Center for Global Development

Initial Reactions to the Announcement on the MCA

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On November 25 the Bush administration announced new details for implementing the Millennium Challenge Account. Overall, the announced steps are very positive. They underscore the administration's commitment to making this new initiative work effectively, both in terms of full funding and in reorganizing the way that aid is delivered. The administration's fact sheet accompanying the announcement can be found at http://www.cgdev.org/nv/features_MCA.html

Country Selection

The method of choosing the countries is basically sound. The 16 indicators chosen are sensible, with some caveats. The data are publicly available and the methodology is relatively transparent. Experts could debate at the margins adding more variables (especially under "investing in people") and the value of some of the specific indicators, but these kinds of changes would have a relatively small impact on the countries actually chosen. The fact that countries need only to score in the top half on 8 of the 16 indicators to qualify means that the administration is not demanding that countries be purists in following a particular economic ideology. A preliminary analysis suggests that 11 countries (and perhaps 13) would be eligible during the first year, as shown in the accompanying table. There are as many as 4 others that would have qualified, except they were below the median on the corruption indicator (more on this below). Two of those countries (Benin and Lesotho) are eliminated because the do not have current data on corruption. However, data are likely to become available for those countries before MCA goes into effect. Both are likely to qualify, bringing the number of countries to 13.

It is important to note that in all probability, this list differs slightly from the administration's list because of differing data (one of us using more revised data than the other, etc). Moreover, this list could change in two ways. First, as new data become available and specific indicators are revised (which will

Possible Qualifying Countries
Albania
Bangladesh
Bolivia
The Gambia
Georgia
Honduras
Malawi
Mongolia
Nepal
Senegal
Sri Lanka
Eliminated by Corruption
Benin*
Lesotho*
Moldova
Nicaragua
*corruption data not available

certainly happen before the first countries are declared eligible), this list could change. Second, the administration has proposed that the MCA's Board of Directors can recommend to the President that the list of eligible countries be modified slightly to either remove some countries or add others under specified parameters. (This issue is explained in greater detail in the fact sheet). Some discretion makes sense, given the gaps, lags, and other weaknesses inherent in the data. Care must be taken, however, that this discretion is used very carefully and in only a very limited set of circumstances to guard against too much political influence in the selection process. By next week we will distribute a paper with a more complete analysis of the process of choosing countries for the MCA.

Ownership

The emphasis put on country ownership during the briefing was encouraging. Although there was nothing on this issue in the fact sheet or the public announcements, it appears that the administration is leaning towards a system in which eligible countries would write proposals (or business plans) describing their objectives and strategy, how they would use the money, the benchmarks used for evaluation. Giving recipient countries this responsibility is a revolutionary change in US foreign assistance.

Organization

An independent government corporation is a suitable home for the MCA. Both the oversight board (chaired by the Secretary of State) and the plan to staff the corporation with personnel from a variety of both government and non-government agencies will strengthen its operations. The biggest advantage of the new corporation is that it can avoid being bogged down by political pressures, bureaucratic procedures and multiple congressional mandates that ultimately weaken other agencies such as USAID.

Concerns

While the overall direction of the MCA is very positive and deserving of support, I have three concerns. First, I am not persuaded by the proposal to include lower-middle income countries with incomes between $1,435 and $2,975 starting in the third year. These countries have access to private capital flows, IBRD loans, and other sources of financing that are not available to the poorest countries. While many of these countries have large populations of poor people, their needs are not nearly as great as the low-income countries, and they have more options to address the problem. It seems to me that the US should continue to provide those countries with foreign assistance through traditional channels, but not through the MCA. The simple truth is that as more countries in this income range become eligible, there will be fewer MCA funds available for the poorest countries that are implementing sound development strategies.

Second, the criterion that a country must score above the median on the corruption indicator raises some statistical difficulties. Corruption scores are based on survey data, and survey results are always estimated with margins of error. The corruption indicator used by the administration is the best available, and is compiled in a way to minimize the

margins of error, but errors remain.[1] The problem is that for a country with an *observed* score just below the median, we cannot be certain that its *actual* corruption level is below the median. Margins of error could be the difference between qualifying and not qualifying for some countries. Although I have great sympathy for a high standard on corruption, the make-or-break requirement may unnecessarily eliminate some countries.

Third, the separation of US foreign assistance into two agencies could lead to a lack of coordination and overlapping functions. The new agency could also draw staff and resources from USAID. More broadly, while the MCA is a major step in the right direction, it is only one component of a complete foreign assistance strategy. Still lacking is a sound strategy to work in the "second tier" countries that don't quite qualify for the MCA, a strategy to work in weaker countries, and a strategy to work in countries in conflict and failed states. Importantly, the administration stills lacks a clear strategy for fighting the HIV/AIDS pandemic. The introduction of the MCA provides USAID with the opportunity to redefine itself with a strong role in confronting these issues.

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[1] The corruption indicator (and four other variables used as selection criteria) are compiled by Daniel Kauffman, Art Kraay, and Pablo Zoido-Lobatón at the World Bank Institute and are available at http://www.worldbank.org/wbi/governance.