Testimony of Patrick C. Fine before the U. S. House of Representatives Committee on Foreign Affairs Subcommittee on Africa, Global Health, and Human Rights

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Millennium Challenge Corporation
United States of America

Good morning Chairman Smith, Congressman Payne, and all the members of the Subcommittee. I am pleased to join my colleagues from the Department of State and USAID to discuss U.S. assistance to Africa and the unique role that the Millennium Challenge Corporation plays in advancing American interests by reducing poverty and promoting good governance in Africa. If there are no objections, I will summarize my remarks and submit my full statement for the record.

Africa is home to more impoverished nations than any other region in the world. Appropriately, most of MCC's partner countries are in Africa—where two-thirds of our funds are dedicated. Although countries in conflict like Cote d'Ivoire grab the headlines, I have witnessed remarkable progress in the over thirty years that I have been living and working in Africa, and I've seen the vital role that U.S. assistance has played in increasing access to education, combating disease, promoting human rights, and strengthening market economies.

President Obama laid out a clear vision for development that articulates the strategic, economic and moral imperatives that explain why development assistance is vital to U.S. national security. The President's Global Development Policy recognizes that protecting our interests and advancing our ideals requires economic and diplomatic tools such as the MCC, USAID and the State Department.

The MCC is a specialized instrument that works with poor but well-governed countries. Our programs build capacity, including trade capacity, and strengthen relationships with important emerging economies.

As you know, MCC only works with countries selected using publicly available, third-party indicators that measure the extent to which a country is ruling justly, investing in its people, and providing economic freedom. Making selectivity a core feature of our business model creates an amazingly powerful set of incentives for good policy performance. This is often called the "MCC Effect," and we have seen governments undertake reforms to become eligible for MCC assistance. More importantly, countries make these reforms before we put *any* money on the table; to retain other assistance programs already in implementation; and now—as the first generation of compacts complete—to become eligible for a second compact.

Within the context of the U.S. Government's overall diplomatic relationship with a country, and working especially closely with the Department of State and USAID, we continually work with our partner countries on policies and practices needed to ensure the sustainability of our investments. At a macro level this means engaging civil society, respecting the rule of law, confronting corruption, and valuing human rights. At the investment level, we condition assistance on sector level reforms, making it clear that if commitments are not met, we reserve the right to suspend or cancel a compact. In fact, we have a record of doing just that.

Secretary of State Clinton has described development resting on a three-legged stool made up of government, the private sector, and civil society. Each leg must be strong—and they all must be balanced—to support the difficult work and political will that goes into bringing about the kind of change that expands opportunities and reduces poverty.

The MCC selective process creates direct incentives for governments to adopt policies that promote economic growth, and our emphasis on country ownership and placing responsibility for program implementation on our partner countries also strengthen the other legs of the stool.

We actively encourage participation from civil society groups in our programs. They must be consulted during compact development, and they must be represented on the local governing boards our partner countries establish to oversee the programs.

We also make concerted efforts to promote private sector participation. The reason is simple: MCC programs reduce constraints to economic growth, but it is the private sector—whether we are talking about small-scale commercial farmers, the truckers who transport goods on improved roads, or large-scale follow-on investments in manufacturing or retail—that create jobs and income and put a country on the path away from aid dependency.

In return for scarce U.S. taxpayer dollars, we advance U.S. economic and security interests. The emerging economies of sub-Saharan Africa are the growth markets of the 21st century. Between 2000 and 2008, GDP per capita income in sub-Saharan Africa grew by 54 percent when adjusted for purchasing power parity.

Our competitors see these opportunities and they are investing heavily. The World Bank expects international capital flows to the region to be higher than anywhere else in the world—4.9 percent this year and 5.2 percent in 2012. America's development assistance helps unlock the potential in these markets, fosters personal and business relationships that grow into mature trade relationships, and promotes our security interests.

Look at the track record of MCC in terms of results that benefit the poor, and in terms of the incentives for good policy performance that create the business environment to allow countries to increasingly finance their own development, and you'll see this taxpayer money is well spent.

America's Interest in African Development

Africa remains the world's poorest continent. Rising food prices have increased hardship for poor households and in some countries, such as Cote d'Ivoire, Zimbabwe and the Democratic Republic of the Congo, armed conflict, bad leadership and corruption deny millions of good, hardworking people the opportunity to build better lives.

Meanwhile, Africa also is presented with unprecedented opportunities. Bill Gates noted in a recent speech that half of American exports go to developing markets. As the population and economy of these countries grow, so will that number. Mr. Gates calls development "the smartest way our government spends money."

By investing in poor but well-governed countries in Africa and around the world, MCC is building capacity and strengthening relationships with these emerging economies. We must be mindful that we are not the only country with an interest in doing so. If we cut back on our development efforts, we will leave a vacuum in these nations that someone else will fill, ceding valuable opportunities to build trade relationships, create American jobs, and promote American interests.

MCC also is helping to make Americans safer and more secure by promoting stability and developing strong partners in key regions around the world. Defense Secretary Robert Gates has been one of the most persuasive advocates for financing development work. In recent remarks, Secretary Gates stated:

> *"…[I]n military planning, what we call phase zero is, how do you prevent conflict? How do you create conditions so we don't have to send soldiers? And the way you do that is through development. Development contributes to stability. It contributes to better governance. And if you are able to do those things and you're able to do them in a focused and sustainable way, then it may be unnecessary for you to send soldiers. …Development is a lot cheaper than sending soldiers."*

That is one reason why President Obama, like President Bush, has made development—together with defense and diplomacy—a critical pillar of our national security.

MCC's Work in Africa

As I said, MCC works with the world's best-governed poor countries, and through our highly competitive country selection process, a large portion of our investment portfolio has been dedicated to Africa.

Of the 23 MCC Compacts signed to date, 13 have been with African countries: Benin, Burkina Faso, Cape Verde, Ghana, Lesotho, Madagascar, Mali, Malawi, Mozambique, Morocco, Namibia, Senegal, and Tanzania. Of the 21 countries in MCC's Threshold Program, 12 have been in Africa: Burkina Faso, Guyana, Kenya, Liberia, Malawi, Mozambique, Niger, Rwanda, São Tomé and Principe, Tanzania, Uganda and Zambia.

Nearly sixty percent of our compact countries are located in Africa, and projects in those nations receive two-thirds of our funds.

When the President last year unveiled his new Global Development Policy that I spoke of, he made clear that the United States is "changing the way we do business" in development. Laying out a set of principles and practices that are at the core of MCC's model, he called for all U.S. Government agencies to embrace a focus on results, selectivity, country ownership and transparency.

In his budget request for Fiscal Year 2012, President Obama requested $1.125 billion for MCC, signaling once again that the agency's distinctive model will continue to play an important role in the effort to cultivate opportunity and prosperity in poor countries around the world. President Obama's Fiscal Year 2012 Budget request would enable MCC to sign compacts with Georgia and Ghana, as well as fully fund a compact with Indonesia.

MCC, like other U.S. Government agencies, is operating in a constrained budget environment. MCC holds itself accountable to the American people to ensure that every taxpayer dollar generates the best possible return on investment. As good stewards of American taxpayer resources, every day we ask ourselves the tough, fundamental questions about the effectiveness and efficiency of our approach to development and our operations.

For example, MCC recently took action to prohibit state-owned enterprises from bidding on MCC contracts. MCC's original procurement guidelines included no guidance on this matter, and many—including some members of this committee—rightly expressed concern. MCC's aim is to ensure a level playing field for commercial firms that bid on MCC-funded contracts. Because state-owned enterprises have built-in advantages such as access to preferential credit terms, we took this step to ensure private companies—including American companies—get a fair opportunity to compete for MCC-funded contracts.

MCC's estimated budget requirements for proposed compacts are based on several factors, including policy performance on MCC's indicators, total population, population living below national poverty lines, absorptive capacity, and, specific to Africa in the case of Ghana, performance in previous compact implementation. Final compact amounts will be based on funding availability and on the scope of agreed-upon projects.

After seven years of operations, MCC has committed \$8.2 billion to reducing poverty in 23 countries, \$4.2 billion of which has been contracted and \$2.2 billion of which has been disbursed.

For this investment of \$8.2 billion in taxpayer money, we expect to generate \$12.3 billion in increased incomes for 172 million people over the coming years.

Two of the three countries selected as eligible for a second MCC Compact are African countries, Cape Verde and Ghana. Ghana was selected as eligible for compact assistance in January 2011 by the MCC Board and has just begun the rigorous process of developing an MCC Compact. It was selected because of its continued strong policy performance, status as an important emerging market, strategic importance both globally and regionally, and the successful implementation of its first compact.

The Republic of Ghana consistently performs well on MCC's indicator criteria and is generally viewed as one of Africa's most stable policy performers. Since 2004, Ghana has scored among the top low-income countries on the Control of Corruption indicator. In a region where constitutional transfers of power are often disputed, Ghana has a record of peaceful democratic elections and the transfer of power to opposition parties. In 2009, Ghana ranked better than almost two-thirds of all countries on Transparency International's Corruption Perceptions Index, and is preparing for transparent management of potential oil revenues.

MCC's Selective, Targeted Approach to Development Assistance

One of the most distinctive features of MCC is our broad-based, bipartisan support. The MCC approach to development—with our focus on economic growth, sustainability, country ownership, transparency and accountability—has been embraced by Democrats and Republicans in Congress; Presidents Obama and Bush; Secretaries Clinton, Rice and Powell; and leading voices from the right and the left, from the Heritage Foundation and the American Enterprise Institute to the Brookings Institution and the Center for American Progress.

Why has MCC won the support of policymakers and analysts across the political spectrum? Because of our innovative, reform-minded mission and business model. MCC's mission is to reduce poverty through economic growth in a select number of well-governed countries. MCC selects country partners carefully to ensure the highest returns on our investments and creates strong incentives to advance democratic, market-based principles.

MCC takes the idea of that three-legged stool needed to sustain economic development and stability in any nation very seriously, and as I have said our programs integrate development of each of the three legs—government, private sector and civil society. These legs must be strong and balanced if the stool is to support the weight of society.

First, the government. Part of MCC's accountability model is the ability and willingness to say "no"—no to countries that do not meet MCC's high standards for eligibility, and no to proposed investments that do not have promising returns for economic growth and poverty reduction. In determining eligibility for funding, MCC evaluates whether a country has created a policy environment for sustained economic growth through 17 independent, transparent policy indicators that measure a country's commitment to ruling justly, economic freedom, and investing in its own people. This has given rise to the "MCC Effect," in which we see countries make positive reforms in the hope of becoming eligible for MCC assistance. For example, before investing in Lesotho, we worked with the government to change a law that treated adult women as minors, so that women could be full participants in the economy. Meanwhile, the principle of country ownership strengthens and builds capacity of governments by requiring them to establish institutions capable of carrying out infrastructure projects and implementing other programs.

Second, the private sector. Inherent in MCC's model is the idea that the key to sustainable development is encouraging private investment—and therefore reducing dependence on foreign aid—in developing countries. That is why engagement in the private sector is central to our philosophy. We select and design projects based on the likelihood that they will lead to private sector activity, and we engage private businesses at every step of the process to gather input and encourage them to partner with us. For example, in Ghana, our work to improve irrigation led a company called VegPro to lease a 1,070-hectare farm. This investment will offer new employment opportunities for people in the region. It will also give Ghanaian farmers access to the European markets as VegPro will be signing purchase agreements with farmers and their organizations.

Finally, civil society plays an equally vital role in development and we work hard to strengthen this sector, as well. During compact development, we require our companies to gather input from civil society groups, forcing them to consult and collaborate with groups who might otherwise be disregarded. In addition, the local Millennium Challenge Account, or MCA, boards that implement our projects in-country are required to include members who represent civil society groups.

By adopting this approach, MCC's goal is to foster balanced growth in each developing country and create an accountable, responsive government; an active private sector; and an engaged watchdog and partner in civil society. Signing up to work with MCC means a country is committing itself to tackle the tough policy reforms necessary to create an environment in which the private sector can thrive, citizens can hold their governments accountable, and U.S. taxpayers can see they are getting a good return on their investment. Our goal is to help poor countries rise out of poverty and achieve self-sufficiency, as well as to create stable trading and investment partners for the United States, which will strengthen the American economy and make our nation more secure.

MCC is Delivering Results

MCC's focus on economic growth, sustainability, country ownership, transparency, and accountability is working. All development partners, both donors and host countries, are interested in achieving results. What distinguishes MCC is our commitment to technically rigorous, systematic, and transparent methods of projecting, tracking, and evaluating the impact of our programs. MCC's results exist along a continuum—from policy changes countries make to become compact eligible ("the MCC Effect"), to interim outputs and outcomes as compacts mature, to our ultimate goal: income increases over the long term.

We expect MCC's current investments to benefit roughly 40 million people in our partner countries in Africa—and we expect incomes in those countries to rise by over $8.8 billion over the life of those investments.

Even before these income gains are achieved, MCC and our country partners have tangible results to show. To date, MCC investments in new or improved irrigation and technical assistance have facilitated the adoption of new agricultural practices on 82,510 hectares of land. Our funded programs have trained over 150,000 farmers in techniques that help them produce higher-quality, higher-value crops. We have provided funding for $66 million in agricultural loans, and have financed assistance for over 3,800 private enterprises involved in agriculture-related business. We have supported construction of more than 890 kilometers of roads that link markets and encourage trade, and have another 2,400 kilometers under construction. These interventions aim to increase incomes through market-driven agriculture. MCC tracks these results closely because they are the drivers of the income gains we and our partners aim to achieve.

While these results are important indicators of success, they do not tell the whole story. We are pleased that our program outputs are on track, but we hold ourselves to a higher standard: are MCC investments increasing incomes? That is why we use independent third-party evaluators to track the results of MCC investments even after the compact ends. We are eagerly awaiting these results from our first completed compacts, but preliminary data from the field is promising.

For example, in Honduras, which was the first country to complete an MCC Compact last September, we have preliminary data from our agriculture program implementer showing that farmers who received assistance from MCC saw their annual net income rise 88 percent, from $1,880 per hectare of land cultivated using new practices to $3,550 per hectare.

I want to stress that this is preliminary data, and we will know much more when the work of our independent evaluators is completed. But it is consistent with the output- and policy-based results that we have seen and the personal stories I have heard directly from farmers and entrepreneurs with whom I have visited.

MCC and the African Growth and Opportunity Act

Next month, Zambia will host a forum to discuss the impact and future of the African Growth and Opportunity Act (AGOA), which was passed by Congress and signed into law by President Clinton in 2000.

The goal of AGOA was to create opportunities for economic growth in Africa by expanding opportunities for exports from qualifying countries to the United States. Total AGOA imports have risen from about $8 billion in 2001 to more than $44 billion last year. Excluding energy-related goods, AGOA imports last year rose to $4 billion, an increase of 18 percent over last year and nearly three times the amount in 2001. This increase is encouraging but it is not good enough.

MCC is focused on creating investment- and trade-ready environments in Africa that will help our partner countries take full advantage of AGOA-related opportunities. As recently as 2008, MCC was the largest U.S. Government source of trade-related funding for sub-Saharan Africa. MCC is placing greater focus on demand-driven strategies that connect beneficiaries to global markets. And our partner countries are already undertaking reforms to attract investment, so they have a natural head start on laying the groundwork to take advantage of AGOA.

For example, Tanzania is putting its MCC funding to work rehabilitating trunk roads that will connect the seaport of Tanga with the city of Horohoro at the Kenyan border. This investment will boost trade between Tanzania and Kenya, reducing transportation costs between these two markets and improving access to Kenya's major port of Mombasa.

In Cape Verde, MCC's investments were used to modernize the Port of Praia, which handles half of the island nation's cargo. The funds were used to establish a cargo village for storage, construct an access road, and improve security. The improvements to the port, combined with the concurrent privatization of port services, will maximize its operational capacity and productivity, promoting growth in the commerce and tourism industries.

MCC investments are also opening doors for increased trade in the landlocked country of Mali. Mali's one major airport has one of the shortest and oldest runways in West Africa. As a consequence, the volume of goods that can be safely transported in and out of the country is severely limited. Mali's MCC Compact includes rehabilitation and extension of the runway, construction of a new terminal, and a number of other airport infrastructure projects. These improvements, together with management system improvements and private sector partnerships, will improve airport security and efficiency while allowing for new small-business airport concessions that will create jobs and increase revenue. It will also allow thousands of small farmers greater access to lucrative markets.

These are just a few examples of MCC investments that are building the foundation for our African partners to take full advantage of AGOA and unlock the potential to reduce poverty through economic growth.

MCC's Subsequent Compacts Will Focus on Constraints to Investments

Entering our eighth year, MCC is beginning a new phase of innovation and partnership. As first compacts strengthen the foundation for economic growth, subsequent compacts—new MCC investments with countries that have successfully concluded their first compacts—are expected to target constraints to private investment. MCC aims to help countries like Ghana, which was reselected as a candidate country for subsequent compacts, solidify an economic growth path that attracts private investment, reducing the need for aid.

MCC's engagement with partner countries is not open-ended. MCC carefully considers the appropriate nature and duration of each country partnership based on the country's policy and implementation performance, as well as the opportunities for an impact on growth and poverty reduction. A defining characteristic of MCC's model of aid effectiveness is selectivity, both in the countries we work with and the investments we make. MCC's business model emphasizes selectivity and our mandate to partner with countries where investments will have the greatest potential returns in terms of poverty reduction and economic growth, and where U.S. taxpayer resources can be used most efficiently and effectively.

While a single compact alone cannot address all binding constraints to a country's growth or transform an entire economy, especially in Africa where many of our partners start at a much lower GDP, a subsequent compact in a country that continues to perform well has the potential to help countries change their growth path away from aid dependence and toward greater reliance on private sector investment and internally generated revenue. For the poorest countries, even the ones with the right policies in place, it may take decades of sustained growth to lift citizens out of poverty. For low-income countries like Tanzania, where the annual per capita income is $500, economists estimate that it could take over 20 years to double per capita income even if the country sustains annual per capita growth of four percent (a historically high rate).

This does not mean, however, that MCC engagement should last anywhere near that long. On the contrary, MCC's role is targeted and selective, and only the best performers will be eligible for continued, limited engagement. MCC's Board is particularly discerning when determining eligibility for follow-on partnerships. In addition to good policy performance, countries must show meaningful progress toward achieving first compact results before being considered for a subsequent compact. Of the 10 countries that will successfully conclude first compacts by the end of 2012, MCC's Board has thus far only selected three as eligible for a subsequent compact. Cape Verde was selected in Fiscal Year 2010 and Georgia and Ghana in Fiscal Year 2011.

In our approach to subsequent compact design, MCC focuses increasingly on specific constraints to investment and private sector engagement; by removing such constraints, MCC helps to expand opportunities for U.S. businesses in emerging markets. This is in line with the President's Global Development Policy directive to foster the next generation of emerging markets by encouraging broad-based economic growth and democratic governance.

MCC supports this effort by reaching out to the private sector, by grounding our investment choices in a constraints analysis that identifies specific obstacles to private sector-led growth, by introducing financial instruments designed to enhance access to capital, and by promoting innovative project content in areas of potential growth, such as alternative energy, applied technology and financial inclusiveness.

The potential to leverage MCC funding with a direct impact on investment growth serves as one of the screens for evaluation of second compact programming, in addition to MCC's mandate to promote poverty reduction through economic growth. By helping these countries solidify the progress they have made and become better integrated in the global market system, the United States is opening new investment opportunities for American firms, as well.

MCC Believes Corruption Erodes Private Sector Growth

I would like to discuss another critical topic, which is how MCC deals with corruption in potential or current partner countries. Because corruption has the power to completely undermine private sector growth—as well as any investment MCC or other donors make in developing countries—we take this issue very seriously.

MCC's approach to fighting corruption begins before we even select a country for eligibility. MCC's corruption indicator is a key part of country eligibility decisions. In fact, it is the only "hard hurdle" in the eligibility system. Our scrutiny does not stop after selection. Corruption is closely monitored as a country develops a compact and proceeds into compact implementation. MCC has a publicly available anti-fraud and corruption policy that outlines precautions that we take and describes ways of responding to any instances of corruption in a compact program. We are currently training our local MCA accountable entities on how to apply this policy and develop risk assessments for their own work.

In addition to protecting against corruption in our compacts, and assessing individual cases of corruption, MCC assesses broader patterns of government actions that undermine institutions of accountability: courts, anti-corruption commissions, auditors and the media. Governmental actions that undermine these institutions of accountability make individual instances of corruption more likely, enable corruption to flourish, and cultivate a culture of impunity. By emphasizing the institutional response, MCC incentivizes governments to take greater responsibility for rooting out corruption.

For example, MCC and several other donors made clear to the Government of Senegal that recent changes to their procurement code and the regulatory entity responsible for its oversight, in part due to legitimate national security concerns, were an accountability concern to us. In response, the government entered into discussions with donors, including MCC specifically, to address our concerns as they further revised the procurement code. Consequently, they have taken steps to amend the objectionable changes—including a January 2011 decree and a more recent draft decree under consideration by the Government of Senegal and various stakeholders. MCC is studying these amendments.

Working with some of the poorest countries in the world means working with countries that struggle with policy performance including corruption. MCC's challenge is to find the right way to pursue poverty reduction while staying true to our model of selectivity and accountability, and this is particularly true in the case of corruption.

MCC's Proposed Legislative Changes Would Strengthen an Already Strong Model

We hope to work with members of this Subcommittee again this year on passage of a package of legislative changes to MCC's current authorities, including allowing for concurrent compact authority and longer compacts in certain circumstances.

The proposed changes are based on lessons learned since MCC's creation in 2004 and will provide the flexibility needed to maximize the impact of MCC programs through more innovative approaches to development assistance.

Concurrent compact authority would allow MCC to sign separate compacts with a country based on the specific timing requirements of individual projects rather than as part of a package driven on a single timeline. Concurrent compacts would improve MCC's ability to manage our compact pipeline with greater predictability and serve as an added incentive for policy reforms in partner countries.

With concurrent compacts, the agency could move forward with projects that are investment-ready, instead of putting several projects at various stages of readiness into a single compact or delaying compact signing for a promising but less-developed project. As part of a larger, cohesive framework, concurrent compacts will allow for smaller, staggered agreements; speed implementation; improve project management by allowing countries to focus on managing fewer projects at a time; build management capacity with early projects; ease the current burden of managing large, complex compact programs; and foster innovation by allowing MCC to pursue new approaches and partnerships that will help to speed up the compact development process.

Additionally, while having definite time frames for MCC Compacts is an important best practice for effective foreign assistance, in some cases projects face implementation challenges that mean they cannot be completed within the mandated five-year period, particularly given MCC's emphasis on country-led implementation and MCC's high accountability standards. In these cases, MCC's options for responding to implementation challenges are limited by the five-year time frame. Allowing MCC, in exceptional circumstances, to extend the duration of our five-year compact period for up to two additional years would allow MCC and our partner countries to pursue a fuller set of options for managing challenges and achieving compact objectives.

MCC also has sought legislative changes aimed at ensuring that changes in countries' income categories do not necessarily prevent the agency from working with the best policy performing countries that also have populations living in extreme poverty. Each year, countries abruptly graduate from one income category to another with no transition period. Sudden shifts in income category, due in part to changes in currency exchange rates, pose serious issues for MCC. This impacts whether they can be candidates for MCC assistance at all, and changes both the policy performance standards against which they are measured and the levels of funding they can receive.

Conclusion

With that, Chairman Smith, I would like to again state my appreciation for your continued support of results-based foreign assistance, and we look forward to continuing our strong working relationship with you, Congressman Payne, and other members of the subcommittee.

I would be happy to answer any questions that you may have.

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