

Millennium Challenge Corporation

Aid Effectiveness: Putting Results at the Forefront

MCC's "New Institutional Approach"

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The development community generally agrees on two things: 1) the amount of foreign assistance needs to increase; and 2) foreign assistance needs to be used more effectively. The Millennium Challenge Corporation (MCC) was created to address both of these needs—to increase the amount of United States assistance, but also to channel these resources through a new institution designed to reflect best practice in aid effectiveness.

These best-practice elements are easy to identify in MCC’s institutional framework, and include a governance-oriented country selection process, as well as design and implementation strategies that emphasize broad participation and country ownership. These elements, among others, shape the engagement between MCC and its country partners, and reflect an effort to put into place a *process* that avoids many of the pitfalls that have undermined aid effectiveness in the past.

Enhancing Aid Effectiveness *means* Getting Better Results

Getting the process right is important, but best practice in process does not guarantee tangible and meaningful results on the ground.¹ Consequently, MCC has incorporated a number of additional institutional mechanisms that place the generation of measurable results at the center of its work. These mechanisms also enable external audiences to better understand the intended results and to assess the extent to which MCC meets them.

These additional analytical features include: technical analysis to identify problems and identify possible remedies; benefit-cost analysis to assess the economic justification of the proposed investments; strict monitoring and reporting requirements during implementation; and rigorous independent impact evaluations.

While these methods are tried and tested and broadly accepted within the development community, what is truly innovative about MCC’s approach is the *systematic* application of these analytical techniques to virtually every element of every program and the *transparency* provided by the use of these techniques and MCC’s public dissemination of their outputs. No investment strategy guarantees positive results every time, but MCC’s consistent use of this formal analytical framework helps the agency avoid foreseeable problems and, by documenting investments that fail to meet anticipated targets, will help MCC learn and avoid repeating errors in future programs. Further, by making the analyses available on its website, MCC will ensure that the lessons learned do not remain in-house, but rather will contribute to the growing literature on what works, and what doesn’t, in foreign assistance.

¹ At times, the international discussion on “aid effectiveness” seems more committed to harmonizing processes than to achieving results. The Paris Declaration on Aid Effectiveness, for example, commits signatories to five principles, only one of which mentions results, and that one is termed “managing for results,” again referencing process rather than substance. Improving the *process* of aid is important, but a combination of good processes and poor programs will always deliver poor results.

The MCC Approach

MCC's analytical framework keeps the focus on results throughout the process of compact development and implementation. The framework provides clarity on what MCC and its country partners are trying to accomplish—enhancing economic growth as a means of increasing local incomes and lowering poverty—and this focus on objectively measurable outcomes sharply reduces the ambiguity and sometimes conflicting objectives that can undermine development assistance. By focusing on raising the low incomes that actually define poverty, MCC is able to project the anticipated impacts of our programs before investments are made and to measure the actual results during and after implementation.

MCC's approach to results has three distinct phases:

- i. pre-investment analyses;
- ii. monitoring and assessment in implementation; and
- iii. post-implementation evaluation.

The collection and analysis of quantitative data play a critical role in each phase, helping to identify problems, assess alternatives, track progress, and measure results. In some situations, data are missing and assumptions must be made, but the quantitative analyses are naturally suited to sensitivity analysis, allowing the implications of alternative assumptions to be considered. Ultimately, the strength of the framework emanates from the manner in which it helps, or forces, analysts and decision-makers, within both MCC and its country partners, to state explicitly the basis for their assessments and how decisions were made.

The framework also enhances public engagement by providing accessible information regarding decisions, progress, and results. Even before actual results are generated, the quality of MCC's programs is open to critical review. MCC welcomes discussion of the merits of the 18 country programs that have been signed to date, and a distinctive feature of MCC's approach to results is that an informed discussion of the expected costs and benefits of each MCC activity is possible, even prior to program implementation. MCC is in the process of making its quantitative analyses available on-line as a means of facilitating this important public engagement on its work.²

I. Pre-Investment Analyses

Aid agencies have long struggled with the task of directing their funds effectively. Internal institutional preferences and priorities may reduce the efficiency of their assistance from the recipient's perspective. For example,

² The benefit-cost analyses can be found at: <http://www.mcc.gov/programs/err/index.php>. Information about planned and ongoing impact evaluations can be found at: <http://www.mcc.gov/programs/impacetevaluation/index.php>. MCC will post all reports and the underlying data sets and supporting documents on this website, as well, as they become available.

“tied aid” rules that force aid agencies to procure consultants and materials domestically both raise the cost and lower the effectiveness of the programs. Similarly, sector-specific preferences in the giving country, via earmarks or institutional design and expertise, potentially channel funds away from the areas that might otherwise generate the greatest impact on the beneficiaries. Moreover, these influences can change with the arrival of new personnel or the emergence of new fads in development, sometimes leading to improvements in program focus but almost always disrupting implementation in the field.³

Developing countries often have been culpable, as well, for the dilution of aid effectiveness, presenting laundry lists for aid agencies to fund that often blend domestic *political* priorities with those that reflect objective welfare-ordered priorities.⁴ Sometimes, countries are unwilling to undertake the political or institutional reforms that are essential for the aid-funded programs to work. In other cases, the unwillingness or inability to fund essential operations and maintenance expenditures has become part of a dysfunctional cycle, in which donors pay for much-needed infrastructure, but poor maintenance that leads to its rapid deterioration makes the initial investment unwise—even as it makes a second or third round of investments essential.

MCC was created with an eye to changing this relationship. The institution was insulated from donor-country interests in a number of ways. The transparent use of third-party data to select countries according to performance on a set of objective policy indicators ensures that eligibility criteria rather than geopolitical interests determine which countries get programs. No “tied aid” rules were imposed, nor were any country- or sector-specific earmarks. The principle of country ownership was enshrined to ensure that MCC partner countries would identify their own development priorities within the context of MCC’s institutional objective of reducing poverty by accelerating economic growth and propose activities that they would be willing and able to implement.⁵

MCC uses two forms of pre-investment analyses that are designed to help partner countries to find this subset of national development priorities that will accelerate growth:

- i. a technical assessment of the economic context is undertaken to locate core impediments to growth; and
- ii. project-specific benefit-cost analyses are used to quantify the economic merits of proposed investments.

³ The Paris Declaration is aimed exactly at curbing these kinds of practices that are driven by donor preferences. Getting the aid process right clearly can help eliminate some of the practices that reduce aid effectiveness, even if it cannot guarantee good programs.

⁴ These political priorities are often understandable and need not be considered pernicious. For example, national governments may feel pressure to treat regions equally in terms of the use of central revenues. In some cases, making investments that sustain social stability also support long-term growth. In other cases, however, such considerations may be at odds with both the objective of enhancing efficiency and economic growth *and* the objective of reducing poverty.

⁵ A more complete discussion of MCC’s approach to Country Ownership can be found in a working paper written by Alicia Phillips-Mandaville, MCC’s Associate Director of Development Policy at: <http://www.mcc.gov/documents/mcc-082908-workingpaper-ownership.pdf>

Together, these analyses serve to generate program proposals that have internal economic logic, usually supported by compelling empirical evidence, that the investments will generate adequate returns, shared by the poor, to justify the proposed use of funds.

Constraints Analysis. As the first step towards submitting a proposal, MCC asks country partners to establish local teams to undertake a Constraints Analysis (CA) to identify the main bottlenecks to growth in the local economy. Modeled on the “growth diagnostics” framework developed by Hausmann, Rodrik and Velasco, the CA is a data-driven economic assessment of the possible strategies for promoting growth.⁶

The CA is designed to help countries sort through two competing agendas. On the one hand, national development strategies invariably include an array of priority activities, many of which may have compelling justifications but nonetheless will not lead to economic growth. On the other hand, market-oriented reform strategies preferred by many donors often include a large number of sensible institutional and policy reforms but do not help policy makers decide which are most important and deserving of scarce institutional and human resources and finite political capital. The CA can help country counterparts sift through the evidence to find the appropriate intersection of core priorities that hold the potential to accelerate growth.⁷

When MCC instituted the CA as part of its engagement with country partners in early 2007, it was the first development agency to adopt a form of growth diagnostic as a standard practice. Not surprisingly, country counterparts were unfamiliar with the relevant literature, which was thin, and there were few examples that could be used to guide their analyses. Consequently, the early CA experiences required considerable collaboration as both sides learned how to use the tool effectively.

More recently, however, the growth diagnostic framework has found broader acceptance and use in the development community. In its initial engagements with the two newest country partners, Malawi and the Philippines, MCC found recent growth diagnostic exercises had been recently conducted, in both cases providing a solid basis framework for further analysis and subsequent discussions.⁸ Ultimately, the CA is an analytical framework for focusing on problems that, when appropriately addressed, can be expected to raise incomes.⁹

6 “Growth Diagnostics,” by Ricardo Hausmann, Dani Rodrik, and Andres Velasco, March 2005. The paper can be found online at: <http://ksghome.harvard.edu/~drodrik/barcelonafinalmarch2005.pdf>.

7 Rodrik cautions that the methodology “cannot be applied mechanically,” and MCC, too, is wary of the danger that the CA might become just one more task for countries to complete before submitting their proposal. Nonetheless, MCC believes that the use of economic theory and empirical evidence in this problem identification exercise will help strengthen the quality of programs proposed by country partners.

8 Country partners are responsible for conducting the CA. Where recent growth diagnostics have already been done, however, MCC does not demand redundant analysis, and may accept existing growth diagnostics funded by others. In such cases, however, country partners need to present the report as representing their own views of the core economic impediments to growth or amend the report.

9 For example, in countries where there is clear evidence that the road network is an impediment to growth, sensible investments to improve the network (and the system that maintains it) could be expected to generate adequate returns; in contrast, where transportation costs are low and the system is working well, the CA should direct country teams towards other sectors to look for high-return investments. Readers can learn more about the practical conduct of such analyses in: “Doing Growth Diagnostics in Practice” by Ricardo Hausmann, Bailey Klinger, and Rodrigo Wagner: <http://www.cid.harvard.edu/cidwp/pdf/177.pdf>.

Results-Focused Project Design. The initial CA identifies a small number of sectors where problems may be limiting economic growth. Partner countries need to extend this analysis to identify the root causes of problems, formulate potential solutions, and evaluate alternatives to define investments for MCC consideration. This more detailed diagnostic exercise relies crucially on stakeholder consultations and participation, and should demonstrate a chain of results from project inputs, to activities, outputs, outcomes and long-term impacts.¹⁰ By focusing on expected results from the very outset of project design, our counterparts are encouraged to develop the indicators and associated baseline and target values for tracking the performance of each proposed investment.

Benefit-Cost Analysis. As country partners move from problem identification to the development of specific investment proposals, MCC encourages them to consider multiple alternative responses and requires them to evaluate the possible activities using benefit-cost analysis (BCA) models. MCC's approach is generally consistent with standard practices used by other foreign assistance agencies and those used by domestic US government agencies.¹¹

Perhaps the most important distinction of MCC's approach is on the benefit side, where BCA models only include changes in local income. MCC's mandate starts with the recognition that income-based poverty measures are broadly accepted and used around the world; if an agency has as its mission the reduction of measured poverty, it needs to be able to demonstrate that it is raising incomes.

While the multidimensional nature of poverty is also widely accepted in the development community, most of these dimensions are themselves positively correlated with income levels. Access to education and health care services, for example, improves almost everywhere as incomes rise. Indeed, the importance of raising incomes for the poor can only be understood in the context of the additional needs that will be met—food, clothing, schooling, health care.

From an institutional perspective, this focus on incomes actually enables MCC to talk about results in a rigorous fashion. Because costs and benefits are measured using the same metric, MCC is able to ask the fundamental question of aid effectiveness—do the expected results of this program justify the allocation of scarce aid dollars to this specific activity?

¹⁰ This terminology is adapted from the Organization for Economic Co-operation and Development (OECD) Development Assistance Committee (DAC). See OECD-DAC. 2002. *Evaluation and Aid Effectiveness. Glossary of Key Terms in Evaluation and Results Based Management.*

¹¹ MCC practices are broadly consistent with those described in OMB Circular A-94: <http://www.whitehouse.gov/omb/circulars/a094/a094.html>. There are a few notable differences, including the role of “international effects,” which are central to MCC's work but are treated differently by domestic agencies. Another important distinction is that MCC calculates “economic rates of return” and compares them to country-specific hurdle rates, rather than using a standard discount rate to calculate Net Present Values (NPVs) for each project. When MCC reports NPVs as additional information, a 10% discount rate is used rather than the 7% rate described in the OMB circular, consistent with the conventional practice in international development and reflecting the expectation that the opportunity cost of capital is higher in developing countries than in the US.

The formal representation of a development project in this fashion helps (or forces) program planners to be explicit about each element of the project: what will be done; when it will be done; how much it will cost; what the results will be (in measurable ways). For each of these steps, credible evidence is required to demonstrate that the model (and the project it represents) is plausible. Subjective judgments can never be eliminated from the decision process, but BCA places a premium on objective, quantitative information wherever possible and identifies those places where subjective judgment is required.

How MCC uses BCA results. This specification of activities and the channels by which the activities will raise incomes enables MCC to review and verify the BCA models and all underlying assumptions and evidence. But the value of benefit-cost analysis goes well beyond the final decision to invest (or not). First, country partners use BCA results to help prioritize among the proposed activities—often an essential task when not all of the requested activities can be funded. Second, country partners, often working with MCC, can use the results to redesign the project to lower costs or to enhance benefits. If the ERR for paving a rural road is very low, for example—reflecting high construction costs relative to the anticipated use of the road—program designers might consider lower-cost alternatives for finishing the road. Third, the final BCA models enable outside observers to review decisions made by country partners and by MCC and to hold both parties accountable for the use of the funds. Local observers can question the domestic priorities reflected in the country proposals, and MCC decisions are also opened to review and scrutiny in a way that would not be possible without BCA.

Conducting Benefit-Cost Analysis

Costs. BCA models begin with an itemization of the costs of the program that flow from its final design. Costs include those covered with MCC funds, as well as expenses covered by other sources, such as other donors or beneficiaries. Costs can change as design elements are refined to maximize impact, to enhance targeting, or to better reflect the resources available, and reflect the best understanding of future prices.

Benefits. Projects are expected to generate tangible outcomes that will lead to higher incomes for beneficiaries, and the benefit streams reflect this underlying logic. The actual mechanisms linking investments to higher incomes vary across project types, but in every case the logic linking activities to higher incomes should be clear. For example, improved village water supply can raise incomes in three ways: 1) by making possible new investments, often at the household level; 2) by saving time by bringing sources closer to homes, with the saved time then used in other ways to raise incomes; and 3) by lowering the incidence of water-borne diseases, leading to fewer sick days and higher productivity. These benefit streams usually can be estimated using information that has been gathered about the effect of similar projects elsewhere.

Counterfactual. To estimate **net** benefits, BCA models require an explicit assumption about what would happen without the project. This “counterfactual” scenario takes into account recent trends of rising (or falling) productivity and incomes to isolate the changes in the future that will happen as a result of the program.

Economic Rate of Return. The estimated ERR is defined as the interest rate at which net benefits would equal zero. If the ERR is higher than the hurdle rate (which is country-specific but always falls between 10-15%), MCC considers the project to have an economic justification to proceed.

In making its final investment decision, MCC considers factors other than the ERR. As a result, a project with a low ERR might be approved or a project with a high ERR might be rejected on the basis of other considerations. Even in such cases, the estimated ERR provides a solid foundation for assessing how much non-economic benefits/costs might be needed to justify an investment decision given the ERR.

BCA and Aid Effectiveness. Whenever discussions of “aid effectiveness” focus solely on process, they miss the point that more effective foreign assistance means generating more results. Almost any development project will generate *some* results for beneficiaries, and too many project reviews do little more than claim to have had a non-zero impact.¹² The use of anecdotes to describe results—a project helped 5 businesses, 20 farmers, or 100 women—is perhaps the most common example of this. Such stories may reflect real impact, but are the gains important enough to justify the investment of \$1 million? \$5 million? \$50 million? Anecdotes and unquantifiable benefits cannot provide consistent answers to these questions.

MCC uses BCA to break with this practice by explicitly asserting that aid effectiveness means investing foreign assistance resources in ways that generate *enough* benefits to justify the cost. This standard for results is not only much higher than “more than zero impact” reflected by anecdotes; it is also more objective and more transparent. Using pre-investment analyses to identify activities that have a plausible prior expectation of adequate results does not guarantee success—but BCA

Benefit-Cost Analysis provides a pre-investment estimate of impact

BCA provides a detailed description of a proposed activity, and allows MCC and its country partners to understand the anticipated impact of the activity on local incomes. Many country programs include agricultural components similar to the following example:

Agricultural Training Proposal. A project aims to train 10,000 farmers to grow fruit as a means of raising household income by 50%.¹ The BCA model would describe the elements of the project below and provide evidence that the numbers were realistic:

- the method for delivering the training (e.g., government extension agents, NGOs, private consultants) and the corresponding costs;
- the anticipated adoption rate among those receiving training (usually well below 100% of participants will actually use the new practices);
- the average expected change in the pattern of production (adopters usually change practices on only part of their land); and
- the average expected additional income earned by farmers adopting the new practices compared to the counterfactual of what they would have earned without the training.

By comparing the anticipated benefits of the project with the expenditures that are required to accomplish the targets, MCC and its country partners can assess the economic rationale of the investment. Raising farm incomes by 50% is a laudable objective, but the economic rationale for the project also depends on how much it costs.

¹ Development agencies fund such projects all the time, but it is surprising how rarely they are subjected to formal BCA to determine whether the anticipated gains are plausible given recent experience and available evidence and, if so, whether the benefits justify the expenditures of the project.

¹² The term “non-zero” reflects the reality that development activities almost always can be expected to have *some* positive effect, but if one cannot say “how much,” one cannot demonstrate that the benefits justify the use of a given amount of scarce development assistance.

is an essential element of an approach that helps MCC avoid investing in activities that lack a reasonable prior expectation of tangible and measurable success.

Of course, the quality of the analysis matters, too. In a review of the practice within the World Bank, one study compared program outcomes with the *quality* of pre-investment assessments and found that projects that had poor-quality assessments were 7 times more likely to perform unsatisfactorily after 3 years, and 16 times more likely after 4 years.¹³ MCC oversees the quality of its BCA process in a number of ways. The initial work, whether generated by country counterparts or consultants, is reviewed by MCC staff economists. These BCA models are subject to an additional peer review by economists outside the country program. The public posting of the models on the MCC website provides a final layer of transparency and review.

II. Monitoring in Implementation

Of course, *predicting* results with BCA is not the same as *measuring* actual changes experienced by households and firms in low-income countries. Focusing on investments with high ERRs does raise the probability of success, but even the best designed activities can encounter difficulties in implementation that lead to lower-than-expected results. To mitigate this risk, MCC works closely with country counterparts—the local institutions accountable to MCC for implementing the program—to develop a Monitoring and Evaluation (M&E) plan that provides timely information of the status of each activity.

MCC requires that every Compact include a formal M&E plan, making this management tool a core part of the bilateral agreement. MCC agrees to provide the funds necessary for the program, but country partners not only accept responsibility for implementing the program according to the M&E plan, but also for reporting progress on a quarterly basis with reference to that M&E plan. Such a framework makes it possible for MCC to hold up subsequent disbursements until adequate documentation is provided that the previous funds have been spent and relevant milestones have been met.¹⁴

The Link between BCA models and M&E Plans

A further value of the formal benefit-cost models is that they form the basis for developing M&E plans. BCA models, which include an accounting of costs for each activity during the five-year Compact, directly suggest implementation timeframes, with a sequence of key milestones and deliverables emanating from both cost and benefit calculations. In particular, the estimated benefit streams are logically and explicitly linked to anticipated

¹³ See Jenkins, Glenn P. “Project Analysis and the World Bank,” *American Economic Review*, May 1997, 87(2), pp. 38-42.

¹⁴ In this context, pressure on MCC to accelerate disbursements can have a perverse effect on results, as the message communicated to country partners is *spend* rather than *spend well*. Indeed, local MCC partners may both need and desire the threat of suspended disbursements to provide the incentives to their local partners to perform their responsibilities.

outputs (e.g., numbers of farmers trained) and outcomes (e.g., higher incomes among adopters), all of which are specified in quantitative terms.

The connection between the BCA and the M&E plan is important. As long as both parties, MCC and its country partners, accept the specifications in the pre-investment BCA model, they also accept that implementation should be able to proceed according to the assumptions in the model. In this way, the expectation of formal mutually-accepted M&E targets imposes an inherent discipline on the prior mutually-accepted BCA. If the implementation milestones are known to be optimistic or unrealistic, then the original BCA is itself flawed and likely overstated the eventual results.

M&E Plans in Implementation

By definition, pre-investment analyses and the pre-implementation M&E plans cannot incorporate unanticipated changes in the economic context. For example, while a good BCA model should incorporate risks and uncertainty associated with regular weather patterns (including infrequent but regular random events, like droughts that hit once every three years, on average), the best models will poorly represent implementation experience when the once-in-a-century flood hits twice during the five-year program.

Few analysts in the private sector (and fewer in the international aid community) anticipated the effect of construction related to the 2010 World Cup in Africa on the availability of contractors in the region, a factor that partly explains the higher-than-expected bids being tendered for competing construction activities (like those funded by MCC). Even fewer analysts predicted the recent price spikes in energy and food markets. These latter price movements are also producing higher bids, as well as generating a systematic pattern of unavoidable cost overruns for projects already contracted in 2006 and 2007.

Revising implementation strategies. While M&E plans cannot avert or neutralize the effect of sudden price movements (or other factors that may lead to missed implementation targets), they are a vital early warning system that flags non-performance both for MCC and our country counterparts and sets into motion institutional responses to redress the cause of non-performance, when possible. In some situations, revising the implementation plan (e.g., hiring independent contractors rather than relying on public agencies or NGOs) may be an adequate response that gets implementation back on track.

Restructuring Compacts. In other cases, such remedies may not be possible. The recent price changes mentioned earlier, for example, effectively reduced the real value of the Compact budget for some MCC partners. What once were reasonable pre-investment estimates suddenly were seen as significantly underfunded budgets, and MCC has little recourse to add funds to enable completion of the full proposal. In such cases, M&E plans and the data reported against those benchmarks makes it possible for MCC to collaborate with country partners to find an acceptable solution.

When all of the activities retain an economic justification, even in the higher price environment, MCC may encourage its partners to locate additional funding from other sources. In other cases, some elements of the country program may no longer have a compelling economic rationale—a road or a bridge that made sense when prices were low may no longer be a national economic priority if it costs twice as much.¹⁵ In such cases, MCC has found that country partners are prepared to restructure their program by shifting MCC resources out of lower-return activities. By eliminating certain activities, country partners may be able to free up enough resources to complete implementation of the most important high-return activities in their program. The number of beneficiaries may fall as a result of this restructuring, but the overall economic return on investment might actually go up as a result of the elimination of low-return investments.¹⁶

M&E Plans and Future Compacts

As the earliest compacts near completion, MCC anticipates that many partner countries will be interested in the possibility of a second compact. Indeed, a number of countries have already inquired as to whether program planning can begin soon to avoid or minimize the gap between the completion of the first program and the commencement of the second.

In these preliminary conversations, progress to date, as measured by regular reports against the M&E plan, provides important information that can be used by MCC in two ways. *First*, reports of implementation provide an initial indication of whether the project met its targets in implementation, not just in terms of outputs (e.g., number of farmers trained), but also in terms of outcomes (e.g., additional income generated for beneficiaries). This information will help inform any discussion of whether a project should be funded by MCC in a second program (either expanded or sustained). In most cases, MCC and country partners should be able to revisit and revise, as necessary, the ERR projections that were made for the first compact using actual values for a proposed second program. In some cases, the M&E results will help reshape or rescope the program design for future years.

Second, the M&E plan provides a useful accounting of the institutional relationship between MCC and its country partners, and between those partners and their implementing agencies. This performance record should help all parties assess the past engagement and identify areas that need to be improved in a future program. Indeed, the hope for a second compact may be an important incentive for some country partners to be able to demonstrate publicly the successful performance of the first compact.

The M&E plan is an important tool, then, both for MCC and its partners. It is used to establish clear and measurable objectives that, in turn, make it possible to report progress during implementation and the achievement of

¹⁵ Of course, price changes that raise costs also are likely to affect the estimated benefit streams, and MCC considers both effects when it reviews the economic models of current programs.

¹⁶ Often MCC staff collaborate with country partners to revisit original BCA models. During implementation, new data on parameters (e.g., prices, quantities) and relationships may make it possible to update the analysis. The results are used to inform decisions to adjust the implementation strategy to enhance the impact of the overall program. When such analysis is done, the results will also be posted on MCC's public website.

targets at the end of the program (or sooner). In this way, the M&E plan underpins accountability for results for all relationships. Country partners and their implementing agencies are accountable to MCC, to the intended beneficiaries, and to the broader societies that supported the original program designs. MCC is accountable to country partners for providing the obligated resources and support, and also accountable to American taxpayers to deliver results. The systematic use of M&E plans, with their measurable targets, makes it possible for each of these parties to acquit their responsibilities.

III. Independent Impact Evaluations

Sometimes, reporting on progress and accomplishments relative to the M&E plan provides an adequate basis for assessing results. The initial BCA models estimate what would have happened without the project, so attaining of targets may be seen as evidence of results. Where program implementation approaches are well-established and results are predictable, a good monitoring plan will document the achievement of those results.

In other contexts, however, projects are proposed for which there is little evidence of predictable results. Program designers may find it impossible to build BCA models for such projects with any confidence. Indeed, partly because donors in the past have been reluctant to devote scarce resources to post-project studies of effectiveness, those same donors today find themselves funding a wide array of activities that have little solid evidence of more than a non-zero impact.

MCC faces this dilemma, too, as countries may propose remedies that have little supporting evidence. In such cases, MCC and its country partners still formulate BCA models to estimate the likely results, but recognize that even the best information on program effects may allow only speculative estimates. Where there is little expectation of results, MCC might decide not to fund those activities; but in cases where project implementation may provide useful new information, MCC may fund both the project (sometimes on a pilot scale) and an independent impact evaluation.

The Essence of an Impact Evaluation. The term “impact evaluation” (IE) commonly refers to program assessments that are designed to compare changes in income among program participants to changes in income experienced by a similar population group that is not included in the program (often referred to as the “control”). In this way, an IE makes it possible to measure what would have happened without the program (the counterfactual scenario in BCA models).

An agriculture program, for example, might report huge income increases among the farmers who received training, meeting the targets set in the M&E plan. An outside observer, however, would not know if these gains were *caused* by the program or by some other factor, such as early and ample rains. By measuring changes in incomes for program farmers and for similar farmers who received no training, the results of an impact evaluation can

determine whether it was the program (only program farmers experienced higher incomes) or the weather (all farmers experienced higher incomes).

Limitations on the use of IEs. Given their value, one might want to conduct an impact evaluation on every project. Unfortunately, there are a number of factors that limit the use of IEs. *First*, such evaluations are costly. A rigorous study of a 5-year agricultural training program might cost several million dollars, funds that might otherwise be used to train more farmers.¹⁷ *Second*, such evaluations often require modifications to the implementation plan, and sometimes these adjustments are deemed to be unacceptable.¹⁸ *Third*, there are programs that are so idiosyncratic that conducting an IE would not generate useful information for future programs. And *fourth*, some program designs and sectors simply do not allow the identification of a reasonable control population. But while each of these concerns may limit the opportunities to use IEs, there is a growing recognition within the development community that there have been far too few, rather than too many, independent impact evaluations.¹⁹

The Rationale for IEs. Given the difficulty and expense of IEs, MCC uses resources budgeted for rigorous evaluations judiciously. To determine which activities should be evaluated, MCC looks at three factors: i) the need for information, as described above; ii) the learning potential from the evaluation; and iii) the cost and feasibility of implementing the IE.

The learning potential reflects the idea that IEs are often best considered a global public good, in that the total benefits from the research may far exceed those enjoyed by the people involved in the study, and include those benefits accruing to other potential participants in future programs (and in other countries). Indeed, in some cases, an IE may add little benefit to the particular program being studied.²⁰ An evaluation may have great value, nonetheless, if other donors can use the results of the IE to design better aid programs and public services, and country partners often anticipate that the IE findings will help inform the design and implementation of future activities, as well. Today, few donors doubt the necessity of investing more in IEs, but MCC remains at the forefront in terms of the frequency with which it conducts these rigorous independent reviews and the transparency to which it has committed in disseminating the findings.

17 Of course, the response to this possible objection is that, without an IE, donors cannot be sure that farmer training programs are the best (or even a good) use of those resources.

18 Objections to adjusting the implementation plan to accommodate an IE may come from country partners, implementing agencies, and even beneficiary populations. In the absence of prior evidence about expected results, however, a decision to invest without an IE seriously weakens the link to results.

19 In 2004, the Center for Global Development convened a working group to study the practice of impact evaluation in international development. The report of that working paper, entitled “When Will We Ever Learn? Improving Lives through Impact Evaluation” documents the magnitude of what they term an “evaluation gap,” and can be found online: <http://www.cgdev.org/content/publications/detail/7973>. Another compelling discussion of the important role of IE in development can be found in Abhijit Banerjee’s essay, “Making Aid Work,” published in the July/August 2006 issue of the Boston Review, parts of which are available online at: <http://bostonreview.net/BR31.4/contents.html>.

20 In some cases, mid-term surveys may provide information that is useful to program implementers, but the final evaluation results usually come too late to inform the implementation of the project being studied.

The Independence of Impact Evaluations at MCC. MCC works with country counterparts to identify opportunities within the proposed program for conducting an IE. MCC is unlikely to proceed with an IE unless there is strong local buy-in from relevant government agencies and the local populations (both beneficiaries and the necessary control groups). Without such support, the risk of failure is simply too high, as problems may arise midstream that scuttle the IE and lead to a waste of evaluation resources.²¹

While MCC works closely with country counterparts in the early stages and includes IEs as part of the formal M&E plan, IEs are generally financed separately from the compact with funds that remain under MCC's control. Moreover, IEs are performed by independent contractors, often affiliated with universities or think tanks, whose distance from the project enables them to make objective assessments of the program's impact.

Further, MCC protects the independence and integrity of the evaluations by making all of the relevant information available to the public in a timely manner. While this claim may sound premature given that no IEs have been completed to date, MCC has made the commitment to disseminate all relevant information on its website, adding a mechanism that provides for external scrutiny.

MCC has already listed all IEs currently underway, along with an explanation of the project activity, the intended results, and the plan for the IE. After each evaluation is completed, MCC will make all data available online, as well, to allow other scholars to review, critique, and possibly extend the work. Moreover, all contracts with independent evaluators explicitly allow them to publish their work independently; in other words, MCC will use its own website to disseminate the results, and indeed may add commentary to explain projects and interpret results. But MCC understands that the value of IEs comes from the broader dissemination of information and the learning that comes from both success and failures. Indeed, both are important elements of enhancing aid effectiveness.

Conclusion

This analytical framework helps both MCC and country partners retain a focus on results throughout the compact development and implementation processes. While naturally it cannot guarantee that any activity will have the anticipated effect, the approach introduces a number of important elements into MCC's business model that should improve effectiveness (i.e., increase the impact on local incomes).

²¹ While the agreement to include an IE may generate real and broad excitement in the planning stage, support may wane during implementation for a variety of reasons, most related to unforeseen difficulties that slow or undermine the generation of results. For example, the implementing partners responsible for a training program that experiences lower-than-expected take-up implementing partners may want to tap into control populations to meet targets, but by doing so may undermine the ability of the expensive evaluation to generate meaningful information. In other cases, early evidence that a program is ineffective may come with a vested interest in the program to argue against a rigorous IE and favor other evaluation methods that may be more ambiguous in the conclusions. To mitigate these risks, MCC invests considerable effort in the earliest stages to ensure broad acceptance of the value of the IE, especially among those groups that value the information that will be generated.

- ★ The problem identification process keeps the discussion focused on investments that will accelerate economic growth and will steer the process away from investments that may have political value but limited economic merit.
- ★ The benefit-cost analysis requires an explicit description of activities and anticipated outputs and outcomes, which allows a series of reviews that protects the integrity and transparency of the process. As a result, claims of expected results can be tested *before* investment decisions are made to ensure that proposed projects make sense.
- ★ The M&E framework ensures that the requisite information is being collected and reported regularly. This process provides helps country partners identify projects that are encountering difficulties, allowing a sensible restructuring or reprogramming of their funds. The M&E framework also allows an assessment of results for most MCC-funded activities.
- ★ The commitment to undertake independent impact evaluations reflects MCC's emphasis on results, as such studies can be expensive and can take years to generate actionable information. At the same time, however, the aid community now accepts that it has underinvested in impact evaluations, leaving questions unanswered and allowing donors to repeat mistakes. MCC seeks to be innovative in its programming, but also recognizes that experimentation without evaluation undermines aid effectiveness.

With this in mind, MCC's framework on results places great emphasis on what is known and what is reasonable, even while seeking opportunities to add to the body of knowledge about what donors can do to improve the lives of their beneficiaries.

MCC's model of using foreign assistance as an investment that will raise incomes in poor countries is at a critical juncture. Some observers ask, "What has MCC accomplished?" That question cannot be answered without referring to the mechanisms that MCC has institutionalized to predict, track, and measure results.

Of course, MCC is already reporting preliminary information on performance in implementation, but many MCC investments, including those in health and education, will take years to complete and then effect change in people's lives. Long-term investments in sustained economic growth represent an *essential* element of any effective poverty alleviation strategy, and MCC's analytical approach ensures that its funds are used effectively to that end.

Describing Results

Describing results clearly and publicly should be an essential part of any development agency's mandate, and yet few are able to clearly communicate the impacts they are having. Given the best intentions within the development community to help the poor and the competition among implementers for donor funds, this paucity of results is surprising.

One part of the explanation for the lack of "results" statements is surely the disincentives to report failures. Although everyone recognizes the need for more development assistance and more effective assistance, they also understand that these two objectives may conflict at times. Reporting failures may generate the perverse result of fewer funds flowing to a specific country or sector, even though the reported failure might serve to enhance the effectiveness of the next round of investments, whether the resources come from MCC, some other donor, or domestic revenues.

Another part of the explanation for poor reporting in the development community is that a **good** description of results is almost always a **complicated** story of results. Reporting the number of beneficiaries, for example, the easiest standard, suggests implicitly (and incorrectly) that higher numbers are necessarily better than lower numbers. In fact, the **number** of beneficiaries by itself is essentially a meaningless statistic. Is Program A, with 100 beneficiaries, better than Program B, with only 50? The answer depends on a number of other factors.

Magnitude of benefits. In addition to the number of people touched by the program, one also needs to know the average size of impact on each person. Some investments, like roads, affect large numbers of people, raising incomes for many, but only by a little bit. Other investments target small numbers but deliver significant benefits to those fortunate enough to participate. Clearly, to say anything meaningful about whether Program A or B is better, one needs to know **both** the number of beneficiaries and the size of the average benefit. If Program A delivers only \$1 of benefits to 100 people (\$100 total benefits), most observers would prefer Program B that helps only 50 beneficiaries but delivers \$10 of additional income to each (\$500 in total).

Cost of the program. While Program B is seen to deliver five times as many benefits, we also need to know how much each program costs to make a fair comparison. If Program A described above costs only \$100 to deliver \$100 of benefits, it likely would be preferable to Program B that costs \$1,000 but delivers only \$500 in benefits (this is not an implausible scenario—many development projects that are only able to document non-zero benefits are, in fact, generating benefits that are less than total investment costs).

Timing of costs and benefits. Benefits today are more valuable than benefits in the future and costs tomorrow are preferable to costs today; this is especially true for poor households that desperately need resources **now**. Accordingly, a reasoned comparison of projects needs to properly discount future benefits and costs. Even if Programs A and B cost the same amount, Program A that delivers \$100 in the first year would probably be preferred by most households to Program B that delivers nothing for 19 years before providing \$500 in the 20th year.

Distribution of benefits. Finally, one needs to know **who** in society receives the benefits. A project that generates \$500 of benefits, but excludes poor households from participating, may have a much smaller impact on poverty than a project that generates fewer benefits but includes a means-test that allows participation only by the poor. Of course, such extreme results are unlikely. MCC would never fund a project that delivered benefits

Describing Results (con't)

only to the rich, and even the best-targeted programs find it impossible to include only the poor (and programs that generate benefits **only** for the poor may not have the broad social support that is necessary for sustained implementation). In most cases, country proposals to MCC focus on expanding the size of the economy rather than trying to reshape the distribution of wealth, and the connection between rapid economic growth and poverty alleviation is well-established. At the same time, however, MCC is incorporating more rigorous assessments of the distributional impacts of its programs to better document the impact they are having on low-income households. This distributional analysis will provide information not only on the number of beneficiaries, but also the amount of benefits and demographic information describing the distribution of benefits to the extent feasible and reasonable, given the available data.

To fully understand the impact of a foreign assistance program, one needs to assess not simply the number of beneficiaries, but also the total amount of benefits, the total costs, the timing of benefits and costs, and the distribution of benefits and costs. The complexity of the story certainly at least partly explains why so few aid agencies regularly describe the overall effect of their programs on the poor.