

MILLENNIUM CHALLENGE CORPORATION: CAN THE EXPERIMENT SURVIVE?

EXECUTIVE SUMMARY

THE PAPER IN A NUTSHELL

- The Millennium Challenge Corporation (MCC) is a noble experiment in development aid, but will fail to reach its full potential if Congress, the administration, and the new leadership at MCC do not resolve a number of fundamental issues critical to its long-term viability and success. In particular, Congress needs to significantly increase the resources it allocates to programs that focus on economic growth; embrace innovation and greater risk in the design and implementation of programs; and take a flexible, long-term view of what increased development aid is likely to achieve. For its part, MCC must review and adjust its indicators for aid eligibility; modify the mechanism by which it engages the private sector; and undertake a number of other needed reforms.

VITAL STATISTICS

- The Millennium Challenge Corporation (MCC) was established in 2004 to provide grants to a select group of developing countries that demonstrate a commitment to good governance, invest in the health and education of their people, and adopt sound economic policies.
- Since its founding, MCC has entered into compacts with 20 of 24 eligible countries, committing more than \$7.2 billion to long-term sustainable development.
- MCC's annual appropriations from Congress have ranged from \$875 million to \$1.7 billion.
- Although the U.S. government spends more than any other country on foreign aid in absolute terms, in 2008 this amount represented only 0.81 percent of the annual U.S. budget and 0.19 percent of gross national income (GNI).

RECOMMENDATIONS FOR CONGRESS AND THE ADMINISTRATION

- **Agree on the vision:** MCC's work has been complicated by vague and often shifting expectations. Congress and the administration should work with MCC to articulate a common vision for the agency, then stick to that vision.
- **Forbid earmarks:** One of MCC's greatest strengths is that it encourages countries to take ownership of projects on their own soil. Congress must resist the urge to earmark MCC funding or otherwise dictate how compact funds may be spent.
- **Forbid a "Buy-American" requirement:** Allowing recipient countries to procure supplies without a "Buy-American" requirement ensures they receive the best product for the lowest cost. It also strengthens local companies by allowing them to compete on equal footing with U.S. and other foreign vendors.
- **Maintain MCC's independence:** MCC's success stems from its relative insulation from the short-term political pressures of the State Department and other agencies. Congress should therefore resist efforts to merge MCC into USAID or State.
- **Permit no-year money:** Complex projects often take two or more fiscal years to complete. Congress should continue to permit MCC to take full advantage of its "no-year" authority by allowing the agency to carry unobligated balances forward from one fiscal year to the next.
- **Remove the 25 percent LMIC funding restriction:** MCC is currently barred from allocating more than 25 percent of its funds to lower-middle income countries (LMICs). This funding restriction significantly hampers MCC's ability to address pockets of extreme poverty and should be abolished.
- **Permit concurrent and longer compacts:** MCC may not currently enter into more than one compact at a time with a given country and compacts are limited to five years. To enable greater flexibility and allow shovel-ready projects to move forward more quickly, Congress should permit as many as four concurrent compacts per country and increase the maximum allowable time span to ten years.

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EXECUTIVE SUMMARY, CONTINUED

RECOMMENDATIONS FOR THE MILLENNIUM CHALLENGE CORPORATION (MCC)

- **Clearly define and defend MCC's governing principles:** MCC needs to clearly and aggressively position itself as a long-term investment vehicle that aims to have a meaningful impact on poverty reduction and growth.
- **Eliminate the threshold program:** MCC today operates a threshold program to help borderline countries become aid eligible. This responsibility should be turned over to USAID, which is far better equipped for the task. Funds freed up by this change should then be used by MCC to promote health and education.
- **Review and adjust the eligibility indicators:** Eligibility for MCC funding is based on a country's performance relative to its neighbors as measured by seventeen different indicators. These metrics provide a transparent, apolitical, and objective mechanism for establishing eligibility. They should also be periodically reviewed and adjusted to ensure they accurately reflect recipient countries' real world performance.
- **Utilize more innovative and riskier investment models:** MCC today operates under the "project finance" model of designing, funding, and evaluating specific programs and projects. It should consider alternative mechanisms, such as the creation of guarantee funds for private sector investment in energy, transportation, and other infrastructure projects or sector-targeted budget support.
- **Modify the mechanism for engaging the private sector:** MCC has yet to develop a mechanism for attracting significant upfront investment from the private sector. To do so, MCC should attempt to identify specific private sector companies interested in making such investments and consider signing compacts directly with private sector entities.
- **Simplify the approvals, reporting, and auditing requirements:** Based on anecdotal evidence from the field and the drumbeat of complaints by recipient countries, it is clear that MCC's approval and reporting processes are too onerous. The list of MCC-required approvals should be significantly curtailed and the number and complexity of country reports dramatically reduced. MCC should also require annual, rather than quarterly, country reporting.
- **Provide earlier, more robust training for country counterparts:** The initial MCC operating model underestimated the lack of capacity in recipient countries. Training of local officials in program design, procurement, and financial management needs to begin much earlier in the compact development process.

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