



Validation Report

Reference Number: PCV: PAK 2008-25
Project Number: 32146
Loan Numbers: 1807, 1808(SF), and 1809(SF)
May 2009

Pakistan: Energy Sector Restructuring Program

Independent Evaluation Department
Asian Development Bank

ABBREVIATIONS

ADB	–	Asian Development Bank
CPPA	–	central power purchasing agency
EA	–	executing agency
EIRR	–	economic internal rate of return
ESRP	–	Energy Sector Restructuring Program
FESCO	–	Faisalabad Electric Supply Company
HUBCO	–	Hub River Power Plant Company
IED	–	Independent Evaluation Department
IMF	–	International Monetary Fund
IPP	–	independent power producer
JPC	–	Jamshoro Power Company Limited
KAPCO	–	Kot Addu Power Company Limited
KESC	–	Karachi Electric Supply Corporation
MOF	–	Ministry of Finance
NEPRA	–	National Electric Power Regulatory Authority
OGRA	–	Oil and Gas Regulatory Authority
PCR	–	project completion report
RRP	–	report and recommendation of the President
SDR	–	special drawing rights
TA	–	technical assistance
WAPDA	–	Water and Power Development Authority

NOTES

- (i) The fiscal year (FY) of the Government and its agencies ends on 30 June. “FY” before a calendar year denotes the year in which the fiscal year ends.
- (ii) In this report, “\$” refers to US dollars.

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PROGRAM COMPLETION REPORT VALIDATION

A. Basic Project Data		PCR Validation Date::	May 2009	
Project and Loan Numbers:	32146 1807/1808(SF)/1809(SF)		Appraisal	Actual
Program Name:	Energy Sector Restructuring Program (ESRP)	Total Program Costs	356.0	203.4
		Loan (\$ million)	355.0	203.4
		Loan 1807	300.0	153.0
		Loan 1808(SF)	50.0	50.4
		Loan 1809(SF)	5.0	0.0
Country:	Pakistan	Total Cofinancing:	1.0	0.0
Sector(s):	Energy	Borrower:	1.0	0.0
ADB Financing (\$ million)::	ADF: 55.0	Effectiveness Date	15 Dec 2000	
	OCR: 300.0	Closing Dates:		
Approval Date:	14 Dec 2000	Loan 1807	30 Jun 2004	19 Jun 2004
Signing Dates:		Loan 1808(SF)	30 Jun 2004	20 Dec 2000
	Loan 1807	15 Dec 2000	Loan 1809(SF)	30 Jun 2004
	Loan 1808(SF)	19 Dec 2000		
Loan 1809(SF)	24 Jan 2001			
Project Officer:	R. Stroem	<u>Designation:</u> Principal Energy Specialist	<u>From</u> 2000	<u>To</u> PCR
Evaluator:	C. Brown	Director	H. Hettige	
Quality Control Reviewer:	H. Hettige/ B. Palacios			

B. Program Description (summarized from the report and recommendation of the President [RRP])

(i) Rationale.

Pakistan's energy sector faced a financial crisis that basically stemmed from weak governance, political interference in decision-making, poor staff morale, and disregard of prudent business practices. The worsening problems in these areas have had a major impact on the financial performance of the utilities and have hindered the effectiveness and sustainability of the energy sector. Weak governance has resulted in inefficient utility operations, power theft, reduced billing and collection, and nonpayment of arrears. These practices have affected the poor segment of the population more than the affluent and contributed to the financial crisis in the sector. The absence of an immediate policy response for the energy sector would have serious economic repercussions. Radical reforms and tough adjustment measures, including market-driven systems, were needed to restore viability in the sector and to make it self-sustaining. Asian Development Bank (ADB) support of the Government's initiatives for structural reforms in the energy sector was essential given the urgent need to introduce competition as the driving force for improvement and private sector participation as a vehicle for creating a competitive environment.

(ii) Impact.

Ensuring a stable supply of energy is essential for the country's economic recovery, which will also result in additional job-generating activities for the poor. The Program provides a sound basis for the Government to carry out reforms and to restructure the energy sector. The development of a competitive electricity market under the reform program will result in efficiency gains that will have a positive impact on poverty reduction.

(iii) Objectives Expected Outcomes.

The objectives of the RRP were not separately listed or stated specifically as objectives but rather embodied in general discourse in the text (RRP paras 54—56). The following¹ are paraphrased from the RRP.

1. **Loans 1807 and 1808.** The ultimate goal (objective) of the Program was sector economic efficiency and consumer satisfaction. This was to be achieved through the following specific objectives:
 - a. To reform the energy sector in Pakistan, (provide a competitive power sector able to provide required quantities of quality power at least cost to the consumer),
 - b. To achieve sustainable growth in the energy sector,
 - c. To increase efficiency in the use of resources, and
 - d. To improve customer focus in the delivery of services.
 - e. Not specifically stated in the Objectives and Scope Section of the RRP but from all of the documentation on the project, other expected outcomes would be:
 - f. Improvement in the national economy, and
 - g. The overarching outcome of poverty reduction.
2. **Loan 1809.** The attached technical assistance (TA) loan was provided (i) to enhance capacity in the energy sector to support the implementation of ESRP and to monitor and evaluate its impacts on residential and commercial consumers during the implementation period; and (ii) to minimize the negative effects on KESC employees resulting from the organization's restructuring arrangements including cash payments above the statutory minimum for laid-off workers, if involuntary layoffs were required.

(iv) Components (Key Conditions):

1. **Loans 1807 and 1808.** At the time of Appraisal the ESRP identified the following areas of reform, (components), as necessary to achieve the objectives of the Project:
 - a. enhancing governance in the sector,
 - b. enhancing the legal and regulatory framework and strengthening of the capacity of the sector regulator,
 - c. financial restructuring and privatization of Karachi Electric Supply Corporation (KESC),
 - d. restructuring of Water and Power Development Authority (WAPDA) and privatization of corporatized entities,
 - e. enabling a competitive electricity market,
 - f. resolving the independent power producer (IPP) issues and the Hub River Power Plant Company (HUBCO) and the Kot Addu Power Plant Company (KAPCO) cases, and
 - g. enhancing reform in the natural gas and petroleum sub sector.
2. **Loan 1809.** Two major components of the TA loan were defined as (i) poverty impact assessment and (ii) labor retrenchment and redeployment. Within these major components a number of sub components were designed, as follows:
 - a. Poverty impact assessment:
 - i. assess and monitor the distributional impact of the restructuring program with special emphasis on evaluating the direct and indirect effects on the poor and the most vulnerable groups of consumers,
 - ii. identify channels for consumer advocacy, and
 - iii. strengthen consumer participation and capacity of consumer group organizations, in particular for the most vulnerable groups.

¹ From a review of the report and recommendation of the President (RRP) and program completion report (PCR), this Validation finds that the objectives and outcomes have not been clearly and crisply defined. This Validation considers the objectives and expected outcomes, as derived from the RRP, are as indicated above. This is not a serious issue except to clarify the usage of the terms in this report. See also Section 9, Comments on PCR Quality and the Recommendations in Section 5c.

- b. Labor retrenchment and redeployment
 - i. problem identification and analysis,
 - ii. program formulation, and
 - iii. implementation and monitoring.

The TA would also design and conduct a public awareness campaign to build consensus for the ESRP.

C. Evaluation of Design and Implementation (PCR assessment and Validation)

(i) Relevance of design and formulation:

In 2000, when the ESRP loans of ADB were approved, Pakistan was in a state of economic crisis. Foreign exchange was in acute shortage, leading to concerns about Pakistan's ability to meet its external commitments. The power sector was a major source of the deficit. The most severe impact of the crisis was on the poor. With these conditions the urgency in the design of the loans was assisting the power sector at a time of crisis, maintaining the economic viability of the country and ultimately alleviating poverty through the above objectives. ADB's participation in the ESRP was developed in close consultation with the Government, and other ESRP development partners, including the International Monetary Fund (IMF) and the World Bank. The Government's ESRP and ADB's ESRP loans were an integral element of the IMF's structural adjustment program, which recognized that, to address the overall macroeconomic crisis, the crisis in the power sector had to be dealt with. Loans from the IMF and ADB were closely linked. The loans were fully consistent with ADB's country strategy, which at the time of appraisal envisaged the use of program loans to promote sector restructuring, privatization, and commercialization. The PCR rated the design and formulation of the ESRP as "relevant". Because the objectives were directed at improving the welfare of the poor and the country's economy this Validation confirms that the design and formulation as "relevant."

(ii) Key conditions:

At appraisal, two program loans and one TA loan were proposed for the Program with a total value of \$355 million. The Government of Pakistan was the Borrower and the Ministry of Finance (MOF) was the executing agency (EA).

1. **Loans 1807 and 1808.** The Program loans defined seven components (key conditions) as outlined in Section B(iv). Costs for the individual components were not estimated in the loans but rather the loans were provided as discretionary funds of the Government and not tied to any specific components although the usage of the funds was defined in the loans and the release of each tranche was based on meeting specific covenants.

Loan 1807 for \$300 million from ordinary capital resources was provided to help defray the cost (both restructuring and social costs) associated with the restructuring process. Of this \$300 million, \$50 million was provided as an incentive loan to the Government for meeting covenants early in the Program.

Loan 1808 for \$50 million from Special Funds was a companion loan to 1807 provided to cover labor retrenchment costs for KESC and WAPDA, and a skills development program.

The proceeds of the first tranche of Loan 1807 went to the restructuring of KESC, according to the conditions of the loan. The Government also allocated Loan 1808 for the restructuring. It was also understood that \$50 million of the Program loans would go to the Ministry of Petroleum. However, because the second and third tranches of the loan were cancelled, as explained below, this did not happen. By late 2003, as macroeconomic conditions in the country improved and other sources of funds became available, mainly from United States support, the Government came to view ADB loans as a high-cost source of finance and decided to repay some of them. Loan 1807 was one of these loans, and it was repaid in full in January 2004, 5 months before the original scheduled closure date. The second and third tranches of the loan were closed (cancelled) at the same time, at the request of the Government.

2. **Loan 1809.** TA Loan 1809 for \$5 million from Special Funds was designed to develop technical assistance projects to cushion the social impact of KESC and WAPDA restructuring and privatization, and it was to be disbursed according to the time frames of those projects. However, in June 2004, the MOF stated that it *had “decided not to retain the TA loan as this will not add value to the privatization of KESC”*. The loan was then cancelled by the Government on 30 June 2004 and the Government did not proceed with the technical studies that were supposed to be financed under the loan.

(iii) Program Cost, Disbursements, Borrower contribution, and Conformance to Schedule (as relevant to program performance)

A summary of the ESRP loans at appraisal and a loan closing is provided in Table 1.

**Table 1: Energy Sector Restructuring Program
(\$ million)**

Loan No.	Type	Tranche			Total Loan Amounts		
		1 st	2 nd	3 rd	Appraisal	Cancelled	Closing
1807	Program	100	75	75	250	147 ^a	103
	Program (incentive tranche)	50			50		50
Total Loan 1807		150	75	75	300	147	153
1808	Program				50		50.4
1809	Technical Assistance				5	5	0 ^b
Total All Loans					355	152	203

^a The balance of \$147 million was cancelled on 19 January 2004.

^b The loan was cancelled on 20 June 2004.

Sources: ADB. 2007. *Program Completion Report on the Energy Sector Restructuring Program in Palistan*. Manila.

1. **Program Costs.** The program costs are shown in the above table. Loans 1807 and 1808 were designed to cover part of the costs of the Government's ESRP. The costs of the ESRP could not be estimated precisely but was broadly estimated at \$1.7 billion, with the financial costs of restructuring the power, natural gas, and petroleum subsectors composing the largest part. Other development partners also supported the large cost of the ESRP.
2. **Borrower Contribution.** There was no Borrower contribution attached to the ADB program loans. The Government did incur a significant part of the structural adjustment costs prior to loan releases which were subject to retroactive financing. Also, the Government did cover about \$1 million of local costs associated with the TA Loan. As outlined in Section C(ii), only \$153 million out of \$355 million was drawn on the program loans, with \$147 million paid off early, as discussed under Schedule and Disbursements below.
3. **Schedule and Disbursements.** All three loans were scheduled to be closed in June 2004. Each disbursement of the ADB was timed to coincide with milestones in the reform and restructuring process, as identified in the loan conditionalities. The conditions for the release of the \$150 million first tranche of Loan 1807 and all of the \$50 million of Loan 1808 were met by the Government during loan negotiations and these funds were therefore disbursed right after the loans were approved in December 2000. Loan 1808 was closed in the same month. The disbursement of the \$50 million incentive tranche of loan 1807 was delayed by several months because the Government needed additional time to meet the early covenant conditions but these conditions were eventually met and the incentive tranche was disbursed in April 2001. Tranche 2 of loan 1807 was also delayed because of difficulties in meeting loan conditions for the privatization of KESC. Progress was slow but positive. However, as reported in Section C(ii), above:

- a. Tranches 2 and 3 of Loan 1807 were paid off early, and the loan cancelled in January 2004, 5 months earlier than scheduled. Certainly not all of the work was completed nor all covenants met.
- b. Loan 1809 was cancelled in June 2004, before it was drawn on, and the Government did not proceed with the technical studies that were supposed to be financed under the loan.

(iv) Implementation Arrangements, Conditions, and Covenants, and related Technical Assistance

Implementation Arrangements, Conditions and Covenants.

The MOF was responsible for implementing the Program, but many other ministries and organizations, in particular the Ministry of Water and Power, the Ministry of Petroleum, National Energy Price Regulatory Authority (NEPRA), KESC, and WAPDA, were also involved. This was a huge undertaking, as a wide range of conditions and covenants, 67 in all, were attached to the loans. These covenants were very specific and highly relevant to the implementation of the ESRP. The MOF ably coordinated their efforts through a committee structure. The arrangements worked well and were effective for delivery of the program outputs. No major changes were made in these arrangements during implementation of the Program. ADB and the MOF corresponded regularly and ADB oversight was provided through regular review missions. It is noted that at the time of appraisal the ESRP was considered an ambitious, difficult and risky program. Delays with such a complex program were expected and did occur. The privatization conditions proved to be the most perplexing. However, both sides clearly worked diligently to ensure compliance as early as possible and the delays were manageable. The Program was thus efficiently managed by the MOF and by ADB.

Technical Assistance.

As noted above the Government was able to design the ESRP without any direct external project preparation support, demonstrating the capacity and the commitment of the Government to the ESRP. During the implementation of the ESRP, two technical assistance projects— *Gas Sector Restructuring*² and *Privatization of KESC*³ provided support to the Government in meeting some of the covenants under Loans 1807 and 1808.

(v) Performance of the Borrower and Executing Agency:

From the ESRP much has been accomplished since December 2000, with ADB loans and guidance and further support from the IMF and other development partners. As reported by the PCR, in May 2007, the loan covenants have been complied with, except for the privatization of Jamshoro Power Company Limited (JPC) and Faisalabad Electric Supply Company (FESCO). According to the Privatization Commission, the two companies could be privatized in 2007.⁴ The role of the MOF as the EA for the loans was also a source of strength for the Program. The MOF was well placed to see the link between Pakistan's macroeconomic crisis and the need for reforms in the energy sector. A well-thought-out structure for monitoring and implementing the ESRP was established.

The Program achieved most of the planned outcomes. All seven outputs of the ESRP were at least partly achieved; KESC was restructured and privatized; the restructuring of WAPDA has also proceeded, albeit slowly; disputes with IPPs were all resolved; cross-indebtedness between power sector entities and the central and state governments has been largely eliminated, such that both government and the utilities are now more accountable for their financial performance; system losses in transmission and distribution have also been reduced, although there is considerable scope for further progress; substantial investment in the transmission and distribution system is being ensured in all the power sector companies. Increased monitoring is being done to avoid

² ADB. 2001. *Technical Assistance to Pakistan for Restructuring the Gas Sector*. Manila. (TA 3711-PAK, for \$1,000,000, approved on 29 August).

³ ADB. 2000. *Technical Assistance to Pakistan for Privatization of Karachi Electric Supply Corporation*. Manila. (TA 3502-PAK, for \$1,000,000, approved on 22 September).

⁴ As of June 2009, expressions of interest are still being solicited for the long-term lease of Jamshoro Power Company Limited. Faisalabad Electric Supply Company is still to be privatized.

power theft; the regulator has gained considerably in capacity, and the enabling environment for a competitive power market has progressed since appraisal; the reform of the natural gas and petroleum sector has proceeded slowly but steadily; the Oil and Gas Regulatory Authority (OGRA) was formed in 2002 and has taken on an increasingly greater role in regulating the oil and gas sector. The unbundling of the sector and the establishment of effective regulation are major steps forward.

Not all was smooth: and many obstacles remain. The PCR reported that: privatization of KESC took considerably longer to achieve than envisaged at the time of the loan but was ultimately successful; capacity shortfalls continue in generation, transmission, and distribution; there were delays in the creation of a central power purchasing agency (CPPA); the Government has failed to announce tariffs for power retailers; there was lack of clarity in subsidy policies for the sector; the corporatized entities. Tranches 2 and 3 of Loan 1807 were paid off early, and the loan cancelled before the planned closing date. Not all of the work was completed nor all covenants met. The Government made a commitment to continue with the ESRP and the PCR has reported that the Government has fulfilled this commitment. The privatization of JPC and FESCO is the only area where covenants have clearly not been complied with. ADB has continued to remind the Government of its commitment but has only a limited ability to influence events, as the loans are closed and the key WAPDA development partner is the World Bank. Similarly, the social program of work planned under Loan 1809 was not carried out because the loan was cancelled by the Government.

The PCR rated the performance of the Borrower and EA as “successful”. This Validation notes that the outputs that were achieved were “successful”. Considering the overall accomplishments and detractions this Validation also rates the performance as “successful”.

(vi) Performance of the Asian Development Bank:

Regular policy dialogue with the Government and monitoring by ADB ensured effective implementation of the Program. During loan negotiations and program implementation ADB also maintained in close coordination with the IMF and other partners in the ESRP. In addition to the ESRP, ADB has supported the power sector of Pakistan with other projects, which in essence supports the ESRP. The PCR reports that ADB has provided technical assistance to restructure the gas sector (footnote 2) and build the institutional capacity of the National Transmission and Despatch Company Limited⁵ and the Alternative Energy Development Board.⁶ A major new loan for the transmission sector was approved in December 2006.⁷ A technical assistance project for the CPPA⁸ is ongoing. ADB's private sector operations have an investment in KESC. A new loan for the distribution sector is being considered. Such wide-ranging assistance to the power sector is well justified. The MOF and other agencies involved in the ESRP have expressed their appreciation of the intensive policy dialogue and support they received from ADB during loan negotiations and implementation, particularly in the privatization of KESC. Much of the success reported in Section C(v), Performance of the Borrower and the EA, is attributable to the support provided by ADB. In administration of the loan, ADB disbursed funds promptly when covenants were met but held firm on releasing loans until the conditions were met, such as for privatization. ADB made regular representation to the Government when progress was slow on such key Conditions. Early cancellation of Loans 1807 and 1809 were unilateral actions by the Government and beyond ADB's control. There were no problems with ADB's performance. The performance of ADB is therefore deemed “satisfactory”.

⁵ ADB. 2003. *Technical Assistance to Pakistan for Institutional Capacity Building of the National Distribution and Dispatch Company. Manila.* (TA 4130-PAK, for \$600,000, approved on 20 June).

⁶ ADB. 2004. *Technical Assistance to Pakistan for Capacity Building of the Alternative Energy Development Board.* (TA 4500-PAK, for \$150,000, approved on 17 December).

⁷ ADB. 2006. *Power Transmission Enhancement Investment Program. Manila.* (Loans 2289-PAK and 2290-PAK(SF), for \$226 million and \$10 million, approved on 13 December, respectively).

⁸ ADB. 2006. *Establishment and Commencement of Operations for the Central Power Purchasing Authority. Manila.* (TA 4870-PAK, for \$950,000, approved on 17 November).

D. Evaluation of Performance (PCR assessment and validation)

(i) Relevance.

To understand the relevance of the ESRP it is necessary to understand the conditions in the energy sector and the country during the design of the loans. As outlined in Section C(i), Loans 1807, 1808, and 1809 were designed at a time of serious macroeconomic crisis for Pakistan, as well as significant, related problems in its energy sector. Both were longstanding problems. ADB began discussing the ESRP with the Government in April 1998. Negotiations were already ongoing between the Government and the IMF, which took the lead on macroeconomic issues. However, in May 1998, Pakistan conducted nuclear tests, and these led to sanctions from many multilateral financial institutions, including ADB. The economic situation quickly became more precarious; the country accumulated substantial arrears in external payments. There were continuing difficult discussions between the Government and the IMF and the ADB throughout 1999 and 2000. Finally the Government committed to necessary reforms and the IMF approved a standby credit for Pakistan of \$596 million in November 2000 and ADB approved the loans as discussed in Section C(ii). The ESRP loans were therefore “relevant” to both the macroeconomic situation and the position in the power sector in late 2000. The loans helped to relieve Pakistan’s balance-of-payments crisis, while the implementation of the associated loan conditions helped to improve conditions in the power sector. The improved conditions, sector governance, etc., as described in Section C(v), indicate that the objectives of the ESRP were relevant at the time of appraisal and continue to be relevant to the energy sector of Pakistan. As it turned out the balance of payments position for Pakistan had improved significantly by late 2003 mainly with support from the United States. However the support of the economy at its time of greatest need was provided by the IMF, ADB and its development partners, and was not only relevant but necessary to maintain stability in the country. The PCR rated the performance as “relevant” and this Validation confirms the rating.

(ii) Effectiveness in Achieving Outcome.

As reported in Section B(ii) above, this Validation considers objectives/outcomes of the Program as:

1. sector economic efficiency and consumer satisfaction,
2. to reform the energy sector in Pakistan, (provide a competitive power sector that can deliver required quantities of quality power at least cost to the consumer),
3. to achieve sustainable growth in the energy sector,
4. to increase efficiency in the use of resources,
5. to improve customer focus in the delivery of services,
6. improvement in the national economy, and
7. the overarching outcome of poverty reduction.

There is no direct quantitative monitoring or evaluation of these outcomes reported in the PCR. However, from apparent signs in the country, there have been reforms achieved in the energy sector (Outcome [b] above) and improvements in the national economy, (Outcome [f]). There was monitoring of the outputs during implementation and during the completion review mission. As the PCR reported, all seven outputs for the ESRP were at least partly achieved. Sector governance and the capacity of the power sector regulator improved. KESC was restructured and privatized. WAPDA was unbundled, although the commitment to achieve partial privatization has so far not been achieved. Disputes with IPPs were all resolved. A more enabling environment for a competitive electricity sector was created through NEPRA, although further actions are needed to achieve this output in full. Reform of the gas and petroleum sector was enhanced.

As the TA Loan was cancelled by the Government, some of the potential positive outcomes of this loan have been negated and, without monitoring, the social impact of restructuring of KESC and WAPDA the outcome of Labor retrenchment and redeployment are not known. Although cancellation of the TA Loan has diminished the benefits of the Program there are nonetheless numerous accomplishments of the Program that will provide or contribute to the expected outcomes and accordingly this Validation rates the achievement of outcome as “effective”.

(iii) Efficiency in Achieving Outcome and Outputs.

The Government took many of the first steps of the ESRP before the loans were effective and thereby contributed to the efficient implementation of the Program. There were delays resulting from the hesitancy of the Borrower and EA to make difficult decisions, particularly on privatization, which caused some inefficiency during the Program. Such delays were not unexpected and were addressed earnestly by the EA and with sensitivity by ADB to minimize the inefficiencies. Notwithstanding the delays, most of the covenants with respect to the Loans 1807 and 1808 were met before they were closed. This was also before the original intended closure. As indicated above the outputs and immediate outcomes, at the same time, were effective. There is no quantitative report on the scope of work versus the \$153 million disbursed by the program loans but all indications are that these funds were used effectively and efficiently used. The PCR reported that the Program was efficiently managed by the MOF and by ADB. Considering, what has been recognized as a difficult and risky program and considering the successes, as reported above, the economic and social benefits are judged to have been achieved at near least cost. Thus this Validation agrees with the PCR that the Program was “efficient” in achieving outcome and outputs.

(iv) Preliminary Assessment of Sustainability.

The PCR reports that, within the power sector most of the structural reforms of the ESRP, such as enhancing governance in the sector, enhancing the legal and regulatory framework, strengthening of the capacity of the sector regulator, enabling a competitive electricity market, are in place or progressing towards achieving these outputs. Pakistan's macroeconomic outlook has improved considerably since 2000 with demonstrated economic growth and a significantly improved balance of payments. However, it is considered that to maintain sustainability, further support is needed to ensure a continuing development of the young competitive and commercial energy sector. The Government must remain committed to reform and ADB should stay engaged with the sector, to sustain the policy dialogue over reform and to provide financial support to help keep the reform program on track. Noting that these assertions are likely, this Validation agrees with the PCR that the sustainability of the program outcomes is “likely”.

(v) Impact (both intended and unintended).

The ultimate expected outcomes (and therefore areas of greatest expected impact) of the ESRP were economic efficiency and consumer satisfaction in the energy sector. Improvement in the national economy and the overarching outcome of poverty reduction were also key expected outcomes. The PCR reports that the loans have had a positive impact in these areas. The Government has committed to a lifeline tariff for low levels of consumption, which was a condition of the loans. The improvements in power sector performance, from unbundling and privatization, should make power more widely available across Pakistan, particular for the poor. Wider availability will increase income opportunities for the poor and non-poor. Costs should reduce through the pressure of competition. The loans have helped to improve the economic and financial performance of the power sector, which feeds directly into the economy. Thus the economic impact of the loans was also positive in helping to ensure greater macroeconomic stability and improved balance of payments since 2000. There were no direct environmental safeguard issues to be concerned with for the ESRP loans. Delays in implementation of the Program also delayed the benefits of the Program but these are minor concerns compared to the large benefits provided by the loans. Cancellation of TA Loan 1809 was a setback and detailed information on the impact of the restructuring of KESC and WAPDA is not available. This is addressed further under Recommendations below. The PCR considered the impact of the ESRP as “positive”. Overall, considering the impact resulting from the key outputs of the ESRP, this Validation rates the impact to be “substantial”.

E. Overall Assessment, Lessons, and Recommendations (Evaluator assessment)

This Validation finds the Overall Assessment, Lessons, and Recommendations of the PCR complete and cogent; and generally agrees with the same. To make this report complete the following is in essence a summary of the PCR findings with some minor editing and elaboration of points made.

(i) Overall Assessment:

The ESRP was implemented broadly as designed and has attained most of its planned objectives. Effective monitoring of the Program during implementation was provided by ADB through open dialogue with the Government and regular review missions. Some aspects of the Program were delayed, and the achievement in some areas, for example, privatization, was incomplete (at the time of cancellation of the loans). The cancellation of loans was a setback. However the Government has made a commitment to continue with the ESRP and has expressed the view that initial impediments to privatization have been removed, and further progress on implementation of Program is expected as planned. Since loan closing, the PCR reported that the Government has followed up on this commitment. The growing skills of the power sector regulator, the privatization of KESC, the improvement in the environment for IPP investment in the power sector, and the unbundling of WAPDA are real successes. Outcomes and impacts were mostly positive. As reported by the PCR and as indicated from the above Sections, overall, from the point of view of relevance, efficacy, efficiency, and sustainability, the Program is considered "successful". This Validation agrees with the PCR and also rates the Overall Assessment as "successful".

(ii) Lessons:

This Validation agrees with the Lessons to be learned that are identified by the PCR and paraphrased as follows:

1. The early processing of the loan and the success with respect to meeting the loan covenants demonstrate the importance of investing time in loan processing and setting tough conditions for loan approval.
2. The Program could have included a mechanism of formal review after about 18 months in order to consider revising the content and timing of loan covenants. The objective would be to make the covenants more relevant to prevailing conditions, strengthen or bring forward some conditions, and waive or defer others.
3. A well-thought-out structure for implementing the ESRP monitoring was established. The loans for the ESRP were closely coordinated with those of the IMF and other development partners, particularly the World Bank. This close coordination was a key strength in successful implementation of the ESRP.
4. If ADB attaches great importance to similar analysis, it should consider ensuring that commitment to undertake the analysis is irrevocable, for example, by making the work a loan condition and carrying out preliminary work before loan approval.
5. Where possible, ADB should link its loan conditions to aspects of the Program where it has strongly positioned itself in the policy dialogue and should take a leadership role in the financing partnership.
6. Difficult lending conditions like the requirement to privatize KESC are achievable, but ADB (and the EA) must be prepared to persevere over a long period and extensive support must be provided through technical assistance and policy guidance.

(iii) Recommendations:

This Validation agrees with the recommendations in the PCR as paraphrased below, with two supplementary recommendations.

1. **Future Monitoring.** ADB should maintain its policy dialogue with the Government over reform in the energy sector. ADB's ongoing loan programs provide ample opportunity for reform dialogue and leverage on ESRP expected outputs.
2. **Covenants.** As in the above recommendation on Future Monitoring, further reform oriented covenants with respect to ESRP outputs should be incorporated in future loans to take advantage of the potential leverage.
3. **Additional Assistance.**
 - a. Substantial ADB involvement in future programs can help sustain the progress made under the ESRP. However, the investment needs to be linked to further reform efforts in such areas as: (i) commitment by the Government to announce tariff decisions approved by NEPRA in a timely manner and enable cost recovery across the power sector; (ii) clear policies on and payment arrangements for any subsidies for power supplies; (iii) stronger commitments to conclude the restructuring of WAPDA and the privatization of some of its successor companies; (iv) progress toward open access in the power sector,

at least for larger power consumers; (v) swift establishment of an independent CPPA; and (vi) strengthening of NEPRA as the independent power sector regulator.

- b. In general, the model for future lending on large, long term projects should be multitranche facilities, so that the lending programs can be linked to progress on ongoing conditions and to further reform efforts.
- c. ADB should also aim to provide funds in areas where it can take the lead in policy dialogue and reform, to ensure effective use of ADB funds.

(iv) Recommendations of Validation supplementary to the PCR.

As a supplement to the PCR recommendation on future monitoring, ADB should:

1. Evaluate the outcome of the labor retrenchment and redeployment resulting from the restructuring and privatization of KESC and WAPDA, to ensure that no social safeguard issues have come about on an ADB heavily supported program.
2. Ensure that Objectives, Outcomes, Components or Key Conditions and Outputs are clearly and definitively stated in the RRP's and PCR's and succinctly presented in the Design and Monitoring Framework and not buried in paragraphs of text.

F. Monitoring and Evaluation (M&E) Design, Implementation and Utilization (PCR assessment and Validation).

ADB provided close M&E during implementation of the ESRP, mainly through the ADB formal review missions, which were part of ADB's program design, and also through coordination of activities with the IMF, World Bank and other development partners. ADB's dialogue and counsel with the Government were based largely on this M&E which was essential and contributed significantly to the success of the Program. No post program monitoring was included in the design. A subprogram to monitor the effectiveness of the retrenchment and redeployment for KESC and WAPDA restructuring was planned as part of TA Loan 1809 but not implemented because the loan was cancelled. Further monitoring is proposed with respect to this subprogram in the recommendations herein.

G. Other (Safeguards, including governance and anticorruption; Fiduciary aspects):

(i) Safeguards.

Under the covenants of Loans 1807, 1808 and 1809 the Borrower and EA were required to ensure that social safeguards were addressed, with conditions covering (i) policy statements on economic and social objectives in the restructured power sector, (ii) mitigation measures to ensure that no undue adverse impacts are imposed on poor and low-income consumers during privatization of KESC, and (iii) labor restructuring strategy. It is noted that the PCR has indicated that most of these covenants were complied with. However, as discussed in several sections above, the TA Loan 1809 was particularly designed to undertake (i) a poverty impact assessment to monitor and evaluate impacts on residential and commercial consumers, with special attention to the poorest segment of consumers; and (ii) a labor impact assessment and provide a mitigation plan for privatization of KESC and WAPDA. This plan was cancelled with the loan precluding a significant social safeguard evaluation in the ESRP. This is considered further in the recommendations. There were no environmental safeguard issues in the ESRP.

(ii) Governance, Anticorruption and Fiduciary Aspects.

Governance, anticorruption and fiduciary aspects were central issues for ADB and its support of the ESRP. At the time of appraisal, worsening problems in these areas had a major impact on macroeconomic performance and hindered the effectiveness and sustainability of the power sector. Specifically, weak governance resulted in inefficient utility operations, power theft, illegal power supply, reduced billing and tariff collections, and nonpayment of arrears. These corrupt practices opened the way for massive waste and contributed to a build up of financial insolvency of the public utilities, which was possible only through corruption and malpractice at all levels of the organizational hierarchy—the government, politicians, labor, and the society in general. All of the key conditions of the ESRP as outlined in Section B(iii) are directly targeting governance, corruption and fiduciary concerns. Those conditions cover enhancing governance, enhancing the regulatory capacity and the capacity of the sector regulator, enhancing sector reform and enabling a competitive electricity market.

The PCR reports that, within the power sector most of the structural reforms of the ESRP that were designed for sustainability, such as, enhancing governance in the sector, enhancing the legal and regulatory framework, strengthening of the capacity of the sector regulator, enabling a competitive electricity market, are in place or progressing towards achieving these outputs. Pakistan's macroeconomic outlook has improved considerably since 2000 with demonstrated economic growth and a significantly improved balance of payments. This improvement in the national economy was an expected outcome of the ESRP but cannot be credited fully to the ESRP. However, if the expected outcomes can be sustained a marked reduction in corruption can be expected and, as indicated in Section D(iv), sustainability is likely.

H. Ratings:	PCR	IED Review	Reason for Disagreement/Comments
Relevance:	Relevant	Relevant	
Effectiveness in Achieving Outcome:	Effective	Effective	
Efficiency in Achieving Outcome and Outputs:	Efficient	Efficient	
Preliminary Assessment of Sustainability:	Likely	Likely	
Performance of Borrower and EA:	Satisfactory	Satisfactory	The performance of the Borrower and EA are considered in most activities to have performed very well but less so on some issues like privatization resulting in a rating of satisfactory.
Performance of ADB:	Satisfactory	Satisfactory	
Impact:	Positive	Substantial	This validation sees significant positive impacts already on the macroeconomy and the energy sector and the outputs will likely provide continuing positive impacts on the social environment.
Overall Assessment:	Successful	Successful	This validation has generally agreed with the assessment by the PCR. The overall assessment of this Validation is successful on the high side.
Quality of PCR:		Satisfactory	Although this validation has taken a number of different positions with respect to the performance of the TA, nonetheless all of the important information on the Program is in the PCR for the reader to form his own opinion and therefore is satisfactory.

ADB = Asian Development Bank, EA = executing agency, IED = Independent Evaluation Department, PCR = project completion report.

I. Comment of PCR Quality:

The PCR is well written and complete in content. Substantial documentation has been provided to support the conclusions and recommendations. The one criticism is that the objectives and outcomes are not clearly and crisply defined;⁹ and the reader has to do some searching for them. This criticism does not seriously detract from the quality of the PCR, as the key issues, the scope of work and performance evaluations are clear and understandable. In the PCR's review of the performance of the ESRP, this Validation considers that the PCR has been fair but somewhat conservative in its evaluation. Considering the high quality of the report overall this Validation rates the PCR as Satisfactory.

J., Recommendation for IED follow-up.

No need for project performance evaluation.

K. Data sources for Validation.

Back to office reports, program completion reports, and various communications related to program implementation.

⁹ There is no list of items in the PCR that are definitively referred to as objectives. In Section II B, Program Outputs, there are seven items listed that are not stated to be outputs but from the heading and the text this Validation considers them as outputs. But in Section III B, para 49, it states "All seven objectives of the ESRP were at least partly achieved", and this Validation can only assume the writer is referring to the seven outputs in Section II B. Without going in to detail this Validation found that the objectives were not clearly and crisply defined in the RRP either. It is recognized that differences of opinion arise on outputs versus objectives and outcomes and so a recommendation has been made for ADB to address this issue for future reports.

REGIONAL DEPARTMENT'S RESPONSE TO THE PROJECT COMPLETION REPORT VALIDATION REPORT

On 18 July 2008, Director, OED2, Operations Evaluation Department (OED), received the following comments from the Infrastructure Division, Central and West Asia Department.

CWID has reviewed the PCR Validation Report related to the PAK: Energy Sector Restructuring Program (loans 1807/1808/1809), and we fully support the report as we found it to be well written, tackling the relevant issues, and makes a great effort in assessing the good outputs and outcomes from the issues that still need to be addressed in the Pakistan energy sector.