

Report on the Criteria and Methodology for Determining the Eligibility of Candidate Countries for Millennium Challenge Account Assistance in FY 2004

Summary

This report is provided in accordance with Section 608(b) of the Millennium Challenge Act of 2003, Pub. L. 108-199, Division D (the “Act”).

The Act authorizes the provision of assistance to countries that enter into compacts with the United States to support policies and programs that advance the prospects of such countries to achieve lasting economic growth and poverty reduction. The Act requires the Millennium Challenge Corporation (“MCC”) to take a number of steps to determine the countries that, based on their demonstrated commitment to just and democratic governance, economic freedom and investing in their people, will be eligible to receive Millennium Challenge Account (“MCA”) assistance during a fiscal year. These steps include the submission of reports to appropriate congressional committees and the publication of notices in the Federal Register that identify:

1. the “candidate countries” for MCA assistance (Section 608(a) of the Act);
2. the eligibility criteria and methodology that the MCC Board of Directors (the “Board”) will use to select “eligible countries” from among the “candidate countries” (Section 608(b) of the Act); and
3. the countries determined by the Board to be “eligible countries” for a fiscal year and the countries on the list of eligible countries with which the Board will seek to enter into MCA “Compacts” (Section 608(d) of the Act).

This report sets out the criteria and methodology to be applied in determining eligibility for FY 2004.

Methodology

The Board will select eligible countries based on their overall performance in relation to their peers in three broad policy categories: Ruling Justly, Encouraging Economic Freedom, and Investing in People. Section 607 of the Act requires that the Board’s determination of eligibility be based “to the maximum extent possible, upon objective and quantifiable indicators of a country’s demonstrated commitment” to the criteria set out in the Act. For FY 2004, candidate countries are those countries that are eligible for assistance from the International Development Association, have a per capita income equal to or less than \$1415, and are not ineligible to receive United States economic assistance.

The Board will make use of sixteen indicators to assess policy performance of individual countries (specific definitions of the indicators and their sources are set out in Annex A). These

indicators are grouped for purposes of the assessment methodology under the three policy categories as follows:

| Ruling Justly: | Encouraging Economic Freedom: | Investing in People: |
|---|---|---|
| 1. Civil Liberties 2. Political Rights 3. Voice and Accountability 4. Government Effectiveness 5. Rule of Law 6. Control of Corruption | 1. Country Credit Rating 2. 1-year Consumer Price Inflation 3. Fiscal Policy 4. Trade Policy 5. Regulatory Quality 6. Days to Start a Business | 1. Public Expenditures on Health as Percent of GDP 2. Immunization Rates: DPT3 and Measles 3. Public Primary Education Spending as Percent of GDP 4. Primary Education Completion Rate |

In making its determination of eligibility with respect to a particular candidate country, the Board will consider whether such country performs above the median in relation to its peers on at least half of the indicators in each of the three policy categories and above the median on the corruption indicator. One exception to these relative comparisons is inflation, for which a country needs to pass an absolute test of having an inflation rate under 20%.

The indicators methodology will be the predominant basis for determining which countries will be eligible for MCA assistance. In addition, the Board may exercise discretion in evaluating and translating the indicators into a final list of eligible countries. In this respect, the Board may also consider whether any adjustments should be made for data gaps, lags, trends, or other weaknesses in particular indicators. Likewise, the Board may deem a country ineligible if it performs substantially below average on any indicator and has not taken appropriate measures to address this shortcoming.

Where necessary, the Board may also take into account other data and quantitative information as well as qualitative information to determine whether a country performed satisfactorily in relation to its peers in a given category. As provided in the Act, the CEO’s report to Congress setting out the list of eligible countries and which of those countries the MCC will seek to enter into Compact negotiations will include a justification for such eligibility determinations and selections for Compact negotiation.

There are elements of the criteria set out in the Act for which there is either limited quantitative information (e.g., rights of people with disabilities) or no well-developed performance indicator (e.g., sustainable management of natural resources). Until such data and/or indicators are developed, in assessing performance in these areas the Board may rely on supplemental data and qualitative information such as:

- **Ruling Justly:** The State Department Human Rights report contains qualitative information to make an assessment on a variety of criteria outlined by Congress, such as the rights of people with disabilities, the treatment of women and children, worker rights, and human rights. As additional information, the Board may also consider how the country scores on Transparency International’s Corruption Perceptions Index.
- **Economic Freedom:** The Board’s assessment of a country’s commitment to economic policies that promote private sector growth and the sustainable management of natural

resources may make use of quantitative and qualitative information such as access to sanitation, deforestation, conservation of land and marine resources, land tenure institutions, and protection of threatened and endangered species. The MCC will consult with experts and work to refine this approach over time.

- Investing in People: Both the level and the trend in girls' primary enrollment rates may be considered as extra information to assess a country's commitment to Investing in People.

Relationship to Legislative Criteria

Within each policy category, the Act sets out a number of specific criteria. A set of objective and quantifiable indicators is being used to establish eligibility and measure the relative performance by candidate countries against these criteria. The Board's approach to determining eligibility ensures that performance against each of these criteria is assessed by at least one of the sixteen objective indicators and most are addressed by multiple indicators.

Section 607(b)(1): Just and democratic governance, including a demonstrated commitment to--

(A) promote political pluralism, equality, and the rule of law:

Indicators – Political Rights, Civil Liberties, Voice and Accountability and Rule of Law

(B) respect human and civil rights, including the rights of people with disabilities;

Indicators – Political Rights and Civil Liberties.

(C) protect private property rights;

Indicators – Civil Liberties, Regulatory Quality and Rule of Law.

(D) encourage transparency and accountability of government; and

Indicators – Political Rights, Civil Liberties, Voice and Accountability, and Government Effectiveness.

(E) combat corruption;

Indicators – Civil Liberties and Control of Corruption.

Where necessary the Board will also draw on supplemental data and qualitative information including: the State Department's Human Rights Report and Transparency International Corruption Perception's Index.

Section 607(b)(2): Economic freedom, including a demonstrated commitment to economic policies that--

(A) encourage citizens and firms to participate in global trade and international capital markets;

Indicators – Country Credit Rating, Fiscal Policy, Inflation, Trade Policy, and Regulatory Quality.

(B) promote private sector growth and the sustainable management of natural resources;

Indicators – Inflation, Days to Start a Business, Fiscal Policy, and Regulatory Quality.

(C) strengthen market forces in the economy; and

Indicators – Fiscal Policy, Inflation, and Regulatory Quality.

(D) respect worker rights, including the right to form labor unions; and

Indicators – Civil Liberties.

Where necessary the Board will also draw on supplemental data and qualitative information including: the State Department’s Human Rights Report, access to sanitation, deforestation, conservation of land and marine resources, land tenure institutions, and protection of threatened and endangered species.

Section 607(b)(3): Investments in the people of such country, particularly women and children, including programs that--

(A) promote broad-based primary education; and

Indicators – Primary Education Completion Rate and Public Spending on Primary Education.

(B) strengthen and build capacity to provide quality public health and reduce child mortality.

Indicators – Immunization and Public Spending on Health.

Where necessary the Board will also draw on supplemental data and qualitative information including: the State Department’s Human Rights Report and Girl’s Primary Enrollment Rate.

Annex A: Indicator Definitions

The following 16 indicators will be used to measure candidate countries' adherence to the criteria found in Section 607(b) of the Act. The indicators are intended to assess the degree to which the political and economic conditions in a country serve to promote broad-based sustainable economic growth and thus provide a sound environment for the use of MCA funds. The indicators are not goals in themselves; rather they measure policies that are necessary conditions for a country to achieve broad-based sustainable economic growth. The indicators were selected based on their relationship to growth and poverty reduction, the number of countries they cover, their transparency and availability, and their relative soundness and objectivity. Where possible, the indicators rely on indices of performance developed by independent sources.

Ruling Justly:

- 1) *Civil Liberties*: A panel of independent experts rates countries on: freedom of expression, association and organizational rights, rule of law and human rights, and personal autonomy and economic rights. Source: *Freedom House*.
- 2) *Political Rights*: A panel of independent experts rates countries on: the prevalence of free and fair elections of officials with real power; the ability of citizens to form political parties that may compete fairly in elections; freedom from domination by the military, foreign powers, totalitarian parties, religious hierarchies and economic oligarchies; and the political rights of minority groups. Source: *Freedom House*.
- 3) *Voice and Accountability*: An index of surveys that rates countries on: ability of institutions to protect civil liberties, the extent to which citizens of a country, are able to participate in the selection of governments, and the independence of the media. Source: *World Bank Institute*.
- 4) *Government Effectiveness*: An index of surveys that rates countries on: the quality of public service provision, civil services' competency and independence from political pressures, and the government's ability to plan and implement sound policies. Source: *World Bank Institute*.
- 5) *Rule of Law*: An index of surveys that rates countries on: the extent to which the public has confidence in and abides by rules of society; incidence of violent and non-violent crime; effectiveness and predictability of the judiciary; and the enforceability of contracts. Source: *World Bank Institute*.
- 6) *Control of Corruption*: An index of surveys that rates countries on: the frequency of "additional payments to get things done," the effects of corruption on the business environment, "grand corruption" in the political arena and the tendency of elites to engage in "state capture." Source: *World Bank Institute*.

Encouraging Economic Freedom:

- 1) *Country Credit Rating*: A semi-annual survey of bankers' and fund managers' perceptions of a country's risk of default. Source: *Institutional Investor Magazine*.
- 2) *Inflation*: The most recent 12 month change in consumer prices as reported in the IMF's International Financial Statistics or in another public forum by the relevant national monetary authorities. Source: *Multiple*.
- 3) *Fiscal Policy*: The overall budget deficit divided by GDP, averaged over a three-year period. The data for this measure is being provided directly by the recipient government and will be cross checked with other sources and made publicly available to try to ensure consistency across countries. Source: *National Governments*.
- 4) *Days to Start a Business*: The Private Sector Advisory Service of the World Bank Group works with local lawyers and other professionals to examine specific regulations that impact business investment. One of their studies measures how many days it takes to open a new business. Source: *World Bank*.
- 5) *Trade Policy*: A measure of a country's openness to international trade based on average tariff rates and non-tariff barriers to trade. Source: *The Heritage Foundation's Index of Economic Freedom*.
- 6) *Regulatory Quality Rating*: An index of surveys that rates countries on: the burden of regulations on business, price controls, the government's role in the economy, foreign investment regulation and many other areas. Source: *World Bank Institute*.

Investing in People:

- 1) *Public Expenditure on Health*: Total expenditures by government at all levels on health divided by GDP. Source: *National Governments*.
- 2) *Immunization*: The average of DPT3 and measles immunization rates for the most recent year available. Source: *The World Health Organization WHO*.
- 3) *Total Public Expenditure on Primary Education*: Total expenditures by government at all levels on primary education divided by GDP. Source: *National Governments*.
- 4) *Primary Completion Rate*: The number of students completing primary education divided by the population in the relevant age cohort. Source: *World Bank and UNESCO*.