Does the "MCC Effect" Exist? Results from the 2012 MCA Stakeholder Survey

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Summary

The Millennium Challenge Corporation (MCC) provides US foreign assistance to poor countries that first demonstrate their commitment to good governance against publicly-available policy indicators. Can MCC's indicator-based selection process itself encourage policy reform? Bradley Parks and Zachary Rice, of the College of William and Mary, share with the Center for Global Development the results of a global survey about whether this "MCC effect" exists. The short answer: yes, but more so in some areas (control of corruption and fiscal policy) than others (democracy indicators). And policymakers seem to support MCC's performance-based aid allocation model and the idea that the agency can do more to expand the reach of its incentive effect.

The MCA Monitor provides rigorous policy analysis and research on the operations and effectiveness of the Millennium Challenge Corporation. It is part of CGD's Rethinking US Foreign Assistance program that tracks efforts to reform aid programs and improve aid effectiveness. The Center for Global Development is grateful for contributions from the Bill & Melinda Gates Foundation in support of this work.

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Center for Global Development

Survey Background

In the fall of 2012, the College of William and Mary's Institute for the Theory and Practice of International Relations conducted a Millennium Challenge Account (MCA) Stakeholder Survey. This survey had six objectives: (1) to measure the perceived strength, scope, and usefulness of the Millennium Challenge Corporation's (MCC's) "incentive effect," (2) to analyze the conditions under which the MCC has informed, motivated, accelerated, sustained, or otherwise influenced developing countries' reform efforts, (3) to shed light how MCA eligibility standards have influenced government decisions and actions, (4) to explore the perceived effectiveness of MCC threshold and compact programs, including the impact of threshold programs on reform outcomes, (5) to gauge the influence of the MCA eligibility criteria vis-à-vis other reform promotion tools, and (6) to identify whether and to what degree application of the MCA eligibility standards has had negative unintended consequences.

We do not claim that these survey results constitute definitive evidence on the influence of the MCA eligibility criteria or the impact of MCC programming. However, the 2012 survey does capture the opinions and experiences of 640 development policymakers and practitioners from 100 low- and lower-middle income countries, respondents who are particularly knowledgeable about the MCC's policy influence and impact. Only individuals who worked in countries meeting the per capita income requirements for MCA candidacy between 2004 and 2012 were included in the study. Survey respondents included heads of government, ministers, deputy ministers, and other senior officials from developing countries; US Ambassadors, USAID Mission Directors, and MCC Resident Country Directors; staff from institutions responsible for designing, implementing, or evaluating MCC compact or threshold programs; and members of civil society organizations and business associations who are knowledgeable about MCA policy and programming issues.

The Influence of the MCA Eligibility Criteria

The US government's decision to make access to MCA funding conditional upon a country's performance on 17 third-party measures of policy performance created both a reward and an incentive for governments that rule justly, invest in their people, and promote economic freedom. Scholars, policy analysts, and legislative overseers generally do not dispute the fact that the MCC has delivered on its promise to *reward* developing countries that possess reasonably sound policies and institutions with generous financial assistance. However, the MCC's impact as an *incentive* for reform is not well understood. A small body of evidence suggests that governments have implemented legal, policy, institutional, and regulatory reforms to enhance their chances of becoming eligible for MCA assistance (Johnson and Zajonc 2006; Öhler et al. 2012). However, scholars, policymakers, and practitioners know relatively little about the strength and scope of the so-called MCC Effect and why it seems to exert different levels of influence across countries and policy areas.

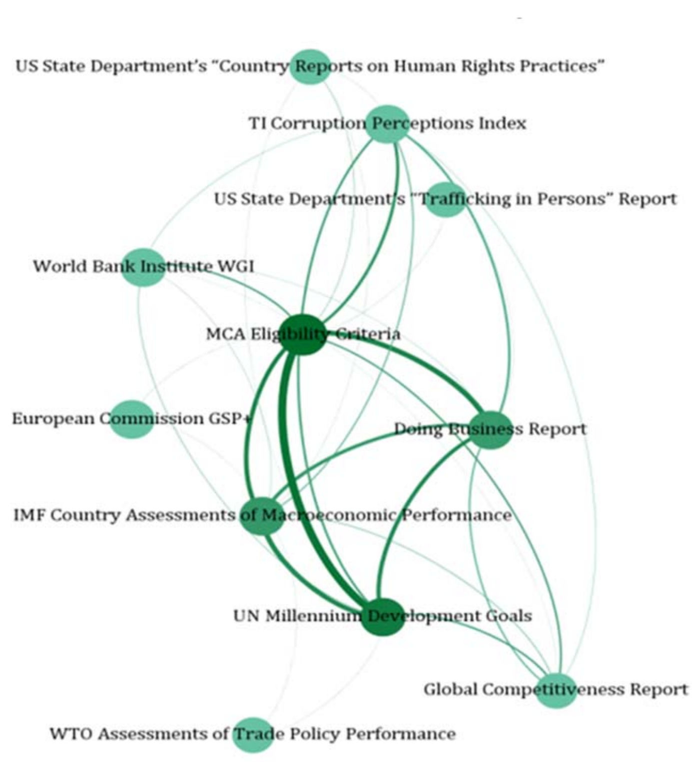
Findings

The 2012 MCA Stakeholder Survey provides new evidence about the influence of the MCA eligibility criteria on the reform efforts of developing countries. It also sheds light on the influence of the MCA eligibility criteria vis-à-vis other external tools of conditionality and socialization.

1. **MCA eligibility criteria were repeatedly identified as one of the three most influential external assessments of government performance**

When asked to identify the three most influential external assessments of government performance from a list of 18 options, respondents repeatedly identified the MCA eligibility criteria and the UN Millennium Development Goals among the three most influential assessments. Other influential policy monitoring and reform promotion tools included the IMF's country assessments of macroeconomic and the World Bank's *Doing Business* Report.

MCA Influence in Relational Perspective



The survey data suggest that the policy influence of external assessments may have more to do with signaling credibility to investors, creditors, and donor agencies than directly influencing specific aid allocation decisions. Some of the most influential indicators—including the Millennium Development Goals, Transparency International's *Corruption Perceptions Index,* and the World Bank's *Doing Business* Report—are not directly tied to the provision of aid resources.

A network map (shown above) helps provide a relational perspective on some of the factors contributing to the outsized policy influence of the MCA eligibility criteria. The MCA eligibility assessment is broadly influential, but it also serves as a 'bridge' between—and a complement to—other US and multilateral reform promotion tools.

2. The influence of the MCA eligibility criteria has increased, not diminished, over time

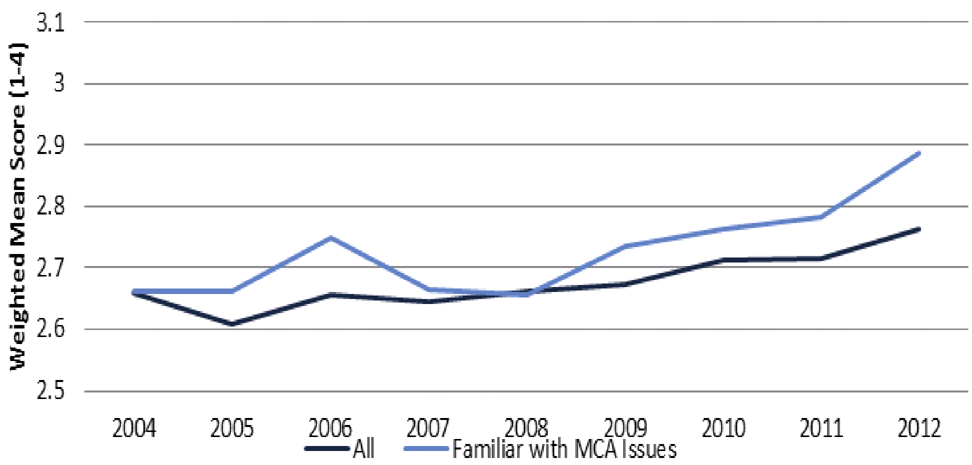
In a study recently published in the European Economic Review, several scholars from University of Göttingen, Heidelberg University, and the Kiel Institute for the World Economy report results suggesting that the policy influence of the MCA eligibility standards—in particular, the Control of Corruption standard—has waned over time (Öhler et al. 2012). The results from the 2012 MCA Stakeholder Survey provide evidence of a different pattern. Analysis of time-varying survey responses suggests that the MCA eligibility criteria have exerted *greater* influence over time.

While there is evidence that all of the MCA eligibility indicators have had some degree of influence on developing country reform efforts, four—control of corruption, fiscal policy, business startup, and primary education expenditures—have had the strongest influence in low- and lower-middle income countries between 2004 and 2012. The influence of the MCA eligibility indicators in the Investing in People category has also proven strong and consistent across stages of the policy process: agenda setting, reform design, and implementation.

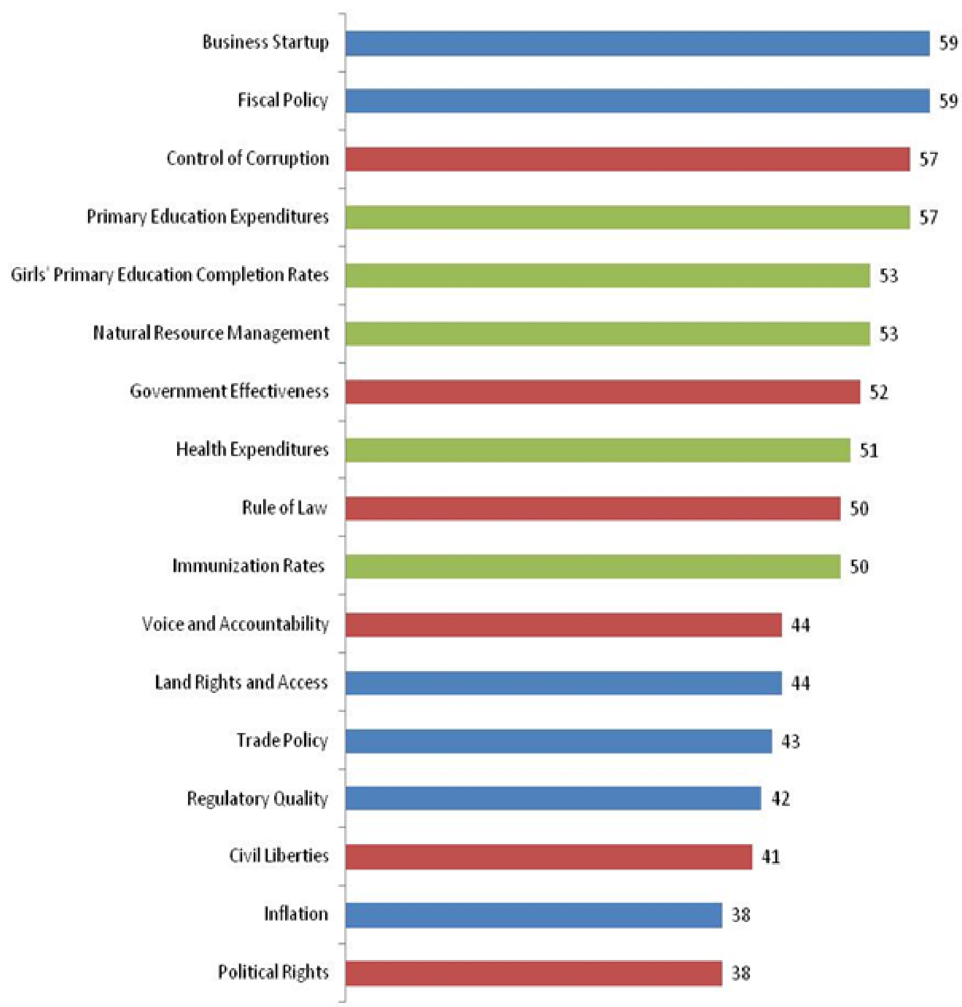
3. Reform influence of the democracy indicators has been limited

A considerably weaker effect was found among the so-called democracy indicators: Political Rights, Civil Liberties, and Voice and Accountability, possibly reflecting the difficulty of democratic reform or the absence of a compelling political motivation for leaders to undertake reforms that might result in their removal from office. This result underscores the rationale for—and suggests the need to temper expectations regarding the likely policy influence of—the MCC's new democratic rights "hard hurdle" (Dunning 2011).

Increasing Influence of MCA Eligibility over Time



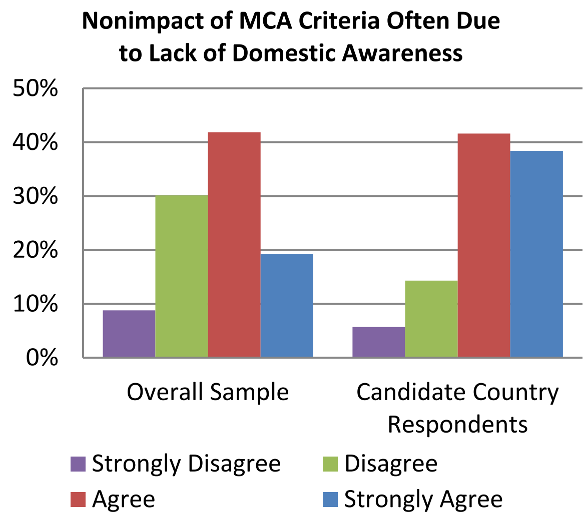
The Policy Influence of Specific MCA Eligibility Indicators*



* To eliminate the risk of double counting, policy influence is measured here by the number of countries (out of 82) in which at least one respondent indicated that a policy reform or ajdustment was undertaken to improve the score of his or her country on a specific indicator. Red represents indicators from the "Ruling Justly" category. Green represents indicators from the "Investing in People" Category". Blue represents indicators from the "Economic Freedom" category.

Why Are the MCA Eligibility Standards More Influential in Some Countries Than Others?

Scholars and policy analysts have proposed various explanations for why some countries are more responsive to the MCA eligibility standards than others. Several findings from the 2012 MCA Stakeholder Survey speak to this policy question.



4. **Respondents indicated that a low level of government responsiveness to the MCA eligibility indicators is often the result of a lack of awareness on the part of domestic authorities**

Respondents who indicated that the MCA eligibility criteria had no role or a marginal role in domestic reform efforts identified a lack of awareness among domestic authorities as the primary reason for limited influence. While a three-fifths majority of the overall sample of respondents from compact, threshold, and candidate countries agreed that lack of awareness was a reason for the MCA's limited policy impact, this figure rises to 80% when one restricts the sample to candidate country respondents. This finding suggests that the MCC and other parts of the USG could undertake more targeted policy outreach, awareness raising, and technical assistance activities with governments in candidate countries.

5. **Reform influence may also be weakened by doubts about whether the MCC follows the rules in making eligibility determinations**

The survey results suggest that policymakers and practitioners from *candidate* countries are more likely to question the credibility of the formal MCA eligibility rules—that is, the notion that the MCC Board of Directors will select countries based on merit rather than US foreign policy interests, population size, or other undisclosed considerations—than respondents from threshold countries and compact countries. This finding suggests that the MCC's Board of Directors may need to communicate better the decision rules it uses to determine individual country eligibility. The MCC currently provides written justification for all of the countries it deems compact- or threshold-eligible, but does not provide a detailed, country-by-country explanation of its *ineligibility* designations. Greater disclosure of how it makes *ineligibility* decisions could strengthen the "MCC Effect." In fairness, there may be many good reasons why the USG chooses not to disclose this information: retaining congressional support, preserving bilateral relationships, maintaining flexibility to select countries where the opportunity to reduce poverty is substantial, etc. However, from the narrow perspective of trying to incentivize reform efforts in developing countries, nondisclosure of the full range of factors used to make eligibility determinations is probably not optimal.

Unintended Consequences

Many development scholars worry that external tools of policy influence will have far-reaching, unintended consequences and ultimately do more harm than good. Critics of the MCC have proposed that the MCA eligibility standards might exert outsized policy influence, but divert a government's attention away from higher-priority policy issues or negatively limit a government's policy autonomy. Others have argued that the MCA eligibility standards might lead to excessive focus on measurement and data quality issues and that countries might "game the system" by following the letter but not the spirit of the law. Still others fear that rigorous application of the MCA eligibility criteria might impose significant domestic or external audience costs and thus provoke MCA candidate governments to ally themselves with non-DAC suppliers of development finance.

We find relatively little evidence to support these claims in the survey data. Respondents generally disagreed that the MCC's approach of tying eligibility for assistance to third-party indicators of policy performance had resulted in an excessive focus on measurement and data quality issues. Similarly, respondents did not agree that the MCA eligibility criteria had the effect of limiting the "policy space" of developing country governments: 91.5% of respondents expressed disagreement or strong disagreement with the notion that the MCC's performance-based aid allocation model had limited the policy autonomy of governments in a negative manner.

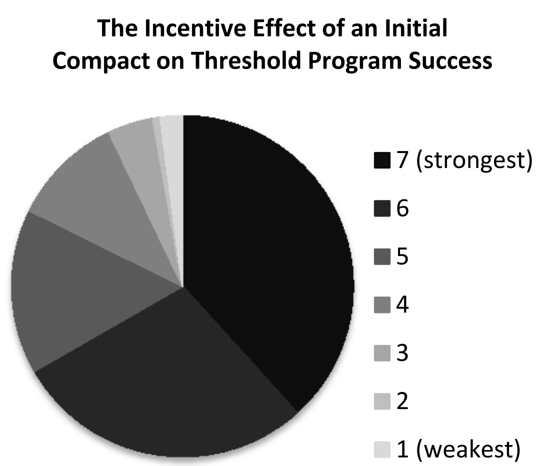
Program Implementation and the "MCC Effect"

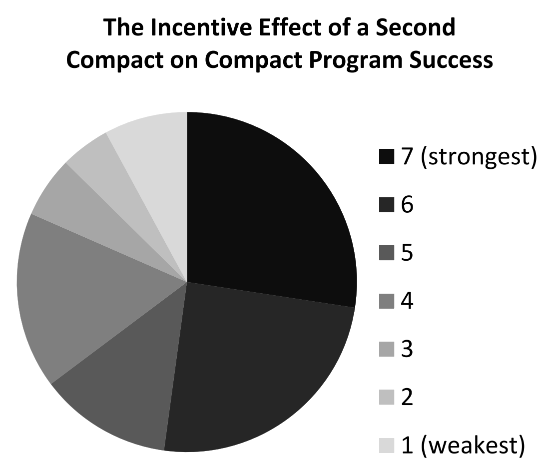
In December 2012, the MCC highlighted the importance of the "MCC Effect" in the board of directors' decision to make Liberia, Niger, and Sierra Leone compact-eligible countries. In a press release, the MCC cited examples of anticorruption, health policy, and environmental protection reforms undertaken by these governments to achieve MCA eligibility (MCC 2012). We find evidence in our 2012 survey to support MCC's claim that the prospect of an initial compact has served as an effective incentive for policy reform.

The "MCC Effect" seems to be particularly strong in threshold countries, with 68% of respondents from those countries reporting that the MCA eligibility criteria were either "central to a few important reform efforts" or "instrumental to many important reform efforts." The "MCC Effect" is also present in compact countries and candidate countries, but the survey evidence suggests that it is less strong in these countries: 64% of respondents from compact countries and 41% of respondents from candidate countries reported that the MCA eligibility criteria were either "central to a few important reform efforts" or "instrumental to many important reform efforts."

6. **The incentive of a follow-on program has a greater impact on the successful implementation of reform-oriented threshold programs than on compact programs.**

We also asked respondents whether the prospect of a (first or second) compact provided an incentive for effective program implementation. Over 38% of respondents indicated—on a scale of one to seven—that the prospect of an initial MCA compact had the strongest possible effect (7) in giving domestic authorities an incentive to implement a threshold program successfully. By contrast, when asked to identify the extent to which the prospect of a second compact contributed to compact program success, this figure dropped more than 10 percentage points—to 27.4%. The survey evidence therefore suggests that the incentive of a follow-on program has a greater impact on the successful implementation of reform-oriented threshold programs than on compact programs, which place greater emphasis on capital investments.





7. **Respondents broadly agreed that threshold programs have been successful**

When asked to compare the success of threshold programs to other externally funded reform programs, 68% of respondents indicated that threshold programs were equally or more successful than other programs.

The particularly high level of MCC policy influence and programmatic impact that respondents reported in threshold countries is striking in light of the concerns that US legislators have recently raised about the program's raison d'être and efficacy. In 2010, John Kerry and Richard Lugar, two prominent members of the US Senate Foreign Relations Committee, sent a letter to the MCC's incoming CEO, indicating that "we believe that the [threshold] program, as it stands, requires significant overhaul and substantial rethinking. We are not convinced that the program is achieving the goals and objectives it was originally created to accomplish, and we think the mandate of the program has become increasingly muddled.…We believe a comprehensive review of the goal, purpose, and utility of the [threshold] program is in order, and we are open to fairly wide changes that would modify the [threshold] program's mandate and implementation" (Kerry and Lugar 2010).

In response to these concerns, the MCC announced a course correction in 2011: Rather than design threshold programs to help governments improve their performance vis-à-vis the MCA eligibility standards and meet the formal compact eligibility requirements, it decided that countries deemed eligible for threshold funding would be asked to design and implement reform programs that target the binding constraints to economic growth (MCC 2011; Yohannes 2012).

While the data from the 2012 MCA Stakeholder Survey on the perceived influence and impact of threshold programs are no substitute for rigorous programmatic impact evaluations, they do suggest that original design of MCC threshold programs resulted in a strong incentive effect and significant programmatic results.

8. **Respondents identified two main factors that have contributed to the success and failure of threshold programs**

Participants in the survey who were knowledgeable about individual threshold programs were asked to identify which factors contributed to the success or failure of the program. Respondents generally agreed that "the prospect of an MCC compact gave domestic authorities an incentive to implement the threshold program successfully" was the primary reason for threshold program success. The second most popular explanation for threshold program success was that MCC-funded activities "reflected the government's previously-defined priorities."

Respondents also coalesced around several factors that have contributed to unsuccessful threshold programs. The survey data suggest that when the MCC's Board of Directors selects threshold-eligible countries, they may not screen as aggressively as they should for a government's willingness to undertake difficult reforms. The single most popular explanation of why threshold programs did not succeed was that "senior policymakers were insufficiently committed to the necessary reforms."

9. MCC compacts are regarded by USG and non-USG policymakers and practitioners as a highly effective mechanism for delivering foreign assistance

Sixty-two percent of survey respondents reported that MCA compact programs have proven more successful than other assistance programs funded by donor agencies and international organizations. An additional 18% reported that compact programs were equally successful as other foreign assistance programs. The survey data also demonstrate that developing country officials are more confident about the development impact of MCC compacts than USG officials.

10. Respondents identified a common set of factors that have contributed to the success and failure of compact programs

They zeroed in on several key "success factors": competent program management by in-country MCA implementing entities, the use of a competitive and transparent bidding process, sound financial management practices, and close alignment of programmatic activities with the partner government's development priorities. On the other hand, of 12 possible explanations for MCA compact success, the prospect of a second compact received the third lowest score.

Survey respondents also cited insufficient domestic political leadership support in counterpart countries, program implementation interruptions triggered by political transitions, and poor program management by in-country MCA implementing entities as the primary reasons for unsuccessful compacts. Overall, the survey evidence suggests that misuse of US taxpayer dollars has not plagued MCC compact programs. Respondents did not identify the misuse of program funds as one of the major factors contributing to unsuccessful compact programs.

Aid Conditionality and Country Selectivity Perception Gap

There is evidence that researchers and policymakers perceive the issues of aid conditionality and country selectivity differently.

11. **Policymakers and practitioners do not express the same aversion to aid conditionality and selectivity that one observes in the development research community.**

Survey respondents identified "eliminating all forms of conditionality" as one of the two least desirable changes to foreign assistance policy. On the other hand, we found strong support among policymakers and practitioners for the MCC's approach of tying the provision of assistance to a country's commitment to good governance. Survey respondents also expressed particularly strong support for the "Cash on Delivery" aid modality proposed by the Center for Global Development.

12. **Additionally, the survey data highlight mixed support for Paris Declaration reforms**

Policymakers and practitioners expressed a desire for greater country ownership of the development agenda and increased support for institution-building activities. However, much of the conventional wisdom about "what will make aid more effective"—including the provision of forward-looking aid expenditure information, the streamlining of administrative reporting requirements, and a reduction in the practice of "tied aid"—finds less support in our survey findings. Some of the most popular ideas for reforming foreign assistance, such as conditioning the provision of aid on democracy and governance issues and the use of results-based aid delivery modalities, are not included in the Paris Declaration.

Conclusion

The results from the 2012 MCA Stakeholder Survey suggest that the MCA eligibility assessment is an effective instrument for encouraging policy and institutional reform in developing countries. However, the "MCC Effect" is not evenly distributed across countries, time, and policy domains. Some governments are more responsive to the MCA eligibility standards than others. One way to account for this variation is simply to ask policymakers and practitioners from developing countries whether, why, and how governments respond to the USG's MCA policy instrument. This was the methodological ambition of the 2012 MCA Stakeholder Survey. Our hope is that the methods that we employed in this survey will inspire and inform future efforts to learn about the influence and effectiveness of performance-based aid programs, like the MCA, by listening to policymakers and practitioners who work on the frontlines in developing countries. We also hope that our findings will encourage discussion, debate, and introspection within the MCC and other aid agencies and international organizations about how existing reform promotion tools can be retooled for maximum impact.

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