



Report and Recommendation of the President to the Board of Directors

Project Number: 47273
September 2014

Proposed Multitranche Financing Facility Democratic Socialist Republic of Sri Lanka: Integrated Road Investment Program

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Asian Development Bank

CURRENCY EQUIVALENTS

(as of 6 August 2014)

Currency unit	–	Sri Lanka rupee/s (SLRe/SLRs)
SLRe1.00	=	\$0.0076787223
\$1.00	=	SLRs130.230000

ABBREVIATIONS

ADB	–	Asian Development Bank
ADF	–	Asian Development Fund
EIRR	–	economic internal rate of return
EMP	–	environmental management plan
IEE	–	initial environmental examination
km	–	kilometer
MFF	–	multitranches financing facility
MOHPS	–	Ministry of Highways, Ports and Shipping
OCR	–	ordinary capital resources
RDA	–	Road Development Authority

NOTE

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

Vice-President	W. Zhang, Operations 1
Director General	H. Kim, South Asia Department (SARD)
Director	H. Yamaguchi, Officer-In-Charge, Transport and Communications Division, SARD
Team leader	C. Chen, Senior Transport Specialist, SARD
Team members	J. Ghimire, Counsel, Office of the General Counsel T. Kawabata, Transport Specialist, SARD T. Koike, Financing Partnerships Specialist, Office of Cofinancing Operations A. Nanayakkara, Senior Project Officer (Road and Transport), Sri Lanka Resident Mission (SLRM), SARD R. V. Peri, Principal Transport Specialist, SARD J. Ranaweera, Associate Financial Control Officer, SLRM, SARD L. M. Tai, Senior Transport Specialist, SARD K. Yangzom, Environment Specialist, SARD S. Zhao, Social Development Specialist, SARD
Peer reviewers	Z. Wu, Transport Specialist, Central and West Asia Department D. Mizusawa, Infrastructure Specialist, Southeast Asia Department

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INVESTMENT PROGRAM^a AT A GLANCE

1. Basic Data		Project Number: 47273-002					
Project Name	Integrated Road Investment Program	Department /Division	SARD/SATC				
Country Borrower	Sri Lanka Government of Sri Lanka	Executing Agency	Ministry of Highways, Ports and Shipping				
2. Sector	Subsector(s)	ADB Financing (\$ million)					
✓ Transport	Road transport (non-urban)		800.00				
		Total	800.00				
3. Strategic Agenda	Subcomponents	Climate Change Information					
Inclusive economic growth (IEG)	Pillar 2: Access to economic opportunities, including jobs, made more inclusive	Adaptation (\$ million)	15.00				
Environmentally sustainable growth (ESG)	Global and regional transboundary environmental concerns	Climate Change impact on the Project	Medium				
4. Drivers of Change	Components	Gender Equity and Mainstreaming					
Governance and capacity development (GCD)	Organizational development	Effective gender mainstreaming (EGM)	✓				
Private sector development (PSD)	Conducive policy and institutional environment						
5. Poverty Targeting		Location Impact					
Project directly targets poverty	No	Rural	High				
6. Risk Categorization:	Complex						
7. Safeguard Categorization	Environment: B Involuntary Resettlement: B Indigenous Peoples: C						
8. Financing							
Modality and Sources	Indicative Tranches (\$million)						Amount (\$ million)
	I	II	III	IV	V	VI	
ADB							800.00
Sovereign MFF-Tranche (Loan): Asian Development Fund	100.00	9.00	0.00	0.00	0.00	0.00	109.00
Sovereign MFF-Tranche (Loan): Ordinary capital resources	0.00	91.00	200.00	150.00	150.00	100.00	691.00
Cofinancing							0.00
None							
Counterpart							106.00
Government	18.00	15.00	25.00	18.00	18.00	12.00	106.00
Total	118.00	115.00	225.00	168.00	168.00	112.00	906.00
9. Effective Development Cooperation							
Use of country procurement systems	No						
Use of country public financial management systems	Yes						

INVESTMENT PROGRAM^a AT A GLANCE

10. Country Operations Business Plan		
CPS	http://www.adb.org/sites/default/files/cps-sri-2012-2016.pdf	
COBP	http://www.adb.org/documents/sri-lanka-country-operations-business-plan-2014-2016?ref=countries/sri-lanka/strategy	
11. Investment Program Summary		
<p>The investment program will improve the accessibility of the road network in rural areas of Sri Lanka, and thereby increase the involvement of the rural population in nationwide economic and social development. An integrated road network will support long-term rural development. The investment program will upgrade and maintain about 2,200 kilometers (km) of rural access roads to all-weather standard; rehabilitate and maintain to a good condition about 400 km of national roads; and improve the capacity of road agencies—including the Ministry of Highways, Ports and Shipping (MOHPS), the Road Development Authority (RDA), provincial road agencies, and local authorities—with respect to road asset management, project management, and contract administration. The investment program will play a catalytic role in the sustainable development of Sri Lanka.</p> <p>Impact and Outcome: The impact (of the facility) is Improved connectivity between rural communities and socioeconomic centers in Sri Lanka. The outcome (of the facility) is Increased transport efficiency on project roads.</p> <p>Outputs: (i) Improved road conditions between the selected rural communities and socioeconomic centers, and (ii) Enhanced capacity of road agencies.</p> <p>Implementation Arrangements: Ministry of Highways, Ports and Shipping will be the executing agency.</p> <p>Project Readiness: Engineering design and bidding documents already finalized.</p>		
12. Milestones		
Modality	Estimated Approval	Estimated Completion^b
Multitranche financing facility	25 September 2014	30 September 2024
Tranche I	30 October 2014	30 September 2021
Tranche II	5 December 2014	30 September 2024
Tranche III	12 October 2016	30 September 2024
Tranche IV	12 October 2017	30 September 2024
Tranche V	12 October 2018	30 September 2024
Tranche VI	12 October 2020	30 September 2024
13. Project Data Sheet (PDS)		
PDS^c	http://www.adb.org/projects/47273-002/main	

^a Multitranche Financing Facility (MFF).

^b For MFF, this refers to the end of the availability period; for tranches, this refers to the tranche closing date.

^c Safeguard documents can be viewed by clicking the Document's hyperlink in the Project Data Sheet (PDS) page.

I. THE PROPOSAL

1. I submit for your approval the following report and recommendation on a proposed multitranche financing facility (MFF) to the Democratic Socialist Republic of Sri Lanka for the Integrated Road Investment Program.

2. The investment program will improve the accessibility of the road network in rural areas of Sri Lanka, and thereby increase the involvement of the rural population in nationwide economic and social development.¹ An integrated road network will support long-term rural development. The investment program will upgrade and maintain about 2,200 kilometers (km) of rural access roads to all-weather standard; rehabilitate and maintain to a good condition about 400 km of national roads; and improve the capacity of road agencies—including the Ministry of Highways, Ports and Shipping (MOHPS), the Road Development Authority (RDA), provincial road agencies, and local authorities—with respect to road asset management, project management, and contract administration.² The investment program will play a catalytic role in the sustainable development of Sri Lanka.

II. THE INVESTMENT PROGRAM

A. Rationale

3. Sri Lanka occupies a strategic position near the main sea trade routes between Asia and Europe, which allowed Colombo to develop as an international port city, and subsequently as a transshipment point for cargo originating in or destined for the Indian subcontinent. The island country consists mostly of flat or rolling coastal plains, with mountains in the south–central core. About 85% of Sri Lanka’s population (20.3 million in 2012) lives in rural and peri-urban areas.³

4. Sri Lanka has experienced strong economic growth following the end of civil conflict in May 2009. Economic growth was 8% in 2010 and 2011; slowed to 6.4% in 2012 due to weak external demand, drought, and floods; and then rebounded to 7.3% in 2013. It is envisaged that an improving external environment, higher investment, and a recovery in domestic consumption will sustain a rapid economic growth during 2014–2015.⁴ Sri Lanka’s economic expansion has been driven by the industry and services sectors, which account for 89% of gross domestic product, followed by the agriculture sector, which contributed the remaining 11%.⁵ As a result of the robust growth, the national poverty headcount ratio fell to just below 9% in 2010 from over 15% in 2006. Nevertheless, less-developed areas did not exhibit consistently higher elasticity of poverty reduction (proportional change in poverty per unit growth in gross domestic product per capita).⁶ The poor transport infrastructure, in particular the provincial and local authority roads, has hindered the spread of economic activities and access to basic social resources.

5. **Sector road map.** Sri Lanka’s road network is dense and well laid out, providing basic access to the country’s population and economic activity centers. The 132,693 km road network

¹ The Asian Development Bank (ADB) provided project preparatory technical assistance for the Integrated Road Operation and Development Investment Program (TA 8473-SRI).

² The design and monitoring framework is in Appendix 1.

³ World Bank and United Nations Human Settlements Programme (UN-Habitat). 2012. *Turning Sri Lanka’s Urban Vision into Policy and Action*. Washington, DC.

⁴ ADB. 2014. *Asian Development Outlook, 2014: Fiscal Policy for Inclusive Growth*. Manila.

⁵ Central Bank of Sri Lanka. 2013. *Annual Report of the Monetary Board to the Hon. Minister of Finance for the Year of 2012*. Colombo.

⁶ International Monetary Fund. 2013. *Sri Lanka: 2013 Article IV Consultation and Proposal for Post-Program Monitoring*. Washington, DC.

in Sri Lanka is classified into national, provincial, and local authority roads, according to administrative responsibility.⁷ Notable progress has been achieved since 2007 in addressing the immediate trunk road network deficiencies,⁸ but progress on provincial and rural roads is relatively slow.⁹ The main challenges facing road connectivity are that most rural access roads, including provincial and local roads, cannot provide all-weather access, and part of the trunk road network is in poor condition. These issues arise because of (i) competition for budget allocations with other sectors; (ii) inadequate fundraising in both the public and private sectors; (iii) inadequate rural road design standards and construction specifications; and (iv) the limited capacity of road agencies, particularly at the provincial and local levels.

6. A road asset management system is functioning in RDA to plan and program road projects. The government established a road maintenance trust fund in 2005. The fund has served a useful purpose in terms of securing a maintenance budget, and raising awareness of the importance of maintenance. In the long term, the government plans to expand the fund to cover provincial and rural roads, but this will require that a harmonized approach to road asset management be adopted by the various road agencies.

7. **Strategic context.** The government's national strategy for 2010–2020 aims to accelerate economic growth, improve social indicators, eradicate hard-core poverty, and improve the environment.¹⁰ Inadequate, poor-quality infrastructure is identified by the strategy as a major constraint to sustaining rapid economic growth, and the strategy places the highest priority on improving the country's road network. The road network development investment in 2011 at national, provincial, and local levels was about six times higher in nominal terms than in 2005. The public investment strategy proposes to sustain annual public investment at more than \$1.3 billion until 2016, which would thereafter help develop and maintain the road network.¹¹

8. In line with the government's national strategy, the country partnership strategy 2012–2016 of the Asian Development Bank (ADB) aims to address the major constraints for sustaining inclusive growth in post-war Sri Lanka.¹² The transport sector is one of the key areas in implementing the strategy. As agreed with the government, ADB will contribute to the sector outcome of improved nationwide connectivity.

9. **Policy framework.** The central government is responsible for transport policy and interprovincial (national) road transport infrastructure. Provincial governments are responsible for provincial roads, and local authorities for the local authority roads. The government has adopted a two-tier strategy to provide nationwide connectivity: (i) establishing a trunk road network with expressways and well-connected national roads, and (ii) completing a rural road network to connect the rural population to trunk roads. RDA's project management capacity has been well developed through large-scale projects, beginning in 2007. A skills transfer program is

⁷ National roads, comprising about 11,922 km of class A and class B roads, are managed by the central government through the RDA. The provincial road network, comprising 15,975 km of class C and class D roads, is managed by the provincial councils. In addition, about 80,000 km of local roads (class E) are managed by local governments.

⁸ The proportion of national roads in good condition rose from 35% in 2007 to 48% in 2011, those in fair condition dropped from 19% to 11%, and those in poor condition declined from 46% to 41%.

⁹ The government has established *Maga Neguma*, a rural road program, to improve rural roads through RDA. The program has improved about 10,000 km of rural roads at the request of local authorities since 2004, but about 90% of the rural road network still requires rehabilitation.

¹⁰ Government of Sri Lanka, Ministry of Finance and Planning, Department of National Planning. 2010. *Sri Lanka: The Emerging Wonder of Asia: Mahinda Chintana—Vision for the Future*. Colombo.

¹¹ Government of Sri Lanka, Ministry of Finance and Planning, Department of National Planning. 2013. *Unstoppable Sri Lanka 2020: Public Investment Strategy, 2014-2016*. Colombo.

¹² ADB. 2011. *Country Partnership Strategy: Sri Lanka, 2012–2016*. Manila.

being established to build the capacity of provincial and local road agencies; it will involve their staff in RDA's road asset management, project management, and contract administration activities. The development of the national road network is guided by the national road master plan.¹³ Improvements to rural access roads, including provincial and local authority roads, are scheduled annually to address the community demands. To supplement the capacity of provincial governments and local authorities, RDA, the provincial road agencies, and the local authority jointly implement rural road improvement works.

10. In line with the two-tier strategy, the government plans to implement an investment plan for rural road connectivity. The plan is designed to provide physical infrastructure and capacity to enhance the road connectivity of rural areas. About 1,000 rural communities will be selected as rural hubs according to their population and development potential. Access routes—including local authority, provincial, and national roads—will be upgraded or rehabilitated. The total investment demand is about \$1.8 billion. The government requests that ADB finance the program in five provinces (Southern Province, Sabaragamuwa Province, Central Province, North Central Province, and North Western Province) and one rural district (Kalutara District of Western Province). The government has also requested Japan International Cooperation Agency to finance projects in the other areas to complement ADB's assistance.

11. The investment program is in line with the government's sector objective of establishing a modern transport system. An MFF is proposed as the financing modality for the investment program because it will allow long-term partnership between the government and ADB on policy dialogue and capacity development within a large-scale program.¹⁴ A portfolio review of ADB-funded road projects confirmed that the implementation capacity in Sri Lanka is adequate.

B. Impact and Outcome

12. The impact of the investment program will be improved connectivity between rural communities and socioeconomic centers in Sri Lanka. The outcome will be increased transport efficiency on project roads.

C. Outputs

13. The investment program will deliver two outputs: (i) improved road conditions between the selected rural communities and socioeconomic centers, and (ii) enhanced capacity of road agencies. The two outputs will be achieved through two components of the investment program.

- (i) **Road improvement component.** This component will design, improve, and maintain about 2,200 km of rural access roads, including provincial and local authority roads, and about 400 km of national roads. The rural access roads will be improved to all-weather standards, and be maintained for 3 years. Selected national road corridors will be improved and/or maintained for 7 years, while short, isolated sections will be maintained for 3 years after improvement.
- (ii) **Capacity development component.** This component will build the capacity of road agencies in road asset management, project management, and contract administration. RDA will take the lead in developing a harmonized approach to road asset management in central, provincial, and local governments. Consulting services will be engaged to assist with development of the RDA's capacity, and the transfer of skills from RDA to provincial and local road agencies.

¹³ RDA, Planning Division. 2007. *National Road Master Plan, 2007–2017*. Colombo.

¹⁴ Comparison of Financing Modality (accessible from the list of linked documents in Appendix 2).

14. The investment program will comprise five projects: project 1 in Southern Province, project 2 in Sabaragamuwa Province and the Kalutara District of Western Province, project 3 in Central Province, project 4 in North Central Province, and project 5 in North Western Province.¹⁵ The first tranche will finance the first slice of project 1, and deliver three outputs: (i) improved road conditions between selected rural communities and socioeconomic centers in Southern Province; (ii) enhanced capacity of road agencies, including MOHPS, RDA, and road agencies in Southern Province; and (iii) preparation of subsequent tranches.

D. Investment and Financing Plans

15. The investment program is estimated to cost \$906 million (Table 1).

Table 1: Investment Program
(\$ million)

Item	Amount ^a
A. Base Cost^b	
1. Civil works	701.12
2. Consulting services	40.48
3. Recurrent costs (project management)	15.00
Subtotal (A)	756.60
B. Contingencies^c	130.90
C. Financing Charges During Implementation^d	18.50
Total (A+B+C)	906.00

^a Includes taxes and duties of \$82.60 million to be financed from government resources.

^b In mid-2014 prices.

^c Physical contingencies computed at 10% for civil works, and 10% for consulting services. Price contingencies computed at about 2% on foreign exchange costs and about 6% on local currency costs; includes provision for potential exchange rate fluctuation under the assumption of a purchasing power parity exchange rate.

^d Includes interest and commitment charges. Interest during construction for Asian Development Bank (ADB) loan(s) has been computed at the 5-year forward London interbank offered rate plus a spread of 0.5% for the ordinary capital resources loan, and at 2.0% per annum for the loan from ADB's Special Funds resources. Commitment charges for the ordinary capital resources loan(s) are 0.15% per year to be charged on the undisbursed OCR loan amount.

Source: Asian Development Bank.

16. The government has requested an MFF in an amount up to \$800 million equivalent from ADB's ordinary capital resources (OCR) and Special Funds resources to help finance part of the investment program, including civil works contracts (improvement and maintenance), consulting services, project management, and part of the contingencies.¹⁶ The MFF will consist of multiple tranches, subject to the government's submission of related periodic financing requests, execution of the related loan and project agreements for each tranche, and fulfillment of terms and conditions and undertakings set forth in the framework financing agreement.¹⁷ The government will finance the feasibility study and engineering design, taxes and duties, and part of the contingencies, for a total of \$106 million. In addition, the government has requested Japan International Cooperation Agency to finance projects in the remaining areas of the other four provinces (Northern Province, Eastern Province, Uva Province, and Western Province) so that the whole country will be covered.

¹⁵ List of Projects (accessible from the list of linked documents in Appendix 2).

¹⁶ About \$21 million of performance-based maintenance under civil works contracts will be financed by the MFF to support the government in exploring a sustainable contract model of road operation and maintenance. This support will also alleviate the government's budget and capacity constraints on road maintenance.

¹⁷ Framework Financing Agreement (accessible from the list of linked documents in Appendix 2).

17. The MFF combines OCR and Asian Development Fund (ADF) financing up to the aggregate MFF amount. The provision of any ADF resources will be balanced by a corresponding reduction in available OCR financing (and vice versa), with total financing provided under the MFF not to exceed the aggregate MFF total of \$800 million equivalent. Any ADF allocation will be subject to (i) the availability of ADF resources; (ii) Sri Lanka's access to such resources pursuant to ADB's Graduation Policy,¹⁸ and the requirements of ADF donors; and (iii) the availability of such resources to Sri Lanka given ADB's policy on performance-based allocation of ADF resources.¹⁹

18. **Disbursement-based approach and time-slice financing.** The financing plan and an indicative tranche schedule are in Table 2. The MFF will finance slices of long-term contract packages under the investment program. Each tranche will finance slices of a group of contracts for civil works or consulting services. Each contract is sliced according to the indicative tranche schedule.²⁰ The amount of each tranche will be requested according to the disbursement progress and projection. The tranche schedule is based on the disbursement projection to improve the disbursement ratio and minimize financing charges.

19. The preconstruction activities, such as appraisal and procurement, will be all advanced to the first 2–3 years of the investment program. The government has completed preparation and due diligence for project 1, and will complete the preparation of other projects by October 2014. Following the disbursement-based approach, the government intends to request tranche 1 together with the facility to finance the first slice of project 1, and to request tranche 2 by the end of 2014 to finance the first slice of other projects.

Table 2: Financing Plan

Source	Amount (\$ million)	Share of Total (%)	Indicative Tranche Schedule and Amount (\$ million)					
			1 (2014)	2 (2014)	3 (2016)	4 (2017)	5 (2018)	6 (2020)
Asian Development Bank	800.0	88.3	100.0	100.0	200.0	150.0	150.0	100.0
Government	106.0	11.7	18.0	15.0	25.0	18.0	18.0	12.0
Total	906.0	100.0	118.0	115.0	225.0	168.0	168.0	112.0

Source: Asian Development Bank.

20. **Project 1 and tranche 1.** Project 1 is estimated to cost \$235 million. Tranche 1 will require a loan of \$100 million from ADB's Special Funds resources.²¹ The loan will have a 25-year term, including a grace period of 5 years, an interest rate of 2.0% per annum during the grace period and thereafter, and such other terms and conditions as agreed to in the framework financing agreement, and further supplemented under the draft loan and project agreements.

E. Implementation Arrangements

21. The implementation arrangements are summarized in Table 3.²²

¹⁸ ADB. 2008. *Review of the 1998 Graduation Policy of the Asian Development Bank*. Manila.

¹⁹ ADB. 2004. *Review of the Asian Development Bank's Policy on the Performance-Based Allocation of Asian Development Fund Resources*. Manila; and ADB. 2008. *Refining the Performance-Based Allocation of Asian Development Fund Resources*. Manila.

²⁰ Disbursement-Based Approach and Time-Slice Financing (accessible from the list of linked documents in Appendix 2).

²¹ Periodic Financing Request for Tranche 1 (accessible from the list of linked documents in Appendix 2).

²² Facility Administration Manual (accessible from the list of linked documents in Appendix 2).

Table 3: Implementation Arrangements

Aspects	Arrangements		
Implementation period	September 2013–March 2024		
Estimated completion date	30 March 2024		
Management			
(i) Oversight body	<p>National Steering Committee: Chair: Secretary, Ministry of Highways, Ports and Shipping. Members: Chief secretaries of the provinces under the investment program; secretary, Finance Commission; director general, RDA; senior project director and project directors of each project of the investment program; commissioners of local government authorities under the investment program; heads of provincial road agencies; district secretaries; External Resources Department, National Planning Department, and Project Monitoring and Management Department of the Ministry of Finance and Planning</p> <p>Provincial Coordination Committees: Chair: Chief secretary of the province. Members: Project director (secretary to the committee), district secretaries, representatives of provincial road agencies, representatives of local authorities</p>		
(ii) Executing agency	Ministry of Highways, Ports and Shipping		
(iii) Key implementing agency	RDA		
(iv) Implementation unit	RDA, 40 staff (to be strengthened as required).		
Procurement	International competitive bidding	40–50 contracts	\$701.1 million
Consulting services	Project implementation consultants (QCBS 90:10)	About 400 person-months of international and 7,000 person-months of national services (4 contracts)	\$29.5 million
	Individual consultants	96 person-months of international and 160 person-months of national services	\$5.0 million
Retroactive financing and/or advance contracting	Retroactive financing and advance contracting will be used for civil works and consulting services financed by tranche 1. Under each tranche, ADB may, subject to its policies and procedures, allow on request (i) advance contracting of civil works, equipment and materials, and consulting services; and (ii) retroactive financing of eligible expenditures for civil works, equipment and materials, and consulting services up to 20% of proposed individual loan, incurred prior to loan effectiveness but not earlier than 12 months before the date of signing of the related legal agreement.		
Disbursement	The loan proceeds will be disbursed in accordance with ADB's <i>Loan Disbursement Handbook</i> (2012, as amended from time to time) and detailed arrangements agreed upon between the government and ADB.		

ADB = Asian Development Bank, QCBS = quality- and cost-based selection, RDA = Road Development Authority.
Source: Road Development Authority.

III. DUE DILIGENCE

A. Technical

22. Engineering design has been carried out for all project roads under project 1 based on site condition surveys, field investigations, and climate risk assessment.²³ The engineering

²³ Climate Risk Assessment and Management Report (accessible from the list of linked documents in Appendix 2).

designs are optimized for economy and construction efficiency in accordance with international and national design standards. For provincial and rural roads, a context-sensitive design approach is adopted to incorporate community concerns. Construction will use proven technology and standard materials compatible with local conditions. Project 1 of the investment program has two groups of civil works contracts: (i) conventional road contracts, including construction and 3-year performance-based maintenance; and (ii) road management contracts, including 7 years of rehabilitation and maintenance to deliver a predefined level of services.

B. Economic and Financial

23. In addition to the large vehicle operating cost and time savings, all-weather rural access road will result in significant benefits, such as increased agriculture productivity, easier access to health and education, poverty reduction, and better employment opportunities for the rural population. These social benefits are not captured by the conventional economic analysis model. Therefore, an economic internal rate of return (EIRR) threshold of 10% is adopted for rural access roads. For national roads, a threshold of 12% EIRR is used. The economic analysis of project 1 indicated it is economically viable, with an overall EIRR of 19.1%.²⁴ A sensitivity analysis on capital costs, benefits, and implementation delays confirmed its economic viability.

24. The unit costs related to operation and maintenance of project roads will decrease after construction is completed. Recent trends indicate that future budget allocations for national roads will be adequate. The government envisages that in the long term, the road maintenance trust fund will allow access by provincial and local road agencies. The investment program will build the capacity of provincial and local road agencies to facilitate the process of granting access of the trust fund to non-national roads, and to enhance their financial sustainability.

C. Governance

25. **Policy and legal.** The implementation arrangements of the investment program will involve three levels of government: central, provincial, and local. At the central level, the MOHPS is responsible for the formulation of policies and performance monitoring. RDA was established as a statutory authority with a separate legal status by the Road Development Authority Act in 1981. RDA's chairperson reports to the secretary of MOHPS. At the provincial and local levels, the provincial councils are responsible for the work of the respective local authorities within the provincial councils, under the 13th amendment to the Constitution enacted in 1987 and the Pradheshiya Sabha Act No 15 in 1987. In keeping with the devolution norm of Sri Lanka, RDA acts as if contracted by the provincial authorities to construct roads that belong to the local authorities, and a memorandum of understanding to this effect will be executed. The arrangements follow existing practice in Sri Lanka, where local authorities generally lack the capacity and resources for such projects.

26. The implementation arrangements satisfy the RDA Act, which requires that RDA consult with other government agencies regarding projects within their respective areas. The national steering committee and provincial coordination committees will ensure proper coordination.

27. **Institutional capacity.** MOHPS and RDA have sufficient capacity, past experience, and institutional strength to procure the civil works, select consultants, and administer contracts. Participation of provincial, district and local authorities in the steering and coordination committees has been arranged, with consideration of their respective institutional capacity.

²⁴ Economic and Financial Analysis: Project 1 (accessible from the list of linked documents in Appendix 2).

28. **Financial management.** A financial management assessment was carried out for RDA. RDA has prior and ongoing experience implementing ADB-funded projects. It has satisfactory capacity in project financial accounting and in ADB disbursement procedures. RDA has a dedicated project accounting and finance team with suitably qualified accountants. RDA will establish and maintain separate project records and accounts to identify the financing resources received and expenditures made for the project, thus ensuring an adequate audit trail. The government's Auditor General's Department will annually audit the project accounts and related financial statements in accordance with international auditing standards.

29. **Procurement and anticorruption.** Procurement will be in accordance with ADB's Procurement Guidelines (2013, as amended from time to time). The Bribery Act, No. 11 of 1954 (as amended from time to time), the Declaration of Asset and Liabilities Act, No. 1 of 1975, and the Permanent Commission to Investigate Allegations of Bribery and Corruption Act, No. 19 of 1994 provide a legal basis to deal with bribery and corruption. The auditor general monitors procurement activities. ADB's Anticorruption Policy (1998, as amended to date) was explained to and discussed with the government, the MOHPS, and RDA. The specific policy requirements and supplementary measures are described in the facility administration manual.

D. Poverty and Social

30. **Poverty reduction and social impacts.** Project 1 will improve the socioeconomic situation and enhance poverty reduction in Southern Province. About 1.2 million people live in the 45 divisions within project areas. Consultation and social surveys were conducted along all project roads, and covered 4,899 households (approximately 38% of the households along the project roads), with 14 focus group discussions. The current road conditions were described as bad by 80% of surveyed households. Communities indicated that the poor conditions prevented safe travel, and cited that positive benefits will include improved access to education and health, better transport services, and increased job opportunities. Communities will be consulted through a transect walk to ensure that the final design of provincial and rural roads incorporate their concerns on construction, social and environmental issues, and road safety.²⁵

31. **Gender and development.** The country now ranks midway on the United Nations gender-related development index. The social study found that women were actively engaged in family and community activities and decision-making processes: 80% always participating in family decision making, 54% contributed to household income, and 53% were involved in community activities. Sixty-two percent of women stated they were willing to participate in the project through (i) working as maintenance laborer or civil works wage laborer, and (ii) operating a small business to provide services to contractors. Women indicated that improved road accessibility will provide better access to health, education, social, and economic opportunities. A gender action plan has been prepared for project 1.²⁶ Gender mainstreaming activities include (i) ensuring that at least 40% of the people consulted in the final design of rural access roads are women; (ii) integrating features that increase safety and meet the needs of the elderly, women, children and the disabled; (iii) ensuring that at least 30% of local employees hired for road maintenance are women and that they receive equal wages for equal work; (iv) providing training in road maintenance to all employed women; and (v) encouraging women's participation in awareness campaigns on road safety, sexually transmitted infections, and human trafficking.

²⁵ Summary Poverty Reduction and Social Strategy: Project 1 (accessible from the list of linked documents in Appendix 2).

²⁶ Gender Action Plan: Project 1 (accessible from the list of linked documents in Appendix 2).

32. **HIV/AIDS and human trafficking.** The HIV prevalence rate is low in Sri Lanka. The establishment of the National Program for Sexually Transmitted Diseases and AIDS Control helps refurbish health clinics and establish outreach and awareness programs. This investment program has incorporated measures to mitigate HIV/AIDS risks by undertaking awareness training for civil works contractors and for project-affected communities at prominent village locations. Awareness-raising activities will be conducted separately for men and women. The social impact assessment did not identify human trafficking as a significant issue in the project area. It is anticipated that civil works contractors will hire local laborers and not require migrant workers. Affected communities will be provided with awareness training on human trafficking.

E. Safeguards

33. **Involuntary resettlement and indigenous peoples.** Project 1 is classified as category B in involuntary resettlement in accordance with ADB's Safeguard Policy Statement (2009). The improvement of rural access roads and national roads will be within the existing alignment with no widening. Due diligence for project 1 identified no impacts to land, structures, private trees, or community resource properties.²⁷ However, resettlement impacts may be encountered at a later stage of the 7-year road management contract. A grievance redressal mechanism will be set up in all project areas. A resettlement framework has been prepared to guide compliance with social safeguard requirements in succeeding projects.²⁸ If land is required for the rural access roads when implementing succeeding projects, the voluntary land donation system will be used. The system has been used effectively under other rural development programs in Sri Lanka. Specific procedural requirements for land donation, involving comprehensive consultations with the communities, have been prepared in the resettlement framework. The government will ensure that land donation is undertaken without coercion and documented in a transparent manner, and will have the process verified by an independent monitor. For national roads requiring land, acquisition will take place in accordance with requirements of the government and ADB's Safeguard Policy Statement, per the resettlement framework. Project 1 is not expected to impact indigenous peoples and is consequently designated category C. An indigenous peoples planning framework has been prepared to guide the planning and preparation of future projects.²⁹ The due diligence report, the resettlement framework and the indigenous peoples planning framework have been disclosed on the ADB website.

34. **Environmental impact.** The scope of works under project 1 involves rehabilitation and maintenance of existing rural and national roads. Therefore project 1 has been designated category B in accordance with ADB's Safeguard Policy Statement. A consolidated provincial-level initial environmental examination (IEE) report has been prepared,³⁰ and an environmental assessment and review framework has been prepared to guide compliance with the environmental safeguard requirements of the government and ADB's Safeguard Policy Statement in succeeding projects.³¹ The IEE and the environmental assessment and review framework fulfill ADB's Safeguard Policy Statement requirements and have been disclosed on the ADB website. Anticipated environmental impacts under project 1 entail typical road construction-related issues such as generation of dust, noise, exhaust, waste from construction sites and worker camps, water contamination, occupational health and safety, erosion, and siltation. Mitigation measures have been included in a standard environmental management

²⁷ Resettlement Due Diligence Report: Project 1 (accessible from the list of linked documents in Appendix 2).

²⁸ Resettlement Framework (accessible from the list of linked documents in Appendix 2).

²⁹ Indigenous Peoples Planning Framework (accessible from the list of linked documents in Appendix 2).

³⁰ Initial Environmental Examination: Project 1 (accessible from the list of linked documents in Appendix 2).

³¹ Environmental Assessment and Review Framework (accessible from the list of linked documents in Appendix 2).

plan (EMP) as part of the IEE. The contractor will be required to prepare contract package-specific EMPs based on their final design, road-specific environment checklists, and the standard EMP. Consultations have been conducted during the project preparation, and the IEE incorporates the concerns of the affected persons and stakeholders.

35. RDA has an experienced environment and social development division to manage both safeguard issues, and a safeguard team from the division will be deputed under the project implementation unit. The unit will also be supported by consultants for monitoring and reporting on safeguard implementation. Safeguard training workshops will be held regularly.

F. Risks and Mitigating Measures

36. The overall risk assessment is medium without mitigation and low with mitigation. Integrated benefits and impacts are expected to outweigh costs. Major risks and mitigating measures are detailed in the risk assessment and risk management plan.³² The key risk is frequent implementation delays resulting from the need to prepare detailed engineering designs and prolonged land acquisition and resettlement. To mitigate this risk, engineering design and bidding documents have been prepared in advance, and land requirements minimized.

IV. ASSURANCES

37. The government, the MOHPS, and the RDA have assured ADB that implementation of the investment program shall conform to all applicable ADB policies including those concerning anticorruption measures, safeguards, gender, procurement, consulting services, and disbursement as described in detail in the facility administration manual and loan documents.

38. The government, the MOHPS, and the RDA have given ADB certain undertakings for the MFF, which are set forth in the framework financing agreement. Specific covenants agreed by the government, the MOHPS, and the RDA with respect to individual tranches under the MFF are set forth in the loan agreement and project agreement for the respective tranches.

V. RECOMMENDATION

39. I am satisfied that the proposed multitranche financing facility would comply with the Articles of Agreement of the Asian Development Bank (ADB) and recommend that the Board approve the multitranche financing facility to the Democratic Socialist Republic of Sri Lanka for the Integrated Road Investment Program in an aggregate principal amount not exceeding the equivalent of \$800,000,000, which comprises:

- (i) the provision of loans from ADB's Special Funds resources, with interest and other terms to be determined in accordance with ADB's applicable policies relating to Special Funds resources; and
- (ii) the provision of loans from ADB's ordinary capital resources, with interest and other terms to be determined in accordance with ADB's London interbank offered rate (LIBOR)-based lending facility

and is subject to such other terms and conditions as are substantially in accordance with those set forth in the framework financing agreement presented to the Board.

Takehiko Nakao
President

3 September 2014

³² Risk Assessment and Risk Management Plan (accessible from the list of linked documents in Appendix 2).

DESIGN AND MONITORING FRAMEWORK FOR THE INVESTMENT PROGRAM

Design Summary	Performance Targets and Indicators with Baselines	Data Sources and Reporting Mechanisms	Assumptions and Risks
<p>Impact Improved connectivity between rural communities and socioeconomic centers in Sri Lanka</p>	<p>By 2027: The number of rural hub centers connected to socioeconomic centers by all-weather roads increases by 1,000</p>	<p>Annual report of the Ministry of Finance and Planning RDA survey</p>	<p>Assumptions Government's development strategy effectively coordinated with road sector investment Planned transport projects implemented as scheduled</p>
<p>Outcome Increased transport efficiency on project roads</p>	<p>By 2024: Travel time on project rural roads reduced by 20% from 2013 rate Travel time on project national roads reduced by 10% from 2013 rate Use of roads built or upgraded (average daily vehicle-km in the first full year of operation) reaches 2.8 million</p>	<p>For all indicators: RDA survey</p>	<p>Assumption Government provides counterpart funds for the project on time</p>
<p>Outputs 1. Improved road conditions between the selected rural communities and socioeconomic centers</p>	<p>By 2024: About 2,200 km of rural access roads improved to all-weather standard About 400 km of national roads rehabilitated and maintained under performance-based contracts Gender targets achieved for road maintenance works</p>	<p>For all indicators: RDA project performance monitoring system</p>	<p>Risk Implementation delayed by extreme weather conditions</p>
<p>2. Enhanced capacity of road agencies</p>	<p>By 2024: Program for skills transfer to provincial and local road agencies from RDA established and functioning Rural road design standard, construction specification, and maintenance manual endorsed by RDA</p>	<p>Capacity-building program reports Capacity-building program reports</p>	<p>Assumption Consensus reached with other government agencies on strategy to improve the overall rural connectivity</p>

Design Summary	Performance Targets and Indicators with Baselines	Data Sources and Reporting Mechanisms	Assumptions and Risks
	About 80 staff have received training on road asset management, project management, and/or performance-based road contracts	Training program reports	
<p>Activities with Milestones</p> <p>1. Improved road conditions between the selected rural communities and socioeconomic centers</p> <p>1.1 Mobilize project implementation consultants by 2014</p> <p>1.2 Complete engineering design and bidding documents by 2016</p> <p>1.3 Award all contracts for civil works by 2018</p> <p>1.4 Complete civil works by 2024</p> <p>1.5 Implement performance monitoring survey of the investment program from 2014 to 2024</p> <p>2. Enhanced capacity of road agencies</p> <p>2.1 Mobilize capacity-building consultants by 2017</p> <p>2.2 Establish a skill transfer program to provincial and local road agencies by RDA by 2018</p> <p>2.3 Develop a capacity development program on road asset management for RDA, provincial and local road agencies by 2018</p> <p>2.4 Develop rural road design standard, construction specification, and maintenance manual by 2020</p> <p>2.5 Develop standard bidding documents and contract administration manual for road management by 2020</p> <p>2.6 Conduct training programs by 2024</p>		<p>Inputs</p> <p>Asian Development Bank: \$800 million</p> <p>Government: \$106 million</p>	

km = kilometer, RDA = Road Development Authority.
Source: Asian Development Bank.

LIST OF LINKED DOCUMENTS

<http://adb.org/Documents/RRPs/?id=47273-002-3>

1. Framework Financing Agreement
2. Periodic Financing Request for Tranche 1
3. Sector Assessment (Summary): Transport (Road Transport)
4. Facility Administration Manual
5. Contribution to the ADB Results Framework
6. Development Coordination
7. Economic and Financial Analysis: Project 1
8. Country Economic Indicators
9. Summary Poverty Reduction and Social Strategy: Project 1
10. Gender Action Plan: Project 1
11. Initial Environmental Examination: Project 1
12. Environmental Assessment and Review Framework
13. Resettlement Framework
14. Indigenous Peoples Planning Framework
15. Risk Assessment and Risk Management Plan

Supplementary Documents

16. Resettlement Due Diligence Report: Project 1
17. Disbursement-Based Approach and Time-Slice Financing
18. List of Projects
19. Climate Risk Assessment and Management Report
20. Comparison of Financing Modality