

## Modernizing Kerala's Government Program

Kerala, with its population of 32 million, has impressive human development indicators and a high degree of social participation, but financial problems and rising debts are threatening its ability to provide essential services to poor and marginalized communities.



Kerala is one of three Indian states to receive ADB assistance

and fostering sustainability. The Program will contribute to the government of Kerala's poverty reduction and development strategy contained in the Tenth Five Year Plan (2002-2007) and the MGP.

According to Yoshihiro Iwasaki, Director General of ADB's South Asia Department, "We welcome Kerala's commitment to reform and ADB and the state government intend this loan to be the beginning of a long-term partnership that involves work in sectors such as power and infrastructure." The Program, based on a locally defined set of reforms and drawn up after extensive consultations, will focus on

- ◆ creating an environment to achieve fiscal sustainability;
- ◆ enhancing the quality, equity and value-for-money of public services;
- ◆ improving the targeting and quality

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The Asian Development Bank (ADB) Country Strategy and Program for India supports policy and institutional reforms to achieve equitable and universal provision of basic services; strengthen measures for raising, allocating, and accounting for resources in line with pro-poor policies; and make government more accountable and transparent. As state governments have a significant responsibility in overseeing and managing the delivery of basic services, an important dimension of ADB's strategy is to focus on state-level operations. In the mid-1990s at the request of the Government, Gujarat and Madhya Pradesh became the first two focal states for ADB assistance and Kerala became the third.

Kerala received its first loan of \$200 million from ADB to support a major program of fiscal reform and social development. Kerala is also one of three focal states benefiting from the Government of the Netherlands' bilateral assistance to India. ADB and the Government of the Netherlands, which is cofinancing the Modernizing Government and Fiscal Reform Program in Kerala with a \$50 million grant, will provide technical and financial assistance to implement reforms. The Modernizing Government Program (MGP), is designed to make government more efficient, effective, and responsive to the needs of the people. It will also enhance the state's social and economic development by increasing accountability and pro-poor outcomes, improving services delivery,

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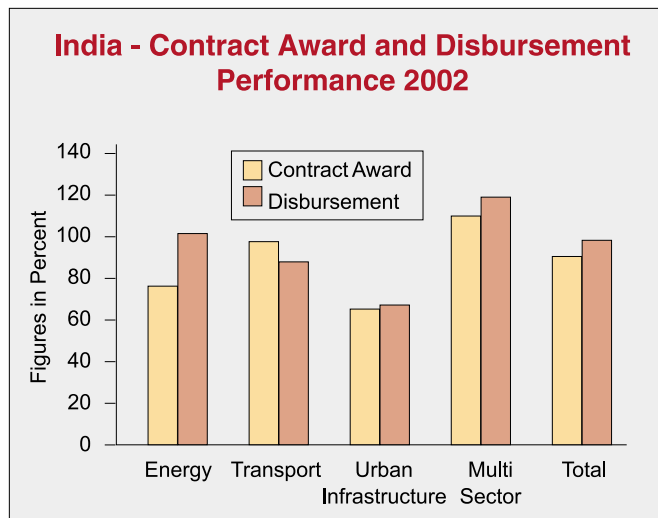
# ADB Improves Portfolio Performance in 2002

## Portfolio Highlights

Up to 2002, the Asian Development Bank had approved 66 loans for India totaling \$11.5 billion in the public sector. ADB also approved 10 loans for \$155.7 million, 19 equity investments totaling \$110.8 million, and a line of equity for \$5 million in the private sector. This is a significant increase from 1986 when ADB set up operations in India with only 2 loans totaling \$250 million. Lending has since focused on the

infrastructure, including urban infrastructure, energy, and financial sectors. In 2002 ADB approved 7 loans (6 projects) totaling \$1,183.6 million, making India the largest borrower. Twenty-six technical assistance projects for \$13.2 million, 2 grants totaling \$5.3 million and 2 equity investments for \$25 million in the private sector were also approved. Contract awards for the year amounted to \$862.4 million, accounting for 93% of the award target of \$928.9 million. This is the highest contract award in the last 10 years. Disbursements of \$576.5 million accounted for 98% of the annual target of \$589 million, representing a significant increase of 114% over the 2001 disbursement of \$270 million.

The Indian portfolio has the unique feature of state-level support programs, under which ADB enters into longer-term development commitment with a selected state. ADB's subnational



programs of this type exist only in India. India and ADB are now gearing up for an even larger partnership in the coming years. ADB's lending and technical assistance programs in India are envisaged to cover more sectors and states. Endorsement by ADB's Board of Directors is required before the enhanced lending and technical assistance programs can become operational.

**New Loans:** ADB is expanding its lending program in India to several new sectors in keeping with its goal of improving delivery of pro-poor services. The state of Kerala received its first loan of \$200 million to support a fiscal reform and social development program. ADB and the Government of the Netherlands will provide the technical and financial assistance for the state to implement its reforms.

A \$313.6 million loan was approved

in December 2002 to support institutional and policy reforms in the Indian railways sector to finance priority investments and capacity expansion. In addition, ADB is providing a technical assistance grant for \$500,000 for management consulting services to help implement the reforms. ADB will participate in the Government of India's program to upgrade its national highway system through a \$320 million loan, also approved in December

2002. This is the fourth in a series of loans extended to the National Highway Authority of India to rehabilitate and widen national highways in India. The project will be completed in June 2006 and support institutional reforms and incorporate capacity building for dealing with social issues such as HIV/AIDS and road safety.

ADB is helping to increase access to medical care through a loan approved for \$20 million equivalent to establish a network of medical facilities in the private sector in the National Capital Region of Delhi. Denominated in Indian rupees, this is also ADB's first local currency loan for a private sector project in any of its developing member countries. A \$150 million loan for India's Power Finance Corporation Ltd. and two loans for \$180 million for the Madhya Pradesh State Roads Sector Development Program were also approved in 2002. ■

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- of poverty reduction programs and social services; and
- ♦ increasing transparency, responsiveness, accountability, and efficiency of state and local governments.

The Program will also support the implementation of legislation on the right to information and public disclosure and strengthen links between state and local

governments to deliver services. It will develop and implement policies for monitoring services delivery and will boost social services in neglected areas.

The loan carries a 15-year term, including a grace period of 3 years. The Central government will disburse the assistance as 70% loan and 30% grant. According to the state's Finance

Minister, K. Sankaranarayanan, Kerala's administrative reform mechanism for modernizing the government program will be improved through ADB assistance. The Asset Renewal Fund for renovating the infrastructure in the local governments and the Social Security Fund will be given priority to maximize benefits from the loan and the Government will maintain full accountability and transparency. ■

# A Boost to India's Railway System

In the face of increasing competition from roads, the railways' share of the transport market in India has dropped over the last 2 decades. Worsening financial performance, congested routes, lack of resources for investment, and a high level of accidents further hamper the sector. The annual number of derailments accounting for the majority of accidents, rose from 282 to 344 between 1997 and 2001. The Government is keen on ensuring the safety and security of rail passengers and improving technical and administrative aspects.

The Asian Development Bank approved in December 2002 a \$313.6 million loan to provide the much-needed boost to India's vast railway system. The Railway Sector Improvement Project will implement institutional and policy reforms to improve the railway's commercial viability and finance priority investments in capacity expansion. ADB is also providing a \$500,000 technical assistance grant for management consulting services to help implement the reforms. According to Tyrrell Duncan,

ADB Senior Transport Economist, "the Indian Railways is the country's biggest employer, with about 1.54 million staff, so its size and status as a government department present special management challenges."

The Project establishes an 8-year framework linking ADB lending for railways to the implementation of successive milestones in the Indian Railways' reform program. ADB will provide support for the first stage of reforms, particularly accounting practices and management information systems; establishing the main lines of business as separate profit centers; and restructuring production units. It will also revamp and separate non-core activities so these can be operated along commercial principles.

To develop innovative solutions to the problem of loss-making branch lines, the private sector will be encouraged to help streamline staffing and service operations and improve revenue collection. The project is expected not only to improve the Indian Railways' business performance but also to enhance efficiency of the transport

system thereby helping to spread economic growth, create jobs, and increase incomes across the country. The project will be implemented principally in the Golden Quadrilateral and its Diagonals which together account for about two-thirds of the Indian Railways freight traffic. Nitish Kumar, Railway Minister, said the Golden Quadrilateral network carried 65% of the total freight and 55% of the passenger traffic, even though it accounted for only 16% of the total network. The objective of the project is to address capacity bottlenecks on main freight routes and to enable increased railway traffic. Aside from increased capacity on the Golden Quadrilateral and its Diagonals, the project will develop port connectivity and multi-modal corridors, and construct major bridges.

The investment component of the project will begin with four subprojects for building or expanding railway lines in the relatively poor states of Chhattisgarh and Orissa. Subprojects will be added as the project continues. The total project cost is estimated to be \$579.2 million, of which the Government will provide 46% or \$265.6 million. ADB will provide the balance through a loan from ordinary capital resources, with a 25-year term that includes a grace period of 5 years.

A special purpose vehicle (SPV) for executing railway projects on the Golden Quadrilateral will be formed to execute projects on commercial principles, including resource mobilization and expeditious implementation of identified projects. The creation of the company is in line with the recommendations of the chambers of commerce and various expert groups that have advocated the separation of railway infrastructure from operations. The investment will be part of the Government's medium-term railway sector investment known as the National Rail Vikas Yojana, to be implemented over a 5-year period from financial year 2003 to 2007. ■



ADB is providing support for investments in capacity augmentation to address freight bottlenecks and safety

## ADB Supports Power Sector Reforms

The financial position of many of India's state electricity boards has been deteriorating because of insufficient cost recovery, inadequate tariffs, and high operating costs. Most boards are now being restructured under different initiatives to improve financial viability and operational efficiency. The Asian

Development Bank approved a \$150 million loan to India's Power Finance Corporation Ltd. (PFC) to help reform the power sector in the states. PFC, which began lending to the power sector in 1988 and promoted reforms from 1996, is in a position to support state-level power sector reforms.

PFC will lend funds to state

electricity boards and other state-level power utilities that are committed to instituting reforms to make the sector operationally efficient and financially self-sustaining. The funds will be used to finance projects that will reduce system losses, increase operational efficiency, and improve services delivery to consumers. The PFC loans will be linked to the milestone corresponding to the particular stage of the agreed reform process. The loans will help upgrade transmission and distribution systems, build transmission and distribution facilities for system expansion, and modernize generating plants.

The State Power Sector Reform Project is part of efforts to make state power sectors financially self-sustaining. It is aimed at supporting reforms in selected, reform-oriented states and establishing independent regulatory bodies. It will unbundle sector entities to make them commercially and operationally autonomous and efficient, and financially viable.

ADB will finance 60% of the total project cost. ADB's loan will have a 20-year term, including a grace period of 5 years. The Project is to be completed in December 2007. ■



Power Grid and ADB officials inspecting progress at an ADB-assisted project site

## Highway Upgrade to Stimulate Growth

The Asian Development Bank will participate in the Government of India's program to upgrade its national highway system through a loan approved in December for \$320 million to rehabilitate and widen 504 km of the national highways at the western end of the East-West Corridor, which runs 3,300 km from Gujarat to Assam. The ADB loan is the fourth in a series of loans extended to the National Highway Authority of India (NHAI) to support the government's National Highway Development Program for upgrading the

Golden Quadrilateral that connects the four metropolitan cities of Delhi, Mumbai, Kolkata, and Chennai. A part of the upgraded section will be developed under a build-operate-transfer (BOT) scheme. The project, due for completion in June 2006, will be based on close consultations with NHAI. The program is intended to support institutional reforms through several policy initiatives such as strengthening financing capability and building capacity for dealing with social issues such as HIV/AIDS and road safety.

According to Shunso Tsukada, ADB Senior Transport Specialist, "An improved road network will increase economic opportunities of rural communities. It will provide better access to services such as health and education, greater job mobility, and enable villagers to shift from subsistence farming to more commercial agricultural production."

The total project cost is estimated at \$576 million equivalent, of which \$211 million will come from the Government and \$45 million from the private sector. ADB's loan has a 25-year term, including a grace period of 5 years. ■

# Reforming the Road Sector in Madhya Pradesh

The rapid deterioration of the road network, increased road transport capacity bottlenecks and unreliable road transport services have become major constraints to social and economic development of Madhya Pradesh, one of the focal states where ADB operates in India. Further constraints in road development are inefficient use of scarce financial resources for road maintenance, and the inadequate institutional and technical capability of Madhya Pradesh's public works department to manage the road sector. In December 2002, ADB approved a program loan of \$30 million and a project loan of \$150 million to support road sector reform and rehabilitate the road network in Madhya Pradesh.

The Madhya Pradesh State Roads Sector Development Program aims to establish more effective and efficient management of state roads and ensure more reliable road transport services to support the state's social and economic development, and thus reduce poverty. The program loan addresses policy and institutional frameworks in the state's



A bus shelter under construction on an Indian highway

public works department by implementing reform measures and providing institutional capacity building for good governance in managing the sector; improving road asset management; boosting institutional effectiveness and efficiency; and identifying pilot cases for outsourcing

and better private sector participation.

The project loan is designed to rehabilitate about 1,750 kilometres of state highways and rural connector roads. It will also provide investments to rehabilitate and improve physical transport connections to the state's most important socioeconomic centers. Benefits include improved mobility and political and economic empowerment of the poor by giving better access to the mainstream economy, business opportunities, and social services.

The program loan is to be released in two tranches of \$12 million and \$18 million, respectively. It has a term of 15 years, including a grace period of 3 years.

In addition, ADB will administer a \$1.5 million technical assistance grant, funded by the Government of the United Kingdom, to assist the state government in implementing institutional reforms. The reforms aim at supporting the road network; strengthening transport planning, project financing, investment management and environmental management; disseminating recommendations through training programs; and assisting in labor rationalization and social safety net programs. ■



The National Highway Authority of India is constructing four-lane highways and strengthening existing two-lane roads

# Initiatives in the Private Sector

## ADB Approves First Local Currency Loan to the Indian Health Care System

The private sector is becoming an important player in the health care sector in India but the absence of a proper framework for regulating and monitoring the quality of medical services creates a wide discrepancy in the standard of services among health care providers. Max Healthcare Institute Ltd., owned by Max India Ltd. proposes to set up an integrated healthcare system in the National Capital Region of Delhi. ADB proposes to support the initiative by providing a \$20 million loan denominated in Indian rupees. This is ADB's first local currency loan for a private sector project in any of its developing member countries.

According to B. Anantharaman, Group Finance Director, Max India Ltd., "ADB recognizes that the private sector

has an important role in meeting the growing demand for health care services in India. This loan is an acknowledgement of our unique health care model which is committed to the highest standards of excellence in patient care, scientific knowledge and medical education."

The Medical Service Network Project is aimed at alleviating a critical shortage of health care services in NCR Delhi by expanding access to medical services and helping to raise healthcare quality to international standards. The project will build and operate 23 medical facilities in all 3 levels of service—primary, secondary and tertiary—and will include up to 16 neighborhood primary clinics, 5 secondary medical centers, each serving a population of about 2.5 million; and 2 tertiary hospitals.

ADB plans to issue a local currency-denominated bond in the Indian capital market to fund this project and other private sector projects. The Government recently approved this proposed local bond issue. According to Robert Bestani, Director General of ADB's Private Sector Operations Department, this is a landmark project because it is "ADB's first local currency loan in India and also the first private sector infrastructure project in the country for 6 years." ADB supports the use of local currency debt for projects that have revenues largely in local currency to avoid currency mismatches. "The ADB bond issue will establish a benchmark in Indian capital market for long-term debt papers," adds ADB Treasurer Thierry de Longuemar.

## ADB supports Mortgage Lending by Indian Financial Institutions

India's housing demand shortfall was about 20 million units in 2001. Lack of access to finance is a major factor for this shortfall. Mortgage lending activity in India is very low—the total number of mortgages in India amounts to less than 2 % of the total GDP, compared with about 51 % in the United States and 20-30 % in Southeast Asian economies.

Although ADB's involvement in India's housing sector is relatively recent, it is now the major international lender in this sector and plays a lead role in supporting the Government's policy and institutional reform agenda. ADB's first public sector loan for housing was a \$20 million line of credit to the Housing Development Finance Corporation (HDFC) under the Karnataka Urban Infrastructure Development Project. In September 1997, ADB's Board approved 3 loans of \$100 million each to the National Housing Bank (NHB); the Housing and

Urban Development Corporation; and HDFC. The loans were used as lines of credit for financing housing and housing-related poverty reduction projects and were given to community-based finance institutions (CFIs), housing finance institutions (HFIs), private companies, or directly to households. Another line of credit for the housing sector was approved by ADB in 2000 which currently is being administered through 2 institutions, the National Housing Bank (\$40 million) and ICICI (\$80 million) and is exclusively meant for low income households.



Following the success of the Housing Finance Project, ADB approved on 26 November 2002, ADB participation to the extent of \$10 million in the form of equity in the India Mortgage Guarantee Company (IMGC). The objective of the company will be to provide mortgage guarantees that protect the primary mortgage lenders, such as banks and housing finance companies, in case of borrower default. Currently the selective lending practices of HFIs are often marked by conservative standards requiring high down payments, high interest rates and short tenures, all resulting in higher instalments and lower affordability. The project is therefore expected to have a direct impact on the current housing shortage in India.

The proposed investment in IMGC is consistent with ADB's Private Sector Development Strategy that is aimed at strengthening developing member countries' capital markets including the housing finance sector. ■

# Fostering Renewable Energy Development

A \$100 million loan project from the Asian Development Bank to the Indian Renewable Energy Development Agency Ltd. (IREDA), approved in 1996 for investment in renewable energy technologies in India, was completed in 2002. This is in support of India's Natural Energy Plan, which focuses on renewable energy development. The loan was used for 14 bagasse cogeneration subprojects, \$55 million; wind power generation subprojects, \$40 million; and installation of solar thermal water heaters, \$4 million.

While the project targeted an additional 125MW of power generation, the subprojects are expected to generate about 318 MW. Of the estimated potential of 3,500 MW of bagasse-based capacity in the country, IREDA has installed 447 MW capacity, of which 267 MW capacity has been provided under the project. In wind generation, IREDA assisted installation of 621 MW, of which the project installed a capacity of 51.42 MW.



A solar thermal installation assisted under an ADB project

ADB's assistance has enabled IREDA to leverage additional long-term sources of funding from other international funding agencies as well as to meet India's priorities in this sector. At India's request, ADB could

consider further support to this sector to assist India in mitigating power shortages, particularly in remote locations through build up of decentralized power generation capacities. ■

## South Asia Business Facilitation Cell Set Up in Bhutan

Staff of the India Resident Mission (INRM) represented the Asian Development Bank (ADB) and delivered the keynote address at the South Asia Business Forum (SABF) business facilitation cell's inaugural meeting in Thimpu, Bhutan on 8 November 2002. The meeting marked the inauguration of the SABF web site and was a step forward in accomplishing the Action Plan adopted by the Trade, Investment, and Private Sector Cooperation Working Group under the South Asia Subregional Economic Cooperation (SASEC) initiative of ADB.

Lyonpo Khandu Wangchuk, Bhutan's Minister for Trade and Industry, inaugurated the business facilitation cell and web site. ADB was represented by Sujatha Viswanathan, Social Economist, INRM with Sushil Khanna, ADB consultant who also participated and made a presentation. The meeting was attended by the secretaries of Finance, Agriculture, Home, Trade and Industry, and Commerce as well as representatives from the private sector.

In his inaugural address, the Trade Minister, Wangchuk,

complimented the Bhutan Chamber of Commerce and Industry for establishing the business facilitation cell, which would help promote private sector cooperation in the region. He also cited ADB's role in funding and coordinating the SASEC program. The Trade Minister expressed the Government of Bhutan's commitment to maintain the pace of reforms and transition to the global trading system and to accord the highest priority to private sector development. Ms. Viswanathan stressed the importance of cooperation in reducing poverty in the subregion in her keynote address. She emphasized the crucial role of the private sector and complimented the BCCI on this initiative.

Bap Kinga, BCCI Vice President in his concluding remarks thanked the Government, ADB and the private sector for their role in promoting subregional private sector cooperation. He expressed confidence that the business facilitation services through the cell will not only enhance the Chamber's service capacity but also promote business development in the subregion and reduce poverty through economic prosperity.

## INRM discusses Kelkar Report on Tax Reform

The India Resident Mission of the Asian Development Bank organized a High Level Panel Discussion on 12 December on the Consultation Papers of two Task Forces on Direct and Indirect Taxes under the chairmanship of Vijay Kelkar. A Ministry of Finance team led by Vijay Kelkar participated in the discussion. The Task Forces on Direct and Indirect Taxes have recommended wide-ranging reforms in tax policy as well as tax administration. The recommendations include taxation of services and reported agricultural incomes, and elimination of a whole range of tax exemptions to broaden the tax base, while at the same time raising the minimum taxable income limit to offset bracket creep. The recommendations also suggest simplification of the rate structure of taxes. Key proposals on tax administration include computerization and use of information technology enabled services, along with capacity building for improved tax administration and a taxpayer service.



Former ADB President Kimamasa Taramizu (second row, third from right) with ADB staff at a reception hosted by INRM Country Director, Louis de Jonghe (second row, fifth from right)

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### NEWS FROM India

The quarterly newsletter of the Asian Development Bank (ADB) India Resident Mission (INRM) aims to enhance communications between ADB and its client groups. *News from India* disseminates information on ADB activities and provides a forum on development issues in India. Articles in the newsletter, however, do not necessarily reflect the official ADB view. We welcome readers' comments and suggestions.

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