Testimony of Daniel W. Yohannes Chief Executive Officer, Millennium Challenge Corporation to the Senate Foreign Relations Committee

April 13, 2011

MILLENNIUM
CHALLENGE CORPORATION
UNITED STATES OF AMERICA

Thank you, Mr. Chairman, and every member of the Committee for the opportunity to discuss the work of the Millennium Challenge Corporation. I am honored to be here and to work with the Committee to reduce poverty and advance American interests and values, around the world.

Mr. Chairman, as you know, promoting stability, building the next generation of emerging markets, and developing strong and capable partners makes Americans more secure. But to be successful, we need a robust, effective array of development tools. That is why I am so pleased to be here with my good friend, USAID Administrator Shah.

President Obama has called on MCC to play a distinct, integral role in implementing the new U.S. Global Development Policy, one that complements the work of USAID. Dr. Shah and I coordinate closely to find ways our agencies can work together and leverage our comparative advantages to help poor countries help themselves.

The Millennium Challenge Corporation (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.

Before discussing President Obama's Fiscal Year 2012 budget request for MCC, and highlighting issues of strategic importance to the agency in the coming months, I would like to address three fundamental questions about MCC. First, what makes us distinctive? Second, are we delivering results? And third, how are the American people benefitting from MCC's investments?

MCC's Selective, Targeted Approach to Development Assistance

What makes MCC distinctive? 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.

There is good reason we have won the support of policymakers and analysts across the political spectrum: 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—not just in MCC countries but in emerging markets across the developing world.

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. We believe that engaging with developing countries in a selective, targeted way is not only fiscally responsible in the short term, but also is critical to poor countries attracting private investment and ending their reliance on aid in the long run.

Good governance is critical for economic growth. We look for opportunities for reform in areas that will ensure the sustainability of our investments. These reforms have included changes to national policies, laws, regulations, and even the traditional ways of doing business by government institutions. 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. In most cases, these reforms, and the domestic capacity that MCC's country-led programs build, not only help unlock the full potential of U.S. taxpayer dollars, but also help improve the broader conditions for continued growth and investment in our partner countries.

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

The second fundamental question I confront on a daily basis is on MCC's impact: Are we 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 more than 170 million people in the poorest countries around the world—and we expect incomes to rise by over $12 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 – an area slightly larger than Shenandoah National Park in the United States. 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 though market-driven agriculture. MCC tracks these results closely because they are the drivers of the income gains that 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 are so excited about preliminary, promising data that is coming from Honduras, our first completed compact program.

In Honduras, 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's Investments Are Helping to Build the Next Generation of Emerging Markets and Make Americans More Secure

The third fundamental question is: Are the American people benefitting from MCC's investments? President Obama's new development policy is building on the best ideas of the Bush Administration and calling on U.S. development agencies to help build the next generation of emerging economies. By doing so, we are investing in a better future that offers opportunities to poor people in MCC partner countries *and* to American businesses and our own citizens.

In a speech earlier this year, Bill Gates noted that fully half of current U.S. exports—more than half a trillion dollars—go to developing markets. Looking forward, leading economists expect the developing world to become the growth engine of the global economy.

MCC investments look to remove constraints to growth so that the private sector will invest and flourish. These investments are helping to build a foundation for U.S. exports and increased business activity, which will mean increased growth and job opportunities here at home.

MCC is funding more public-private approaches that can leverage our effort and bring in the private sector from the beginning. We are focusing on policy reforms, such as an initiative in Jordan that has attracted $90 million in private investment in the water sector.

Our approach creates strong incentives for policies that are business-friendly. In Cape Verde, for example, the time required to register a business dropped from 54 days to as little as one day. Those are the kinds of changes that convert foreign assistance from a well-intentioned contribution into a productive investment.

Our commitment to private sector engagement is the reason we have taken action to prevent 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 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.

The President's Fiscal Year 2012 Budget Request for MCC

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

In his budget for Fiscal Year 2012, President Obama requested $1.125 billion for MCC, making the agency a central part of the U.S. Government's effort to promote 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's estimated budget requirements for these compacts are based on several factors, including policy performance on MCC's indicators, total population, population living below national poverty lines, absorptive capacity, and, in the case of Ghana and Georgia, performance in previous compact implementation. Final compact amounts will be based on funding availability and on the scope of agreed upon projects.

MCC requests $912 million of the total Fiscal Year 2012 request for compact programs, divided between a second tranche of funding for Indonesia and subsequent compacts for Georgia (est. $100–150 million) and Ghana (est. $350–400 million). Because of its proposed size, the Indonesian compact would be funded over Fiscal Years 2011 and 2012, for a total compact range of $700–770 million.

Indonesia is the fourth most populous country and the largest Muslim-majority country in the world, with more than 100 million of its 250 million people living on less than $2 per day. Given Indonesia's strategic importance to the United States, its economic potential, and the high number of people living in poverty, an MCC compact would be a smart investment for the American people.

Both Ghana and Georgia were selected by the MCC Board of Directors as eligible to develop subsequent compacts. These countries were selected because of their continued strong policy performance, their status as important emerging markets, their strategic importance both globally and regionally, and their successful implementation of their 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.

Georgia is recognized globally as one of the best investment climate reformers, even though 30 percent of its population still lives on less than $2 a day. Over the last five years, its scores on the World Bank's Doing Business assessment have improved more than any other country in the index. The country has also made significant strides to privatize state-owned industries and improve its Transparency International rank on the corruption perception index. This good economic policy performance is reflected by the fact that Georgia has seen a 55 percent increase in new businesses registered.

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 newly-selected Georgia and Ghana, 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 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, 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.

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, and any investment MCC or other donors make in developing countries, we take this issue extremely 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.

Earlier in my testimony, I spoke of the strong results we are seeing from our partnership with Honduras. Honduras, however, did not pass MCC's control of corruption indicator at the time of country selection for Fiscal Year 2011. For me, it was difficult to not have Honduras selected for a second compact. But MCC tries to stick to its principles, and we place great emphasis on fighting corruption.

While the State Department remains the lead on working with the Government of Honduras to address human rights and political issues, MCC has been engaged in very constructive conversations with the government to improve performance on accountable governance, enhanced management of public resources, and fiscal transparency. The Honduran government has initiated a set of reforms to improve budget management and transparency, increase civic participation in budget preparation and reporting, upgrade legislative oversight, and strengthen internal and external audit functions.

Our scrutiny regarding corruption 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 MCC takes 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 implementing agency, 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 changes that would have weakened procurement procedures – 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 the Committee 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 could otherwise slow down 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 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 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

Mr. Chairman, my own background is in banking—and I bring a banker's perspective to my job. But my perspective is also informed by my travels in poor countries; by my personal experience; and by my faith in the values that make America strong—freedom, opportunity, responsibility, and the willingness to lend a helping hand.

I have seen the toll poverty takes—in broken dreams and wasted potential. But I've also seen how much hardworking men and women can achieve when they are given the tools and the chance to build a better life. I am proud that our nation supports those aspirations for dignity and progress, and grateful to this Committee for your leadership in promoting the security and stability of these countries.

Thank you for this opportunity to testify. I request that an extended version of my testimony be entered into the record, and am happy to answer your questions.

2011-001-0570-01