

**Testimony by
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Thank you very much Mr. Chairman—and members of the committee—for the opportunity to appear before you this morning. Six months ago, I was testifying before you as President Bush’s nominee to become the first Chief Executive Officer of the Millennium Challenge Corporation (MCC). Yet during these past six months, MCC has designed and implemented its operational structure, carefully reviewed and selected countries that are eligible to formally apply for assistance from the Millennium Challenge Account (MCA), announced the first threshold countries and—at this very moment—we are evaluating the first proposals and concept papers that have arrived from 13 of the 16 countries.

As the Committee is well aware, it was only on January 23rd of this year—with sustained bipartisan support—that MCC was established as a unique and innovative foreign assistance program. By establishing MCC, the United States Government has boldly (and generously) begun a new era in poverty reduction and sustainable development. Underlying all our efforts is a pronounced emphasis on policy reform. We believe that by providing incentives for countries to adopt policies for governing wisely, investing in their own people, and promoting economic freedom, we strengthen abroad the critical relationship between free market ideals and fundamental democratic principles that together form the “bedrock” of stable and responsible nations.

MCC is unique because it was deliberately designed to make U.S. aid more effective by linking increased foreign assistance to good governance and sound policies. We are innovative in several important respects: countries are selected based on their capacity to perform according to the stringent standards mandated by Congress; countries are also selected based on their ability to participate—as full partners—in the development process. This genuine partnership with selected countries means that they themselves will design programs—with MCC evaluation and guidance—that directly address the root causes of poverty; it means that the countries themselves

will seek to stimulate economic growth in those areas that they determine are most important.

Since January 23rd, MCC has set ambitious goals for itself, and then met them, moving as fast as legislation allowed. MCC legislation has a series of sequential requirements – naming candidate countries, publishing criteria and methodology for selection, and holding a public comment period – each followed by a waiting period before selection can take place. MCC opened its doors with only 7 staff members. I am both grateful and proud to inform the Committee that MCC has met—and in some cases surpassed—every one of these requirements. On May 6, MCC Board of Directors (Board) was able to select with confidence the first 16 countries eligible to submit proposals for MCC assistance; again, all of this activity took place as quickly as the current law would allow.

These 16 countries, which when combined represent more than 130 million people, were selected out of 63 of the poorest countries in the world. The selection was based on published criteria, including how well (or poorly) the 63 countries performed on 16 indicators developed and monitored by the World Bank Institute, Freedom House, and other entities independent of the U.S. government. MCC uses these 16 independently derived indicators to evaluate the policy performance of countries in terms of whether or not they are “governing justly, investing in their people, and encouraging economic freedom.”

Let me emphasize that the performance of the candidate countries on the sixteen policy indicators are completely transparent: any member of the Committee, any government staff, and—perhaps most important—any interested member of the public can look at our website (www.mcc.gov) and see how the candidate countries scored this year. In order to become candidates for fiscal year 2004, countries had to have an annual per capita income of under \$1,415 US dollars (the historic cutoff for the International Development Association), be eligible for assistance from IDA, and be eligible to receive U.S. assistance.

FY 2005 Selection Process:

MCC has already announced the names of the 71 candidate countries for fiscal year 2005. Because the MCA legislation no longer required that countries be eligible for IDA loans, the number of competing countries has

grown. We expect our Board to select 2005 Millennium Challenge Account (MCA) eligible countries before the end of the year, probably next month.

It is also important to point out that since the FY04 selection criteria and methodology were announced, MCC has received valuable public comment. These comments were taken into account during our review of the criteria for FY05. In a direct response to public comments, MCC replaced the Primary School Completion Rates indicator (for all students) with a Girls' Primary Completion Rates indicator. We made the change to emphasize clearly the proven importance of primary education for women in terms of poverty reduction and high economic return because data was now available to provide a measurable ranking. The second indicator change MCC made was to lower the ceiling inflation rate indicator from 20 to 15 percent in order to make the indicator a more meaningful test of a country's economic policies.

In addition to the two changes to the selection criteria for FY05, MCC will explore potential changes for the future, such as measuring a country's support for entrepreneurial activities, improved focus on investments in people, and the economic cost of trade barriers. Taking into account suggestions from the public and advice from Congress, MCC will also establish a working group to help identify—or promote the development of—an indicator to measure a country's policies as they affect its natural resources. The group will be chaired by MCC Board Member (former Governor of New Jersey, and most recently head of the Environmental Protection Agency) Christine Todd Whitman. This group will work with outside groups and experts to establish criteria and invite ideas for such an indicator.

Country Compacts:

Within weeks of the selection of the first round of MCC eligible countries in May, we had MCC teams on the road to visit the countries. Working together with USAID and our Embassies, we explained to a wide variety of groups in each nation that we want each country, through a consultative process with civil society and the private sector, to develop a Compact proposal -- which is essentially a plan that lays out country priorities and objectives for the use of MCA assistance to address barriers to poverty reduction and growth in the country. These proposals form the basis for discussions between MCC and the country on their priorities and, finally, for

negotiating a mutually agreeable Compact that includes plans for ensuring accountability, and clearly lays out the responsibilities of each partner.

As investors using US taxpayer dollars, we are not pushing any particular sector or project, but instead we seek to help these countries find the best investment opportunities for poverty reduction and growth. President Bush has requested \$2.5 billion for FY05. In an analysis earlier this year, the GAO estimated that, with a funding level of \$3.5 billion- the President's FY 2005 request plus FY 2004 enacted levels – the MCC could fully fund three-year Compacts in only 8 to 14 countries.

We will be looking at proposals we have received as investment opportunities. The return we want to see is poverty reduction and sustainable economic growth in the countries. We want to give them an opportunity to escape the cycle of dependency, and actively change the economic path of their country and part of our strategy is that this is best accomplished by allowing them to take ownership of the success of the program.

That means that the programs are about *our partner countries' priorities, their ideas, their activities, their policy reforms and compacts should* reflect the priorities and needs of the people of the country – not just the government – by placing a strong emphasis on civic and private sector participation in setting priorities and then implementing these priorities. This is why we have met with key individuals in each country – inside and outside of government – such as the private business sector, NGO's, and other organizations that have an important stake in the positive development of their nation.

We have advised countries that we would assess their proposals based on a number of criteria, including:

- the proposal's contribution to poverty reduction and economic growth;
- the breadth of public support within the country for the proposal; and
- the government's commitment to continued policy improvement.

We explained to them that MCA eligibility does not mean automatic entitlement to funding, and that MCC allocation and funding decisions will be driven by the quality of each country's proposal and their ability to

successfully implement the Compact as well as the Congressionally mandated criteria for a robust financial management plan so that US taxpayer money is optimally used.

We have been impressed with the efforts of MCA eligible countries so far and the innovative steps they have taken to ensure a broad based consultative process. Some countries have consulted NGO and business sectors for the first time. Mongolia is holding public meetings in all four corners of its large expanse. Armenia and Georgia have broadcast public meetings on national TV. One official from an MCA country said, “even if we receive less than requested, the intangibles gained from taking control of our own development destiny are the most important part of the process.” Indeed, we are finding that the process itself is an incentive for progress.

Just as important, when countries don’t achieve eligibility, the potential for qualification is a continuing incentive for them to make reforms and become eligible. One country passed four pieces of anti-corruption legislation and began enforcement. The stated reason: the hope of qualifying for MCA funding. And since the announcement of potential MCA indicators in February 2003, the median number of “days to start a business” dropped from 61 to 47 in MCA candidate countries.

Many countries decided to include additional parties in the consultation, and as a direct result of this increased participation they have achieved a much deeper analysis and more careful prioritization. They know this will lengthen the proposal development process, but they believe it will increase proposal quality and as well as its acceptance within the country.

The first country proposal reached MCC in mid-August and a number of MCA countries have now submitted proposals and concept papers. What we have seen in the proposals and concept papers thus far covers almost all areas linked to economic growth and poverty reduction: for example, education, water, micro-credit, rural development, infrastructure, and financial sector development. We have begun our due diligence processes. We are asking direct questions. What is the link to poverty reduction and growth? Who are the beneficiaries? How will you measure results? How do you rank your priorities? How will the proposal impact the environment? How does your proposal relate to what the government and other donors are doing? Will the money be well handled? Is procurement going to be fair and transparent?

As part of our due diligence process, we have already begun consultations with the United Nations, the World Bank, the UK's Department for International Development (DFID), Japan and other donors. We are doing analysis on the growth and poverty reduction potential among proposals. We are working closely with USAID, State and other USG departments to think through technical issues, to coordinate our activities, and to maximize the effectiveness of our assistance.

MCC anticipates that we will begin consulting with Congress about entering our first Compact negotiations in the near future, as prescribed in our legislation. This consultation will occur once MCC has conducted a thorough review of a country's proposal to determine whether there is a basis for conducting a more formal negotiation. We believe that due to our efforts as well as the efforts of the countries, that we will make significant progress on several proposals by the end of this year. My personal hope is that we could sign one or more Compacts by the end of the year. Let me be clear, however, MCC is not in the business of rushing funds out the door before it is satisfied that the proposed Compact will achieve real, measurable results.

Threshold Program:

As I emphasized earlier, underlying all MCC's efforts is the importance of incentivizing policy reform. In many ways, this is the challenge in the Millennium Challenge Account. But we don't just want to challenge these countries that are eligible, but also those countries that currently fall short on MCC indicators but are making efforts to reform. We believe this objective is enhanced by the Threshold Program.

The Board made the decision to set aside an initial pool of up to \$40 million dollars from fiscal year 2004 funds to go to the "Threshold" countries that are very close to qualifying and have demonstrated a commitment to undertake the policy reforms necessary to improve their growth conditions and their prospects for qualifying for the MCA. For FY 2004, the Board selected Albania, East Timor, Kenya, Sao Tome and Principe, Tanzania, Uganda, and Yemen to be invited to submit their proposals for improving their MCA indicators.

To encourage and support reform, we will be working closely with USAID to assist these “Threshold” countries with targeted programs that will help improve their policies so that they have better chance qualifying for MCA assistance. Moreover, such a program can help countries put in place the policies that provide the foundation for increasing productivity, reducing poverty, and moving toward more sustained economic growth. Distinct from the poverty reduction and economic growth programs that are MCC’s primary focus, the hope of qualification presents these countries with an opportunity to actively address and improve their performance on the policy indicators.

This type of reform requires leadership and commitment. Like MCC’s primary programs, the responsibility lies with the countries. If these countries want to undertake this challenge and opportunity – we will support their efforts. However, I want to make it clear that simply participating in this program will not guarantee eligibility for MCA assistance. Eligibility, with or without Threshold Program participation, will be judged by clearly measurable data and concrete efforts made by the governments.

Change will not be easy and will not soon be reflected in country scores. The policy areas where these countries will need to focus can only be changed with consistent effort and a high level of political commitment -- over a period of time.

Building on our strong working relationship with USAID, MCC will ask countries to submit their plans for reforming failing indicators and we will evaluate their final proposals based on political commitment, looking for specific actions that the government will undertake. MCC will soon post guidance on our website explaining the parameters for submitting such a proposal.

MCC has also increased its staffing and has developed detailed hiring plans to ensure that MCC will have the right number of people and skill sets to analyze proposals from both eligible countries and those in the Threshold Program. In less than nine months the number of staff has gone from 7 to 63 (which includes contractors) and we have sought to bring MCC the most highly qualified individuals, with diverse backgrounds and years of experience in government, private sector development, multilateral institutions, NGO’s, and higher education. I could continue speaking for a considerable length of time about our goals for specific departments, the

meticulous and frankly demanding way in which we are constructing the foundations of MCC. But perhaps your questions will allow me to address these subjects in detail.

In closing, Madagascar, one of our potential partners, has a population of 16.4 million people who, on average, earn less than 64 cents a day. These people live with hopes and aspirations for a better life that are as of yet unrealized. The Millennium Challenge Account exists to help them and others among the world's poorest countries to achieve their potential. MCA also exists because of a significant bipartisan consensus here in Congress that clearly recognizes the importance of effective and lasting global poverty reduction.

Through MCC we have the capability to carry that task forward – to do our part in creating a world of free and prospering nations.

And I believe that, together, we can do this by working closely with partner countries, by insisting on commitment and accountability, and by focusing on growth, nudging each nation toward a more flourishing, more stable future. And that will be a great good, for us all.

I thank the Committee for its attention and support. I would be glad to answer any questions you may have about MCC operations.