

Pakistan

Sector Assessment Review

Asian Development Bank

October 2003

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FOREWORD

A sector assessment review was first prepared for the Pakistan program in October 1997, but the report was circulated only within concerned Departments at ADB. The review was then updated in March 2000, and published as an internal ADB document. The sector assessment reviews are intended to form the basis for a discussion on sector priorities as a whole, as well as on development targets and priorities within each sector of operation. The reviews thus serve to generate debate on how limited resources are to be allocated across sectors, and how the focus of lending is to be narrowed to achieve specific development goals within sectors. The reviews not only highlight ADB's operational coverage of priority areas, but also provide an insight on the policy and institutional framework supporting development activities in each sector, and help Bank staff to form a considered assessment of the operational constraints likely to surface. The current sector assessment review, which is the third in the series, reflects the priorities of ADB's Country Strategy and Program for Pakistan, completed in May 2002. As such, the review assesses ADB's operations in the area of Governance in addition to the "traditional" sectors of Bank operation such as infrastructure and social development.

Although the review provides an overview of ADB's operations in Pakistan since lending to the Government of Pakistan began in 1968, it focuses more on the nature of ADB's operations over the last five years, following the macroeconomic crisis of 1998. This period, which covers the ambitious macroeconomic and governance reforms carried out by the Government of Pakistan, has been a significant one for ADB operations in the country. ADB has supported the reform effort through enhanced levels of assistance, and targeted investment projects with the objective of poverty reduction and employment generation, totaling more than \$3.2 billion, or an average of over \$800 million a year over the period from 1999-2002. In comparison, average annual lending in the period from 1990 to 1998 was just over \$500 million per year. The increased lending is also more specifically focused on supporting poverty reduction and improvements in systems of governance.

Although the previous sector assessment reviews have mainly served as background documents for country operations for ADB staff, the current comprehensive review is being published for a wider audience in Government, academia and civil society institutions. We hope that this publication will be useful to our development partners in policy making and implementation, as well as to a wide range of stakeholders who are interested in economic and social development in general, and in ADB activities in particular.

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Country Director
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INTRODUCTION

In October 1997 the first sector assessment review of Pakistan's country program was circulated in the Projects Departments. A second review two years later was done following the submission of the 1999 Country Assistance Program (CAP) and incorporating the main features of the cooperative work of bank departments. The present Sector Assessment Review of ADB operations in Pakistan concentrates on strategic focus, portfolio performance and impact of ADB's assistance since 1999 and follows the approval of the Country Strategy and Program (CSP) 2002-2006 in May 2002 and approval of the CSP Update (CSPU) in August 2003. It is intended as a basis for discussion of sector priorities and to focus on the coverage of priority areas and concerns, including the constraints and realities of government policies, programs and institutions.

This report will help the South Asia Department (SARD) to evaluate the country's situation, moving beyond macroeconomic analysis to provide a clear understanding of outstanding issues and key development challenges in individual sectors; it will serve as an advocacy document with the government and other donors and as an input into prospective CSP/CSPU processes. The sector assessment will be updated periodically to reflect developments in the sectors concerned. Assistance, contributions, and suggestions from staff in other Departments and Divisions will be appreciated.

LIST OF ABBREVIATIONS

| | |
|---------|--|
| ADB | Asian Development Bank |
| ADBP | Agriculture Development Bank of Pakistan |
| ADF | Asian Development Fund |
| ADTA | Advisory Technical Assistance |
| AG | Auditor General |
| AJP | Access to Justice Program |
| ASPL-I | Agriculture Sector Program Loan I |
| ASPL-II | Agriculture Sector Program Loan-II |
| AWB | Area Water Board |
| BOI | Board of Investment |
| CBOs | Community Based Organizations |
| CBR | Central Board of Revenue |
| CDC | Central Depository Company |
| CGA | Controller General of Accounts |
| CMDP | Capital Market Development Program |
| COF | Country Operational Framework |
| COS | Country Operational Strategy |
| CPRM | Country Portfolio Review Mission |
| CPMUs | Core Project Management Units |
| CSP | Country Strategy and Program |
| CSPU | Country Strategy and Program Update |
| C&WD | Communications and Works Department |
| DGG | Directorate General of Gas |
| DGPC | Directorate General of Petroleum Concessions |
| DIMRC | Drought Impact Mitigation and Recovery Component |
| DSP | Decentralization Support Program |
| DSS | Decentralized Social Services |
| DWT | Dead Weight Ton |
| ECD | Early Childhood Development |
| EOBI | Employee Old Age Benefit Institution |
| EPB | Export Promotion Bureau |
| ESAF | Extended Structural Adjustment Facility |
| ESRPL | Energy Sector Restructuring Program Loan |
| FATA | Federally Administered Tribal Areas |
| FFC | Federal Flood Commission |
| FMGP | Financial Markets and Governance Program |
| FO | Farmers' Organizations |
| GDP | Gross Domestic Product |
| GRAP | Gender Reform Action Plan |
| IDBP | Industrial Development Bank of Pakistan |
| IMF | International Monetary Fund |
| IPP | Independent Power Project |

| | |
|----------|---|
| IPRSP | Interim Poverty Reduction Poverty Paper |
| JBIC | Japan Bank for International Cooperation |
| KESC | Karachi Electric Supply Company |
| KMC | Karachi Metropolitan Corporation |
| KSE | Karachi Stock Exchange |
| KWSB | Karachi Water and Sewerage Board |
| LGO | Local Government Ordinance |
| MELGRD | Ministry of Environment, Local Government and Rural Development |
| MFI | Micro Finance Institution |
| MINFAL | Ministry of Food, Agriculture and Livestock |
| MLJHR&PA | Ministry of Law, Justice, Human Rights and Parliamentary Affairs |
| MOSEWD | Ministry of Special Education, Social Welfare and Women's Development |
| MOWP | Ministry of Water and Power |
| MSDP | Micro-finance Sector Development Program |
| MTIP | Medium-term Investment Plan |
| NBFC | Non-bank Finance Companies |
| NBF | New Bank Fund |
| NCSS | National Clearing and Settlement System |
| NDFC | National Development Finance Corporation |
| NDP | National Drainage Program |
| NEPRA | National Electric Power Regulatory Authority |
| NGOs | Non-government Organizations |
| NHA | National Highway Authority |
| NRB | National Reconstruction Bureau |
| NSS | National Saving Schemes |
| NTDC | National Transmission and Distribution Company |
| OCR | Ordinary Capital Resources |
| OGDCL | Oil and Gas Development Corporation |
| OGRA | Oil and Gas Regulatory Authority |
| PCR | Project Completion Report |
| PEFG | Pakistan Export Finance Guarantee |
| PEPCO | Pakistan Electric Power Company |
| PFC | Province Finance Commission |
| PHED | Public Health Engineering Department |
| PICIC | Pakistan Industrial Credit and Investment Company |
| PIDA | Provincial Irrigation and Drainage Authorities |
| PIDs | Provincial Irrigation Departments |
| PMS | Portfolio Management Seminar |
| PMU | Project Management Unit |
| PNSC | Pakistan National Shipping Corporation |
| P & D | Planning and Development Department |
| PR | Pakistan Railways |
| PRA | Petroleum Regulatory Authority |
| PRGF | Poverty Reduction Growth Facility |

| | |
|--------|--|
| PRG | Partial Risk Guarantee |
| PRM | Pakistan Resident Mission |
| PRPA | Poverty Reduction Partnership Agreement |
| PRSP | Poverty Reduction Strategy Paper |
| PTA | Pakistan Telecommunication Authority |
| PPTA | Project Preparatory Technical Assistance |
| RETA | Regional Technical Assistance |
| RFSDP | Rural Finance Sector Development Program |
| RSDP | Road Sector Development Program |
| SARD | South Asia Regional Department |
| SAP | Social Action Program |
| SBA | Standby Arrangement |
| SBP | State Bank of Pakistan |
| SECP | Security and Exchange Commission of Pakistan |
| SME | Small and Medium Enterprise |
| SMEDA | Small and Medium Enterprise Development Authority |
| SMETEF | Small and Medium Enterprise Trade Enhancement Facility |
| SSGC | Sui Southern Gas Company |
| SNGPL | Sui-Northern Gas Pipelines Ltd |
| TA | Technical Assistance |
| TCF | Trillion Cubic Feet |
| TEPI | Trade, Export Promotion and Industry Program |
| TMA | Tehsil Municipal Administration |
| WAPDA | Water and Power Development Authority |
| WASA | Water and Sanitation Authority |
| WSS | Water Supply and Sanitation |
| WTO | World Trade Organization |
| ZTBL | Zarai Tarraqiati Bank Ltd |

NOTES

Currency Equivalents (As of 3 October 2003)

| Currency Unit | — | Pakistan Rupees (PRe/PRs) |
|---------------|---|---------------------------|
| PRe 1.00 | = | \$0.0168 |
| \$ 1.00 | = | PRs 59.40 |

The fiscal year (FY) of the Government ends on 30 June. FY before a calendar year denotes the year in which the fiscal year ends, e.g., FY2002 ends on 30 June 2002. All year figures without the prefix "FY" are calendar years.

In this paper, "\$" refers to US dollars.

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OVERVIEW

A. The Setting

The Government of Pakistan's development strategy and the Economic Revival Program of 1999 identified four priority areas: revitalizing the agriculture sector, promoting small and medium scale industries, expanding the oil and gas sector and promoting information technology. Good governance was specified by the Government as a cornerstone of the economic revival program.

As a precursor to a comprehensive Poverty Reduction Strategy Paper (PRSP), the Government prepared the Interim Poverty Reduction Strategy Paper (IPRSP) in November 2001 as a strategy to establish future development priorities, and as an input for the International Monetary Fund (IMF) Poverty Reduction Growth Facility (PRGF), the Government committed to increase pro-poor expenditures, through budgetary readjustments, annually by 0.2 percent of GDP to 4 percent of GDP by 2004. Specific programs for poverty alleviation, good governance, enhanced tax collection and decentralization were also initiated by the Government under the IPRSP. The draft PRSP (summarized version) was published in May 2003, which has the following five pillars: accelerating economic growth and maintaining macroeconomic stability; investing in human capital; augmenting targeted interventions; expanding social safety nets; and improving governance.

Between 1999 and 2002 the real Gross Domestic Product (GDP) in Pakistan grew between 3 and 4 percent per annum - barely adequate to meet the rising needs of its population that is growing at the annual rate of 2.2 percent. The per capita income fell from \$ 457 in FY 1998 to \$419 in FY2002. The low economic growth was largely due to lack-luster performance of the agriculture sector, where a third successive year of water shortages took its toll on the production of major crops, and the stagnation of the manufacturing sector due to the uncertainty prevailing in the economic and political environment.

Just as the economy was beginning to recover from the setback due to international economic sanctions imposed since the nuclear tests of May 1998, the events of September 11, 2001 initially deteriorated Pakistan's fiscal and external balances. Through much of FY2002 the already intractable economic conditions were further confounded due to the conflict in Afghanistan and border tensions with India. However, the Government moved ahead in implementing vital governance, financial and economic reforms, which helped in restoring Pakistan's credibility with the international community. The successful completion of the IMF supported Standby Arrangements (SBA) and the agreement on the Poverty Reduction and Growth Facility (PRGF) was a major achievement for the government. This was followed by the

1. However, the growth performance improved in FY 2003, with the GDP registering a growth rate of 5.1 percent.

lifting of economic sanctions by international donors in late 2001, resumption of bilateral assistance from key donors and greater access to G-7 markets.

A significant accomplishment in the period was the debt restructuring agreement reached with the Paris Club in December 2001, which would free up scarce resources for development and poverty reduction and thus make it possible for Pakistan to achieve sustained growth earlier than would have been otherwise possible. During this period the exchange rate also remained stable and gross foreign exchange reserves (including foreign currency deposits held by commercial banks) rose to more than \$10 billion by end December 2002 (equivalent to about 11 months of imports) the highest level ever for Pakistan. This was mainly due to a substantial rise in workers' remittances and higher levels of official transfers. Moreover, greater scrutiny of balances held abroad by Pakistani nationals and the clamp down on informal channels of international money transfer aided the surge in receipt of official remittances.

General elections were held in the country in October 2002 and the Pakistan Muslim League (Quaid-i-Azam Group) succeeded in forming the government at the Center and in one province, while being a part of a coalition government in two other provinces. The newly elected governments have expressed their commitment to continue the reform process that began three years ago. Mr. Zafrullah Khan Jamali, the newly elected Prime Minister of the country, has retained Mr. Shaukat Aziz as the Minister of Finance, and Mr. Hafeez Shaikh, the former Finance Minister of Sindh, has been appointed as Minister of Privatization. Meanwhile local governments that were formed on August 14, 2001 at the district,

tehsil and union council levels, following the devolution of power plan, are operational, in line with the mandate provided under the Local Government Ordinance, 2001.

The economy's overall performance improved significantly in FY2003. The gross domestic product (GDP) growth rate is estimated at 5.1 percent compared with 3.4 percent in FY2002. The higher growth was made possible by strong performance in all sectors of the economy: 4.1 percent growth in agriculture, 5.4 percent in industry (7.7 percent in manufacturing), and 5.3 percent in services. Supported by the sharp fall in interest rates, total investment increased to 15.5 percent of GDP in FY2003, and the fiscal deficit declined to 4.6 percent of GDP. For the first 9 months of FY2003, inflation declined to 3.3 percent; exports and imports increased by 16.6 percent and 21.9 percent respectively; and workers' remittances increased to \$3.1 billion from \$1.5 billion during the same period in the last fiscal year. As a result, the current account surplus, excluding official transfers, increased to \$2.6 billion compared with \$1.0 billion during the same period in the last fiscal year. The foreign exchange reserves with the State Bank of Pakistan (SBP), at \$9.8 billion on 31 August 2003, have increased to 8 months of imports.

A. The ADB in Pakistan

ADB and Pakistan have been partners in development for over 30 years. From the time that the first loan was extended by ADB in 1968, cumulative assistance of \$ 12.609 billion has been provided to Pakistan to-date for 191 loans.² Of this, approximately 52 percent was provided from the Asian Development Fund (ADF) the Bank's

2. Excluding the \$ 1.1 billion of approvals that were cancelled, mostly due to loan savings percent.

Table 1: ADB's Lending to Pakistan by Sector
(As of December 2002)

| Sector | Cumulative Total Lending | | | Net Ongoing Loan Amount | | |
|-----------------------|--------------------------|-----------------|------------|-------------------------|----------------|------------|
| | No. | \$ Million | % | No. | \$ Million | % |
| Agriculture | 59 | 3,684.6 | 29.0 | 15 | 1,352.1 | 30.7 |
| Energy | 45 | 3,062.0 | 24.0 | 5 | 686.4 | 15.6 |
| Finance | 25 | 1,693.0 | 13.5 | 3 | 266.0 | 6.0 |
| Industry | 9 | 798.4 | 6.5 | 4 | 157.0 | 3.6 |
| Social Sectors | 28 | 1,260.0 | 10.0 | 12 | 544.2 | 12.4 |
| Transport | 14 | 1,117.0 | 9.0 | 5 | 485.5 | 11.0 |
| Governance | 7 | 661.0 | 5.0 | 7 | 661.1 | 15.0 |
| Others & multi-sector | 4 | 333.0 | 3.0 | 2 | 250.0 | 5.7 |
| Total | 191 | 12,609.0 | 100 | 53 | 4,402.3 | 100 |

concessional financing, the remaining 48 percent came from ADB's Ordinary Capital Resources (OCR). More than \$9.0 billion had been disbursed till December 2002. Additionally, the ADB has also provided grant technical assistance of nearly \$100.0 million for 253 projects to Pakistan for project preparation, capacity building and training.

Over the period 1999-2002 the average annual lending to Pakistan has been around \$800 million up from approximately \$500 million each year for the four year period between 1994-97. During the same period the country received an average of \$250 million of ADF funding annually, making it one of the largest ADF borrowers amongst developing member countries. In 2001, ADB's loan program was increased to \$957 million from \$707 million in 2000. The areas of assistance under this expanded program include: (i) improving economic efficiency and export performance, (ii) human and social development, (iii) governance and (iv) institutional strengthening. To operationalize the program, ADB provided major policy-based program assistance to support the Government's ambitious reform agenda while assisting the Government meet its needs for budgetary support. An additional \$100 million was also provided

for emergency drought relief assistance from loan savings in 2001.

To provide enhanced support to the Government for its reform program and poverty reduction initiatives, the loan program in 2002 was further expanded to \$1.1 billion comprising 7 loans, while the total grant assistance through 17 TAs was \$7.7 million. Fifty three public sector loans covering thirty eight projects for a net loan amount of \$4.4 billion were ongoing as of December 2002 while 57 TAs for a total of \$29.5 million were also ongoing. Moreover, 12 loan/equity projects for a total of \$50.0 million and two complementary projects for \$40.9 million were under implementation.

Project Portfolio Performance

In recent years ADB's portfolio of projects showed improvement as a result of continuing efforts by the Pakistan Resident Mission (PRM) and the Government to enhance portfolio performance by holding quarterly, federal and provincial level review meetings and through closer interactions with the executing agencies. Portfolio supervision as indicated by average supervision intensity showed improvement from 16.2 staff-days per project in 2000 to 21.4

staff-days per project during 2001 to 24.6 staff-days per project in 2002. This included organizing a Country Portfolio Review Mission (CPRM), a Portfolio Management Seminar (PMS) for senior government officials, regular quarterly Provincial Portfolio Review Meetings (PPRMs), loan reviews and Portfolio Management Workshops for project directors during the year. In dialogue with ADB, the Government also established a Task Force for monitoring project performance and resolving project/portfolio related issues that require federal Government's attention. To further improve project implementation capacity through greater ownership, and to ensure continuity through project processing to implementation, ADB has agreed with the Government on a new initiative to establish core project management units (CPMUs) for all new projects at the fact-finding stage. The Government, including all provincial governments, has agreed to establish revolving funds for funding CPMUs, prior to approval of projects, from 1 July 2003. This will facilitate actions to be taken for all startup activities. To strengthen the Government's existing capabilities for project monitoring and evaluation, ADB approved a TA on Strengthening Portfolio Performance and Monitoring in November 2002.³ A proposed \$ 150,000 TA during 2003 will aim to strengthen the financial management capacities of Project Management Units (PMU).

Disbursement, including for program loans continued to show improvement over the last three years. During 2002, the disbursement ratio was slightly down to 23.2 percent from 28.2 percent in 2001, and 27.5

percent in 2000. However, this figure still compared favorably against the ADB-wide average of 20.5 percent. Annual disbursements have averaged \$503.9 million in the last five years and for the year ended December 2002, the annual disbursement was \$501.4 million against a target of \$498.95 million including all on-going project loans and four on-going program loans. Contract awards for ADB projects in Pakistan have averaged \$376.0 million over the past five years, however, as of December 2002, the country portfolio projects achieved 101 percent in contract awards, which was \$424.6 million against the projection of \$420.0 million for 2002.

The net resource transfer from ADB to Pakistan has never been negative, however, a projected decline in the ratio of program lending in the total lending program projected for 2004-2006,⁴ with a corresponding increase in the ratio of investment lending with historically much lower disbursement rates, may have an implication on the level of this transfer.

With respect to portfolio performance during 2002,⁵ of the 53 projects/programs, forty four (83 percent) were judged to be satisfactory, eight (15.1 percent) partly satisfactory and one (2 percent) unsatisfactory. This is an improvement over portfolio performance during 2001 when out of 51 projects, thirty eight (74.5 percent) were judged to be satisfactory, and eleven (21.6 percent) were partly satisfactory. 'Problem loans' constituted 17 percent of the total project portfolio during 2002 compared to over 30 percent in 2001.

3. TA 3982-PAK: Strengthening Portfolio Performance and Monitoring for \$650,000 approved on 8 November 2002.

4. While the share of program loans in Pakistan's total portfolio has been unusually high in the past three years with ADB supporting a number of new reform initiatives undertaken by the Government, this ratio would have to go down progressively in future to bring it to the ADB-wide average of 25 percent.

5. Country Portfolio Review Mission (CPRM 2002).

Table 2: ADB Technical Assistance to Pakistan by Sector
(As of 31 December 2002)

| Sector / Subsector | Total TAs ^a | | | PPTAs | | | Active TAs as of December 2002 | | |
|-----------------------------|------------------------|-------------|------------|------------|-------------|------------|--------------------------------|-------------|------------|
| | No. | \$ Million | % | No. | \$ Million | % | No. | \$ Million | % |
| Agriculture | 80 | 35.25 | 35.3 | 51 | 19.05 | 52 | 7 | 3.7 | 12.5 |
| Energy | 29 | 11.3 | 11.3 | 8 | 1.4 | 3.8 | 4 | 3.3 | 11.2 |
| Finance/Industry | 38 | 11.8 | 11.8 | 4 | 2.4 | 6.5 | 12 | 6.6 | 22.4 |
| Social Infrastructure | 55 | 18.2 | 18.8 | 35 | 11.2 | 31 | 7 | 2.9 | 9.8 |
| Transport and Communication | 24 | 5.7 | 5.8 | 13 | 2.65 | 7.2 | 8 | 1.4 | 4.7 |
| Multisector/Others | 27 | 17.4 | 17.4 | | - | | 3 | 0.8 | 2.7 |
| Governance | | | | | | | 16 | 10.8 | 36.6 |
| All Sectors | 253 | 99.7 | 100 | 111 | 36.7 | 100 | 57 | 29.5 | 100 |

^a Excludes 8 cancelled TAs; 6 supplementary TAs are not counted as separate projects.

Whereas the overall objectives of most post-evaluated projects were met and their economic viability confirmed, a number of projects suffered from implementation delays. Implementation delays of post-evaluated projects had a variety of causes. External 'force majeure' factors played a major role and seriously interfered with projects especially in the energy, industry and finance sub-sectors. Of the factors within joint government/Bank control, deficiencies in project design were predominant among the causes of completion lags. A lack of time and resources (including TA) for sound project preparation produced tentative proposals and often resulted in a major revision in project costs. Another factor in completion lags was a lack of attention to training, especially in projects involving new technology. More often than not the training component was only partly completed.

Compliance with major loan covenants, particularly on timely submission of auditor's reports, continue to be satisfactory. For the 28 Pakistan projects due for compliance, the submission of 18 (64.3 percent) audit reports for FY2002 due on 30 June 2002, was on time, while only 6 (21.4 percent) were late. Of the remaining four, one report was

found to be in partial compliance while 3 did not comply. This is an improvement over FY2001 when the submission of only 33 percent of the due audit reports was on time while 50 percent audit reports was delayed.

ADB's Strategic Focus in 1999-2002

In the early years of operation in Pakistan ADB essentially focused on project financing for major infrastructure projects. However, during the last decade its development strategy has undergone significant changes. In the early 1990s, ADB concentrated on addressing the structural constraints to development faced by the country and supported the transformation of the economy to becoming a more export oriented one, in which the private sector would play a dominant role. By 1995 however the Bank's Country Operational Strategy (COS) signaled a major shift toward a greater emphasis on human development; the prominence of private sector participation and the need to address critical bottlenecks in physical infrastructure remained, but economic growth was supported as a complementary objective, to generate employment for a rapidly growing labor

force as well as to generate resources required for investment in human and physical capital. However, despite increased donor assistance, the emphasis on human resource development (HRD) in the country was constrained due to a weak absorptive capacity, shortages of counterpart funds, and the deteriorating economic situation.

It became necessary for the ADB to reassess its operational strategy following the economic and fiscal crisis in the aftermath of the 1998 nuclear tests. This led to the formulation of a two-year Country Operational Framework (COF) in 1999—an interim strategy aimed to take into account the changed economic and political realities. While the strategic objectives of the 1995 COS remained broadly valid, the COF focused more sharply on areas where the Government's commitment to reforms was strongest, and the development impact could be maximized given the scarce resources. These included: (i) improving economic efficiency and export performance, (ii) human and social development, (iii) governance and (iv) institutional strengthening. Under this broad framework, ADB provided major policy based assistance to support the Government in introducing macro level governance and economic reforms.

Country Strategy and Program (2002-2006)

In 2001, ADB initiated preparation of a new medium term country strategy and program for Pakistan, as it became evident that the country was moving into a new phase of structural reforms. ADB's efforts were guided by the fact Pakistan had undergone an economic crisis and there were various reasons to believe that the poverty level in the country, which had been increas-

ing through the 1990s was likely to have further increased in the post-1998 period. Poverty reduction has always been an important objective for the ADB and the Bank's Poverty Reduction Strategy approved in November 1999, articulated poverty reduction as its overarching goal.

The Poverty Assessment, published in August 2002, provided the basis for the Bank's Country Strategy and Program (CSP) for Pakistan for the period 2002-2006. The CSP was approved by the ADB Board in May 2002. The overall aim of the CSP is to support poverty reduction in the country through provision of assistance in priority areas of shared strategic interest and importance. Supporting good governance is a major focus of the Bank's medium term development strategy in Pakistan together with sustainable pro-poor growth with emphasis on rural areas and employment generation, and inclusive social development. The CSP also addresses cross-cutting concerns related to gender, environment, regional cooperation, and private sector development.

In September 2002 ADB and the Government of Pakistan signed a Poverty Reduction Partnership Agreement (PRPA) based on the CSP, which set out a shared vision for reducing poverty and key priorities for joint development cooperation to achieve this vision. To achieve reduction in poverty, the Government and ADB agreed on the following priorities: (i) improving quality of governance, including devolution of power to local communities, restructuring of government, and reform of the civil service, judiciary and the police; (ii) achieving broad-based growth through development of small and medium enterprise (SMEs) and a diversified agriculture sector; (iii) asset creation for the poor, especially women, through support of microfinance and rural development programs; (iv)

human development through education and health programs, with gender equality; and (v) social safety nets with targeted programs for vulnerable groups. These priorities were consistent with those of the Government's poverty reduction strategy that had earlier been laid out in the IPRSP, and are also now reflected in the draft PRSP.

Looking Ahead

The CSPU for 2004-2006, approved in August 2003, has affirmed that the strategic priorities outlined in the CSP continue to be relevant, are in line with the priorities of the new Government, and will therefore remain unchanged. To this end, ADB will support the deepening of the ongoing governance and macroeconomic reforms, through provision of assistance for second generation reforms at the provincial and sector levels. Gender reforms would be an integral part of the governance program and ADB's strategy would focus on supporting political, administrative, and fiscal initiatives to consolidate these reforms. ADB will continue to support effective relations between the non-government sector and provincial governments in respect of policy advocacy, in the implementation of the new institutional arrangements at the local level that provide for greater citizen involvement in the affairs of government; ADB will also aim to strengthen NGO engagement in the delivery of services.

With the expected improvement in economic growth, ADB will reinforce its emphasis on rural development and employment generation to ensure that the growth is pro-poor. An important addition proposed in ADB's strategy in this regard is its re-engagement in the water resources sector through province-focused projects on water conservation, drought mitigation, and rehabilitation of the irrigation infra-

structure. As regards inclusive social development, ADB's emphasis will remain on improving delivery of social services by supporting both increased public sector allocations made possible by enhanced fiscal space, and improved governance through strengthening devolution, sector administration, and financial management.

The CSPU proposes a lending program of \$2.7 billion (\$ 890 million per annum) for 2004-2006 for a total of 26 firm projects. Currently identified technical assistance for the same period amounts to \$16.1 million for 43 projects. In line with the focus on good governance in the strategy, the share of the lending program for 2004-2006 earmarked for governance has increased from 24 percent in the CSP to 34 percent in the CSPU. The lending program also envisages expanded assistance in the agriculture and rural development sector, and for crosscutting thematic priorities of subregional cooperation and sustainable environment management. The focus on assistance in the social sectors, the transport and communication sector, and the energy sector, also continues under the CSPU. The proposed 2003 program comprises seven firm loans for a cumulative value of \$720 million, of which \$230 million will be provided from the concessional ADF window. In addition, \$6.7 million will be provided in grant assistance for 19 TAs during 2003 (which includes cofinancing support of \$1.4 million from other donors).

The nine sectors that are covered in the following sections are: (i) agriculture and rural development, (ii) water resources, (iii) water supply & sanitation and urban development, (iv) finance, (v) social sectors including education, health and population, (vi) trade and industry, (vii) governance, (viii) energy, and (ix) transport and telecommunications.

AGRICULTURE AND RURAL DEVELOPMENT

| | | |
|--|---|-------------------|
| ADB Lending to the Sector 1968-2002 | : | \$3,684.6 million |
| Percentage of ADB Lending to PAK 1968-2002 | : | 29% |
| Ongoing Loan Amount as of 31 Dec 2002 | : | \$1,352.1 million |
| Disbursement as of 31 Dec. 2002 | : | \$600.99 million |
| Percent Disbursed as of 2002 | : | 42% |

Background

The estimated 97 million rural population of Pakistan is spread over 14.3 million households. Agriculture is the most important sector for employment and income generation in the country, particularly in rural areas, where about 70 percent of the poor live. They include landless laborers, tenant farmers, and small farmers cultivating marginal land or small holdings below 2 hectares. The sector includes forestry and fisheries and accounts for about 26 percent of real GDP and about 50 percent of employment. Growth in the sector has slowed down considerably from an average of 4.3 percent in the 1990s to 1.4 percent in 2002. Other than declining output of major crops, lack of protection from price volatility, increase in cost of inputs including fertilizer and fuel, and the prevailing drought conditions have exacerbated this decline. According to calculations by the Federal Bureau of Statistics (FBS) based on Pakistan Integrated Household Survey (PIHS) data, the head count estimate of rural poverty in 1999 was 36.3 percent.⁶ The incidence of rural poverty is likely to have become worse in the last three years as employment has moved towards non-farm related activities. This is apparent in falling rural per capital real cash, as farmers opted to cut down production and defer their expenditure on development activities.

The core problems in the sector are low productivity and profitability. The major causes of low productivity and profitability include low quality inputs, imperfect commodity markets, insecure land tenure, poor quality support services (research and extension), inefficient water resource management, poor delivery and sustainability of agriculture finance, inadequate rural infrastructure and deteriorating natural resources. Persistence of poverty in the rural areas is also closely linked to the highly skewed and unequal pattern of land distribution, with an accompanying need for land reform. A supportive policy and institutional environment for meaningful private investment in the sector has also been absent.

Government Policy and Institutional Framework

The key objectives of government policy are to achieve robust and sustainable growth in the agriculture sector through efficient import substitution, export orientation and enhanced productivity. The Government's strategy⁷ has set targets at achieving an annual rate of production increase averaging 5 percent and achieving food security and self-reliance by 2010. The main elements of its strategy are to enhance per hectare productivity through price incentives,

6. The draft Poverty Reduction Strategy Paper prepared by the Ministry of Finance in May 2003, gives the overall incidence of poverty as 32.1 percent in 2001.

7. As presented in "Agricultural Strategies for the First Decade of the New Millennium" approved in March 2001.

support services and market reforms. Its focus will be on increasing the production of wheat, cotton and rice through remunerative market-based prices, evolving new technologies, help improving marketing and storage facilities both in the public and private sectors and providing access to optimum technologies to farmer. Another element of government policy is to increase per unit yields in the agriculture sector and increase the production of high value added non-traditional crops like edible oil and tea etc. Moreover the Government is encouraging corporate agriculture to bring vast tracks of uncultivable land under cultivation and increase the flow of credit to the sector. Water management is another component of agriculture strategy, with renovation and desilting of canals and lining of water-courses as its immediate priorities. For livestock and fisheries the emphasis is on enhancing quality and productivity through genetic improvement, ensuring availability of feed and fodder and comprehensive disease control.

The federal Ministry of Food, Agriculture and Livestock (MINFAL) is responsible for economic coordination and policy planning of agriculture, food security, livestock and fisheries activities. The provincial agriculture departments have primary responsibility for implementation of the policy framework, extension services and livestock. Agricultural support services are provided by both the private and public sectors while agricultural production is almost entirely a private sector activity. Thus planning, coordination, basic research and high-level manpower training are the responsibilities of MINFAL. Distribution of inputs including fertilizer and seeds⁸ are handled by both the public and private sectors, while fertilizer imports are made

entirely by the private sector. The procurement of wheat is handled by the public and private sectors while all other commodities are handled by the private sector. Agriculture prices are meant to be market based; however government intervention in agriculture markets remains somewhat excessive, particularly in the form of price subsidies for wheat.

The SBP traditionally provided credit to farmers and sector activities through the Agriculture Development Bank of Pakistan (ADBP), the cooperative banks and nationalized commercial banks. In 2000 the Government set up the *Khushhali* Bank with assistance from ADB⁹ - a micro-finance institution with the mandate to act as facilitator and micro-finance manager to expand the network of microfinance in the country.

In the case of rural development projects, the provincial planning and development departments provide overall project supervision and coordination through project management units. The implementing agencies are typically the provincial line departments and large NGOs.

History of ADB's Operations and Implementation Experience

During the 1970s and 1980s ADB's lending program to the Agriculture sector was very broad in scope and included assistance to agriculture credit, fertilizer production and supply, cash crops, and storage. Loans covered a wide range of sub-sectors, including agro-Industry and industrial crops about (5 percent), agriculture support facilities e.g., credit, storage, agricultural inputs, marketing, and exten-

8. There are about 300 private seed companies including four multinationals.

9. Loans PAK-1805 & 1806 (SF) - Microfinance Sector Development for \$200 million approved on 13 December, 2000.

sion, (77 percent), and integrated areas development (18 percent). During the 1980s 36 percent of total lending in the sector was provided for three program loans (Agriculture Inputs Program, Crop Intensification Program, and Agriculture Program).¹⁰ However, since the late 1980s, the program was made more focused, and during the 1990s ADB had varied and extensive involvement in the agriculture sector comprising 18 projects and 28-29 percent of the annual lending, aimed at: (i) enhancing agricultural productivity, (ii) promoting market-oriented policy reforms, (iii) strengthening the institutional framework and (iv) developing resource-scarce areas of the country.

On the policy side, assistance was focused largely on sector specific reforms, budgetary support, creation of a free market for agriculture inputs and outputs, and strategic investment to revitalize the sector. This was accomplished through the Agriculture Sector Program Loan I (ASPL-I) of \$ 200 million (1990-1994) and a number of community based multi-sectoral area development projects that provide communities, in less developed areas an opportunity to improve their quality of life through provision of infrastructure and community organization. Moreover assistance was provided during 2000 through the Forestry Sector Project¹¹ for the implementation of the Forestry Sector Master Plan, which had earlier been prepared with ADB assistance in 1992.

The ASPL-I was less than successful in

the achievement of its objectives¹² due to the fact that it was based on insufficient sector analysis, contained too many reform measures and covered too many sub-sectors broadly. Consequently, although major policy reforms were undertaken within the project context, their implementation was only partial and their impact, not significant. For instance: (i) while market prices of fertilizer were deregulated, the subsidy to the fertilizer producers in the form of lower gas tariffs did not change, (ii) Support prices of wheat and other commodities was raised, but these were not raised up to their levels in the international markets. Moreover, although a wealth-tax based on the agriculture land-produce index was imposed, there was insufficient collection due to inadequate capacity. One of the key lessons learnt from ASPL-I was that policy reforms in agriculture should be undertaken in a step-by-step manner and require a longer term (5-10 years) commitment, particularly in a highly traditional society like Pakistan (with politically well connected landholders and vested interest groups).

Various Bank assessments and review missions also found that rural development projects in the past focused more on technical and engineering aspects and did not give adequate attention to the legal, political, institutional and the socio-cultural environment. A number of them¹³ also experienced delays and revisions in design and scope due to (i) limited availability and untimely release of local funds, (ii) late starts and protracted implementation delays due to political disruption and security problems,

10. Loan 825-PAK(SF)/826-PAK: Agriculture Inputs Program for \$150 million approved on 18 December, 1986; Loan 438-PAK(SF): Crop Intensification Program for \$14 million approved on 12 December, 1979; and Loan 1062-PAK(SF): Agriculture Program for \$200 million approved on 11 December, 1990.

11. Loan 1403-PAK(SF): Forestry Sector Project for 42.6 million approved on 9 November 1995.

12. PPA PAK-22272: Program Performance Audit Report on the Agriculture Program Loan 1062 - Agriculture Program, October 2000.

13. Loan 1012-PAK(SF): Second Barani Area Development Project for \$25 million approved on 20 February 1990, Loan 1179-PAK(SF): NWFP Barani Area Development Project for \$32.8 million approved on 24 September 1992

(iii) design deficiencies arising from lack of information or poor understanding of social conditions. Moreover it was felt that to have an impact, rural development projects should be implemented through a phased approach, participatory impact assessments should be carried out from time to time and the designed M&E systems should be simple and not beyond the comprehension of project implementation entities.

Lessons learned also include the need for active participation of all beneficiaries (landowners, tenants and livestock farmers) through formal agreements with communities and Country Based Organizations (CBOs) and to encourage the expanded role of women in sector activities. Project experience also showed that ownership of the development activities and its operations and maintenance by the communities is essential for sustainability.

ADB's Program and Future Strategy for the Sector

Consistent with the Government's assessment ADB considers agriculture as the vital sector for employment generation and poverty reduction. Reforms to achieve a sustainable production and marketing system, modernization and diversification to improve competitiveness and higher value addition, and a supportive policy and institutional environment for private investment are considered key elements to realize the employment generation potential of the sector. The ADB CSP for Pakistan links poverty reduction to improved social services, and growth in agriculture, rural development, and microfinance sectors among others.

ADB's current strategy is to continue a sustained policy dialogue at the national, provincial, and district government levels, as well as civil society and the private sector, to facilitate progressive increase in agriculture productivity and profitability. It aims to improve rural livelihoods through enhanced focus on addressing issues in governance through capacity building and building up of socio-economic capital. Another element of the present strategy is to promote technology appropriate for the poor, and prioritize necessary infrastructure investments in the sector.

Research shows that yield gaps in agriculture are significant between farmers who have access to institutional credit and those that don't. After the successful setting up of the *Khushhali* Bank in 2000 under the Microfinance Sector Development Program, the ADB has undertaken a major initiative under the Rural Finance Sector Development Program¹⁴(RFSDP) to set up an accessible, affordable and sustainable rural finance system that will help the middle and lower end of the rural market to benefit from economic opportunities for increasing income and employment. This initiative is expected to provide the necessary impetus to the economic climate in rural areas where income levels are one-third less than those in urban areas.

Restructuring and privatization of inefficient and loss-incurring agriculture and rural finance institutions, is another feature of ADB's strategy in the sector. Historically the Agriculture Development Bank of Pakistan, the primary rural finance institution with the largest borrower base, suffered from financial and liquidity problems due to poor governance, subsidized

14. Loan 1987 & 1988 PAK(SF) - Rural Finance Sector Development Program (RFSDP) for \$250 million approved on 20 December 2002.

lending and politicization of its loan monitoring and recovery operations. In 2002 ADBP was incorporated as the *Zarai Tarraqiati Bank Ltd* (ZTBL) under the Companies Ordinance as part of the ADB assisted Microfinance Sector Development Program (MSDP). This was the first step towards restructuring ADBP to re-focus its operations towards the lower end of the rural finance market, under the RFSDP.

Community based and multi-sector area development projects focusing on farm and non-farm income generating opportunities for poverty reduction are part of ADB's present strategy. Assistance is being provided¹⁵ to regions with the highest concentration of the poor i.e. Bahawalpur (36 percent) and D G Khan (24 percent) in Pakistan to increase income levels and the quality of life in these areas. In implementing these projects the strategy will be to ensure beneficiary involvement at all stages of project preparation and implementation as a pre-requisite to enhanced capacity building and for each component to define the exact role of the communities, private sector, CBOs/NGOs and in particular government agencies, given their limited financial resources and administrative constraints.

In the forestry sub-sector the ADB's strategy is based on measures to implement the Forestry Sector Master Plan approved in December 1992. It supports policy towards protection, production and participation, strengthen institutional capacity to sustainably manage forests and rangelands, involvement of communities in rehabilitation of degraded areas, and conservation of

biodiversity and protection of the ecosystems.

Key Features of Ongoing and Future Loans/TA in the Sector

Present ADB lending to the Agriculture sector is almost 29 percent of total lending. A second program loan the - \$ 350 million ASPL-II¹⁶ (2001-2005) was approved in 2001 with the foremost aim of implementing some of the key sector wide reforms that were initiated under the ASPL-I. It addresses some major constraints and aims to assist in enhancing the sector's ability to provide a sustainable means of livelihood to half of the country's labor force. A five-year period of implementation is planned with three loan tranches to be carefully sequenced in accordance with Government commitments to implement the Program. It is envisaged that three years will be required for implementation of the core policy agenda while an additional two years will be required to allow flexibility and ensure adequate monitoring. This includes further liberalization of the markets for agriculture inputs and products, increasing the role of the private sector in marketing and storage of principal agricultural commodities, and increase competition with a special focus on small and marginal farmers.

Ongoing integrated rural development projects account for about 22 percent of the current agriculture sector portfolio.¹⁷ These include the four area development projects in regions with a high incidence of rural poverty, namely: the DG Khan Rural Development Project, Bahawalpur Rural

15. Loan 1467-PAK(SF): Bahawalpur Rural Development for \$38 million approved on 26 September 1996; Loan 1531-PAK(SF): Dera Ghazi Khan Rural Development for \$36 million approved on 4 September 1997; Loan 1672-PAK(SF): Malakand Rural Development for \$41 million approved on 18 March, 1999.

16. Loans: PAK(SF) 1877, 1878, Agriculture Sector Program II for \$348 million and PAK (SF)1879 Agriculture Sector Program II (TA loan) for \$2.0 million approved on 13 December 2001.

17. Excluding water resources projects.

Development Project, Malakand Rural Development Projects, and the NWFP Barani Area Development Project II.¹⁸ Activities under these projects include the improvement of irrigation infrastructure and roads in the area, village development services, access to financial services and economic and marketing activities, community development, and organizational and skills training for the beneficiary communities, particularly women.

In the forestry sector the ADB is supporting the Government's effort towards expanding the forest resources in the NWFP, which has the largest area of the country's productive forest resources. The outputs of the \$ 42.6 million Forestry Sector Project¹⁹ includes a resource inventory and management planning strategy, legal reforms, institutional strengthening of the forestry department and physical development of 25 sub-projects for afforestation and reforestation. Project activities include (i) enhanced protection of forests, (ii) sustainable harvesting of natural and man-made forests, and (iii) involvement of communities in formulation and implementation of forestry development work.

As mentioned earlier, a key accomplishment of ADB's assistance has been the setting up of the *Khushhali* Bank - the primary micro-finance institution (MFI) in the country. It aims to benefit the urban and rural poor through income generation activities/small-scale enterprise and small infrastructure projects. The *Khushhali* Bank is a public-private enterprise that aims to catalyze sector growth in partnership with NGOs.

A \$50 million project for Rural Development in Sindh was approved in October 2002 to build management capacity of district governments and civil society through partnership with NGOs/CBOs. It will enhance rural development within a framework that supports the Government's devolution initiative for people-centered, rights and responsibility-based and service oriented government structures. The project also focuses on improving social and economic status of tenants and marginal farmers, women and artisans. A \$52 million integrated rural development project in *barani* (rain-fed) areas in NWFP was approved in November 2000, while a similar project for \$ 60 million in *barani* areas of Punjab is in the pipeline for 2004. These rural development projects aim to strengthen the rural asset base; enhance infrastructure; and are expected to lead to sustainable natural resource management; with an improved governance environment through more community participation and management of resources. A TA for FATA Rural Development was approved in 2002,²⁰ which will lead to a \$40 million loan in 2003 for the FATA Rural Development Project. This project aims to enhance opportunities for rural economic growth through mainstreaming of poorer and less-developed areas in the tribal belt, which lag behind the rest of Pakistan in almost all socioeconomic indicators.

A \$100 million Agriculture Diversification and Agribusiness Development project is also in the pipeline for 2004 with the aim of increasing private sector investment and development to maximize agribusiness opportunities in

18. See footnote 15 above.

19. Loan 1403 PAK(SF): Forestry Sector Project for \$56 million approved on 9 November, 1995.

20. TA-3984: Federally Administered Tribal Areas (FATA) Rural Development for \$750,000 approved on 13 November 2002.

high value crops. The 2005 loan pipeline includes a \$70 million Balochistan Rural Development and Drought Mitigation Project, and a \$ 60 million Sindh Coastal and

Inland Community Development Project. The 2006 pipeline also includes a forestry sector project in Sindh for \$30 million.

List of Approved Loans in the Agriculture & Rural Development Sector
(as of 31 December 2002)

| Loan No. | Project Name | Net Amount (\$ million) | Milestone Dates | | Implementation Period (years) | | |
|----------|--------------|----------------------------|---|----------------|----------------------------------|-------------|-------|
| | | | Approval | Date Closed | | | |
| 1 | 0034 | Rice Milling | 3.120 | 25-Aug-70 | 2-May-78 | 7.69 | |
| 2 | 0054 | Fisheries Development | 5.133 | 22-Dec-70 | 29-Jan-76 | 5.11 | |
| 3 | 0171 | SF | Multan Fertilizer | 7.750 | 19-Dec-73 | 29-Sep-78 | 4.78 |
| 4 | 0172 | SF | Multan Fertilizer | 19.250 | 19-Dec-73 | 19-Sep-78 | 4.75 |
| 5 | 0252 | SF | Mirpur Mathelo Fertilizer | 11.738 | 18-Dec-75 | 11-Oct-84 | 8.82 |
| 6 | 0253 | SF | Mirpur Mathelo Fertilizer | 35.603 | 18-Dec-75 | 11-Oct-84 | 8.82 |
| 7 | 0330 | SF | Chashma Right Bank Irrigation | 31.500 | 15-Dec-77 | 11-Jul-89 | 11.58 |
| 8 | 0428 | SF | South Rohri Fresh Groundwater Irrigation | 32.844 | 27-Nov-79 | 22-Jan-92 | 12.16 |
| 9 | 0433 | SF | Aquaculture Development | 14.100 | 6-Dec-79 | 21-May-90 | 10.46 |
| 10 | 0438 | SF | Crop Intensification Program | 12.562 | 12-Dec-79 | 11-Apr-86 | 6.33 |
| 11 | 0439 | SF | Baluchistan Livestock Development | 7.088 | 12-Dec-79 | 26-Sep-88 | 8.80 |
| 12 | 0494 | SF | Second Marine Fisheries Development | 26.351 | 11-Dec-80 | 26-Apr-94 | 13.38 |
| 13 | 0495 | SF | On-Farm Water Management | 21.718 | 15-Dec-80 | 4-Apr-89 | 8.31 |
| 14 | 0617 | SF | Agricultural Development Bank of Pakistan | 43.480 | 14-Dec-82 | 16-Jun-93 | 10.51 |
| 15 | 0619 | SF | Baluchistan Fisheries Dev Project | 32.692 | 21-Dec-82 | 26-Aug-91 | 8.68 |
| 16 | 0621 | SF | Sind Livestock Development Project | 9.130 | 21-Dec-82 | 9-Nov-89 | 6.89 |
| 17 | 0700 | SF | Left Bank Outfall Drain (Stage I) | 169.427 | 25-Oct-84 | 8-Jan-98 | 13.21 |
| 18 | 0723 | SF | Chashma Command Area Development Project | 40.343 | 13-Dec-84 | 21-Feb-95 | 10.20 |
| 19 | 0734 | SF | Gujranwala Agricultural Development Project | 30.544 | 19-Feb-85 | 21-Nov-94 | 9.76 |
| 20 | 0750 | SF | Small Dams Projects | 31.032 | 31-Oct-85 | 14-Mar-96 | 10.38 |
| 21 | 0772 | SF | Pat Feeder Canal Rehabilitation & Improvement Project | 162.151 | 17-Dec-85 | 3-Apr-00 | 14.30 |
| 22 | 0791 | SF | Cotton Development Project | 42.221 | 30-Sep-86 | 28-Jan-99 | 12.34 |
| 23 | 0800 | SF | Baluchistan Groundwater & Trickle Irrigation Project | 6.225 | 20-Nov-86 | 27-Aug-96 | 9.78 |
| 24 | 0810 | SF | Second Agricultural Development Bank of Pakistan | 40.116 | 4-Dec-86 | 17-Jul-95 | 8.62 |
| 25 | 0811 | SF | Second Agricultural Development Bank of Pakistan | 40.056 | 4-Dec-86 | 17-Jul-95 | 8.62 |
| 26 | 0825 | SF | Agricultural Inputs Program | 80.342 | 18-Dec-86 | 31-Dec-89 | 3.04 |
| 27 | 0826 | SF | Agricultural Inputs Program | 71.944 | 18-Dec-86 | 31-Dec-89 | 3.04 |
| 28 | 0837 | SF | Flood Protection Sector Project | 123.644 | 25-Aug-87 | 15-Apr-99 | 11.65 |
| 29 | 0838 | SF | Chitral Area Development Project | 17.679 | 27-Aug-87 | 29-Oct-97 | 10.18 |
| 30 | 0851 | SF | Fruit & Vegetable Marketing Project | 19.761 | 29-Oct-87 | 1-Feb-96 | 8.27 |
| 31 | 0871 | SF | Second On-Farm Water Management Project | 27.570 | 8-Dec-87 | 6-Jul-95 | 7.58 |
| 32 | 0874 | SF | Chasma Right Bank Irrigation Project (Stage II) | 48.163 | 10-Dec-87 | 9-Mar-95 | 7.25 |
| 33 | 0901 | SF | Khushab Salinity Control & Reclamation Project | 52.119 | 22-Sep-88 | 5-Mar-99 | 10.45 |
| 34 | 0916 | SF | Second Aquaculture Development Project | 11.206 | 3-Nov-88 | 29-Jul-96 | 7.74 |
| 35 | 0973 | SF | Livestock Development Project | 23.860 | 28-Sep-89 | 6-Jan-99 | 9.28 |
| 36 | 0976 | SF | Swabi Salinity Control & Reclamation Project | 95.615 | 26-Oct-89 | 31-Jan-00 | 10.27 |
| 37 | 1012 | SF | Second Barani Area Development | 22.830 | 20-Feb-90 | 24-Dec-98 | 8.85 |
| 38 | 1044 | SF | Agricultural Credit Project | 73.360 | 6-Nov-90 | 30-Jun-94 | 3.65 |
| 39 | 1062 | SF | Agriculture Program | 198.371 | 11-Dec-90 | 30-Jun-94 | 3.55 |
| 40 | 1076 | SF | Sindh Forestry Development Project | 23 | 33262 | 37287 | 11 |
| 41 | 1101 | SF | Kotri Barrage Rehabilitation Project | 16.710 | 26-Sep-91 | 27-Nov-00 | 9.18 |
| 42 | 1179 | SF | NWFP Barani Area Development Project | 31.404 | 24-Sep-92 | 1-Feb-01 | 8.36 |
| 43 | 1297 | SF | Third Punjab On-farm Water Management Project | 46.351 | 8-Mar-94 | 26-Aug-02 | 8.47 |
| 44 | 1350 | SF | Marala-Ravi Link Canal System | 2.803 | 31-Jan-95 | 30-Jul-98 | 3.50 |
| | | Subtotal/Average | 1862.671 | | | 8.63 | |

| Loan No. | Project Name | Net Amount (\$ million) | Milestone Dates | | Implementation Period (years) |
|-------------------------|--------------|--|-----------------|----------------|----------------------------------|
| | | | Approval | Date Closed | |
| Ongoing Loans | | | | | Age |
| 45 | 1146 SF | Chashma Right Bank Irrigation (Stage III) | 210.74 | 17-Dec-91 | 11.05 |
| 46 | 1294 SF | Pehur High-level Canal | 123.00 | 22-Dec-93 | 9.03 |
| 47 | 1403 SF | Forestry Sector | 20.62 | 9-Nov-95 | 7.15 |
| 48 | 1413 SF | National Drainage Sector | 164.66 | 12-Dec-95 | 7.06 |
| 49 | 1467 SF | Bahawalpur Rural Development | 34.85 | 26-Sep-96 | 6.27 |
| 50 | 1531 SF | Dera Ghazi Khan Rural Development | 35.19 | 4-Sep-97 | 5.33 |
| 51 | 1578 SF | Second Flood Protection Sector | 99.16 | 13-Nov-97 | 5.13 |
| 52 | 1672 SF | Malakand Rural Development | 41.74 | 18-Mar-99 | 3.79 |
| 53 | 1787 SF | North West Frontier Prov Barani Area Dev-phase I | 54.25 | 28-Nov-00 | 2.09 |
| 54 | 1805 SF | Microfinance Sector Development Program (MSDP) | 70.91 | 13-Dec-00 | 2.05 |
| 55 | 1806 SF | Microfinance Sector Development | 83.41 | 13-Dec-00 | 2.05 |
| 56 | 1877 SF | Agriculture Sector Program II | 129.15 | 13-Dec-01 | 1.05 |
| 57 | 1878 SF | Agriculture Sector Program II | 230.96 | 13-Dec-01 | 1.05 |
| 58 | 1879 SF | Agriculture Sector Program II - TA | 2.12 | 13-Dec-01 | 1.05 |
| 59 | 1934 SF | Sindh Rural Development | 51.32 | 20-Nov-02 | 0.11 |
| Subtotal/Average | | | 1,352.09 | | 4.28 |
| Total | | | 3,214.76 | | |

List of Approved TAs in the Agriculture and Rural Development Sector
(as of 31 December 2002)

| TA No. | Project Name | Type | Revised Amount (\$ million) | Milestone Dates | | Implementation Period (years) | |
|--------|--------------|---|-----------------------------|-----------------|-------------------|-------------------------------|-------|
| | | | | Approval | Financial Closing | | |
| 1 | 221 | Agricultural Processing Facilities Study | PP | 0.150 | 15-Dec-77 | - | - |
| 2 | 234 | Baluchistan Livestock Development | PP | 0.220 | 11-May-78 | 1-Aug-79 | 1.22 |
| 3 | 242 | Second Fisheries Development | PP | 0.350 | 24-Aug-78 | 1-Dec-87 | 9.28 |
| 4 | 318 | Aquaculture Development II | PP | 0.135 | 6-Dec-79 | 1-Dec-87 | 7.99 |
| 5 | 321 | Baluchistan Livestock Development | AO | 0.240 | 12-Dec-79 | 1-Dec-87 | 7.98 |
| 6 | 352 | On-Farm Water Management | PP | 0.132 | 21-May-80 | 1-Feb-81 | 0.70 |
| 7 | 364 | Sind Livestock Development | PP | 0.210 | 26-Aug-80 | 1-Oct-82 | 2.10 |
| 8 | 397 | Baluchistan Fisheries Development | PP | 0.350 | 23-Jan-81 | 1-Oct-82 | 1.69 |
| 9 | 403 | Forest Development | PP | 0.116 | 18-May-81 | 1-Sep-82 | 1.29 |
| 10 | 443 | Agro-Industries Credit | PP | 0.150 | 23-Dec-81 | 1-Jan-83 | 1.02 |
| 11 | 457 | Revised Chasma Right Bank Irrigation | PP | 0.240 | 20-Apr-82 | 1-Jun-83 | 1.12 |
| 12 | 486 | Foodgrain Storage | PP | 0.050 | 13-Sep-82 | 1-May-83 | 0.63 |
| 13 | 500 | Baluchistan Fisheries Development | AO | 0.250 | 21-Dec-82 | 1-Apr-91 | 8.28 |
| 14 | 539 | South Rohri On-Farm Water Management | AO | 0.400 | 9-Sep-83 | 1-Dec-89 | 6.23 |
| 15 | 543 | Small Dams | PP | 0.390 | 13-Oct-83 | 1-Jun-85 | 1.64 |
| 16 | 560 | Foodgrain Storage | AO | 0.150 | 6-Dec-83 | - | - |
| 17 | 596 | Left Bank Outfall Drain Stage 1 | PP | 0.250 | 15-May-84 | 1-Mar-89 | 4.80 |
| 18 | 612 | Baluchistan Groundwater Development | PP | 0.330 | 12-Jul-84 | 1-Dec-90 | 6.39 |
| 19 | 645 | Pat Feeder Canal Rehabilitation & Imp. Project | PP | 0.350 | 12-Dec-84 | 1-Dec-87 | 2.97 |
| 20 | 646 | Fruit & Vegetable Storage & Marketing | PP | 0.230 | 13-Dec-84 | 1-Dec-88 | 3.97 |
| 21 | 664 | Cotton Development Project | PP | 0.175 | 26-Dec-84 | 1-Dec-87 | 2.93 |
| 22 | 699 | Baluchistan Trickle Irrigation Project | PP | 0.225 | 21-Aug-85 | 1-Dec-87 | 2.28 |
| 23 | 708 | Master Plan for Barani Area Development (UNDP) | AO | 1.300 | 15-Oct-85 | 1-Mar-91 | 5.38 |
| 24 | 743 | Fisheries Sector Study | AO | 0.290 | 29-Jan-86 | 1-Dec-88 | 2.84 |
| 25 | 748 | Flood Control Sector Project | PP | 0.300 | 18-Feb-86 | 1-Dec-88 | 2.79 |
| 26 | 772 | Agricultural Inputs Program | PP | 0.053 | 5-Jun-86 | 1-Dec-88 | 2.49 |
| 27 | 803 | Chashma Right Bank Irrigation Project (Stage II) | PP | 0.285 | 8-Oct-86 | 1-Dec-88 | 2.15 |
| 28 | 804 | Livestock Sector Study | AO | 0.188 | 13-Oct-86 | 1-Dec-88 | 2.14 |
| 29 | 805 | Second On-Farm Water Management | PP | 0.239 | 16-Oct-86 | 1-Dec-88 | 2.13 |
| 30 | 826 | Savings Mobilization by ADBP | AO | 0.240 | 4-Dec-86 | 1-Mar-90 | 3.24 |
| 31 | 827 | Institutional Building of ADBP (UNDP Financed) | AO | 1.315 | 4-Dec-86 | 1-Aug-97 | 10.67 |
| 32 | 838 | Sind Forestry Development Project | PP | 0.150 | 22-Dec-86 | 1-Apr-91 | 4.28 |
| 33 | 882 | Strengt. Chick-Pea Research in Collab. with Icrisat | AO | 0.350 | 9-Jun-87 | 1-Mar-92 | 4.73 |
| 34 | 895 | Khushab Salinity Control And Reclamation | PP | 0.215 | 26-Aug-87 | 1-Apr-98 | 10.61 |
| 35 | 914 | Fruit & Vegetable Export Marketing Study | AO | 0.350 | 29-Oct-87 | 1-Feb-91 | 3.26 |
| 36 | 916 | Swabi Scarp (Co-Fin. Gov't. of Switzerland) | PP | 0.505 | 4-Nov-87 | 1-Aug-89 | 1.74 |
| 37 | 928 | Small-Scale TA for the Livestock Sector | PP | 0.075 | 27-Nov-87 | 1-Apr-98 | 10.35 |
| 38 | 935 | Fruit & Vegetable Marketing Project (UNDP Financed) | AO | 2.225 | 29-Oct-87 | 1-Apr-98 | 10.43 |
| 39 | 954 | Study of the Federal Bank for Cooperatives | AO | 0.350 | 12-Feb-88 | 1-Apr-91 | 3.13 |
| 40 | 1099 | Rural Dev. Strat for Sind Arid Zone(Co-Fin W/ UNDP & Swiss) | AO | 0.750 | 29-Dec-88 | 1-Dec-95 | 6.93 |
| 41 | 1149 | Seed Industry Development Project (JSF-Financed) | PP | 0.350 | 25-Apr-89 | 1-Feb-91 | 1.77 |
| 42 | 1170 | Forestry Sector Master Plan (Bank/JSF/UNDP) | AO | 2.400 | 22-Jun-89 | 1-Jan-97 | 7.53 |
| 43 | 1170 | Forestry Sector Master Plan (Bank/JSF/UNDP) | AO | 1.153 | 22-Jun-89 | 1-Jan-97 | 7.53 |
| 44 | 1173 | Chasma Right Bank-irrigation Proj (Stage III)(JSF-Fin) | PP | 0.575 | 7-Jul-89 | 1-Sep-91 | 2.15 |
| 45 | 1321 | NWFP Barani Area Development (JSF-Financed) | PP | 0.460 | 13-Jun-90 | 1-Dec-91 | 1.47 |
| 46 | 1357 | Barani Farming Sys. Training & Research (UNDP-Financed) | AO | 0.691 | 27-Jun-91 | 1-Aug-98 | 7.10 |
| 47 | 1406 | Loan & TA Grant - Domestic Resource Mobilization | AO | 0.600 | 6-Nov-90 | - | - |

| TA No. | Project Name | Type | Revised Amount (\$ million) | Milestone Dates | | Implementation Period (years) | |
|--------|--------------|--|-----------------------------|-----------------|-------------------|-------------------------------|-------------|
| | | | | Approval | Financial Closing | | |
| 48 | 1407 | Loan & TA Grant-Legal Services | AO | 0.071 | 6-Nov-90 | 1-Apr-98 | 7.41 |
| 49 | 1408 | Loan & TA Grant-Improved Tillage Technology | AO | 0.371 | 6-Nov-90 | - | - |
| 50 | 1438 | Loan/TA Study on Policies for Fertilizer Import/Marketing | AO | 0.300 | 11-Dec-90 | | 2.98 |
| 51 | 1450 | Land Resource Evaluation & Planning (JSF-Financed) | PP | 0.557 | 24-Dec-90 | - | - |
| 52 | 1468 | Loan & TA Grant - Institutional Strng of Sindh Forest Dept (TASF) | AO | 0.560 | 24-Jan-91 | 1-Apr-00 | 9.19 |
| 53 | 1477 | Third On-Farm Water Management Project (Swiss Gov't.) | PP | 0.098 | 4-Feb-91 | 1-Oct-91 | 0.65 |
| 54 | 1481 | Study of Crop-Based Irrigation in NWFP | AO | 0.860 | 19-Feb-91 | 1-Sep-97 | 6.54 |
| 55 | 1582 | Restoration & Improvement of Marala-Ravi Link System | PP | 1.150 | 23-Oct-91 | 1-Jan-96 | 4.19 |
| 56 | 1629 | Strengt. Env'l Mgt for Water Resources Dev.(JSF) | AO | 1.000 | 17-Dec-91 | 1-Apr-98 | 6.29 |
| 57 | 1709 | Pehur High-level Canal Project | PP | 0.745 | 3-Jun-92 | 1-Jan-96 | 3.58 |
| 58 | 1733 | Cholistan Development Project | PP | 0.350 | 17-Jul-92 | 1-Apr-94 | 1.71 |
| 59 | 1768 | Punjab Irrigation W Conservation (Sector) Project | PP | 0.600 | 20-Oct-92 | 1-Apr-98 | 5.45 |
| 60 | 1825 | SSTA for 3rd Punjab On-Farm Water Management | PP | 0.100 | 24-Dec-92 | 1-Apr-98 | 5.27 |
| 61 | 1927 | North West Canal Remodeling Proj. (JSF Financed) | PP | 1.300 | 16-Aug-93 | 1-Apr-98 | 4.63 |
| 62 | 1948 | Forestry Sector Project | PP | 0.560 | 9-Sep-93 | 1-Apr-98 | 4.56 |
| 63 | 2125 | Balochistan Groundwater Res. Reassessment | AO | 0.224 | 20-Jul-94 | 1-Dec-96 | 2.37 |
| 64 | 2384 | Forestry Dev. Project in Northern Areas | PP | 0.090 | 25-Aug-95 | 1-Apr-98 | 2.60 |
| 65 | 2452 | Irrigation Management | PP | 0.300 | 27-Nov-95 | 1-Apr-98 | 2.35 |
| 66 | 2562 | Second Flood Protection Sector (JSF) | PP | 0.800 | 30-Apr-96 | 1-May-99 | 3.00 |
| 67 | 2585 | Dera Ghazi Khan Rural Development (JSF) | PP | 0.600 | 10-Jun-96 | 1-Apr-00 | 3.81 |
| 68 | 2604 | Malakand Rural Development Project (JSF) | PP | 0.700 | 8-Jul-96 | 1-Apr-00 | 3.73 |
| 69 | 2918 | Balochistan Rural Development (JSF Financed) | PP | 0.800 | 24-Nov-97 | - | - |
| 70 | 2937 | Rural Microfinance (JSF-Financed) | PP | 0.600 | 12-Dec-97 | 1-Mar-01 | 3.22 |
| 71 | 3131 | Strengt. Farmer's Capacity in Small Dams Operations | AO | 0.149 | 15-Dec-98 | 1-Apr-01 | 2.30 |
| 72 | 3132 | Sindh Rural Development | PP | 0.800 | 22-Dec-98 | 1-May-01 | 2.36 |
| 73 | 3151 | NWFP Barani Area Development | PP | 0.500 | 31-Dec-98 | 1-Jul-01 | 2.50 |
| 74 | 3231 | Punjab Water Sector Development | PP | 0.150 | 30-Jul-99 | 1-Jan-00 | 0.42 |
| | | Subtotal/Average | | 34.836 | | | 4.15 |
| | | Ongoing TAs | | | | | |
| 75 | 2327 | Bhawalpur Division Area Development (JSF) | PP | 0.600 | 9-May-95 | 30-Sep-00 | |
| 76 | 3130 | Water Resources Strategy Study | AO | 0.650 | 15-Dec-98 | 30-Nov-02 | |
| 77 | 3229 | Agriculture Sector Program | PP | 0.350 | 20-Jul-99 | 30-Nov-02 | |
| 78 | 3383 | Integrated Pest Management | AO | 0.500 | 28-Dec-99 | 31-Jul-03 | |
| 79 | 3725 | Additional Preparatory Work on the Sindh Rural Development Project | PP | 0.150 | 24-Sep-01 | 30-Jun-02 | |
| 80 | 3984 | Federally Administered Tribal Areas Rural Development (JSF) | PP | 0.750 | 13-Nov-02 | 30-Oct-04 | |
| 81 | 4058 | Agribusiness Development | PP | 0.700 | 19-Dec-02 | 30-Nov-03 | |
| | | Subtotal | | 3.700 | | | |
| | | Total | | 38.536 | | | |

WATER RESOURCES

| | | |
|--|---|--------------------|
| ADB Lending to the Sector 1968 - 2002 | : | :\$1,505.8 million |
| Percentage of ADB Lending to PAK 1968 - 2002 | : | :12.0% |
| Ongoing Loan Amount as of 31 Dec 2002 | : | :\$597.56 million |
| Disbursement as of 31 Dec. 2002 | : | :\$345.9 million |
| Percent Disbursed as of 2002 | : | :53% |

Background

Pakistan's 16.2 million hectares of irrigated land supply more than 90 percent of the value of agricultural production in the country. The Indus Basin Irrigation System commands an area of 36.2 million hectares, and represents the world's largest contiguous irrigated system with large investments over the last two centuries in barrages, link canals and 43 major canal command areas. More recently investments in tubewells have led to an even wider use of groundwater. However, there has been a sharp deterioration in the quality of the irrigation and drainage system, due to geological deterioration of watersheds resulting in changes in hydrology, deforestation, waterlogging and salinity. Inefficient management of water systems and consequent low delivery efficiency and inequitable distribution, inadequate O&M, insufficient pricing and cost recovery, have lately plagued the sector.

Total installed hydropower capacity is 5,042 MW, which is approximately 50 percent of total installed capacity of the WAPDA owned system. Localized and widespread flooding is common in Pakistan despite the construction of reservoirs and major investments in flood protection. The main causes of flood are the progressive denudation of river catchments and the

general deterioration of the river channels from significantly reduced flows during non-flood season.

Government Policy and Institutional Framework

Water Management is a significant element of Government strategy for the agriculture sector, heightened by the drought in many parts of the country during recent years. Desilting of canals, lining of irrigation channels and watercourses and their renovation are immediate priorities. For rain-fed areas, schemes of water harvesting, utilization of small dams and rejuvenations of farmers' mini-dam schemes are already being implemented. In 1997, a major program, of institutional and policy reforms for improved water resource management, was initiated under the National Drainage Program (NDP)²¹ and Provincial Irrigation and Drainage Authorities (PIDA) were introduced in each of the four provinces.

The federal Government has the responsibility for coordination and policy formulation at the national level. National distribution of water and management of multi-purpose reservoirs on the Indus and its tributaries are also a federal responsibility. Otherwise the provinces administer their

21. Loan 1413-PAK(SF): National Drainage Sector Program for \$140 million approved on 12 December 1997. Co-financing for the NDP was provided by World Bank (\$285 million) and Government of Japan JBIC (\$100 million). Farmers Organizations will contribute \$32.1 million (4.1%) and Federal and the Provincial Governments will contribute \$227.9 million (29%).

own water sectors. The Ministry of Water and Power (MOWP) at the federal level has responsibility for the Water and Power Development Authority (WAPDA), of which the water wing has the task for irrigation and drainage projects throughout the country. Project executing agencies include provincial Departments of Irrigation and Public Health Engineering (PHED) and the departments of agriculture. WAPDA is generally responsible for water resource planning and development at the national level. Under the NDP, WAPDA only executes water sector projects of an inter-provincial nature unless at the request of the provincial authorities. The provincial departments are responsible for remodeling of the smaller distributaries and minor canals, and conversion of watercourses to minors. Provincial departments of agriculture are generally involved in implementation of agricultural development components.

The Federal Flood Commission (FFC) of the MOWP is the relevant agency for planning and implementation of major flood protection projects countrywide. Detailed engineering and construction of all flood protection works, collection of necessary planning data, design and construction of flood protection structures, and flood management is undertaken by Provincial Irrigation Departments (PIDs) and provincial PIDAs, which as autonomous institutions were to subsume the role and functions of the PIDs as a part of a general policy of decentralization under the NDP. A residual policy and regulatory role has been retained within the PIDs. For each main canal command area, semi-autonomous and financially accountable area water boards (AWB) have been

established with responsibility for irrigation and drainage development and management. At the next level down, the distributary canal, independent Farmers' Organizations (FO) will enter into contracts for water with the AWBs and will assume responsibility for management.

History of ADB's Operations and Implementation Experience

Historically, together with Finance/ Industry and Power the Water sector was one of the main areas of ADB involvement in Pakistan. Sector activities included irrigation, drainage, tubewells, watershed management and flood protection projects. During the 1980s and the 1990s the share of lending to the sector as a percentage of total lending to the country was between 16 and 18 percent. Focus of ADB assistance was the improvement and expansion of irrigation and drainage facilities, and construction of flood protection facilities through major irrigation projects in 1991²² and 1997²³ and flood protection projects in 1989²⁴ and 1992.²⁵ In the late 1980s, the ADB became the major donor to the sector, followed by the World Bank, and the Government of Japan. Small-scale irrigation and on-farm water management have also been supported through area development projects and on a stand-alone basis, respectively.

In the early 1990s the ADB's policy dialogue mainly focused on enhanced mobilization of resources and the efficient utilization of funds for O&M of infrastructure. The policy and institutional reform agenda, was closely coordinated with the

22. Loan 1146-PAK(SF): Chasma Right Bank Irrigation (Stage III) for \$185 million approved on 17 December, 1991.

23. Loan 1578-PAK(SF): Second Flood Protection for \$100 million approved on 13 November, 1997.

24. Loan 957-PAK: Flood Damage Restoration for \$44 million approved on 30 March, 1989.

25. Loan 1209-PAK: Flood Damage Restoration (Sector) for \$100 million approved on 15 Dec, 1992.

World Bank and was focused on the decentralization of water resources facilities, increased beneficiary participation in design and operation of facilities, better inter-agency coordination of planning and management of water resources development, and strengthening of environmental assessment and monitoring. The impact of the sector policy dialogue was mixed. While several increases in irrigation service fees were introduced, the poor collection performance limited their impact. Inadequate O&M, low cost recovery and inefficient operations and management in the system adversely affected the sector's performance and led to progressive deterioration of irrigation and drainage systems.

In the mid-1990s, under the ADB/World Bank funded NDP,²⁶ a major institutional reform package was agreed including: (i) development of a comprehensive national water resources policy; (ii) introduction of more efficient and effective institutional framework for sector management through creation of autonomous PIDAs, establishment of water boards, institutional reform of WAPDA's water wing, and participatory system management at the distribution canal level; (iii) increased resources mobilization for O&M through eventual self-financing of PIDAs, increase and rationalization of irrigation service fees, introduction of drainage charges, increased revenues for WAPDA's water wing, and transfer of O&M responsibility from on-farm irrigation/drainage to beneficiaries; (iv) increased efficiency of public sector institutions and expenditures; and (v) improved environmental management. However, progress under the NDP so far has been disappointing. While some measures, particularly related to PIDAs were implemented, policy improvements under the

NDP have been very slow in coming, due in part to delays in effectiveness of the Project. The lack of successful and timely implementation of NDP's policy agenda also demonstrated lack of Government's commitment to reform the sector and its institutions and thus the donors including WB and ADB limited the scope of assistance to the sector.

The average implementation period for closed projects in the sector was about nine years. According to four PPARs and PCRs, the main causes of implementation delays include insufficient counterpart fund allocations and releases; slow procurement; and incomplete designs and changes of scope. Experience with the ongoing portfolio confirms the generally slow pace of implementation of projects in the sector and significant upfront delays. Of nine ongoing loans approved for \$903 million from 1991 to 1999, only about 50 percent has been disbursed to date. This mainly affected two projects, namely Chasma Right Bank Irrigation and Pehur High Level Canal²⁷ which were delayed due to initial procurement problems, and the availability of counterpart funds. The effectiveness of the NDP was also delayed by two years due to a cross-effectivity condition with the approval of the World Bank's NDP. Also, disbursements will only be gradual given the civil works nature of most contracts.

In the past inclusion of detailed engineering design under investment loans for several large projects were also a reason for slow start. This has now been corrected with design of new projects carried out under engineering loans. The post-evaluated projects indicate a need for: (i) greater attention to the non-civil works aspects including post-construction follow-up; (ii) sufficient maintenance by beneficiaries; and

26. See footnote 18.

27. Loan 1294-PAK(SF): Pehur High Level Canal for \$127.6 million approved on 22 December, 1993.

(iii) effective extension services. The role of appropriate water pricing and service fees on production systems and resource use were also identified as essential to economic efficiency of irrigation investments.

Progress on the policy package promoted under the 1997 Second Flood Protection Project,²⁸ particularly with regard to the collection rates of the agriculture income tax, increased O&M allocations, and introduction of a flood cess, have also not been forthcoming, which has led to delayed implementation. Availability of counterpart funds for the NDP and Second Flood Protection projects will also require close monitoring once activities resume.

ADB's Program and Future Strategy for the Sector

The critical importance of the water resources sector to the country's economy and environment (90 percent of crop production depends on irrigated land) and the ADB's leading role in the sector, justifies a continued involvement in irrigation, drainage, and flood protection. This was further borne out through the ADB's assistance under NDP towards improving the sector's policy and institutional reforms that were expected to result in accelerated agricultural growth and poverty reduction.

Future ADB activities will pay greater attention to careful sector/preparatory work, status of ongoing portfolio, and, most importantly, the progress of the ongoing policy and institutional reform agenda and the Government's firm commitment to further changes. In this connection, the Water Resources Strategy Study²⁹ under an ADB financed grant TA prepared a national

water sector profile and developed a sector strategy for agriculture water resources, including institutional and management issues, social and financial issues and technical issues. It has also defined a medium-term investment plan (MTIP) to support decision making by international agencies including ADB, Japan Bank for International Cooperation (JBIC) and the World Bank. The MTIP comprises water resources development, irrigation drainage and flood protection, water supply and sanitation, environment and hydropower including policy support, institutional development and capacity building which will provide a direction for investment decisions of the ADB for the 2002-2005 period. The Study is expected to be approved by the Government in June/ July 2003.

Sustainability aspects will become the ADB's major strategic and operational concern in the water sector in Pakistan. Less emphasis on new lending activities should also translate in more stringent up-front requirements particularly with regard to sustainability aspects and deferment of new approvals until such requirements are met. Stricter enforcement of covenants would also need to be applied.

Key Features of Ongoing and Future Loans/TAs in the Sector

Future ADB investments in the water resources sector and related policy dialogue will focus on making the reforms initiated under NDP work, and lead to accelerated agriculture growth and poverty reduction. The underlying principle of these reforms is to decentralize the operation and maintenance functions and reduce government

28. See footnote 20.

29. TA 3130-PAK: Water Resources Strategy Study for \$650,000 approved on 15 December, 1998.

subsidies, in particular for irrigation and on-farm drainage. To support the efforts for reforms and improve overall water resource management, assistance for rehabilitation and improvement of irrigation and drainage systems will be selectively considered, as well as new water resources development initiatives within the context of rural development and poverty alleviation. The NDP envisaged activities in all the four provinces and the Water Wing of the WAPDA. Whereas progress of activities is quite good in Sindh and NWFP where in addition to the PIDAs, FOs have been formed, the progress is relatively slow in Punjab. Balochistan, which had opted out of the project earlier, has rejoined the NDP. ADB's assistance of \$140 million has been reduced to \$54 million because of reallocation for drought mitigation. The loan closing date has been extended to 31 August, 2004 due to diversion of funds towards emergency assistance for the Drought Impact Mitigation and

Recovery Component (DIMRC).

Because of the sector's huge financial requirements and the need to provide a sharper focus in the selection of new ADB investments, the recommendations of the Water Resources Sector Strategy Study with regard to water sector planning and management and its MTIP will direct future investments in the sector. An ADTA has been proposed in 2004 to engage in policy dialogue with the Government, to be followed by a series of province-specific water resource projects. The first allocation of \$170 million for this purpose has been made in 2006, while the order in which support to the individual provinces will be provided, is to be decided subsequently.

The list of approved loans and TAs for the Water Resources Sector is included in the list of approved loans and TAs in the Agriculture and Rural Development Sector.

RURAL WATER SUPPLY, SANITATION AND URBAN DEVELOPMENT

| | |
|--|-------------------|
| ADB Sector Lending 1968-2002 | : \$433.1 million |
| Percentage of Total ADB Lending to PAK (1968-2002) | : 4% |
| Ongoing Commitment as of 31 December 2002 | : \$165.0 million |
| Disbursements as of December 2002 | : \$147.2 million |
| Percent Disbursed | : 62% |

Background

Pakistan's population estimated at 149 million in 2003 is growing at about 2.15 percent per annum. The urban population of almost 53.3 million (39 percent) is estimated to be growing at 5 percent per annum reaching 115 million or 50 percent of the total population by 2020. Pakistan's water supply and sanitation infrastructure is inadequate to cope with the twin problems of a burgeoning population and the rapid pace of urbanization in the country. These have also resulted in uncontrolled and unplanned development of cities and towns, deteriorating environment and deficiencies of basic infrastructure. At present, the overall water supply coverage is 63 percent (83 percent in urban areas and 53 percent in rural areas) and sanitation 39 percent (59 percent in urban and 27 percent in rural areas), of the total population. Piped water supply is irregular, often provided for less than six hours per day and system losses are high, estimated at 50 percent. Water pollution is a major concern and the source is from both municipal and industrial users, with only about 1 percent of wastewater treated prior to disposal. Only the larger cities have a sewerage network while these facilities are totally lacking or inadequate in the rural and low-income urban areas. Even in the larger cities the systems were installed or upgraded more than twenty years ago and these are now operating beyond capacity

and in severe need of repair and maintenance. Moreover only 40 percent of solid waste is transported for final disposal. Urban road networks are inadequate in most instances and municipal facilities such as public markets and community buildings are insufficient to support human development and economic growth in urban centers. The maintenance of all infrastructures is given low priority.

The sector suffers from under-investment in both rural and urban infrastructure and total government budgetary allocations to the sector amount to an estimated 0.2 percent of the GDP, or a mere 0.8 percent of the total government expenditure on public health services. Other major constraints include poor public sector management, limited skilled human resources and financial capacities, low cost recovery, absence of the private sector due to lack of appropriate regulatory framework and inadequate user or beneficiary involvement in design and O&M of services.

Government Policy and Institutional Framework

Limited access to Water Supply and Sanitation (WSS) facilities has been identified as one of the common characteristics of poverty in the country and the cause of health-related problems. Under its poverty

reduction strategy the Government is committed to meeting the demand of communities for water, through its own resources and accessing resources of external agencies. The Government's overall target is to provide safe drinking water to 68 percent and sanitation facilities to 44 percent of the population by 2004. The recently established local government institutions have been assigned the task of providing and managing WSS facilities using community-based, demand-driven approaches.

At the federal level the Ministry of Environment, Local Government and Rural Development (MELGRD) is the key agency responsible for planning and policy development for water supply, sanitation and environmental protection. Other relevant institutions at the federal level include the Ministry of Health in relation to water quality surveillance and impact on health. The overall responsibility for planning and development at the provincial level rests with the provincial Planning and Development Departments (P&DDs). At the provincial level, the LGRD departments, the provincial PHEDs were responsible for carrying out water supply schemes and sewerage works, while land use planning and guiding and controlling urban growth is in the purview of the Physical Planning and Housing Departments. The provincial Urban Development Boards and the Urban Development Authorities in large cities are responsible for urban planning and implementation of development plans within designated areas. The Communications and Works Departments (C&W) has the mandate for construction, repair, operations and maintenance of provincial roads.

In 1992 the Government adopted a uniform policy framework for rural WSS and each provincial government has adopted a policy for involving communities

in the design and implementation of schemes that would be handed over to communities for full operation and maintenance, with training in O&M to be provided by PHED staff. There is no national urban policy framework and the sector suffers due to lack of any urban planning, land-use control, and construction regulations, coupled with limited skilled human resources, and financial capacities in most urban centres. This constrains the Government's ability to meet the needs of urban communities leading to uncontrolled and unplanned development of cities and towns and deteriorating urban environment.

Under the Local Government Ordinance that was promulgated in August 2001 a decentralized three-tiered system was introduced. Under this system the PHEDs have been dismantled up to the higher middle order management and a third district cadre of civil servants has been created, who will report directly to district governments. Union Councils and *Tehsil* Municipal Administration (TMAs) are responsible for identification, coordination, management and implementation of project activities in rural and urban areas. The Local Government Plan integrates the rural with the urban local governments, into one coherent structure, in which the district administration is answerable to an elected chief executive of the district. These local governments will now determine budgets and expenditures for most services, whereas only the policy, standard setting, and monitoring functions will remain with the provincial and federal government. However adequate capacity of TMAs to undertake this will take years to develop through a carefully structured and sustained human resource development program and setting up of vertical and horizontal linkages.

History of ADB's Operations and Implementation Experience

ADB's involvement in the sector during the 1980s and 1990s was relatively small, at 8 projects, and remained at a constant 5 percent of total lending to Pakistan. Out of total assistance to the sector, 63 percent was for urban water supply and sanitation, 27 percent for urban development, and 10 percent (one loan) for rural water supply and sanitation. Karachi was the main recipient of ADB assistance in this sector with 46 percent of total sector lending.³⁰ With the exception of Karachi where there was a longer term ADB involvement, assistance was provided to smaller towns in Sindh, NWFP, and Punjab with a strategy focused on reducing rural-urban drift to the major metropolitan centers.

ADB has to-date provided assistance of more than \$450 million to sector projects. Major projects in the last decade include the \$55 million Karachi Urban Development Project³¹ the \$85 million Karachi Sewerage Project,³² and the \$66 million Second Urban Development Project.³³ The \$46 million Punjab Rural Water Supply and Sanitation Project³⁴ (1995-2002) provided safe drinking water and drainage facilities to about 800,000 people in seven districts of Punjab using community based approaches.

The main focus of ADB assistance for the sector, in conformity with the 1995 COS and the 1999 COF, was on environmental aspects

and the needs of the poor. Policy dialogue broadly covered: (i) institutional restructuring with emphasis on elimination of overlapping functional responsibilities, professionalization of urban management, staffing policies, and devolution of services delivery; (ii) private sector involvement in the delivery of selected urban services; (iii) budgeting and finance and increased cost recovery and municipal revenue; and (iv) increased community involvement. Capacity building efforts were pursued for institutional strengthening of provincial and municipal urban management and operations, including planning and implementation capabilities, financial management, and environmental management.

Portfolio performance in the sector was constrained by a number of issues including: (i) legal and administrative issues relating to processing procedures and requirements, (ii) coordination difficulties and (iii) technical and project management issues, (iv) inadequate and delayed counterpart funding. The adoption of a centralized top down engineering oriented approach in the design of past projects has also been an important cause for implementation problems. In addition lack of ownership at the local government level, minimal beneficiary participation, poor O&M, low financial and economic rates of return and high turnover of personnel has somewhat undermined project sustainability.

An important lesson from the Karachi Urban Development Project is that urban upgrading is complex, and a piecemeal

30. Loan 0793-PAK(SF): Karachi Urban Development Project for 55.2 million approved on 14 October, 1986; Loan 1001-PAK(SF): Karachi Sewerage for \$ 51 million approved on 14 December, 1989; Loan 1002 Karachi Sewerage for \$34 million approved on 14 December, 1989.

31. See footnote 30.

32. See footnote 30.

33. Loan 1004-PAK(SF): Second Urban Development Project for \$66 million approved on 19 December 1989.

34. Loan1349-PAK(SF): Punjab Rural Water Supply and Sanitation (Sector) Project for \$46 million, approved on 31 January, 1995.

approach involving a few selected problems is not an optimal solution. Urban upgrading should be designed from a plan that integrates all aspects of urban infrastructure and must involve the participation of the ultimate beneficiaries to increase ownership. The main weakness was project design, which in the absence of an appropriate PPTA, was unable to identify the institutional shortcomings of the Karachi Metropolitan Corporation (KMC) and Karachi Water and Sewage Board (KWSB).

Experience with both urban and rural project in the sector have demonstrated that community participation throughout the whole project cycle should be the key focus of interventions, without which long-term sustainability would be jeopardized. Particular lessons learnt include: (i) the need for equal participation of all community groups particularly females, (ii) communication with the project communities on selection criteria and identification of schemes, (iii) assessing their willingness to pay, and (iv) involvement of the private sector, among others.

The benefits of community-based WSS projects, away from the government subsidized inefficient WSS services to an efficient community-run system (where the users are responsible for 100 percent of the O&M cost of the schemes) has been demonstrated for the first time through the Punjab Rural WSS project. It not only created a number of opportunities for the very poor people in the area but was also successful in reducing the incidence of water borne diseases and providing sources of income generation.

ADB's Program and Future Strategy for the Sector

The ADB's operational strategy for Pakistan supports human resource development and social infrastructure requirements. The sector approach is to assist policy reforms to support devolution to local government institutions and decrease disparities within rural and urban areas, to reduce infrastructure deficiencies in the sector and improve resource mobilization capacities of local government institutions. The Government has resolved to continue implementing rural WSS programs in accordance with its uniform policy framework. The fact that these schemes should be community based and O&M should be borne entirely by the beneficiaries has also been endorsed by the ADB-assisted Water Sector Strategy Study (2002).³⁵

For rural WSS the ADB has selected the sector loan modality as the appropriate method of financing. Through this, support will be provided to the Government's community-based approach to sub-project formulation, implementation and O&M. The Local Government Ordinance 2001 has altered the administrative structure and delegated financial authority from the provincial to the district and lower levels of government. The ADB's strategy includes support to the new devolved city and town administration and builds their capacity. Through capacity building and institutional strengthening, the strategy aims to equip the MCs and TMAs and other tiers of local government with the capacity to manage

35. TA-3130: Water Resources Strategy Study for \$ 650,000 approved on 15 December, 1998.

their newly acquired powers and to enable them to enter into new institutional arrangements with the private sector, NGOs and the communities.

A key issue in this regard is the transfer of funds from the province to the districts and TMAs in a manner that strengthens local government autonomy while ensuring that policies, procedures and standards are followed and maximum benefit of provincial funding is achieved. Closely related issues are the inter-government linkages, decision-making processes, and, in particular, strengthening planning and financial management capacities of local governments. The need to reorient and strengthen the functions of provincial line-departments pertaining to policy formulation, setting performance and monitoring standards, providing technical support, and exercising appropriate legal control over local governments is of prime importance in this regard.

Key Features of Ongoing and Future Loans/TAs in the Sector

The recently approved projects include the \$50 million (Second) Punjab Community Rural Water Supply and Sanitation project,³⁶ and the \$30 million NWFP Urban Development Sector Project³⁷ approved in November 2001. Upcoming loans include the Southern Punjab Basic Urban Services Project (included as a stand-by loan in 2003 for \$90 million), the Rawalpindi Environment Improvement Project (included in 2004 for \$80 million), and the Sindh Basic Urban Services (included in 2005 for \$60 million).

The Punjab Community WSS project is a

follow up to a first phase, and will provide organized WSS facilities to 2,500 impoverished village communities in twenty six districts of Punjab, located in areas of acute water scarcity or where groundwater is unfit for human consumption. This will particularly benefit women and girls in the area who bear the burden of fetching water. An estimated 2.3 million people will directly benefit from the sub-projects which include: (i) 500 community-based low-cost water supply and drainage projects and rehabilitation of 250 older ones, (ii) hygiene education and a revolving fund for installing household latrines, (iii) strengthening and capacity building of local government institutions in order for them to fulfill their new roles, (iv) social uplift and poverty eradication program to provide micro credit in the area and (v) construction of additional school space. Of the total project cost around 6.5 percent will be the communities' contribution.

The NWFP Urban Development project is a sector loan based on the NWFP government's overall long term sector requirements for 2001-2020 and supports the Government's poverty reduction and devolution initiatives. It will cover a total of 24 urban centers in the NWFP, classified as MCs with a total population of approximately 1.0 million or around 32 percent of the overall provincial urban population. The project includes both an institutional and an infrastructure component. Under the former the project will support devolution including project implementation and municipal finance capacity building of urban local government, while under the latter high-priority basic infrastructure investments will be financed including water supply, sewerage, solid waste management and

36. Loan 1950 - PAK(SF): Punjab Community Water Supply and Sanitation Sector for \$ 50 million approved on 28 November 2002.

37. Loan 1854 PAK(SF): NWFP Urban Development Sector for \$ 20.8 million approved on 8 November 2001.

roads and local access.

The upcoming Southern Punjab Basic Urban Services project involves provision of water and sanitation services and institutional strengthening of local governments in twenty one cities in 6 districts of Southern Punjab. The prospective Rawalpindi Environment Improvement Project will aim to improve living conditions and quality of life of the people in Rawalpindi where there is inadequate water, sewerage and solid waste management facilities. The ongoing PPTA³⁸ will prepare recommendations for strengthening the TMA, and WASA for sustainable operations of the municipal functions under the devolution plan and Rawalpindi Development Authority (RDA) for its urban development functions. The ensuing project will facilitate sustainable urban development, alleviate water shortage and address severe environmental problems faced by poor urban communities. The Sindh Basic Urban Services Project will facilitate sustainable urban development in selected low income communities in urban centers in Sindh. This will consist of provision of environmental infrastructure leading to improved health profiles and mitigation of environmental degradation.

ADB plans to support Decentralized Social Services (DSS) programs in each province, starting with a \$ 150 million program for Sindh in 2003, followed by a \$150 million program in Punjab in 2004, a \$ 70 million program in Balochistan in 2005, and a \$ 100 million program for NWFP in 2006. A total assistance of \$470 million during 2003-2006 is anticipated. The purposes are to improve the social status of Pakistan's poor citizens, strengthen local governments, and facilitate sector reforms to improve efficiency, equity, effectiveness and sustainability of social services. Each project will provide a fund that districts may draw on through their annual plans to address specific constraints in improving social services, and expending these where justifiable, on a competitive basis. The fund may be used to support gaps in service delivery requiring recurrent or development spending in the water supply and sanitation sector, in addition to education, health, population welfare sectors. A separate fund will be used to facilitate reforms, capacity building, monitoring and evaluation, and other provincial investments supporting the improvement of service delivery.

38. PPTA 4033 - Rawalpindi Environment Improvement for \$ 400,000 approved on 21 April, 2003.

List of Approved Loans in the Water, Sanitation & Urban Development Sector
(as of 31 December 2002)

| Loan No. | Project Name | Net Amount (\$ million) | Milestone Dates | | Implementation Period (years) |
|----------|--|----------------------------|-----------------|----------------|----------------------------------|
| | | | Approval | Date Closed | |
| 1 | 0263 SF Hyderabad Water Supply & Sewerage | 17.55 | 13-Apr-76 | 12-Apr-89 | 13.01 |
| 2 | 0331 SF Faisalabad W. Supply Sewerage & Drainage | 37.34 | 15-Dec-77 | 4-May-89 | 11.39 |
| 3 | 0793 SF Karachi Urban Development Project | 59.65 | 14-Oct-86 | 12-Nov-96 | 10.09 |
| 4 | 1001 SF Karachi Sewerage Project | 46.15 | 14-Dec-89 | 25-Apr-98 | 8.37 |
| 5 | 1002 Karachi Sewerage Project | 34.00 | 14-Dec-89 | 5-Feb-98 | 8.15 |
| 6 | 1004 SF Second Urban Development Project | 73.43 | 19-Dec-89 | 26-Nov-02 | 12.95 |
| | Subtotal/Average | 268.12 | | | 10.658 |
| | Ongoing Loans | | | | Age |
| 7 | 1260 Urban Water Supply & Sanitation | 54.28 | 4-Nov-93 | | 9.16 |
| 8 | 1349 Punjab Rural Water Supply & Sanitation (Sector) | 37.55 | 31-Jan-95 | | 7.92 |
| 9 | 1854 NWFP Urban Development Sector | 21.85 | 8-Nov-01 | | 1.15 |
| 10 | 1950 Punjab Community Water Supply & Sanitation Sector | 51.32 | 28-Nov-02 | | 0.09 |
| | Subtotal/Average | 165.00 | | | 4.58 |
| | Total | 433.12 | | | |

List of Approved TAs in the Water, Sanitation & Urban Development Sectors
(as of 31 December 2002)

| TA No. | Project Name | Type | Revised Amount (\$ million) | Milestone Dates | | Implementation Period (years) | |
|--------|--------------|---|-----------------------------|-----------------|-------------------|-------------------------------|-------------|
| | | | | Approval | Financial Closing | | |
| 1 | 119 | Lyallpur W Supply, Sewerage & Drainage Dev | PP | 0.150 | 2-Jul-74 | 1-Dec-76 | 2.42 |
| 2 | 120 | Hyderabad W Supply, Sewerage & Drainage Dev. | PP | 0.150 | 2-Jul-74 | 1-Aug-76 | 2.08 |
| 3 | 297 | Rawalpindi Water Supply & Sewerage | PP | 0.200 | 28-Jun-79 | 1-Feb-81 | 1.60 |
| 4 | 641 | Urban Sector Profile Study | PP | 0.075 | 10-Dec-84 | 1-Dec-87 | 2.98 |
| 5 | 942 | House-Building Finance Corporation | AO | 0.318 | 8-Jan-88 | 1-Mar-90 | 2.15 |
| 6 | 943 | Second Urban Development Project | PP | 0.401 | 8-Jan-88 | 1-Feb-90 | 2.07 |
| 7 | 963 | Urban Water Supply & Sanitation Sector Study | AO | 0.350 | 11-Mar-88 | 1-Mar-90 | 1.97 |
| 8 | 981 | SSTA for Low-Income Housing | PP | 0.100 | 7-Jun-88 | 1-Dec-90 | 2.48 |
| 9 | 1246 | Strengt.of Billing & Collection Ops of KWSB | AO | 0.184 | 14-Dec-89 | 1-Jun-94 | 4.47 |
| 10 | 1248 | Urban Fin. Mangt & Accounting (JSF-Financed) | AO | 0.700 | 19-Dec-89 | 1-Mar-94 | 4.20 |
| 11 | 1249 | Urban Infrast Needs Assessment (JSF-Financed) | AO | 0.600 | 19-Dec-89 | 1-May-96 | 6.37 |
| 12 | 1349 | Urban Water Supply & Sanitation | PP | 0.635 | 8-Aug-90 | 1-Oct-97 | 7.15 |
| 13 | 1736 | Punjab Rural Water Supply Sector | PP | 0.490 | 23-Jul-92 | 1-Jun-96 | 3.86 |
| 14 | 1744 | SSTA for W S & Sanitation Auth. for Rawalpindi | AO | 0.100 | 18-Aug-92 | 1-Apr-98 | 5.62 |
| 15 | 1762 | Third Urban Development Project | PP | 0.600 | 1-Oct-92 | 1-Apr-95 | 2.50 |
| 16 | 2006 | Second Urban Water Supply & Sanitation (JSF) | PP | 0.500 | 3-Dec-93 | 1-Oct-97 | 3.83 |
| 17 | 2639 | Urban Institutional Strengthening | AO | 0.100 | 9-Sep-96 | 1-Apr-98 | 1.56 |
| 18 | 2928 | Quetta W Supply & Environmental Improvement (JSF) | PP | 0.900 | 5-Dec-97 | 1-Mar-01 | 3.24 |
| 19 | 2940 | NWFP Urban Development (JSF-Financed) | PP | 0.950 | 12-Dec-97 | 1-May-01 | 3.39 |
| 20 | 3124 | Urban Sector Strategy Study | AO | 0.150 | 15-Dec-98 | 1-Apr-01 | 2.30 |
| | | Total/Average | | 7.653 | | | 3.36 |
| | | Ongoing TAs | | | | | |
| 21 | 3802 | Southern Punjab Basic Urban Services (JSF) | PP | 0.800 | 14-Dec-01 | 31-Aug-03 | |
| 22 | 3862 | SSTA Punjab Comm. Water Supply & Sanitation | PP | 0.125 | 4-May-02 | 31-Aug-02 | |
| | | Total | | 0.925 | | | |
| | | Total | | 8.578 | | | |

FINANCE, TRADE AND INDUSTRY

| | |
|--|----------------------|
| Lending 1968-Dec 2002 | : \$2,491.60 million |
| Percentage of Total ADB Lending to PAK (1968-2002) | : 20% |
| Ongoing Commitments as of 31 December 2002 | : \$673.0 million |
| Disbursements | : \$39.48 million |
| Percent Disbursed | : 6% |

FINANCE

Background

The banking sector in Pakistan consists of a total of 39 commercial banks, of which 3 are public sector or nationalized banks, 3 privatized banks, 13 private banks and 18 foreign banks. On an assets basis the market share of public sector banks has reduced from over 92 percent in 1990 to around 45 percent in 2002 due to privatization. Non banking institutions or Non-Bank Finance Companies (NBFCs) consist of Development Finance Institutions (DFIs), 14 investment banks, 33 leasing companies, 45 *modaraba* companies, 4 asset management companies, 2 housing finance companies, 2 discount houses and 2 venture capital companies.

Liberalization of the finance sector has continued since the early 1990s and the last few years have witnessed a rationalization of their operations through mergers and liquidations. Despite improving profiles of financial institutions their capital base is still somewhat marred by the large stock of non-performing loans, which will be gradually written-off. The improvements in the country's external sector have led to a phenomenal rise in the deposit base of banks. A major contributing factor is the rising level of overseas remittances through official channels. In an environment of declining lending rates it has resulted in a

substantial increase in the availability of credit in the economy.

Government Policy and Institutional Framework

A large number of commercial banks have been privatized and loss-making DFIs and NBFCs have been merged and their portfolios restructured. These institutions mainly catered to the medium and large-sized clients for industrial and agriculture financing. In recognition of their potential for growth and employment, and the need to have an anti-poverty focus, the creation of micro-credit institutions for small and medium sized borrowers in rural and urban areas is being actively encouraged by the Government. Moreover it has undertaken institutional and capital market reforms with the express purpose of leveling the playing field for all participants.

The State Bank of Pakistan (SBP) is the apex financial institution, which is the prudential regulator of all deposit-taking institutions. It is autonomous and manages the monetary, credit, interest-rate and foreign exchange policies in the country. The SBP supervises all private commercial banks, public sector banks and the foreign banks, while the Securities and Exchange Commission (SECP) regulates investment banks specialized institutions dealing with industrial and agricultural sector lending and DFIs. The once nationalized commercial

banks barring one or two have all been privatized or are in the process of partial privatization. The DFIs have also been merged, and/or down-sized. To encourage lending to small and medium sized borrowers the SBP has permitted setting up of the Small and Medium Enterprises (SME) Bank, the *Khushhali* Bank and the First Micro Finance Bank, for which it has relaxed the regulatory environment.

There are three stock exchanges in the country, located in Karachi, Lahore and Islamabad. Karachi Stock Exchange (KSE) remains the premier exchange, with a market capitalization exceeding Rs. 600 billion and over 700 listed companies. The KSE uses T+3-system for settlement, whereas the Central Depository Company (CDC) is the electronic bookkeeper, which handles scrip-less stocks. The CDC also manages the newly established National Clearing and Settlement System (NCSS), which will eventually become the clearing-house for all the stock exchanges.

The SECP is responsible for the regulation of the stock exchanges and corporate entities including NBFCs, which until recently were regulated by the SBP. The SECP also regulates the insurance sector and is responsible for the review of published accounts, and compliance with corporate laws of all listed companies in the country.

The Ministry of Privatization and Investments is responsible for the privatization of public sector entities. Although the privatization program has had limited success in recent years due to the political and financial risk of the markets, the planned privatization program, which includes privatization of Pakistan State Oil and Habib Bank Ltd., are likely to be major factors in increasing Foreign Direct Investment (FDI) during the next two years.

History of ADB's Operations and Implementation Experience

The Finance Trade and Industry sector was the largest recipient of ADB assistance in the 1970s/1980s. Sixty-six percent of lending to the sector was provided for DFI-type lending, 18 percent to the industrial sector, and 16 percent for a Capital Market Development Program Loan (CMDP). Most DFI loans in the form of credit lines were provided to three major institutions, Pakistan Industrial Credit and Investment Company (PICIC), Industrial Development Bank of Pakistan (IDBP) and National Development Finance Corporation (NDFC). ADB assistance to DFIs was stopped during the late 1980s mainly because of liberalization of financial markets which resulted in privatization and the emergence of alternative competitive sources of funds for financial institutions and the industrial sector. Direct assistance to industries was also discontinued for the same reasons. Since then, ADB assistance to trade, finance, and industry has been in the form of policy-based lending and through its private sector window.

In the 1990s ADB had four projects in the sector but none of them explicitly addressed the issue of corporate governance of state owned financial institutions, which had a growing portfolio of bad debts and other organizational issues. There also existed a large non-formal finance sector that was dominated by money lenders and those providing credit at extremely high interest rates in exchange for agriculture land and assets as security. Implementation experience from integrated multi-sectoral loans showed that there was a demand for micro-credit, and communities were successfully mobilized through NGOs however there were no permanent institutions to meet

these needs in a sustained fashion.

During the 1990s loans were provided for financial sector intermediation³⁹ and capital market development and governance reform. Under the Capital Market Development Program (CMDP)⁴⁰ that started in 1997 and ended in October 2001, there were seven components relating to different aspects of capital market development including: (i) the creation of a policy environment to enhance competition and creation of a level playing field; (ii) strengthening of governance, (iii) regulation and supervision of institutions; (iv) upgrading of capital markets infrastructure, (v) development of corporate debt market, (vi) reform of *modarabas*, leasing companies, mutual funds, and (vii) reform of the insurance sector.

ADB's Program and Future Strategy for the Sector

Restoring private sector confidence is the key to reviving economic growth in the country. Improvement in Pakistan's macro-economic fundamentals because of the stabilization program and better governance should help in restoring private sector confidence, increasing investment and accelerating growth. ADB assistance will continue to support the Government's reform agenda by extending capital market reforms and other non-bank financial services in particular through improvement of the fiscal, savings and interest rates and investment policy environment, increase in supply of financial instruments and improvements in market infrastructure and development of complementary financial services and institutions. Restructuring and

privatization of state owned financial institutions, development of the long term bond market, sound contractual saving institutions and instruments by reducing the reliance on National Saving Schemes (NSS), is another objective of the sector strategy.

Under the CMDP, assistance is being provided for addressing issues of corporate governance with an emphasis on developing robust capital markets and institutions with emphasis on full corporate disclosures, independence of corporate boards and protection of small investors etc. Other than the policy and governance reforms undertaken at the macro level, the most notable achievement of the CMDP was the setting up of the SECP in 1999 as a successor to the Corporate Law Authority, with full operational autonomy. The SECP's core function is the regulation of the securities markets, both primary and secondary, market intermediaries and as a regulator of non-bank financial institutions. The SECP since its creation has been successful in deepening the market, restoring integrity and investor confidence and its actions will go a long way in ensuring good governance and transparency in stock market operations in the country. The recent rise in the stock market to its highest level in the last ten year can be partly attributed to the regulatory and structural reforms that have been put into place by the SECP. It has also led to the consolidation of leasing companies and *modarabas* and the mutual funds industry.

The ADB's initiatives to develop SMEs, rural finance and agribusiness will help to deepen and diversify private sector activities. A key institutional accomplishment has been the establishment of the

39. Loan 1371-PAK: Financial Sector Intermediation Loan \$100 million approved on 7 September 1995 and closed on 31 December 2000.

40. Loan 1576-PAK: Capital Market Development Program \$250 million approved on 6 November 1997.

Khushhali Bank in 2000 under the \$150 million MSDP⁴¹ in order to increase the outreach of microfinance services in the country. The *Khushhali* Bank and four dedicated funds set up under the MSDP have proved effective in extending the outreach of microfinance services, enhancing social capital and reducing vulnerability of poor households. New microfinance institutions are likely to be set up with the promulgation of a microfinance law.

The \$250 million RFSDP has been designed for a three year period starting 2002 to assist the Government in accelerating rural economic growth by addressing the key constraints in rural finance. It consists of a program and policy loan and a project loan. Its four components include: (i) creating a favorable policy environment (ii) institutional restructuring of the ADBP, (iii) setting up of a new bank fund (NBF) and (iv) product and process innovation.

Key Features of Ongoing and Future Loans/TAs in the Sector

Regulatory and reform measures have been undertaken under the CMDP and the MSDP and now will be consolidated under the recently approved \$260 million Financial Markets and Governance Program (FMGP) loan.⁴² The FMGP reform agenda is structured around five components: (i) improvement of the fiscal, interest rate and investment policy environment; (ii) improvement of governance of market participants and

transparency in information disclosure; (iii) increase in supply of financial instruments and improvements in market infrastructure; (iv) increase in demand for financial instruments through promotion of contractual savings and institutional investment; and (v) development of complementary financial services and institutions.

The Program reform agenda is supported by two TA loans for strengthening regulation, enforcement and governance of non-bank financial markets; and strengthening of pension, insurance and savings systems. The first TA⁴³ will develop solutions to improve Pakistan's pension system and capacity building of Employees Oldage Benefits Institution (EOBI), strengthen the capacity of key government institutions including the Central Directorate of National Savings, mobilization and management of contractual savings and capacity building for investment management in State Life Insurance Corporation, while the second TA⁴⁴ will ensure sustainable development of non-bank financial markets and protection of investors and policy holders through capacity building of SECP's enlarged mandate for regulation and supervision of non-bank financial institutions, insurance and pensions, restructuring of stock exchanges; and mechanisms for skills development and training.

To enhance the inflow of investment through institutional channels into Pakistan's capital market, ADB has provided a Partial Risk Guarantee (PRG) facility

41. Loan 1805-PAK: Microfinance Sector Development Program (MSDP)-Program Loan for \$70 million approved in December 2000; Loan 1806-PK: Microfinance Sector Development Program (MSDP)-Project Loan for \$80 million approved in December 2000.

42. Loan 1955-PAK(SF): Financial Markets and Governance Program (FMGP) for \$260 million approved on 5 December, 2002.

43. L/TA 1956-PAK(SF): Strengthening Pensions, Insurance, and Savings Schemes for \$4.4 million approved on 5 December 2002.

44. L/TA 1957 PAK(SF): Strengthening Regulations, Enforcement and Governance of Non-bank Financial Markets for \$4.5 million approved on 5 December 2002.

within the FMGP loan to guarantee to international investors, payment of proceeds from eligible investments, if that payment is not made as a result of a guaranteed risk, including restriction on foreign exchange convertibility and transferability blockage. The PRG will, however, not cover any risks that affect the value of the investment itself. The aim of the PRG is development of non-bank financial markets and services; and to ensure continued availability of insurance for non-commercial risks following the terrorist events in the United States on 11 September 2001 and its implications on the international insurance industry. The PRG will be counter-guaranteed and indemnified by the Government. The maximum aggregate liability under the PRG covered by ADB at any time will not exceed \$25 million, but the PRG may be enhanced through co-guarantee arrangements with the private sector. It is envisaged to leverage the ADB investment by a factor of up to ten times, for total cover of about \$250 million.

The *Khushhali* Bank set up under the MSDP provides individual and group loans between Rs. 3000 and Rs. 30,000 without any collateral. In the last two years it has shown its capability in savings mobilization, credit delivery and lending to cover risk analysis and credit screening. Almost 30 percent of the loan beneficiaries are women. By the end of 2001, it had disbursed an amount of Rs. 100 million to 15,000 beneficiaries. Within the next five years, it is expected to cover 35 districts and have a loan portfolio of Rs. 7.6 billion, covering 600,000 households throughout the country. The *Khushhali* Bank also supports social mobilization activities within poor communities and development of infrastructure such as water channels and link roads in neglected rural areas. It is also planning to commence activities in urban areas.

The RFSDP approved in December 2002

has been designed for a three-year period to assist the Government in accelerating rural economic growth by addressing the key constraints in rural finance. The RFSDP consists of a program and policy loan and a project loan for the restructuring of the ADBP. Under RFSDP the reforms at ZTBL (formerly ADBP) will continue. These include partial privatization and inclusion of a majority of private sector board members. Its scope of activities will include farm and non-farm lending, and a small-farmer and gender focus reaching 600,000 clients by end-2005. A related initiative under the RFSDP will be the New Bank Fund (NBF) for encouraging the establishment of sustainable MFIs at the provincial and district levels. The MFIs will provide affordable and sustainable services including savings, credit and leasing to the poor households. Social intermediation will precede and accompany MF services to ensure that social and gender dimensions of poverty are adequately addressed. Under the RFSDP it is also intended to reform cooperatives into provincial MFIs, to broaden their scope from agriculture lending to Rural Finance and create credit unions. It will also re-organize the activities of commercial banks in the rural sector towards the upper end of the rural finance market

For private sector development, a PPTA for the Public-Private Infrastructure Finance Facility has been advanced to 2003 from 2004 pipeline, followed by a loan in 2005 for \$200 million. The objective is to encourage private sector participation to build investor confidence and promote investment in infrastructure development activities in the country. The Microfinance Sector Development Program II for \$ 100 million is also in the pipeline for 2006. A PPTA is expected to be approved during 2005. This is expected to assist the government to broaden and deepen the microfinance sector, enlarge retail capacity, enhance

outreach and extend the range of services. Key features of the project include further improvement in policy, institutional strengthening and formalization of risk mitigation aspects (deposit protection and risk insurance) and investments in development of the demand side.

TRADE AND INDUSTRY

Background

Despite being endowed with large natural resources and a cheap labor force Pakistan has a very narrow manufacturing industrial base contributing no more than 15 percent to the GDP. The manufacturing sector employs around 4.1 million people, around 11 percent of the total labor force; virtually all are in the private sector.⁴⁵ The biggest share of the labor force, around 83 percent is employed by SMEs. The industry sector has been adversely affected with: (i) distortions in the trade regime that encouraged uneconomic substitution, (ii) inability of the export policy incentives to off-set biases, (iii) high cost of financial intermediation due to fiscal pressures and an inefficient banking system, and (iv) the legacy of nationalization and state sector ownership of industrial assets, which discouraged investments in the sector. The uncertain political environment in the country has also contributed towards the lack luster performance of the sector and discouraged meaningful investments by domestic and foreign investors.

To significantly reduce poverty, Pakistan must increase its per capital growth rate to about 5 percent annually on an equitable and sustainable basis. Development of SMEs and exports will play an important role. Pakistan's share in world

trade is disproportionately low and exports are concentrated by sector and by client base. Exports mainly consist of textile manufactures, which comprise almost 65 percent of total exports and food and food products that are almost 14 percent of total export. Pakistani exporters are essentially price takers, who compete for market access by lowering prices. Thus a decline in international prices of textile manufactures and a strengthening rupee against the US dollar makes exports highly vulnerable. On the other hand the largest item of the import bill is petroleum products, the demand for which is inelastic and price is highly dependant on the world oil prices.

Government Policy and Institutional Framework

The Government's current policies to revive economic growth include steps to expand the industrial base particularly of the export-oriented manufacturing concerns, to generate growth in the SME sub-sector and to attract private foreign investment. In particular the SMEs have been targeted as having a significant potential for employment generation. According to Small and Medium Enterprise Development Authority (SMEDA) 1.5 million jobs could be created in SMEs in five key sectors that have tremendous export potential, during 2000-2005. The Government also aims to increase the overall investment rate from 14.7 percent of GDP in FY2001 to 20.6 percent by FY2011, and the national savings rate from 12.7 percent of GDP in FY2001 to 20 percent by FY2011. A substantial portion of the improvement in savings is expected to come from increased government saving.

The federal Ministries of Industry and Commerce largely regulate trade and

45. Only 42 manufacturing enterprises remain in the public sector and employ about 36,000 people.

industry. There are a number of semi-autonomous institutions such as SMEDA, the Export Promotion Bureau (EPB), the Board of Investment (BOI) and special purpose financial institutions such as the SME Bank.⁴⁶ Sectoral Committees oversee various industrial sub-groups such as the Engineering Development Board and the Textile Board. Moreover the Government formulates new policies from time to time in key sub-sectors to encourage investment, production and movement up the value added chain. Some policies announced in the past include the Fertilizer Policy and the Energy Policy, where a large number of incentives were provided for new investments in the industry etc.

As discussed earlier in paragraph 94, the relevant institution for privatization of state-owned enterprises is the Ministry of Privatization and Investment, while tariff reforms fall under the purview of the Central Board of Revenue (CBR).

History of ADB's Operations and Implementation Experience

In 1988 the first Industrial Sector Program Loan for \$200 million was provided⁴⁷ in order to promote economic growth, de-regulation and privatization. Under this Program the focus was on institution building of the EPB and privatization of

public sector manufacturing entities. Evaluation of the \$200 million Industrial Sector Program that was completed in May 1991 showed the need for assistance to further support trade liberalization, strengthen the export incentive framework and accelerate privatization. The evaluation also stressed the need for close dialogue with all key agencies and the private sector, which in the long run, would benefit from the reform process. Consequently, while the EPB remained active in managing the Textile Quota, it had little impact on increasing the over all volume of exports. Through the Trade, Export Promotion and Industry Program (TEPI)⁴⁸ ADB provided assistance to the trade sector adjustment operations for the first time. TEPI was accompanied by three TA loans for Modernization of Customs Administration,⁴⁹ Institutional Support for Trade Regime,⁵⁰ and Institutional Strengthening of the BOI.⁵¹

ADB's Program and Future Strategy for the Sector

In accordance with the agreements under the TEPI, the Government gradually reduced the number of directives and did away with ad-hoc procedures and tax exemptions that used to be provided. Innovative duty exemption procedures were formulated in order to provide incentives to exporters and back-to-back domestic letters of credit were introduced. Capacity

46. The SME Bank was formed through a merger of two DFIs: Small Business Finance Corporation (SBFC) and Regional Development Finance Corporation (RDFC) in 1999.

47. Loan 0931-PAK: Industrial Sector Program Loan for \$100 million approved on 13 December 1988 Loan 0932-PAK(SF): Industrial Sector Program Loan for \$100 million approved on 13 December 1988.

48. Loan 1680-PAK (SF) Trade, Export Promotion and Industry (TEPI) Program for \$300 million approved on 31 March 1999.

49. Loan 1681-PAK(SF): Modernization of Customs Administration Technical Assistance for \$3.0 million approved on 31 March 1999.

50. Loan 1682-PAK(SF): Institutional Support for Trade Regime TA for \$3.0 million approved on 31 March, 1999.

51. Loan 1683-PAK(SF): Institutional Strengthening of the Board of Investment (BOI) for \$1.0 million approved in March 1999.

building needs of public and private institutions including EPB and BOI to increase the efficiency of the trade regime were assisted. Consequently the EPB's focus has shifted towards managing the export incentive policy framework encouraging high-value addition, market diversification and improved competitiveness of exports.

Assistance has also been provided by ADB to the trade sector adjustment operations including tariff rationalization and the removal of non-tariff barriers, the modernization of customs administration and assistance for anti-dumping measures and pre-shipment finance guarantee. The aim is to move Pakistan's industrial strategy away from import-substitution towards export led growth by placing local exporters on equal footing with the international players and preparing Pakistan for the World Trade Organization (WTO) regime.

The main emphasis of ADB activities has been on improving the efficiency of markets and macroeconomic fundamentals via the stabilization program, and better governance with the objectives of restoring private sector confidence, increasing investment and accelerating growth. ADB will now provide support to identify and implement reform measures needed to enhance international competitiveness of the private sector for export-led pro-poor growth. ADB will also provide political risk and other guarantees, and support public-private partnerships in infrastructure and other sectors, to build investor confidence and promote investment in the country. In addition, ADB will continue its initiatives to develop SMEs.

Key Features of Ongoing and Future Loans/TA in the Sector

SMEs were identified as the driving force of export-led growth within the Industry and Trade sector and thus a targeted intervention under the SME Trade Enhancement Facility⁵² (SMETEF) was included to build upon initiatives that were implemented under TEPI. SMETEF will improve trade financing and export performance by (i) funding a new dollar based trade finance facility with credit enhancement accessible to direct, indirect and emerging exporters, and particular attention to the needs of SMEs; (ii) providing a partial risk guarantee by the ADB with a Government counter-guarantee to cover sovereign risk associated with the opening of letters of credit (L/Cs) by Pakistani importers; (iii) establishing the Pakistan Export Finance Guarantee Agency Limited (PEFG) to cover pre-shipment performance risks and issue bankable collateral to SME exporters; and (iv) providing a technical assistance (TA) cluster for institutional strengthening of the EPB.

As part of the FMGP approved in December 2002 for \$ 260 million the ADB is supporting a second Partial Risk Guarantee for companies with direct investment in the country. To ensure availability of insurance cover for terrorism-related risks that is no longer readily available in the commercial market following the terrorist attacks in the US on 11 September 2001 - and thus to protect economic and financial sector soundness - ADB will support the establishment of a specialist reinsurance vehicle and

52. Loan 1796-PAK(SF): S-M Size Enterprise Trade Enhancement Finance (SMETEF) for \$150 million approved in December, 2000.

guarantee the capacity of the vehicle for payment of eligible claims in case of a claim event. The PRG will be counter-guaranteed and indemnified by the Government. The maximum aggregate liability under the PRG covered by ADB at any time will not exceed \$175 million, but the PRG may be enhanced through co-guarantee and commercial re-insurance arrangements.

A \$100 million Small and Medium Enterprise Sector Development program is in the pipeline for 2003. The SME sector development program will be a hybrid of program and project activities to provide for innovative mechanisms to support the SME

sector. The Program will address issues related to the improving the business environment for SMEs with a view to reducing transaction cost and lowering barriers of transition from the informal to the formal sector; assisting financial institutions in improving their service outreach to SMEs, and assisting SMEs improve awareness and obtain access to business development services and technology enhancement. A stand-by loan of \$150 million for Trade, Export Promotion and Industry Program (TEPI II) has been programmed for 2006. This will cover the trade and industrial policy and WTO compliance issues.

List of Approved Loans in the Finance Sector
(as of 31 December 2002)

| Loan No. | Project Name | Net Amount (\$ million) | Milestone Dates | | Implementation Period (years) | |
|----------|--------------|---|-----------------|----------------|----------------------------------|-------------|
| | | | Approval | Date Closed | | |
| 1 | 0006 | First Industrial Development Bank of Pakistan | 4.567 | 12-Dec-68 | 31-Mar-73 | 4.30 |
| 2 | 0053 | Second Industrial Development Bank of Pakistan | 14.540 | 22-Dec-70 | 26-May-76 | 5.43 |
| 3 | 0120 | Pakistan Industrial Credit & Investment Corporation | 5.856 | 21-Dec-72 | 7-Mar-78 | 5.21 |
| 4 | 0121 | SF Pakistan Industrial Credit & Investment Corporation | 5.905 | 21-Dec-72 | 7-Mar-78 | 5.21 |
| 5 | 0256 | Third Industrial Development Bank of Pakistan | 24.931 | 23-Dec-75 | 30-Jun-81 | 5.52 |
| 6 | 0269 | Second Pakistan Industrial Credit & Investment Corporation | 24.533 | 29-Jun-76 | 18-Jan-82 | 5.56 |
| 7 | 0303 | National Development Finance Corporation | 27.809 | 23-Aug-77 | 5-Jan-84 | 6.37 |
| 8 | 0455 | Third Pakistan Industrial Credit & Investment Corporation | 31.029 | 25-Mar-80 | 7-Oct-86 | 6.54 |
| 9 | 0564 | SF Second National Dev. Finance Corp Project | 49.875 | 22-Dec-81 | 31-Mar-87 | 5.27 |
| 10 | 0608 | SF Fourth Industrial Development Bank of Pakistan Project | 19.887 | 7-Dec-82 | 28-Dec-88 | 6.06 |
| 11 | 0609 | 4th Industrial Development Bank of Pakistan Project | 19.611 | 7-Dec-82 | 28-Dec-88 | 6.06 |
| 12 | 0678 | Development Financing Project | 48.743 | 20-Dec-83 | 7-Nov-89 | 5.89 |
| 13 | 0679 | SF Development Financing Project | 67.660 | 20-Dec-83 | 7-Nov-89 | 5.89 |
| 14 | 0775 | SF Second Development Financing Project | 60.871 | 19-Dec-85 | 21-Jan-91 | 5.09 |
| 15 | 0776 | Second Development Financing Project | 50.000 | 19-Dec-85 | 21-Jan-91 | 5.09 |
| 16 | 0878 | Third Development Financing Project | 173.484 | 17-Dec-87 | 7-Jan-93 | 5.06 |
| 17 | 0879 | SF Third Development Financing Project | 21.682 | 17-Dec-87 | 19-Apr-93 | 5.34 |
| 18 | 0902 | Small-Scale Industry Project | 46.377 | 22-Sep-88 | 28-Sep-95 | 7.02 |
| 19 | 0996 | Fourth Development Financing Project | 204.979 | 12-Dec-89 | 6-Nov-97 | 7.91 |
| 20 | 1371 | Financial Sector Intermediation Loan | 24.547 | 7-Sep-95 | 31-Dec-00 | 5.32 |
| 21 | 1576 | Capital Market Development Program | 250.000 | 6-Nov-97 | 31-Oct-01 | 3.99 |
| 22 | 1577 | SF Capacity Building of Securities Market | 3.551 | 6-Nov-97 | 30-Jul-02 | 4.73 |
| | | Subtotal/Average | 1,180.44 | | | 5.59 |
| | | Ongoing Loans | | | | Age |
| 23 | 1955 | Financial (Non-Bank) Markets & Governance Program | 260.000 | 5-Dec-02 | | 0.07 |
| 24 | 1956 | SF Strengthening Pension, insurance & Saving Systems | 3.072 | 5-Dec-02 | | 0.07 |
| 25 | 1957 | SF Strengthening Regulations, Enforcement & Governance of Non-bank Financial Markets | 3.072 | 5-Dec-02 | | 0.07 |
| 26 | 1987 | Rural Finance Sector Development Program | 225.000 | 20-Dec-02 | | 0.03 |
| 27 | 1988 | Rural Finance Sector Development | 25.000 | 20-Dec-02 | | 0.03 |
| | | Subtotal/Average | 516.144 | | | 0.05 |
| | | Total | 1,696.58 | | | |

List of Approved Loans in the Industry & Trade Sector
(as of 31 December 2002)

| Loan No. | Project Name | Net Amount (\$ million) | Milestone Dates | | Implementation Period (years) |
|----------|---|----------------------------|-----------------|----------------|----------------------------------|
| | | | Approval | Date Closed | |
| 1 | 0350 SF D.G. Khan Cement | 44.40 | 24-Aug-78 | 10-Nov-86 | 8.22 |
| 2 | 0384 Automotive Components Manufacturing | 26.77 | 20-Dec-78 | 8-Oct-87 | 8.81 |
| 3 | 0931 Industrial Sector Program | 100.00 | 13-Dec-88 | 17-May-91 | 2.42 |
| 4 | 0932 SF Industrial Sector Program | 100.78 | 13-Dec-88 | 28-May-91 | 2.45 |
| 5 | 1680 Trade, Export, Promotion & Industry Program (TEPI) | 300.00 | 31-Mar-99 | 27-Dec-01 | 2.75 |
| | Subtotal/Average | 571.95 | | | 4.93 |
| | Ongoing Loans | | | | Age |
| 6 | 1681 Mdrnztm of Customs Admin Tech Assistance | 3.00 | 31-Mar-99 | | 3.76 |
| 7 | 1682 Institutional Support for Trade Regime TA | 3.00 | 31-Mar-99 | | 3.76 |
| 8 | 1683 Instl Strengthening of the Board of Investment | 1.00 | 31-Mar-99 | | 3.76 |
| 9 | 1796 Foreign Currency Export Finance Facility (FCEP) | 150.00 | 7-Dec-00 | | 2.07 |
| | Subtotal/Average | 157.00 | | | 3.33 |
| | Total | 728.95 | | | |

List of Approved TAs in the Finance Sector
(as of 31 December 2002)

| TA No. | Project Name | Type | Revised Amount (\$ million) | Milestone Dates | | Implementation Period (years) | |
|--------|--------------|--|-----------------------------|-----------------|-------------------|-------------------------------|-------------|
| | | | | Approval | Financial Closing | | |
| 1 | 163 | Industrial Development Bank of Pakistan | AO | 0.150 | 23-Dec-75 | 1-Apr-79 | 3.27 |
| 2 | 875 | SSTA for Pakistan Venture Capital Ltd. (PVCL) | PP | 0.060 | 13-May-87 | 1-Dec-88 | 1.56 |
| 3 | 1033 | Credit Guarantee Scheme | AO | 0.150 | 22-Sep-88 | 1-Aug-90 | 1.86 |
| 4 | 1034 | Institutional Building of RDFC (UNDP Financed) | AO | 0.250 | 22-Sep-88 | - | - |
| 5 | 1035 | Pilot Assistance Program for Micro Industries | AO | 0.200 | 22-Sep-88 | - | - |
| 6 | 1036 | Institut-Building for Provincial Small Industries Corporation | AO | 0.400 | 22-Sep-88 | 1-Sep-92 | 3.95 |
| 7 | 1095 | Study on the Rationalization of DFIS | AO | 0.259 | 3-Jan-89 | 1-Jan-92 | 2.99 |
| 8 | 1096 | Study On Devt of Secondary Market for Fixed-Income Securities | AO | 0.176 | 3-Jan-89 | 1-Mar-94 | 5.16 |
| 9 | 1236 | Institnl Bldg of Corp. Law Authority & Study of Mutual Fund Ind | AO | 0.310 | 12-Dec-89 | 1-Jun-00 | 10.48 |
| 10 | 2812 | Interest Rate Management of National Saving Scheme | AO | 0.100 | 18-Jun-97 | 1-Oct-00 | 3.29 |
| 11 | 2865 | Restructuring of Public Sector Mutual Funds | AO | 0.800 | 15-Sep-97 | 1-Sep-00 | 2.96 |
| 12 | 2905 | Impact Analysis of Privatization in Pakistan | AO | 0.126 | 3-Nov-97 | 1-Feb-00 | 2.25 |
| 13 | 3612 | Operational Review of the State Life Insurance Corporation | AO | 0.660 | 21-Dec-00 | - | - |
| | | Subtotal/Average | | 3.641 | | | 3.78 |
| | | Ongoing TAs | | | | | |
| 14 | 2393 | Loan & TA Grant - Capital Market Development (JSF) | AO | 0.865 | 7-Sep-95 | 30-Apr-00 | |
| 15 | 2825 | Capital Market & Insurance Law Reform | AO | 0.100 | 14-Jul-97 | 31-Dec-02 | |
| 16 | 2866 | Reform of the Insurance Industry | AO | 0.700 | 15-Sep-97 | 31-Dec-00 | |
| 17 | 2867 | Reform of Pension & Provident Funds | AO | 0.600 | 15-Sep-97 | 30-Jun-01 | |
| 18 | 3559 | Enhancing Cap. Market Depth for Preparing Capital Mkt Devt Prgm II | PP | 0.150 | 7-Dec-00 | 17-Dec-01 | |
| 19 | 3650 | Institutional Strengthening of the State Bank of Pakistan | AO | 0.450 | 23-Apr-01 | 30-Jun-03 | |
| 20 | 3696 | Capacity Bldng for Capital Market Dev. & Corporate Governance | AO | 0.600 | 7-Aug-01 | 30-May-03 | |
| 21 | 4015 | Enhancing Cap. for Resource Management & Poverty Redn in Punjab | AO | 0.680 | 5-Dec-02 | 31-May-04 | |
| | | Subtotal/Average | | 4.145 | | | |
| | | Total | | 7.786 | | | |

List of Approved TAs in the Industry and Trade Sector
(as of 31 December 2002)

| TA No. | Project Name | Type | Revised Amount (\$ million) | Milestone Dates | | Implementation Period (years) |
|--------|--|------|--------------------------------|-----------------|-------------------|-------------------------------|
| | | | | Approval | Financial Closing | |
| 1 | 402 Gypsum Mining | PP | 0.190 | 12-May-81 | 1-Dec-87 | 6.56 |
| 2 | 701 Pakistan Engineering Company Ltd Rehab & Expansion Project | PP | 0.163 | 30-Aug-85 | 1-Dec-88 | 3.26 |
| 3 | 742 Development of Small-Scale Industries | AO | 0.330 | 31-Dec-85 | 1-Dec-88 | 2.92 |
| 4 | 1037 Promotion of Subcontracting Between Ssis & L-Scale Industries | AO | 0.350 | 22-Sep-88 | - | - |
| 5 | 1085 Disinvestment Strategy of Public Enterprises (JSF-Financed) | AO | 0.240 | 13-Dec-88 | 1-Sep-92 | 3.72 |
| 6 | 1201 Institutional Development of the National Tariff Commission | AO | 0.475 | 4-Sep-89 | 1-Jun-99 | 9.75 |
| 7 | 784 Nok Kundi Iron Ore Project | PP | 0.190 | 23-Jul-86 | 1-Dec-88 | 2.36 |
| 8 | 984 SSTA for Review of Indl Policy Framework | AO | 0.030 | 10-Jun-88 | 1-Dec-89 | 1.48 |
| 9 | 1084 Regional Ind Potential & Indstrl Pollution Control Policy(JSF) | AO | 0.296 | 13-Dec-88 | 1-Jun-92 | 3.47 |
| 10 | 1167 National Mineral Exploration Program (JSF-Financed) | AO | 0.390 | 16-Jun-89 | 1-Jul-94 | 5.04 |
| 11 | 1259 Restructuring Investment Promotion Bureau(IPB)-(JSF-financed) | AO | 0.350 | 22-Dec-89 | 1-May-00 | 10.36 |
| 12 | 1669 Small-Scale TA for Second Industrial Sector Program Loan | PP | 0.100 | 4-Feb-92 | 1-Jan-94 | 1.91 |
| | Subtotal/Average | | 3.104 | | | 4.62 |
| | Ongoing TAs | | | | | |
| | 3183 Montring Socioecon. Impact of Trade, Export Promo & Ind Prog Loan | AO | 0.150 | 13-Apr-99 | 31-Dec-02 | |
| | 3558 L/TA: Institutional Strengthening of EPB (Cluster) | AO | 0.800 | 7-Dec-00 | 30-Sep-03 | |
| | 3835 Small & Medium Entreprise Development Program | PP | 0.800 | 14-Feb-02 | 31-Mar-03 | |
| | 3944 Industrial Environment Management | AO | 0.700 | 22-Oct-02 | 31-Aug-03 | |
| | Subtotal | | 2.450 | | | |
| | Total | | 5.554 | | | |

GOVERNANCE

| | | |
|--|---|-------------------|
| Lending 1968-December 2002 | : | \$661.1million |
| Percentage of Total ADB Lending to PAK (1968-99) | : | 5% |
| Ongoing Commitments as of 31 December 2002 | : | \$661.07 million |
| Disbursements as of December 2002 | : | \$254.012 million |
| Percent Disbursed as of 2002 | : | 38.4% |

Background

Good governance has emerged as Pakistan's foremost development priority given the over centralization, political instability and the rampant corruption that prevailed prior to and during the 1990s. This not only eroded business confidence but also had a negative impact upon economic growth and increased the incidence of poverty in the country. The crisis of governance thus undermined state institutions and the rule of law and led to the alienation of the citizenry from the state.

The Government has demonstrated a strong commitment to governance reforms, which in the past have often been resisted by powerful pro-status quo vested interests. Central to the government's commitment to governance reforms is strengthening the rule of law and reforming key institutions. It has also been recognized that long-term economic recovery hinges upon the effective implementation of these reforms.

Government Policy and Institutional Framework

In 2001 the Government adopted the IPRSP, followed by the draft PRSP, as a dynamic framework to tackle the twin challenges of reviving economic growth and reducing poverty in the country. It is recognized in these documents that "improving governance is central to fighting poverty, and thus cuts across all the elements of

Pakistan's poverty reduction strategy." Concurrently, decentralization is recognized as the primary means to improve basic service delivery and to address the gaps in human development indicators.

The Government's governance reform agenda covers three key areas: (i) improving the public financial management system, public accounting and auditing functions, civil service and tax administration, (ii) enhancing effectiveness of delivery of basic public services through a comprehensive devolution plan; providing access to justice, and reducing vulnerability of poor through legal, judicial and police reforms; and (iii) tackling corruption by reducing incentives for it through privatization, deregulation, tariff reduction, and tax system reforms; and establishing an effective anticorruption agency as a deterrent.

Between March 2000 and August 2001, the Government restructured the prevailing administrative system and under the stewardship of the National Reconstruction Bureau (NRB) bold reform measures were undertaken including the promulgation of the Local Government Ordinance (LGO) and countrywide elections to install representative councils at three levels of local government. A firm commitment to gender reform and social development as an integral part of decentralization was also embedded in the LGO with 30 percent of seats in all local government institutions were reserved for women. These underway governance reforms will have major impli-

cations for relations between the state and non-state institutions and their successful implementation will nurture consensus building between government institutions, the civil society and the private sector.

The LGO of 2001 is the fundamental blue-print for decentralization that assigned explicit powers, responsibilities and service delivery functions to three tiers of local government: district, *tehsil* and union and ensures that elected representatives are in control of local level revenues, expenditures and administration. A vital objective of the LGO is also to bring “justice to the doorstep” of the people, and to improve efficiency, equity and accountability at all levels of state and non-state interaction.

Devolution, first from the provincial to elected local governments and then from the federal to the provincial level will bring fundamental changes to how all public services are planned, financed and managed. The bulk of the basic poverty-focused services, for health, education, agriculture, water and natural resources management have been devolved to district and lower local governments. Provinces will assume new responsibilities to support and supervise the performance of local governments, which would no longer work as administrative appendages, but as independent corporate bodies accountable to the electorate through political leaders.

Institutions spearheading the governance reform effort at the federal level include the NRB, the office of the Auditor General (AG), the office of the Controller General of Accounts (CGA), the Ministry of Women's Development (MOWD) and the National Accountability Bureau (NAB). The NRB is the concerned institution for the devolution program and is responsible for the effective implementation of the LGO-2001. The CGA and AG are responsible for

financial reporting and auditing, and will ensure that the local levels of government follow sound financial reporting systems. The NAB is the federal anticorruption agency. A number of institutions will be set up in the context of the devolution program; these include a Local Government Commission and Provincial Finance Commissions to ensure formula-based fiscal transfers and transparent reporting of expenditures at the local level. The new Police Ordinance will amend the Police Act of 1861 and will redefine the administrative structure of the police and provide a statutory base for the establishment of national, provincial and district level Public Safety Commissions. Citizen Community Boards and Public Safety and Justice Committees will monitor local government. While the former are also empowered to prioritize investments up to 50 percent of the local development budget for basic infrastructure and services, the latter will offer new possibilities to depoliticize the police, establish its independence and to increase their accountability to ordinary citizens.

ADB's Program and Future Strategy for the Sector

Institution and capacity building has been ongoing in virtually all areas where ADB is involved, and improving governance was also a major theme of portfolio management in the past. The ADB's support strategy in the sector is to promote good governance in the management of the development process; public resource and expenditure management; transparency and accountability of economic policies; strengthening of institutions, systems and capacity; and promotion of local participation and ownership. Direct assistance to the Government's reform agenda constitutes a substantial proportion of ADB's country program. This consists of two program loans

namely Access to Justice Program (AJP)⁵³ and Decentralization Support Program (DSP).⁵⁴ The AJP aims to integrate access to justice issues into the larger development debate in the country, set the policy and legal framework for sustainable judicial and police reforms and initiate a set of activities to address pressing issues in the sector. The AJP takes a comprehensive approach towards addressing issues relating to legal and judicial reforms and administrative reforms at the provincial and district levels along with police reforms.

The DSP essentially supports the Government's poverty reduction strategy through providing support for implementation of reform policies related decentralization, gender and social development. Its objectives include assisting policy support for decentralization and related administrative and institutional reforms, effective and sustainable province and local government relations and the local level management of resources accountably and equitably, efficient service delivery by public and private agencies in accordance with norms of public participation, access to information and accountability.

Key Features of Ongoing and Future Loans/TA in the sector

The key objective of the AJP is to assist the Government through the Ministry of Law, Justice, Human Rights and

Parliamentary Affairs (MLJ&PA) to improve access to justice so as to (i) provide security and ensure equal protection under the law to citizens, in particular the poor; (ii) secure and sustain entitlements and thereby reduce the poor's vulnerability, (iii) strengthening the legitimacy of state institutions, (iv) create conditions conducive to pro-poor growth, especially by fostering investor's confidence. ADB sponsored a series of studies under two TAs preceding the AJP⁵⁵ that recommended a phased judicial reform agenda, while an ongoing TA⁵⁶ is pilot testing some of these proposals and building the capacity for reform. In the context of the Local Government Plan, the ADB is also assisting in the survey of existing legal needs at the local level and the capacity of various institutions in this respect. A \$20 million TA cluster loan was approved to support institutional development for AJP. It will focus on (i) governance structures, systems, and capacities to articulate policy/laws (ii) public knowledge and empowerment (iii) performance and accountability; (iv) policy impact and innovation; and (v) supporting further legal and policy reform. Another TA⁵⁷ equivalent to \$900,000 will be provided to support a program management unit (PMU) within the MLJ&PA and an independent monitoring and evaluation system.

In October 2002 the \$300 million DSP was approved. This includes support for two TA loans at a total cost of \$30 million: the first is a TA for Local Government

53. Loan 1897-(PAK) SF: Access to Justice Program for \$243 million approved in December 2001, Loan 1898-PK(SF) Access to Justice Program for \$86.8 million approved in December 2001, Loan 1899-PK(SF) Institutional Development for Access to Justice for \$20 million approved in December 2001.

54. Loan 1936-PK(SF): Decentralization Support Program for \$270 million approved in October 2002.

55. TA-2979: Strengthening Government Legal Services and Subordinate Judiciary for \$150,000 approved on 31 December 1997. TA-3015: Legal and Judicial Reforms for \$995,000 approved on 7 May 1998.

56. TA-3433 Strengthening of Institutional Capacity for Judicial and Legal Reforms for \$2.9 million approved on 27 April 2000.

57. L/TA-3823: Supporting & Monitoring Progress under the Access to Justice Program for \$900,000 approved on 20 December 2001.

Performance Enhancement⁵⁸ and the second is a TA on Gender and Governance Mainstreaming.⁵⁹ The objective of the program is improved local government representation, accountability and efficiency, resulting in improved service delivery through fiscal support for reforms in (i) policies, laws and regulation, (ii) institutional strengthening and capacity building, and (iii) fiscal, restructuring and budgetary measures. Stakeholders at all three levels of government and civil society actively participated in the design of the DSP through three related technical assistance activities during 2001 and 2002. These included the TA⁶⁰ for Fiscal decentralization, the TA⁶¹ for Institutional Strengthening for Government-NGO cooperation and TA⁶² for Gender Reform Assistance Program, under which Gender Reform Action Plan (GRAP) are being currently prepared. The four GRAP themes are (i) improving representation of women in political and administrative structures, (ii) encouraging policy shift from social welfare and women's development to social development and gender equality, (iii) restructuring institutions dealing with gender and social development, (iv) engendering the planning and budgetary processes.

The Local Government Performance Enhancement TA will be executed by the MOF and federal and provincial agencies over a four-year period starting June 2003. It will include ongoing actions and initiatives to articulate the legal and policy framework established, into government institutions and fiscal arrangements, which must necessarily be updated and refined during

the course of implementation. The TA on Gender and Governance Mainstreaming will be implemented by the MWD and provincial departments. It will become effective upon approval of the federal and provincial GRAPs and will essentially support their implementation in a phased manner, like TA1.

The proposed \$450 million Punjab Public Sector Resources Management Program, with a first phase of \$150 million included in the lending program for 2003, is currently under preparation and will support poverty reduction through improved public sector resource management and pro-poor development planning in Punjab. It aims to increase participation and competence for transparent, accountable and sustainable public service delivery in the province. The total program period is expected to last about four years, the first sub-program is likely to be followed by two subsequent programs of \$100-150 million each about 12-18 months after completion. A similar resource management program for \$120 million is also under consideration for the Balochistan province for 2004. A Cluster TA for a total amount of \$800,000 for the Program has been included in 2004 and 2006 pipeline.

The proposed program for 2004 includes a \$300,000 FATA Governance ADTA, which is expected to be followed by a proposed \$25 million FATA Governance Program in 2005. The purpose of this is to bring FATA in line with key policies, laws and institutional reforms being promoted under the DSP and the AJP. Specific measures will include

58. L/TA-1937: Local Government Performance Enhancement for \$23 million approved on 21 November 2002.

59. L/TA-1938: Gender and Governance Mainstreaming for \$7.0 million approved on 21 November 2002.

60. TA - 621: Fiscal Decentralization for \$1.875 million approved on 17 January 2001.

61. TA - 3618: Institutional Strengthening for Government-NGO Cooperation for \$400,000 approved on 21 December 2000.

62. TA - 3832: Gender Reform Program for \$600,000 approved on 1 February 2002.

developing institutional capacity, administrative, legal and economic reforms. Another pipeline project for 2006 is the \$150 million Punjab Local Justice Support Program. The rationale of this program is to

consolidate and extend the scope of systemic reforms under the AJP at the federal and provincial levels, to the local and district level and strengthening of civil society organizations.

PAKISTAN: List of Approved Governance Loans
(as of 31 December 2002)

| Loan No. | Project Name | Net Amount (\$ million) | Milestone Dates | | Implementation Period (years) |
|-------------------------|--------------|---|-----------------|----------------|----------------------------------|
| | | | Approval | Date Closed | |
| 1 | 1897 | Access to Justice Program | 246.052 | 20-Dec-01 | 1.03 |
| 2 | 1898 | Access to Justice Program | 89.194 | 20-Dec-01 | 1.03 |
| 3 | 1899 | Institutional Development for Access to Justice | 21.196 | 20-Dec-01 | 1.03 |
| 4 | 1935 | Decentralization Support Program | 207.406 | 21-Nov-02 | 0.11 |
| 5 | 1936 | Decentralization Support Program | 66.519 | 21-Nov-02 | 0.11 |
| 6 | 1937 | Local Government Performance Enhancement | 23.537 | 21-Nov-02 | 0.11 |
| 7 | 1938 | Gender & Governance Mainstreaming (TA Loan) | 7.163 | 21-Nov-02 | 0.11 |
| Subtotal/Average | | | 661.067 | | 0.50 |

List of Approved Governance TAs
(as of 31 December 2002)

| TA No. | Project Name | Type | Revised Amount (\$ million) | Milestone Dates | | Implementation Period (years) |
|-------------------------|--------------|---|--------------------------------|-----------------|-------------------|-------------------------------|
| | | | | Approval | Financial Closing | |
| 1 | 2979 | Strengthening Government Legal Services & Subordinate Judiciary | AO | 0.150 | 31-Dec-97 | |
| 2 | 3015 | Legal & Judicial Reform | AO | 0.995 | 7-May-98 | |
| 3 | 3390 | Capacity Building for Debt & Risk Management of Min of Finance | AO | 0.995 | 5-Jan-00 | |
| 4 | 3433 | Strengthening of Institutional Capacity for Judicial & Legal Reform | AO | 2.900 | 27-Apr-00 | |
| 5 | 3618 | Institutional Strengthening for Government-NGO Cooperation | AO | 0.400 | 21-Dec-00 | |
| 6 | 3621 | Fiscal Decentralization | AO | 1.875 | 17-Jan-01 | |
| 7 | 3630 | Poverty Analysis & High-level Forum in Pakistan | AO | 0.150 | 7-Feb-01 | |
| 8 | 3640 | Supporting Access to Justice Under the Local Govt Plan | AO | 0.150 | 19-Mar-01 | |
| 9 | 3682 | Supp for Implmntn of Natl Policy & Action Plan Vs Child Labor | AO | 0.150 | 4-Jul-01 | |
| 10 | 3744 | Supporting Government Restructuring & Reform | PP | 0.150 | 18-Oct-01 | |
| 11 | 3823 | L/TA: Supprtng & Mntrng Progress Under Access to Justice Program | AO | 0.900 | 20-Dec-01 | |
| 12 | 3832 | Gender Reform Program (TASF/Neth) | AO | 0.600 | 1-Feb-02 | |
| 13 | 3926 | Support to the Implementation of Decentralization | AO | 0.450 | 13-Sep-02 | |
| 14 | 3982 | Strengthening Portfolio Performance & Monitoring | AO | 0.650 | 8-Nov-02 | |
| 15 | 3991 | Debt Management Strengthening of Economic Affairs Division | AO | 0.150 | 20-Nov-02 | |
| 16 | 4033 | Enhancing Access to Comprehensive Insurance Cover After 9/11 | AO | 0.150 | 13-Dec-02 | |
| 17 | 4043 | Str the National Accountability Bureau (GCF) | AO | 0.120 | 18-Dec-02 | |
| Subtotal/Average | | | | 10.935 | | |

SOCIAL SECTORS

| | | |
|--|---|-------------------|
| ADB Lending 1968-2002 | : | \$1,260.0 million |
| Percentage of ADB Lending to PAK 1968-2002 | : | 10% |
| Ongoing Commitment as of 31 December 2002 | : | \$379.16 million |
| Disbursements as of December 2002 | : | \$325.94 million |
| Percent Disbursed as of December 2002 | : | 58% |

Background

Despite Pakistan's comparative high economic growth in the 1980s, its human development status remained poor. This was largely due to the low investments in social sectors and the high rate of population growth. Higher population growth frustrated all efforts at reducing poverty and improving the availability and quality of social services. It also accelerated environmental deterioration, water scarcity and created food shortages, further compounding the country's social problems.

Thus in 1993-94 Government developed a comprehensive approach to social development under the Eighth Five-year plan that aimed at increasing fiscal efforts and addressed the institutional impediments in the delivery of basic social services. The Social Action Program (SAP)⁶³-a multi-donor initiative was designed to provide a broad-based integrated program approach to address cross-sectoral issues. Despite the overall poor level of budget expenditure in education (2.7 percent of GNP in 1997),⁶⁴ Pakistan was provided assistance for spending for basic education⁶⁵ in addition to health, population and WSS by the SAP.

Government Policy and Institutional Framework

Historically the overall responsibility of the Education and Population sectors used to be divided between the federal government and the four provincial governments and relevant provincial departments, with Health being primarily a provincial subject. The federal government continues to establish policy guidelines, allocates development funds in the health and population sub-sectors while it determines the curriculum and examination system for education. Over time the federal government assumed a greater role even though the responsibility of implementation lay largely with the provincial governments.

However, under the decentralization plan the bulk of the basic poverty-focused services, for health, education, agriculture, water and natural resources management have been devolved to district and lower local governments. Thus, provinces will assume new responsibilities to support and supervise the performance of local governments at the district and *tehsil* level, not as administrative appendages, but as independent corporate bodies accountable to the

63. The Social Action Program (SAP), initiated in 1993 by donors including World Bank, ADB, the Netherlands Government, DFID and the European Union etc., aimed to raise the status of human development in Pakistan through support for basic services in elementary education, primary health care, population welfare, and rural water supply and sanitation. Total direct and indirect donor support for the program was about \$1.5 billion.

64. Source: UNICEF, 1998.

65. Primary Education and Middle Schooling.

electorate through political leaders.⁶⁶ Provincial governments are currently preparing to bring the TMAs under the national accounting systems from 1 July 2003 onwards. The Province Finance Commissions (PFCs) are operational and have devised varied formulae in each province on the basis of population, area and prevailing socio-economic conditions for making fiscal transfers to the local government budgets

History of ADB's Operations and Implementation Experience

ADB assistance to social sectors historically included a number of education, health, population and WSS projects. Under the ADB assisted Social Action Program project (SAPP-I)⁶⁷ support was provided, in the context of the larger multi donor initiative, towards beginning a process of fundamental change in basic social service delivery and improvement in social conditions, particularly of the rural poor and women. This was followed by SAPP-II⁶⁸ in 1996 in order to build upon the experiences gained during SAPP-I and for Government to focus more on quality, management improvement and increased involvement of stakeholders. The program consisted of assistance to primary (later elementary) education, primary health, population and rural WSS.

ADB loans to the education sector in Pakistan have focused on areas of primary education, teacher training, science education, textbook printing and basic education (in the case of the SAP). During the 1990s loans were targeted exclusively at female

education, such as the Primary Education (Girls) Sector Project⁶⁹ approved in 1989 and the Second Girls' Primary School Education Project⁷⁰ which became effective in January 1998. NGO involvement in these projects is increasing, particularly in community supported non-formal education projects and projects for girls and women.

The ADB has also been one of the lead donors in the health and population sub-sector. It has had a key role in helping Government to set program and organizational priorities, improve system designs, develop human resources for the sector, and improve service delivery to ensure better impact of policies and programs. ADB assistance to the sector started in 1981 and registered a significant increase during the 1990s with a total of 6 projects for \$193.4 million.

Experience from completed projects in the social sectors indicates weak implementation, frequent staff turnover and inadequate recurrent budgets. Of the projects that were evaluated in the education sector the Teachers Training project and the Primary Education Girls Project were rated as Partly Successful due to delays of a year or two in completing civil works, weak project management and supervision by the federal coordination unit. These projects also suffered from incomplete training components and underutilization of loan funds for capacity building, procurement and consultants. While the physical facilities were mostly complete, the focus on qualitative changes was inadequate and thus the objective of institutional capacity building was minimally achieved.

66. For additional details please refer to paragraphs 82 and 83.

67. Loan 1301-PAK(SF): Social Action Program (Sector) for \$100 million approved on 23 June, 1994.

68. Loan 1493-PAK(SF): Social Action Program II for \$200 million approved on 28 November, 1996.

69. Loan 0977-PAK(SF): Primary Education (Girls) Sector Project for \$43 million approved on 26 October 1989.

70. Loan 1454-PAK(SF): Second Primary Education (Girls) Project for \$45 million approved on 15 August 1996.

Bank-financed health sector projects were appropriate in their scope in that they aimed to improve services for mothers and children by improving access to primary healthcare and training of female staff. However their emphasis was on access rather than improvement in qualitative aspects of primary healthcare through better supervision and management. According to the completion reports of three projects each of these also required two additional years for completion and the delays were mainly due to reasons cited above for the education projects. Additionally it was felt that there was insufficient recognition of local conditions and lack of involvement of Government in project design leading to unfamiliarity with ADB procedures and lack of preparedness.

The SAP helped make governance, financing and capacity issues in the social sectors more transparent and was a good mechanism in coordinating donor efforts in the social sectors and promoting policy dialogue on a common basis with the Government. It raised the profile of social sectors and made them a priority for resource allocation, although the practical expression of Government's commitment primarily relied on incremental revenues rather than reallocation among sectors. It is understood that many of the problems in these sectors were not SAP specific but reflected the deep-rooted problems of the public service at large. Moreover, it has been acknowledged that the objectives of the SAP may have been too ambitious given the social, economic and political context of the country. The need for greater accountability and increased transparency in resource allocation for social sector development were also highlighted only during SAP II.

While SAP II had provided more focus on governance issues, it arrived at a time of serious political and economic constraints.

Subsequently the new government in 1999 had decided to improve public social services delivery through its devolution plan. By 2001 the ADB and other donors became concerned about the inadequate impact of SAPI and SAPII, and the future implementation of SAPII after the devolution program was well underway. The ADB thus diverted approximately \$43 million towards drought relief assistance and disbursed the remaining funds to the provinces and closed the project by December 2002.

With particular reference to the SAP there are several lessons to be learnt that are well documented in evaluation reports, among others these include: the need for prioritization with clearly stated guiding principles and time sequencing of policy reforms, the need to focus on governance issues through reforming institutional structures rather than using non-responsive traditional institutions and structures that are unable to deliver, the need to overcome resistance from government functionaries or by-passing them in terms of involving the private sector/NGOs directly in service delivery, and the need to focus on outcomes rather than on inputs and outputs.

ADB's Program and Future Strategy for the Sector

In education the ADB's sectoral strategy emphasizes access to quality basic education, especially for females, community/NGO participation in management and monitoring of schools and adequate provision of recurrent expenditures for teachers' training, school supplies and improved curriculum. In Health, expanded access for females, beneficiaries' participation, private sector involvement, decentralized management and adequate provisions of basic medicines are some of the main sectoral concerns. In Population the ADB

emphasized the need for integrated services with basic health service.

While the SAP experience showed that lack of resources is a constraint, it also showed that mismanagement of resources resulting in poor delivery of services is a more pressing concern. Though Government recognizes the need to improve the human development indicators, the need to achieve fiscal stabilization precludes enhanced allocations for these sectors in the medium term and underscores the utilization of available resources more effectively and efficiently.

ADB's approach in social sectors continues to focus on the provision of access to basic human needs. Assistance in education focuses on supporting the expansion of quality basic education particularly for girls in rural areas and improving access for gender parity. Quality improvements and the system's capacity building continue to be major concerns. Community participation and involvement of NGOs and the private sector are new elements of education and other social sector projects, in order to promote ownership and accountability for quality improvement and increasing enrollment and retention in the case of education and quality service delivery in case of health and population.

The Government is relying heavily on the devolution program to make a difference by promoting competition, ownership and accountability in the delivery of public services and by involving people more actively in community issues. ADB's strategy aims to assist the Government in making devolution a success. The activities to be

supported by ADB include (i) improving provincial public resource management capacity (ii) establishing decentralized financing, planning and delivery of selected social services (iii) improving quality of primary education by supporting changes in governance structure-institutions and incentives, promoting public-private/civil society partnerships in the context of devolving service responsibilities to local government, and (iv) improving municipal services in the context of devolving of municipal functions to local government, with particular focus on service for the poor.

Key Features of Ongoing and Future Loans/TA in the Sector

ADB's overall strategy in the health and education sectors identifies human development with a particular emphasis on women, as the country's priority. Thus the program focus is on female education, nutrition, population and improvement in primary healthcare for women and children, with private sector participation and beneficiary participation and ownership. Ongoing projects in the education sector include the \$78 million Middle School Project,⁷¹ \$60 million Technical Education Project⁷² and \$40 million Second Science Education Sector.⁷³ While in the Health sector the \$47 million Women's Health project⁷⁴ is ongoing and the \$36 million Reproductive Health⁷⁵ project is about to start. The women's health project was approved in 1999 in all provinces to expand service provision, develop district health systems that are women friendly, and strengthen human and institution capacity to improve women's health in the long term. Two projects for \$100 million

71. Loan 1278-PAK(SF): Middle School Project for \$78 million approved on 2 December 1993.

72. Loan 1373-PAK(SF): Technical Education for \$60 million approved on 19 September 1995.

73. Loan 1534-PAK(SF): Second Science Education Sector for 40 million approved on 11 September 1997.

74. Loan 1671-PAK(SF): Women's Health for \$47 million approved on 16 March 1999.

75. Loan 1900-PAK(SF): Reproductive Health for 36 million approved on 20 December 2001.

are programmed for 2003-2004, including the \$30 million Early Childhood Development project, the \$50 million Technical Education Project.

The recently approved \$75 million Decentralized Elementary Education project, in 16 districts of the Sindh province and urban slums of Karachi, supports the decentralization of education services.⁷⁶ Through this intervention, 1,400 primary schools for females will be upgraded to elementary level and along with 2,000 existing elementary schools, they will be provided with substantial staff and resources to raise the quality of learning and efficiency. It will involve communities to increase enrollment and reduce the number of dropouts through School Management Committees where both teachers and parents are represented, and build capacity at the school-community, sub-district, district and provincial education offices to better plan, manage, budget and monitor school performance, especially attendance and to strengthen local decision making and accountability.

A series of Decentralized Social Services (DSS) projects have been programmed for approximately \$120 million in Sindh during 2003, \$150 million for Punjab in 2004, for \$70 million for Balochistan in 2005 and for \$100 million for NWFP in 2006 in the pipeline. The objectives of these programs are to improve the social status of Pakistan's poor citizens, strengthen local governments, and facilitate sector reforms to improve efficiency, equity, effectiveness and sustainability of social services. Each project will provide funds that districts may draw on

through their annual plans to address specific constraints in improving social services. The fund may be used to support gaps in service delivery requiring recurrent or development spending in all social sectors. A separate fund will be used to facilitate reforms, capacity building, monitoring and evaluation, and other provincial investments supporting the improvement of service delivery. Closely related issues are the inter-government linkages, decision-making processes, and, in particular, strengthening planning and financial management capacities of local governments. The facilitation of predictable inter-governmental fiscal transfers is meant to take place under the aegis of the PFCs. In addition to PPTA for \$400,000 for DSS (Balochistan) and DSS Capacity Building ADTA for \$400,000 Sindh, PPTAs and ADTAs have been programmed in 2006 to assist in coordinating the DSS planning and management

A \$50 million project for the Restructuring of Technical Education and Vocational Training System is also in the pipeline for 2004, for which TA assistance is currently underway.⁷⁷

Other ongoing TAs include: Support for the Implementation of the National Policy and Action Plan to Combat Child Labor.⁷⁸ The ADB is supporting the government in increasing the effectiveness of the enforcement of child labor laws, and promoting self monitoring by business. Through its rural development program in Sindh, ADB is also addressing the issue of bonded labor in partnership with concerned local governments and NGOs.

76. Loan 1916-PAK(SF): Decentralized Elementary Education (Sindh) for \$75 million approved on 19 September 2002.

77. TA 4048: Restructuring of Technical Education and Vocational Training System for \$150,000 approved on 18 December 2002.

78. TA-3682: Support for the Implementation of the National Policy and Action Plan to Combat Child Labor for \$150,000 approved on 4 July 2001.

There is an ongoing PPTA on the Early Childhood Development (ECD) Project supported by a grant of \$500,000.⁷⁹ The proposed project will be around \$30 million and its objective will be to improve the development conditions of children. By reducing the prevalence of underweight, anemic and stunted children, providing integrated services delivery in health and nutrition with community based initiatives and better child care, and establishing a support strategy that will improve the capacity of the local governments and local NGOs to assist communities in planning, financing and monitoring of ECD activities. Under the TA it is proposed to carry out a feasibility study in selected districts of the four provinces in order to explore the

possible project intervention.

The ADB will also provide \$400,000 for a PPTA to prepare a Family Protection Project (included in the pipeline for 2005 for \$30 million) with the goal to provide the Government with a comprehensive strategy to combat domestic violence and violence against women in the family through implementation of the National Strategic Framework for Family Protection. The pipeline also includes a Social Health Insurance Project whereby \$400,000 will be provided for a PPTA during 2005 and a loan of \$50 million during 2006. The project will evaluate social protection and will help establish a social health insurance system in the country.

79. TA-3975: Early Childhood Development (JSF) for \$ 500,000 approved on 5 November 2002.

List of Approved Loans in the Social Sectors
(as of 31 December 2002)

| Loan No. | Project Name | Net Amount (\$ million) | Milestone Dates | | Implementation Period (years) |
|----------|--|----------------------------|-----------------|----------------|----------------------------------|
| | | | Approval | Date Closed | |
| 1 | 0419 SF Technical Teachers' Training & Polytechnic Institute | 18.74 | 29-Oct-79 | 20-Nov-92 | 13.07 |
| 2 | 0562 SF Health & Population | 10.69 | 15-Dec-81 | 22-Oct-90 | 8.86 |
| 3 | 0710 SF Second Health & Population Project | 10.78 | 29-Nov-84 | 29-Apr-94 | 9.42 |
| 4 | 0759 SF Science Education for Secondary Schools Sector Project | 17.81 | 28-Nov-85 | 26-Jan-95 | 9.17 |
| 5 | 0850 SF Third Health Project | 21.00 | 29-Oct-87 | 8-Aug-96 | 8.78 |
| 6 | 0977 SF Primary Education (Girls) Sector Project | 42.61 | 26-Oct-89 | 21-Mar-97 | 7.41 |
| 7 | 1210 SF Teacher Training Project | 21.43 | 15-Dec-92 | 18-Jul-02 | 9.59 |
| 8 | 1277 SF Population Project | 23.07 | 2-Dec-93 | 8-Jun-00 | 6.52 |
| 9 | 1301 SF Social Action Program (Sector) Project | 103.15 | 23-Jun-94 | 18-Nov-97 | 3.41 |
| 10 | 1493 SF Social Action Program (Sector) Proj. II | 157.37 | 28-Nov-96 | 12-Dec-02 | 6.04 |
| | Subtotal/Average | 426.65 | | | 8.23 |
| | Ongoing Loans | | | | Age |
| 11 | 1200 SF Health Care Development | 42.85 | 1-Dec-92 | | 10.09 |
| 12 | 1278 SF Middle School | 48.23 | 2-Dec-93 | | 9.08 |
| 13 | 1373 SF Technical Education | 46.60 | 19-Sep-95 | | 7.29 |
| 14 | 1454 SF Second Girls Primary School Sector | 41.73 | 15-Aug-96 | | 6.38 |
| 15 | 1534 SF Second Science Education Sector | 39.24 | 11-Sep-97 | | 5.31 |
| 16 | 1671 SF Women's Health | 45.55 | 16-Mar-99 | | 3.80 |
| 17 | 1900 SF Reproductive Health | 38.54 | 20-Dec-01 | | 1.03 |
| 18 | 1916 SF Decentralized Elementary Education | 76.41 | 19-Sep-02 | | 0.28 |
| | Subtotal/Average | 379.16 | | | 5.41 |
| | Total | 805.81 | | | |

List of Approved TAs in Social Sectors
(as of 31 December 2002)

| TA No. | Project Name | Type | Revised Amount (\$ million) | Milestone Dates | | Implementation Period (years) | |
|--------|--------------|--|-----------------------------|-----------------|-------------------|-------------------------------|-------------|
| | | | | Approval | Financial Closing | | |
| 1 | 312 | Upgrading of Hospitals & Training of Para Technicians | PP | 0.170 | 13-Nov-79 | 1-Jul-81 | 1.63 |
| 2 | 339 | Agro-Technical Education | PP | 0.147 | 28-Feb-80 | 1-Dec-81 | 1.76 |
| 3 | 538 | Second Health & Population | PP | 0.050 | 12-Sep-83 | 1-Feb-85 | 1.39 |
| 4 | 604 | Science Education for Secondary Schools | PP | 0.150 | 6-Jun-84 | 1-Dec-88 | 4.49 |
| 5 | 639 | Maintenance & Repair of Bio-Medical Equipment | AO | 0.500 | 29-Nov-84 | 1-Jun-92 | 7.51 |
| 6 | 766 | Third Health & Population | PP | 0.236 | 15-May-86 | 1-Dec-87 | 1.55 |
| 7 | 806 | Second Polytechnic Institutes Project | PP | 0.150 | 16-Oct-86 | - | - |
| 8 | 907 | Primary Education (Girls) Project | PP | 0.175 | 13-Oct-87 | 1-Feb-89 | 1.31 |
| 9 | 913 | Health Manpower & Training Plan | AO | 0.383 | 29-Oct-87 | 1-Dec-90 | 3.09 |
| 10 | 999 | Technical & Vocational Education Dev Study | AO | 0.495 | 1-Jul-88 | 1-Mar-94 | 5.67 |
| 11 | 1245 | Marine Outfall Study | AO | 0.282 | 14-Dec-89 | 1-Dec-93 | 3.97 |
| 12 | 1297 | SSTA for Dev. of Education Master Plan | AO | 0.100 | 10-May-90 | 1-Mar-94 | 3.81 |
| 13 | 1314 | 4th Health & Pop. (Manpower Dev't) (JSF) | PP | 0.100 | 1-Jun-90 | 1-Dec-91 | 1.50 |
| 14 | 1386 | Teacher Training Project (by JSF & Gov't. of Norway) | PP | 0.260 | 11-Oct-90 | 1-Feb-98 | 7.32 |
| 15 | 1460 | Education Prog. for Tech., Educ & Vocational Training (JSF) | AO | 0.160 | 26-Dec-90 | 1-Jun-99 | 8.44 |
| 16 | 1687 | Lower Secondary Education | PP | 0.300 | 3-Apr-92 | 1-Jun-96 | 4.16 |
| 17 | 2005 | Institutional Dev of the Min. of Population Welfare | AO | 0.700 | 2-Dec-93 | 1-Aug-99 | 5.67 |
| 18 | 2106 | Instit. Strength. & Impact Assessment Project (Part A) | AO | 0.520 | 23-Jun-94 | 1-Jun-98 | 3.94 |
| 19 | 2142 | Second Primary Education for Girls Project (JSF) | PP | 0.250 | 19-Aug-94 | 1-Jun-98 | 3.79 |
| 20 | 2149 | Technical Education | PP | 0.100 | 14-Sep-94 | 1-Jun-98 | 3.72 |
| 21 | 2289 | Impact Assessment of Policy & Instit. Reform Measures (Netherland) | AO | 0.080 | 27-Dec-94 | 1-Aug-98 | 3.60 |
| 22 | 2358 | Secondary Science Education (JSF) | PP | 0.450 | 6-Jul-95 | 1-Jun-99 | 3.91 |
| 23 | 2475 | Second Social Action Program | PP | 0.100 | 15-Dec-95 | 1-Jun-99 | 3.46 |
| 24 | 2547 | Nonformal Education for Rural Women (JSF) | PP | 0.600 | 23-Mar-96 | 1-Dec-00 | 4.70 |
| 25 | 2576 | Public-private Partnership In Health Study (JSF) | AO | 0.450 | 31-May-96 | 1-Jun-98 | 2.00 |
| 26 | 2577 | Women's Health Project (JSF) | PP | 0.500 | 4-Jun-96 | 1-Apr-00 | 3.83 |
| 27 | 3122 | Technical Education Facilities Rehab Plan | AO | 0.150 | 15-Dec-98 | - | - |
| | | Subtotal/Average | | 7.558 | | | 3.85 |
| | | Ongoing TAs | | | | | |
| 28 | 3144 | Primary School Quality Improvement | PP | 0.500 | 23-Dec-98 | 30-Jun-02 | |
| 29 | 3386 | Health Sector Reform In North West Frontier Province | AO | 0.500 | 29-Dec-99 | 30-Jun-02 | |
| 30 | 3387 | Reproductive Health (JSF) | PP | 0.300 | 29-Dec-99 | 31-Jul-01 | |
| 31 | 3975 | Early Childhood Development (JSF) | PP | 0.500 | 5-Nov-02 | 31-May-03 | |
| 32 | 4048 | Restructuring of Technical Education & Vocational Training System | PP | 0.150 | 18-Dec-02 | 31-Jul-03 | |
| 33 | 2840 | Multi-Donor Support Unit of the Social Action Program | AO | 0.600 | 13-Aug-97 | 31-Aug-02 | |
| 34 | 4047 | Sindh Devolved Social Services | PP | 0.120 | 18-Dec-02 | 31-May-03 | |
| | | Subtotal | | 2.670 | | | |
| | | Total | | 10.228 | | | |

ENERGY

| | |
|--|---------------------|
| ADB Lending 1968-2002 | : \$3,062.0 million |
| Percentage of ADB lending to PAK 1968-2002 | : 24% |
| Ongoing commitments as of 31 December 2002 | : \$686.389 million |
| Disbursement as of December 2002 | : \$467.44 million |
| Percent Disbursed as of December 2002 | : 68.1% |

Background

Petroleum products account for about half of the energy consumption in Pakistan, and their share has been increasing. The total proven original recoverable reserves of oil are estimated at 668 million barrels and the remaining recoverable reserves at 252 million barrels. Pakistan's oil sector has experienced steady growth, while consumption of petroleum products has risen on an average by about 6 percent per annum in the last six years, the indigenous production has remained static at about 50,000 to 60,000 barrel per day during the last six years. Oil accounts for 42.8 per cent of the primary energy in Pakistan but is largely imported. The high dependence on imports has a major impact on the economy. The current production of oil in Pakistan meets around 15 per cent requirements of over 18 million tons per year. Petroleum products consumption is increasing by about 4-5 percent per annum. Crude oil produced is transported by pipelines/bowzers to the four refineries, one in the North, at Mehmood Kot in mid country and the other two located in Karachi. The total refining capacity has jumped up from around 7.5 million tons a year to 11 million tons per annum with the commissioning in September 2000 of mid-country PARCO Refinery.

Pakistan has a well-developed and integrated infrastructure of transporting, distributing and utilizing natural gas. Current gas production in the country is 2.4 billion cubic feet per day (bcfd) and its share

in the energy mix is around 38 percent. Gas production and consumption during the last six years has risen by 5 percent per annum and indications are that it may reach 3 bcfd by 2005. The underlying demand far exceeds the indigenous supply, which has increased 58 percent from 1.4 bcfd in FY1991 to 2.2 bcfd in FY2000. It is envisaged that increase in gas usage will continue with some of the independent power projects (IPPs) switching to dual firing. This will decrease the fuel import requirement and provide an opportunity for domestic gas producers to increase their production. Estimates show that of the 36.18 trillion cubic feet (tcf) original recoverable gas reserves, 13.07 tcf have so far been consumed.

Government Policy and Institutional Framework

The energy sector has been in the forefront of the Government's program of deregulation restructuring and privatization since the early 1990s. This was also necessitated by the increasing costs and diminishing returns in the sector and the constraints in financing the costs of long term energy development programs. The Government's 8th Five Year Plan (1993-94 to 1998-99) recognized that "issues facing the Energy Sector are not only restricted to meeting demand in a rational manner but also to restructure hitherto prominently public sector monopolies and to address on a crash and long-term basis, the limitations of the presently proven energy resources." The

Plan thus promoted conservation, demand management and rational use of energy resources.

Increase in self reliance by exploration of indigenous resources, rationalization of prices and decentralization and regulation of the energy sector agencies to increase self-financing and involvement of the private sector have been the major thrust of Government policy in the sector. The ensuing Power and Petroleum Sector Policies in the early 1990s thus enabled public-private partnerships in these key sub-sectors, with assistance from the major donors.

Government policy has focused on the restructuring of the power sector by breaking up the monopoly of the two large vertically integrated public utilities-WAPDA and the Karachi Electric Supply Company (KESC) in the power sector and the restructuring of the two gas transmission and distribution companies Sui-Southern Gas Company Ltd. (SSGC) and Sui-Northern Gas Pipelines Ltd. (SNGPL). Management of these public utilities had been highly politicized and they suffer from inefficient operations and issues related to weak governance.

The Cabinet Committee on Energy, chaired by the Prime Minister, is largely responsible for developments in the sector through review and policy of programs and investments in the Petroleum and Natural Gas sub-sectors. The supporting ministries include the Ministry of Planning and Development, Ministry of Water and Power and the Ministry of Petroleum and Natural Resources (MPNR). A National Electric Power Regulatory Authority (NEPRA) was set up in 1995 to act as an overseer and regulator of generation, transmission and distribution activities in the power sub-sector, while the Oil and Gas Regulatory Authority (OGRA) has been set up recently to regulate the oil and gas sub-sector.

Although WAPDA and KESC are no longer pure monopolies in power generation, their hold on transmission and distribution makes them the sole-buyers of power produced by the 16 IPPs who own 5,417MW of generation capacity. WAPDA accounts for about 84 percent of electricity sales in Pakistan while the remaining 16 percent is by the KESC. WAPDA and KESC continue to hold a monopoly over transmission and distribution throughout the country by means of numerous power distribution companies (DISCOs). Although the restructuring of WAPDA should have led to the setting up of a transitional entity Pakistan Electric Power Company (PEPCO), a National Transmission and Distribution Company (NTDC) and independent, corporatized power generation companies, this has not happened thus far.

Within the MPNR, Petroleum Concessions are granted by the Directorate General of Petroleum Concession (DGPC) while other activities relating to gas are handled by the Directorate General of Gas (DGG). The government-owned Oil and Gas Development Co. Ltd. (OGDCL) is the public sector entity responsible for oil and gas exploration and development. A large number of international companies are engaged in exploration under joint-venture arrangements with OGDCL and the Government. Transmission and distribution of gas is carried out largely by SNGPL in the north and SSGC in the south, while the transmission network of Mari Gas Company supplies gas to three large fertilizer (urea) producers.

History of ADB's Operations and Implementation Experience

The energy sector has been one of the largest recipients of ADB assistance.

Together with the World Bank and JBIC, donors have provided almost thirty percent of the external financing requirements of the two sub-sectors. In the gas sector, the ADB assisted projects in the South of the country while the World Bank limited its involvement to the north.

With about 21 percent of ADB lending to Pakistan, the power sub-sector has historically been the largest recipient of ADB assistance. Sixty four percent of lending to the sector was directed to power generation (39 percent hydropower, and 25 percent thermal power), and the remaining 36 percent for power transmission and distribution. Three fourths of the ADB's assistance (\$1,575 million for 13 loans) was provided to WAPDA and the rest to KESC. Together with the World Bank and JBIC, the ADB has been the major source of external assistance to the sector, having provided about one third of total external resources over the 1984-1996 period. The ADB is also, by far, the main provider of external assistance to KESC for a total of \$180 million. In power generation, the ADB has significantly contributed to major multi-donor undertakings such as the Tarbela for a total of \$ 300 million and Ghazi Barotha Hydropower schemes for a total of \$300 million.

ADB financed nine projects in excess of \$ 360 million in the gas sub-sector through 11 loans between 1974 and 1991. The projects' largely focused on increasing the availability of gas by alleviating constraints on production, transmission and distribution. Initial assistance in the sector involved increasing the transmission capacity of the SSGC system. Subsequent assistance included the development of the Pirkoh gas field, its integration into the national system, and the development of various small gas fields. In general a good balance was maintained between lending and non-lending activities. Between 1985 and 1991 the ADB

provided six AOTAs to the gas sub-sector in the areas of institutional strengthening, environmental and safety aspects, and for a Hydrocarbon Sector Strategy Study in 1991. For details please refer to Table.

As it became apparent that the private sector should take an increasingly important role in the sector, the ADB and other donors reduced their involvement in the sector. Under the 1997 structural adjustment program the Government agreed to the privatization of the major Government oil and gas corporations including SSGC, SNGPL and the OGDCL. The OGRA was recently made fully operational and is expected to become a credible, effective and autonomous organization.

Historically ADB projects mainly provided assistance to WAPDA, KESC, SSGC and significantly contributed towards large undertakings such as Tarbela and Ghazi Barotha Hydropower projects. During the 1990s the ADB provided seven loans and 29.4 percent of its lending to the energy sector to augment generation, transmission and distribution networks of the power sub-sector and to further develop the existing oil and gas fields. The key lessons learned from assistance to the power sector was that supporting capacity expansion without addressing the issues of corporate governance only substitutes one set of problems with another.

A majority of the completed projects in the energy sector were generally classified as successful. There was close conformity with project design despite several time and cost overruns. However there were several inadequacies in compliance with addressing wider systemic and governance issues such as system's losses, efficiency, management and organization at the beneficiary institutions such as WAPDA, KESC and SSGC. The key lessons learned from assistance to the

sector was that supporting capacity expansion without addressing the issues of corporate governance only substitutes one set of problems with another.

ADB's Program and Future Strategy for the Sector

The \$350 million Energy Sector Restructuring Program Loan (ESRPL) approved in December 2000⁸⁰ and the reforms agreed under the project include the implementation of a strategic plan for restructuring, corporatization and privatization and to provide a legal framework for their implementation, in close coordination with other donors, particularly the World Bank. This includes the corporatization of WAPDA, OGDCL, their financial restructuring and privatization of key corporate entities in the two sub-sectors. It also included settlement of disputes with the IPPs strengthening of regulatory aspects. To this end, under the Petroleum Regulatory Authority (PRA) Act after establishing NEPRA the Government has created the OGRA and the Petroleum Regulatory Board. It has approved the restructuring and privatization plan of SNGPL and SSGC and has received an Expression of Interest for the sale of KESC.

The Bank's strategic focus will remain on support for deregulation, privatization and greater use of indigenous energy resources while attracting foreign investment. The ADB also sees tremendous scope in greater regional cooperation vis-à-vis transportation i.e. the road network and the energy infrastructure. While the main investors in such activities will be from the private

sector, the ADB has a potential catalytic role in review and reform of regulation, support to feasibility studies and mitigation of sovereign risk through its guarantee operations.

Key Features of Ongoing and Future Loans/TAs in the Sector

The first tranche of the ESPRL of \$200 million was released in two parts in December 2000 and May 2001. The second tranche of \$75 million was planned for December 2001, has been delayed to mid-2003, to coincide with the privatization of one GENCO (power-generation company) and one DISCO. The third tranche will be disbursed upon the impending privatization of KESC. No new loans have been programmed for the sector until the policy objectives of the ongoing ESPRL are met.

Since 1999 a total of \$3.0 million has been provided as Technical Assistance to the sector. During 2000 an AOTA⁸¹ provided to support the privatization of KESC. Under this TA a new privatization advisor was engaged to review the work of previous financial advisors, provide regulatory advice to the Government and the ADB in order to promote competitive market structure for efficiency gains, carry out financial due diligence and develop a privatization strategy along with evaluation of bids of interested parties. Another AOTA was provided in 2000 for the capacity building of NEPRA⁸² in developing guidelines for transmission and distribution companies, assisting NEPRA to review the Grid and other Codes and to strengthen

80. The ESPRL is expected to be extended till December 2003.

81. TA-3502: Support for Privatization of Karachi Electric Supply Corporation for \$1.0 million approved on 22 September 2000.

82. TA-3409 Capacity Building of NEPRA for \$1.0 million approved on 6 March 2000.

procedures for handling customer complaints.

In 2001 a TA for Restructuring of the Gas Sector⁸³ was approved. Its scope included: the analysis of the gas transmission and distribution industry structure, development/evaluation of viable options for restructuring of the industry and its implementation, examining options for enhancing sector efficiency, competition and attraction of foreign capital. This includes development of financial, legal, social and technical aspects, which build upon the selected industry structure and enables the implementation of the restructuring plan and successfully conclude the privatization transactions in the sector.

An AOTA was successfully completed in 2002 that reviewed Government strategy for gas sector development and provide for the direction and future plan in the sector. Recent discoveries of additional gas reserves in the country require the building of additional transmission infrastructure. \$250 million has been earmarked for a proposed project that may serve as a catalyst to attracting private investment for new transmission pipelines.

A PPTA of \$600,000 is also currently in the pipeline for 2004 for a potential \$200 million Renewable Energy Development Project to be approved by 2005. Under this

project assistance will be provided to replicate the Chashma Hydropower Project in smaller models of 40-50 MW on the irrigation channels in NWFP to provide electricity to small off-grid villages.

In December 2002 a \$1.37 million Regional Technical Assistance (RETA) was approved for a potential \$2.0-2.5 billion Turkmenistan-Afghanistan-Pakistan gas pipeline project. This potential project will consist of a 1,700 kilometer pipeline to transport 20 billion cubic feet of natural gas annually from the Dauletabad fields in Southeast Turkmenistan to consumers in Afghanistan, Pakistan and possibly India. The estimated design and construction period for this pipeline project is four years.

The pipeline includes a \$50 million Cleaner Fuel Project in 2004 whereby the air quality in large metropolises will be improved through introduction of new bus fleets in Lahore and Karachi that use CNG as fuel source. This will also lead to a reduction in the annual import of volume of fuel oil and diesel. A Power Transmission and Distribution Enhancement Project is in the pipeline for 2006. The goal of this project is to ensure a reliable and high quality power supply to an ever-increasing number of industrial, commercial and retail consumers, which underpins national economic growth and the reduction of poverty.

83. TA-3711 Restructuring the Gas Sector for \$1.0 million approved on 29 August 2001.

List of Approved Loans in the Energy Sector
(as of 31 December 2002)

| Loan No. | Project Name | Net Amount (\$ million) | Milestone Dates | | Implementation Period (years) | |
|----------|--------------|---|-----------------|----------------|----------------------------------|-------------|
| | | | Approval | Date Closed | | |
| 1 | 0099 | Power Generation, Transmission & Distribution | 14.300 | 12-Oct-72 | 28-Jul-78 | 5.79 |
| 2 | 0100 | SF Power Generation, Transmission & Distribution | 12.200 | 12-Oct-72 | 21-Dec-78 | 6.19 |
| 3 | 0150 | Power Generation Transmission & Distribution (Supplementary) | 6.800 | 22-Nov-73 | 3-Oct-78 | 4.87 |
| 4 | 0151 | SF Power, Generation, Transmission & Distribution (Supplementary) | 2.200 | 22-Nov-73 | 18-Jan-80 | 6.16 |
| 5 | 0168 | SF Mangla Hydropower | 3.900 | 17-Dec-73 | 18-Dec-80 | 7.01 |
| 6 | 0169 | Mangla Hydropower | 12.592 | 17-Dec-73 | 2-Sep-85 | 11.72 |
| 7 | 0181 | Sui-Karachi Gas Pipeline | 29.063 | 14-Mar-74 | 27-Feb-80 | 5.96 |
| 8 | 0187 | Sui-Karachi Gas Pipeline (Supplementary) | 12.102 | 6-Aug-74 | 30-Jun-79 | 4.90 |
| 9 | 0200 | SF Tarbela Hydropower | 34.000 | 28-Nov-74 | 4-Mar-82 | 7.27 |
| 10 | 0201 | Tarbela Hydropower | 12.955 | 28-Nov-74 | 20-May-85 | 10.48 |
| 11 | 0230 | SF Gas Turbine Generation | 22.000 | 26-Aug-75 | 5-Jan-79 | 3.36 |
| 12 | 0332 | Tarbela Hydropower (Supplementary & Extension) | 33.121 | 15-Dec-77 | 15-Aug-85 | 7.67 |
| 13 | 0390 | SF Pipri Thermal Generation | 27.955 | 22-Dec-78 | 16-Apr-85 | 6.32 |
| 14 | 0391 | Pipri Thermal Generation | 22.022 | 22-Dec-78 | 12-Mar-85 | 6.22 |
| 15 | 0470 | Indus Right Bank Pipeline Gas Compression | 14.800 | 30-Sep-80 | 31-Dec-85 | 5.25 |
| 16 | 0505 | SF Load Despatch & Transmission | 66.200 | 22-Dec-80 | 5-Apr-91 | 10.29 |
| 17 | 0516 | SF Pipri II Thermal Generation | 37.338 | 23-Jun-81 | 19-Jan-88 | 6.58 |
| 18 | 0561 | SF Rural Electrification Sector | 25.698 | 15-Dec-81 | 13-Apr-89 | 7.33 |
| 19 | 0565 | Pirkoh Gas Development Project | 44.690 | 22-Dec-81 | 31-Dec-87 | 6.03 |
| 20 | 0578 | SF Pipri II Thermal Generation Project-supplementary | 17.154 | 29-Jul-82 | 18-Apr-86 | 3.72 |
| 21 | 0601 | Tarbela Hydropower Extension Project | 17.719 | 23-Nov-82 | 18-Apr-88 | 5.41 |
| 22 | 0653 | Gas Purification & Compression Project | 11.198 | 17-Nov-83 | 15-Jul-88 | 4.66 |
| 23 | 0660 | SF Guddu Combined Cycle Project | 80.279 | 6-Dec-83 | 6-Dec-91 | 8.01 |
| 24 | 0661 | Guddu Combined Cycle Project | 47.558 | 6-Dec-83 | 7-Nov-90 | 6.93 |
| 25 | 0701 | Tarbela Hydropower Extension(Units 11&12) Project | 108.888 | 25-Oct-84 | 31-Oct-94 | 10.02 |
| 26 | 0702 | SF Tarbela Hydropower Extension(Units 11&12) Project | 25.784 | 25-Oct-84 | 31-Oct-94 | 10.02 |
| 27 | 0760 | Tarbela Units 13 & 14 And 500 KV Transmission Project | 71.620 | 28-Nov-85 | 1-Nov-94 | 8.93 |
| 28 | 0770 | Second Pirkoh Gas Development Project | 40.655 | 12-Dec-85 | 17-Sep-90 | 4.77 |
| 29 | 0824 | WAPDA Tenth Power(Sector Loan) Project | 144.699 | 18-Dec-86 | 13-Apr-95 | 8.32 |
| 30 | 0836 | Indus Right Bank Pipeline Capacity Extension Project | 28.725 | 25-Aug-87 | 21-Oct-91 | 4.16 |
| 31 | 0869 | Oil & Gas Development Project | 29.368 | 3-Dec-87 | 23-Oct-95 | 7.89 |
| 32 | 0925 | KESC Fifth Power (Sector Loan) Project | 98.436 | 24-Nov-88 | 31-Mar-98 | 9.35 |
| 33 | 0929 | Third Pirkoh Gas Development Project | 65.350 | 13-Dec-88 | 20-Jan-00 | 11.11 |
| 34 | 0930 | SF Third Pirkoh Gas Development Project | 46.255 | 13-Dec-88 | 20-Jan-00 | 11.11 |
| 35 | 1073 | WAPDA Eleventh Power Project | 207.082 | 20-Dec-90 | 5-Aug-97 | 6.63 |
| 36 | 1094 | Second Oil & Gas Development Project | 28.151 | 22-Aug-91 | 15-Mar-99 | 7.57 |
| 37 | 1138 | Sui-Southern Gas System Rehabilitation & Expansion Project | 168.986 | 3-Dec-91 | 6-Jan-99 | 7.10 |
| 38 | 1143 | WAPDA Twelfth Power (Sector) Project | 125.000 | 13-Dec-91 | 16-Nov-00 | 8.93 |
| 39 | 1144 | SF WAPDA Twelfth Power (Sector) Project | 128.473 | 13-Dec-91 | 21-Nov-00 | 8.95 |
| 40 | 1808 | SF Energy Sector Restructuring Program | 50.391 | 14-Dec-00 | 20-Dec-00 | 0.02 |
| | | Subtotal/Average | 1975.707 | | | 7.08 |
| | | Ongoing Loans | | | | Age |
| 41 | 1314 | KESC Sixth Power (Sector) | 40 | 22-Sep-94 | | 8.3 |
| 42 | 1315 | SF KESC Sixth Power (Sector) | 41 | 22-Sep-94 | | 8.3 |
| 43 | 1424 | Ghazi Barotha Hydropower | 300 | 16-Jan-96 | | 7.0 |
| 44 | 1807 | Energy Sector Restructuring Program | 300 | 14-Dec-00 | | 2.0 |
| 45 | 1809 | SF Capacity Enhancement in the Energy Sector (TA Ln) | 5 | 14-Dec-00 | | 2.0 |
| | | Subtotal/Average | 686.39 | | | 5.5 |
| | | Total | 2,662.10 | | | |

List of Approved TAs in the Energy Sector
(as of 31 December 2002)

| TA No. | Project Name | Type | Revised Amount (\$ million) | Milestone Dates | | Implementation Period (years) | |
|--------|--------------|---|--------------------------------|-----------------|-------------------|-------------------------------|-------------|
| | | | | Approval | Financial Closing | | |
| 1 | 101 | Mangla Hydropower | AO | 0.150 | 17-Dec-73 | 1-Oct-75 | 1.79 |
| 2 | 118 | KESC Generation & Transmission Feasibility Study | PP | 0.200 | 2-Jul-74 | 1-Mar-77 | 2.67 |
| 3 | 222 | Thermal Power Plants Maintenance | AO | 0.150 | 15-Dec-77 | 1-Nov-83 | 5.88 |
| 4 | 411 | Power Development & Tariff Study | AO | 0.350 | 27-Aug-81 | 1-Dec-87 | 6.27 |
| 5 | 525 | KESC-Site Combined Cycle | PP | 0.050 | 8-Jul-83 | 1-Jul-84 | 0.98 |
| 6 | 704 | Gas Development Project | PP | 0.275 | 13-Sep-85 | 1-Dec-93 | 8.22 |
| 7 | 728 | Operational Strategy Study of Pgcl | AO | 0.250 | 12-Dec-85 | 1-Jun-89 | 3.47 |
| 8 | 763 | Oil & Gas Development | PP | 0.075 | 12-May-86 | 1-Dec-88 | 2.56 |
| 9 | 835 | A Study for the Integrated Operations of Wapda & KESC Systems | AO | 0.481 | 18-Dec-86 | 1-Apr-98 | 11.29 |
| 10 | 869 | Sml-Scl Ppta for KESC Pwr Expansion Project | PP | 0.075 | 6-Apr-87 | 1-Mar-91 | 3.90 |
| 11 | 894 | Technical Services for the Office of Directorate General (Gas) | AO | 0.266 | 25-Aug-87 | 1-Dec-93 | 6.27 |
| 12 | 900 | Southern Gas Transmission & Distribution | PP | 0.440 | 7-Sep-87 | 1-Dec-93 | 6.24 |
| 13 | 1078 | Second Oiland Gas Development (JSF-Financed) | PP | 0.315 | 1-Dec-88 | 1-Dec-89 | 1.00 |
| 14 | 1447 | Loan & TA Grant - Power & Institutional Study | AO | 0.788 | 20-Dec-90 | 1-Apr-98 | 7.28 |
| 15 | 1448 | Loan & TA Grant - Development of a Mis for WAPDA | AO | 0.415 | 20-Dec-90 | 1-Apr-98 | 7.28 |
| 16 | 1512 | SSTA for a Prog. for Safe Repair & Operation of Gas Processing | AO | 0.100 | 15-Apr-91 | 1-Mar-95 | 3.88 |
| 17 | 1616 | Hydrocarbon Sector Strategy Study | AO | 0.600 | 20-Nov-91 | 1-Aug-94 | 2.70 |
| 18 | 1618 | Financial Restructuring & Mngt Strng of SSGC | AO | 0.860 | 3-Dec-91 | 1-Apr-98 | 6.33 |
| 19 | 1619 | Env'l. Safety & Efficiency Improvements of SSGC's Ops.(France) | AO | 0.680 | 3-Dec-91 | 1-Apr-98 | 6.33 |
| 20 | 1625 | Loan/TA Grant-power Gen. Coordination Imp & Tariff Ting | AO | 0.585 | 2-Jan-92 | 1-Apr-98 | 6.25 |
| 21 | 1655 | SSTA for KESC Organizational & Financial Restructuring Study | AO | 0.075 | 13-Jan-92 | 1-Jun-94 | 2.38 |
| 22 | 2163 | Demand Side Management Study | AO | 0.090 | 22-Sep-94 | 1-Aug-99 | 4.86 |
| 23 | 2525 | Power Efficiency Project (France & Bank) | PP | 0.850 | 16-Jan-96 | - | - |
| 24 | 2594 | Natural Gas Import Study (France) | AO | 0.600 | 26-Jun-96 | 1-Dec-00 | 4.44 |
| 25 | 2809 | Private Hydropower Policy Study | AO | 0.100 | 11-Jun-97 | 1-Jun-00 | 2.98 |
| | | Subtotal/Average | | 8.820 | | | 4.80 |
| | | Ongoing TAs | | | | | |
| 26 | 2162 | KESC Restructuring & Privatization Study | AO | 0.300 | 22-Sep-94 | 31-Mar-03 | |
| 27 | 3409 | Capacity Building of the National Electric Power Regulatory Authority | AO | 1.000 | 6-Mar-00 | 30-Sep-02 | |
| 28 | 3502 | Support for Privatization of Karachi Electric Supply Corporation | AO | 1.000 | 22-Sep-00 | 31-Dec-02 | |
| 29 | 3711 | Restructuring the Gas Sector | AO | 1.000 | 29-Aug-01 | 30-Jun-04 | |
| | | Subtotal | | 3.300 | | | |
| | | Total | | 12.120 | | | |

TRANSPORT AND COMMUNICATION

| | |
|--|---------------------|
| Total ADB Lending 1968-1999 | : \$948.0 million |
| Percentage of Total ADB Lending to PAK (1968-99) | : 8% |
| Ongoing Commitment as of 31 December 1999 | : \$629.974 million |
| Disbursements | : \$296.24 million |
| Percent Disbursed | : 47% |

Background

Transport is an important sector of the economy in Pakistan and contributes almost 6 percent to GDP. Road transport is the dominant mode of transport in the country, carrying 91 percent of all passenger traffic and 95 percent of all freight traffic in the country. During the 1990s the demand for road transport grew by 7-8 percent per annum, as GDP grew by 4-5 percent. The total number of registered vehicles doubled from 1.8 million in 1990 to more than 4.1 million in 2000, while the road network doubled to 250,000 kilometers within the same period. Efficient road transport and improved access to less developed areas while essential for poverty reduction and economic growth in the country, is totally lacking in many parts of the country. Although the transport network has become more extensive over the years, investment in the sector has not matched demands of greater mobility and trading opportunities. Resource constraints have also led to inadequate road rehabilitation and maintenance. There is also an urgent need to develop management and professional skills in institutions that are tasked with managing the transport network. The need for institutional strengthening and well-designed sector development plans are particularly apparent at the provincial level. Even in the largest province of Punjab the condition of roads is very poor and they suffer from lack of maintenance and capacity constraints.

The Pakistan Railways Network, caters

to large-scale movement of freight as well as passenger traffic, and comprises 7,791 kilometers of track, 577 locomotives and 23,893 freight wagons. During FY 2001-2002 the traffic volume included 69 million passengers and freight carried was 5.9 million tones or 4,688 million freight tones kilometers. Pakistan Railways (PR) has historically suffered from the standard deficiencies of state-owned enterprises including overstaffing, ghost employees, poor maintenance and lack of capital expenditure. Recently, however, the Government has initiated a restructuring process to address major operational and financial issues refurbishment of equipment and bogeys. Similarly, investment in the track has resulted in improvement in running times.

Pakistan has two major operating ports serving 803,943 square kilometers of hinterland as well as offering services for landlocked Afghanistan. The Karachi Port has 28 general cargo berths with draft of 10 to 11.3 m. and three oil jetties-two of which are capable of handling 75,000 dead weight ton (DWT) ships; the third is being reconstructed to serve 75,000 DWT ships. Port Qasim is the second most important deep-sea port for handling Pakistan's foreign trade. It needs a great deal of improvement to reduce pressure on Karachi Port. It has been especially designed to handle bulk cargo so far. During FY2002, 26,692 metric tones of cargo was handled at the Karachi port. A third port is under construction at Gwadar and will be completed by 2007. In

1971, the shipping industry was nationalized and all shipping lines were merged under the Pakistan National Shipping Corporation (PNSC).⁸⁴ PNSC has a fleet of 22 vessels and its subsidiary, the National Tanker Company, owns one tanker. Due to its small size and inadequate capacity, the national fleet is presently shipping approximately 10 percent of regular cargo and 25 percent of liquid cargo.

Pakistan is linked to almost all the countries of the world through five international airports, namely: Karachi, Islamabad, Lahore, Peshawar and Quetta. Air traffic and service providers have suffered to a great extent following the war against Afghanistan and more recently the Iraq war. This has constrained and limited the service availability for air transport and cargo opportunities. A package of incentives has recently been introduced to attract foreign airlines to route flights through Pakistan. Reduction of landing/ housing charges by 50 percent at Karachi for flights has also been implemented. In telecommunication the Pakistan Telecommunication Authority (PTA) has been set up recently and PTCL is being privatized.

Government Policy and Institutional Framework

The Ministry of Communication is responsible for national highway development and maintenance through the National Highway Authority (NHA), and for road transport regulations and policies, shipping, and ports. Construction and maintenance of national highways are responsibility of the Federal Government, which finances their development and maintenance through NHA and Provincial Communications and Work Departments (CWD). The NHA is an

autonomous highway agency with a functional structure and decentralized implementation through regional offices at provincial levels. The ADB and the World Bank have provided assistance to reorganize and commercialize the NHA, shifting its focus towards a network operator and service provider role and strengthening of its financial systems and governance.

The MELGRD is entrusted with rural development. MELGRD through the Federal Rural Development Engineering cell is the coordinator of rural road projects. Planning and budgeting capacities at the provincial CWD is weak and modern road asset management and maintenance systems are not fully institutionalized and integrated into the operations of the CWD. Due to the devolution program the CWDs are being restructured at the provincial level while new district administrations are being set up. Up until recently the four provincial highway departments were responsible for 90,000 km of road; some parts of that network are now being transferred to the district administration. For instance in Punjab 34 new district administrations have been created, consequently 34,479 or almost 79 percent of all provincial road networks have been transferred to the district administration along with 11,000 staff. These major structural changes will have implications for the effectiveness and efficiency of the sector and the working of district administrations.

History of ADB's Operations and Implementation Experience

In the 1970s and the early 1980s, of the total ADB lending to the Transport and Communications sector, 65.2 percent was directed to road transport, 6.4 percent or \$49

84. PNSC has 90.2 percent government ownership and 4.9 percent private sector ownership.

million to ports development, and 28.4 percent or \$200 million to telecommunications. Assistance to the ports sector only included two loans for Port Qasim Development (one project),⁸⁵ both of which are now closed. The three telecommunication loans⁸⁶ are now all closed. Assistance to the road sub-sector started in 1985 and included three farm-to-market/rural roads projects,⁸⁷ one bridge project,⁸⁸ and one provincial highway project.⁸⁹ To-date ADB's total financing for roads projects is \$747 million.

The ADB's approach to the road sector has largely been one of working at the provincial level and targeting provincial road networks in the country. In the 1990s the ADB approved six loans totaling \$597 million covering umbrella programs in all four provinces. However, a number of implementation delays and problems were faced. Some major projects in the sector include the Provincial Highways Project, various Farm-to-Market Roads as well as assistance for construction of the Sukkur Bridge.

One of the key issues with highway projects in the past has been the very low (only 22 percent) levels of total commitments disbursed. Implementation of four umbrella projects suffered from fragmentation of efforts, and coordination problems, which led to project implementation delays. Adopting a provincial focus, the identified weaknesses in the umbrella projects were addressed in subsequent provincial road

projects for Sindh and Punjab. An overall national framework for policy reforms in the road sector will be put in place under the newly approved Road Sector Development Program (RSDP)

ADB's Program and Future Strategy for the Sector

ADB strategy at the present time is to focus on sustainable development of provincial roads, institutions and networks allowing for ownership, accountability and enhanced development impact. The emphasis is on policy reforms at the provincial and district level, support for capacity building at the provincial and district level, removal of capacity bottlenecks and physical rehabilitation of key provincial road networks. This is expected to have a positive impact on poverty reduction and poor economic growth.

Given the large number of policy and institutional issues a sector wide approach towards road development has been adopted by ADB to sequence interventions in individual provinces over several years. The focus of ADB operations in the road and road transport sector concentrates on developing and integrating provincial and rural roads through provincial level interventions that will promote a strategic approach for selection of specific road links, better management of O&M and improved technical capabilities and development of domestic (private) contracting industry.

85. Loan 0279 & 0280 Port Qasim for \$50 million approved on 18 November 1976.

86. Loan 0570-(PAK)SF: Telecommunications Project for \$21 million approved on 17 June 1982.
Loan 0761-(PAK): Second Telecommunications Project for \$70 million approved on 28 November 1985.
Loan 1025-PAK(SF): Third Telecommunications Project for \$110 million approved on 16 August 1990.

87. Loan 0758-PAK(SF): Farm to Market Roads Project for 37.7 million approved on 26 November, 1985.
Loan 0917-PAK(SF): Second Farm to market Roads Project for \$114 million approved on 8 November 1988.
Loan 1401-(PAK)SF: Rural Access Roads for \$125 million approved on 9 November 1995.

88. Loan 1323-(PAK)SF: Sukkur Bridge Project for \$35 million approved on 29 September 1994.

89. Loan 1185-(PAK)SF: Provincial Highways Project for 145 million approved on 5 November, 1992.

The ADB also sees tremendous scope in greater regional cooperation vis-à-vis transportation i.e. the road network and the energy infrastructure. While the main investors in such activities will be from the private sector, the ADB has a potential catalytic role in review and reform of regulation, support to feasibility studies and mitigation of sovereign risk through its guarantee operations.

Key Features of Ongoing and Future Loans/TA in the Sector

A \$200 million assistance for the Road Sector Development Program was approved in 2001 for Sindh,⁹⁰ which looks at policy and institutional reform in the national road agencies and provides specific investment assistance for provincial and rural roads in the province. Private sector development and integration of knowledge industries into the revitalized C&W Department is a key feature of this initiative. A \$150 million was approved for a similar sector Road Sector Development Program in Punjab. The Punjab project consists of three components: (i) an institutional development component with capacity building at the CWD and district level, (ii) rehabilitation of 303 kilometers of provincial highways, and (iii) rehabilitation of 1,100 kilometers of rural access roads, which will follow a sector approach. Fifty five percent of the core rural roads are in poor and disadvantaged districts in Punjab. All components support the implementation of a policy framework including a five-year time bound action plan. The policy actions include the

strengthening of the core road management functions in the CWD management structure, (ii) preparing to convert the CWD into a highway authority or corporation, (iii) expanding the Roads Asset Management System, (iv) strengthening road maintenance, (v) establishing a Road Maintenance Fund, (vi) introducing measures to improve axle-load control, (vii) improving road safety, (viii) expanding private sector participation, (ix) building capacity in environment, social assessment and resettlement planning. Similar programs for the Balochistan and NWFP provinces have been included in the 2003-2005 pipeline of ADB assistance.

In Punjab through an ADB assisted TA⁹¹ a reorganization program has been approved for the CWD that emphasizes the adoption of modern road management and maintenance systems, strengthening of financial accounting systems, procurement and audit functions and institutional capacity building at the district levels. Moreover the restructuring aims to strengthen planning and budgeting and separate it from the executive functions. It also includes a component to increase private sector participation in road sector infrastructure and maintenance.

There is tremendous potential for road sector projects linked to improving sub-regional connectivity with Afghanistan and the Central Asian States. In this regard, a sub-regional component is already in the pipeline for 2003 for the \$150 million Balochistan Road Sector Development Project, which includes a pilot study on

90. Loan 1891-PAK(SF): Road Sector Development Program for \$50 million approved on 19 December 2001. Loan 1892-PAK(SF): Road Sector Development Program-Provincial Sector Development Component for \$77 million approved on 19 December 2001, Loan 1893-PAK(SF): Road Sector Development Program-Provincial Sector Reform Component for \$80 million approved on 19 December 2001.

91. TA-3166 Management Assistance to the Punjab Communications and Works Department for \$150,000 approved on 8 February, 1999.

cross-border facilities, and for NWFP Road Sector Development Project proposed for 2004. This will increase the proposed loan to \$ 250 million. A Subregional Connectivity Project has also been included in 2006 for \$100 million, as improved connectivity is essential in promoting cooperation in trade and commerce amongst countries in the region including Afghanistan and Central Asia. ADB is actively involved in the road sector in Afghanistan as the infrastructure is

extremely poor following the war and civil unrest in the country. ADB support includes TA⁹² for capacity building and TA⁹³ to develop a framework and legislation for cross-border transport, covering Pakistan, Afghanistan and countries in Central Asia. ADB is also financing the rehabilitation of the highways in Afghanistan including the main southwest highway connecting Afghanistan with Balochistan.

92. ADB 2002: TA to Afghanistan for Capacity Building for Reconstruction and Development Project, Manila.

93. ADB 2002: TA to Afghanistan for Development of Framework and Legislation for Cross-Border Transport. Manila.

List of Approved Loans in the Transport and Communications Sector
(as of 31 December 2002)

| Loan No. | Project Name | Net Amount (\$ million) | Milestone Dates | | Implementation Period (years) |
|----------|--|----------------------------|-----------------|----------------|----------------------------------|
| | | | Approval | Date Closed | |
| 1 | 0279 SF Port Qasim | 37.80 | 18-Nov-76 | 4-Feb-82 | 5.22 |
| 2 | 0280 Port Qasim | 10.80 | 18-Nov-76 | 12-Dec-83 | 7.07 |
| 3 | 0570 SF Telecommunications Project | 21.00 | 17-Jun-82 | 23-Feb-89 | 6.69 |
| 4 | 0758 Farm-to-Market Roads Project | 37.77 | 26-Nov-85 | 7-Mar-95 | 9.28 |
| 5 | 0761 SF Second Telecommunication Project | 68.85 | 28-Nov-85 | 21-Jul-93 | 7.65 |
| 6 | 0917 Second Farm-to-Market Roads Project | 113.49 | 8-Nov-88 | 16-Dec-97 | 9.11 |
| 7 | 1025 SF Third Telecommunications Proj. | 108.66 | 16-Aug-90 | 3-Sep-96 | 6.05 |
| 8 | 1185 Provincial Highways Project | 144.48 | 5-Nov-92 | 11-Nov-02 | 10.02 |
| 9 | 1323 Sukkur Bridge Project | 33.56 | 29-Sep-94 | 6-Jul-01 | 6.77 |
| | Subtotal/Average | 576.41 | | | 7.54 |
| | Ongoing Loans | | | | |
| | 1401 Rural Access Roads | 123.45 | 9-Nov-95 | | 7.15 |
| | 1891 Road Sector Development Program | 49.44 | 19-Dec-01 | | 1.03 |
| | 1892 Road Sector Dev Program-Prvnc'l Sect Dev Component | 76.98 | 19-Dec-01 | | 1.03 |
| | 1893 Road Sector Dev Program-prvnc'l Sect Reform Component | 80.30 | 19-Dec-01 | | 1.03 |
| | 1928 Punjab Road Development Sector | 155.33 | 31-Oct-02 | | 0.17 |
| | Subtotal/Average | 485.50 | | | 2.08 |
| | Total | 1,061.90 | | | |

List of Approved TAs in the Transport Sector
(as of 31 December 2002)

| TA No. | Project Name | Type | Revised Amount (\$ million) | Milestone Dates | | Implementation Period (years) | |
|--------|--------------|---|--------------------------------|--------------------|-----------|-------------------------------|-------------|
| | | | | Financial Approval | Closing | | |
| 1 | 472 | Channel Maint & Dredging Study for Port Qasim | PP | 0.085 | 26-Jul-82 | 1-Jul-84 | 1.93 |
| 2 | 582 | Farm-to-Market Roads | PP | 0.165 | 16-Jan-84 | 1-Dec-88 | 4.88 |
| 3 | 724 | Rural Telecommunications Strategy Study | AO | 0.100 | 28-Nov-85 | 1-Mar-94 | 8.26 |
| 4 | 739 | Rural Road Improvement Project | PP | 0.075 | 31-Dec-85 | 1-Dec-88 | 2.92 |
| 5 | 917 | Oil Terminal Project | PP | 0.404 | 5-Nov-87 | 1-Mar-94 | 6.32 |
| 6 | 1055 | Rehab & Improvement of Provincial Roads | PP | 0.250 | 8-Nov-88 | 1-Oct-92 | 3.90 |
| 7 | 1056 | Advisory Assist. to Domestic Road Contractors | AO | 0.830 | 8-Nov-88 | 1-Dec-93 | 5.07 |
| 8 | 1461 | SSTA for Ports Subsector Tariff Review | AO | 0.100 | 7-Jan-91 | 1-Mar-94 | 3.15 |
| 9 | 1738 | SSTA for Oil Terminal Project | AO | 0.096 | 24-Jul-92 | - | - |
| 10 | 1778 | Third Farm-to-Market Roads | PP | 0.250 | 5-Nov-92 | 1-May-96 | 3.49 |
| 11 | 1779 | Second Highways Project (JSF) | PP | 0.250 | 5-Nov-92 | 1-May-99 | 6.49 |
| 12 | 1870 | SSTA for Farm-to Markets Roads Projects | AO | 0.105 | 21-Apr-93 | 1-Sep-95 | 2.36 |
| 13 | 1938 | National Ports Master Plan & Management Study | AO | 0.900 | 24-Aug-93 | 1-Apr-98 | 4.61 |
| 14 | 2074 | Sukkur Bridge Project | PP | 0.100 | 30-Mar-94 | 1-Dec-95 | 1.67 |
| 15 | 2176 | Priv Part. In Highway Financing Cons. & Operation | AO | 0.475 | 29-Sep-94 | 1-Apr-98 | 3.51 |
| 16 | 2437 | Loan & TA Grant 2nd Rural Access Roads Project | PP | 0.250 | 9-Nov-95 | 1-May-99 | 3.48 |
| | | Subtotal/Average | | 4.435 | | | 4.14 |
| 17 | 3166 | Management Assistance to the Punjab Communications & Works Department | AO | 0.150 | 8-Feb-99 | 30-Jun-00 | |
| 18 | 3675 | Environmental Assessment | AO | 0.050 | 3-Jul-01 | 30-Jun-02 | |
| 19 | 3676 | Institutional Reform & Road Maintenance Financing Study | AO | 0.150 | 3-Jul-01 | 30-Jun-02 | |
| 20 | 3677 | Preliminary Engineering Update (Punjab) | PP | 0.150 | 3-Jul-01 | 31-Oct-02 | |
| 21 | 3678 | Poverty Reduction Study | AO | 0.100 | 3-Jul-01 | 30-Jun-02 | |
| 22 | 3679 | Social Impact Analysis & Resettlement Planning | AO | 0.100 | 3-Jul-01 | 30-Jun-02 | |
| 23 | 3680 | Preliminary Engineering Update (Sindh) | PP | 0.150 | 3-Jul-01 | 30-Sep-02 | |
| 24 | 3897 | Balochistan Road Development Sector Project | PP | 0.550 | 24-Jul-02 | 30-Dec-03 | |
| | | Subtotal | | 1.400 | | | |
| | | Total | | 5.835 | | | |

PAKISTAN: List of Approved Multisectoral Loans
(as of 31 December 2002)

| Loan No. | Project Name | Net Amount (\$ million) | Milestone Dates | | Implementation Period (years) |
|----------|---|----------------------------|-----------------|----------------|----------------------------------|
| | | | Approval | Date Closed | |
| 1 | 0957 SF Flood Damage Restoration Project | 39.397 | 30-Mar-89 | 8-Oct-93 | 4.53 |
| 2 | 1209 SF Flood Damage Restoration (Sector) Project | 77.641 | 15-Dec-92 | 8-Feb-99 | 6.15 |
| | Subtotal/Average | 117.038 | | | 5.34 |

List of Approved MultiSectoral TAs
(as of 31 December 2002)

| TA No. | Project Name | Type | Revised Amount (\$ million) | Milestone Dates | | Implementation Period (years) |
|--------|---|------|-----------------------------------|-----------------|----------------------|----------------------------------|
| | | | | Approval | Financial Closing | |
| 1 | 1160 SSTA Review of Gov Procedures for Project Impl. | AO | 0.011 | 30-May-89 | - | - |
| 2 | 2107 Loan & TA Grant - Assistance to MSU Project | AO | 0.500 | 23-Jun-94 | 1-Jun-98 | 3.94 |
| 3 | 1266 Strengthening of Env. Management (JSF-Financed) | AO | 0.600 | 21-Dec-89 | 1-Aug-94 | 4.61 |
| 4 | 2181 Strengthening Economic Analysis Capabilities of SBP | AO | 0.536 | 17-Oct-94 | 1-Aug-01 | 6.79 |
| 5 | 2190 Strengthening Aid Management Capacity of Min. of Finance | AO | 0.860 | 25-Oct-94 | 1-Apr-98 | 3.44 |
| 6 | 2276 Implementation of National Conservation Strategy | AO | 0.850 | 29-Dec-94 | 1-May-98 | 3.34 |
| 7 | 2514 Development of a Gender Data Base | AO | 0.200 | 27-Dec-95 | 1-Aug-99 | 3.60 |
| 8 | 2647 Pakistan 2010-Long Term Perspective Study | AO | 1.140 | 24-Sep-96 | 1-Mar-01 | 4.44 |
| 9 | 2781 Strength. Aid & Debt Mgt. Cap. of Min. of Finance (Phase II) | AO | 0.790 | 17-Apr-97 | 1-Sep-00 | 3.38 |

CONCLUSION

ADB's program in Pakistan has been evolving in response to the changing socio-economic scenario and the development needs of the country. The Bank has consistently reviewed its operational strategy for the country, to ensure that it meets Pakistan's development needs in critical times. In the immediate aftermath of the nuclear tests of May 1998 the leading donors imposed embargoes on further aid to the country, affecting Pakistan's development agenda and its ability to meet international financial commitments. The country had barely emerged from this crisis, with the help of the multilateral financing institutions, when it was gripped by a series of political crises, culminating in the military takeover of October 1999. Once again, the reaction of the international community was unfavorable, and economic activity was affected adversely by the prevailing climate of uncertainty.

The Government that came to power in October 1999 moved boldly and quickly to implement policies to stabilize the economy and introduced a series of structural reforms. By the end of the fiscal year 2001, it had succeeded in arresting the deceleration in the economy to some extent, and key macroeconomic indicators such as inflation, fiscal deficit and current account balance showed distinct improvements. Just as the economy started gearing up, however, it received another shock in the form of the events of September 11, due to which Pakistan was caught in the crossfire of a global conflict. ADB was quick to realize that the Government's structural reform agenda could suffer a severe setback after the events of September 11, and the Bank's response reflected its commitment to partially mitigate the negative impacts of the regional conflict on Pakistan's economy.

Following elections to the National and Provincial Assemblies held in October 2002, new governments at the federal and provincial levels were formed in late November 2002. Federal government and the highest political levels in the provincial governments have reaffirmed their continued commitment to the ongoing governance and economic reform program, and the economic and social policy emphasis on macroeconomic stability, poverty reduction, and growth.

Over the last decade, the ADB's development policy in Pakistan has undergone some changes in response to the country's development needs, shifting from an emphasis on infrastructure projects to a more defined focus on poverty reduction, human development and improved governance. This is reflected in its support to policy reform in key sectors such as agriculture and trade and finance, in addition to reform in corporate governance, and in institutions such as the police and the judiciary. In the near-term, ADB looks forward to working with the Government on policies that improve governance, enhance economic growth and reduce poverty. The road ahead remains challenging, but success requires that the Government stay the course of reforms. In this endeavor, with stakeholder consultation, the ADB stands ready to continue to support Pakistan's multifaceted development initiatives.