

**An Analysis of the Factors Affecting to the  
Financial Performance of Government Development Projects  
in Sri Lanka**

**by**

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“The work described in this thesis was carried out by me under the supervision of Prof. Kennedy D Gunewardana, Department of Accounting, University of Sri Jayawardenapura and a report on this has not been submitted in whole or in part to any university or any other institution for another Degree/Diploma”.



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“I certify that the above statement made by the candidate is true and that this thesis is suitable for submission to the University for the purpose of evaluation”.



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## **ABSTRACT**

This analysis focuses on assessment of the variables affecting on financial performance of the government development projects in Sri Lanka. The sample comprised of 136 mega development projects (Projects with a total estimated cost more than Rs. 3 billion) that are being implemented by the line ministries. Ten (10) numbers of independent variables in project planning and the implementation stages have been selected to measure their effects on the financial performance of government projects. The criterion variable, financial performance of projects was measured against these ten variables as at the end of second quarter 2012. The independent variables were measured using a pre prepared questionnaire and data was also analyzed by using multiple regression analysis.

The major issues identified at each stage of the project cycle are categorized mainly into two categories - in Project Planning and Project Implementation. It is founded that the financial performance of the development projects in each stage of project cycle have been affected by factors such as procurement, Land acquisition, Project Financing, Project Feasibility and Staffing. Project procurement is the most significant factor amongst all the measured variables. In addition to that it was founded that the land acquisition and project financing also have a significant influence. The majority of the factors which have affected for the financial performance of the development projects are represented in the implementation stage of the project cycle.

**CHAPTER 1**

**INTRODUCTION**

## **1. Introduction**

### **1.1. Background to the Study**

Globally, development projects play a very important role in the achievement of the development goals of a country, in order to provide a better standard of living for the citizens. In this sense developing countries are implementing development projects extensively and they obtain foreign funds and expertise knowledge, through building up multilateral and bilateral relationships to accomplish the overall development goals. In the Sri Lankan context development projects are the major driving force of economic and socio-cultural development of the country. Development projects have to be made use of as a powerful development tool to address the major development issues, that we experience, such as reducing unemployment rate, minimizing income disparity, increasing per capita income, maximize sector contributions to gross domestic product, maximum usage of domestic resources (raw material and man power) etc.

Sri Lanka needs to considerably catch- up its growth rate not only to secure its place in the region as a newly emerging economy, but also to ensure that the country's economy is capable of providing better livelihood for all citizens, including those who are below the poverty line.

Several government agencies are involved in project management at national, provincial, district and pradeshiya sabha levels. The appraisal done by eac level may differ based on different criteria. At national level, especially at the appraisal and approval stage, the procedure adopted is different according to the size of the projects, and therefore projects

are presently classified as small projects, medium projects, large projects and mega projects. Most of the projects are funded by both foreign funds and local funds as well.

All mega projects are financially supported by international agencies such as United Nation Development Programme (UNDP), United Nations International Children Assistance Fund (UNICEF), United Nations Education and Scientific Organization (UNESCO), World Health Organization (WHO), foreign donor agencies such as Japanese International Cooperation Agency (JICA), United States Agency for International Development (USAID), Canadian International Development Agency (CIDA), Swedish International Development Agency (SIDA), Norway Agency for Development (NORAD), international or regional banks such as World Bank (WB), Asian Development Bank (ADB), Japan Bank for International Cooperation (JBIC) and Overseas Economic Cooperation Fund (OECF). Such financial assistance is provided on the basis of grants, aid (concessionary loans) or commercial loans. All external financial inflows for investment in projects should be channeled through the General Treasury of the Government of Sri Lanka and incorporated in the annual national budget.

## **1.2. Significance of the Study**

As a developing country, Sri Lanka's economic growth in the past three decades had been moderate and lagged behind the growth rates achieved by the dynamic emerging economies in East Asia. The protracted civil war which ravaged the country for over three decades resulted in the inability of the country to reach its potential. With the conclusion of



the war in May 2009 the government has set its vision to rebuild the country and has set a target of raising the GDP to 8% in the medium term of the next three years.

In order to achieve the above growth the development activities are being given the highest priority, with assistance of the multilateral and bilateral donors through their support for programmes and projects in all major sectors such as Agriculture, Industry and Services. The programmes and projects undertaken in this area include large as well as mega projects. A total of 648 Development Projects were on going at the end of second quarter 2012. Out of these projects 215 are funded by foreign donors, while the balance is funded by local funds. All 648 projects are of high values, with the Total Estimated Cost (TEC) of each project being over Rs. 50 million. The funding for the projects is from both foreign and local sources. It is revealed that the total annual capital budget allocation is Rs. 294 billion of which foreign assisted developments projects amounts Rs. 231 billion, i.e. 78% of the budget of all development projects. According to the progress report of the Department of Project Management and Monitoring, it is revealed that out of the total 215 foreign funded projects 93 projects (41%) are behind schedule (Department of Project Management and Monitoring 2012). The Asian Development Bank (ADB) is one of the donor agencies that finance a significant share of public investments in Sri Lanka. Studies have revealed that only a little over 55% of the reviewed ADB projects in Sri Lanka have been generally successful (ADB, 2006). This indicates the need to pay special attention to successful implementation of government development projects. Therefore it is very important to explore and identify the reasons for the higher degree of unsuccessful projects out of the total development projects implemented and to take necessary corrective action

to rectify this shortcoming, and to suggest strategies to enhance the performance in achieving desired objectives of the government development projects in Sri Lanka.

### **1.3. Research Problem**

The development of a country greatly depends to a great extent on the efficiency, effectiveness and the sustainability of the development programmes and projects. The experiences over several decades in Sri Lanka have revealed that the performance of many development projects were not reached at the level expected at the beginning and remained below the satisfactory level. As a result of this, the proportion of successful projects has fallen down on one hand and the share of projects encompassed with problems has increased on the other. Although project performance is affected by many internal and external factors, some factors are more influential than others and therefore they are very critical. Hence, it is important to identify such critical factors first to ensure the smooth implementation of projects. It is also necessary to analyze factors at each stage of project cycle to get a proper understanding on critical factors which will directly influence to the financial performance of the government development projects.

Since most of mega projects which were accounted in this study are either financed by a donor agency or a country, the poor performance in projects implementation will create negative impact not only on the government development process but also on the loan portfolio of the country. This will create a pressure on the balance of payment of the country as the payment of commitment chargers and interest payments are to be paid even

for the amounts which have not effectively been utilized. Therefore it is imperative to “critically analyze the factors which are being affecting for the poor financial performance of the government development projects in Sri Lanka”.

#### **1.4. Objectives of the Study**

The overall objective of the study is to identify and analyze the factors, which have been affected for the poor performance of government development projects in Sri Lanka. The specific objectives of the study are;

- (1) To identify the factors which have been affected for the financial performance of the government development projects
- (2) To explore the degree to which contribution of each identified factor for the financial performance
- (3) To ascertain which stages of the project cycle need more attention for enhancing the efficiency and the effectiveness of the projects
- (4) To suggest strategies to reduce the poor financial performance of projects for achieving the desired objectives of the development projects

#### **Research Questions**

- (1) What are the factors, which contribute for the poor financial performance of government development projects?
- (2) What is the degree to which contribution of each factor for the financial performance of the development projects in Sri Lanka?
- (3) What are the stages in project cycle where critical factors do exits most and influential