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Promoting Economic Prosperity Through the Millennium Challenge Account

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The United States has demonstrated considerable dedication to promoting economic development in sub-Saharan Africa. America has provided about $48 billion (in 2003 dollars) in bilateral official development assistance to sub-Saharan Africa since 1960.[1]

Under President George W. Bush, America has doubled its development assistance to $19 billion in 2004, including tripling its assistance to sub-Saharan Africa since 2000. It has expanded access to the U.S. market through the African Growth and Opportunities Act. The U.S. is the world's largest humanitarian aid donor, providing $3.3 billion in 2003. The U.S. is the world's largest source of bilateral and multilateral support to combat HIV/AIDS, malaria, and other infectious diseases, including $2.4 billion in international HIV/AIDS programs.[2]

Yet the U.S. is often criticized for not providing enough resources for development. The basis for this criticism is the theory that if only aid flows increased, developing countries would achieve economic growth and development. Economic analysis and the historical record do not support this reasoning.

The United States and other donor nations have spent over $2.2 trillion on bilateral and multilateral development assistance (in 2003 dollars) since 1960 to help poor countries attain economic growth and prosperity—about a fourth of it in sub-Saharan Africa.[3] Few recipients have achieved substantial improvements in per capita income, and in no case has a development success story been clearly attributable to economic assistance. The evidence provided by numerous studies

Talking Points

- The lessons from nearly five decades indicate that, while there may be a role for assistance and donor nations, the key to development lies in the hands of governments in developing countries.
- For development to occur, governments must remove obstacles preventing their people from seizing opportunities to benefit them, their families, and their communities. This is best done by adopting policies consistent with free markets and the rule of law that are the key to economic growth and development.
- By focusing on countries that are committed to policies conducive to economic growth and development, the MCA sends the right message that developing countries cannot be passive in development, but must undertake reform to make it possible. The MCA captures the nature of this partnership by creating incentives for poor nations to adopt economic freedom, the rule of law, and good governance.

This paper, in its entirety, can be found at:
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indicates that this failure is due not to insufficient funds, but to the poor policies of recipient countries.

Taking lessons from this experience, in 2002, the Bush Administration proposed a new development assistance program—the Millennium Challenge Account (MCA)—for countries "ruling justly, investing in their people, and encouraging economic freedom."[4] The MCA is different from previous aid programs because recipients earn eligibility by surpassing minimum criteria based on simple, transparent, and publicly available performance indicators. These indicators have been selected based on evidence that they contribute or are complementary to long-term growth and prosperity, rather than on subjective, political motivations unrelated to development.

This approach to development emphasizes that a successful strategy requires commitment to good policy by developing countries. Aid cannot overcome anti-market economic policies, bad governance, and a weak rule of law. By focusing MCA resources on countries that have demonstrated commitment to reform in these areas, the U.S. is encouraging policy change among recipients and increasing the likelihood of improved economic growth and development.

The Disappointing History of Development Assistance

Sub-Saharan Africa is the only region of the world that is not on track to meet a single target of the U.N. Secretariat's indicators for achieving the Millennium Development Goals (MDGs), including reducing poverty, hunger, and infant mortality; improving secondary school enrollment for girls; increasing immunization; and increasing access to potable water.[5]

Meeting the development goals—and, more important, creating the ability for countries to continue progress already made toward these goals—depends in great part on increasing economic growth. Indeed, the World Bank estimated that halving severe poverty in sub-Saharan Africa by 2015 would require annual growth of at least 7 percent. Focusing on improving particular indicators may offer paths for foreign assistance to provide short-term relief of suffering in specific areas, but it will do little to help poor countries achieve the economic growth necessary for them to develop and graduate from the need for assistance in the first place.[6]

For decades, the United States and other donor nations have tried to catalyze economic growth in poor countries through bilateral and multilateral development assistance. The record is one of failure. Between 1960 and 2003, the U.S. and other developed nations spent over $2.2 trillion (in 2003 dollars)[7] in bilateral and multilateral aid on development projects in low-income and lower-middle-income countries.[8]

Of the 111 countries for which data are available, 35 (about one-third) actually saw their per capita income shrink (in 2000 dollars) despite over four decades of development assistance. In other words, their populations became poorer than they

1. Organisation for Economic Co-operation and Development, *International Development Statistics*.
2. U.S. Department of State, "The U.S. Approach to International Development: Building on the Monterrey Consensus," September 12, 2005, at *www.state.gov/r/pa/scp/2005/53037.htm*.
3. Organisation for Economic Co-operation and Development, *International Development Statistics*.
4. "President Proposes $5 Billion Plan to Help Developing Nations," Remarks by President George W. Bush on Global Development, White House, Office of the Press Secretary, March 14, 2002, at *www.whitehouse.gov/news/releases/2002/03/20020314-7.html*.
5. "Ends Without Means," *The Economist*, September 11, 2004, p. 72.
6. Indeed, nearly every country in sub-Saharan Africa improved in life expectancy, literacy, maternal mortality, and infant mortality (all of which are MDG indicators) from 1970 to 1990. Yet few countries experienced increased economic growth and development. World Bank, *World Development Indicators 2005*.
7. Organisation for Economic Co-operation and Development, *International Development Statistics*, at *www.oecd.org/dataoecd/50/17/5037721.htm* (September 14, 2005), and World Bank, *World Development Indicators 2005*, at *www.worldbank.org/data/onlinedatabases/onlinedatabases.html* (September 14, 2005; subscription required).

were in 1960. Another 26 countries experienced slight compound annual growth in per capita gross domestic product (GDP) of less than 1 percent, and a further 25 saw slightly better compound annual growth in per capita GDP between 1 percent and 2 percent. Just 25 experienced annual compound growth of more than 2 percent in per capita GDP, and only 11 of the 25 experienced the level of growth necessary (over 4 percent annual growth) to noticeably close the gap with rich nations.

The record is particularly poor in sub-Saharan Africa. Despite $543 billion (in 2003 dollars; see Table 2) in assistance between 1960 and 2003, including $47.7 billion from the U.S., sub-Saharan Africa's per capita income increased from $416 to only $514 (in 2000 dollars).[9] Some have argued that this lack of growth is due to a paucity of aid and call for a "Marshall Plan" for Africa modeled after the effort to rebuild post–World War II Europe.

But an objective look at the Marshall Plan reveals that, in terms of aid to GDP, sub-Saharan Africa has received a Marshall Plan several times over. As shown in Table 1, the United Kingdom was the largest single recipient of Marshall Plan assistance, receiving the equivalent of 20 percent of its 1950 GDP in assistance between 1946 and 1952 (in constant 1950 dollars). The largest single annual disbursement in 1947 was equivalent to 11.5 percent of its GDP in 1950.[10] In 2003, 21 countries in sub-Saharan Africa received more assistance in relation to their GDP than the U.K. did in 1947. Only South Africa and Nigeria received less aid between 1960 and 2003 as a percent of its 2003 GDP than the U.K. did under the Marshall Plan. Most received aid equivalent to several times their 2003 GDP.

Despite this assistance, sub-Saharan Africa has been treading water, with one-third of countries experiencing a net decline in their per capita GDP since 1960. To put this in perspective, if all of the aid spent over those four decades were gathered together in today's dollars and simply handed out to the 719 million people of sub-Saharan Africa, per capita GDP would increase by over $756—more than doubling its current per capita GDP. If just the $23.7 billion (in current dollars) in aid provided to the region in 2003 were handed out, per capita income would increase by $33.

Clearly, aid has not been invested in a manner that results in greater economic growth. Chart 1 illustrates the provision of economic assistance to sub-Saharan Africa and the region's erratic growth record.

Over the past decade, economic studies have concluded that economic freedom, good governance, and the rule of law are key drivers in promoting economic growth and reducing poverty. A 1997 World Bank analysis of foreign aid found that, while assistance positively affects growth in

8. This figure actually understates external contributions to development by ignoring private-sector contributions to development. This oversight not only dramatically underestimates development resources, but also ignores the most effective resources. As observed in the U.S. Institute of Peace's *American Interests and UN Reform*, "Most resources for economic development and sustainable poverty reduction come through trade, private financial flows, international charitable organizations and expatriate remittances. The 0.7 percent of GDP target would be more meaningful if other contributions relevant to development were incorporated into this calculation, including private charitable donations." Using such a calculation, the U.S. Agency for International Development estimates that total U.S. assistance to developing countries may have been five times its official development assistance in 2000. Other efforts to measure contributions to development, such as the Commitment to Development Index, which ranks the U.S. twelfth out of 21 nations, similarly portray U.S. contributions more positively than a simple measure of government assistance as a percentage of GNP. See U.S. Institute of Peace, *American Interests and UN Reform: Report of the Task Force on the United Nations* (Washington, D.C.: U.S. Institute of Peace, 2005), p. 107, at *www.usip.org/un/report/usip_un_report.pdf* (September 14, 2005); U.S. Agency for International Development, *Foreign Aid and the National Interest: Promoting Freedom, Security, and Opportunity* (Washington, D.C.: U.S. Agency for International Development, 2002), p. 131, Table 6.1, at *www.usaid.gov/fani/Full_Report--Foreign_Aid_in_the_National_Interest.pdf* (September 14, 2005); and Center for Global Development, *Commitment to Development Index*, at *www.cgdev.org/section/initiatives/_active/cdi* (September 14, 2005).

9. Organisation for Economic Co-operation and Development, *International Development Statistics*, at *www.oecd.org/dataoecd/50/17/5037721.htm* (September 14, 2005), and World Bank, *World Development Indicators 2005*, at *www.worldbank.org/data/onlinedatabases/onlinedatabases.html* (September 14, 2005; subscription required).

10. GDP data before 1950 were not available or were subject to question. GDP data for the other Marshall Plan recipients were not available. This is unlikely to change the overall picture, however, as France, Germany, and the U.K. were by far the largest recipients of Marshall Plan funds.

Table 1 HL 920

Aid Under the Marshall Plan

Country	Aid from 1946 to 1952 (millions 2003 dollars)	The Largest Single Year of Marshall Plan Aid (millions 2003 dollars) *	Aid from 1946 to 1952/GDP in 1950 **	Largest Single Year of Marshall Plan Aid Disbursements/GDP in 1950 ***
France	$22,333	$8,397	12.0%	4.5%
Germany	$25,205	$8,041	16.8%	5.4%
United Kingdom	$48,103	$27,201	20.3%	11.5%

Notes: *1949 for France and Germany. 1947 for the United Kingdom. ** and *** The ratio beween aid and GDP was computed by using constant 1950 data. Aid data in constant 2003 dollars were deflated to constant 1950 dollars.

Sources: Aid data for Marshall Plan countries: U.S. Agency for International Development, Greenbook, available at *http://qesdb.cdie.org/gbk/index.html*; 1950 GDP data for Marshall Plan countries were computed by using 1950 GDP data in national currency and 1950 exchange rates from the International Monetary Fund's *International Financial Statistics*, available at *http://ifs.apdi.net/imf/logon.aspx* by subscription.

countries with good economic policies (free markets, fiscal discipline, and the rule of law), countries with poor economic policies did not experience sustained economic growth regardless of the amount of foreign assistance received.[11]

Other studies have reached similar conclusions, maintaining that aid can increase economic growth in certain circumstances.[12] These studies conclude that aid may help the poor to cope temporarily with some of the consequences of poverty, but that countries beset by a weak rule of law, corruption, heavy state intervention, and other policies that retard growth will not experience increased economic growth even with greater amounts of economic assistance. Subsequent studies question whether aid could spur growth even in good policy environments.[13]

Yet many advocates of aid ignore this research and evidence. The U.N. Millennium Project, commissioned by U.N. Secretary-General Kofi Annan in 2002 to assess what is necessary to meet the MDGs, advocated "a big push of basic investments between now and 2015 in public administration, human capital (nutrition, health, education), and key infra-

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11. Craig Burnside and David Dollar, "Aid, Policies, and Growth," World Bank, Policy Research Department, Macroeconomic and Growth Division, June 1997, and World Bank, *Assessing Aid: What Works, What Doesn't, and Why* (Washington, D.C.: World Bank, 1998).

12. Other studies arrive at similar conclusions. For example, economists Richard Roll and John Talbott support this conclusion with evidence that the economic, legal, and political institutions of a country explain more than 80 percent of the international variation in real per capita income between 1995 and 1999 in more than 130 countries. Richard Roll and John Talbott, "Developing Countries That Aren't," unpublished manuscript, University of California at Los Angeles, November 13, 2001, p. 3. Other comparable studies include Paul Collier and Jan Willem Gunning, "Why Has Africa Grown Slowly?" *Journal of Economic Perspectives*, Vol. 13, No. 3 (September 1999), pp. 3–22; Robert J. Barro and Xavier Sala-i-Martin, *Economic Growth* (New York: McGraw-Hill, 1995); Jeffrey D. Sachs and Andrew Warner, "Economic Reform and the Process of Global Integration," in William C. Brainard and George L. Perry, *Brookings Papers on Economic Activity, 1995* (Washington, D.C.: Brookings Institution Press, 1995), pp. 1–118; and David Dollar, "Outward-Oriented Developing Economies Really Do Grow More Rapidly: Evidence from 95 LDCs, 1976–1985," *Economic Development and Cultural Change*, Vol. 40, No. 3 (April 1992), pp. 523–544.

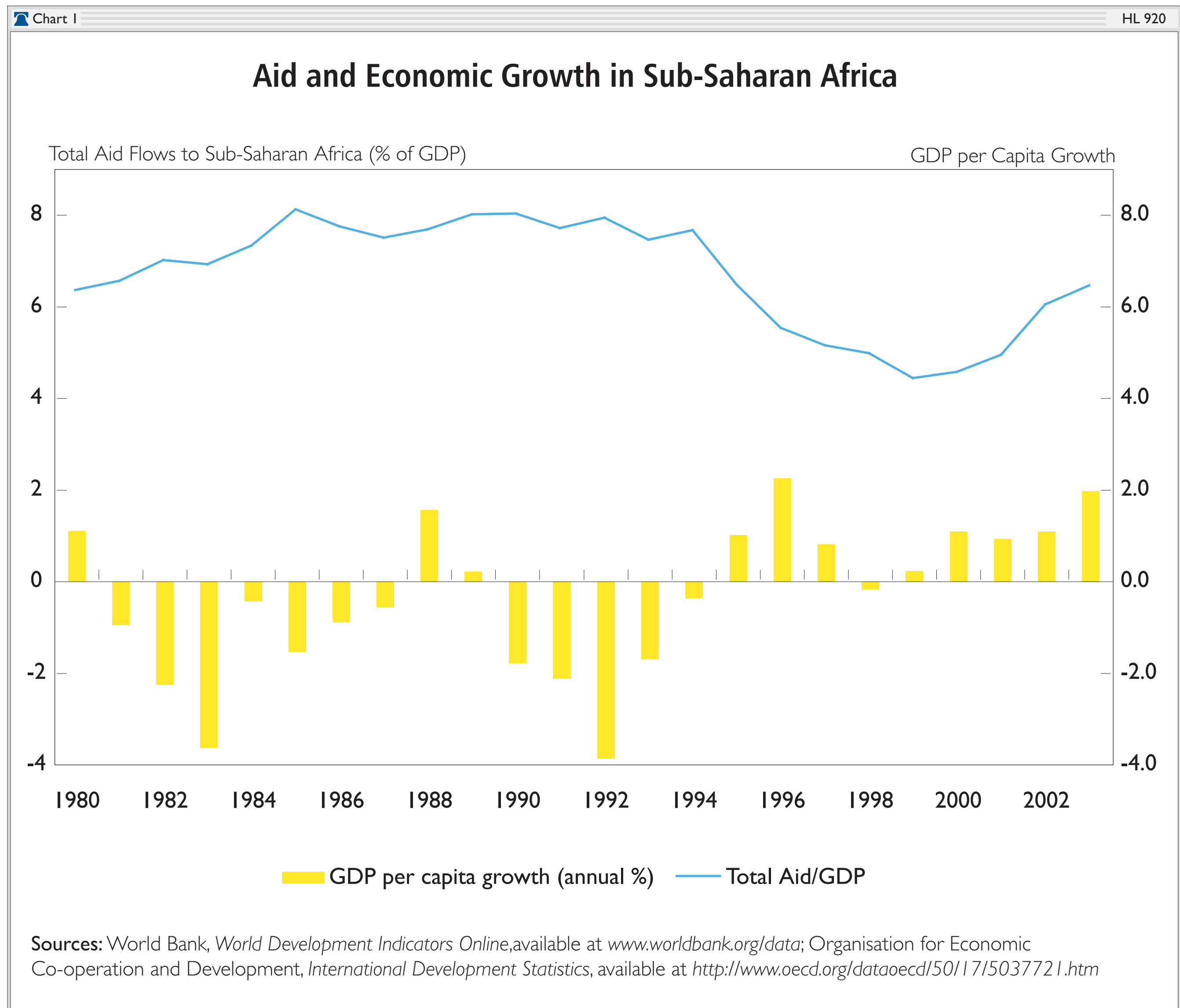
13. William Easterly, "Can Foreign Aid Buy Growth?" *Journal of Economic Perspectives*, Vol. 17, No. 3 (Summer 2003), pp. 23–48, at *www.nyu.edu/fas/institute/dri/Easterly/File/EasterlyJEP03.pdf* (September 21, 2005).

Table 2 HL 920

Total ODA to Africa 1960 to 2003

Country	Total Net Official Development Assistance from 1960 to 2003 (millions 2003 dollars)	Total Net Official Development Assistance in 2003 (millions 2003 dollars)	Total Net Official Development Assistance 1960 to 2003 /GDP in 2003	2003 Net ODA/GDP in 2003	Compound Growth Rate in Per Capita GDP 1980 to 2003
Angola	$8,218	$497	59.4%	3.6%	(0.56)
Benin	$7,880	$293	221.5%	8.2%	0.80
Botswana	$5,430	$28	72.1%	0.4%	6.31
Burkina Faso	$13,734	$454	328.4%	10.9%	1.26
Burundi	$7,524	$224	1263.5%	37.6%	0.21
Cameroon	$17,211	$884	137.8%	7.1%	0.76
Cape Verde	$3,436	$143	430.9%	18.0%	3.33
Central African Rep.	$6,161	$50	512.2%	4.1%	(0.96)
Chad	$8,662	$247	332.1%	9.5%	(0.33)
Comoros	$2,065	$24	647.4%	7.7%	(0.61)
Congo Dem.Rep. (Zaire)	$29,875	$5,381	526.8%	94.9%	(3.02)
Congo, Rep.	$6,223	$70	174.6%	2.0%	0.99
Ivory Coast	$19,095	$252	136.7%	1.8%	0.27
Djibouti	$4,115	$78	658.4%	12.4%	(3.95)
Equatorial Guinea	$1,030	$21	35.3%	0.7%	9.34
Eritrea	$2,194	$307	292.3%	40.9%	2.11
Ethiopia	$28,115	$1,506	422.7%	22.6%	(0.04)
Gabon	$4,189	-$11	69.2%	-0.2%	1.99
Gambia	$2,850	$63	777.7%	17.1%	0.52
Ghana	$19,076	$907	250.2%	11.9%	(0.04)
Guinea	$8,824	$238	243.1%	6.6%	1.30
Guinea-Bissau	$3,522	$145	1475.7%	60.8%	(0.83)
Kenya	$27,178	$485	189.1%	3.4%	1.10
Lesotho	$4,781	$78	444.1%	7.2%	3.71
Liberia	$5,575	$107	1260.8%	24.2%	(3.96)
Madagascar	$14,789	$538	270.2%	9.8%	(1.18)
Malawi	$14,416	$498	847.4%	29.3%	1.14
Mali	$16,012	$527	368.4%	12.1%	0.87
Mauritania	$10,485	$239	886.7%	20.2%	1.42
Mauritius	$2,314	-$15	44.1%	-0.3%	4.35
Mozambique	$25,503	$1,034	590.3%	23.9%	1.66
Namibia	$2,611	$147	61.1%	3.4%	(0.28)
Niger	$13,207	$453	483.5%	16.6%	(1.36)
Nigeria	$10,558	$318	18.3%	0.6%	0.48
Rwanda	$12,050	$332	715.6%	19.7%	0.16
Sao Tome & Principe	$1,048	$38	1758.9%	63.2%	(0.27)
Senegal	$21,509	$446	331.7%	6.9%	(0.10)
Seychelles	$1,138	$9	161.9%	1.3%	n/a
Sierra Leone	$5,579	$301	563.6%	30.4%	(1.02)
Somalia	$16,873	$175	n/a	n/a	n/a
South Africa	$5,530	$625	3.3%	0.4%	0.85
Sudan	$27,178	$617	152.8%	3.5%	0.95
Swaziland	$2,575	$28	135.2%	1.5%	1.91
Tanzania	$38,145	$1,669	370.5%	16.2%	1.26
Togo	$6,094	$47	346.5%	2.6%	1.03
Uganda	$17,719	$959	281.4%	15.2%	2.20
Zambia	$21,130	$565	487.4%	13.0%	(0.92)
Zimbabwe	$10,038	$186	56.6%	1.0%	0.26
SUM or AVERAGE	$543,461	$22,210	423.3%	15.0%	0.72

Sources: ODA data from Organisation for Economic Co-operation and Development, *International Development Statistics*, available at *http://www.oecd.org/dataoecd/50/17/5037721.htm*; GDP data for Sub-Saharan countries from World Bank's *World Development Indicators Online*, available at *https://publications.worldbank.org/subscriptions/WDI/* by subscription



Sources: World Bank, *World Development Indicators Online*,available at *www.worldbank.org/data*; Organisation for Economic Co-operation and Development, *International Development Statistics*, available at *http://www.oecd.org/dataoecd/50/17/5037721.htm*

structure (roads, electricity, ports, water and sanitation, accessible land for affordable housing, environmental management)."[14] Jeffrey Sachs, special adviser to the U.N. Secretary-General on global poverty, reaches similar conclusions in *The End of Poverty*, which asserts that developed countries must transfer "about $100 [billion] to $180 billion per year for the period 2005 to 2015" to meet the MDGs and that "Africa needs around $30 billion per year in aid in order to escape from poverty."[15]

Two recent economic studies, however, dismantle the arguments used by Sachs and the U.N. for increased aid. Former World Bank economist William Easterly specifically analyzed the evidence on whether increased aid or investment can spur growth:

> The classic narrative—poor countries caught in poverty traps, out of which they need a Big Push involving increased aid and investment, leading to a takeoff in per capita

14. U.N. Millennium Project, *Overview Report*, 2005, p. 19, at *www.unmillenniumproject.org/reports/index_overview.htm* (September 21, 2005).

15. Jeffery D. Sachs, *The End of Poverty: Economic Possibilities for Our Time* (New York: Penguin Press, 2005), pp. 298–300 and 309.

> income—has been very influential in development economics. This was the original justification for foreign aid…. *Evidence to support the narrative is scarce*…. Takeoffs are rare in the data, most plausibly limited to the Asian success stories. Even then, the takeoffs do not seem strongly associated with aid or investment in the way the standard Big Push narrative would imply.[16]

A 2005 study by two economists at the International Monetary Fund (IMF) corroborates this conclusion. Their research found "no evidence that aid works better in better policy or geographical environments, or that certain forms of aid work better than others."[17] The same authors published a subsequent study that concluded:

> We examine one of the most important and intriguing puzzles in economics: why it is so hard to find a robust effect of aid on the long-term growth of poor countries, even those with good policies…. We find that aid inflows have systematic adverse effects on a country's competitiveness, as reflected in a decline in the share of labor intensive and tradable industries in the manufacturing sector. We find evidence suggesting that these effects stem from the real exchange rate overvaluation caused by aid inflows. By contrast, private-to-private flows like remittances do not seem to create these adverse effects….[18]

A Better Strategy for Development. This does not mean that development is an unreachable goal. A World Bank study found that increased integration into the world economy from the late 1970s to the late 1990s led to higher growth in income. The more integrated countries achieved 5 percent average annual growth in per capita income during the 1990s.[19] In contrast, the non-globalizing nations experienced average growth of only 1.4 percent during the 1990s, and many experienced negative growth rates.

A related World Bank study found that increased growth resulting from expanded trade "leads to proportionate increases in incomes of the poor" and that "globalization leads to faster growth and poverty reduction in poor countries."[20] Easterly concurs in his 2005 study, finding "support for democratic institutions and economic freedom as determinants of growth that explain the occasions under which poor countries grow more slowly than rich countries."[21]

These studies support research at The Heritage Foundation. Analysis of 11 years of *Index of Economic Freedom* data[22] indicates that the best way for countries to increase economic growth is to adopt policies that promote economic freedom and the rule of law. The *Index* analyzes 50 economic indicators in 10 independent factors: trade policy, fiscal burden of government, government

16. William Easterly, "Reliving the 50s: The Big Push, Poverty Traps, and Takeoffs in Economic Development," Northwestern University, Kellogg School of Management seminar, June 1, 2005, at *www.kellogg.northwestern.edu/finance/faculty/seminars/easterly_william.pdf* (September 21, 2005). Emphasis added.

17. Raghuram G. Rajan and Arvind Subramanian, "Aid and Growth: What Does the Cross-Country Evidence Really Show?" National Bureau of Economic Research *Working Paper* No. 11513, abstract, July 2005, at *papers.nber.org/papers/w11513* (September 14, 2005).

18. Raghuram G. Rajan and Arvind Subramanian, "What Undermines Aid's Impact on Growth?" National Bureau of Economic Research *Working Paper* No. 11657, abstract, October 2005, at *www.nber.org/papers/w11657*.

19. Paul Collier and David Dollar, *Globalization, Growth, and Poverty: Building an Inclusive World Economy* (Washington, D.C.: World Bank and Oxford University Press, 2001), p. 5.

20. David Dollar and Aart Kraay, "Trade, Growth, and Poverty," World Bank, Development Research Group, abstract of draft, March 2001, at *www.worldbank.org/research/growth/pdfiles/Trade5.pdf* (September 14, 2005).

21. Easterly, "Reliving the 50s," p. 29.

22. See Marc A. Miles, Edwin J. Feulner, and Mary Anastasia O'Grady, *2005 Index of Economic Freedom* (Washington, D.C.: The Heritage Foundation and Dow Jones & Company, Inc., 2005), at *www.heritage.org/index* (September 21, 2005).

intervention in the economy, monetary policy, capital flows and foreign investment, banking and finance, wages and prices, property rights, regulation, and informal market activity. These 10 factors are graded from 1 to 5, with 1 being the best score and 5 being the worst. The scores are then averaged to give an overall score for economic freedom. Countries are designated "free," "mostly free," "mostly unfree," or "repressed" based on their overall scores.

As shown in the *Index*, "free" countries have an average per capita income twice that of "mostly free" countries. "Mostly free" countries have a per capita income more than three times that of "mostly unfree" and "repressed" countries. This relationship exists because countries that maintain policies that promote economic freedom provide an environment that facilitates trade and encourages entrepreneurial activity, which in turn generates economic growth. Not only is a higher level of economic freedom clearly associated with a higher level of per capita GDP, but higher GDP growth rates are associated with improvements in a country's economic freedom score.[23]

Charts 2 and 3 illustrate that this relationship holds for sub-Saharan Africa.[24]

Origins of the MCA

The evident inadequacy of development assistance in catalyzing economic growth and development led the Bush Administration to propose the Millennium Challenge Account. The MCA is an attempt to learn from the development failures of the past by targeting assistance toward low-income and lower-middle-income countries with a demonstrable record of embracing policies linked to stronger growth. As noted by Ambassador John Bolton:

> In Monterrey, Mexico in 2002, we all made commitments to fight poverty through development. We agreed that we had to change the models of the past, which focused primarily on resource transfers, to solutions premised on the proven methods of good governance, sound policies, the rule of law, and mobilization of both public and private resources.[25]

The MCA is designed to show countries how to enhance their prospects for economic growth and development with the overarching goal of helping countries graduate from the need for foreign assistance.

How Does the MCA Work? While disagreement remains over the effectiveness of aid, there is general agreement that aid is far less effective in bad policy environments and can prove counterproductive. The Millennium Challenge Corporation (MCC), which runs the MCA, seeks to maximize chances that aid will be used positively by focusing resources on countries with good policies. Under the MCA, nations are eligible to receive assistance only if they adopt policies associated with improved economic growth.

To capitalize on this evidence, the Administration identified three policy areas—good governance, investment in health and education, and promoting economic freedom—and 16 performance indicators that measure these areas. (See text box, "MCA Criteria.")

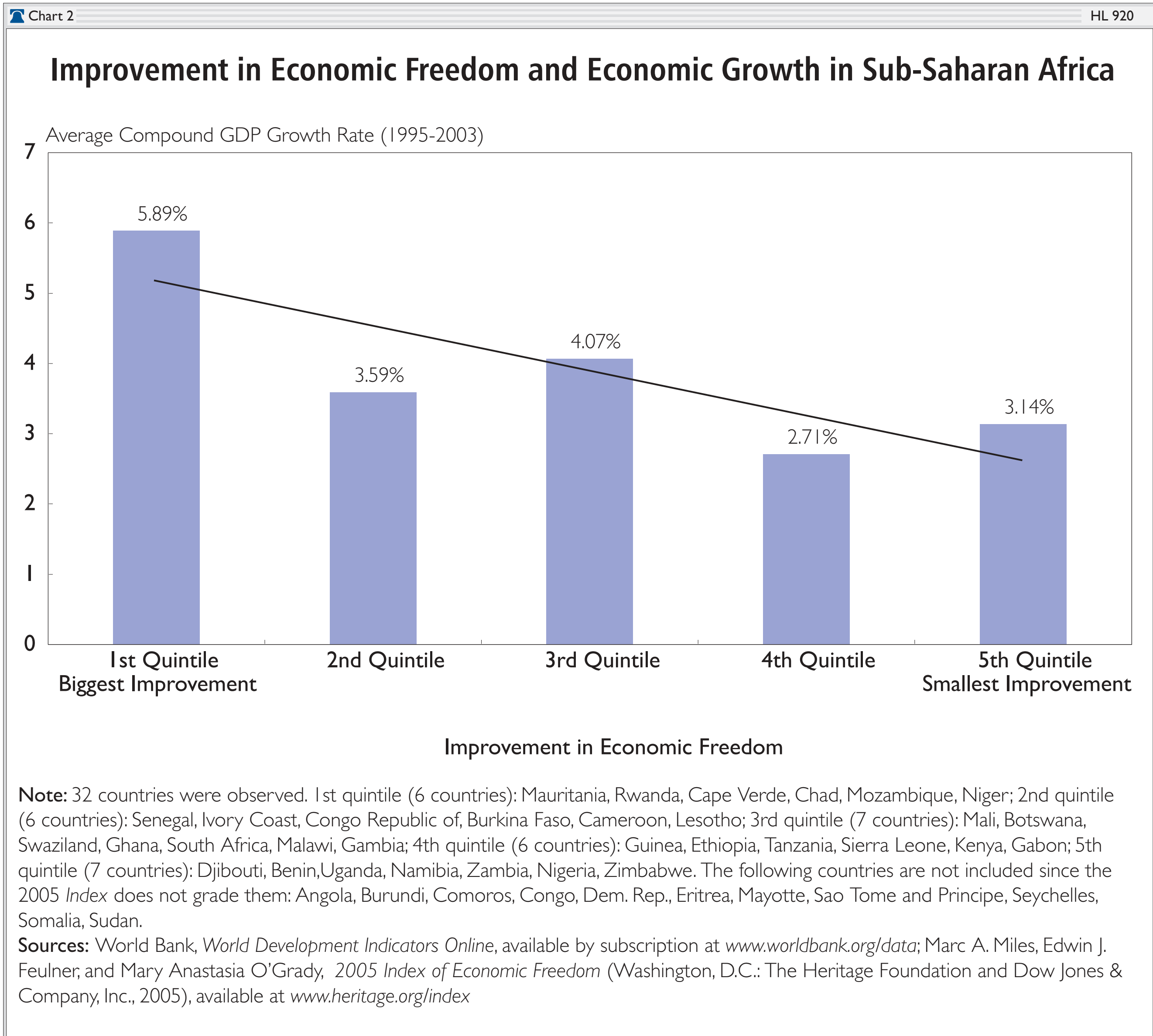
To qualify for the MCA, a country must score above the median[26] for half of the indicators in each policy area—that is, it must be above the median in at least three of the six performance indicators that measure good governance, two of the four that measure investment in people, and three of the six that measure economic freedom. It must also be within specified income levels.[27] The Bush

23. Marc A. Miles, "Introduction," in Marc A. Miles, Edwin J. Feulner, and Mary Anastasia O'Grady, *2004 Index of Economic Freedom* (Washington, D.C.: The Heritage Foundation and Dow Jones & Company, Inc., 2004), p. 21.

24. There are no "free" economies in sub-Saharan Africa, although Botswana ranks among the 40 freest economies and continues to improve steadily.

25. John Bolton, U.S. Ambassador to the U.N., open letter on the draft outcome document, August 30, 2005, at *www.un.int/usa/ reform-un-jrb-ltr-dev-8-05.pdf* (September 14, 2005).

26. The median for each indicator is calculated from the indicator values for all countries in the same per capita income group.

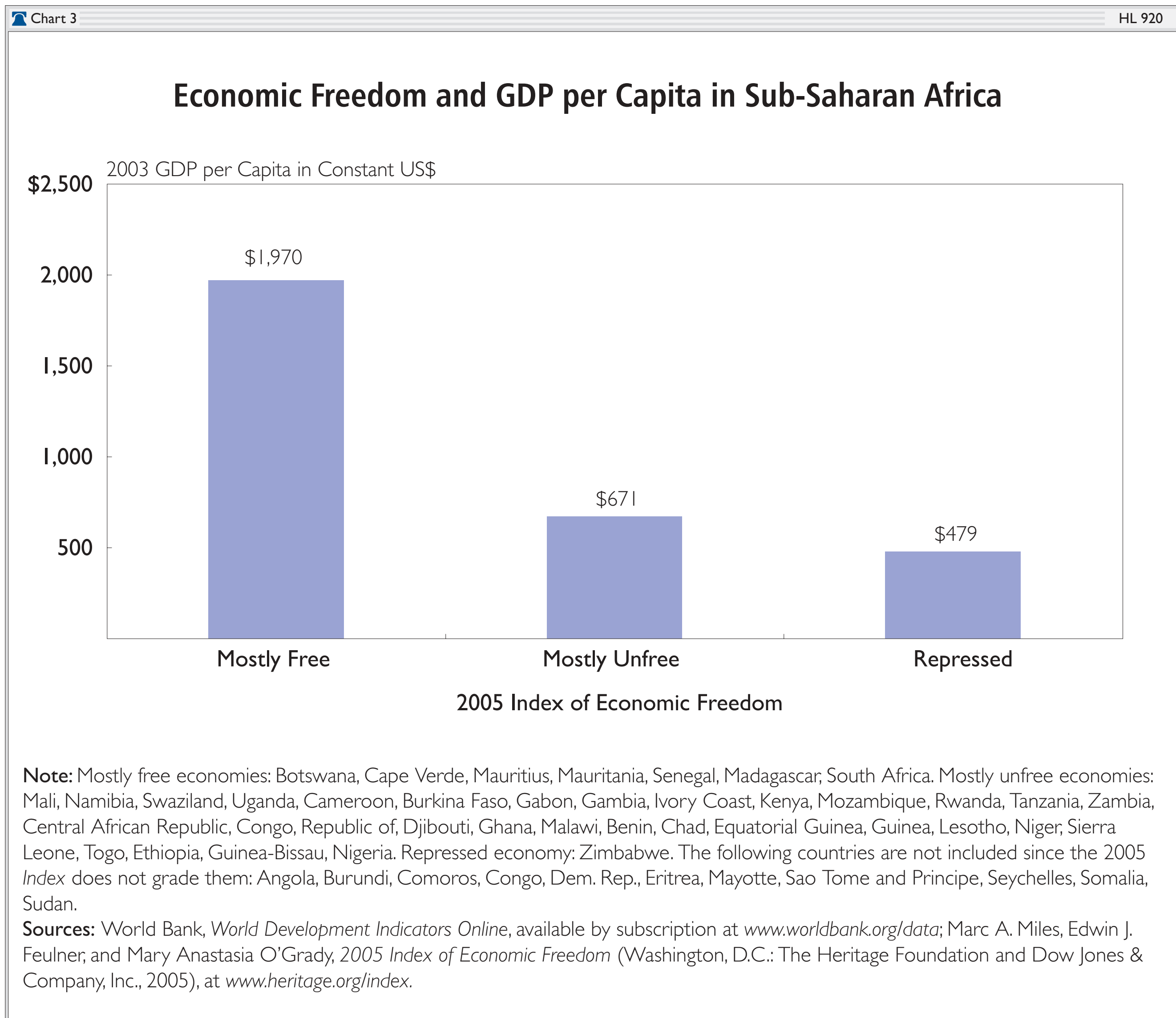


Note: 32 countries were observed. 1st quintile (6 countries): Mauritania, Rwanda, Cape Verde, Chad, Mozambique, Niger; 2nd quintile (6 countries): Senegal, Ivory Coast, Congo Republic of, Burkina Faso, Cameroon, Lesotho; 3rd quintile (7 countries): Mali, Botswana, Swaziland, Ghana, South Africa, Malawi, Gambia; 4th quintile (6 countries): Guinea, Ethiopia, Tanzania, Sierra Leone, Kenya, Gabon; 5th quintile (7 countries): Djibouti, Benin,Uganda, Namibia, Zambia, Nigeria, Zimbabwe. The following countries are not included since the 2005 *Index* does not grade them: Angola, Burundi, Comoros, Congo, Dem. Rep., Eritrea, Mayotte, Sao Tome and Principe, Seychelles, Somalia, Sudan.
Sources: World Bank, *World Development Indicators Online*, available by subscription at *www.worldbank.org/data*; Marc A. Miles, Edwin J. Feulner, and Mary Anastasia O'Grady, *2005 Index of Economic Freedom* (Washington, D.C.: The Heritage Foundation and Dow Jones & Company, Inc., 2005), available at *www.heritage.org/index*

Administration also has determined that countries must pass the "control of corruption" indicator to qualify.[28] In addition, the MCC has identified "threshold" countries that do not meet MCA criteria but are eligible for MCA assistance in a limited manner based on their commitment to "the reforms necessary to improve policy performance and eventually qualify for MCA assistance."[29]

The MCA is a departure from traditional development assistance. Recipient countries possess an

27. For fiscal year 2006, low-income countries with a per capita gross national income of $1,575 or less and lower-middle-income countries with a per capita GNI between $1,575 and $3,255 or less are eligible for MCA assistance. In previous years, only low-income countries were considered. The median scores for each income group will be computed separately. For FY 2006 there were 69 low-income countries and 29 lower-middle-income countries identified as candidates for MCA grants. Millennium Challenge Corporation, "Report on Countries That Are Candidates for Millennium Challenge Account Eligibility in Fiscal Year 2006 and Countries That Would Be Candidates But For Legal Prohibitions," at *www.mca.gov/countries/candidate/FY06_candidate_report.pdf*.



Note: Mostly free economies: Botswana, Cape Verde, Mauritius, Mauritania, Senegal, Madagascar, South Africa. Mostly unfree economies: Mali, Namibia, Swaziland, Uganda, Cameroon, Burkina Faso, Gabon, Gambia, Ivory Coast, Kenya, Mozambique, Rwanda, Tanzania, Zambia, Central African Republic, Congo, Republic of, Djibouti, Ghana, Malawi, Benin, Chad, Equatorial Guinea, Guinea, Lesotho, Niger, Sierra Leone, Togo, Ethiopia, Guinea-Bissau, Nigeria. Repressed economy: Zimbabwe. The following countries are not included since the 2005 *Index* does not grade them: Angola, Burundi, Comoros, Congo, Dem. Rep., Eritrea, Mayotte, Sao Tome and Principe, Seychelles, Somalia, Sudan.

Sources: World Bank, *World Development Indicators Online*, available by subscription at *www.worldbank.org/data*; Marc A. Miles, Edwin J. Feulner, and Mary Anastasia O'Grady, *2005 Index of Economic Freedom* (Washington, D.C.: The Heritage Foundation and Dow Jones & Company, Inc., 2005), at *www.heritage.org/index.*

unusual degree of influence over the proposals and are primarily responsible for implementation. The countries qualify themselves through their policies and then initiate negotiations, once deemed eligible, by proposing a comprehensive development strategy to be funded by MCA grants and demonstrate how that strategy would improve economic growth and reduce long-term poverty. The MCC requires eligible countries to submit proposals because these countries know the weaknesses in

28. On May 6, 2004, the board of directors announced 16 eligible countries for 2004 (Armenia, Benin, Bolivia, Cape Verde, Georgia, Ghana, Honduras, Lesotho, Madagascar, Mali, Mongolia, Mozambique, Nicaragua, Senegal, Sri Lanka, and Vanuatu) and dispatched teams to educate these countries about the MCA and the proposal process. On November 8, 2004, the MCC identified 16 eligible countries for 2005. (Morocco was added for 2005, and Cape Verde was dropped because its per capita income exceeded the legislated threshold, although in 2006 it should be eligible for MCA grants as a lower-middle-income country.)

29. Thirteen countries have been identified as threshold countries—seven countries for 2004 Threshold funding (Albania, East Timor, Kenya, Sao Tome and Principe, Tanzania, Uganda, and Yemen) and six countries for 2005 (Burkina Faso, Guyana, Malawi, Paraguay, Philippines, and Zambia). Millennium Challenge Corporation, "Threshold Program," at *www.mca.gov/countries/threshold/threshold_guidance_en_FY05.shtml*.

MCA Criteria

To measure whether a country is *governing justly*, the MCA will evaluate:

1. Civil liberties (Freedom House);
2. Political rights (Freedom House);
3. Voice and accountability (World Bank Institute);
4. Government effectiveness (World Bank Institute);
5. Rule of law (World Bank Institute); and
6. Control of corruption (World Bank Institute).

For *investing in people*:

1. Public expenditures on health as percent of GDP (national governments);
2. Immunization rates—DPT and measles (World Health Organization);
3. Public primary education spending as percent of GDP (national governments); and
4. Primary education completion rate for girls (World Bank/UNESCO).

For *promoting economic freedom*:

1. Cost of starting a business (World Bank);*
2. Inflation (International Monetary Fund and others);
3. Three-year budget deficit as a percent of GDP (International Monetary Fund and national governments);
4. Days to start a business (World Bank);
5. Trade policy (The Heritage Foundation/*Wall Street Journal*); and
6. Regulatory quality (World Bank Institute).

* Replaced country credit rating in 2006.

their economies and their needs far better than do aid donors. While the MCC will monitor implementation, progress toward targets, and fiscal accountability measures, the hands-off approach requires careful analysis in the initial stages to ensure that the proposals are correctly implemented, are designed to facilitate economic development, and possess adequate oversight.

Because the MCC is not required to disburse appropriated funds annually, there is less pressure to agree to questionable projects. The MCC evaluates country proposals and offers advice or requests additional information necessary to meet legislative requirements. Only when both parties are satisfied with the development plan is an agreement to disburse funds entered into. This negotiated agreement is called a "compact" by the MCC.

Compacts totaling $905.3 million with Cape Verde, Georgia, Honduras, Madagascar, and Nicaragua are complete, and funds are being disbursed.[30] Compacts are being negotiated with the 12 other countries eligible for MCA funds.

What Is the MCA's Relationship with Africa? As discussed, MCA grants are awarded based on how a country performs against the average in 16 different indicators. There are no regional quotas, and political considerations are minimal. Even with this objective determination, sub-Saharan Africa does quite well with Benin, Cape Verde, Ghana, Lesotho, Madagascar, Mali, Mozambique, and Senegal deemed eligible for MCA grants from that region—nearly 50 percent of the 17 countries eligible for MCA grants in 2004 and 2005. Similarly, sub-Saharan Africa claims over half of the 13 countries selected as MCA threshold countries (Burkina Faso, Kenya, Malawi, Sao Tome and Principe, Tanzania, Uganda, and Zambia).

As would be expected based on this ratio, two of the five countries that signed compacts with the MCA as of October 15, 2005, are from sub-Saharan Africa. Both Cape Verde and Madagascar signed compacts for $110 million in 2005. Furthermore, the MCC reports, "On July 22, 2005, Burkina Faso

30. Millennium Challenge Corporation, "Report on Countries That Are Candidates for Millennium Challenge Account Eligibility in Fiscal Year 2006 and Countries That Would Be Candidates But For Legal Prohibitions."

became the first Threshold Country to be approved for MCA funding. $12.9 million has been awarded to Burkina Faso for their Plan designed to improve girls' primary education."[31]

The first steps of developing the MCA compact process were slow. As a new approach to aid emphasizing country ownership, both the MCC and the eligible governments were uncertain as to how to proceed. After lengthy negotiations, however, the process did achieve a development program targeting country priorities. Two examples from sub-Saharan Africa:

- Cape Verde settled on a compact addressing four impediments to economic growth: severe water scarcity, lack of adequate infrastructure, weak institutional support for the private sector, and an insufficiently trained work force. MCA grants focus on increasing agricultural productivity by improving water management, improving agribusiness development services, and increasing access to credit and capacity of financial institutions; integrating internal markets and reducing transportation costs by improving road infrastructure and upgrading the Port of Praia; and developing the private sector by improving the investment climate and reforming the financial sector.[32]
- Madagascar requested support to address its poorly functioning financial system that does not serve the rural poor and a weak land-titling system that impedes investment in poor rural areas and access to credit. MCA grants will support formalizing the titling and surveying systems, modernizing the national land registry, and decentralizing services to rural citizens; expand financial services to rural areas, improve credit skills training, and streamline a national payments system; and assist farmers and entrepreneurs in identifying new markets and improve their production and marketing practices.[33]

Compact negotiations with other countries continue. While the slow speed of negotiations was a universal disappointment, experience and a more regularized process should speed future compacts. Indeed, the speed of negotiations has reportedly improved since the first compact was signed, and the MCC is using its funds to facilitate ongoing negotiations. For example, the MCC approved a $3.275 million grant in August 2005 to assist Ghana in developing its MCA compact. According to the MCA, Ghana wants to use MCA funds to enhance its position as an exporter of high-value fruit and vegetables by improving the investment climate, roads, irrigation, training, and access to finance.[34]

Hopefully, Ghana will sign its compact soon and benefit from that assistance. However, the real benefit from the MCA for Ghana and other nations lies in its ability to support and encourage policy change among candidate countries competing for MCA grants. It is progress toward economic freedom and the rule of law that will ultimately determine the economic fate of sub-Saharan Africa and represents the true potential for the MCA to help bolster economic growth and development.

The evidence thus far indicates that such an influence exists. Even before the MCA approved its first grant, it spurred reform among candidate countries. For instance, one of the economic indicators used by the MCA to determine eligibility is the number of days it takes to open a business. It chose this indicator as a measure of the regulatory burden on entrepreneurship and business investment.

According to the World Bank, which is the source for this indicator, establishing a business in sub-

31. Millennium Challenge Corporation, "Threshold Countries," at *www.mca.gov/countries/threshold/index.shtml*.

32. Millennium Challenge Corporation, "Summary of the Millennium Challenge Compact with the Republic of Cape Verde," at *www.mca.gov/about_us/congressional_notifications/071205-cn_CapeVerde.pdf*.

33. Millennium Challenge Corporation, "Summary of the Millennium Challenge Compact with the Republic of Madagascar," at *www.mca.gov/about_us/congressional_notifications/042605-cn_Madgascar_compact.pdf*.

34. Millennium Challenge Corporation, "Millennium Challenge Corporation Signs $3 Million Pre-Compact Grant with Ghana," August 11, 2005, at *www.mca.gov/public_affairs/press_releases/pr_081105_Ghana.shtml*.

Saharan Africa took 74 days on average in 2004 (the MCA's first year). In 2006, the average had fallen to 63 days and, out of the 31 countries measured in both 2004 and 2006, 17 countries reduced the number of days required versus only five that increased the number of days required.[35] Moreover, six countries not measured in *Doing Business in 2004* provided the World Bank the data necessary to conduct their measurement in the 2006 edition. Thus, the opportunity to receive MCA grants is both providing an incentive for countries to improve their business environment and encouraging transparency.

Another example is the interest MCA candidate countries have expressed in how the *Index of Economic Freedom* measures trade policy (another MCA measure) and how they could improve their score. This interest has arisen among MCA-eligible countries and those hoping to qualify in the future.

Conclusion

The lessons from nearly five decades of development efforts indicate that sub-Saharan Africa needs policy change far more than increased aid. Indeed, recent studies question whether aid benefits development at all. While there may be a role for assistance and donor nations, the key to development lies in the hands of governments in developing countries.

For development to occur, governments must remove obstacles preventing their people from seizing opportunities to benefit them, their families, and their communities. This is best done by adopting the policies that bolster economic freedom, good governance, and the rule of law—policies that are the key to economic growth and development with or without foreign assistance. As noted by President Bush in 2002,

> When nations close their markets and opportunity is hoarded by a privileged few, no amount of development aid is ever enough. When nations respect their people, open markets, invest in better health and education, every dollar of aid, every dollar of trade revenue and domestic capital is used more effectively.[36]

By focusing assistance on countries that are committed to policies conducive to economic growth and development, the MCA sends the right message that developing countries cannot be passive in development, relying on aid, but must undertake reform to make it possible. The MCA captures the nature of this partnership by creating incentives for poor nations to adopt economic freedom, the rule of law, and good governance. As noted in *The Road to Prosperity*:

> In technical terms it is not the level of poverty that is most vicious, but rather the absence of change or opportunity to escape that poverty. Where the 20th century approach produced a vicious cycle of aid, default, and dependency on foreign governments, the IMF, or the World Bank, the 21st century holds out the prospect that countries can generate growth and prosperity themselves, without foreign interference.[37]

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35. World Bank, *Doing Business in 2006: Creating Jobs* (Washington, D.C.: World Bank, 2006), pp. 95–97, and *Doing Business in 2004: Understanding Regulation* (Washington, D.C.: World Bank, 2004), pp. 118–120.
36. George W. Bush, "A New Compact for Development in the Battle Against World Poverty," March 22, 2002, at *http://usinfo.state.gov/journals/itgic/0402/ijge/gj01.htm*.
37. Marc A. Miles, ed., *The Road to Prosperity: The 21st Century Approach to Economic Development* (Washington, D.C.: The Heritage Foundation, 2004), p. 8.