## BASIC INFORMATION

### A. Basic Project Data

<table>
<thead>
<tr>
<th>Country</th>
<th>Project ID</th>
<th>Project Name</th>
<th>Parent Project ID (if any)</th>
</tr>
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<tbody>
<tr>
<td>India</td>
<td>P171665</td>
<td>First Building Fiscal and Institutional Resilience for Growth Development Policy Loan for Punjab (P171665)</td>
<td></td>
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</tbody>
</table>

<table>
<thead>
<tr>
<th>Region</th>
<th>Estimated Board Date</th>
<th>Practice Area (Lead)</th>
<th>Financing Instrument</th>
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<tbody>
<tr>
<td>SOUTH ASIA</td>
<td>18-May-2020</td>
<td>Macroeconomics, Trade and Investment</td>
<td>Development Policy Financing</td>
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<tr>
<th>Borrower(s)</th>
<th>Implementing Agency</th>
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<tr>
<td>Republic of India</td>
<td>Government of Punjab</td>
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### Proposed Development Objective(s)

The development objective of the proposed operation is to support the Government of Punjab’s efforts toward strengthening policies, systems and capabilities for managing public finances, and improving resource efficiency in the Agriculture-Water-Electricity nexus.

### Financing (in US$, Millions)

<table>
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<tr>
<th>Summary</th>
<th>DETAILS</th>
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<tbody>
<tr>
<td><strong>Total Financing</strong></td>
<td><strong>World Bank Group Financing</strong></td>
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<td><strong>World Bank Lending</strong></td>
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<td><strong>150.00</strong></td>
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Decision

The review did authorize the team to appraise and negotiate
B. Introduction and Context

Country Context

India

While real GDP growth has slowed in recent years, India remains one of the fastest growing major emerging market economies. Real Gross Domestic Product (GDP) growth has moderated from 8.3 percent in FY16/17 to 7.0 percent in FY17/18 and further to 6.1 percent in FY18/19. It is projected to reach 5 percent in FY19/20. The current growth deceleration reflects a multitude of factors: long standing structural bottlenecks, as well as unresolved balance sheet issues in the banking and corporate sectors, compounded more recently by stress in the non-banking segment of the financial sector as well as by increased risk aversion among banks and corporates.

Although risks have increased to some extent, India’s macroeconomic policy framework is considered adequate for the proposed Development Policy Operation (DPO). Momentum has slowed, but economic growth is expected to pick-up from FY20/21 onwards and the economy has proven to be resilient to external shocks. The deviation from the planned path of fiscal consolidation announced in the Union budget comes with a clear ‘return path’, with the fiscal deficit-to-GDP ratio envisaged at near 3 percent of GDP by FY22/23, for the central government. The recent cut in corporate taxes and the modifications in personal income tax structure will lead to temporary revenue shortfalls but are expected to boost consumption and investment in the medium-term. Structural reforms, including efforts to address financial sector weaknesses, are ongoing and are expected to pay-off over time. In recent years, the monetary policy framework has been strengthened and the recent easing of monetary policy has been cautious. Debt and deficit levels are relatively high, but ample domestic funding is available and refinancing risks are moderate. India’s exposure to external volatility has increased, but high reserve levels and limited external financing needs provide adequate buffers. Downside risks to this assessment include a slower than expected resumption of growth and the materialization of shocks to global trade and/or oil prices. However, these do not affect the bottom-line assessment.

Punjab

Punjab was once India’s most prosperous state, but it now faces structural development challenges. A traditionally agrarian state, Punjab benefited greatly from the Green Revolution, which allowed it to become India’s most prosperous and developed state (including in terms of built infrastructure and human development) in a matter of years. The huge grain surpluses produced by its farmers helped India achieve food self-sufficiency. However, the wheat-paddy cropping model that once supported Punjab’s growth is today constraining the state’s development, as it comes with significant detrimental environmental impacts and is sustained through large input subsidies that drain public resources. Over the past decade, Punjab grew at an annual average rate of 6.1 percent compared with a national average of 7.0 percent. The state has also had to contend with high fiscal deficits (averaging 4.1 percent of Gross State Domestic Product (GSDP)) and rising debt over the last decade. Low fiscal space has limited investments in infrastructure and public services - particularly in cities- which has in turn held back the development of vibrant manufacturing and services activities.

The GoP is keen to address these challenges to the state’s long-term growth. The Government has initiated reforms to strengthen its fiscal position, most recently by adopting Rules for the Fiscal Responsibility and Budget Management (FRBM) Act, to promote enhanced adherence to fiscal anchors and to put limits on guarantees. It is also taking measures to strengthen the delivery capacity of the public sector through modernized systems for fiscal and debt management, better alignment between planning and budgeting, and repurposing administrative structures and making greater use of data. At the local level, initiatives have also been initiated to ensure that cities have better planning tools and more sustainable access to own revenue streams.
Meanwhile, the GoP has made combating groundwater depletion a topmost priority, bringing in an integrated focus on reforms in agriculture, power and water management to address this long-term challenge. The combination of a policy of subsidised electricity for agriculture and guaranteed crop sales through public procurement have contributed to a nearly blanket coverage of water-intensive rice across the state, with strong disincentives to diversify to more sustainable and higher-value cropping patterns. These skewed incentives have also resulted in unsustainable increases in the annual rate of groundwater utilization. State-wide, over 80 percent of blocks are classified as ‘overexploited’ and annual groundwater extraction exceeds availability by 14 billion cubic meters. The GoP has initiated coordinated action to promote diversification toward alternative crops, incentivize farmers to use groundwater more prudently, and strengthen institutions for managing groundwater resources more holistically. For example, it is providing subsidies to individual farmers to put in place underground irrigation pipes; it has also mandated that the timing of rice planting coincide with the monsoon rains and initiated an exercise to develop a state-wide water management plan. Finally, it has launched the Pani Bachao, Paise Kamao “Save Water, Earn Money” program which is unique in that it provides monetary incentives to farmers to reduce their electricity usage for groundwater pumps and therefore to save water, while also mainstreaming the deployment of meters.

The proposed development policy engagement seeks precisely to support these reform efforts of the Government of Punjab to address the root causes of these development challenges. Specifically, it aims at strengthening policies, systems and capabilities for managing public finances, (pillar 1) and improving resource efficiency in the Agriculture-Water-Electricity nexus (pillar 2).

Relationship to CPF

The proposed operation is fully aligned with the India CPF. The CPF supports the development agenda of India through a balanced focus on “what” areas merit attention and “how” to engage to deliver results. The three priority areas of CPF are (i) promoting resource efficient growth (ii) enhancing competitiveness and enabling job creation and (iii) investment in human capital. These three “Whats” of the CPF are to be delivered through four specific approaches (“Hows”) to achieving results: (i) leveraging the private sector (ii) strengthening public sector institutions, (iii) engaging Federal India, and (iv) promoting a “Lighthouse India” concept that connects practical know-how for the benefit of India and the wider world. In addition, the CPF supports three cross cutting themes: pursuing climate smart engagements, systematically addressing gender-based inclusion gaps, and harnessing high-impact technologies for development. The proposed operation is squarely aligned with the first “What” (supporting resource efficient growth) as well as with the “Hows” (strategically engaging with states and strengthening public institutions); it also addresses the cross-cutting themes of gender inclusion and climate smart focus.

A key new feature of the CPF is the development of multi-year strategic state engagements, and the proposed DPO will support the state of Punjab under this new approach. The focus on state partnerships involves moving from self-standing operations in states, to programmatic engagements that address state-specific development priorities and improve systems and implementation capabilities for sustained development impact. The proposed DPO will support select high priority policy reforms and strengthen systems and institutions in Punjab. These are strengthening public finances, improving resource efficiency in the agriculture-water-electricity nexus, and strengthening urban finances to enable structural transformation and allow cities to become drivers of growth.

C. Proposed Development Objective(s)

The development objective of the proposed operation is to: support the Government of Punjab’s efforts toward strengthening policies, systems and capabilities for managing public finances, and improving resource efficiency in the

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1. Extraction exceeds recharge.
Agriculture-Water-Electricity nexus.

Key results expected from this operation are:

Under Pillar 1

(i) improved transparency and quality of public procurement
(ii) improvement in financial decision-making systems and capabilities
(iii) more strategic budget preparation, and introduction of gender budgeting
(iv) institutionalization of strong public investment management capabilities
(v) strengthened data systems and management
(vi) improved planning capability and fiscal space for urban local bodies

Under Pillar 2

(i) crop diversification away from water-intensive crops
(ii) adoption of more water-efficient agricultural technologies and cropping practices
(iii) ground-water and electricity savings, in Pani Bachao feeders
(iv) improved monitoring and management of ground-water resources

D. Project Description

Policy reforms and actions under the two pillars are complementary. Pillar 1 supports reforms to improve the management of public resources at the state level and create fiscal space at the municipal level, and pillar 2 supports coordinated actions to promote the diversification away from water-intensive crops, incentivize farmers to reduce their use of electricity and water, and strengthen institutions for managing groundwater resources more holistically.

The main objective of Pillar 1 is to strengthen the policies, systems and capabilities of the state to manage its finances. This will be pursued through a coordinated strategy to (i) strengthen public financial management and procurement, (ii) improve the state’s strategic planning and budgeting capacity, underpinned by improved data systems, and (iii) create fiscal space at the municipal level for urban infrastructure development and service delivery. Specific reforms of the GoP supported under the operation include:

(i) the adoption of a new public procurement law to strengthen the accountability and efficiency of public procurement
(ii) a comprehensive restructuring of the Finance Department to strengthen its operational efficiency
(iii) the introduction of gender budgeting in Punjab to ensure better outcomes from public spending for women
(iv) the adoption of a more strategic framework for assessing and vetting public investments
(v) a strengthening of the frameworks for municipal planning and financing of water and sewerage services, to improve service delivery at the local level.

Pillar 2 supports a mix of institutional, regulatory, and economic reforms in agriculture, power and groundwater management, to support the state’s transition towards greater efficiency of resource use. Punjab is the first state in India to adopt an integrated approach to the agriculture-water-electricity nexus and the operation seeks to leverage these efforts. Specifically the operation will support the efforts of the GoP to:

(i) effectively implement the state’s amended APMC Act (2017), through the adoption of implementation rules
(ii) scale up the Direct Benefit Transfers (DBTE) for agriculture electricity consumers and “demonstration farm” pilots to incentivise more efficient water usage and cropping practices
(iii) strengthen the regulatory and institutional architecture for groundwater management through the adoption and implementation of a new Water Resources Management Act.
E. Implementation

Institutional and Implementation Arrangements

The Department of Finance, Government of Punjab, is responsible for the monitoring and evaluation of the program supported by this operation. As the main implementing department, it will coordinate with all other relevant GoP agencies and departments, to collect the necessary data to assess implementation, monitor progress and evaluate results. The monitoring and evaluations systems are deemed adequate.

F. Poverty and Social Impacts, and Environmental, Forests, and Other Natural Resource Aspects

Poverty and Social Impacts

Actions under Pillar 1, related to enhanced PFM systems, fiscal management and planning, as well as data, are expected to have neutral or positive social and poverty impacts. More rigorous, cost effective and prudent use of fiscal resources so that the value of every rupee spent by the state is maximized and the burden of debt on future generations is minimized can potentially have neutral or positive social and poverty impacts. In addition, the transition of Punjab toward data driven e-governance is also expected to result in more nimble delivery of key social and administrative services to citizens. Targeted improvements in municipal planning and revenue raising capacities are expected to translate into improved service delivery while having modest distributional impacts and providing safeguards for vulnerable households.

Measures, supported under Pillar 2, designed to help address the impact of agricultural patterns and practices on groundwater depletion are also expected to potentially have positive social and poverty impacts. This is because the poor - many of which are landless farm workers from scheduled castes - are most likely to be disproportionately affected by the impact of climate change and groundwater depletion on agricultural yields and sustainability going forward. Moreover, the gradual drop in water tables implies that farmers will have to dig deeper boreholes and invest into more powerful pumps going forward – which may not be accessible to the poorer among them. Current electricity subsidies for agriculture are regressive in that they tend to benefit disproportionately to large landholders who are also the greatest power consumers for water extraction. Finally, it is also likely that poor and vulnerable households are more affected by the health impacts of increased pollutants found in groundwater (including arsenic, selenium and uranium).

Environmental, Forests, and Other Natural Resource Aspects

Reforms to support solutions in terms climate resilient agriculture and ground water conservation can potentially have positive effects on the environment and natural resources and help combat the impacts of climate change. Through Pillar 1, the program will promote a shift toward assessing large public investments through a climate lens, which can help developing multiple mitigation and adaptation strategies within the state budget. It also supports direct policy actions to regulate and optimize the use of surface water in urban areas and therefore constitutes an adaptive strategy for climate change. Pillar 2 adds on significantly to the climate change adaptation measures by proving solutions for more efficient use of ground water through shifting towards more water-efficient cropping patterns and incentivizing behavior change. Improving groundwater-efficiency and reductions in consumption of electricity under the DBTE is expected to result in electricity and water savings and is therefore critical to climate change adaptation and mitigation.

G. Risks and Mitigation

The overall risk rating of this operation is substantial. Substantial risks are associated with (i) the macroeconomic environment at national and state levels (ii) sector strategies and policies, (iii) institutional capacity for implementation, and (iv) stakeholders. These risks, if materialized, could negatively impact the implementation of prior actions and the
achievement of the intended positive results, which would in turn affect the meeting of the development objectives. Governance, Fiduciary, environment and social risks are rated as moderate.

Macroeconomic and fiscal risks are substantial. Economic activity in India has slowed significantly over the past year, and the resulting fiscal pressures experienced by the center have possible implications for intergovernmental fiscal relations. These would be magnified in the event of unanticipated shocks to the global economy and/or increases in international oil prices. Nonetheless, India’s macroeconomic fundamentals remain very robust under all but the most adverse and unlikely scenarios. The World Bank’s most recent forecasts project a gradual resumption of growth and improvement in general government fiscal balances. Punjab’s own finances are also vulnerable to shocks, either in the form of slower than expected growth and revenue shortfalls or in that of contingent liabilities’ realization. World Bank is providing dedicated technical assistance in the areas of medium term fiscal planning, debt management and comprehensive financial analysis of the power sector, including forward looking scenarios.

To manage the risks of sector strategies and policies, the State government has put in place inter-departmental coordination mechanism and is adopting an incremental approach to carefully build the support of key stakeholders and implementing pilots to establish ‘proof-of-concept’ on ground.

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<td>Approved By</td>
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<td>Country Director:</td>
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