

“U.S. Assistance for the Northern Triangle of Central America”  
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Thank you, Chairman Graham, Ranking Member Leahy and members of the Committee. I am delighted to be here today and I look forward to discussing MCC’s work in Central America.

MCC helps relatively well-governed poor countries reduce poverty through economic growth and the agency’s work, along with our sister agencies in the U.S. government, advances American security, values and prosperity. When people have stability and opportunity, they are more likely to stay in their home communities and are better able to address health and security challenges that have international implications.

**MCC Model**

MCC is an important tool in U.S. foreign policy. We work to catalyze economic growth in the best-governed poor countries, and we support and coordinate with other U.S. government agencies to achieve our shared goals. MCC’s investments with partner countries drive economic growth and create opportunities to escape poverty in three interrelated ways.

- First, by consistently applying stringent eligibility criteria to select our partners, MCC is able to leverage and incentivize policy, regulatory and institutional reforms. MCC uses third-party data to assess a country’s policy performance in three categories: ruling justly, investing in people, and encouraging economic freedom. Without good policies in each of these areas, countries cannot achieve sustainable economic growth and, as such, our assistance would not be as effective. In addition to providing a roadmap to determine which partners are more likely to provide better development outcomes, this selection process also drives countries to reform policies to qualify for MCC’s assistance. Once a country is selected, MCC is often able to successfully push for major policy and sectoral reforms that complement and sustain project investments. Together, these reforms and investments help draw in private sector investment and create opportunities for sustainable growth long after our five-year partnership.
- Second, MCC uses an evidence-based, business-like approach to choosing investments that will yield the best return in terms of economic growth and poverty reduction. After selection, MCC immediately begins working with partner governments to identify the most binding constraints to economic growth. This is a data-driven process to understand what is holding countries back and limiting private investment and job creation. The choice of what sector to focus on, therefore, is demand driven and based on the needs of each individual partner country.

We invest in projects that lead to economic growth and help people lift themselves out of poverty, like power, clean water, land rights and roads. We also leverage these large

investments to ensure partners undertake policy reforms that promote the sustainability of our investments and benefit the most vulnerable populations. After agreeing on the outlines of a project, MCC's economists carefully estimate the anticipated costs and benefits of the projects to ensure that we design an efficient solution that generates a return on investment and fosters self-sufficiency.

- Finally, MCC's focus is not only on building infrastructure or completing a specific project, but also on building expertise and know-how in our partner governments to transparently and effectively implement other projects after MCC's investment comes to a close. Through MCC's country-led approach, countries learn effective project implementation, accountable fiscal stewardship, and transparent procurement processes that outlast the program. MCC is guided by the principle that we cannot solve the problems of our partner countries for them; we provide diagnostic tools, incentives and support for our partners to make the policy and institutional changes needed for them to address their own problems. We are an important part of the solution, but our partners are ultimately responsible to implement the projects funded by MCC, to follow through on the policy reforms, and, perhaps most important, to transfer this knowledge to manage their own resources with the same transparency and accountability that MCC demands in the projects that we fund.

Maintaining the maximum level of country ownership over the process of implementing MCC-funded projects, which encourages the level of responsibility and knowledge sharing we expect, while at the same time ensuring the proper oversight of U.S. taxpayer dollars is of utmost importance and always a delicate balance. MCC requires that partner governments establish an entity to implement the projects, usually known as an "MCA." Like MCC, the MCAs are government bodies, with governing boards that include public and private sector representation and they are accountable for overseeing the day-to-day implementation of the projects. In Honduras, where MCC had a compact from 2005 to 2010, the government has been using the unit established during the compact to implement over \$1 billion in other development programs. While this country ownership model is unique, MCC uses our experience and lessons-learned to support the efforts of our interagency partners and the governments of the Northern Triangle countries. Moreover, these entities have developed solid reputations for transparency and capacity in their countries. They set an important example of a government entity delivering effectively, transparently, and without regard for political bent. Such examples are scarce and are valuable in setting a higher bar for government performance.

## **Progress in Central America**

MCC is working in the Northern Triangle countries of El Salvador, Honduras and Guatemala to promote prosperity and strengthen governance in the region, supporting the objectives of the U.S. Strategy for Engagement in Central America as well as the Northern Triangle governments' Alliance for Prosperity.

Annual government expenditures by the Northern Triangle countries are more than 10 times the amount of official development assistance they receive from international donors. The efficient and effective use of their own government funds, therefore, is critical to provide the security, health, education, and infrastructure needed to achieve sustainable economic development and reduce poverty. To promote effective, transparent use of government resources, MCC not only invests in needed infrastructure and promotes policy and institutional reforms, but we also seek

to strengthen partner governments' implementation capacity to deliver services to their people. MCC is at the forefront of this critical but still often elusive effort. Our approach involves assessments, training, oversight, and hands-on support for human resource management, financial management, procurement, and auditing which, along with the vital reforms, are leveraged through the large grant funds, or the prospect of grant funds. Ultimately, by helping to strengthen policies and government institutions, we advance the sustainability of our investments and reduce dependency on foreign aid.

MCC is already part of the solution in Central America with over \$320 million currently committed through our compact and threshold programs. MCC has invested more than \$1.1 billion in the region since 2005 seeking to foster the enabling environment for faster economic growth by improving the climate for private sector investment, strengthening human capital to create jobs and opportunities in the region, and reforming public financial management and increasing transparency and accountability to promote good governance and reduce corruption.

After successful completion of its first five year compact with El Salvador, which invested \$461 million to strengthen the transportation, power and agricultural sectors, El Salvador and MCC signed a new \$277 million compact in September 2014 to improve the country's regulatory environment, enhance the role of public-private partnerships in delivering key services, improve the quality of education, and improve a key highway and border crossing infrastructure to reduce transportation costs.

MCC also has threshold programs with Guatemala and Honduras. Threshold programs are significantly smaller grants for countries that are close, but do not yet meet our criteria for a compact. In 2013, we launched a \$15.6 million threshold program with Honduras to improve the country's public financial management and the efficiency and transparency of public-private partnerships. In April 2015, we signed a \$28 million threshold program with Guatemala to support reforms to the country's secondary education system that match skills to labor market demands, and to improve tax and customs administration so that the government can generate greater resources to invest in the Guatemalan people.

### **Constraints to Growth in Central America**

The political economy of Northern Triangle democracies has been characterized by patronage based politics, weak rule of law resulting in gang and drug related criminal activity, low effective tax rates, and a lack of accountability. These factors have led to governments with small budgets that are poorly executed due to corruption and inefficiency, and as a result, they have been unable to adequately provide infrastructure, health, education, and security services to their people.

A lack of critical services over the years has yielded low educational attainment, high transportation costs, and entrenched crime that constrains private investment and job creation and drives migration. These problems affect both the rich and poor in Central America. The wealthy can pay for private schools, health care, and security, but the majority of the people struggle to provide a decent life for their families.

Over the last ten years, we have seen many members of the political and economic elite call for more transparent government, adequate tax revenue, better infrastructure and improved health care, education, and security services. We have also seen citizens take to the streets and

social media to hold their leaders accountable for providing transparent, efficient and effective government.

In response to the desire to tackle these problems and with the support of the U.S. and other development partners, there have been significant efforts recently to improve governance:

- Courageous local prosecutors have taken on political corruption and organized crime with the help of the International Commission Against Impunity in Guatemala, the Mission to Support the Fight Against Corruption and Impunity in Honduras and El Salvador's Anti-impunity Unit within the AG's office
- Governments have increased transparency and exposed themselves to social accountability
- There have been payroll audits to purge government payrolls of dead, absent and non-working recipients
- Progress has been made in making teacher appointments based on merit
- Honduras reduced its fiscal deficit from above 7% to below 2%
- Progress has been made on police reform and neighborhood policing and community outreach has been re-established

These are deeply entrenched and mutually reinforcing problems, and progress has not been universal, but there has undoubtedly been progress.

### **MCC's 2006 and 2014 Compacts with El Salvador**

In 2012, MCC and El Salvador successfully completed a \$461 million compact to strengthen the transportation and agricultural sectors and improve the education system in the country's Northern Zone. The program brought people in the Northern Zone training, education, rural electrification, community infrastructure and 125 miles of road. According to evaluations by independent consultants:

- 146,000 rural residents received access to electrification
- More than 600,000 people benefited from the construction of the Northern Transnational Highway
- Approximately 26,000 received access to potable water
- Approximately 17,000 people were beneficiaries of the Productive Development project, which transitioned producers to higher-profit activities, generated new investment, expanded markets and sales, and created new jobs
- Approximately 12,000 youths were trained in various technical trades
- Approximately 5,000 people, including students and teachers, obtained scholarships for study and training

Households with access to potable water in the Northern Zone increased from 79% in 2007 to 86% in 2011. Electricity coverage increased from 78% in 2007 to 90% in 2011.

After the success of the compact signed in 2006, and with continued strong policy performance as reflected by the MCC policy indicators, MCC and the Government of El Salvador signed a new compact on September 30, 2014 to invest up to \$277 million on improving education, logistical infrastructure, regulatory environment and institutional capacity, with the goal of promoting economic growth and private investment in the country.

El Salvador has committed to increase the country's productivity and competitiveness in international markets by partnering with the private sector to generate economic growth and addressing institutional, human, and logistical constraints to international trade in goods and services. The Government of El Salvador has committed to contribute \$88.2 million to support MCC's investment, double the 15% host country contribution required by MCC, reflecting the government's solid commitment to the compact.

The current compact has three primary projects:

- The Human Capital Project focuses on preparing the people of El Salvador to better meet the demands of a global economy by improving the quality of education and better matching the supply of skills to the labor market. The project is composed of two activities:
  - The Education Quality Activity supports complementary interventions in competency-based education, increased classroom time, teachers training, and improvements to the institutional environment that are conducive to learning. It also includes investments in approximately 344 schools in the coastal zone of El Salvador where dropout rates are the highest, with a focus on grades 7-12.
  - The TVET System Reform Activity seeks to strengthen ties between the skills demanded by the labor market and those supplied by private and public vocational education and training providers. The intended result of the activity is that, students in these TVET programs will graduate with skills that better match the job market.
- The Investment Climate Project is composed of two activities:
  - The Regulatory Improvement Activity is designed to prioritize and promote business regulation reforms resulting in more efficient and profitable operations for firms doing business in El Salvador. MCC funding supports the development of an institutional framework and system, which includes the establishment of an institution that will focus exclusively on regulatory improvement, and the prioritization and implementation of a select set of key reforms. The first reforms package, submitted in December of 2016, contained 36 recommendations in public administration, international trade, and development of public private infrastructure. These reforms will result in more efficient and profitable business operations for the private sector.
  - The Partnership Development Activity seeks to improve the capacity of the Government of El Salvador to partner with the private sector to provide key public goods and services through the use of: (i) public-private partnerships to enable the government to tap private capital to finance, develop, and manage key infrastructure needed to increase productivity, and (ii) the El Salvador Investment Challenge to identify important private investment potential and efficiently allocate limited government resources to public goods and services needed to support this investment.
- The Logistical Infrastructure Project will address two transportation bottlenecks that have led to high transportation and logistics costs for regional trade.
  - The Coastal Highway Expansion Activity will serve to relieve congestion at the most trafficked segment of El Salvador's key coastal corridor.

- The Border Crossing Infrastructure Activity will make significant infrastructure and systems improvements at a major border crossing with Honduras, reducing wait times at the border and relieving freight and passenger traffic congestion.

### **MCC's Threshold Program in Honduras**

Prior to MCC's current partnership, MCC completed a compact with Honduras in September 2010. The \$205 million compact invested in a broad range of constraints to economic growth in the agriculture sector, including assisting farmers with technical training, providing farmers with access to credit, and building farm-to-market roads. The compact also invested in rehabilitating the primary national highway that connects Honduras with international markets.

After completing the compact in 2010, Honduras experienced political instability. Because of this, MCC's Board of Directors did not select the country for a second compact. Honduras was, however, selected as eligible for threshold program assistance to catalyze needed reforms. The Honduran government is subsequently working on substantial reforms to fiscal transparency in order to improve accountability and limit opportunities for corruption, in hopes of qualifying for a compact once again.

MCC's \$15.6 million Honduras Threshold Program is designed to improve public financial management and create more effective and transparent public-private partnerships. The program is helping the Government of Honduras save money in procurement, improve delivery of public services, and reduce opportunities for corruption—ultimately improving the efficiency and effectiveness of how the Government of Honduras uses its own resources. Honduras passed 10 of 20 scorecard indicators in FY17.

The Honduras Threshold Program includes two primary projects:

- The Public Financial Management Project is working to make the management of government finances more efficient and transparent. The project has four activities:
  - The Budget and Treasury Management Activity is strengthening budget formulation and execution in the government's executive and legislative branches. Through the U.S. Department of Treasury's Office of Technical Assistance (OTA), MCC and Honduras are working to strengthen the Ministry of Finance's budgeting capabilities and increase legislative oversight of the budget process. In addition, MCC is supporting an audit of government payment arrears and promoting institutional reforms so that vendors are paid consistently and on time, resulting in increased competition and reduced opportunities for corruption.
  - The Procurement Activity is increasing the transparency, accountability and quality of public procurement. MCC funding is supporting: an e-catalogue that allows bulk purchases, saving time and money; the creation of a procurement evaluation unit to assess the quality of procurement throughout the government; and a procurement training and certification program that includes a legal change to phase-in a requirement for a procurement certified government official to manage procurement processes.
  - The Supreme Audit Authority Activity is strengthening the ability of this governance institution to conduct performance audits.

- The Grant Facility for Social Accountability Activity is designed to increase demand for greater accountability and responsiveness from Honduran public officials and service providers, with the ultimate objective of improving national and municipal government efficiency and effectiveness. The largest grant is \$1.2 million to the local chapter of Transparency International (the Association for a More Just Society) to implement their agreement with the Honduran government to review the performance in procurement and human resource management in the Ministries of Health, Education, Infrastructure, and Security as well as the tax authority.
- The Public-Private Partnerships (PPP) Project aims to improve the efficiency and transparency of PPPs in Honduras by supporting activities designed to increase the government's capacity to develop, negotiate, implement and oversee PPPs. The activities under this project include:
  - The Core PPP Capacity Activity is designed to improve the capacity of, and procedures utilized by, Honduran government agencies with key PPP responsibilities to develop and implement PPPs in accordance with best practices, including by supporting the Ministry of Finance in properly identifying and managing fiscal risks in its PPP portfolio; and
  - The Design and Implementation of PPPs Activity provides specialized technical assistance to improve the development and implementation of PPPs.

### **MCC's Threshold Program in Guatemala**

MCC and the Government of Guatemala are currently partnering to implement a \$28 million threshold program to increase revenues and reduce opportunities for corruption in tax and customs administration, attract more private funding for infrastructure, and provide Guatemalan youth with the skills they need in the job market.

Guatemala did not pass MCC's FY17 scorecard although they did improve and now pass 9 out of 20 indicators – one more than FY16. While Guatemala does pass the democratic rights scorecard indicators - a prerequisite for passing the scorecard overall - it fails the control of corruption indicator at the 22<sup>nd</sup> percentile. MCC recognizes that work remains to improve Guatemala's scorecard performance and its control of corruption score, but believes progress can be made through our partnership to benefit the Guatemalan people.

The Guatemala Threshold Program includes two primary components:

#### ➤ Education Project:

This \$19.3 million project supports the Government of Guatemala in improving the quality and relevance of secondary education to prepare its youth to succeed in the labor market. The threshold program is supporting efforts by the Ministry of Education to develop programs that improve teacher skills, the quality of teaching, and the effectiveness of technical and vocational education and training.

The project promotes high-quality teaching in lower-secondary schools by supporting the Ministry of Education to develop, implement, and refine a continuous professional development system for teachers, as well as establish school networks to improve learning and accountability. The project also helps the Ministry of Education in its efforts to offer

technical and vocational education to students and design and implement new curricula that better meets labor market demand.

➤ Resource Mobilization Project:

This \$5.8 million project increases the availability of revenues by improving the efficiency of tax and customs administration. It also supports the efforts of the Government of Guatemala to design and implement public-private partnerships to attract private funding for important infrastructure projects and free up public resources for citizens.

MCC and the Government of Guatemala together are undertaking reforms to improve tax and customs revenue by reducing the rate of rejected audit cases; using risk management to facilitate clearance of low-risk cargo and compliant traders at ports of entry, focusing on high-risk cargo and traders; implementing a post-clearance audit program for customs; and improving control of the physical movement of people and cargo.

## **Conclusion**

While the challenge in Central America is great, there has undoubtedly been progress in El Salvador, Guatemala, and Honduras and opportunities are at hand to continue that progress. MCC is committed to continuing our work with partner agencies to create the conditions for greater economic growth by improving the climate for private investment, strengthening human capital to create jobs and opportunities in the region, and improving public financial management and social accountability to advance good governance and reduce corruption.

Thank you very much for your time and attention.