

C. LANKA

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ACRONYMS

AMP	-	Accelerated Mahaweli Program
CUP	-	Currency Use Payment
DARP	-	Diversified Agricultural Research Project
DA	-	Development Assistance
EDB	-	Export Development Board
EEP	-	Export Enhancement Program
EIED	-	Employment Investment & Enterprise Division
FIAC	-	Foreign Investment Advisory Committee
FSN	-	Foreign Service National
GCEC	-	Greater Colombo Economic Commission
GDP	-	Gross Domestic Product
GSL	-	Government of Sri Lanka
HG	-	Housing Guarantee
IBRD	-	International Bank for Reconstruction & Development
IDI	-	International Development Intern
IESC	-	International Executive Service Corps
IMF	-	International Monetary Fund
ISM	-	Irrigation Systems Management
JCC	-	Joint Career Corps
MARD	-	Mahaweli Agriculture Rural Development
MOH	-	Ministry of Health
NFDM	-	Non Fat Dry Milk
O&M	-	Operations & Maintenance
OE	-	Operational Expenses
OYB	-	Operational Yearly Budget

PASA - Participating Agency Service Agreement
PDSP - Project Development Sector Program
PEPP - Private Enterprise Promotion Project
PP - Project Paper
PRE - Private Enterprise Bureau
PSDP - Private Sector Development Program
PSC - Personal Services Contract
PVO - Private Voluntary Organization
REDS - Rural Enterprise Development Sector
SEC - Securities Exchange Commission
SFC - Subsidiary Food Crops
SLBDC - Sri Lanka Business Development Center
SOE - State Owned Enterprise
TA - Technical Assistance
TCN - Third Country National
UNP - United National Party
USDH - United States Direct Hire

I. OVERVIEW

A. Program Goals and Objectives

The accompanying CDSS Up-date provides the basis for the modifications to the development strategy proposed by the Mission. Two strategic objectives are presented: (1) increased rural incomes, productivity and food consumption and (2) an expanded private sector role in development. These two primary focuses are supplemented by a new set of "cross-cutting themes" which both underscore special concerns in our residual and evolving portfolio and established a further basis for policy dialogue. The first strategic objective is a broadening of the prior objective of improving agricultural productivity and farm incomes. This broadening was done in recognition that rural and specifically farm income is to some extent dependent on off-farm income sources and that it is necessary to focus on off-farm employment to absorb excess on-farm labor. While we are concerned about rural incomes, agriculture will remain the major preoccupation given its predominance in rural Sri Lanka. Food consumption has been added because most rural people in Sri Lanka are food producers and attempts to increase incomes and productivity will lead to increased food consumption as well. Food self-reliance and the improvement of nutrition levels are appropriate national goals as well, and ones to which our programs will contribute.

The second strategic objective is a substantial change from the previous rural enterprise and employment focus. Employment generation remains a concern, but the imbalance between private and public sector productive capacity has generated a need to look beyond just

employment. We will attempt to address this structural problem by both increasing private sector investment and reducing the public sector's commercial activities.

New policy developments within the Agency (as per paragraph 6 of STATE 37076 dated 9 February 87) have been carefully considered in formulating our program in Sri Lanka. In regard to child survival, Sri Lanka has already surpassed the targets set in the Blueprint for Development and is not a priority country for assistance programs of this type. In education Sri Lanka also exceeds the Blueprint goals but under a highly centralized system. The Mission is supporting efforts under the centrally funded BRIDGES project to improve education planning and decentralize control. Privatization plays a major part in our strategy as a piece in our efforts to increase the private sector's role in development. We are working to diversify agricultural production, some of which we anticipate will lead eventually to agricultural exports. However, none of the selection of crops we are working with are expected to have any significant adverse impact on U.S. agricultural exports. Likewise, our private sector projects will be developing some export oriented enterprises. We plan to carefully review these efforts to assure that we do not support the manufacture of goods considered import sensitive in the U.S. The Mission does not currently program the local currency generated from our Title I program, but the rupees are attributed to GSL development development acceptable to the Mission. We are prepared to move to direct programming of the local currency, and have so indicated to the GSL, if counterpart funding for our project portfolio becomes a serious problem. We feel the issues of biological diversity and tropical rain forests in Sri Lanka have been identified,

and are being adequately addressed by Sri Lankan and donor authorities. We will submit the required supplemental analysis within sixty days. We have used participant training extensively in the past and will continue to do so in the years ahead. The training is done in direct support of our strategic objectives and is funded accordingly. A new participant training activity is being prepared for obligation this Spring and will reflect the findings of the recent intra-agency committee.

B. Progress Against Objectives, Old and New

The past year was not a particularly good one for improved rural incomes. Using paddy production and prices as a proxy measure, real incomes dropped slightly primarily due to decreased total acreage harvested. Irregular monsoon rains were the principal culprit, further indicating the need for diversification and improved irrigation water delivery. Diversification efforts have improved now with the USAID project on subsidiary field crop (SFC) research beginning full implementation. Under that project a baseline survey was completed which will provide the basis for measuring future progress in this area.

As part of the modification of the strategy we have redefined the measurement of progress on our first strategic objective. The target will now be real net rural income and food consumption in the dry and intermediate zones increasing a rate of 3% or more per annum by 1992. Over the next year we will be further developing the means to measure those levels. Intermediate objectives identified are increased acreage under irrigation, increased paddy production, improved water management and increased SFC contribution to incomes. We have specified the dry and intermediate zones because that is where our program will have its greatest geographic impact.

With the strategy shift from employment and rural enterprises to expanding the private sector we have redefined some of our benchmarks. For those still relevant we have made some progress. An industrial development policy for Sri Lanka which clearly delineates the public and private sector roles was presented to the Cabinet Secretaries in February 1987 and should be made official in the near future. The government has taken additional steps toward privatization with two new bills before parliament which will facilitate privatization and the government continues to progress, albeit in a somewhat ad hoc manner, in moving toward privatization of a number of specific business concerns. Also, President Jayewardene recently participated in two national conferences on this subject thus indicating its increased importance, and giving us new hope for further advances.

Our new intermediate objectives in this area will be to stimulate private enterprise undertakings, encourage privatization of state owned enterprises, strengthen capital markets, strengthen institutions that promote the private sector and generate private investment in the Mahaweli.

As we made the modifications to the strategy, we have had some difficulty in determining both sectoral and intermediate objective targets. In particular, we have had difficulty in establishing sectoral goals that are broad enough to be nationally significant, yet not so broad that progress on our project and policy interventions can not be realistically attributed to their realization. Last year's Action Plan was overly ambitious and overly detailed when considered against this

year's guidelines. Moreover, seeking to qualify such targets, we have found that much of the data used in Sri Lanka is now relatively old as it is based on surveys and other work done in the early 80's. Baseline data on which to measure progress from this point on is extremely hard to find. We are especially "out of synch" in relation to our private sector development targets where we expect the design work to contribute to setting progress benchmarks. Data to track progress will be developed as the new sectoral goals are refined and new projects designed.

C. Constraints to Progress

As explained in greater detail in the CDSS update and this document, in addition to the overall ethnic situation, we foresee two major constraints on the Sri Lankan side to pursuit of our broadest objectives in the coming twenty-four months. The first is the sharp squeeze on fiscal resources (likely to be exacerbated by the current drought) which has the effect of both reducing growth levels, and possibly limiting counterpart staff and funds available to our project activities. The second is the fact of a hotly contested national elections for President (in 1988) and Parliament (in 1989) which may inhibit the boldness in undertaking major shifts in economic policy and priorities in the intervening years. This latter situation is compounded by the preoccupation of principal national leaders in settling the ethnic strife.

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The impact of the squeeze on fiscal resources is likely to be mitigated by the stated GSL intention that activities with donor-matches receive priority for rupee funding. We will have to monitor this carefully, however, particularly as it pertains to counterpart staffing (there is an overall GSL freeze on new staff). If rupee financing

becomes problematic, we may wish to consider more detailed, specific programming of Title I counterpart. The impact of the election scenario is more speculative especially since, on the more positive side, it may prompt the ruling UNP to take some dramatic and positive measures that they believe underscore their differences from the opposition.

On the AID side, the principal constraint to program impact is the recent reduction of staff and program levels. This has been noted critically by senior GSL leaders, thereby affecting the overall U.S. posture here. Programmatically, the cuts have forced a reduction and concentration in our portfolio that effectively removes us from some key sectors.

Ironically, as developed more fully in the CDSS Overview, the constrained financial environment has provided us new opportunities for policy-dialogue. The next two years will see greater focus on such activities along with increased attention to the possibilities for effective donor coordination on both policy and implementation issues, and further efforts to integrate resources, especially PL 480, in order to reinforce our objectives.

D. Management Issues and Preoccupations, Old and New

At this time last year the Mission was considering a shift to program assistance modalities. For reasons cited in the overview to the CDSS update, a full bore campaign to implement such an approach has been rejected at least for the next few years. Also contemplated last year was a Title III program. However, it was determined that Title III would have been only marginally more effective yet would have been more staff

intensive than the Title I program. The Mission opted to continue with Title I, a decision concurred in by the GSL. Finally, the Mission planned to move in 1987 on the private sector activities by developing both the REDS and the Private Sector Development Program.

Reconsideration of the program led us to believe that we were trying to move too fast on that front, and we decided to hold them both off a year while we thoroughly tested the waters. We feel the program now better reflects current Sri Lankan development needs and Agency priority interests. This Action Plan reflects that revised program focus and presents our achievements and plans in that framework.

The redefinition of objectives and restructuring of the program were principal achievements over the past year and were of particular concern to the new Mission management. Overall decreases in staff have been accompanied by shifts in available positions and functions in an effort to buttress our new, more focussed program

In FY 86 the implementation issues raised by PEPP (383-0082), Water Management (383-0057) and the completion of major Mahaweli construction under MBD II (383-0073) were primary preoccupations of Mission staff. As those issues have been resolved others have taken their place such as conflicts with security objectives in the Mahaweli Environment project (383-0075), a satisfactory wrapping up of the contentions claims issue on MBDI and counterpart staffing requirements in agriculture and irrigation.

As there were no new projects begun in FY 85 and ongoing projects were fully funded, there has been a press of new project development in FYs 86 & 87. ISM (383-0080) and AGPLAN (383-0083) were designed in final and signed late in FY 86. MARD (383-0086), DS&T (383-0085) and PVO II

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(383-0101), and MADS (383-0103) are being designed now. These new projects are all essential in terms of implementing our strategy.

As mentioned previously, the two new projects proposed for FY 88 have been identified before: Rural Enterprise Development Sector (REDS), 383-0090 and Private Sector Development Program (PSDP), 383-0100. REDS will develop in the Mahaweli methodologies for increasing private sector investment in the rural areas. PSDP will cover a wide range of private sector development activities from capital market improvement to strengthening organizations that promote and support the private sector. PSDP will also address privatization issues and provide assistance to the GSL in actual divestiture. Design work has begun on both projects.

A new project start in FY 89 will be dependent on the needs of ongoing projects. The mortgage will reach a critical level at the end of FY 88 and funding requirements of projects already started may account for all FY 89 availabilities. With that in mind, we are preparing a new project for FY 89 which could be made a shelf item for 1990: Development of Agricultural Marketing Systems (DAMS), 383-0093. DAMS will be directed at marketing systems for non-rice agricultural products and will stress private sector involvement.

Over the coming years we will want to consolidate our strategy and further develop our progress indicators. We will be working to make DA, PL 480 and Housing Guaranties work together in achieving the objectives we have established. While setting a firm direction to our program, however, we want to build in the flexibility needed to allow us to react to opportunities in other key development problems.

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II. PERFORMANCE AND PLANS

A. Rural Incomes, Productivity & Consumption:

1. Identify Goals - Goals set in last years Action Plan were established to measure changes in farm income and productivity in the smallholder subsector. Indicators to measure both rice and subsidiary food crops output and yield were identified and are specified below along with an assessment of progress toward the goals during the course of the year.

2. Progress Toward Goals in 1986 - The year of 1986 was not a particularly good year for smallholder agriculture. Several shifts from normal monsoon rain patterns led to a net decrease of 5% in the amount of paddy produced over 1985 which likely caused a small decrease in real small farm income. The pace of expansion of major irrigation facilities slowed because of constraints in financing. The thrust toward crop diversification, however, was bolstered by the USAID-funded Diversified Agriculture Research Project (DARP) which began full implementation during the year. A brief discussion of the progress made toward the specific goals is provided below.

- (a) "Small farmer incomes increasing by 5% or more in real terms by 1990, with a 2% increase in real incomes in 1986." Lacking a direct measure of small farm incomes, paddy production must serve as a proxy for small farmer income. The Mission is trying to develop an income indicator to take into account

production of other farm commodities and non-farm income. As stated above, real farm incomes probably dropped slightly because of a reduced harvested acreage of paddy and a decline in total production by 5%. However, despite the overall production decline, average yields increased by about 1%, reflecting a greater proportion of total production from irrigated lands. Aggregate food consumption levels were maintained through increased rice imports to compensate for shortfalls in production.

- (b) "Gross production of subsidiary field crops increasing by a 15% annual average from 1985 to 1990." Under DARP, a baseline survey was completed during 1986 and is now being analyzed for both Yala and Maha seasons; it will form a basis for measuring future progress toward this goal as well as (c) below. Current production estimates are not adequate to assess whether any change in SFC production occurred during 1986. However, technology generated by DARP-supported research is only beginning to be extended and would not yet have a measureable effect.
- (c) "Per acre production of SFCs increasing by 10% annually from 1987 to 1990." As for (b) above, the baseline data for measuring SFC production increases will not be available before analysis of the DARP baseline survey data. An SFC research program was initiated during 1986. A comprehensive work plan addresses seed production, marketing and a study of SFC cropping patterns and practices, as well as technical

agronomic research. However, effects of DARP on farm level yields would be negligible during 1986.

3. Redefinition of Goals - The overall goal of increased rural income and productivity and food consumption has not changed appreciably from the 1986 Action Plan. Growth targets should be reduced to conform more realistically to the constraints to rural income growth and to the data that will be available to measure income changes.

However, recent increasing cost of production trends for rice will partially offset gains in income from increased extents and yields in the short-run. Likewise, relatively weak demand and low international prices for other field crops will preclude the rapid pace of expansion envisioned in the 1986 Action Plan. The food consumption dimension has been incorporated in the goal statement for several reasons: 1) Food consumption and expenditure data have been more reliable indicators of family welfare in the past than income data, though no current data is available for either, and we expect this indicator to be increased by the USAID program; 2) In Sri Lanka, the majority of consumers are also food producers, so increased productivity and incomes resulting from AID support should result in greater food availability at lower cost and in turn increase consumption; and 3) PL 480 Title I will also increase the availability of food for low income consumers.

The goal is also given a geographic focus in the dry and intermediate zones where most current and planned USAID interventions are directed and where the greatest potential for measurable impact on rural incomes and productivity over the medium term exists. Incorporating these refinements, the goal is now restated as follows:

Real net rural income in the dry and intermediate zones
increasing at a rate of at least 3% per annum by 1992.

This goal will be pursued by USAID through interventions which:

- ** increase the extent of irrigated land (ISM, MDS);
- ** improve water management at both farm and system levels (ISM, MARD, Title I Self-help);
- ** strengthen the generation and delivery of agricultural technology (DARP/MARD);
- ** develop farm support services and viable small-farmer organizations (MARD/ISM); and
- ** rationalize public sector resource allocation to agricultural development (AGPLAN).

After System B of the AMP is completed, achieving the goal through further increases in the extent of irrigated land will not be a major aspect of the USAID program. Further productivity and income gains are most likely to be achieved by improving the performance of existing irrigation systems, agricultural technology adoption, and strengthening the linkages from agricultural producers to consumers through improved market performance. A supportive policy framework is in place with only marginal changes required as outlined under (5) below. Exogenous variables such as rainfall and world commodity prices will have an important impact on sector performance.

Progress toward achieving the goal will be measured through changes in production and consumption in the administrative districts of the dry

and intermediate zones for which production statistics are reported. Additionally, data from cost of production surveys will allow the Mission to estimate net income from the small farm subsector. Non-farm income is more difficult to measure, therefore the Mission must develop a mechanism to estimate this income source. When national food consumption/expenditure surveys are resumed, they will produce additional data to measure progress in both the farm and non-farm sector.

Intermediate objectives and targets are:

- (a) "Increase the extent of irrigated land by 86,000 acres by 1992." Approximately 8000 acres are already in production in Mahaweli System B Left Bank; another 40,000 will be brought into production as a result of the MDS project and the earlier Mahaweli Basin Development, Phases I and II. Under the Irrigation Systems Management project, rehabilitation and management improvement of existing schemes should result in increased irrigation coverage of 46,000 acres. Nationally, additional increases will occur with the support of other donors, particularly the Right Bank of System B (Phase I), the remaining 26,000 acres not yet brought into production in Mahaweli System C, the Kirindi Oya scheme, and the rehabilitation of Undawalawe.

- (b) "Increase paddy (rice) production by an average of 5% per annum from 1987-1990 in the dry and intermediate zones." Increased output during this period will be primarily a function of increasing extent through irrigation; however a 1% annual increase in yields is also expected from improved

agronomic practices. Annual crop production estimates by GSL Department of Census will be the primary source for monitoring progress.

- (c) "Improved operation and maintenance of major irrigation works over 234,000 acres in Mahaweli System B and ISM project area." There are no readily available composite measures to monitor progress toward this goal at a national or regional level. Variables which would ideally be incorporated and monitored include quantity of water used per crop, timeliness of water delivery, maintenance standards of physical facilities, frequency of farmer meetings and collection rates and use of irrigation fees. These variables will be monitored at the irrigation system level as part of ISM and MARD projects. A crude indicator of progress would be the level of crop yields.

- (d) "Increase the contribution of subsidiary food crops to farm incomes by an average of 5% per year from 1987-1992." Increased plantings of SFC's will occur in irrigated lands, particularly during Maha season, which will lead to increased extent and improved yields.

4. Major Programmatic and Management Actions - A major component of meeting our goals is the design and implementation of two new Mahaweli area projects (MARD, MADS). These projects are aimed specifically toward raising farmer incomes in the left bank of Mahaweli System B and will affect 24,000 settler families. Project design will occur in 1987 with implementation beginning in 1988. Successful implementation of the ISM

project will also be an important part of the program. PL 480 Title I self-help measures Successful implementation of the ISM project will also be an important part of the program. PL 480 Title I self-help measures will increasingly play a role in integrating Mission DA efforts in policy dialogue as described in (5) below. Land tenure issues, irrigation policy and research priorities will be addressed through self-help measures that will support initiatives that cannot be comprehensively dealt with through individual projects.

5. Policy Agenda - The agricultural policy framework for Sri Lanka is generally very supportive to agricultural development. Free market pricing for both factors and products prevail. Research expenditure is a relatively low 0.8% of GDP against 2% recommended by the World Bank, and allocation of research resources is not fully consistent with the explicit GSL desire to support a transition to diversified farming. Many of the problem areas have been identified in the National Agriculture, Food & Nutrition Strategy. Appropriate steps are being taken to address them, many with USAID assistance, including diversified cropping research (DARP) and institutional coordination (AGPLAN). USAID attention during the planning period will focus on the following priority agricultural policy issues.

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- (a) Efficient uses of irrigation resources. USAID will encourage more effective use of the scarce water resources through (i) better management of irrigation systems, (ii) increased involvement of farmers in operations and maintenance, and (iii) greater O&M cost recovery from users. These issues are

being addressed specifically through both projects (MBD II, MDS, MARD, ISM) and Title I self-help measures. Some specific objectives for this policy goal are specified under 3(c) above. USAID believes that improved performance of the existing irrigation infrastructure is one of the most effective avenues for enhancing rural income growth. More efficient use of available water resources will result in more area planted and higher yields on existing lands. Additionally, the marginal cost of implementing these policies is quite low as the infrastructure is largely in place. The sustainability of irrigation investments is equally important through effective collection and allocation of user fees, and the integration of users into the decision-making process.

- (b) Allocation of agricultural research resources. Greater emphasis will be sought for non-rice food crop research through increasing the quantum of scientific staff working on crop diversification and improving inter-agency coordination of SFC research.

- (c) Land tenure policy. Fragmentation of small farms threatens to perpetuate subsistence agriculture by reducing farm size below the economic threshold. The transfer of full ownership rights to small farmers including rights to transfer ownership will allow the market to allocate land holdings. This issue is complex and will not be easily resolved, however, it has been consistently identified as vital to allowing agriculture to drive economic growth. PL 480 self-help measures are being used as tools to address this problem.

6. Problems and Constraints - Agricultural development faces numerous constraints. International protectionism and low commodity prices hamper the development of export opportunities for non-traditional agricultural export crops such as cereals. Concurrently, domestic demand for non-rice food crops is weak, limiting implementation of the diversification strategy.

Technical constraints abound. The highly variable rainfall creates great uncertainty, which is to some extent being alleviated by the development of irrigation systems. Additional productive land resources are very scarce and coupled with population pressures, results in very small farm units that are unable to adopt modern income generating technology. Soils are of only moderate productivity, and large extents of upland are unirrigable, severely limiting their production potential.

Institutional constraints relate largely to the fragmentation of responsibility for agriculture within the government. Numerous ministries and departments have agricultural functions along with many parastatals. Agricultural programs and projects are therefore narrowly based and uncoordinated. Additionally, the desire of the GSL to control government budget deficits will undoubtedly shrink the investment budget and has already resulted in a government hiring freeze. The budget problems will make it increasingly difficult to develop and implement projects. Donor coordination is lacking, which results in competition for GSL resources and overlapping and sometimes duplicative donor projects. The private sector is emerging to provide agricultural services but needs greater encouragement to become more active in supporting agriculture.

B. PRIVATE SECTOR ROLE IN DEVELOPMENT

1. Identify Goals - In the last Action Plan, the private sector as such was not identified as an area of focus. Activities dealing with the private sector were subsumed under the area of increased off-farm employment and rural enterprise. This year, we have separated development of the private sector out as a separate area of our program with the goal to increase the role of the private sector in the economy and to, conversely, decrease the role of the state. The achievement of this goal will be measured by both decreases in the proportion of GDP produced by the public sector vs. the private sector as well as absolute increases of the private sector's contribution to GDP. The analytical framework developed in the Arthur D. Little study of the private sector completed in 1983 will be used as the starting point for establishing updated figures and periodically measuring performance of the economy against the baseline.

2. Progress Toward Goals - A discussion follows of the progress made in the private sector as measured against the goals set out last year under the rubric of off-farm employment and rural enterprise:

a. Underemployment levels in the Mahaweli region reduced from 40% to 25% or less by 1991. While precise data is not available, several actions have been taken over the last year to mitigate the unemployment problem in the Mahaweli areas. With new AID financing under the Mahaweli Basin Development Project, Phase I, the EIED shows promise of becoming a viable entity to assist with employment creation in the Mahaweli (the establishment of small enterprise development units in the Mahaweli

systems, the creation of the Mahaweli Venture Capital Company (involving a grant from Appropriate Technology International), stimulation of private sector commercial farming, initiation of ornamental fish farming, etc.). Peace Corps volunteers are assisting with business development in the Mahaweli areas, the MASL is experimenting with different land tenure arrangements to allow for commercial activities and diversification, and the DARP project has been redirected to work directly in Mahaweli areas. In the agricultural sector which is the primary employer, the opening of new irrigation works and delivery of water to new settlers has provided these people employment.

b. Four hundred thousand jobs in the private sector created by 1990. In 1986, it is estimated that the private sector created about 70,000 jobs. The PEPP has, to date, been the primary, albeit limited, vehicle for AID's contribution to the achievement of this benchmark. Under the PEPP, a mix of about thirty new investments can be directly attributed to the project, including some foreign joint ventures, as well as small scale local market oriented investments.

c. Selective reversion of state-owned enterprises to the private sector. While government action still does not match its rhetoric, there have been promising initiatives in a number of important areas (enabling legislation, textiles, insurance, telecommunication) - and two recent national conferences in which the President participated should give new momentum to the process. A full USAID privatization strategy will be formalized in the PSDP project including the establishment of quantified targets. For the moment USAID has formed a private sector advisory group to advise on how USAID can most effectively proceed in the area of privatization. A preliminary data gathering activity on GSL state-owned enterprises has been undertaken, and we will develop a public

relations/education strategy. In addition, in the months ahead USAID will fund privatization studies for the Thripasha factory (with PRE help), the Fisheries Corporation (through SLBDC) and the seed industry (with the Dutch).

d. An industrial development policy for Sri Lanka established by 1987 giving priority attention to the private sector. The policy was presented to the Cabinet secretaries in February 1987. SLBDC participated in the development of this policy and will be a leading private sector organization on the Industrial Council which has been set up to implement the policy. The initial report of the industrial policy committee is very consistent with AID goals, calling for, among other things, market determined interest rates, privatization of state corporations, tariff reforms, and rationalization of the labor laws. We will closely monitor GSL implementation of this policy and assist in any appropriate ways.

3. Redefinition of Goals - We have redefined five intermediate objectives that will facilitate goal achievement:

a. To stimulate specific private enterprise undertakings.

* Additional 20 new private sector investments started through investor services (e.g., feasibility and market studies, technology/product development, buyer search, joint venture search, etc.), entrepreneur development programs (with a focus on rural areas), and credit/equity facilities (e.g., PL480 Title I Section 108 lending and investments in sub projects by an AID supported private venture capital company).

* Through EIED, 50 new small enterprises and 15 larger (agri-business or commercial farms) will be started in the Mahaweli areas in the next two years.

b. To stimulate the privatization of state owned enterprises.

* Specific privatization actions taken by the GSL through AID assisted studies and analyses, a possible fund to help finance privatizations and support for a GSL privatization/implementation unit (should it be established). Quantification of our goals will be developed during the PDSP design.

c. To strengthen the capital markets and enhance the availability of capital, both debt and equity, to meet the requirements of the private sector, and to facilitate privatization.

* Complete a review of Sri Lankan capital markets; in the process of designing PSDP, and determine a strategy to develop and improve them. Special attention will be directed to the embryonic stock market and the regulatory commission (SEC) now being established.

* Establish a venture capital company which will both expand the availability of equity for risk ventures and broaden the base of ownership.

* Complete a review of interest rates as they apply to the housing sector and seek ties to the similar study of term lending rates to industry being carried out by the World Bank.

d. Strengthened institutions that promote the private sector, with specific attention to the need for better coordination among the private sector institutions to increase their collective influence on national economic issues. The principal institutions are the private chambers of commerce and industry, private trade, manufacturing and exporter associations, the SLBDC and other private non-profit business promotion organizations, and government export and investment promotion organizations such as the EIED, EDB, FIAC, and GCEC. This might also include addressing the need to give more emphasis to business education in the school system, a collateral benefit being its contribution to the

improvement of English language usage. Specification of this goal will again take place during PSDP design.

4. Major Programmatic and Management Actions for FY 87-89

*The newly created Office of Private Sector Development will be staffed to manage the private sector portfolio and maintain momentum on the private sector program.

* Revisions will be made to the PEPP (restructuring the role of SLBDC, possible additional assistance to the IESC, etc.) based on the recent evaluation.

* Our initial support of the Mahaweli Authority of Sri Lanka's Employment, Investment and Enterprise Development activity (EIED) will be expanded to become the new Rural Enterprise Development Sector Project (REDS). The PID for this project will be submitted in June 1987 and a final project paper is expected to be approved by the Mission in mid FY 88. One option under consideration (if EIED is developing slowly or if investment opportunities in Mahaweli are limited by security concerns) is an incorporation of the REDS component within PSDP.

* Design of the Private Sector Development Program also calls for a PID to be completed by June 1987 and a PP to be completed by March 1988. This will be the principal vehicle for carrying out the intermediate objective noted above. The Mission will have to carefully review the current and prospective political climate for private sector development as part of the design process (see problems and constraints).

* The possibility of AID support in the form of a loan to a private sector Venture Capital Company with PRE support is being explored and if the decision is to proceed, we expect to have the activity underway in late 1987 or early 1988, possibly linked to the PSDP.

* A PL 480 Section 108 program was signed up in November 1986. We plan to execute a rupee loan agreement by mid 1987 with a local Intermediate Financial Institution. Assuming successful implementation of this first Section 108 activity, we plan to include Section 108 in future year Title I agreements.

* The Ministry of Health is interested in privatization of the Thripasha factory. An AID funded feasibility study will be completed in June 1987 and follow up activities will depend on the outcome of that report. Under a Title I self-help component, and with the help of DARP staff and the Dutch, we are also studying options for the privatization of the seed industry in Sri Lanka. A pilot activity will be underway in late 1987. We are also, through SLBDC, financing a feasibility study of privatization of the fisheries corporation.

5. Policy Agenda

Our own major policy agenda item continues to be to diminish the role of the state owned enterprises due to their large impact on the budget deficit. The recently released industrial development policy statement gives much attention to privatization and is very consistent with the types of ideas that AID is supporting in this field. We will, therefore, work with the GSL to implement many of the privatization recommendations made in this industrial development policy.

We will also be involved in the rationalization and enhancement of capital markets. For example, we are concerned with encouraging the government to charge market rates of interest for their housing loans. We have insisted on gradual increases in the rates charged under the HG loan and we will be undertaking a study this spring in conjunction with the

Ministries of Finance and Housing to assist in determining what an appropriate market rate would be. We are becoming more deeply involved in the network of facilities providing rural credit (HG loans and technical assistance through the thrift network; a prospective grant to CARE for entrepreneur credit to women through district co-op banks; and an analysis of agricultural credit constraints in MARD). Our work in developing a venture capital firm and in establishing a PL 480 Section 108 credit also involve us in these issues. Our principal involvement in capital markets will, however, flow from our design work under the PSDP project; one target area will be developing the breadth and depth of the nascent stock market, a pre-condition for any broadscale privatization. Enhancement of this facility is likely in turn to require a variety of statutory and regulatory changes.

In many ways, our cross-cutting themes (more fully developed in the CDSS update) constitute a "policy" agenda, i.e., cost recovery, increased use of market forces, and reductions in subsidies. We will be seeking opportunities not only to develop these motifs within the context of individual projects, but to draw from our collective experience with them in ways that may have broader implications.

6. Problems and Constraints - The CDSS Update identified a number of constraints to the development of the private sector. Two of these, the political situation and the security problems, bear special discussion.

The ruling UNP party will have to stand for election in 1989 with Presidential elections in November 1988 preceding Parliamentary elections sometime in 1989. As in any society, the status of the economy will be an important factor but, given Sri Lanka's historical radical swings between

parties which espouse opposite views on how to manage an economy, the status of the economy will be of crucial importance. In order not to alienate the large numbers of voters who are sympathetic to a more socialist orientation than has been pursued by the current government, it is possible that the UNP may not pursue efforts to enhance the role of the private sector, and particularly to diminish the role of the public sector, as strenuously as we might like. The combination of the struggle within the UNP to see who will succeed the current president, the fact that the next elections will be held on a proportional representation system which will make it more difficult for a single party to gain a two-thirds majority, and the uncertainty surrounding the future of the overarching issue of the ethnic problem, all make the outcome difficult to predict. An SLFP victory in 1989 may have serious ramifications on our private sector development program. However, it should be noted that the SLFP has been moving away from its dogmatic socialist line and is expected to have a more balanced economic policy should it come to power.

The continued ethnic problems are an obvious deterrent to private sector investment in Sri Lanka, both foreign and local. While a settlement would be necessary for investment to grow by any dramatic amount, we feel that our program can proceed under the present circumstances. We are attempting to establish an environment that will allow for further expansion in private sector development in the country. Should there be a peace settlement, our work will be made easier. Without a settlement, we still feel that much can be achieved in improving the environment for private sector development.

C. CONTINUING PROGRAMS

1. Identify Goals - In conformance with the strategy we are reducing our activities in sectors other than those clearly identified above. As noted in the Overview, due to funding and staff limitations, our objective in relation to the health, environment, and energy sectors is to complete the projects now underway and to phase out our participation concurrent with the completion of those projects.

2. Progress Toward Goals - We have begun the phase down and have not planned any new activities in these areas with the exception of a) the PVO project which serves one of our cross-cutting themes (described in the CDSS) and will be redirected to reinforce our principal goals and b) the ongoing HG program which is central to the achievement of several of our cross-cutting themes. The benchmarks given in the previous Action Plan were principally related to project implementation and have not been commented on here for that reason.

3. Redefinition of Goals - Our principal goal continues to be the phase out of our efforts in these sectors as projects currently underway are completed. We have, however, brought new prominence and attention to special components of these activities by highlighting their contribution to our cross-cutting themes. Our commitment to WID objectives remains strong and will continue to imbue our approach to all study and design objectives.

4. Major Programmatic & Management Actions - Over the next 18 months we will complete the Malaria Control (383-0043) and the Reforestation and Watershed Management (383-0058) projects as well as eliminate the second of our health officer USDH positions. We are still holding to our timetable for withdrawal from the Title II activity (also backstopped by our health officers), and we are hopeful that privatization of the Triposha facility will be possible. The Water Supply and Sanitation project has two years to run, but seems well on its way to achievement of its objectives and can be handled even with the departure this summer of our USDH environmental engineer. We will continue to address the project level policy issues necessary to successfully complete our current projects. We do not anticipate any problems with completing our phase out of these areas of project activity. We will continue to approve centrally or regionally funded programs which can a) have a significant impact relative to cost, b) require minimal staff involvement, and c) can significantly contribute to the leverage and access available for policy dialogue even though those activities may be outside the scope of our Mission strategy.

III. SPECIAL CONSIDERATIONS

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A. FINANCIAL ISSUES

1. Pipeline: At the end of December 1986, the Mission pipeline stood at \$76,846,000 (\$32,835,000 grant; \$44,011,000 loan). This represents 23% of accumulated obligations as of the end of CY 1986. A large portion of the pipeline is attributable to fully-funded new projects in the portfolio: Irrigation Systems Management (383-0080), Diversified Agriculture Research (383-0058), and Water Supply & Sanitation (383-0088). In addition, the FVO Co-financing (383-0060) project has expended slower than expected, and we plan to deob-reob any uncommitted funding from that project into a new FVO Co-financing II project (383-0101) during the summer of 1987. Finally, a large portion of the pipeline already has firm commitments which will be expended.

The remaining pipeline is from ongoing Mission projects. particularly the Mahaweli Phase I and Phase II projects. The pipeline on the Mahaweli projects will be reduced substantially during the remainder of FY 87 and the beginning of FY 88 as final claims are submitted and residual costs are settled. For other projects we expect substantial expenditures in the Malaria Control project (383-0043) and Reforestation & Watershed Management project (383-0055). In addition, the projects designed in late FY 86 - Irrigation Systems Management and Agricultural Planning and Analysis - should show significant expenditures as the first year start up phase of those projects ends. The pipeline also should decline over the next several years because of OYB levels decreasing below anticipated levels and a shift to major implementation actions as we move beyond the intensive FY 87 design period.

2. Mortgage: By the end of FY 88 the Mission's mortgage will be \$38.8 million or 216% of our expected obligation level (\$18.0 million) for the years beyond. The mortgage is held in the six new projects to be started in FYs 87/88. Mortgage will be a serious problem for the Mission. With the six new starts in FYs 87/88, there will be little opportunity for a new project in FY 89. A new project in that year will require that all ongoing projects be funded at minimum levels, a position we will want to review carefully in relation to the implementation status of those ongoing projects. While we think it important to get the Development of Agricultural Marketing Systems project (383-0093) started in FY 89, we do not want to end up "nickel and diming" the continuing portfolio. The deob-reob plans outlined below will reduce the mortgage amount and relieve some of the pressure on the FY 89 program level.

With or without a new project start in FY 89 the mortgage problem should ease that year. The new project would add \$12-14 million to the mortgage at a time when it will be decreased by \$15-16 million in obligations. Also, the unique situation which created the current high mortgage is not likely to be repeated soon. FY 87 began with only \$4.7 million in mortgage as all but one ongoing project had been fully funded. This situation together with the modifications in the program strategy necessitated several new project starts in FY 87 thus leading to the usually high mortgage. That problem was compounded by the decreased OYB levels.

3. Obligation Plans: (in \$ thousands)

ARDN Account	FY 87		FY 88		
	\$ Amount	Date of Oblig.	\$ Amount	Date of Oblig.	
383-0080	ISM	4,754	Feb.87	-	-
383-0085	DS&T	2,500	Apr.87	2,000	Dec.87
383-0086	MARD	4,000	Aug.87	3,000	Feb.88
383-0090	REDS	-	-	2,000	Apr.88
383-0100	PSDP	-	-	3,000	Jun.88
383-0101	FVO II	1,546	Jun.87	1,000	Dec.87
383-0103	MADS	5,200	Aug.87	7,000	Feb.88
TOTALS		18,000		18,000	

4. Debt-Recb Actions for FY 87 (in \$ thousands)

PROJECT NO	PROJECT TITLE	FUND ACCT	DECB. PLANS		RECB. PLANS	
			LOAN	GRANT	LOAN	GRANT
383-0043	Malaria Control Vector Biology & Control (Centrally Funded)	HE	-	450	-	-
383-0057	Water Management	FN	1,133	295	-	-
383-0055	Reforestation	FN	1,000	-	-	-
383-0086	MARD	FN	-	-	1,133	295
383-0103	MADS	FN	-	-	1,000	-
383-0060	FVO Co-Finance	FN	-	750	-	-
		HE	-	630	-	-
		SD	-	500	-	-
383-0101	FVO Co-Finance II	FN	-	-	-	750
		HE	-	-	-	630
		SD	-	-	-	500
TOTALS			2,133	2,625	2,133	2,625

III.B. Evaluation Plan (USAID/Sri Lanka)

1. Evaluation Schedule

Date	Project & Number	Type/Purpose of Eval	Funding	Last Eval
FY 1986/7 (Completed) *****				
Oct 1985	Rice Research Project 383-0040	Post-FACD Impact Evaluation	central	
Nov 1985	Mahaweli Environment 383-0075	Mid-term	project	
Mar 1986	Malaria Control 383-0043	Mid-term	project	
June 1986	PVO Co-Financing I * 383-0060	Second Mid-term	project	1983
Nov 1986	Private Enterprise Promotion * (PEPP) 383-0082	Mid-term	project	none
Planned FY 1987 *****				
Mar 1987	Mahaweli Environment 383-0075	Review of CY1986 project implementation progress	project	12/85
April 1987	National Institutes of Health Science (NIHS), 363-0062	End of Project	project	10/83
April 1987	Housing Guarantee Program * 383-HG-002 & 003	Final for Phase II Mid-term for Phase III	PD&S	
May 1987	Centrally Funded Population * Activities	A sector review to recommend priorities after completion of direct Mission funding in Health & pop.	central	none
May 1987	Agriculture Education Development (AED) 383-0049	End of Project	PD&S	10/82
June 1987	Diversified Agricult Research (DARP) 383-0058	First mid-term	project	none
Planned FY 1988*****				
Oct. 1987	Water Supply & Sanitation 383-0088	Mid-project evaluation	project	none
Nov 1987	Malaria Control 383-0043	End of Project	project	3/86
April 1988	Irrigation Management Sector * Review	An overall evaluation of Mission activities in irrigation management.	PD&S	none
July 88	Reforest Watershed Management	End of Project evaluation	PD&S	12/84
Aug 1988	Mahaweli Basin Phase I * EIED Amendment 383-0056	End of Activity	project	none
July 1988	Private Enterprise Promotion *	End of Project	project	11/86
Planned FY 1989 *****				
February 1989	Diversified Agriculture Sector * Review -or-	An evaluation of Mission/GSL activities and strategies for building diversified agriculture, including DARP, MARD, AGPLAN, REDS.	PDS	n.a
June 1989	Diversified Ag. Research	Second mid-project	project	12/84
March 1989	Irrigation Systems Management *	First mid-project evaluation	project	none
June 89	PVO Co-Financing I & II	End of Project for Co-Fi I and initial review of Co-Fi II	project	6/86 none
Planned FY 1990*****				
October 1989	MARD/MDS	First mid-term	project	none
Jan 1990	Agriculture Planning & Analysis	First Mid-term	project	none

2. Evaluation Prior to Project Design - Prior evaluations are being incorporated in varying degrees in designing all four new FY 87 projects. For two projects, the impact of evaluations has been particularly important. The design of the Mahaweli Downstream Support (383-0103) project underwent considerable development in part based on the discussion of the earlier Mahaweli Sector Support Loan (383-0078) in the 1985 tripartite Mahaweli evaluation. The schedule for designing a follow-on PVO Co-Financing II (383-0101) project was accelerated and several experimental elements incorporated (such as the use of an intermediary organization to fund "micro-grants" to small local organizations) based on the June 1986 evaluation of PVO Co-Financing (383-0060). The designs of the Mahaweli Agriculture and Rural Development Project (383-0086) and the Development Studies and Training (383-0085) are also grounded in observations of the Mahaweli tripartite evaluation and the 1984 evaluation of the earlier Development Studies and Training (383-0044) project.

Several FY 87 evaluations are expected to contribute substantially to future project design. Since the Private Enterprise Promotion (383-0082) project is the Mission's first project focused on private sector development, the just-completed mid-term evaluation of that project will contribute to the designs of both the Rural Enterprise Development (383-0090) project and the Private Sector Development Program (383-0010). The evaluation of the Housing Guaranty Program Phases II & III will feed into the design of the next phase, and the population sector evaluation will contribute to Mission decisions on future centrally funded project proposals in that sector.

The Mission's longer range evaluation plan includes broad evaluations of important sectors in the Mission portfolio (irrigation management and diversified agriculture). These are intended to reassess overall Mission (and GSL) strategy in those sectors and will affect the focus of future projects.

The Mission will continue to view evaluations as means to point out lessons learned for future project development. Those evaluations which have or will contribute to project design have been marked with an asterick (*) on the table III.B.1 above.

3. Identification of Major Evaluation Findings - Four major evaluations were completed during FY 86. Though several had important project-level implications, none raised serious questions concerning CDSS objectives or assumptions.

The evaluation of the Mahaweli Environment Project (383-0075) identified a number of critical implementation steps to be taken in 1986 to reverse the initial poor performance of the project; extension of the project would be contingent on taking those steps. The PVO Co-Financing (383-0060) evaluation endorsed the basic structure of the project, but suggested that mechanisms be developed to broaden the range of PVOs supported and improve PVO design and management skills.

The Malaria Control (383-0043) evaluation recommended planning and implementing a regional trial/demonstration integrated malaria control program as a practical step toward adoption of vector control methods. Hambantota District is now being established as the trial district.

C. PL 480

1. Title I

a. Relationship to Mission Strategy - PL 480 has been a cornerstone of our assistance package to Sri Lanka over the years. When other forms of assistance ceased in the 1970's, the PL 480 program carried on. The basic economic justifications for Title I remain: the need for wheat imports (Sri Lanka produces rice but no wheat); the need for budgetary support; and a poor balance of payments position. With weak tea prices, declining numbers of workers in the Middle East and a difficult tourist situation, the balance of payments outlook is not bright. With a budget deficit ratio of 18% of GDP, the budgetary assistance provided by Title I is eagerly sought after by the GSL. The decline in the Development Assistance levels for Sri Lanka, has made Title I a focus of Mission assistance to the country. The self-help measures are seen as policy dialogue tools and have been carefully designed to complement the activities being carried out under the DA portion of our program (see (d) below) and the local currency generations directly support USAID priority sectors. The continual cuts in our Title I dollar levels have the affect of decreasing the effectiveness of our self-help policy leverage.

b. Country Food Situation - Islandwide, rice provides about 50% of all calories consumed by Sri Lankans while bread and wheat flour together account for 9 to 10%. Bread provides 12% of the calories consumed by the urban sector while wheat flour is a large part of the estate sector's diet accounting for 14% of calories there.

Sri Lanka's food situation revolves around its supply of rice. The increase in paddy production at a rate of 6.2% per year since the change in government in 1977 is attributable to an increase in the acreage under cultivation and increases in yields, with both related to the availability of new technologies and a freeing up of the rice marketing system. Rice production has progressed to the point that the country's ability to achieve self-sufficiency in rice now depends largely on the adequacy of rainfall in any given year. It is expected, given the extremely erratic and unstable nature of the island's rainfall pattern, that setbacks in agricultural production will continue (albeit not over as great a range) to occur about once in three years.

Following negligible imports of rice in 1984, the GSL imported 183,000 MT (6% of total supply) in 1985 in order to build up stocks. Poor weather and the impact of the ethnic disturbances on production in the North and East, led to imports of 230,000 MT in 1986, or 11.5% of total supply. Owing to inadequate monsoon rains, rice production this season (Maha 1986-87) is predicted to fall by at least 10 to 20%, thus leading to higher imports.

c. Present Food Policy - The GSL's agricultural policies related to the food sector are sound and continue to be determined by free market mechanisms. Free market producer prices (coupled with underlying price supports) and unrestricted availability of agricultural inputs provide adequate production incentives. Although irrigation development is still a major priority, the GSL is conscious of the need to encourage agricultural production through increased farm productivity, better utilization of existing resources, higher cropping intensities and

diversification. As such, its current policies reflect an increasing focus on water management, agricultural research and diversification, active participation of farmer organizations in agricultural development and management of irrigation water delivery systems, and improved agricultural practices. However, we still foresee the need for some policy changes, particularly in the areas of cost recovery/reduced subsidization (water and fertilizer) and land tenure.

d. Reforms to be Supported with the Program - The Title I self-help measures are designed to support our strategic objectives and compliment our DA program. Due to the critical need for the food resource and the annual nature of the commitment, we have found that the Title I program is the preferred tool for leveraging continued progress of essential reforms. Our three FY 87 measures deal with improving the system of processing and issuing land titles, testing two alternative land alienation models in the Mahaweli areas and developing a national agricultural research plan to set priorities for agricultural research. A topic under consideration for the amendment to the FY 87 agreement is the testing of alternative institutional organizers for water management groups.

One of the self-help measures that was adopted under the amendment to the FY 86 program augments the Mission's privatization efforts and includes activities designed to restructure the seed industry so as to increase the involvement of the private sector. The second measure provides for the establishment of a Council for Agricultural Research Policy, a measure recommended by the National Agricultural Food and Nutrition Strategy (the subject of previous self-help measures).

FY 86 self-help measures that are still active include the development of a much needed agricultural diversification plan to guide diversification activities and the completion of the study to determine the cost per acre of maintaining of irrigation systems land under various irrigation schemes. This data will be used in future discussions on irrigation user charges, cost recovery and subsidy reduction.

We expect future self-help measures to be continuations of our current areas of concern with each year's measures building upon the actions which preceded them. Irrigation management and land alienation in particular are two areas which we foresee the use of Title I to assist in evolving long-term strategies.

e. Uses of the Proposed Commodities - The entire Sri Lankan program is made up of wheat imports. The wheat is milled locally and sold by the government through both government stores and private traders. The commodities are not targeted in any way. If the world price of wheat remains low, we may in the future look to other possible commodities for the Title I program.

f. Local Currency Use - The local currency generated (less a 5% CUP) is deposited in the treasury and is used for development activities agreed to by the Mission. The FY 87 agreement calls for the funds to be spent on activities which directly support USAID priorities: irrigation and water management; agricultural planning, research, and diversification; conservation and reforestation. The Mission has not adopted a policy of jointly programming the local currency resources because the GSL has

demonstrated that PL-480 generations are used properly for development and our DA projects have received required budgetary support. With the major budget squeeze, we will carefully monitor budget allocations and use the potential for joint programming to leverage adequate host country contributions to our DA projects. The Mission has been one of the first countries in the world to initiate a new Section 108 program with 10% of the FY 87 allotment. These funds will be used as an integral part of our strategic objective in support of the private sector.

g. Status of Storage and Distribution - There are no storage or distribution issues relating to the Sri Lanka program. Adequate storage is provided at the Prima Mill in Trincomalee and by the Food Department.

h. Disincentive Issue - The Mission has thoroughly dealt with the disincentive issue in the past, most recently in 86 Colombo 1398 regarding disincentives to rice production and in a paper prepared by our agricultural staff, sent to AID/W in October 1986, which deals with the disincentives to other crops. The Mission is confident that the data shows that there is no disincentive issue in Sri Lanka.

i. Other Issues - Sri Lanka has been active in the USDA sponsored Export Enhancement Program which has allowed the country to commercially purchase wheat at a price as low as \$82 CIF per ton. While an analysis of the subsidy element of the Title I loans demonstrates that Title I is a cheaper source of wheat, the government's enthusiasm for the EEP continues unabated.

2. Title II

Since 1973 the Ministry of Health (MOH) of the Government of Sri Lanka (GSL) and CARE/Sri Lanka, in cooperation with the United States Agency for International Development (AID), have manufactured and distributed Thriposha (a high protein cereal based product) to nutritionally at risk infants, pre-school children and pregnant and lactating women throughout Sri Lanka free of charge. The Thriposha feeding project has grown from initially serving 75,000 beneficiaries in 1973 to a current beneficiary level of 580,000 beneficiaries targeted to receive 1,500 grams of Thriposha monthly.

Given AID's efforts to projectize Title II activities and obtain GSL support to sustain this 14 year old activity, the Mission has sought, and finally obtained, the government's agreement to a phase-over program. (Our interest in so doing has been compounded by the loss of the two USDH health officers who have managed this controversial program).

Since 1980, CARE and the MOH, with USAID support, have also sought to gradually increase the proportion of indigenous commodities (principally corn and soya) used in the production of Thriposha, while reducing the imported component. Over the years, there have been a number of different formulations. Based on recent analyses by the Department of Agriculture and S&T experts, current plans call for the Thriposha formula to consist, by 1989, of 85% indigenous commodities and 15% imported commodities, the import component consisting entirely of non-fat dry milk (NFDM). AID plans to cover the cost of the imported NFDM through 1991, after which all commodities are to be financed by the GSL.

To assist the MOH to prepare for the phase-out of PL 480 commodities and consistent with USAID's strategy to encourage and stimulate private sector development, USAID has proposed to the MOH that a feasibility study be undertaken to detail the options for future management and ownership of the Thriposha food processing complex, including two basic options, namely: (1) continued ownership by the GSL with an incentive-based contract to a private company to manage the factory; or (2) lease and or sale of the factory to a private company coupled with a GSL agreement to purchase the quantity of Thriposha necessary for the MOH Thriposha program. It is anticipated that this study, funded by AID, will also provide data to the MOH and the Ministry of Finance outlining the cost of implementing a free food supplement program in the absence of donated PL 480 Title II commodities and the administrative/managerial services currently provided by CARE.

As the GSL moves ahead with the plan to increase the cooking capacity of the Thriposha factory (CARE and AID will release blocked funds to aid in this expansion) to accommodate the planned proportion of 15% NFDM 85% local corn and soya milk, CARE and USAID will continue to request technical assistance on behalf of the GSL.

If the drought situation persists in the country and if the crop failure is more severe than predicted, it is possible that we may have a drought relief program in the near future.

If the ethnic crisis is resolved, USAID and CARE are prepared to consider using the Title II program to assist in the peace process. Such

a program might consist of a food for work program to aid in the repair of schools, clinics, roads, houses, etc., which have been destroyed during the hostilities. The Mission would also consider a traditional MCH on site feeding program which could have health education, nutrition and oral rehydration components. This would be a new program, limited to the North and East for a specific time period. No attempt will be made to alter the phase-down schedule or increase the level and mix of commodities of the Thripasha program.

The Mission is prepared, in principal, to seek the additional resource that might be available through excess U.S. food. However, except for possible drought relief, we do not propose a Section 416 or Section 206 program for the remainder of FY 87 or FY 88 since it would conflict with our current efforts to insure the GSL's commitment to phase out the current Title II program. Moreover, the loss of our two Americans who have worked on this program would make such undertakings extremely difficult to manage.

We have, however, seriously looked at the possibilities of sponsoring a new national effort under the Title II for Structural Adjustment program. Sri Lanka is currently negotiating a structural adjustment facility with the IMF and World Bank; the measures to be taken by the GSL will be undoubtedly further exacerbate growth, employment, income and nutritional levels that are already in retreat, especially among the poor. Our objective would be to make imported commodities available through the public distribution system which is also the vehicle for a food-stamp program targeting basic foodstuffs to the poor. Our policy objective would be to insure an adjustment of that latter program so that

it simultaneously increases the value of stamps to the genuinely poor, eliminates some middle-income recipients, and avoids increases in the overall subsidy level. We recognize that policy negotiations on revising the food stamp scheme would be difficult. In addition, we have not been able to identify a commodity which is both needed and would meet UMR considerations. Further, a short-term Title II for Structural Adjustment program would create demands on the government that they would be unlikely to be able to fulfill from their own resources - either monetary or from increased domestic production - when our program stopped. With the elections coming in 1989, the government would seriously resist withdrawal of a Title II for Structural Adjustment program as they go for reelection.

D. MANAGEMENT AND WORKFORCE ISSUES

1. Overview of Mission Staffing FY 87-89

a. USDH - The Mission workforce FTE level for FY 87 and FY 88 is 19 USDH employees and that level will be reached by the elimination of three additional positions by the end of FY 87. One of three engineer positions, the health/population development officer and the regional legal advisor positions will be deleted in this process. The closing out of the \$120 million Mahaweli construction project permits the Mission to release the engineer's position and the resident regional legal advisor position, although we will continue to require RLA services of 3-4 weeks per quarter. Focussing the strategy on non health projects after the end of malaria control permits the disestablishment of the Health Office. One project development officer position was transferred to the newly established Private Sector Development Office and the budget and accounts officer position was eliminated to provide an office of two USDH

positions, private enterprise development officers. USAID's rural development IDI has been placed into a program officer position as the evaluation officer and rural development advisor to all offices of the Mission. These changes will be reflected in the reorganization documentation now under preparation by USAID.

The Mission considers the level of 19 positions to be critical to accomplishment of the objectives laid out in the action plan and CDSS update. Staffing levels have already been severely cut from 25 in 1985 to 19 in 1987. Any reductions below that level will reduce our effectiveness in managing the portfolio and continuing the policy dialogue.

The Mission is dependent upon services of regional officers for commodity procurement and contracting assistance. In FY 88 we will also depend on regional services for environmental actions and for legal services after the transfer of the RLA. While service of the regional commodity officer has been excellent, lack of a contract officer services has been a major constraint over the past year.

The transfer of the RLA poses a special issue because it is likely not to be completed prior to the end of FY 87. We request that AID/W provide one over ceiling position to carry the RLA until an appropriate location can be arranged.

b. OE-FUNDED U.S. PSCs - The locally recruited U.S. PSC administrative assistant in the Executive Office is being continued.

c. FSN PSCs - USAID is currently recruiting two program specialists and two secretaries to work in the Private Sector Development Office. A chief accountant and an accounting technician are being recruited to enhance the efforts of our Controller in maintaining that office and the MACS system. It is intended that a local engineer be hired to fill the vacancy created when the USDH engineer departs. It is also intended that ~~a part-time locally available librarian~~ be hired, possibly from dependent rolls, to establish a much needed USAID Library. The Mission, of necessity, will utilize PSCs to an ever greater extent as needs dictate. We anticipate 54 FSN PSCs on board at the end of FY 87.

d. PROGRAM FUNDED STAFF - USAID is recruiting one long-term U.S. staff through a buy-in to an S&T project to assist in the design of two new projects in the Private Development Office.

e. FSN Ceiling - The ceiling for USAID FSNs has been established at 24 positions for FY 87 and 22 positions for FY 88. When the Mission replaces our commodity procurement specialist, we will actually have only 21 FSNs on board. There is no trouble anticipated therefore in achieving the established ceilings.

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f. PASAs, JCCs and TCNs - There are no PASAs, JCCs or TCNs employed by USAID Sri Lanka.

2. Detailed Workforce Tables FY 87-89FY 87, 88, AND 89 WORK FORCE

<u>OFFICE & POSITION</u>	<u>USDH</u>			<u>FSN</u>			<u>FSNPSC</u>			<u>USPSC</u>		
	<u>87</u>	<u>88</u>	<u>89</u>	<u>87</u>	<u>88</u>	<u>89</u>	<u>87</u>	<u>88</u>	<u>89</u>	<u>87</u>	<u>88</u>	<u>89</u>
<u>OFFICE OF THE DIRECTOR</u>												
Mission Director	X	X	X									
Deputy Mission Director	X	X	X									
Secretary	X	X	X									
Secretary				X	X	X						
Program Specialist (Pol)				X	X	X						
Sub Total:	3	3	3	2	2	2						
<u>OFFICE OF REGIONAL LEGAL ADVISER</u>												
Regional Legal Adviser	X											
Secretary								X				
Sub Total:	1							1				
<u>EXECUTIVE OFFICE</u>												
Executive Officer	X	X	X									
Executive Assistant										X	X	X
Financial Assistant				X	X	X						
Systems Manager							X	X	X			
Secretary							X	X	X			
<u>Personnel Unit</u>												
Personnel Assistant				X	X	X						
Roving Secretary							X	X	X			
Telephone Operator							X	X	X			
Telephone Operator							X	X	X			
Receptionist/Guard							X	X	X			
Janitor							X	X	X			
Janitor							X	X	X			
<u>Communications & Records Unit</u>												
Communications Supervisor				X	X	X						
Mail & File Clerk							X	X	X			
Mail & File Clerk							X	X	X			
Duplicating Equip Operator							X	X	X			
Messenger							X	X	X			
<u>Operations Unit</u>												
Operations Manager							X	X	X			
Motor Pool Dispatcher							X	X	X			
Chauffeur				X	X	X						
Chauffeur							X	X	X			
Chauffeur							X	X	X			

Chauffeur							X	X	X			
Chauffeur							X	X	X			
Chauffeur							X	X	X			
Chauffeur							X	X	X			
Chauffeur							X	X	X			
Chauffeur							X	X	X			
Sub Total:	1	1	1	4	4	4	22	22	22	1	1	1
<u>OFFICE & POSITION</u>	<u>USDH</u>			<u>FSN</u>			<u>FSNPSC</u>			<u>USPSC</u>		
	87	88	89	87	88	89	87	88	89	87	88	89

PROGRAM OFFICEPlanning Division

Program Officer	X	X	X									
Rural Dev Officer	X	X	X									
Secretary				X	X	X						
Reports Officer							X	X	X			
<u>Economics Division</u>												
Program Economist	X	X	X									
Program Specialist (Econ)				X	X	X						
Secretary							X	X	X			
<u>Private Voluntary Org. Division</u>												
Program Specialist (PVO)				X	X	X						
Sub Total:	3	3	3	3	3	3	2	2	2			

CONTROLLER'S OFFICE

Controller	X	X	X									
Secretary							X	X	X			
Chief Accountant				X	X	X						
Secretary							X	X	X			
<u>Accounting Division</u>												
Senior Accountant				X	X	X						
Project Accountant				X	X	X						
Accountant/Budget Analyst				X	X	X						
Accountant/Data Controller				X	X	X						
Accounting Technician							X	X	X			
<u>Financial Analyst</u>												
Financial Analyst				X	X	X						
<u>Voucher Examining Division</u>												
Supervisory Voucher Examiner							X	X	X			
Voucher Examiner							X	X	X			
Voucher Examiner							X	X	X			
Voucher Examiner							X	X	X			
Sub Total:	1	1	1	6	6	6	7	7	7			

<u>Water Management Division</u>																																				
Engineering Officer	X	X	X																																	
Secretary							X	X	X																											
Engineer							X	X	X																											
<u>Environment, Water Supply & Sanitation Division</u>																																				
Engineering Officer	X																																			
Engineer						X																														
Engineer							X																													
Secretary							X	X	X																											
Sub Total:	3	2	2	1			7	6	6																											
<u>HOUSING DEVELOPMENT OFFICE</u>																																				
Housing Adviser	X	X	X																																	
Secretary							X	X	X																											
Sub Total:	1	1	1				1	1	1																											
<table border="0" style="width: 100%; text-align: center;"> <thead> <tr> <th rowspan="2"><u>OFFICE & POSITION</u></th> <th colspan="3"><u>USDH</u></th> <th colspan="3"><u>FSN</u></th> <th colspan="3"><u>FSNPSC</u></th> <th colspan="3"><u>USPSC</u></th> </tr> <tr> <th>87</th> <th>88</th> <th>89</th> <th>87</th> <th>88</th> <th>89</th> <th>87</th> <th>88</th> <th>89</th> <th>87</th> <th>88</th> <th>89</th> </tr> </thead> </table>												<u>OFFICE & POSITION</u>	<u>USDH</u>			<u>FSN</u>			<u>FSNPSC</u>			<u>USPSC</u>			87	88	89	87	88	89	87	88	89	87	88	89
<u>OFFICE & POSITION</u>	<u>USDH</u>			<u>FSN</u>			<u>FSNPSC</u>			<u>USPSC</u>																										
	87	88	89	87	88	89	87	88	89	87	88	89																								
<u>HEALTH, POPULATION & HUMAN RESOURCES</u>																																				
Health/Population Dev Officer	X																																			
Secretary								X																												
Program Specialist					X																															
Sub Total:	1				1			1																												
GRAND TOTALS:	23	20	19	22	21	21	54	53	53	1	1	1																								

3. Other Management Issues

a. Reorganization: A mission reorganization has been prepared which restructures the mission to reflect the new strategy directions. In recognition of the change in the nature of the Mahaweli activities from a construction emphasis to development, the former Mahaweli and Water Resource Development Office has become the Office of Engineering and Water Resources. The new Mahaweli development projects will be managed from the line office dealing with that aspect of development (i.e., the agriculture project from the agriculture office, the private enterprise project from the private sector

office and the construction project from the engineering office). Abolishment of several USDH positions to accommodate the reduction of ceiling from 26 to 19 has necessitated transferring of functions within the mission. Population and residual health activities have been the responsibility of an FSN doctor who will be located in the Project Office. The management of Title II activities has been transferred to the Agriculture Office and a decision will need be made on environment affairs transferred to the Project Office. In addition, positions have been transferred internally to permit the establishment of a Private Sector Office which will manage the specific private sector activities, provide a consistent interface with the Sri Lankan private sector, and develop the policy dialogue in this newly emphasized area. We believe that this reorganization places us in the optimum position to implement the strategy we are proposing.

b. Coordination with other USG Agencies: The mission has initiated several cooperative efforts with USIS. We are collaborating on a pamphlet illustrating economic assistance over the past 30 years in Sri Lanka and describing our current programs here. The Mission and USIS are planning joint financing of a group of development oriented parliamentarians in the coming year. Finally, we coordinate closely in press relations with a joint press conference in recognition of the 25th anniversary of AID and the surpassing of the \$1 billion mark in US economic assistance to Sri Lanka as well as more routine joint press statements on the occasion of obligation of additional funds for project and programs.

The mission has recently opened a dialogue with the Peace Corps regarding enhanced cooperation between Peace Corps and AID to implement both the Small Program Assistance project and parallel projects which will be mutually

reinforcing. The Memorandum of Understanding for the SPA project will be signed during the coming months with the mission also helping at a workshop to help volunteers identify good projects and develop good proposals for the SPA project. In the coming year, plans for parallel AID/Peace Corps programming will be further explored with the expectation that by 1989 we will have at least one coordinated activity underway.

c. Procedures: As a result of the mission management assessment in October, 1986, the mission has initiated a program to completely revise all mission orders and to develop a project officer's handbook tailored to our situation. We have also strengthened our funds control procedures to assure prompt payment with appropriate reviews and strengthen requirements for certification of funds availability. Finally, the Project Implementation Review has been intensified with increased emphasis on project outputs and financial performance, both USAID funds and the Host Country contribution.

d. Buildings: USAID will continue to reside in the former U.S. Embassy compound located at 44 Galle Road, Colombo 3. A significant amount of repair and maintenance work is required to raise the safety conditions to a satisfactory level. The work includes rewiring the rear USAID building and replacing its roof. It also entails removing asbestos ceilings, repairing termite damage, and replacing the air-conditioning system in the front building. The American Embassy and Federal Buildings Office (FBO) have begun architect and engineering work but progress is slow. This work is prerequisite to the security work discussed below.

e. Security: The first phase of the security enhancement program (the front perimeter pedestrian and vehicular compound access plan) is near

completion, however, USAID has not received funding for the remaining three phases (phase 2: front public access control; phase 3: rear public access control; and phase 4: rear perimeter fencing and guard post). This plan was envisaged three years ago and it is imperative that pressure be brought to bear to complete it at the earliest possible date. As previously stated, it must be accomplished in conjunction with maintenance and repair work, and our objective is to minimize disruption while completing the jobs in the shortest possible time.

f. Budget Availabilities: The significant reduction in USDH staff levels has permitted us to stay within our OE budget allowances despite the need for major furniture and appliance replacements and residential upgrading. The Embassy, however, has not been as fortunate and Gramm-Rudman constraints have led them to reduce administrative services, including FAAS services.

g. Automation: The MACs system has recently been brought on line and duplicate manual book-keeping will soon cease. We have initiated training courses for mission staff and management in utilization of MACs reports. We are currently conducting a survey to determine the best approach to integrate our numerous PCs into a single system without overburdening our OE budget.

E. GRAY AMENDMENT

1. Progress Indicators:

USAID signed thirteen direct contracts in FY 86. Seven of the thirteen signed were with Gray Amendment (GA) firms and represented 39% of the \$151,470 in funds contracted by the Mission.

Three host country contracts under AID financing were signed during the same period. Two were with a minority controlled PVO for procurement services. These two contracts represent 15% of the \$258,059 in funds committed in host country contracts this year.

In addition, the Mission has been successful in contracting with Gray Amendment firms for pre-design, assessments and evaluations. As mentioned in last year's Action Plan, the Mission has attempted to better control the contracting process by either utilizing existing minority IQCs or "buying into" centrally managed contracts. As a consequence, of the \$803,878 in Mission funds contracted through Work Orders and buy-ins, 45% of the funds went to Gray Amendment firms in seven of the eleven contract actions. This meant that last year's Action Plan benchmark for project evaluations was exceeded as three of the four evaluations and 71% of total person months went to minority firms.

One U.S. minority subcontract under an existing host country contract will expire this fiscal year. However, the large T.A. contract with an 8(A) firm, under the Malaria Control Project, will probably be extended by seven months into mid-FY 88.

2. FY 87 - 88 Benchmarks:

Over the period of FY 87/88, the Mission plans to contract for thirteen project evaluations; to complete six project designs; and, contract for the provision of technical assistance, training, and procurement services for five projects.

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A. Evaluation: The Mission expects to contract approximately three project evaluations with Gray Amendment firms.

B. Design: Because of current commitments on planned design actions on FY 87 projects, is it possible that at least one project design will go to a GA firm.

C. Technical Assistance: If current contract negotiations are successful, the technical assistance under the Irrigation Systems Management Project will be a direct-AID contract with a minority U.S. firm recently graduated from 8(A) status.

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F.

SUMMARY BUDGET TABLE
(\$000's)

PROJECT NO	PROJECT TITLE	FY 87		FY 88		FY 89	
		LOAN	GRANT	LOAN	GRANT	LOAN	GRANT
FN							
383-0080	Irrigation Systems Mgt	3,654	1,100	—	—	—	—
383-0085	Development Studies & Trg.	—	1,500	—	1,050	—	450
383-0086	Mahaweli Ag. & Rural Dev.	2,000	2,000	1,000	1,200	800	500
383-0090	Rural Enterprise Dev Sector	—	—	1,500	1,500	1,630	1,500
383-0093	Development of Agr. Marketing Systems	—	—	—	—	2,000	400
383-0101	EVO Co-Financing II	—	1,546	—	—	—	1,000
383-0103	Mahaweli Downstream Support	4,500	700	4,290	1,000	4,210	300
	Sub Totals	10,154	6,846	6,790	4,750	8,640	4,150
SD							
383-0085	Development Studies & Trg.	—	1,000	—	1,250	—	500
383-0100	Private Sector Dev. Program	—	—	2,000	1,500	2,500	500
383-0101	EVO Co-Financing II	—	—	—	500	—	500
	Sub Totals	—	1,000	2,000	3,250	2,500	1,500
	Country Totals	10,154	7,846	8,790	8,000	11,140	5,650
	TOTAL OMB		18,000		16,790		16,790

New Project Description

1. Project Title and Number: Rural Enterprise Development Sector
(383-0090)

2. AID Funding (\$000)

	<u>FY 1988 Funding</u>	<u>FY 1989 Funding</u>	<u>LOP Funding</u>	<u>Appropriation Account</u>
Total	3,000	3,130	15,000	ARDN
Grant	1,500	1,500	10,000	
Loan	1,500	1,630	5,000	

3. Project Purpose: The purpose of the project is to increase rural employment and raise net farm and off-farm incomes. The project will be carried out in the special irrigation and resettlement areas under the Mahaweli Authority of Sri Lanka and will serve as a testing ground for rural enterprise development strategies applicable throughout the country.

4. Description of the Project: The project will promote the development of a variety of private sector rural enterprises providing goods and services to the Mahaweli settler community and marketing and processing agricultural products from the Mahaweli farms. It will address such constraints to investment in Mahaweli-based enterprises as the inadequate dissemination of accurate price and market information, government policies affecting markets and prices, availability of credit/equity finance for investment projects, and investor concern about risk and feasibility in untried and unfamiliar Mahaweli areas.

Pilot projects for product development/test marketing of promising crops and investment feasibility studies will be supported on a cost-shared basis. At the national level, the institutional capacity will be developed within the Mahaweli Authority of Sri Lanka (MASL) to design and implement comprehensive sets of policies, incentives and programs to promote private sector investment. The lack of established demand (or accessible markets) in the newly settled Mahaweli areas for subsidiary field crops, agro-forestry products, and livestock products will be addressed by the stimulation of medium to larger scale agro-processing industries and trading enterprises creating links to the larger national and international economy.

The project will also have a component addressing the promotion of small-scale enterprises in the Mahaweli areas, building on the already initiated Small Enterprise Development Unit model designed by the MASL's Employment, Investment and Enterprise Development Division (EIED).

The EIED will be the principal implementing agency for the project. In FY 87, the Mission amended the existing Mahaweli Asian Development Phase I Project (383-0056) to provide \$1.8 million in "bridge financing" to the EIED prior to the anticipated start the REDS project in FY 88.

- 5. Relationship of Mission Strategy: The project will directly address the strategy objectives of increased private sector development and increasing rural incomes.
- 6. Target Group: Off-farm and farm settler households in five Mahaweli Special Areas, (System B Left Bank, System C, System G, System H, and Uda Walawe) and private investors in Mahaweli areas.
- 7. PID Approval: The PID will be submitted to AID/W for review in July 1987.
- 8. Special Concerns: Private sector development.

New Project Description

1. Project Title and Number: Private Sector Development Program
(383-0100)

2. AID Funding:

	<u>FY 1988 Funding</u>	<u>FY 1989 Funding</u>	<u>LOP Funding</u>	<u>Appropriation Account</u>
Total	3,500	3,000	15,000	SDA
Grant	1,500	500	5,000	
Loan	2,000	2,500	10,000	

3. Project Purpose: To assist the GSL in privatizing state-owned enterprises and developing the private sector(SOEs).

4. Problems to be Addressed: When the current government came to power in Sri Lanka in 1977, it liberalized the economy and made the creation of jobs its central focus. While the GSL has made significant progress in these areas, over 30 percent of Sri Lanka's GDP is still created by the state sector. SOEs have received subsidies on the order of \$1.5 billion since 1977, about the same as the cost of the entire Mahaweli program thus far. There is a growing consensus within the GSL that government should get out of businesses that could be better run by the private sector, and that a carefully planned program of privatization should be implemented.

Other problems limiting greater private sector participation in the economy relate to: weak capital market development (particularly long-term debt and equity capital); the absence of industrial development policies at subsector levels with clear indications of the private sector's (vs. the State's) anticipated role; inadequate market information, particularly on export market opportunities, coupled with a need to further strengthen institutional capacities and appropriate incentive programs to promote investment projects, again particularly for exports; and the need for better coordination and more effective action by private sector organizations (chambers) which could result in greater influence in decision making and policies and regulations.

5. Description of the Project: The Mission plans to assist the GSL in its move towards privatizing the SOEs and to further develop the role of the private sector. A component for privatization assistance will be designed including grant funds to conduct studies and feasibility analyses and loan funds to assist in financing requirements for specific privatization actions. Other project components will address (a) capital markets development, (b) policy and regulation change, (c) export development, (d) access/linkages to foreign markets/technology/joint ventures opportunities and (e) institution building for private sector chambers and other business

promotion agencies. These components will be grant-funded. In addition to seeking institutional and policy improvements which address broad private sector interests, there will be specific quantifiable objectives in terms of increased investment exports and job creation which can be attributed to the project's activities.

- 6. Relationship of Project to A.I.D. Country Strategy: The project contributes directly to the CDSS objective to develop the private sector. Achievements of the project will improve the GSL budgetary situation (through reduced outlays for SOE, increased revenue, etc.) improve the macro-economic environment, stimulate a reliance on market forces, and enhance the availability of investment capital.
- 7. Target Group: The Sri Lankan private sector.
- 8. PID approval: The Mission will submit the PID for AID/W approval in July 1987.
- 9. Special Concerns: Private sector development.

New Project Description

1. Project Title: Development of Agricultural Marketing Systems

2. Aid Funding and LOP: Total AID Funding \$ 12,000,000

	<u>FY 88 Funding</u>	<u>FY 89 Funding</u>	<u>LOP Funding</u>	<u>Appropr Account</u>
Total	-	2,400	12,000	ARDN
Grant	-	400	5,500	
Loan	-	2,000	6,500	

3. Project Purpose:

Studies have been conducted in the last two years that point to several reasons for the reductions in productivity and farmer incomes. This project will concern itself with three of the constraints that have been identified in the marketing and processing sector. These are:

(a) Inadequate research extension, information, and training on post-harvest technology. Private sector investment is not attracted to these areas, and ultimately the farmer has insufficient incentive to increase and diversify his production or raise a better quality product.

(b) The absence of a well coordinated marketing system, and particularly the inadequate communication of existing market information to farmers and traders.

(c) Inadequate processing, bulking, and storage facilities and inadequate institutional credit mechanisms to establish them.

5. Proposed Project Strategy:

The project will address marketing constraints of smallholder crops through five main components:

(a) Improve the functioning of rural markets and of the broader marketing system for selected smallholder crops.

(b) Expand the availability of technology on post-harvest and food processing practices and support investment and improvements in these areas.

(c) Improve the relevance and availability of marketing information to farmers, traders, and exporters.

(d) Improve the facilities for storage and bulking of produce.

(e) Increase private sector access to credit for marketing and investments in storage and processing facilities.

. 55 '

The project will conduct studies of the current marketing system and support the improvement of the local rural markets (polas). In selected districts, pilot improved "polas" will be established. The project will use polas as a vehicle to improve access to information and credit, as well as improved trader/farmer interaction.

The project will examine and address the availability of institutional credit to potential private sector traders and farmer organizations for processing, storage, and marketing. It is proposed to experiment with credit systems by reducing risk to banks (i.e., guarantees), offering loans against new buildings or equipment, and establishing memoranda of understanding between project and participating banks. The project will introduce appropriate agroprocessing technology to improve the quality of domestic products for local consumption and pave the way for improved local products that can be competitive in the export marketplace.

The majority of training under this project will be short-term observational and hands-on training directed at extension staff, farmer organizations, and private sector businesses.

6. Relationship to Mission Strategy and Policies:

The focus of the project is directly related to major Mission strategic objectives of increasing rural incomes, increasing agricultural production and productivity, increasing employment and enhancing private sector participation in development activities.

7. PID Approval:

The PID will be forwarded to AID/W for approval by June 1988.

8. Target Group:

Small farmers, farmer organizations and private businesses established in project area.

9. Major Project Concerns:

Increased production, institution building, improvement of marketing environment and system, and employment generation

10. Training:

Long-term training: 36 person months
Short-term training: 120 person months

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New Project Description
(Shelf Project)

1. Project Title and Number: Smallholder Coconut Intercropping Project (383-0104)

2. Aid Funding \$'000: Total AID Funding \$12,000

	<u>FY 88</u> <u>Funding</u>	<u>FY 89</u> <u>Funding</u>	<u>LOP</u> <u>Funding</u>	<u>Appropriation</u> <u>Account</u>
Total	-	2,400	12,000	ARDN
Grant	-	400	5,000	
Loan	-	2,000	7,000	

3. Project Purpose:

The purpose of the project is to increase employment opportunities and generate additional incomes at the farm level, through the introduction of intercropping techniques to intensify cultivation and maximise agricultural production for smallholder coconut farmers.

4. Problems to be Addressed:

Although some coconut cultivation is done on large public and private estates, 60% of the area cultivated in coconut is by small farmers holding under four hectares. This land is relatively underutilized. Little intercropping is practiced, except for grazing livestock under coconut trees. Because of the decline in the world market price for coconut and coconut products, smallholder incomes are now particularly low.

Though the potential is considerable for increasing incomes on small farm holdings through fairly labor and land intensive intercropping practices, there are some important constraints to promoting and adopting those practices. Government responsibility for research and extension related to crops suitable for intercropping is divided among several different agencies (the Coconut Development Authority, the Department of Agriculture, the Department of Minor Export Crops, and the agencies responsible for animal production). Thus there is no locus for focusing on the complete farming system with which those practicing coconut intercropping would be involved. Particularly in some hill areas, soil degradation and erosion is a problem which would have to be addressed concurrently with intercropping. Existing credit systems are tied more to monoculture, rather than diversified cropping. And, though marketing systems are in place for coconut and its byproducts, in some areas they may not be well developed for possible intercrops.

5. Project Description:

The project will introduce new farming systems on small coconut holdings involving more intensive use of the land by multi-cropping and multilayering among existing coconut trees. It will identify existing technological packages and crop/stock mixes from Sri Lanka and other countries in the region (such as the Philippines, Malaysia, and India), as well as develop and test other alternatives suitable to Sri Lanka. It will introduce such practices through demonstration and integrated extension dealing with the full cropping system of the farmer. The project will address constraints to intercropping and extension in different agro-ecological regions of the country. Institutional linkages among the involved government research and extension agencies will have to be addressed. Other constraints to intercropping, such as the availability of appropriate credit or marketing, will need to be clearly identified and addressed as the project progresses.

6. Relationship to Mission Strategy and Policies:

The focus of the project is directly on one of the major Mission strategic objectives: increasing agriculture productivity and rural incomes. It is sensitive to agency equity concerns. Because of the land pressure in this part of the island, the main option for increasing small farmer incomes is through much more intensive cultivation. Available intercropping technologies tend to be highly labor intensive, and thus primarily adaptable by very small farmers, rather than large estates. The project would be one of a series of projects dealing with agriculture diversification and intensification; these include Diversified Agriculture Research, the Mahaweli Agriculture Rural Development, and Agricultural Planning and Analysis. It would also relate to one of the Mission's agricultural policy concerns of finding ways to deal with agricultural issues that are interministerial in nature under the present organizational structure.

7. Target Group:

Coconut small holder farmers and off-farm employment.

8. PID Approval:

The PID will be submitted to AID/W for review in March, 1988.

9. Special Concerns:

Diversification of agriculture, increased food production, and employment generation.

New Project Description
(Shelf Project)

1. Project Title and Number: Small Tank Irrigation Management Project (383-0092)
2. AID Funding (\$000): Total AID Funding \$12,000

	<u>FY 88</u> <u>Funding</u>	<u>FY 89</u> <u>Funding</u>	<u>LOP</u> <u>Funding</u>	<u>Appopr.</u> <u>Account</u>
Total:	-	2,400	12,000	ARDN
Grant:	-	400	5,500	
Loan:	-	2,000	6,500	

3. Project Purpose: To increase the production and incomes of small farmers in existing small tank (under 200 acre) irrigation schemes.
4. Problems to be Addressed: Sri Lanka has much farm land irrigated by existing irrigation schemes of varying size. In addition to the several large scale schemes constructed in recent years under the Accelerated Mahaweli Program, there are approximately 30,000 small scale schemes. In most irrigation schemes, farm incomes are inadequate and productivity is considerably below potential.

There are many reasons for the unrealized agricultural potential, though these are not of equal importance in different types of irrigation schemes. At the system level, operations and maintenance, financial management, monitoring and organization of water users are often inadequate. Water distribution is often not responsive to the timing needs of farmers; it usually assumes the double cropping of rice, though this is not now very profitable for the farmer. There is little interaction of agencies responsible for the flow of irrigation water and those concerned with different agricultural production systems; the former have limited knowledge about agricultural requirements and the latter have limited knowledge about irrigation systems. There is only limited coordination between those responsible for irrigation systems and those responsible for agricultural research.

In many irrigation schemes, there is no system for ongoing maintenance and scheduled rehabilitation using local resources. There is often little attention to the inter-relationships of small irrigation schemes with the larger water system of which it is a part (including other connected irrigation schemes, the watershed, inflows to and outflows from the scheme).

At the irrigation turnout level, when users organizations are weak or non-existent, water is often inequitably distributed. At the farm level, water is often inefficiently used. Various institutional supports are often lacking so that information about alternate cropping systems which could be more profitable to the farmers is not provided.

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5. Description of the Project: The project will take a systemic approach to farming in small irrigation schemes. Major elements will include: (1) building irrigation users organizations, which often manage small schemes, (2) improving water distribution in the system and the efficiency of water use by individual farmers, (3) physical rehabilitation of selected small schemes on a cost-shared basis with users groups, (4) establishing sound routine maintenance, (5) revising water management practices to permit more diverse cropping systems.

A major emphasis will be building strong water users organizations, building their planning and financial management skills, and improving their interaction with relevant government agencies. The project will be closely coordinated with USAID's Diversified Agricultural Research project and other water management projects. Important factors in selecting schemes for support under the project will be the hydrologic soundness of the scheme and the willingness of users groups to share in rehabilitation costs.

The project will include some short-term participant training for government officials working with small schemes. It will also include TA to help establish in-country training for local irrigation organizations. Project design will investigate utilizing FVOs in project implementation.

6. Relationship to the Mission Strategy: The project will directly support the Mission's objective of improving rural productivity and incomes by increasing the productive capability of the rural land resource. The project will contribute to the cost recovery and community participation themes and supports the Bureau's irrigation goals. Policy issues will be similar to those of the Irrigation Systems Management (383-0080) project and both will be mutually reinforcing.
7. Target Group: Small farm families who farm land in existing irrigation schemes.
8. PID Approval: The PID will be submitted to AID/W in April 1988 for review.

FY 1988 SRI LANKA ACTION PLAN

PD-AAX-338

1 OF 1 (24X)

SRI LANKA
ACTION PLAN

1987