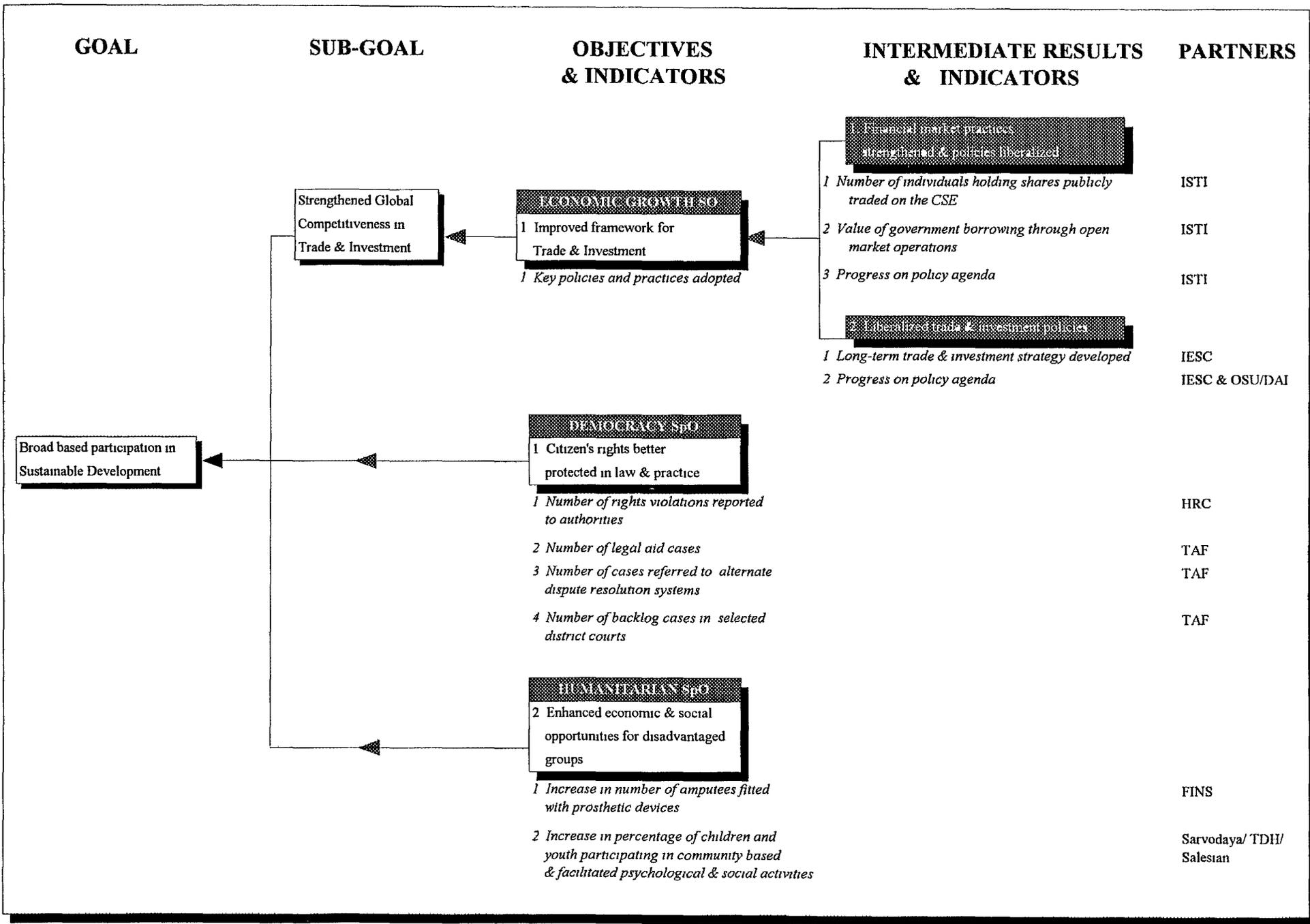
The human development indicators for Sri Lanka are impressive. In the 1990s the population growth rate has averaged 1.5 percent, adult literacy rate is 90%, one of the highest in the world. Sri Lanka has defied the South Asian pattern, where there are only 94 women for every 100 men. Its average of 106 women for 100 men is in line with the worldwide biological norm.

The GSL is a responsible and accountable development partner. However, without significant additional progress in economic growth, resolution of the ethnic conflict and development of better functioning democratic institutions, Sri Lanka will not be able to bring more of its people into the economic mainstream and sustain its gains to date.

Social Progress Indicators	
Life expectancy years (1993)	72
Infant mortality rate (1994)	15
Adult literacy (1993)	90
Gender Disparities	
Life expectancy (1993)	F/M 74/70
Adult literacy (1993)	86/93
Labor force (1993)	36/64
Share in Parliament (1994)	5/95
Per capita GDP (1996)	\$760

## 1.2 Overview of Other Donors

In 1996 Sri Lanka received almost \$1 billion in official development assistance (ODA). This reflects the continued support from the international community for the GSL's development agenda. Total donor disbursements to Sri Lanka were about \$531 million. The United States, with about 4% of total disbursements, was the third largest bilateral donor, and the fifth largest overall. The leading donors were Japan, the Asian Development Bank, the International Development Association, Norway, and the United States. Together with the GSL, the World Bank chairs an annual Consultative Group (CG) meeting of aid donors in Paris. The CG



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facilitates overall coordination of aid policy and implementation, and is supplemented by periodic, less formal meetings in Colombo

## **2.0 THE REVISED STRATEGY, FY 1998 - FY 2000**

### **2.1 The Goal: Broad-Based Participation in Sustainable Development**

USAID's revised program in Sri Lanka is relevant to and can have an impact upon key development issues facing the country. The goal, sub-goal, strategic objective and special objectives, complemented by the programs of the GSL and other donors, form a coherent and well-linked program to address the country's prospects for economic growth, the protection of human rights and strengthening of democratic institutions, and humanitarian assistance. The types of economic growth activities, as well as the methods of implementation, support the expansion of participation by a broader spectrum of the population and a focus on systemic change will help ensure sustainability. Also, assistance in the areas of human rights and democracy will contribute to both a broadening of the participatory base and sustainability.

Using secondary sources, USAID intends to monitor nation-wide trends in employment, including gender disaggregated data, to ensure that the activities in the revised strategy are contributing to the goal.

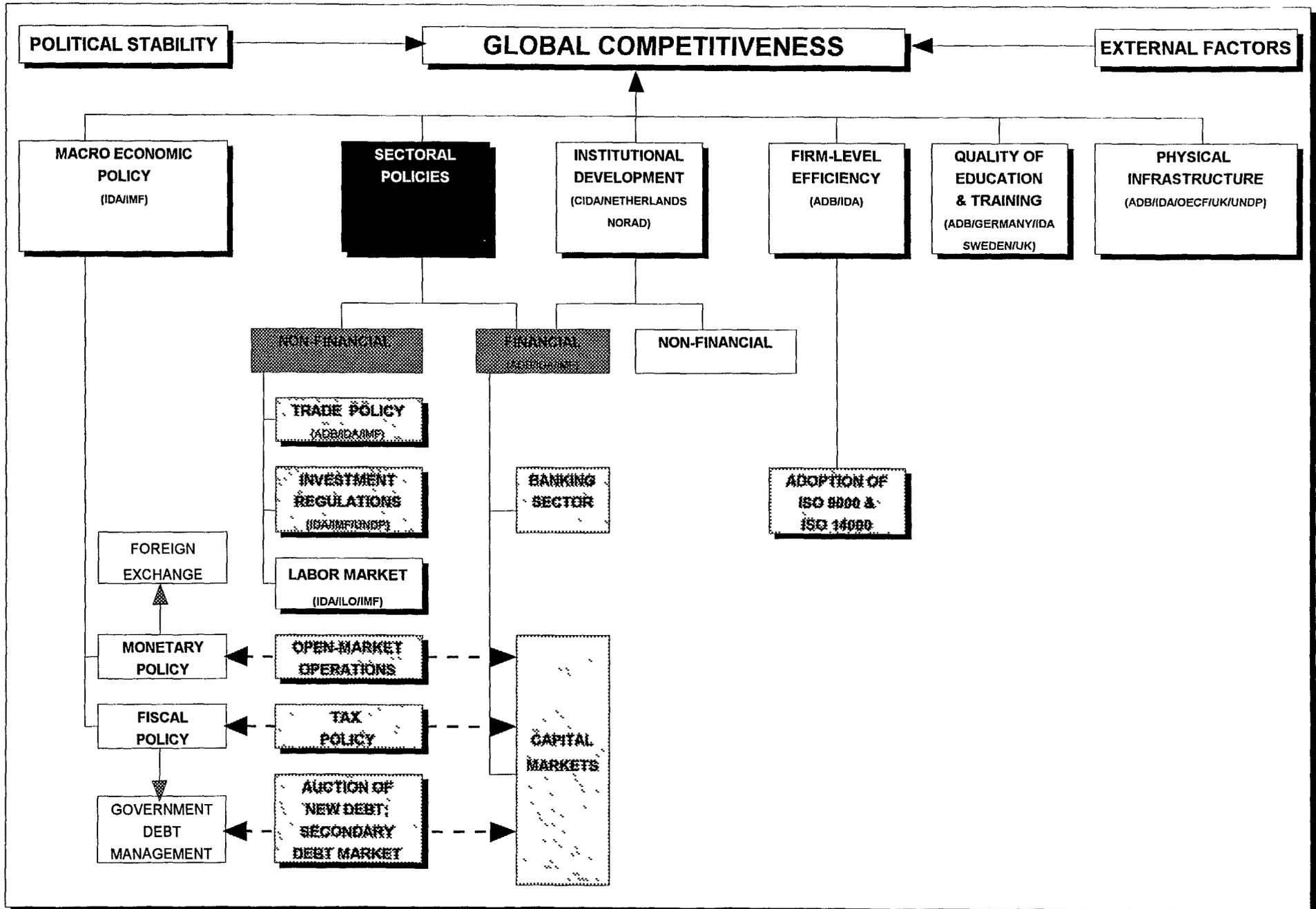
### **2.2 The Economic Subgoal -- Strengthened Global Competitiveness in Trade and Investment**

Sri Lanka's heavy reliance on garment and plantation crops to bolster the trade account is disturbing. In addition to making the island highly vulnerable to external shocks, Sri Lanka has not yet begun to capitalize on the strength of its human resource base. Reforms in labor markets, infrastructure development and macro-economic policies will be needed to diversify and strengthen the economy.

In collaboration with other donors, USAID can fill a critical niche in the area of sectoral policy and an improved framework for trade and investment. The subgoal will be used as a reference point in determining which policies or regulatory reforms are significant and should be included in the program.

At the subgoal level, USAID will monitor national and sectoral trends including value of non-traditional exports, total trade as a percentage of GDP, total stock market capitalization and total private direct investment.

# FACTORS CONTRIBUTING TO GLOBAL COMPETITIVENESS



Note USAID activity areas are shaded

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### 2.3 The Strategic Objective: An Improved Framework for Trade and Investment.

The economy suffers from serious distortions due to tariff and non-tariff barriers restricting the free flow of goods and services. These barriers pose a particularly severe problem for firms attempting to remain competitive through modernization, since it is difficult or impossible to import new technology in many sectors. A lack of breadth and depth in financial markets, combined with trade barriers, inhibit both foreign and domestic investment. If Sri Lanka is to maintain the 6% GDP growth rate achieved in 1997 it must develop a comprehensive plan to diversify the economy, especially production for export, introduce dramatic changes in trade, industrial, and agricultural policies and regulations, and establish a well functioning financial markets system. If the growth rate is stymied, social services will eventually suffer and past achievements in the health and education status of the population could deteriorate.

Limited economic growth resources dictate that USAID/Sri Lanka's program be focused on systemic problems that impede growth and competitiveness. The revised strategy focuses on critical policies, regulations and practices which will improve the economic enabling environment. The Sustainable Economic Growth Program (SEGP) will direct resources towards an *improved framework for trade and investment*, which will contribute to improved financial market and trade/investment systems, policies, and practices which will be necessary to attract the levels of investment required for sustained growth and competitiveness.

Indicator of success

Strategic Objective (SO)	Performance Indicator
Improved Framework for Trade & Investment	1 Cumulative increase of nine policies adopted and practices implemented by 2000

Note: The following stages of the reform process will be used to measure results in the policy/regulatory reform activities: 1) agenda/identification, 2) awareness, 3) evaluation/analysis, 4) dialogue, and 5) adoption. Stage 5) will be measured at the SO level.

At the SO level, USAID will measure adoption rates of key reforms. The policy agenda will be tracked yearly at the Intermediate Result (IR) level according to the stages of the reform process. IR indicators will focus on evaluation/analysis and dialogue stages of the reform process. During the evaluation/analysis stage, policy or regulatory impediments which have been identified as important barriers to competitiveness will be examined and the benefits of reform will be clearly described. During the dialogue stage, partners, associations, USAID and the GSL will engage in discussions on the substance of required reforms, methods of

implementing reforms and the expected impact. A centerpiece of the program will be support to private associations to develop the case for policy or regulatory change. USAID believes that change is more likely if associations of enterprises affected by a particular policy or regulation become the primary advocates for reform.

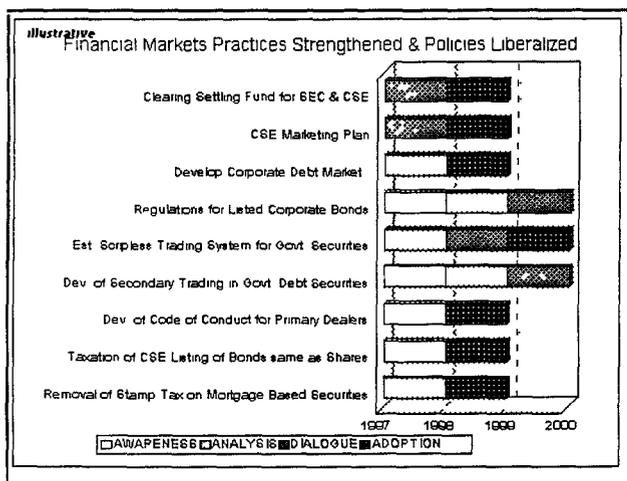
The IRs provide lists of policies, regulations and practices which have been identified. Others may be added to the list (e.g., as a result of the findings of an upcoming competitiveness study in partnership with G/EG/EM), while some may drop off the list. USAID would like to maintain enough flexibility to focus on the most important reform areas in a dynamic, and sometimes volatile, global and domestic economic environment.

### **2.3.1 Intermediate Result 1 (IR1): Financial Market Practices Strengthened and Policies Liberalized.**

A strong and stable financial system is essential for sustainable growth and greatly enhances the participatory base. As evidenced by the financial crisis in some East Asian countries, without a stable and fundamentally sound financial system, economic achievements attained in the past can be jeopardized. An open and transparent, but well regulated financial market system is an absolute requirement for Sri Lanka to maintain and improve its global competitiveness in trade and investment.

In previous years, USAID and its partners have achieved significant results in improving policies and practices in Sri Lanka's financial markets. Although small in capitalization, the Colombo Stock Exchange (CSE) is considered one of the most modern and efficient exchanges in Asia. The Securities Exchange Commission (SEC) is providing sound regulatory guidance and the Central Bank (CBSL) is providing much needed leadership to implement financial reforms that will affect the country's competitive posture. Recently, a policy group consisting of high level members from the Private Enterprise Reform Commission, Ministry of Finance, SEC, CSE, CBSL, the Brokers Association, and the GSL Revenue Department was established under the USAID assistance program. This group provides the leadership for financial sector reform and expansion. USAID activities have also helped to inaugurate the new central depository system, install an automated trading system, establish a primary dealers association, establish a second CSE board for smaller companies to participate in the market, created an Over-the-Counter exchange, and begun the process of creating a clearance and settlement guaranty fund to increase investor confidence. With USAID assistance, the CBSL has begun issuing two-, three- and four-year Treasury Bonds, moving the GSL toward open market operations and a more efficient monetary policy regime. These efforts need to be expanded to lay the required financial systems foundation for future growth, and to attract foreign and domestic investment capital.

The financial markets component of the economic growth objective will include the following activities:



- preparation of a marketing plan and implementation of a marketing strategy to attract investors and increase company listing on the CSE,
- development and implementation of a framework (tax rules, governing regulations, etc) for a viable and transparent corporate debt market,
- establishment of a clearing and settlement guarantee fund for transactions on the CSE (already at the draft stage),

- expansion of GSL borrowing through open market operations, rather than from state-owned banks and pension funds,
- development of a secondary market for trading government securities,
- identification and adoption of key policies to broaden the investor base and improve the overall efficiency of the country's capital markets

#### Intermediate Result 1, Indicators and Targets

Intermediate Result 1	Performance Indicator
Financial Market Practices Strengthened & Policies Liberalized	<ol style="list-style-type: none"> <li>1 Cumulative increase of 15,000 individuals holding publicly traded shares through the CSE by 2000</li> <li>2 Increase of domestic government borrowing through open market operations by five percent per year from 17 percent in 1997 to 32 percent in 2000</li> <li>3 Three policies or improved practices in progress per year (either the analysis/evaluation or dialogue stage)</li> </ol>

Note The following stages of the reform process will be used to measure results in the policy/regulatory reform activities 1) agenda/identification, 2) awareness, 3) evaluation/analysis, 4) dialogue, and 5) adoption Stages 3) and 4) will be measured at the IR1 level

Increases in the number of individuals holding shares indicate the overall vitality of the CSE, reflecting growth in the number of firms listed, wider participation and a broadening of the investor population base. An increase in the percentage of total GSL borrowing through the open market indicates a commitment to free market principles, and has significant influence on interest rates and the CBSL's ability to implement appropriate monetary policy. The policies and practices identified as indicators are important signals of the strength and stability of the financial market system, as well as the capacity of the system to attract the capital needed to fuel sustainable economic growth.

USAID/Colombo, ISTI and staff from ANE and G/EG have worked jointly to refine this ongoing program. It remains an important part of the strategy and ISTI will continue to be USAID's partner, along with the CSE, SEC, the CBSL and the Financial Markets Policy Group. These partners have been strong advocates for programs to strengthen capital markets, including measures to provide an appropriate regulatory framework that protects the institutions and investors while simultaneously providing required free market incentives to attract additional investment.

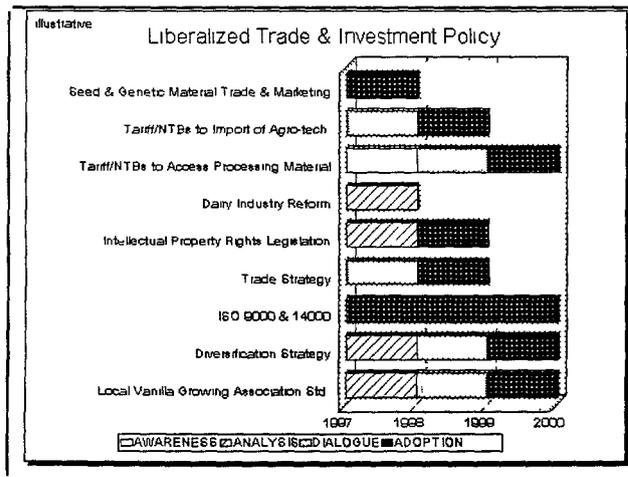
Several Global Bureau funded programs related to the strategy will continue through the strategy period. The Microenterprise Support Activity (MESA) provides grant and technical assistance to promote microfinance investment and service delivery among local NGOs. Using funding from GBureau's PRIME activity, the Women's Development Federation and the Sanasa Federation are being supported. The grants will end in September 2000. G/EGAD/CI is implementing a Loan Portfolio Guaranty program, working with five local banks. The program provides a guaranty up to 50% for small and medium-scale borrowers. The ongoing Housing Guaranty program has two components: a guaranty facility for housing mortgages and a technical assistance facility for environmental infrastructure. Both activities are scheduled to end in September 1998, although extensions are being considered by RHUDO, which manages both programs.

### **2.3.2 Intermediate Result 2 (IR2): Liberalized Trade & Investment Policies**

A sound trade and investment policy environment is essential for businesses to operate efficiently and for sustainable economic growth. Inappropriate policies impede competition and negatively affect the investment climate. Reduced efficiency affects the sustainability of business organizations, and reduces employment and income generating opportunities, thereby limiting prospects for raising standards of living and alleviating conditions of poverty. In this regard, USAID will help create better conditions for broader participation in the growth process across all sectors and sizes of enterprises, socio-economic strata, and among foreign and domestic investors by addressing policy reforms and regulatory issues constraining trade and investment. A liberalized policy environment for trade and investment is directly related to Sri Lanka's ability to become more competitive. With a relatively small domestic market, Sri Lanka's growth

must be export based (products and services) and future increase in employment, incomes and standards of living will come primarily from export-oriented enterprises

This component of the economic growth program will draw on USAID's extensive local business contacts and attempt to strengthen partnerships between the GSL and private enterprise associations. Through previous firm-level assistance, USAID and its partners have developed strong relationships with a wide range of companies and helped to create and strengthen associations, which provides a foundation to advocate policy and regulatory reform. Where possible, associations will be supported with data and analyses to propose policy changes to the appropriate GSL authorities. The following activities have been identified to accomplish



#### IR2

- preparation of a long-term trade and investment strategy for the Department of Commerce, including a diversification plan,
- identification, analysis, promotion and adoption of key reforms which address productivity, the quality of products and services, and Sri Lanka's competitiveness,
- strengthening of the framework to protect intellectual property rights and empower owners by providing a means of relief from infringement and piracy,
- continuation of programs to promote and implement ISO 9000 and 14000 standards

#### Intermediate Result 2, indicators and target

Intermediate Result 2	Performance Indicator
Liberalized Trade & Investment Policies	<ol style="list-style-type: none"> <li>1 Development of a long-term trade &amp; investment strategy</li> <li>2 Three policies or improved practices in progress per year (either the analysis/evaluation or dialogue stage)</li> </ol>

Note The following stages of the reform process will be used to measure results in the policy/regulatory reform activities 1) agenda/identification, 2) awareness, 3) evaluation/analysis, 4) dialogue, and 5) adoption Stages 3) and 4) will be measured at the IR2 level

Assistance will be provided through IESC, OSU/DAI, and G/EG/EM contractors to business and other associations to support their efforts to improve policies which negatively affect their members Policy analyses and specialized short-term technical assistance will consolidate prior achievements in business expansion and improve the enabling environment for trade and investment US Asia Environmental Partnership funding has been added to the cooperative agreement with IESC to support sales of US environmental technology as well as ISO 14000 initiatives

#### Key Assumptions for the SO

GSL remains committed to open markets through economic reform, deregulation and trade liberalization, including adoption of World Trade Organization guidelines

#### **2.4 Special Objective 1 (SpO) - Citizens' Rights Better Protected in Law and Practice**

The President of Sri Lanka has put forward a proposal for constitutional reform to devolve expanded authorities to regional councils, permitting minority groups greater control over local governments This "devolution" package, however, is currently stalled in Parliament The minority parties want it to go further in granting powers to local governments, while the main opposition party, the United National Party (UNP), believes the current package goes too far The UNP has now proposed its own devolution proposal There is still no national consensus on the full extent of devolution, although all parties agree that it is necessary in some form The U S Embassy in Colombo is continuing to work through diplomatic channels to try to bring the parties together on this issue

With the continuation of the civil conflict and uncertainty about the timing of devolution, it is essential that a sound foundation for human rights and access to a fair and efficient judicial system be in place. If lasting peace is to be achieved and devolution is to be sustainable, people must be confident that there is open access to the judicial system and that average citizens, especially minorities and disadvantaged groups, will be treated equally and fairly If such a system is not in place, the task of creating national unity once the conflict ends will be impossible It is also important that human rights programs be expanded into the conflict areas in the north and east

The SpO1 activities will address lack of awareness of rights, lack of access to justice for those who are without recourse due to exorbitant costs involved in hiring lawyers and filing action in courts, law delays and access to justice through provision of alternate dispute resolution systems, the backlog of cases at the district level courts, and the need to further professionalize government and non-government human rights organizations

Initially SpO1 will be implemented primarily through two partners, The Human Rights Commission of Sri Lanka and The Asia Foundation (TAF). The government has recently appointed an independent Human Rights Commission through an act of parliament to improve the human rights situation in the country. The HRC has wide powers to hear, investigate, and rule on human rights violations, but its infrastructure is weak and its staff are mostly untrained. USAID will support improvement of the HRC's operational capabilities, including communication between the head office and their ten regional offices, and computerization. Assistance for setting up of new offices in the conflict area, such as Mannar, will be of special focus and will improve its ability to assist people whose rights have been violated primarily by the security forces. Training in human rights, investigative techniques, and community awareness building will enable HRC officers to record, investigate, mediate, and report violations as well as conduct human rights awareness programs in local communities. This component of the SpO1 will be complemented by technical assistance to the Commission funded by USAID's Office of Transition Initiatives (OTI).

TAF will cover a wider spectrum of activities. Evidence indicates that many human rights violations go unreported due to lack of awareness and confidence in authorities. Activities to promote legal awareness among the people, and to professionalize the organizations providing redress for human rights violations, will increase the number of violations reported. Through TAF, assistance to the government sponsored Legal Aid Commission and NGOs that provide legal aid will increase the availability of legal aid to disadvantaged people whose rights have been violated.

A pilot program providing legal aid to be implemented by the Ministry of Justice (MOJ) will also be supported using development assistance funds remaining in the Citizen's Participation (CIPART) project. While most other legal aid programs provide assistance to victims whose human rights have been violated, this program will also focus on women and children with civil or criminal grievances. For example, women who are not receiving maintenance payments, or children whose testamentary rights have been violated, but are not financially able to file action in a court of law, can obtain relief through this scheme.

Laws delays stemming from congestion at the lower courts is a serious problem in Sri Lanka. USAID and TAF have established a mediation program through the Ministry of Justice, and have succeeded in getting a law passed making it mandatory for cases below a value of Rs 25,000 to be first referred to a mediation board. A sub-grant to the MOJ will further develop and strengthen the mediation boards to receive this increased caseload as well as expand their services into specialized areas such as family and environmental mediation. Assistance will also be provided to expand the mediation boards to new areas of the north and east, and training programs for mediators will be developed in the Tamil language. To further reduce congestion at the courts, a sub-grant to a new NGO promoting commercial arbitration will attempt to remove these cases from the judicial system.

To further expedite pending cases in the lower courts, TAF will also work with the Judicial Services Commission to increase the efficiency of selected courts through computerization. This program builds on the successful computerization of the court of appeal in 1996-97 which reduced the backlog from 13,500 cases pending in 1995 to 8,700 cases in 1997. Other activities will include training in case management and in the special needs of human rights cases.

Women workers in Sri Lanka predominate in the garment and tea sectors. They are paid less than their male counterparts, work long hours in difficult working conditions, and are behind their male counterparts in representation at trade unions. Key components of a proposed program on the rights of women workers include: (1) increasing women's participation in the trade union movement, (2) empowering and protecting the rights of women in unorganized sectors (e.g., migrant workers), and, (3) combatting violence against women workers in the plantation sector.

Indicators and targets

Special Objective1	Performance Indicator
Citizen's rights better protected in law and practice	<ol style="list-style-type: none"> <li>1 Increase in number of violations reported to authorities from 1,320* in 1997 to 2,000 in 1998, 2,500 in 1999 and 3,500 in 2000</li> <li>2 Increase in number of legal aid cases represented from 8,828 in 1997 to 11,000 in 1998, 12,000 in 1999 and 15,000 in 2000</li> <li>3 Increase in number of cases referred to alternate dispute resolution systems from 110,000 in 1997 to 120,000 in 1998, 130,000 in 1999 and 150,000 in 2000</li> <li>4 Decrease in number of backlog cases in selected district courts in Colombo from 12,231 in 1997 to 10,000 in 1998, 5,000 in 1999 and 3,000 in 2000</li> </ol>

\* Reported to the Human Rights Commission of Sri Lanka

When the form and extent of devolution is finally agreed upon, there may be opportunities for USAID to facilitate the process. Provincial governments will face numerous challenges as they become empowered, including fiscal management and governance issues. With ESF or DA funds, if available, this SpO could be expanded to help ensure that devolution succeeds and is

sustainable USAID will conduct an analysis and propose activities for AID/W approval to support the devolution process at the appropriate time during the strategy period

#### Key Assumptions

- 1) GSL's policies will foster broad-based growth and socio-political stability,
- 2) there will be continuing efforts by the GSL to resolve the conflict in the North and East to restore functioning communities, peoples' faith in dispute resolution, and a sense of normalcy in an atmosphere that respects fundamental rights, and
- 3) GSL will continue to support an independent judicial system

#### **2.5 Special Objective 2 (SpO2) - Enhanced Economic and Social Opportunities for Disadvantaged Groups.**

This special objective will facilitate reintegration of people who are disadvantaged, primarily by the ethnic conflict, to recover from their circumstances and to participate in their local communities and economies. The 14 year ethnic conflict in the north and east has disabled thousands of people, displaced hundreds of thousands, and continues to create a large internally displaced population. Providing short-term relief and resettlement assistance to these disabled and/or displaced people is an urgent need and a high priority of the GSL. Unless they are provided with special support, particularly services for children who have lost family members, their opportunity for returning to a normal life will be greatly diminished. Another serious threat to the well-being of children in Sri Lanka is sexual exploitation and abuse. It is estimated that as many as 30,000 children, mostly boys on the western and south-western coasts, are involved in prostitution.

The SpO2 will be implemented through grants to international and non-governmental organizations (NGO), focussing on programs which will 1) attempt to reunite children with their families or relatives, or find appropriate substitute families for other displaced children, 2) address the psychological and social effects of stress and trauma of children affected by the armed conflict, 3) provide prosthetics and other orthopaedic devices to help improve the physical mobility of amputees, and 4) skills training programs to enable vulnerable groups of youth and sex workers to seek alternative employment and socially acceptable income generating opportunities. USAID activities also complement efforts of the UN agencies such as UNICEF, WHO, UNHCR and international voluntary organizations in the delivery of humanitarian assistance. Currently, the Mission works with a number of local organizations in assisting different disadvantaged groups. To reduce the management burden associated with these grants, feasibility of an umbrella mechanism for the program will be explored.

Indicators and targets

Special Objective 2	Performance Indicator
Enhanced Economic and Social Opportunities for Disadvantaged Groups	<ol style="list-style-type: none"> <li data-bbox="630 534 1451 612">1 Cumulative increase in the number of amputees fitted with prosthetic devices from 1,300 in 1997 to 5,800 by 2000</li> <li data-bbox="630 655 1451 761">2 Cumulative increase in the number of new participants in community-based and facilitated psychological and social activities from 9,768 in 1997 to 25,000 by 2000</li> </ol>

Although the conflict continues throughout much of the north and east of the island, the government regained control of Jaffna town and parts of the Jaffna peninsula in late 1996. As part of its strategy to end the conflict, the government has permitted resettlement of the area although it is still under strict military control. Approximately 1/2 of the former population of 850,000 has resettled in the area. Recent local government elections restored civilian administration to the area for the first time in almost 15 years. USAID/OTI is implementing a program to help the area return to normalcy and foster support for peaceful resolution of the conflict. Current activities include support to the Human Rights Commission, microenterprise, and equipment for the Jaffna Technical College. OTI support continues to be needed in this area. Restrictions on the free movement of goods and people into and out of the peninsula because of security concerns make it difficult to support ambitious redevelopment schemes, which could even be harmful at this point. However, USAID and OTI are exploring the possibility of training for newly elected local government officials, credit programs for housing reconstruction, and similar support for those who are too poor to be eligible for regular thrift and credit programs. Limited demining or mine awareness programs will also be explored. If a change in the conflict situation provides an opportunity for greater relief, rehabilitation and or development assistance in Jaffna or other areas affected by the conflict, such activities could be pursued under this special objective.

Key Assumption

GSL remains committed to allowing NGOs to work effectively in the North and East

### 3.0 PROGRAM RESOURCE REQUIREMENTS

Table 1 provides a breakdown of funding requirements to implement and achieve the results of the revised strategy through FY2000. Over the three-year strategy period, the Mission will require a minimum of \$7.5 million in DA funding for the Economic Growth SO. Additional economic growth resources in FY1999 would allow the Mission to respond more quickly and comprehensively to the findings of the competitiveness study planned for FY1998.

The Mission also requests \$3.0 million in ESF to fund its Human Rights/Democracy SpO1 and \$1.7 million from the War Victims Fund (WVF) and Displaced Children and Orphans Fund (DCOF) to fund its Humanitarian Assistance SpO2 over the strategy period.

Funding Category	Strategic Objective			Special Objective 1			Special Objective 2			Total		
	FY1998	FY1999	FY2000	FY1998	FY1999	FY2000	FY1998	FY1999	FY2000	FY1998	FY1999	FY2000
<b>Development Assistance (DA)</b>												
Discretionary Funds	2,998	1,500	3,000	-	-	-	-	-	-	2,998	1,500	3,000
USABF	77	80	80	-	-	-	-	-	-	77	80	80
WVF/DCOF	-	-	-	-	-	-	500	500	700	500	500	700
<b>Economic Support Funds (ESF)</b>	-	-	-	1,000	1,000	1,000	-	-	-	1,000	1,000	1,000
<b>Total</b>	<u>3,075</u>	<u>1,580</u>	<u>3,080</u>	<u>1,000</u>	<u>1,000</u>	<u>1,000</u>	<u>500</u>	<u>500</u>	<u>700</u>	<u>4,575</u>	<u>3,080</u>	<u>4,780</u>
Net* AHC requirements												
* Global Health support												
USAID utilizes PL 480 Title III local currency to supplement activities of the SO and the two SpOs												

The SpO1 will be financed from Economic Support Funds and limited development assistance funds available in the pipeline of CIPART. Local currency balances generated from an earlier PL-480 Title III program will also be used in supporting the program costs of sub-grants given by TAF to local NGOs. The SpO2 will be financed by the following sources: continuing funding partnerships with the DCOF and WVF administered by Global Bureau, a portion of CIPART's special activity pipeline, and Local Currency balances generated from PL480 Title III wheat granted to the GSL during FY91-94.

As of December 31, 1997, the Mission's pipeline was \$12.9 million. Expenditures for the first half year of FY1998 were lower than planned as the Mission curtailed its planned activities due to the change in focus and revision of its strategy. Expenditures for FY1998 are expected to be

around 9.8 million, and the resulting pipeline after obligating FY1998 funds will be around 8.8 million (14 months of forward funding). Expenditures for FY1999 are expected to be 7.2 million. The reduced level of DA funds in FY1999 will create a very tight funds management situation as the pipeline will drop to around \$4.0 million and result in only eight months of forward funding. At these requested low levels a marginal increase or decrease of funds could create a significant impact on program results.

As of December 31, 1997 the local currency special account (from previous PL 480 III programs) pipeline was US\$ 5.7 million (Rupees 347 million). In addition \$3.7 million (Rupees 225 million) is unprogrammed and available to support NGOs of all three objectives of the strategy.

#### 4.0 PROGRAM MANAGEMENT REQUIREMENTS

USAID's operating expense budgets and staff levels have been planned (as submitted in this year's R4) at the minimum required to carry out the revised strategy. The FY1998 OE budget is \$1,506,600 (excluding ICASS charges), a 30% reduction over FY1997 OE obligations. For FY1999, USAID is estimating a 22% decrease in the OE budget to \$1,177,200 and a further 29% reduction in FY2000. These levels represent significant yearly reductions consistent with the smaller staff size and lower program funding levels. In FY1999, as detailed in the R4, wherever practicable, support services will be purchased through ICASS arrangements.

USAID's USDH levels drop from five at the end of FY1997 to four in FY1998 and finally to two in FY1999. OE-funded FSN staff, totalling 53 at the end of FY1997, will be reduced to 25 by the end of FY1998 and to 18 by the end of FY1999. There are an additional four program-funded FSN staff.

Where possible, USAID has consolidated staff functions in order to improve the efficiency of our operations and reduce levels, and will move to ICASS for numerous services (e.g., motorpool, OE procurement, C&R services). Payment mechanisms such as Letters of Credit will be used where practicable to reduce the number of vouchers and the overall workload on the Controllers office. Program and activity implementation mechanisms, such as umbrella grants with sub-grant components, will be used to reduce the direct management burden on the Mission. G/EG programs will be increasingly important mechanisms in the implementation of the economic growth SO. In FY1999, USAID will begin to use G/EG mechanisms to support the SO and by the end of FY2000 the Mission will closeout the three main contracts under the SO. Finally, activities not directly related to the revised Country Program Strategy's SO and two SpOs will be phased out, reducing the number of management units.

## GLOSSARY OF ACRONYMS

CBSL	Central Bank of Sri Lanka
CIPART	Citizens Participation Project
CSE	Colombo Stock Exchange
DA	Development Assistance Funds
DAI/OSU	Development Alternatives Inc /Oregon State University
DCOF	Displaced Children and Orphans Fund
ESF	Economic Support Fund
FSN	Foreign Service National
GDP	Gross Domestic Product
GSL	Government of Sri Lanka
HIG	Housing Investment Guarantee
HRC	Human Rights Commission
IESC	International Executive Service Corps
IR	Intermediate Result
ISTI	International Science & Technology Institute Inc
MOJ	Ministry of Justice
NGO	Non-Governmental Organization
OE	Operating Expense
ODA	Official Development Assistance
OTI	Office of Transition Initiatives
SEC	Securities and Exchange Commission
SO	Strategic Objective
SpO	Special Objective
TAF	The Asia Foundation
UNP	United National Party
USDH	U S Direct Hire
WVF	War Victims Fund