



**MILLENNIUM
CHALLENGE
CORPORATION**
REDUCING POVERTY THROUGH GROWTH

FRANCES C. MCNAUGHT
VICE PRESIDENT, CONGRESSIONAL AND PUBLIC AFFAIRS

CONGRESSIONAL NOTIFICATION TRANSMITTAL SHEET

We wish to inform the Congress of our intent to provide funding of up to US\$284,911,363 for a Millennium Challenge Compact with the Government of Mongolia.

Allocation and obligation of funds may be incurred on or after fifteen days from the date of this notification. MCC intends to obligate pursuant to Section 605 of the Millennium Challenge Act of 2003 (the "Act") up to US\$280,722,013 when the Compact enters into force. These funds will be disbursed on a periodic basis over the course of the Compact subject to satisfaction of relevant conditions precedent.

In order to accelerate implementation of the Compact, MCC will obligate up to US\$4,189,350 of the total amount when the Compact is signed, pursuant to 609(g) of the Act.

The attached notification is being sent to Congress on September 12, 2007.

Sincerely,

Frances C. McNaught
Vice President
Congressional and Public Affairs

Enclosure:
As stated

CONGRESSIONAL NOTIFICATION
September 12, 2007

Pursuant to the Continuing Resolution of 2007 (P.L. 109-3833), the Millennium Challenge Corporation (“*MCC*”) wishes to notify the Congress of MCC’s intent to enter into a Millennium Challenge Compact (“*Compact*”) with the Government of Mongolia (“*GoM*”) through which MCC will grant up to US\$284,911,363 of FY 2007 Millennium Challenge Account (“*MCA*”) funds. MCC intends to obligate up to US\$280,722,013 under Section 605 of the Millennium Challenge Act of 2003 (the “*Act*”) when the Compact enters into force. These funds will be disbursed on a periodic basis over the course of the Compact subject to satisfaction of relevant conditions precedent. In order to accelerate implementation of the Compact, MCC will obligate up to US\$4,189,350 of the total amount (“*Compact Implementation Funding*”) when the Compact is signed, under Section 609(g) of the Act.

The Compact Implementation Funding is included in the total amount of MCA funds under the Compact and will not increase overall MCA funding commitment to Mongolia. These funds will support the following projects (each, a **Project**):

1. Rail Project
2. Property Rights Project
3. Vocational Education Project
4. Health Project

Under Section 610(a) of the Act, the appropriate Congressional committees were notified on September 12, 2007 of MCC’s intent to commence negotiations with Mongolia. Key elements of the Compact are set forth in the accompanying summary. MCC will provide final text no later than 10 days after the execution of the Compact, as provided in Section 610(b) of the Act.

MILLENNIUM CHALLENGE COMPACT BETWEEN THE UNITED STATES OF AMERICA, ACTING THROUGH THE MILLENNIUM CHALLENGE CORPORATION, AND THE GOVERNMENT OF MONGOLIA

The Board of the Millennium Challenge Corporation has approved a five-year, \$284.9 million Millennium Challenge Compact to reduce poverty and increase economic growth in Mongolia.

The Compact is focused on increasing (i) rail traffic and shipping efficiency, (ii) the security and capitalization of land assets and herder productivity and incomes, (iii) employment and income among unemployed and marginally employed Mongolians, and (iv) adoption of behaviors that reduce non-communicable diseases and injuries that have the greatest impact on mortality. The program under the Compact (**Program**), in varying degrees, are expected to impact a very large percentage of Mongolia's projected population by 2028. As a result of the Program, we expect per capita incomes for all Mongolians to be 3.5% higher five years after the start of the Program than they would have been without the Program, and to increase by a total of 4.5% within 20 years after the start of the Program. These increases correspond to increments of \$158 million to annual gross domestic product (**GDP**) after five years, and \$404 million after 20 years.

Background

Mongolia is a landlocked country with a population of approximately 2.8 million, located between Russia and China. Nearly half of the population is concentrated in Ulaanbaatar, its capital, about 60% lives along the rail corridor between Russia and China, and the remainder is largely dispersed throughout the country. Mongolia's aging transport infrastructure and weak institutions are a significant constraint to economic growth and development, particularly given the pressures of the country's abrupt transition to a market economy, the collapse of financial support from Russia, and the rapid urbanization of what traditionally has been a highly dispersed rural herding society. The proposed Program is intended to release the potential of certain critical interlocking human, institutional, and physical resources that factor centrally in Mongolia's efforts to broaden and deepen economic development.

The strategy behind the Program is twofold: (i) to encourage broader and more sustainable growth in the economy by intervention at a critical point of vulnerability currently constraining that growth, and (ii) to target poverty reduction by enhancing the ability of Mongolians, especially the poor and marginalized, to participate more effectively in the developing economy. More specifically, the Program is designed to increase economic activity, including exports, through a substantial improvement in the efficiency and capacity of the rail network, the economic backbone of the country. In addition, the Program is intended to increase opportunities of ordinary Mongolians by enabling them to capitalize on their land assets more effectively as a platform for family income improvement, helping them to qualify for the more demanding and financially

rewarding market-oriented jobs required in a developing economy, and ensuring that they become healthier and more productive as they enter the marketplace. Finally, the Program is structured so as to enhance the sustainability of the proposed Projects by, among others, promoting both long-term changes in the legal and regulatory environment needed to enable the Projects, and building capacity to ensure that the Mongolians can carry forward the Program's intended transformational impact.

A. Rail Project (\$188.38 million)

Mongolia's rail system is the transportation backbone of the economy, contributing more to GDP than in any other country.¹ The rail system moves 97% of the ton-kilometers of freight transport in Mongolia. The existing railway company (*MTZ*), in which the GoM and Government of the Russian Federation each own a 50% interest, operates Mongolia's railway system. This system, with its antiquated infrastructure, equipment and practices, cannot meet current demand for rail services and poses a serious economic bottleneck by limiting growth in domestic and foreign trade and associated investment, and contributing to inflation. The Rail Project addresses this bottleneck through improvements in the efficiency and capacity of the rail system, thereby creating new jobs in industries and businesses related to, or served by, the rail system. To ensure these improvements are sustainable, the Project promotes international-standard rail operations and management practices, transparency of rail finances, and commercialization of the rail system – all part of the foundation for greater private sector involvement and competition in rail transport.

The Project includes (i) the acquisition of certain key rail assets (*e.g.*, locomotives, wagons, signaling equipment and track maintenance equipment) needed to improve efficiency and capacity on the country's single track rail line, (ii) the establishment of a new, initially government-owned, contractor-operated leasing company (*LeaseCo*) to lease rail assets on commercial terms to MTZ and independent shippers, (iii) substantial operational training and financial management technical assistance to MTZ, and (iv) technical assistance to the Mongolia Railway Authority, the recently established regulator of the rail sector. The use of LeaseCo allows the Project to avoid the risks inherent in making equipment available directly to MTZ prior to its achieving commercialization and an acceptable level of transparency. Success will be measured by the increase in Mongolian traffic on the rail system, enhanced revenues for both shippers and the rail system, positive changes in the efficiency of MTZ's operations, and increased economic growth associated with rail traffic capacity and efficiency improvements.

B. Property Rights Project (\$23.06 million)

The inability of Mongolians easily to register and obtain clear title to their land poses a serious obstacle to the GoM's promotion, through policy and legal reforms, of private real property ownership. The problems in the implementation of such reforms have

¹ With 4.93 traffic units (*TUs*) per \$ of GDP, compared to the world average of 0.42 TUs per \$ of GDP, Mongolia ranks first among world railways. See www.adb.org/documents/reports/consultant/best-practices-railways/study-report.pdf.

limited access to credit for small landholders and small business people, discouraged investment, and slowed the deepening of local financial markets. The Property Rights Project will help Mongolian citizens obtain secure, long-term rights to the suburban and peri-urban land they occupy, and promote investments in home improvement, business activities, and agricultural productivity. In a banking sector marked by high interest spreads, the Project will encourage financial institutions to reduce the risk premium on credit by providing their customers with a more secure source of collateral and encourage the emergence of new mortgage-related and other asset-dependent financial products.

This Project will improve the accuracy, accessibility and efficiency of the formal system for recognizing and transferring land rights and will facilitate issuance of up to 75,000 privatized and registered land titles to suburban landholders. The Project also will introduce a long-term leasing system on peri-urban rangeland and other incentives (*e.g.*, technical assistance, wells, animal shelters and fences) that will enable leaseholders significantly to increase income from this land by improving range and livestock management. For the urban component, success will be measured by increases in the number of registered property owners, greater access to credit among project beneficiaries, and higher land values in project areas. For the peri-urban component, success will be measured by improved herd productivity, and a significant rise in leaseholder household incomes.

C. Vocational Education Project (\$25.51 million)

Mongolia's vocational education system has not evolved to serve the demands of a modern, private-sector led economy. The capacity of this system to teach core technical skills and provide critical labor information is weak, training equipment is limited and outdated, and instructors ill-prepared to teach. Essential public-private partnerships to ensure that students receive high quality, demand-driven training are largely absent, and credentialing systems are substandard. As a result, Mongolia imports skilled labor from other markets, leaving high rates of unemployment among unskilled Mongolians, especially youth. The Vocational Education Project will address these problems by building on, and significantly extending, the work of other donors, especially the Asian Development Bank and the Germany's development agency, and by supporting the newly adopted Mongolian National Vocational Education Program.

Specifically, the Project will (i) strengthen the institutional framework needed to support a demand-driven vocational education system, (ii) define industry-led skills training standards for occupations and translate these standards into a modern vocational education curricula supported by new instructional materials and equipment, (iii) develop 30 new career preparation tracks, and (iv) improve teacher training and professional development. To complete the linkage between the public training and private sector employers, the Project also will develop a career guidance and labor market information system. Success will be measured by (i) increased numbers of trainees passing rigorous skills evaluations, (ii) adoption of effective public-private partnerships demonstrated by increased private funding of vocational education institutions, (iii) significant increases in

the rate of employment in the target population, and (iv) more rapid movement from training to employment.

D. Health Project (\$17.03 million)

Mongolia has rapidly increasing rates of non-communicable diseases and injuries (NCDIs), including cardiovascular disease (CVD), diabetes, cancers and injury-induced trauma. Mongolia's mortality and morbidity rates from CVD and cancers greatly exceed those of Western countries and now represent the major cause of death and disability, particularly in younger age groups (*i.e.*, 35 to 55 years of age). Trauma response and emergency medicine are under-developed. At the same time, current NCDI programs in Mongolia are treatment based, with inadequate attention to cost-effective NCDI prevention, early detection, where relevant, and disease management. This has a negative impact on the productivity of the labor force, which is disproportionately affected by NCDIs, and is a significant drain on scarce public health investments. The Mongolian medical system is undertaking a slow and difficult transition from expensive specialist and tertiary services to a system with equal emphasis on public health, client information, and prevention efforts. To date, donor funded programs to reorient the medical system have largely focused on communicable diseases and child health. The evolving epidemiological profile calls for extension of these public health and medical practice changes to emphasize NCDI prevention and adult health maintenance. The Health Project focuses on extending the productive years and productivity of the labor force by reducing the incidence and severity of NCDIs such as cancer, CVD, diabetes and preventable accidents and trauma, and reducing and refocusing total health expenditure.

Specifically, the Project will support (i) research on NCDI related behaviors and practices in Mongolia, (ii) site visits to successful NCDI programs in other countries, (iii) communications and education interventions to promote risk behavior changes, (iv) new treatment and disease management protocols, (v) a limited amount of equipment and intensive in-service training for early detection of cervical and breast cancers, and (vi) training of physicians and general medical personnel in NCDI disease management. The Project funds NCDI outreach, screening, and disease management for a significant proportion of the Mongolian population (up to 60%, as estimated by population linked to the proposed intervention sites) over the five-year term of the Compact, with extensive monitoring, evaluation and feedback to ensure successful interventions and the transmission of best practices to all participants.

Success will be measured by the Project's impact on (i) risk behavior knowledge and practices, (ii) medical services provider attitudes and practices, (iii) early detection of targeted cancers, (iv) the number of clients screened for hypertension and diabetes and management of these conditions, and (v) reduction in the incidence of targeted accidents and trauma. Ultimately, the economic impact of the Project will occur through reductions both in (i) the productivity costs to individual Mongolians and the Mongolian economy and (ii) health system expenditures for management and treatment of NCDIs.