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Economic Challenges of Post-Tsunami Reconstruction: Sri Lanka Two Years On

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1. Background

The earthquake that caused the tsunami on 26th December occurred at 6.58 a.m. Sri Lanka time with the first large wave hitting the east coast at 8.35 a.m. Within a very short time over 36,000 people were dead, and several hundred thousand had been displaced. In addition, massive damage had been inflicted on thousands of houses and other buildings, railways, bridges, communication networks and other infrastructure and capital assets.

Although Sri Lanka had in the past experienced periodic droughts, floods, landslides and the occasional cyclone, it had never experienced a tsunami, or indeed any other type of natural disaster of this scale and magnitude in recorded history.¹ Although the country was completely unprepared for a disaster of this scale, the relief effort got underway almost immediately – with support from domestic and international players – to ensure that survivors were fed, clothed and sheltered, the injured provided with medical attention, and thousands of bodies were cremated or buried. There can be little doubt that the initial response was a success despite the understandable confusion and even chaos that accompanied this effort at times.

However, as the reconstruction and rehabilitation phase has proceeded, it is clear that moving from the immediate relief effort to addressing the massive reconstruction tasks poses a different and, in many ways more complex, set of challenges. For Sri Lanka, as for other affected countries that were ready to accept external assistance, the promised aid appeared to be more than adequate to cover the full costs of both immediate relief and reconstruction, and produced, for a while, an almost euphoric national mood. Against the backdrop of a deteriorating macroeconomic environment by end 2004 – with GDP growth slowing from the second quarter, a persistent build-up of inflationary pressure from mid-year, widening fiscal and external current account deficits, and a rapidly depreciating currency – the tsunami itself provided a measure of stability to an economy that had been straining under growing macroeconomic imbalances, most visibly by averting a growing currency crisis by providing an unanticipated source of foreign capital inflows for the relief and reconstruction effort. The additional influx of foreign capital has not only allowed Sri Lanka to maintain a fairly

¹ Sri Lanka had no effective domestic hazard warning system, and had not felt the need to be part of international early warning systems, such as the Tsunami Warning System (TWS) in the Pacific (with 26 member countries).

healthy BOP since, but relief and reconstruction related expenditures have also given a boost to drive GDP growth to a healthy 6 per cent and over.

While the tsunami may have diverted attention away from the growing structural imbalances in the economy, these have not been eliminated. As the reconstruction and rehabilitation phase proceeds – albeit at a slower pace than initially anticipated – issues regarding the effectiveness with which resources were mobilized, the effectiveness of delivering assistance and its coordination, and the gaps opening up in financing reconstruction and its implications for macroeconomic policy management are taking centre stage. The aim of this study is to contribute to the discussions and debates on appropriate policies for the medium term reconstruction effort by providing an analysis of some of the priority issues. To this end, the study also involved a survey (see Appendix 1 for details on methodology and coverage).

2. Impact of Tsunami

The final death toll has been estimated at around 36,000 (30,958 listed as dead with an additional 5,644 listed as missing). Estimates of those displaced initially vary in the range of 800,000 with the number declining to 516,000 by mid-2005. Tens of thousands of houses were damaged or destroyed while many hotels were severely damaged, and another 6 were completely washed away. More than 240 schools were destroyed or sustained serious damage. Several hospitals, telecommunication networks, coastal railway network, etc., were also damaged.

Box 1 Immediate Impact	
Fatalities:	35,322 people
Injured:	21,441 people
Internally displaced people:	516,150
Widowed, orphaned, affected elderly and disabled:	40,000
Number of lost livelihoods:	150,000 (75% of the total fishing fleet)
Value of lost Assets :	US\$ 900 million
Houses destroyed:	89,000
Schools destroyed or damaged:	182 schools
Schools used as camps for IDPs:	446
Schoolchildren affected:	200,000
Health facilities destroyed or damaged:	97
Tourism Infrastructure damaged:	Large hotels: 53 out of 242 Small hotels: 248 Related small enterprises: 210
Cultivated arable land affected by salinity:	23,449 acres

Source: GOSL (2005a).

The geographic impact of the tsunami was uneven. Much of the coastal belt of the Northern, Eastern and Southern Provinces and some parts of the Western Province were severely damaged. The Eastern Province was particularly hard hit accounting for nearly a half of total deaths and displaced as well as numbers of houses damaged (Table 1).² From the very early stages, there were concerns about how assistance could be channelled to LTTE controlled areas. However, it appears that basic relief supplies did manage to get through to affected people during the early phases of the relief effort.

Table 1: Key Human and Asset Loss by District/Province

District/Province	No. of Deaths ^a	No. of Displaced ^a	No. of Damaged Houses ^b
Galle	4214	128077	11626
Matara	1342	13305	6238
Hambantota	4500	17723	2445
Southern Province	10056	159105	20309
Colombo	79	31239	6345
Gampaha	6	1449	854
Kalutara	256	27713	5741
Western Province	341	60401	12940
Puttalam	4	66	55
North Western Prov.	4	66	55
Ampara	10436	75172	18810
Batticaloa	2840	61912	17405
Trincomalee	1078	81643	7531
Eastern Province	14354	218727	43476
Jaffna	2640	39907	5515
Mullaitivu	3000	22557	5691
Killinochchi	500	1603	288
Northern Province	6200	64067	11494
Total	30955	502366	88544

Notes: a: As of January 2005; b: As of October 2005.

Source: Department of Census and Statistics (DCS).

The preliminary assessment of damages done by end-January 2005 through a joint effort of the Asian Development Bank (ADB), the Japan Bank for International Cooperation (JIBC), and the World Bank (WB) estimated that Sri Lanka had suffered asset damages of around US\$ 1 billion (4.5 per cent of GDP), and estimated that the medium-term financing needs (including immediate relief) would be around at US\$ 1.5-

² The severity of the tsunami disaster in the Northern and Eastern Provinces compounded problems arising from two decades of conflict between the government of Sri Lanka (GOSL) and the Liberation Tigers of Tamil Eelam (LTTE). The majority of an estimated 360,000 conflict related internally displaced people live in these two provinces.

1.6 billion (7.5 per cent of GDP). The largest financing needs were in the housing sector.³ The destruction of private assets was substantial (US\$ 700 million), in addition to public infrastructure and other assets. Loss of current output in the fisheries and tourism sectors – which were severely affected – were estimated at US\$ 200 million and US\$ 130 million, respectively. Key industrial, agricultural and metropolitan centres were relatively unaffected and the damage to capital assets was primarily to tourism and fisheries sectors, each of which contributes only around 1.5-2 per cent of GDP.

Table 2: Estimates of Losses and Needs Assessment on Reconstruction and Rebuilding (US\$ million)

	ADB/JBIC/WB ^a		GOSL		Pledges ^d	Committed ^d
	Losses	Needs	Feb. 05 ^b	May 05 ^c		
Housing	306-341	437-487	400	400	21.7.6	209.3
Roads	60	200	210	353	284.5	261.2
Water & sanitation	42	117	190	205	154.4	91.4
Railways	15	130	77			
Education	26	45	90	170	123.2	123.2
Health	60	84	100	100	157.2	60.1
Agriculture	3	4	10	10	3.1	3.1
Fishery	97	118	250	200	97.0	97.0
Tourism	250	130	58			
Power	10	67-77	-	115	325.9	325.5
Environment	10	18	30	30	1.1	1.1
Microfinance	-	-	150	157	256.6	166.6
Other	90	180	239	424	597.7	165.5
Total (\$ bn.)	0.9-1.0	1.5-1.6	1.8	2.2	2.2	1.5

Notes: a: ADB/JBIC/WB (2005); b: GOSL (2005d); c: GOSL (2005c); d: MFP (2005), *Budget Speech 2006*, (December 2005).

Source: ADB/JBIC/WB and GOSL.

These aggregate figures for financing needs were quite close to the government's own estimate of US\$ 1.8 billion presented in February 2005 though there were some important differences at the sector level damage estimates (GOSL, 2005d). Subsequently, the GOSL firmed up the country's total investment needs to be US\$ 2.2 billion (GOSL, 2005c).⁴ The differences between these estimates reflect the government's more ambitious longer-term plans while the donor assessment was largely

³ The significant differences between total recovery needs and damages in some sectors are due to the fact that recovery strategy for those sectors focuses on long term development targets rather than merely on restoration.

⁴ The GOSL identified its needs for a 3-5 years rehabilitation phase.

geared to restoring the pre-tsunami situation. In line with the regional variation in extent of damages incurred, the largest financing needs were identified in the East (45 per cent), followed by the South (26 per cent), North (19 per cent) and West (10 per cent).

3. Immediate Response

In the immediate aftermath of the tsunami, the Ministry of Public Security, Law and Order set up an operations centre, Centre for National Operations (CNO), to handle the response, and the Secretary to the Ministry was appointed as the Commissioner General of Essential Services to oversee coordination of government agencies involved in rescue and relief. Three Task Forces were set up – Task Force for Rescue and Relief (TAFRER), Task Force for Logistics, Law and Order (TAFLOL), and Task Force for Rebuilding the Nation (TAFREN) to address specific aspects of the relief effort.

While there were hiccups and some amount of confusion in organizing relief, for a country that had not previously experienced such a disaster, Sri Lankan institutions responded reasonably well. Essential medical aid, emergency food and other relief supplies were mobilized within a day. Temporary shelter was provided to the displaced in schools, other public and religious buildings, and tents. Communities and groups cooperated across barriers that had divided them for decades. Public and private sector organizations cooperated and organized relief efforts at many levels. Sri Lanka's past investments in public health paid off in this emergency: the broad-based public health system and community awareness of basic sanitary and hygienic practices ensured that there were no disease outbreaks.

Once the immediate relief and rehabilitation measures for provision of food, shelter, clothing, clean water, and sanitary and medical facilities to affected families had been provided, it was necessary to address community needs to cope with the trauma and start rebuilding their lives. The initial provision of cash grants to meet immediate needs included: (i) compensation of Rs. 15,000 (US\$ 150) for victims towards funeral expenses; (ii) payment of Rs. 375 (US\$ 3.75) in cash and rations for each member of the family unit per week, and a payment of Rs. 2,500 (US\$ 25) towards basic kitchen utensils. These initial measures were largely successful, though there were some problems with lack of coordination.⁵ Overall, the general consensus was that emergency relief was quite successful in meeting the immediate needs of the affected people.⁶

⁵ For example, while food rations were generally available, there were problems with availability of adequate varieties and quality in some locations; complaints emerged about application of different rules for the distribution of rations and cash grants from area to area.

⁶ An assessment of the initial response to the tsunami at the Sri Lanka Development Forum 2005 can be found at www.erd.gov.lk/DevForum/

4. Short Term Economic Impact

The tsunami struck at a time when the Sri Lankan macro economy was already under pressure on several fronts, reigniting fears of a slide into the kind of crisis that was seen in 2001 when the economy contracted by 1.5 per cent (Table 3). On the policy front, there was considerable unease within the business and investor community about the direction of economic policy under a new government elected in April 2004. Its programme, with the stated goal of 'growth with equity', and a strong emphasis on rural economic development, was viewed as being populist and interventionist.

Table 3: Selected Macroeconomic Indicators: 2001-2005

NATIONAL ACCOUNTS		2001	2002	2003	2004	2005
GDP	\$ billion	15.1	16.4	18.2	19.4	23.2
GDP growth	%	-1.5	4.0	6.0	5.4	6.0
Agriculture	%	-3.4	2.5	1.6	-0.3	1.5
Industry	%	-2.1	1.0	5.5	5.2	8.3
Services	%	-0.5	6.1	7.9	7.6	6.4
Investment	% of GDP	22.0	21.3	22.1	25.0	26.5
Savings	% of GDP	15.8	14.5	15.9	15.9	17.2
EXTERNAL SECTOR						
Exports	\$ million	4817	4699	5133	5757	6347
Imports	\$ million	5974	6105	6672	8000	8863
Trade balance	% of GDP	-7.3	-8.5	-8.4	-11.2	-10.9
Current a/c balance	% of GDP	-1.4	-1.4	-0.4	-3.2	-2.8
FDI	% of GDP	0.5	1.1	0.9	1.1	1.0
Official reserves	\$ million	1338	1700	2329	2196	2735
Tourist arrivals	'000 persons	336794	393174	500642	566202	549308
FISCAL VARIABLES						
Govt. expenditure	% of GDP	27.5	25.4	23.7	23.5	24.7
Govt. revenue	% of GDP	16.7	16.5	15.7	15.4	16.1
Fiscal balance	% of GDP	-10.8	-8.9	-8.0	-8.2	-8.7
Govt. debt	% of GDP	103.2	105.4	105.8	105.5	93.9
PRICES AND MONEY						
Rate of inflation	%	14.2	9.6	6.3	7.6	11.6
Interest rate ^a	%	10.8	7.5	5.3	5.3	6.2
Broad money (M2)	% change	13.6	13.4	15.3	19.6	19.1
Exchange rate	Rs/US\$	93.2	96.7	96.7	104.6	102.1
ASPI ^b	1985=100	621.0	815.1	1062.1	1506.9	1922.2

Notes: a. Commercial banks' weighted average deposit rate; b. All share price index.

Source: Central Bank of Sri Lanka, *Annual Report*, various issues.

Economic growth began to slow from the second quarter of 2004 and ended the year with a growth rate of 5.4 per cent. Whilst the election related uncertainties and the

ensuing policy vacuum no doubt contributed to the slowdown in economic activity, some policy weaknesses and the slow pace of reforms contributed to the lacklustre performance. The most visible, and potentially the most destabilizing manifestation of weakening macroeconomic management in 2004 was a persistent build up of inflationary pressure from mid-year onwards. Inflationary pressure was fuelled on multiple fronts, not least by the conduct of an expansionary fiscal policy driven by increased subsidies and transfers.

Domestic imbalances were exacerbated by a ballooning oil import bill which saw the current account deficit on the balance of payments (BOP) widening to over 3.3 per cent of GDP in 2004 (from 0.4 per cent in 2003). This was accompanied by a deceleration of capital inflows, with long-term inflows to the government (consisting primarily of foreign concessional loans) declining by US\$ 130 million in 2004. Foreign borrowings by the commercial banking sector increased significantly in 2004 raising the country's foreign private debt exposure. The currency depreciated by 8.5 per cent against the US dollar despite efforts to bolster the exchange rate which contributed to the decline in Sri Lanka's gross official reserves from US\$ 2.3 billion at the beginning of 2004 to US\$ 1.9 billion by November.

These domestic and external developments led to an acceleration of inflation from mid-2004, and real interest rates turned negative. Symptoms of a bubble economy began to emerge: a sharp increase in credit growth in excess of 20 per cent and a boom in the Colombo stock market unsupported by major indicators of economic fundamentals. The peace process appeared to have stalled, and with privatization initiatives shelved concerns over the government's ability to reduce the fiscal deficit began to increase. Markets started to get jittery with the growing realization that fundamental imbalances in the economy were intensifying. Though the external payments situation improved marginally in December 2004 the rupee depreciation again gathered pace. On 17 December 2004, the currency fell to a historical low of Rs.105 against the US dollar.

Against this backdrop, estimates of the immediate negative impact on output as measured by the GDP figure was expected to be fairly limited – ranging from 0.5-0.7 per cent reduction in 2005 GDP. Although the relatively small impact on GDP appeared somewhat surprising given the extent of the asset and human losses, it is partly because only a relatively small sector of the economy was affected and spending on relief efforts was expected to have an immediate positive effect on current GDP.

5. Rehabilitation/Reconstruction/Recovery Phase

5.1 Recovery Targets/Actual Progress

The government identified the reconstruction and rehabilitation phase to be spread over 3-5 years (GOSL, May 2005). Nevertheless, there were the inevitable pronouncements at the political level that all permanent housing needs would be met within a year. Over time, it has become quite clear that housing needs, for example, are likely to be met fully only in 2007. Reconstruction of damaged schools and hospitals, and rehabilitation of roads, bridges, etc. is likely to take even longer.

5.1.1 Infrastructure

A total of 182 schools and 222 health institutions were affected by the tsunami. Targets in these sectors include the reconstruction and renovation of 182 schools, 4 universities, 7 Vocational Training Authorities, 446 IDP schools (schools used as refugee camps) and the reconstruction and renovation of 222 health institutions. As building schools and hospitals are comparatively time consuming and complex, work in these areas have been divided in to four phases, namely, designing and planning, work to be commenced, work in progress and completion of activities.

By June 2006, reconstruction of 13 schools had been completed with 97 to be completed by the end of the year, 71 schools in 2007 and 3 in 2008. In the health sector, 33 constructions have been completed with work in 76 to end by the end of 2006, 105 in 2007 and 13 in 2008. However, it is acknowledged that due to difficulties in land issues, non-availability of raw materials, donor funding problems, etc. that targets may have to be revised accordingly (RADA, June 2006).

Table 4: Progress in Education and Health Infrastructure

	Education	Health
No. affected	182	222
MOUs signed	173	217
Without donors	9	5
Design & planning stage	78	109
To commence		6
Work in progress	86	69
Completed	13	33

Source: RADA (2006).

Key infrastructure damage was to roads and railways. A total length of approximately 800 kms of national road network and 1500 kms of provincial and local government roads were damaged. The railway infrastructure on a 160 km long stretch was also

severely damaged. The target date for completion of road and bridge reconstruction is set at 2009. The most serious constraint is likely to be lack of capacity and material. It is recognized that the national construction industry does not have the number of contractors, equipment or skilled workforce for a major reconstruction effort (GOSL, 2005a). The spiralling cost of construction material is likely to strain government finances to meet its targets effectively.

Table 5: Progress in Infrastructure

	Damage	Progress
Water & sanitation		130 projects planned. Donor commitment for 96 projects.
Roads	Rehabilitation of 1.172 km of roads	2 projects under way. 8 in tendering process.
Bridges	25 major bridges	4 commenced construction; 10 in tendering process.

Source: RADA (2006).

Relocation of communities have created new infrastructure needs in order to bring access to infrastructure to its pre-tsunami levels. As described in detail later, a large share of relocated households are worse off in terms of access to water, roads, pre-schools and health clinics. There is a need to expand infrastructure plans to incorporate these added needs.

5.1.2 Housing

The initial requirement for transitional shelter was put at 55,000 units but this figure was revised to 60,000 over the months to accommodate 50 per cent of the estimated 500,000 internally displaced while the remainder were assumed to have received shelter from friends, relatives, etc. (GOSL, 2005a). Progress on providing transitional shelters by and large was fairly good; by end 2005 over 56,000 units had already been completed.⁷

Given that most shelters were built with a one year time frame in mind, additional support has been required in instances to maintain and sustain them for another year. Some issues and constraints of transitional shelters that have been identified by RADA (June 2006) include the following: (i) many transitional shelters were found to be in need of basic facilities such as water, sanitation, electricity, waste disposal arrangements, etc.; (ii) there has been a lack of funds to accommodate operational costs such as electricity and water bills, and transport for supervisory visits to these areas; (iii) an estimated 10,604 transitional shelters do not have donors who could undertake care

⁷ By September 2005, only 2000 families were still said to be in emergency accommodation www.reliefweb.int/

and maintenance; (iv) lack of funding set aside for de-commissioning; and (v) absence of a mechanism to track the movement of displaced families from transitional shelters to permanent housing or to the homes of relatives and friends.

Table 6: Current Transitional Shelter Needs

	Jan. 2005	Dec. 2005	June 2006 ^a	Dec. 2006
Government Camps	56,000	53,000	42,196	17,083
Private Homes	42,525	32,525	32,367	
Total	98,525	85,525	74,563	17,083

Notes: a: Post housing policy revision.

Source: RADA (2006).

According to the latest estimates of RADA (June 2006), the total numbers of displaced as of January 2005 was estimated at a total of 98,525 of whom 56,000 were still in government camps (transitional shelter) while the rest were with families/friends. By end December 2005 the numbers displaced had dropped to 85,525 of whom 53,000 were in transitional shelter. This figure is expected to drop to 17,000 by end 2006 where government funded housing under a revised tsunami housing policy is expected to provide the requisite number of housing units in 2007.

The government's early declaration of a buffer zone of 100 metres in the south and southwest coast and 200 metres in the north and east coast of the country led to the initiation of two types of housing programmes: (i) donor-built housing reconstruction, and (ii) home owner-driven housing reconstruction. No reconstruction of houses (partially or fully damaged) was to be allowed within the buffer zone. Thus, all affected households within the demarcated buffer zone were to be provided a house built with donor assistance on land allocated by the state while allowing them to retain ownership of the original land. Households were not required to demonstrate ownership of land to qualify for such assistance.

For those whose damaged houses were deemed to be outside the designated buffer zone, the government agreed to provide grants and loans for households to re-build at the same location. In order to qualify for the entitlement, households were required to prove ownership to the land. The criteria set down in terms of financing such reconstruction included an assessment of damages on a points basis where a house deemed to be more than 40 per cent damaged would qualify for a grant of Rs. 250,000 (US\$ 2,500) in four instalments, based on progress. A grant of Rs. 100,000 (US\$ 1,000) was made available to rebuild a house deemed to be less than 40 per cent damaged, disbursed in two stages.

Predictably, the buffer zone became a politically controversial issue from the very outset. The limits were set in a fairly arbitrary manner, not taking account of topographical and other relevant features of the land that would affect hazard risk. There was also dissatisfaction that the rules were not to be applied across all building units, with tourist enterprises being permitted to rebuild within the designated zone. Many of the tsunami affected fishermen, for example, argued the need to retain close proximity to the coastline to sustain their livelihoods.

However, IPS-TS 2006 results show that about 60 per cent of the surveyed households think that the government's original buffer zone rule was a 'good idea'. The data at the Grama Niladari Division (GND) level agree with this finding with almost all Grama Niladaris (GNs) interviewed agreeing that the government's original buffer zone policy was good. Paradoxically, they were also happy with the relaxation of the buffer zone in 2006. Although there were delays in providing housing because of the buffer zone rule, most households have the prospect of better housing because of this policy: IPS-TS 2005 results find that most houses that were destroyed were smaller than the minimum floor area of 500 sq. ft. specified for new houses under the donor-driven programme.⁸ While all new houses are to be built with permanent housing materials a large share of destroyed houses were made of temporary housing material.⁹ Also, households that did not have legal ownership of land were given houses under the donor-driven programme.¹⁰ These factors may have outweighed the delays in housing progress due to the 2005 buffer-zone rule.

⁸ About, 53 per cent of the surveyed houses made unusable by the tsunami were less than 450 sq. ft, while only 10 per cent were bigger than 600 sq. ft.

⁹ About 32 per cent of roofs of the surveyed houses were made of cadjan or metal sheets, while close to half the surveyed houses had walls made of temporary material.

¹⁰ About 13 per cent of surveyed households inside the buffer zone owned houses on government land, while a further 9 per cent owned houses built on other people's private land.

Box 2
Revised Tsunami Housing Policy

- 1) Government land + donor built house under the donor-driven housing programme primarily for all those who lived within the previous buffer zone
- 2) Government land + government cash grant (Rs. 250,000) to construct a new house + regulated donor assistance provided to complete the houses (not less than Rs. 250,000 depending on costs to meet the minimum standard house) through co-financing agreement.
- 3) Government cash grant (Rs. 150,000 for 3 divisions in Ampara and Rs. 250,000 for Colombo) to purchase land + government cash grant (Rs. 250,000) to construct a house + regulated donor assistance provided to complete (not less than Rs. 250,000 depending on costs to meet the minimum standard house) through co-financing agreement.
- 4) Housing reconstruction grant (Rs. 250,000 for fully damaged homes and Rs. 100,000 for partially damaged homes) + regulated donor assistance provided to complete only fully damaged houses as required for meeting minimum standard house through co-financing agreement.

Source: RADA (2006).

By end 2005, the government had largely abandoned the idea of enforcing the buffer zone restrictions. In particular, the scarcity of land to relocate affected households highlighted the impracticality of enforcing such a zone in the face of a need to ensure permanent housing within a reasonable period of time. A more relaxed buffer zone policy was announced in May 2006 along with a "Revised Tsunami Housing Policy".¹¹ It was essentially aimed at ensuring that all tsunami affected people return or get new houses by the end of year 2006. The policy document promised "a house for a house, regardless of land ownership". It defines two zones (not buffer zones)¹² with 4 housing options with the cost being shared by the government and the donors (see Box 2).

The new housing policy has pushed the total housing needs to 120,000 units.¹³ The key change has been a decision to include those without legal ownership of land outside the former buffer zone and extended families. In effect, it aims to provide every tsunami affected family, including encroachers a house or land and compensation, and

¹¹ The new boundaries are set according to the Coast Conservation Department (CCD) Coastal Management Plan of 1997.

¹² Zone 1 refers to any state reservation within tsunami affected areas while Zone 2 is any area outside Zone 1.

¹³ See RADA (2006). However, it is not clear how the additional housing requirements fit within the designated owner/donor-driven programmes.

encourages those who have land or a house (damaged in the earlier declared buffer zone) to build on the same premises or rebuild the same house. A significant feature of the revised policy is to encourage encroachers, particularly fisher folk to relocate elsewhere under the cash-to-purchase land and cash-to-build options which it is hoped would assist in retaining the land as a buffer zone and reservations.

Secondly, unlike the earlier policy, the government and donors together are to provide for a minimum of Rs. 500,000 (US\$ 5,000) cash support to a tsunami affected family to build a house. The significant cost escalation of construction material and labour undoubtedly required a revision of the earlier estimates. Under the revised policy, the GOSL is to provide the cash grant, initially re-imbursed by different development banks and bilateral donors.¹⁴ The grant of Rs. 250,000 (US\$ 2,500) each from the government and donors is to be given in instalments; a first instalment of Rs. 50,000 (US\$ 500) by the government matched equally by the donor and thereafter followed accordingly. The beneficiary is to receive full title to the property in the resettlement area (while retaining legal ownership of property within re-designated buffer zone).

Finally, under the donor-built reconstruction programme, standard requirements have been set down by the GOSL of a floor area of 500 sq. ft. where the donor is to make available common infrastructure and the government is to provide services up to the relocation site. The technical specifications have been revised to ensure a more equitable basis. This was primarily a response to the initial experience where donors are said to have built houses ranging from Rs. 400,000 to over Rs. 1 million (US\$ 4,000 to over US\$ 10,000) causing friction amongst recipients.¹⁵

Overall, revision to the housing policy means that in addition to the increased cash grant component, the significant increase in the number of housing units deemed necessary will invariably raise questions about the ability to meet the costs of reconstruction within the commitments made by donors. It has also created immense confusion amongst the beneficiary households. Only about a quarter of the households surveyed in the IPS-TS 2006 were clear about their housing entitlements. Close to 60 per cent had indicated that they would like legal advice regarding their rights as a homeowner.

¹⁴ Extended since to co-financing arrangements through local and foreign NGOs as well.

¹⁵ *Sunday Times*, 14 May, 2006. About 3 per cent of the households surveyed in the IPS-TS 2006 had shifted from one NGO allocated list to another. The most common reasons for switching were: expectation of better assistance, to move closer to the sea, or because the first NGO had failed to deliver a house.

Table 7: Housing Requirement

	Requirement Jan. 2005	Completed			Target
		Dec. 2005	June 2006	Sept. 2006	Dec.2006
Donor-driven	30602	4045	11213	11871	16578
Owner-driven	67923	10609	37770	39706	67923
Private donors		3500	6500		5000
Govt. funded ^a					13416
Total	98525	18154	55483		102917

Notes: a: From revised housing policy options 2 and 3 (includes relocation/self-driven government funded housing).

Source: RADA (2006) supplemented by data obtained from RADA for September 2006.

Available housing data suggest that a total of around 58,000 houses have been built (donor-driven, owner-driven and private sector/private individuals). This is close to 60 per cent of the target of 98,525 houses as of the 2004/2005 initial survey. Another 41,000 houses are being constructed (41 per cent of the initial 2004/2005 target). Out of the completed houses, 39,709 units have been completed under the owner-driven programme and 11,875 under the donor-driven programme. The government anticipates that by December 2006, a total of 102,917 houses would be completed with only an additional 17,083 to be constructed in 2007. Despite official figures put out, there appears to be a lack of reliable and consistent information on the number of housing units needed as well as the progress to date.

Table 8: Housing Situation as at July 2006
(by eligibility under 2005 housing programme)

Eligibility	Rebuilt	Relocated	Donor-built on Old Site	Temporary Housing	NI ^a	Total
Donor-driven	52	25	11	175	5	268
	19.4	9.3	4.1	65.3	1.9	100.0
Owner-driven	76	25	22	26	8	157
	48.4	15.9	14.0	16.6	5.1	100.0
Not eligible	34	17	24	59	0	134
	25.4	12.7	17.9	44.0	0.0	100.0
Total	162	67	57	260	13	559

Notes: a: No Information. b.: Households not owning a house before the tsunami (70% of 134) and households owning a house on encroached land (30% of 134) outside the buffer zone were not eligible for a new house under the 2005 housing policy.

Source: Own calculations based on IPS TS 2005 and IPS TS 2006 data.

IPS-TS 2005 and 2006 data give information on the location with respect to the 2005-buffer zone and house and land tenure for 559 households. Of these, 268 were eligible for the donor-driven housing and 157 were eligible for owner-driven housing. A total of 134 households were not eligible for a new house either because they were not house owners before the tsunami (70 per cent of 134) or because they were outside the 2005-buffer zone, and were house owners without land tenure (30 per cent of 134).

The housing progress is worst for people who were eligible for donor-driven housing. About 65 per cent of such households are still in temporary housing situations. At the same time about 56 per cent of households that were not eligible for a new house have also received a house. There appears to be some inconsistencies in the government's housing policy and what has taken place in practice. Some households eligible to relocate under the donor-driven housing programme have rebuilt (19 per cent), while others eligible to rebuild under the owner-driven housing programme have relocated (16 per cent). Some households have received houses outside both these programmes, and others who were not eligible to receive a house under either programme have received houses (see Table 8).

This data signals problems of coordination across various donors, especially those who have provided houses without adhering to government plans. Discussions with GND and district level government officials suggest that reluctance of local non-government agents to share information on aid distribution and their beneficiaries have exacerbated the problem of coordination and monitoring. More seriously, this suggests that the available macro level information on the housing requirement (see Table 7) may be misleading. The macro level takes the difference between the numbers of households eligible for housing and the number of houses already provided as the housing requirement. But, if people have received houses outside their eligibility, or if people who received houses were not those eligible for houses, the above calculation will be incorrect.

Nevertheless, the data suggest that the donor-driven programme as of September 2006 has a relatively slow completion rate (approximately 35 per cent). Delays in the provision of basic infrastructure and access to utilities have also held up the process of beneficiaries moving into new homes. As of end August 2006, only about 7,000 houses had actually been handed over. At the time of the IPS survey carried out in July 2006, about 65 per cent of the surveyed households eligible for donor-driven housing programme were in temporary housing (in camps, rented housing or living with friends and family), compared to 17 per cent of households eligible for the owner-driven housing programme. Also, as detailed later, many relocated households do not have their own sources of water and are worse off in terms of access to roads, pre-schools and health clinics compared to their pre-tsunami levels of access.

Table 9: Status of Donor-Driven Housing Programme
(As at September 2006)

District/Province	Total Houses Damaged ^a	MOUs Signed (No. of Units) ^b	Construction Status (No. of Units) ^b	
			Completed	On-going
Galle	2213	3910	1951	935
Matara	1032	2827	1421	594
Hambantota	2343	4995	3773	328
Southern Province	5588	11732	7145	1857
Colombo	5112	965	221	196
Gampaha	2179	2663	1334	431
Kalutara	643	550	246	0
Western Province	7934	4178	1801	627
Ampara	7236	5251	1094	1238
Batticaloa	1458	3370	406	872
Trincomalee	3428	4017	859	832
Eastern Province	12122	12638	2359	2942
Jaffna	3275	4337	427	766
Mullaitivu	3011	1200		435
Killinochchi	288	1237	143	140
Northern Province	6574	6774	570	1341
Total	32218	35322	11875	6767

Notes: a: Estimates from GOSL (2005a) to indicate regional variation.

b: Data obtained from RADA as of mid-September 2006.

Source: RADA.

The figures also confirm the significant regional variation in housing progress across the country. The Southern Province has met – and in some Districts exceeded – the requisite number of housing units with yet more houses under construction. By contrast, the Eastern Province with the highest requirement of housing is lagging well behind. The Western Province has also not fared well relative to the Southern Province, most likely due to greater difficulties in obtaining suitable land. In accordance with these macro level data, the IPS-TS 2006 survey – conducted in 14 GNDs in the Southern and Eastern provinces – shows that the progress in housing is best for those outside the 2005 buffer zone in the Southern Province. Less than 6 per cent of surveyed households in this region were in temporary housing. The progress in housing is worst for those in the Eastern Province – for households both within and outside the 2005 buffer zone. The progress is especially poor for households affected by the conflict.

The uneven progress in part is no doubt explained by the additional stress of escalation of conflict in the North and East of the country from end 2005. Nevertheless, there has also been much criticism that donors have failed to meet their commitments. It is significant that although MOUs for nearly 35,000 units have been signed, it has also been reported that as per the MOUs signed as of May 2006, work on 12,404 houses (approximately 41 per cent of the donor-driven housing case load) is yet to begin

(RADA, 2006). The completion rate for national NGOs appears to be much better than for international NGOs (Table 10).

Table 10: Houses Assigned and Completed by Donor Type
(As at mid-September 2006)

Donor Type	No. of Units^a	Completed
Private sector/funds	405	143
National NGOs	7240	931
International NGOs	8705	1864
United Nations	249	135
Government agencies	520	140
To be specified	18881	6688
Bilaterals	1048	70
Total	37048	9971

Notes: MOU figure.

Source: RADA, DAD data.

Lack of commitment by NGOs has been cited by RADA as a reason for the slow progress in housing. The head of RADA has alleged that 18 months after the tsunami, international NGOs who had pledged to build 70,000 houses and signed agreements for 19,600 had only completed 2900 houses.¹⁶ Unilateral decisions taken by some INGOs to terminate their MOUs with the government has been an added difficulty in the efforts of housing reconstruction in the country.¹⁷ There have been some allegations that some INGOs left the country with money that was to be used for reconstruction of houses. However, the government has little power to take any legal action as the funds have been channelled directly to INGOs from donors. On the other hand, NGOs have blamed delays in obtaining appropriate land as a key obstacle to meeting their commitments. In addition, it is possible that internal procurement procedures that INGOs in particular may be subject to have also contributed to delays.

¹⁶ *Sunday Observer* 27 August 2006. Some examples cited were INGOs such as CARITAS that had pledged to build 26,000 houses had only managed to complete 72 houses; World Vision Lanka had pledged to build 10,000 houses, but only 198 houses have been completed; and Red Cross had pledged 15,000 houses, but has completed only 169 houses; Care International had pledged 6,800 houses, but has completed only 125 houses.

¹⁷ *Daily Mirror*, 28 January, 2006.

Table 11: Quality of Housing Before and After Tsunami for Relocated Households

	No.	Better Now	Worse Now	No Difference
House design	69	42%	41%	14%
Construction materials used for housing	69	27%	49%	21%
Access to services (water, electricity, road)	69	14%	63%	20%
Primary school within 1 km	73	10%	62%	29%
Clinic within 1 km	73	1%	59%	40%

Source: Own calculations using IPS-TS 2005 and 2006.

These findings are consistent with the IPS-TS community level survey results. These show that lack of land and delays in obtaining donor assistance are main reasons for the slow progress in housing for households eligible for donor-driven housing programme. IPS-TS 2006 data also points to large inconsistencies in allocating houses, which suggests that the housing situation could be different from what is suggested by macro level figures. Of the surveyed people who have already relocated, about 37 per cent were eligible for owner-driven housing programme and a further 25 per cent were not eligible for a house under either programme. In addition to the slow progress in the donor-driven housing programme, IPS-TS 2006 results show that some people are worse off now in terms of quality of housing and access to services (Table 11). Also, survey results show that people's life styles were not taken into consideration when designing houses. E.g., the percent of households using expensive sources of fuel for cooking such as gas and electricity has increased from 10 per cent to 18 per cent, primarily because many of the new houses did not include a kitchen with a chimney to make the use of fuel wood for cooking possible.

Table 12: Status of Owner-Driven Housing Programme

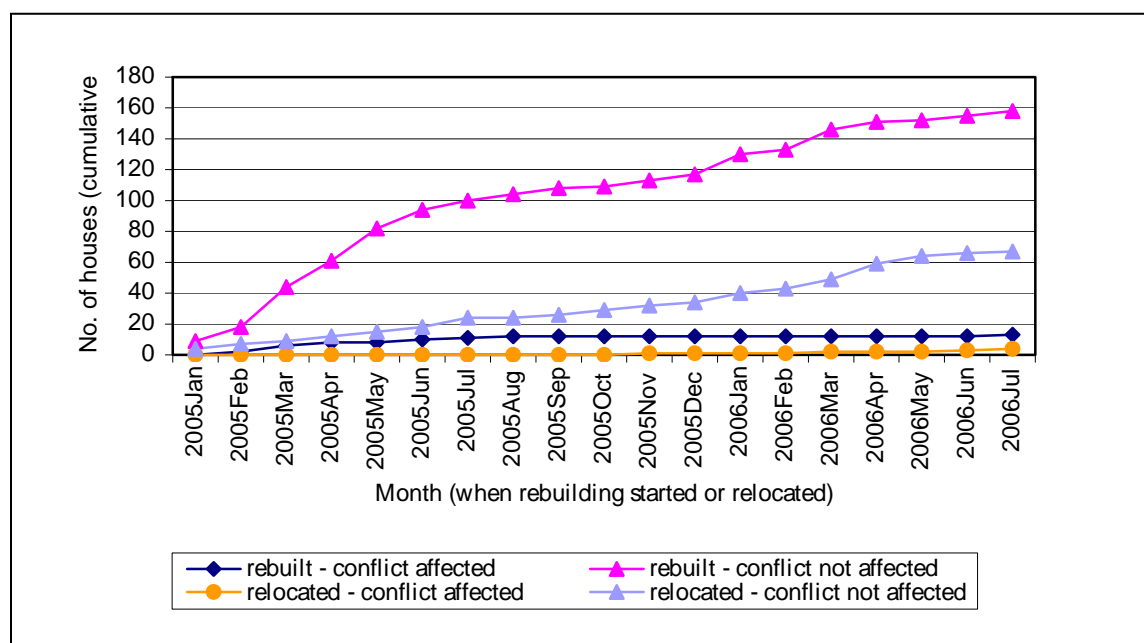
District/Province	As at end May 2006 ^a		As at mid-September 2006 ^b	
	Total Houses Damaged	Amount Paid (US\$ mn)	Units Completed	Units Under Construction
Galle	9266	11.4	8252	1957
Matara	4973	5.9	4774	949
Hambantota	1567	1.7	1247	320
Southern Province	15806	19.0	14273	3226
Colombo	39	0.0	24	15
Gampaha	85	0.1	3987	855
Kalutara	4358	5.0	67	49
Western Province	4482	5.1	4078	919
Ampara	18048	16.8	8986	11633
Batticaloa	18307	22.2	7453	11106

Trincomalee	3269	4.8	3083	440
Eastern Province	39624	43.8	19522	23179
Jaffna	4426	3.4	1614	2808
Mullaitivu	3585	3.3	222	4425
Killinochchi				
Northern Province	8011	6.7	1836	7233
Total	67923	74.6	39709	34557

Notes: a: www.rada.gov.lk.
b: Data obtained from RADA.

Source: RADA.

Figure 1: Housing Progress by Conflict Affected



Source: Own calculations using IPS-TS 2006 data.

In contrast to the donor-driven programme, the owner driven housing reconstruction appears to have proceeded much more quickly (Table 12). Data for disbursement of loans is only available as at end May 2006 and indicated that a total of US\$ 75 million had been disbursed (Table 13). The disbursement also appears to have progressed relatively smoothly with the first instalment been claimed by all affected households. According to IPS-TS 2006 survey data, about 82 per cent of households that have received assistance for rebuilding found obtaining funds from government fairly easy, while only 11 per cent found it very difficult, and the rest had either not attempted to obtain funds from government or had declined to comment. In comparison, 45 per cent of households who had obtained assistance for rebuilding found obtaining assistance from NGOs fairly easy, while 15 per cent found it very difficult.

As would be expected, the progress on partially damaged housing has been much quicker than for fully damaged housing (with just over 16 per cent having obtained the fourth instalment). There appears to be a consistent disbursement across regions vis-à-vis the total damage incurred. For example, the Eastern Province accounted for nearly 60 per cent of the total number of damaged houses and appears also to have received an equivalent share of the total grant disbursement. Nevertheless, it appears once more that the Southern and Western Provinces for instance have been able to have a better completion rate than most other regions. This could partly be due to the extremely slow progress of the rebuilding process in the conflict-affected areas (see Figure 1).

Table 13: Number of Payments Made
(As at end May 2006)

	Fully Damaged	No. of Payments	Partially Damaged	No. of Payments	Total
1 st instalment	Foundation	30959	Walls, roofs, windows	36963	67923
2 nd instalment	Walls	21047	Almost completed	30476	51523
3 rd instalment	Roof	11783			11783
4 th instalment	Expected completion	5080			5080

Source: RADA (www.rada.gov.lk).

Given the relatively smooth progress of the owner-driven housing programme vis-à-vis the donor-driven programme, one option that RADA has put forward is to convert the donor driven housing projects to owner-driven programmes. It is reported that the owner-driven housing programme has “proven to be effective” as the families get the funds directly to their hands.¹⁸ Not only has the owner-driven housing programme moved more swiftly but it has also proven to be cheaper than the donor-driven programme. A single donor assisted housing unit is estimated to require Rs. 1.35 million (US\$ 10,350) to develop given the need to secure land, infrastructure and the need to use registered contractors.¹⁹ There has also been a significant escalation of costs of house reconstruction over time. As of July 2006, it has been estimated that the cost of building a 500 sq. ft. house had crept up to about Rs. 750,000 (US\$ 7,500).²⁰ The government is negotiating with donors to top up funding to ensure that adequate resources are made available to affected families.

¹⁸ *Daily Mirror*, 28 January, 2006.

¹⁹ *Daily Mirror*, 17 July, 2006.

²⁰ *Daily Mirror*, 17 July, 2006.

Thus, RADA has urged the INGOs to transfer the funds they have for tsunami reconstruction to the Treasury so that the government can direct the funds to the victims. Shifting house construction under the owner-driven programme has necessitated additional funding of around US\$ 50 million (MFP, 2006). This is a means of co-financing government efforts by directly distributing among beneficiaries the funds allocated for building by the INGOs themselves. To ensure transparency, donors who opt to convert to the owner-driven programme may also be given a list of beneficiaries whom they can co-finance so that INGOs themselves can verify their needs and make direct payments to these families. The conversion is argued to be the most practical way of resolving some of the logistical issues faced by INGOs in constructing houses themselves. According to available information, the majority of INGOs, barring one had adopted a lethargic attitude over the request to transfer funds. The sole exception appears to have been the Red Cross which had complied with the request to cooperate with the government and converted two-third of their pledges (US\$ 25 million) to the owner- driven programme.²¹

The revision of the housing policy has undoubtedly led to some degree of confusion. With the switch from one scheme to another, district/divisional secretariats have to revise the lists of beneficiaries falling under any one particular scheme. According to the information given by GNs where the IPS community level survey was conducted, on average the number of families to be relocated has decreased from 410 to 239 with the new housing policy. However, there are wide variations in the change in number of families to be relocated by GND. As expected, the change in housing policy has affected the people within the 2005 buffer-zone more. However, of these only 15 per cent of households stated that the change in housing policy affected them 'a lot', and a further 15 per cent were somewhat affected by the housing policy while majority were not affected.

Escalating costs of building materials and skilled labour may also have added to slow progress in housing. In the IPS-TS 2006 survey, all interviewed key informants reported that building material and wages of carpenters and masons have increased since the tsunami. More than three-fourths of the key informants consider prices to have increased by 'a lot', while the others think that they have increased 'somewhat'.

5.1.3 Livelihoods

An estimated 150,000 people lost their main source of income due to the tsunami.²² About 50 per cent are estimated to have been in the fisheries sector, with another 4-5

²¹ *Sunday Observer* 27 August 2006.

²² RADA estimates place those who have lost livelihoods at 200,000 with a further 125,000 jobs being lost indirectly (see www.rada.gov.lk).

per cent in agriculture, and the remaining in tourism and small and micro enterprise related sectors (GOSL, 2005a). Types of livelihood assistance have included grants in kind (income generating assets), grants in cash, loans, training (vocational, business support, etc.), cash-for-work or temporary employment. The results of the IPS-TS 2006 show that all the surveyed GNDs received livelihood support – in terms of equipment and boats, livelihoods training and credit. Of the estimated 150,000 who lost their main source of income, available information suggests that around 75 per cent of the families had regained their main source of income by end 2005 (GOSL, 2005a). This is supported by the IPS-TS 2006 survey where 71 per cent are found to have regained their old source of livelihood. Only 8 per cent of heads of households have changed their livelihood,²³ while 21 per cent are unemployed.²⁴

Tourism infrastructure suffered significant damage in the tsunami. A total of 53 (out of 242) large hotels and a further 248 small hotels were affected. In terms of hotel rooms, about 3,500 out of a total of 13,000 rooms available in medium to large scale hotels were not in service by February 2005. Approximately 210 small enterprises that rely on the tourism industry were also destroyed along the coastline. These are essentially enterprises engaged in informal sector activity (for example, 190 of the 210 destroyed enterprises were not registered with the Tourist Board). Of the 53 large scale hotels damaged, 41 were back in operation by end 2005.

The most severe impact on livelihoods was in the fisheries sector with those engaged in fishing or related activities estimated to make up over one-third of the affected households. Estimates by the Ministry of Fisheries and Aquatic Resources (MFAR, 2006) suggests that over 100,000 people in the fisheries sector were displaced, over 30,000 houses damaged or destroyed (16,434 damaged and 13,329 destroyed) and nearly 4,870 fishermen lost their lives with 136 reported missing. In terms of equipment, an estimated 75 per cent of the fishing fleet (32,000 boats) had been totally destroyed or severely damaged (around 23 per cent were made un-seaworthy and 54 per cent were destroyed). It is estimated that 1 million fishing nets were also lost. Apart from these, the infrastructure of the fishing industry like boat yards, cold rooms, ice plants and fish markets were damaged. Damage to fishery harbours and other infrastructure facilities, government services facilities, coast conservation structures, etc., is placed at US\$ 275 million, while repair and replacement cost of the damaged fleet has been estimated at US\$ 60 million.

²³ About a half the household heads that have changed their livelihoods come from one GND, in the Eastern Province.

²⁴ Further, the current housing situation does not appear to have any effect on livelihood recovery.

The fisheries sector received assistance more so than other affected sectors and saw a rapid recovery of assets in many areas. It is estimated that 100 per cent of damaged boats had been repaired by end 2005. However, it has been noted that in all boat types except the beach seine crafts, the numbers repaired have exceeded the number of boats damaged. Some of the possible reasons cited have been the attraction of boats from non-tsunami affected areas for repairing, boat owners taking this as an opportunity to get minor repairs done to their boats, the possible classification of beach seine crafts as traditional crafts and the possibility that boats classified as destroyed been actually repaired and put back to sea.

Table 14: Fishing Boats Destroyed and Damaged

Boat Type	2004 Fleet	Damaged		Destroyed	
		No.	Repaired	No.	Replaced
Multi-day	1581	676	780	187	0
One day boats	1493	783	904	276	29
FRP boats	11559	3211	4258	4480	4321
Traditional craft	15934	2435	3479	11158	8636
Beach seine craft	1052	161	134	818	204
Total	31619	7266	9555	16919	13190

Source: MFAR (2006), "Strategy and Programme for Reconstruction and Development of the Marine Fisheries Sector".

However, poor quality of repairs has also become an issue. According to results of a survey carried out in December 2005, 8 per cent of the repaired boats were not being used as those fishermen were not satisfied with the repairs.²⁵ It was found that the quality of repair is low mostly amongst the FRP and traditional types of boats. Further, 19 per cent of the new boats provided were found to be not seaworthy. The reasons for the low quality repairs have been attributed to the "unfavourable conditions with inadequate technical inputs and/or supervision". Lack of knowledge and expertise on the part of NGOs as well as the fishermen on FRP boat building, and the non-existence of proper contracts for after-sales services resulted in boat-builders resorting to reducing the quality of material, reducing the thickness, etc., to improve profits and to meet deadlines.

In terms of the boats destroyed, by end 2005, 78 per cent of the destroyed fishing fleet had been replaced (this figure has risen to 95 per cent by mid 2006)²⁶ with pledges for more than 6,000 boats still outstanding. However, uncoordinated distribution efforts also led to conflicts and problems regarding factors like the increasing numbers of boats,

²⁵ Cited in MFAR, June 2006.

²⁶ RADA (2006).

the quality of boats, etc. The oversupply of boats is likely to be unhealthy for the fisheries sector as a whole. Some reasons for the oversupply of boats and other discrepancies were the non-existence of reliable data on the fishing fleet prior to the tsunami and the weaknesses of damage assessments done by a large number of agencies. The collection of data by individuals who were not familiar with the fishermen led many non-fishers to acquire boats. Misidentifications and overlaps have occurred as a result of delays in issuing Entitlement Cards by MFAR and also as a result of one beneficiary list being provided to more than one NGO with the idea of speeding up the process of recovery. Lack of coordination between the fisheries authorities and the NGOs, poor coordination between NGOs themselves and the adverse effects of competition amongst these agencies are some of the reasons for these errors and miscalculations (MFAR, 2006). Anecdotal evidence by district level authorities indicate that reluctance to share information on the part of some NGOs have made the task of coordinating even more difficult.

Another problem identified is that of genuine beneficiaries not receiving new boats. Findings of a survey done by the authorities in December 2005, when extrapolated suggest that only 6,067 of the 13,190 (46 per cent) boats distributed have gone to genuine beneficiaries. Provision of inputs to friends and relatives by small, local agencies as well as 'bypassing the fishing authorities' have resulted in all the boats not being given to true beneficiaries. Further, the provision of small fishing boats was seen as an 'attractive quick fix' with high visibility – easy and not expensive – for many NGOs. However, concerns that asset distribution is not fair may partly be resolved by the secondary market for these goods.

Again, the Southern and Western Provinces appear to have benefited with an excess of replacement in traditional and FRP boats, while the Northern and Eastern Provinces lag behind (Table 15). However, the lack of accurate data for the Northern Province may be one reason for its apparent poorest performance.

Table 15: Destroyed and Replaced Numbers of Boats by Region

District/Province	Traditional Boats		FRP Boats	
	Destroyed	Replaced	Destroyed	Replaced
Galle	549	633	173	376
Matara	507	385	156	88
Hambantota	649	842	387	404
Southern Province	1705	1860	716	868
Colombo	45	60	5	9
Gampaha	50	50	14	26
Kalutara	301	562	47	148

Western Province	396	672	66	183
Puttalam	12	12	14	14
North Western Prov.	12	12	14	14
Ampara	1479	1652	358	360
Batticaloa	2107	2141	494	97
Trincomalee	3034	2153	1097	514
Eastern Province	6620	5946	1949	971
Jaffna	1318	146	887	1744
Mullaitivu	936	0	848	466
Killinochchi	168	0	0	10
Northern Province	2422	146	1735	2220
Total	11158	8636	4480	4256

Source: MFAR (2006).

Access to credit was considered a vital element in supporting livelihood recovery. Most of the affected businesses were informal, small scale industries with an estimated 25,000 micro-enterprises said to have been damaged in the tsunami. In addition, 15,000 tsunami survivors were previously involved in self-employed and informal sector activities such as food processing, coir manufacture, carpentry, tailoring, etc. While over 40 organizations to support and provide a host of microfinance programmes to assist small and medium enterprises (SMEs) was established following the tsunami, the primary support came from two major government finance schemes.

The Central Bank of Sri Lanka (CBSL) has been implementing a microfinance scheme (*Susahana*) through the two state-owned commercial banks. The *Susahana* loan is provided with no repayment required for the first year and interest at a fixed rate of 6 per cent thereafter. The National Development Trust Fund (NDTF) is also offering similar terms through its partner organizations. By June 2006 25,735 loans and grants of Rs. 4769 million (US\$ 47 million) had been provided to micro, small and medium enterprises (RADA, 2006). In terms of their reach, the *Susahana* scheme which had disbursed US\$ 36 million to 8,000 borrowers in the tsunami affected areas by September 2005, it was reported that 75 per cent of the disbursements are in the south and west of the country while 60 per cent of the NDTF scheme was also disbursed in the south with only 40 per cent of its funds going to the north and east of the country (GOSL, 2005a).

It is recognized that a careful balance is needed between maintaining a repayment 'culture' while being realistic about the need for access to credit. Despite claims to the contrary and its stated intention to reach micro-entrepreneurs, the *Susahana* lending schemes have been set up in a way that makes it very difficult for small tsunami affected micro-entrepreneurs to obtain access to the scheme. The conditions for access are onerous. Guarantors are required who have a permanent income above a certain threshold level. Collateral is required, for which land within the buffer zone is not

acceptable. Loans are only to be given for businesses registered before the tsunami, which rules out many smaller unregistered businesses and stops people taking up new livelihoods in response to their changed post-tsunami circumstances, such as the death of the main earner, disability or new responsibilities to care for some family members. The terms of the *Susahana* need to be urgently reviewed to ensure that they can start to reach the poorer micro-entrepreneurs.²⁷

In fact, it has been acknowledged that the ground reality indicates that many businesses cannot apply and banks are reluctant to relax their collateral requirements, with affected businesses in the buffer zone hit especially hard (GOSL, 2005a). The report also finds that very few new clients were reached by the subsidized schemes and that there are a considerable number of entrepreneurs with no access to credit. These findings are supported by the IPS-TS 2006 results which show that only a few households (16 per cent of the sample) have applied for credit. A fair share of households have not applied for loans because they 'didn't know that they were eligible to receive loans' or because 'they were afraid that their applications would be rejected'. Nevertheless, most of those who had applied have received loans. However, they have had to provide collateral, and sometimes a guarantor in order to receive the loan, with the size of loans also being fairly small at less than Rs. 100,000 (US\$1,000).

On a positive note, there is evidence to suggest that micro credit providers improved cooperation and coordination in an attempt to try to maintain the micro credit culture that the post-tsunami surplus of micro credit funds at low interest rates was in danger of undermining.

One of the more successful livelihood related cash grant programmes initiated in January 2005 was to provide a monthly cash grant of Rs. 5,000 (US\$ 50) to each tsunami affected household for a period of 4 months. Over 250,000 households received the first two instalments on time immediately following the introduction of the programme.²⁸ However, directives were given to local level Divisional Secretaries by the Ministry of Finance to revise the lists of eligible beneficiaries which halted payments indefinitely. Eligibility criteria changed from time to time with most tsunami affected families not fully aware of the new criteria. The government circulars announcing the revised criteria appeared very broad, offering significant discretion to local government officers leading to wide variations in interpretation, delays and long back-logs of appeals.

²⁷ There are also non-financial services required to help the poor develop new skills and access markets so that they can put microfinance to good use. There may also be problems accessing credit for those who are not already members of revolving credit societies.

²⁸ According to the IPS-TS 2005 data (collected in April/May 2005), all surveyed GNDs had received the funds of Rs. 15,000 for deaths, Rs. 2500 for kitchen equipment and Rs. 5000 livelihood grant and food/cash coupon.

Interviews with relevant stakeholders, including both affected families and government officials, suggested that households having access to 'regular income' were no longer eligible. It took several months to draw up new lists of those eligible to receive the grant with the number of recipients eligible for the third payment declining by 25 per cent to 165,000 and the fourth round deemed to be still 'on-going' as of December 2005 (GOSL, 2005a).

The grant scheme seems to have proved very effective in reaching most of the affected population, assisting people with little engagement in the formal financial sector even to start deposits (which were mandatory to receive funds). While it may seem equitable to narrow the scope of the grant so that it targets the 'truly needy', in practice the costs of such narrow targeting may well exceed benefits. The over-emphasis on targeting appears somewhat shortsighted in view of the fact that Sri Lanka's national poverty alleviation programme (Samurdhi) is estimated to have a leakage of 40 per cent.

In assessing the changes to this programme, it should be noted that even households with a 'regular' post tsunami income have suffered a major loss of wealth in terms of property and possessions and are cash strapped. The chances of them slipping into the pitfalls of high interest informal sector borrowings to meet many pressing needs are high. Perhaps most critically, any decision to take recipients with a regular income off the list after only two monthly payments generates perverse incentives, effectively penalizing not only those who have held on to previous jobs, but perhaps even more importantly, those who have managed to obtain regular employment after the tsunami. If donor assistance is available for this programme – and it is hard to see why funds are not available going by the May 2005 pledges are being honoured – given the obvious need to provide affected households with some income, cutbacks are hard to justify. Moreover, since bank accounts have been opened for the cash grant transfer, the system is extremely cost effective compared to the high transactions costs of many other tsunami livelihood projects which often incur as much as 30 per cent administrative overhead costs.

Overall, the household and the community level perceptions on income recovery are at variance. The IPS-TS 2006 household level data show that on average close to 60 per cent of households feel that their family incomes are worse compared to pre-tsunami levels in terms of their ability to cover basic needs such as food and health. On the other hand, according to the community level key informants, almost all surveyed GNDs in the Southern Province and close to a half of the surveyed GNDs in the Eastern Province are better off now because of aid, training, and more employment opportunities.

Clearly, there appears to be regional variations in income recovery patterns. Compared to the Southern Province, a higher per cent of households in the Eastern Province feel that their livelihoods have not recovered back to their pre-tsunami levels.²⁹ According to the IPS-TS 2006 data – in both Southern and Eastern provinces – improper distribution of livelihood related assets, the implementation of the buffer zone rule and damages to work places have affected livelihood recovery. In addition to these, inability to participate in training due to security reasons has also slowed down livelihood recovery in the Eastern Province.

5.1.4 Other: Trauma and Stress

The IPS-TS 2006 results indicate some evidence of mental and physical health problems related to the tsunami. A few households reported experiencing more sleeping difficulties, and children having nightmares compared to pre-tsunami levels. About 11 per cent of the households knew of someone committing suicide because of the tsunami. A large number of households – 33 per cent of households in the sample – have been offered or given counselling for distress. The percentage of people who received counselling is comparably higher in the Eastern Province. It is possible that there were already counselling taking place in these areas for victims of conflict related mental health problems.

In addition, a large number of households have stated that some member of the household had experienced deterioration of physical health after tsunami. About 12 per cent of households stated having physically ill or injured members following the tsunami. Of these, 77 per cent claimed that their income earning capacity and/or day-to-day activities was affected by this physical disability.

Nearly 40 per cent of households claimed having children who are yet to restart schooling after the tsunami. This problem was only slightly more pronounced in the conflict affected Eastern Province, indicating that the main reason for school non-restart is not the conflict. Anecdotal evidence provided by field offices indicates that one reason for school non-participation is the receipt of livelihood related assets in excess. In addition to low school participation, around 31 per cent of the households have found that children's performance at schools has declined after the tsunami.

²⁹ The income recovery patterns across GNDs are mixed. In some GNDs more than a half of the people have recovered their livelihoods to the pre-tsunami levels or more, while in most GNDs less than a half have recovered their livelihoods.

5.2 Assistance

At the first Sri Lanka Development Forum held in May 2005, US\$ 3.3 billion was pledged by multilateral and bilateral donors and NGOs for post-tsunami recovery activities (MFP, 2005).³⁰ Of this, loans amounted to US\$ 798 million and the balance to be in grants. NGOs pledged a total of US\$ 853 million on a grant basis. The total assistance provided by the IMF included US\$ 268 million by way of both emergency relief and debt moratorium. Bilateral donors extended a debt moratorium providing relief of US\$ 263 million.

Of total pledges of US\$ 2.8 billion (which excludes debt relief), firm commitments of around US\$ 2.2 billion is reported to have been made (GOSL, 2005a). In addition, an estimated US\$ 150 million was received as contributions from domestic resources (this total does not include relief disbursements for which figures are not available).

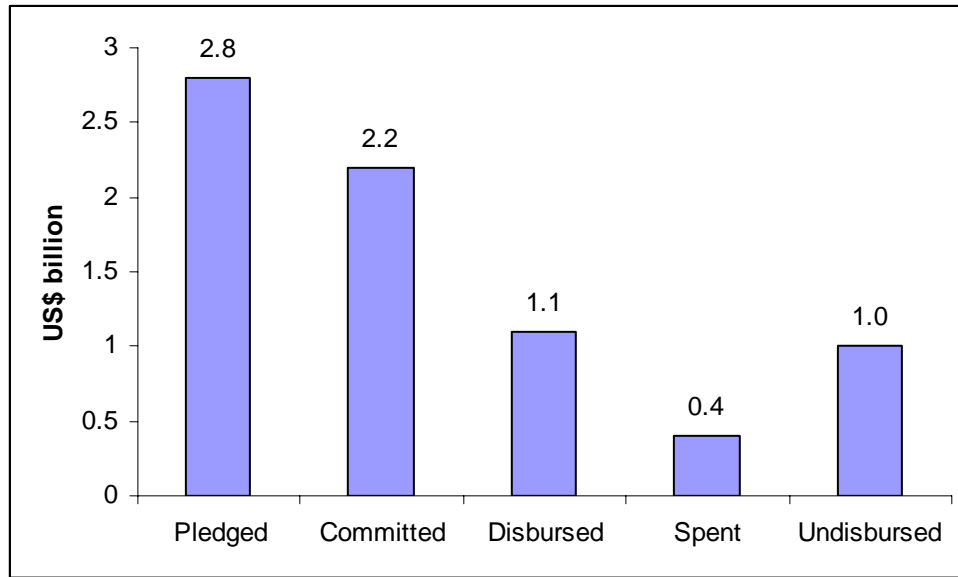
While there seems to be some consensus that foreign resources committed stand at US\$ 2.2 billion, the exact amount of aid disbursed and expended is not clear. By end 2005, government sources suggest that the total foreign resource available for tsunami related rehabilitation and reconstruction programmes amounted to US\$ 1795 (MFP, 2005).³¹ While GOSL (2005a) disbursement figures for 2005 are given as US\$ 600 million, actual expenditure figures are not available. According to figures released by the World Bank as of April 2006, out of US\$ 2.8 billion pledges, US\$ 2.2 billion has been committed, US\$ 1.1 billion has been disbursed and only US\$ 425 million has been spent.³² This appears to be the most likely given that the committed undisbursed balance of foreign aid for post-tsunami reconstruction at end April 2006 is said to be US\$ 960 million (MFP, 2006).

³⁰ The US\$ 3.3 billion includes debt relief/moratorium and IMF support.

³¹ The figure quoted is US\$ 1765 million by mid-2006 (see MFP, 2006).

³² <http://web.worldbank.org/WBSITE/EXTERNAL/COUNTRIES/EXTTSUNAMI>

Figure 2: Status of Recovery Funding



Source: WB and GOSL.

Data available from the Development Assistance Database (DAD) maintained by RADA suggest that as at end August 2006 about US\$ 815 million has been spent.³³ While lack of transparent and consistent data on aid expenditure is a serious concern, the available information does point to the irrefutable conclusion that actual expenditure has been very poor.

Table 16: Total Aid by Funding Agency (US\$ mn)

	No. of Projects	Committed	Disbursed	Expended
Bilaterals	404	1084	608	281
Multilaterals/IFs	55	687	393	358
UN	36	142	125	37
International organizations	30	208	47	47
INGOs	215	302	154	86
NGOs	5	17	7	2
Private sector/funds	47	5	2	3
To be specified	32	20	4	...
Total	761	2467	1342	815

Source: RADA DAD database.

As previously mentioned, the slow progress in housing has been partly blamed on the failure of NGOs to deliver on promises made. The disbursement of funds received by NGOs for post-tsunami reconstruction has also come under scrutiny. A survey carried

³³ The DAD maintained by RADA allows stakeholders to input data and may therefore not be entirely accurate.

out by the Central Bank of Sri Lanka (CBSL) of all bank transactions of NGOs (local and foreign) for the year 2005 found that an estimated 256 NGOs received donations and other funds amounting to Rs. 40 billion (US\$ 400 million) by way of credits to their bank accounts from various foreign and local sources during 2005.³⁴ It was further revealed that nearly 80 per cent of funds received in the bank accounts of all NGOs during 2005 had been withdrawn. As stated earlier, the IPS-TS 2006 results also indicate that delays in donor assistance to be a main reason for the slow progress of the donor driven housing programme. On the positive side, the IPS-TS results show only low levels of corruption at the household level. Very few households had paid bribes to government or NGO officials to receive aid and only 14 households knew of instances where politicians have interfered with the tsunami recovery efforts.

But even if all committed funds are made available, there may still be a problem of utilizing the aid. As far as the ability to utilize aid is concerned, Sri Lanka's past performance raises serious concerns. The rate of aid utilization was low at around 13-15 per cent towards the end of the 1990s before seeing a gradual improvement to a more respectable rate of around 20-22 per cent, though the cumulative undisbursed balance (CUB) has remained stubbornly in the region of US\$ 2.5-3 billion. Many reasons have been cited for the low levels of aid utilization: political interference with regard to planning, implementation and allocation of funds; staffing and related problems in project management; implementation delays (including infrastructure bottlenecks, complex and costly procurement procedures), and excessive conditionality imposed by donors have been viewed as the key constraints. Availability of counterpart funds (local funds with appropriation) has also been an important factor.

The total aid commitment to Sri Lanka in 2005 is estimated at US\$ 1.7 billion – the highest annual commitment in any one single year primarily as a result of the tsunami related inflows (MFP, 2005). Past failures are of course not necessarily a guide to what may happen in the current situation. But they do provide a warning that, unless there is a concerted effort to meet targets and maintain focus, the potential for domestic slippage is ever present.

5.3 Delivery of Assistance

A key issue has been the coordination of the relief and reconstruction effort. In Sri Lanka coordination is required across three groups. First, activities among the various components of the government require coordination – both across sectors and between central and local government. Second, the activities of various agencies and NGOs – with the heavy post-tsunami influx some 180 have been operating in Sri Lanka –

³⁴ CBSL press release, 20 March 2006. Nearly three-quarter of the funds had been received by a handful of 30 NGOs.

require coordination. Third, coordination is required with the LTTE which controls part of the country that was heavily affected by the tsunami.

As mentioned previously, the government set up a Centre for National Operations (CNO) and three task forces. The lead agency to oversee the recovery and reconstruction phase thereafter fell on TAFREN.³⁵ While an overarching authority such as TAFREN was a sensible option to coordinate post-disaster reconstruction, TAFREN itself lacked links to line ministries in its representation (dominated as it was by private sector representation), which hampered its ability to efficiently coordinate activities among government agencies. The division of reconstruction into sectors – such as housing and water and sanitation – in turn raised coordination issues to ensure, for example, that housing units constructed get access to the necessary water, sanitation and electricity provisions. TAFREN was seen to be increasingly attempting to monitor the line agencies and be a ‘one-stop-shop’ but its role and ability to achieve this goal remained somewhat unclear.

In November 2005, a decision was taken to amalgamate TAFREN, TAFOR and TAFLOL into a Reconstruction and Development Authority (RADA) by an Act of Parliament. While the Bill to establish RADA gives it vast powers, it is not clear as to whom RADA will be accountable: the

Parliament or the President. Though the gazette mentions that RADA will be a statutory institution within the Ministry of Nation Building and Development of which the portfolio of the minister responsible is the President himself, the Bill does not state this. This is considered to be major omission as RADA is vested with wide powers in reconstruction and development. In the event that RADA is under the President then, any orders or actions carried out by the President for RADA will carry presidential immunity with it.³⁶ However, if the actions are carried out by a minister (even if the portfolio is with the President) then they do not carry the Presidential immunity and legal action can be taken if required. Under the Bill, RADA also has vast powers over organizations working on reconstruction and development to monitor and control their activities as well as to issue licences for carrying out these activities. It can not only reduce the powers of existing actors but could also reduce the flexibility and space required for reconstruction and development. There is thus some concern that Sri Lanka’s

³⁵ After one month, with the conclusion of immediate relief operations TAFREN and TAFLOL were amalgamated to a single entity – the Task Force for Relief (TAFOR) – to implement all relief measures, and operations of the CNO were scaled down. In February, the CNO was dissolved and officials returned to line ministries. TAFOR and TAFREN took over the responsibilities of the CNO. With the completion of transitional housing, TAFOR was expected to wind down operations and its responsibilities passed to the line ministries.

³⁶ For instance, in acquisition of land in the ‘national interest’.

reconstruction effort is too centrally driven with limited input from local level actors and line ministries.

The second group whose activities need coordination involves the donor community. Sri Lanka has long experience working with major donor agencies and several INGOs have long established operations in the country. There had been some welcome moves towards donor coordination even prior to the tsunami in the context of its conflict-related donor reconstruction programmes. Thus, the World Bank, ADB and JBIC had already established a partnership that enabled the basis for the very useful needs assessment to be done immediately after the tsunami. However, coordination with donor agencies and NGOs became a vastly more complicated issue due to the numbers and practices of the numerous international NGOs (not counting large numbers of individuals and small groups) who came in after the tsunami.

Field observations suggest that lack of coordination has led to considerable maldistribution of aid, clearly visible for example in the distribution of boats in the fisheries sector as mentioned previously. A report released by the Auditor General in looking at rebuilding houses identifies deficiencies in the payment of large sums even for houses with minor damages (e.g. Rs. 100,000 paid for minor damages amounting to Rs. 10,000) and payments made without identifying the value of the damaged houses.³⁷ Provision of houses by some NGOs to 26 families who were not affected, approval of grants out of governmental financial assistance for 5 houses which have been fully constructed by NGOs, payments made to undamaged houses, etc., indicative primarily of a serious lack of coordination amongst those providing relief. As discussed previously, the ground situation on housing is at variance with the government's policy on housing, indicating problems with coordination and monitoring. Also, as mentioned earlier, reluctance of some non-governmental agents, operating independently, even to share beneficiary lists have further complicated the problems of coordination.

Some of the NGOs – both INGOs and domestic NGOs who receive external funds – control significant amounts of money. With their own funding secure, they face few incentives to improve coordination. In fact, some are openly hostile to any government action that seems to place 'controls' on their independence. NGOs vary widely in experience, skills and operating styles. Many NGOs lack experience and local knowledge, and in their haste to spend monies disregard local circumstances and community needs. According to the IPS-TS 2006 results, about 17 per cent of households reported 'bad experiences' with NGO officials, compared to 4 per cent

³⁷ The report on the rehabilitation of losses and damages that was caused by the tsunami covers the period 26 December 2004 to 30 June 2005. See GOSL (2005b).

and 11 per cent of households reporting 'bad experiences' with central and local level government officials, respectively.

Further, the presence of large numbers of donors/NGOs has at times led to competitive behaviour. Deep mistrust has developed in several locations between local NGOs (who have often been working in the area for many years) and some INGOs and agencies who have come for tsunami assistance. Sri Lankan NGOs claim to have been 'crowded out' by some of the better financially endowed larger INGOs, who have 'poached' staff and resources. Certainly some INGOs and agencies have greater expertise in large scale disaster relief (such as provision of transitional shelters and other relief measures), but domestic NGOs (and INGOs that have operated in Sri Lanka for a long period) usually have a much greater appreciation of local conditions and sensitivities. Greater interaction, engagement and coordination between them would benefit the overall relief and reconstruction effort. While mechanisms have been set in place to better coordinate donor activities, including NGOs, at regional and local levels through regular meetings and consultations held by regional administrative officers, it is too early to judge their overall effectiveness. From the perspective of the households, IPS-TS 2006 results show mixed reactions to the effectiveness of assistance by international and local NGOs. About 44 per cent of the households surveyed have felt that INGOs were more effective in delivering aid, while 11 per cent felt that the local NGOs were more effective. About 15 per cent of households felt that there is not much of a difference between local and international NGOs.

The third group with whom activities need to be coordinated is the LTTE. This has been the most difficult and contentious issue. While discussions to establish a mechanism for aid sharing began soon after the tsunami, a mutually acceptable arrangement for aid sharing to enable assistance to flow into the LTTE controlled areas proved elusive. On the one hand, sections within the government and many majority community groups have been opposed to any deal that appears to provide *de facto* recognition to the LTTE as the administrative power in regions controlled by them. On the other hand, the LTTE has been unwilling to accept an arrangement that dilutes their powers. After long drawn out negotiations, a MOU setting out an aid-sharing deal between the GOSL and the LTTE, the Post Tsunami Operation Management Structure (P-TOMS), was signed in June 2005.³⁸

However, this agreement promptly ran into opposition and was challenged in the courts through a fundamental rights petition. The Supreme Court ruled in July 2005 that

³⁸ This was designed as a mechanism to distribute aid in LTTE-controlled areas in the Northern and Eastern Provinces of the country. The P-TOMS agreement envisaged the setting up of a Regional Fund to allow donors to channel tsunami funds directly to the Northern and Eastern Provinces. A multilateral agency (anticipated to be the World Bank) was to be appointed as the custodian.

it was constitutional but certain elements were put on hold by the Supreme Court pending clarification.³⁹ In addition, many of the major donors who had supported the idea of a joint mechanism for aid distribution between the GOSL and the LTTE declined to channel aid directly to the Regional Fund once the MOU was signed claiming that the LTTE remains a 'proscribed terrorist organization' in their countries. After the presidential election in November 2005, with the election of a new President who publicly opposed the agreement, P-TOMS is no longer on the policy agenda. In fact, from December 2005, Sri Lanka has witnessed an intensification of the conflict between the GOSL and the LTTE. Renewed violence has disrupted not only the lives of the tsunami affected people in the area, but a sharp increase in internally displaced is placing pressure on aid agencies to provide relief in addition to the tsunami rehabilitation work.

5.4 Cost Escalation

The funds needed for rebuilding houses and other construction activities, including public infrastructure, were initially estimated on the basis of costs and prices that prevailed immediately after the tsunami disaster. However, there is now clear evidence that construction costs have been rising rapidly over time. This is of course not surprising. The scale of construction that was envisaged was several times higher than what is done in a normal year, with dramatic increases in demand for labour and materials.⁴⁰ Data obtained from companies and organizations involved in house building and IPS field interviews indicated that *total* construction costs for the planned houses for tsunami affected families had already risen by 30-50 per cent by August 2005 (Table 17). The latest figures for September 2006 indicate cost increases from the initial estimates to be as high as 60-80 per cent.

³⁹ Specifically the Regional Fund and the location of the regional committee in the rebel held Kilinochchi.

⁴⁰ Estimates of the extra demand for house construction vary, but they all indicate a massive increase in demand for scarce construction labour and materials. According to the Chamber of Construction Industry as reported the *Daily Mirror*, February 21, 2005, it was estimated that at least 100,000 additional workers will be required; this includes about 13,000 masons, 2000 carpenters, 2500 painters and nearly 54,000 unskilled labourers.

Figure 3: Price Indices for Labour Wages



Source: ICTA, June 2006.

Field interviews that indicated that these increases are driven primarily by higher wages for skilled labour (such as carpenters, painters and masons) whose wages have doubled in some locations are substantiated by data provided by the Institute for Construction Training and Development (ICTA).⁴¹ Labour wages in particular increased sharply immediately following the tsunami disaster and then again towards the end of 2005 (Figure 3).

Table 17: Cost Escalation in Housing Construction

Donor	Unit Area (sq. ft.)	Initial Estimate (Rs.)	August 2005		September 2006	
			Estimate (Rs.)	Comments	Estimate (Rs.)	Comments
Red Cross ^a	600	625,000 (March)	1,000,000	Houses with all basic infrastructure facilities (electricity, water supply, sanitation for each house, roads, etc.).	1,250,- 1,300,000	Cost per housing unit with a tiled roof, basic infrastructure. Price escalation since last year is about 22% due to increase in prices of factors like fuel and labour.
CARE International	550	450,000 (March)	850,000 600,000 550,000 – 650,000	Jaffna Hambantota All other areas (houses with few basic infrastructure)	700- 800,000	This is the average. However, the value differs from district to district.

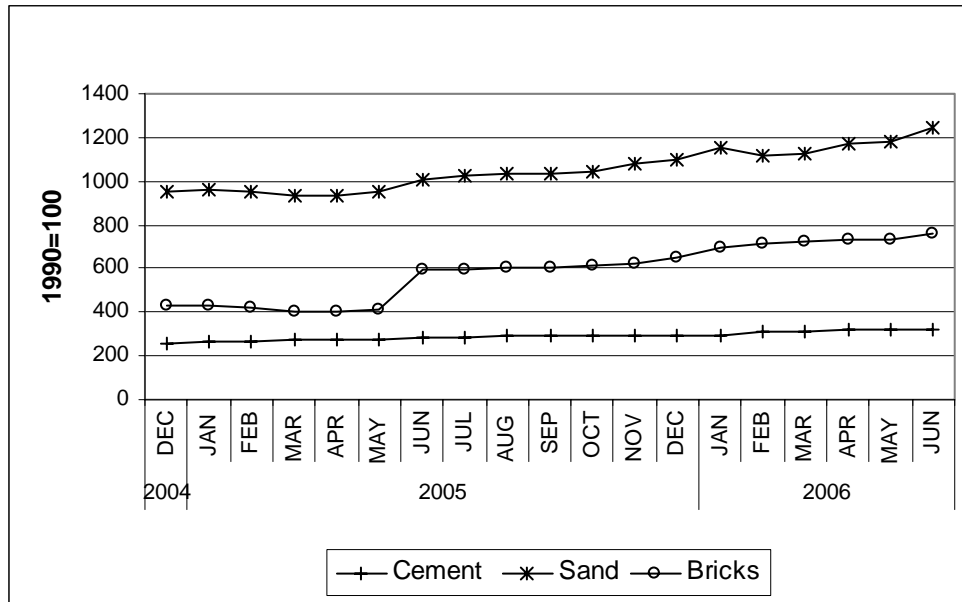
⁴¹ Organizations involved in tsunami housing construction are required to use ICTA registered contractors.

Aitken Spence Co. Ltd. ^b	550	450,000 (March)	> 500,000	With basic infrastructure (with electricity but no water supply)	550,000 (Sep.2005)	A basic housing unit
World Vision Lanka ^c	500	550,000 (March)	700,000	With basic infrastructure	750-800,000	With basic infrastructure
CARITAS Sri Lanka	500	500,000 (May)	650,000	A basic house (no mention of infrastructure)	800,000	A basic housing unit only
Sarvodaya Movement ^d	500	500,000 (May)	650,000	With only a few basic infrastructure facilities	600,000 700,000	South North and East The cost of a basic housing unit only
Forut Institute	550	500,000 (April)	550,000	Only for the house (not with basic infrastructure)	700-900,000 800,000	North With basic infrastructure With basic infrastructure

Notes: a: Estimates said to be costlier because of higher specifications (e.g., use only imported timber); b: Has currently completed its housing reconstruction. Estimate for September 2005; c: Initial estimates based on 500 sq ft. New estimates on 515-550 sq. ft.; d: Initial estimates based on 500 sq ft. New estimates on 540 sq. ft.

Source: IPS surveys.

Figure 4: Prices of Building Raw Materials

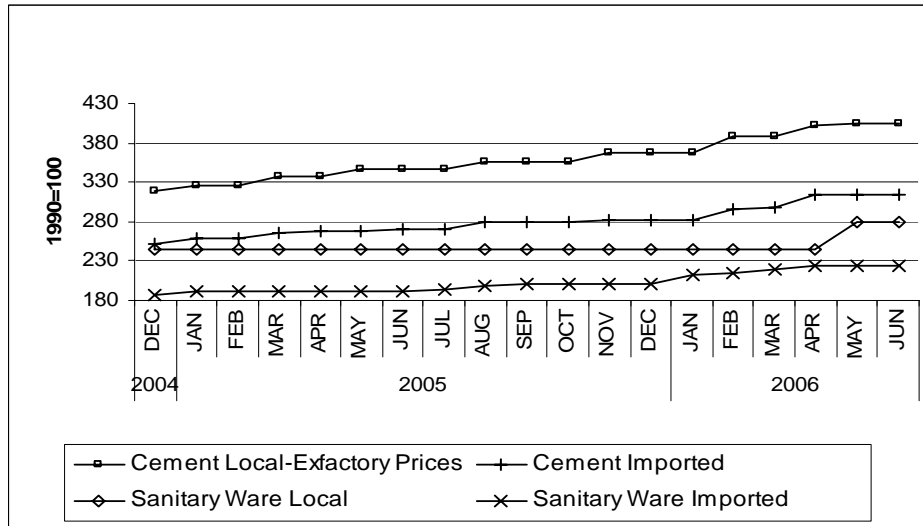


Source: ICTA, June 2006.

Costs have also increased for particular building materials. Construction materials such as cement, sand and bricks have seen a sharp increase in price over time (Figure 4). It should also be noted that price increases for importable materials have been significantly lower than overall construction cost increases (Figure 5). The IPS-TS 2006 survey results verify these findings. As mentioned earlier, more than three-fourths of the surveyed key informants were of the view that wages of carpenters and masons and prices of building materials have increased 'a lot' since the tsunami.

Cost escalation adds to the problem that may already exist in turning pledges into commitments. It should be noted that a third of the pledges made at the donor meeting in May 2005 came from non-governmental sources, whose own sources of funding are not always firm. As already discussed, there are indications of problems with instances of some NGOs that had signed MOUs having failed to even commence work in housing reconstruction. Thus, significant funding gaps may be opening up that holds serious implications for the management of macroeconomic policy.

Figure 5: Imported and Local Price of Building Material



Source: ICTA, June 2006.

5.4 Broader Economic Impacts

The typical pattern for economies struck by unanticipated natural disasters is for a brief deceleration in growth, followed by a rebound as a result of the stimulative effect of reconstruction. GDP growth in fact saw a strong resurgence in 2005 after an initial dip in the first quarter. Predictably the fisheries and hotels and restaurants sub-sectors saw a sharp contraction in output while the construction sub-sector has experienced stronger growth (Table 17). The recovery nevertheless has been better than anticipated; it has been broad based, driven by continued expansion in industry and services as well as a recovery in agriculture following improved weather conditions. With strong output expansion continuing into 2006 (with growth in the first half estimated at 8 per cent with an overall growth forecast of 7 per cent for the year), Sri Lankan economy is likely to see one of its strongest performances ever.

Table 17: GDP Estimates

	Annual		First Half	
	2004	2005	2005	2006
Agriculture	-0.3	1.5	-1.5	7.1
Fishing	1.6	-42.2	-61.1	108.0
Industry	5.2	8.3	8.2	6.1
Construction	6.6	8.9	7.0	7.5
Services	7.6	6.4	6.1	9.1
Hotels & restaurants	13.1	-29.0	-26.0	24.1
GDP	5.4	6.0	5.3	8.0

Source: Central Bank of Sri Lanka, *Annual Report 2005*; Quarterly GDP Estimates (press release).

The tsunami reconstruction undoubtedly brightened prospects for Sri Lanka's short term economic outlook. Total investment/GDP ratio increased by 1.5 percentage points in 2005, much of it driven by government investment. In fact, the investment ratio improved to 29.2 per cent in the first half of 2006 from 25.2 per cent in the same period in 2005 reflected in higher imports of investment goods and construction activities. However, despite improved growth prospects, the underlying structural imbalances in the economy have continued to intensify over time. The most significant has been developments on the fiscal front. Budgetary estimates for 2005-06 were revised following the increased demands on expenditure for tsunami relief and reconstruction and the forecast deficit for 2006 is estimated to be over 9 per cent of GDP.

Table 18: Post Tsunami Fiscal Outlook

(As % of GDP)	2004	2005			2006
	Actual	Approved	Revised	Actual	Approved
Revenue	15.4	17.1	16.5	16.1	17.8
Expenditure	23.5	24.6	24.7	24.7	26.9
Current	19.2	18.4	18.4	18.7	18.7
Tsunami			0.5	0.4	0.1
Capital	4.3	6.2	6.3	6.0	8.2
Tsunami			0.9	1.0	1.7
Fiscal deficit	-8.2	-7.5	-8.2	-8.7	-9.1
Financing					
Foreign loans	1.8	2.1	2.6	2.0	3.0
Foreign grants	0.4	0.4	0.8	1.4	1.6
Domestic	5.8	4.6	4.5	5.2	4.5

Source: Central Bank of Sri Lanka, *Annual Report 2005*.

While the additional tsunami related expenditure is budgeted to be met by foreign grants, financing needs are likely to be much greater for the reconstruction – with cost escalation as well as the increase in numbers of housing units required – even assuming that all commitments are made good. Despite added fiscal pressures, little effort has been expended to curtail spending in other areas, fuelling inflationary pressures from policies unrelated to tsunami reconstruction.⁴²

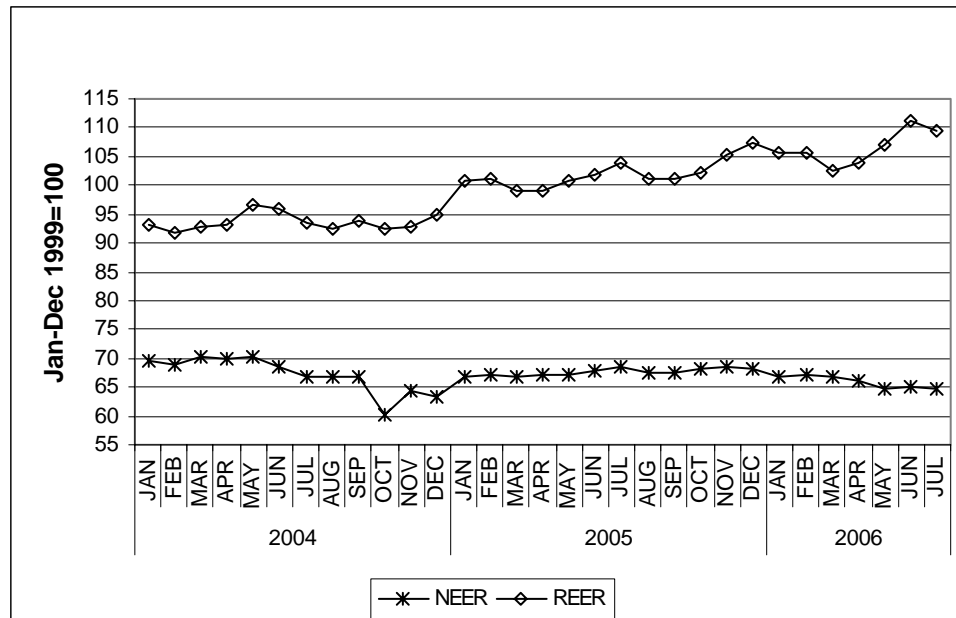
Fiscal profligacy in the face of higher spending on tsunami related rehabilitation combined to ignite significant inflationary pressure in the economy. The initial

⁴² For example, adding workers to the government pay-roll has seen payments on salaries and wages increased from 5.2 per cent of GDP in 2004 to 5.9 per cent of GDP in 2005; transfers and subsidies over time have increased from 4 per cent of GDP in 2003 to 5.4 per cent of GDP in 2005.

response to rising inflationary pressure was slow. Policy rates remained unchanged for 6 months from November 2004 allowing credit growth to expand at a rate of over 20 per cent. Growth in broad money has remained high at around 18-20 per cent in the first half of 2006. The rate of inflation which stood at 11.6 per cent in 2005 is expected to remain above 12 per cent in 2006.

Given the understandable community sensitivity to rising inflation, there are political imperatives to resist exchange rate depreciation and there is some evidence to suggest that the nominal exchange rate may have been propped up by the tsunami related capital inflows. Sri Lanka managed to record an overall surplus of US\$ 500 million on the BOP as against a deficit of US\$ 205 million in 2004 with official reserves also seeing a sharp improvement.

Figure 6: Nominal and Real Effective Exchange Rate



Notes: The NEER and REER are based on trade composition with 24 trading partners.

Source: Central Bank of Sri Lanka (www.centralbanklanka.org)

The influx of increased foreign capital reversed a sharp devaluation of the rupee vis-à-vis the US dollar at end 2004,⁴³ leading to a nominal appreciation of over 5.5 per cent in the week following the disaster. The nominal effective exchange rate (NEER) appreciated by 7.7 per cent in 2005 (compared to a depreciation of 11

⁴³ The currency depreciated to Rs. 105.47 per US dollar on 17 December, 2004 – the highest rate in the interbank market. It had appreciated to Rs. 98.11 by 12 January, 2005. The appreciation of the rupee for the rest of the year was also partly influenced by the movement of major currencies as the US dollar appreciated against them.

per cent in 2004). The higher nominal appreciation and relatively high domestic inflation saw the real effective exchange rate (REER) appreciate significantly by 12.7 per cent (as against a depreciation of 1.1 per cent in 2004). The real appreciation no doubt held adverse implications for the external competitiveness of Sri Lanka's exports.

As the tsunami related capital inflows ease, the government appears to be increasingly looking to raise foreign loans for budgetary support, forecast to increase from 1.8 per cent of GDP in 2004 to 3 per cent of GDP in 2006 to bridge some of the budgetary financing gap. Sri Lanka went in for a sovereign rating in December 2005 as the first step to raising an estimated US\$ 0.5-1 billion through the international bond market. Sri Lanka was assigned a BB- (below investment grade) and a B+ by two rating agencies, and with the escalation in hostilities the credit outlook was downgraded from stable to negative at end April 2006. Despite the inherent risks in increasing exposure to foreign borrowing, as of August 2006, the government had already issued nearly US\$ 500 million Sri Lanka Development Bonds (SLDBs). Overall, the emerging macroeconomic environment raises serious concerns about the sustainability of the country's post-tsunami burst of GDP growth.

5.6 Social Cohesion

The targeting on tsunami affected households often required due to funding constraints, inevitably created conflicts with other unaffected but still poor households in the area. While physical capital was being rapidly replaced, it was done in ways that in instances undermined the social capital of an area by exacerbating existing tensions and rivalries. The IPS-TS 2006 community level data shows conflicts with regard to allocation of new houses, distribution of funds, and allocation of livelihood related assets.⁴⁴ On the positive side, however, most GNs were of the view that almost all conflicts were amicably resolved through discussions with relevant parties.

In some places, tension has grown between fishers and other livelihood groups because the latter feel that the fishing industry has received greater attention. Similar community tensions have emerged in the housing sector where the government in its revised housing policy was forced to lay down specific standards for housing given evidence of significant cost variation in donor built houses. Another source of conflict is that between the tsunami affected and those already displaced by the two decade long conflict in the north and east

⁴⁴ The level and nature of conflicts vary across GNDs, with some GNDs reporting no conflicts while others report all types of conflicts.

of the country. There is a clear need to understand the local situation in order for interventions not to exacerbate existing tensions and conflict. The IPS-TS 2006 data indicate that there were more tsunami aid distribution related tensions in the conflict-affected Eastern Province as compared to the Southern Province.

The spontaneous solidarity that united communities immediately after tsunami rekindled hopes that the ethnic divisions that have cost the country so dearly in recent years may finally be waning. However, the North and East has seen an escalation in hostilities between the GOSL and the LTTE since December 2005 that will further complicate tsunami reconstruction efforts in these parts of the country.

IPS-TS 2006 provides some evidence that drunkenness and smoking has increased due to lack of productive employment and access to cash, which in some cases has led to increased family disputes.

6. Overall Assessment and Discussion

The overall experience of the tsunami has been unique in that a large amount of aid by many organizations in a very short a time led to rapid relief and initiation of reconstruction, but also caused problems – in most disasters in other countries lack of aid is the key issue. Also, more so than in other instances, aid flowed through individual, private and NGO hands instead of via donor agencies or the UN. The type of aid delivery agencies and unusual amount of aid, created some unique challenges:

- Problems of absorptive capacity by government and households
- Many organizations providing aid leading to very high transaction costs
- Rising demand for labour and raw materials causing cost escalation
- Excessive focus on quantity of aid disbursement that undermined effectiveness of aid (e.g., mal-distribution, poor quality fishing boats, etc.)
- Problems of lack of capacity at the local levels to provide information to properly coordinate and monitor aid distribution (more attention was given to setting-up institutions at the centre)
- Problems with coordinating and monitoring due to the lack of a clear and transparent means of sharing information between various governmental and non-governmental agents distributing aid
- Problems with conflicts due to lack of compatibility between assistance provided to conflict affected households and tsunami affected households in the same area.

Some problems highlighted at the start and during the recovery process have been exaggerated and dealt with well. For example:

- Corruption on a grand scale has not been a major issue, perhaps due to the fact that the reconstruction did not involve large scale infrastructure projects that are typically associated with significant levels of corruption. Most corruption identified has been petty corruption by officials in terms of discretionary decisions (e.g., determining fully versus partially damaged house, etc.). In petty corruption, disciplinary action has been taken in a number of cases by the government.
- Concern that asset distribution is not fair (e.g., non fishers getting boats) is being partly solved by the secondary market for these goods.
- Micro credit providers improved cooperation and coordination of rules of the game to try to maintain the micro credit culture that the post-tsunami surplus of micro credit funds at low interest rates was in danger of undermining.
- The government ensured that new food purchases by the World Food Programme (WFP) were from bumper domestic harvests – and not imports – to help farmers recover and maintain rural incomes.
- Establishment of dispute resolution mechanisms from the start for aid delivered through government channels appears to have minimized long-term conflicts related to aid distribution.

Nevertheless, other new problems have become dominant factors nearing the second year of reconstruction, including renewed conflict in the north and east of Sri Lanka. The North and East was already the area most affected by the tsunami, and renewed signs of conflict brought reconstruction largely to a halt and led to many new refugees. Indeed, the regional disparities of the country have been increased by post-tsunami reconstruction. There is evidence, particularly in the Southern Province that many poorer households are physically and financially better off than pre-tsunami. This holds true in a few places in the East, but generally slower progress in the East especially following the resumption of the conflict have increased disparities between the south and the north and east of the country.

The rehabilitation and reconstruction phase has also raised broader issues that require attention including the question of whether assistance should be in cash or kind. Relief in the form of cash payments did seem important, although attempts to target them may have been counter-productive. Assets rather than cash have led to many instances of mal-distribution where wrong people have

got the assets (e.g., non boat owners). However, given that assets can easily be sold, the difference may not matter so much. One problem with assets rather than cash is it can lead to substandard goods which do not meet consumer preferences. For example, instances of boats of poor quality and many houses not always designed as new owners would like them to be. However, it could also be argued that tsunami affected households may have lacked skills and economies of scale to produce these assets any better.

Another issue is whether assistance should be targeted to the vulnerable or provided to all, and when to move from tsunami affected households only. Much of the focus has been on beneficiary lists drawn up by government agencies. This seems to be a very inefficient, corruption prone process. There is a need to create a system whereby only affected households have incentives to declare themselves affected. Local level peer monitoring can also be used as with housing damage verification teams. Under World Bank guidance when preparing beneficiaries for housing, credible attempts were made to make the process transparent. Draft versions of beneficiary lists were posted in public places and affected households were given the opportunity to contest these lists. Village level rehabilitation committees were also established to assess housing damage, and for the purposes of dispute resolution. However, anecdotal evidence suggests some implementation problems with these safeguard measures. For example, local level peer monitoring worked better in rural settings, where communities are cohesive and community groups are present. In urban areas, these were less effective. Although dispute resolution mechanisms were put in place, inconsistencies and inadequacies in regulations and lack of decision making power given to local level authorities prolonged the resolution of some grievances – e.g., the eligibility of households in rented houses to receive benefits. There is also a need for some contribution in kind by tsunami affected households – e.g., employing cash for work at below the going labour rates or requiring some contribution in kind to housing and boat assets.

On targeting within tsunami affected households, an initial cash grant was given to all households – with some leakage – estimated by some to be about 25 per cent. However, Sri Lanka's poverty alleviation programme (Sumurdhi) is estimated to have a leakage of 40 per cent. Thus, the tsunami targeting is much more impressive given the rapid time frame that was involved. The later decision to focus the cash grant on households whose incomes were very low (e.g., excluding government servants) seem to have been counter-productive leading to delayed payments, high transaction costs, incentives for corruption and

inconsistent treatment and much anger and resentment from tsunami affected households.

A third issue on targeting is that once the initial relief and assets recovery takes place, there is a need to move on to broader economic development. For this, the focus can no longer be limited to tsunami affected household only, but must be aimed at developing broader geographic locations or particularly affected economic sectors.

Another key issue is the effectiveness of central government versus local decision-making. Making decisions in disasters requires a complex balance of roles between the central government and the locally affected areas. The central government can provide a clear policy framework and national standards, and a one-stop-shop for initial planning and funding and monitoring of local level recovery efforts. The central government must be responsive to the concerns and feedback raised by the local level. The local government can often be most effective at local decision-making and implementation.

Sri Lanka tended to have an overly centralized focus – with some concerns that local government was not given enough freedom to take decisions and implement – and their concerns about some of the shortcomings were not heeded early enough (e.g., lack of land for buffer zone, concerns with new criteria for cash grant, etc.). Also, the central government rushed to establish new institutions specifically to deal with tsunami related aid distribution, ignoring existing institutions. At the same time, sufficient attention was not given to building capacity at the local levels. This led to duplication of work that resulted in increasing the administrative workload of already under resourced local level players, reducing the efficiency of aid distribution.

7. Conclusions

Our review of Sri Lanka's experience with the tsunami and its aftermath has highlighted several short term as well as longer term issues in managing the challenges posed by a massive reconstruction effort after a natural disaster. Making available immediate relief, including cash grants, is a pre-requisite assist in the recovery process. Temporary cash grants are typically quite modest in the context of the quantum of donor assistance made available. In the case of Sri Lanka, almost as soon as the scheme of making available cash grants to all affected families got underway, concerns were expressed over targeting. Bureaucratic delays in revising lists of beneficiaries led to interruptions to

disbursement as well as to creating perverse incentives where the costs of narrow targeting may very well have exceeded the benefits.

Another key issue has been the coordination of the relief and reconstruction effort. First of all, the absence of clear decision-making has compounded the costs, contributed to delays and caused further hardships to affected households. Changes in policy – for example with regard to buffer-zone related housing issues and disbursement of cash grants – have not been fully transparent. Nor have subsequent revisions been clearly conveyed to affected households in order to inform them of their entitlements. The early decision to impose a ‘no-build’ buffer zone and subsequent revisions have also held up the progress of housing reconstruction and led to mal-distribution of housing entitlements. The delays in matching beneficiaries to houses have resulted in houses not suitable for intended beneficiaries. For example, although more than 90 per cent of affected households used fuel wood for cooking, this source of fuel is not usable in a large per cent of houses, because of the non-existence of a chimney. The alternate sources of fuel available may be too costly.

Lack of coordination of the relief and reconstruction effort amongst various government agencies, NGOs, donors, private sector, etc., is clearly evident in the mal-distribution of income generating assets such as boats as well as in housing. The problem has been particularly aggravated due to the large numbers of NGOs and private sector organizations operating independently to deliver aid. For example, reluctance on the part of some non-governmental agents even to share beneficiary lists have further complicated the problems of coordination. Greater interaction, engagement and coordination led by the GOSL would benefit the overall relief and reconstruction effort. In this regard, special attention should be given to improving the capacity of the government agents, at all levels, especially at the local level.

Lack of consideration to pre-existing socio-economic conditions has created conflicts in some areas.

The financing needs for rebuilding houses and other construction activities is a growing concern in the face of clear evidence that construction costs have been rising rapidly since initial needs assessments were carried out in the aftermath of the tsunami. Cost blowouts will almost certainly create funding gaps, make reconstruction tasks difficult and impose further strains on government fiscal expenditures. The success of the reconstruction effort cannot be divorced from overall macroeconomic circumstances and policies; the additional strains on

existing macroeconomic imbalances of the tsunami reconstruction process it self will raise the costs of policy errors.

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Appendix 1

A1.1 Summary of Methodology – IPS tsunami survey 2005 (IPS-TS 2005)

This section provides a summary of the methodology for selecting the households for the IPS tsunami-housing survey. Full set of questionnaires for both rounds of the survey, and the focus group themes conducted along with the first survey are available on request.

A1.1.1 Selection of Grama Niladari Divisions (GND) and Households

Selection of Districts

Eight districts that were most severely affected by the tsunami in the Northern, Eastern and Southern provinces were selected for the survey. These consisted of: Trincomalee, Batticaloa and Ampara Districts from the Eastern Province, Jaffna and Mullaitivu Districts from the Northern Province, and Hambantota, Matara and Galle Districts from the Southern Province.

Number of Grama Niladari Divisions (GNDs) per District

In these eight districts, GN divisions were first identified where more than 50 per cent of houses were made unusable due to being completely or severely damaged using Department of Census and Statistics (DCS) data.

Table A1.1: Distribution of GNDs across Selected Districts

District	Number of Unusable Houses	No of GNDs Selected for Survey
Jaffna	3686	1
Mullaitivu	5137	1
Trincomalee	4643	2
Batticaloa	9905	4
Ampara	10566	4
Hambantota	1290	1
Matara	2401	1
Galle	6169	2

Note: Information from Mullaitivu was not available for the selection process.

The 16 GNDs for the study were distributed across the 8 districts based on the level of housing damage in each district (Table A1.1). Within the districts, GNDs were chosen based on socio-economic data so as to select a representative set of GNDs considering ethnicity, religion and livelihoods, and the location with respect to the 2005 buffer-zone. Socio-economic data for this purpose for the Southern districts were obtained from the 2001 Census by the Department of

Census and Statistics. Since census data did not extend to the districts in the Eastern and the Northern provinces, socio-economic information for these provinces were obtained through key-informants from those areas. Key-informant information was also used to select GNDs with households both within and outside the 2005 buffer zone. (Information given by key informants in this regard were not entirely accurate, as a result some GNDs that were mostly within the no-built zone remained in the sample). The selected GNDs for the study are given in Table A1.2.

Table A1.2 Selected GNDs for the Study

District	DS Division	Selected GN Division		(A) Complete ly Damaged + Partially Damaged (cannot be used)	(A) as a % of Number of Household s before Tsunami
		Name	No.		
Matara	Weligama	Pelena South	387B	275	68.24
Hambantota	Hambantota	Hambantota East	93	326	50.00
Galle	Habaraduwa Galle four gravets	Koggala	144A	97	54.80
		Dewata	100A	164	55.97
Ampara	Ninthavur Pothuvil Thirukkivil Alayadiwembu	Ninthavur 01	41	222	65.10
		Sinna Ullai	P/18	242	62.05
		Thambiluvil 1 East	TK/12C	360	64.76
		Sinnamugamuwar am	AV/14	226	78.20
Batticaloa	Manmunai North Koralai Pattu Manmunai South & Eru	Navalady	172	433	100
		Thiruchendhoor	172B	618	78.83
		Kalkuda	204	548	74.56
		Onthachimadam North	111	318	76.56
Trincomalee	Kuchcheweli Town & Gravets	Jaya Nagar	239C	378	74.12
		Uppuvelli	243	215	62.12
Jaffna	Vadamarachchi East	Maruthankarny	J/428	292	100
Mullativu	Maritimepattu	Kallapadu	91	N/A	N/A

Household Selection

A sample of 45 households from the list of *unusable houses* for each GND was randomly selected for the household survey, with 30 households outside the no-build zone and 15 within. However, in some GNDs there were less than 30 houses outside the buffer zone. In these instances more houses from within the buffer zone were interviewed to make up the sample. The households were selected using DCS tsunami census data where available. For the two GNDs where DCS data were not available, household lists obtained from GNs were used as a frame.

A1.1.3 Information Gathering

Due to delays in obtaining access, the survey could not cover Jaffna and Mullaitivu districts of the Northern Province. Therefore, information is available only for 14 GNDs in the Southern and Eastern provinces. Information from the selected GNDs were collected at several levels. To obtain community level perspectives on rebuilding, relocation and land issues, focus groups were conducted in all GNDs. In addition, community level information to ascertain community characteristics and information on rebuilding, relocation and land issues were obtained through key informant interviews based on a structured questionnaire. In addition to these interviews, information on land supply in the GNDs was obtained from the relevant Divisional Secretary's Office, also based on a structured questionnaire. The Household level interviews were conducted using a structured household questionnaire. The questionnaires were drafted in English and translated to Sinhala and Tamil for use in different GNDs.

A1. 2 Methodology for IPS Tsunami Survey 2006 (IPS-TS 2005)

Sample

In July 2006, an attempt was made to resurvey all the 622 households that were interviewed for the IPS-TS 2005 with the view to update the latest progress on the reconstruction effort. The survey was designed to address issues of permanent housing paucity, recovery in livelihoods, etc., to get a clearer picture of where Sri Lanka stands in the reconstruction process one and a half years on. In addition to the housing survey, 3 key informant interviews in each GND were conducted. When a household was unable to be located, randomly selected replacement houses were surveyed from the GND. The resulting database consisted of 595 households, of which 564 were from the original 622 households.