



CONGRESSIONAL NOTIFICATION TRANSMITTAL SHEET

We wish to inform you that the Millennium Challenge Corporation intends to obligate up to \$5,780,000 to facilitate the development and implementation of a Millennium Challenge Compact with the Government of Lesotho.

The attached notification is being sent to the Congress on October 17, 2018. Obligation of funds may be incurred on or after 15 days from the date of this notification.

In addition, we have attached supplemental information that further describes the planned use of the funds. If you or your staff would like to arrange a meeting to discuss the program, please contact Jennifer Lackey at (202) 521-3880.

Sincerely,

/s/

Karen Sessions
Vice President
Congressional and Public Affairs

Enclosure: As stated

**MILLENNIUM CHALLENGE CORPORATION
CONGRESSIONAL NOTIFICATION**

October 17, 2018

PROGRAM:	Eligible Countries
APPROPRIATIONS CATEGORY:	Fiscal Year 2019 Program Funds
OBLIGATION AMOUNT:	\$5,780,000

Pursuant to section 7015(c) of the Department of State, Foreign Operations, and Related Programs Appropriations Act, 2018, as carried forward by the Continuing Appropriations Act, 2019, and section 610(a) of the Millennium Challenge Act of 2003, as amended (the “Act”), this is to advise that the Millennium Challenge Corporation (“MCC”) intends to obligate up to \$5,780,000 under section 609(g) of the Act for the purpose of facilitating the development and implementation of a Millennium Challenge Compact with the Government of Lesotho.

The funds are expected to finance activities necessary for MCC to assess the expected impact of the proposed program, further design activities and develop implementation strategies.

SUPPLEMENTAL INFORMATION - MCC 609(G) ACTIVITIES FOR LESOTHO

Background

The Kingdom of Lesotho is a small, mountainous, landlocked country surrounded by the Republic of South Africa. The country is ethnically and culturally homogeneous, with a predominantly Basotho population. About 28 percent of Lesotho's population is urban, and the remaining 72 percent is located primarily in the rural lowlands. Because of its mountainous geography, many rural areas in Lesotho are isolated from centers of economic activity.

The main characteristics of Lesotho's economy are a persistently high unemployment rate, estimated at 28 percent, an exceedingly large and dysfunctional public sector, the highest incidence of HIV and HIV-related tuberculosis in the world, and persistent political turnover. Recent economic growth has been driven by capital- and skills-intensive sectors such as mining, finance and information and communication technology (ICT), leading to "jobless growth" for less skilled workers and highly unequal economic outcomes.

Like several other African countries, Lesotho has a high youth unemployment rate and has tried to absorb surplus labor into the government. Lesotho's is the most extreme case of this strategy, leading to a government wage bill that is among the highest in the world. This strategy has failed to significantly reduce structural unemployment, which results from a very slow rate of job creation, particularly in labor-intensive sectors of the economy. The government has, however, taken advantage of its status under the African Growth and Opportunity Act to produce textiles and apparel and continues to pursue other potential job creating sectors such as further developing its agricultural sector, expanding into different areas of manufacturing, and promoting tourism from South Africa.

By 2016 the poverty rate had increased to 59.6 percent. Extreme poverty is concentrated in rural areas, particularly in the mountain regions, where 71 percent of the population lives below the poverty line. The HIV/AIDS epidemic is also a major obstacle to poverty reduction. Lesotho's burden of disease for working-age individuals is by far the highest in the world, which has placed a huge burden on government expenditures. Weak service delivery, including health services and transport infrastructure, continues to exacerbate economic inequality and hamper the private sector's ability to grow. Lesotho can be considered a vulnerable state given the high levels of inequality and economic exclusion, high incidence of poverty, and weak government capacity to provide conditions for meaningful development.

Lesotho is a parliamentary-representative democratic constitutional monarchy, which transitioned to a multiparty system in 1992. Since 2012, the government has changed four times, mostly peacefully. Following severe political instability in 2015, MCC's Board of Directors deferred selecting Lesotho for compact development in 2015 and 2016 due to concerns over the country's commitment to the rule of law and a desire to give the government time to address reform recommendations from the Southern African Development Community. Since then, the government has taken significant steps to address concerns about Lesotho's commitment to the rule of law—including the removal of a Lesotho Defense Force commander, arrests of soldiers

accused of crimes, and the release of soldiers falsely accused of mutiny. The last political transition occurred with the democratic elections in June 2017, following a vote of no confidence against the then-prime minister. Lesotho is now led by a four-party coalition government that is fragile but currently stable.

Compact Eligibility and Constraints Analysis

In December 2017, Lesotho was again selected to continue development of its second compact, with strong messaging from MCC's Board regarding its expectations of political stability, and of proper maintenance of first compact programs. Political turmoil notwithstanding, Lesotho passed 17 out of 20 scorecard indicators for fiscal year 2018, one of the highest scores among eligible countries.

During the current compact development process, Lesotho has continued to be a strong partner for MCC and has demonstrated an early commitment to an inclusive and transparent compact development process. The government has already committed \$2.1 million to funding a well-qualified compact development team for 2018. From February to May 2018, the Government of Lesotho conducted a constraints analysis to identify the key factors inhibiting economic growth. That analysis identified two primary constraints: (i) ineffective policy planning, coordination, and execution and (ii) poor health related to HIV/AIDS. Together with MCC, the Government of Lesotho identified a strategic approach to strengthen private sector growth by increasing the effectiveness and accountability of policy planning, coordination, and execution. MCC will work with the Government to develop project proposals advancing this strategic approach and expects to address some aspects of health systems strengthening through improved government effectiveness.

MCC currently projects that the MCC Board of Directors will consider a fully-developed compact program for Lesotho in the first or second quarter of FY 2020.

Summary of Potential Compact Projects

Potential compact projects may focus on the following objective:

Strengthening private sector growth by increasing the effectiveness and accountability of policy planning, coordination, and execution. MCC will seek to combine support for reforms with assistance for capacity building and targeted infrastructure. MCC proposes activities to strengthen the capacity of government institution to deliver key infrastructure and services, integrate the perspectives of civil society and private sector organizations into policy planning and implementation, and increase the efficacy of independent oversight mechanisms. This approach will generate meaningful economic growth across Lesotho and will build sustained momentum both for reducing the role of patronage in Lesotho's governance systems and increase accountability for the delivery of public services.

Assistance to Develop the Compact Proposal

In order to assist Lesotho to further develop the proposed compact, MCC intends to fund preparatory and assessment activities in order to design a high-quality and sustainable compact. These funds will be used to initiate further study of the governance and health systems in Lesotho, initiate feasibility studies and detailed designs, and support the compact development team's administrative costs. Funding these activities reflects MCC's commitment to preparing projects in a comprehensive manner prior to compact signing, to reduce implementation risk and increase confidence in the economic justification and technical feasibility of the proposed projects.

Update on and Sustainability of the 2008 Lesotho Compact

The \$362 million Lesotho Compact began in 2008 and ended in September 2013. By compact closing, 1,041,422 people benefited from the projects. The 2008 compact focused on three sectors: water, health, and private sector development, with the aim of stimulating economic growth and building critical infrastructure needed to combat the HIV/AIDS epidemic in coordination with MCC's partner, PEPFAR. The objective of each project and their major outcomes are listed below:

- **The Water Project (\$148M)** upgraded and expanded water systems to increase water supply to domestic and industrial consumers in selected urban and rural areas. It enhanced rural livelihoods through improved watershed management. Major achievements of this project included 208 water retention structures constructed with 150 kilometers of pipes extended and 24 kilometers rehabilitated; construction of 6 pumping stations and 132 water systems; and 24,000 pit latrines built. The water project also trained close to 400 people in wetlands preservation and alternative livelihoods. The Metolong water treatment plant alone provides 25 million gallons of potable water to the people of Lesotho each day.
- **The Health Project (\$144M)** mitigated the negative economic impacts of poor maternal health, HIV/AIDS, tuberculosis and other diseases by strengthening health care infrastructure and human resources. In 2008, the health project put more people in contact with the health system through the 138 clinics that were built or rehabilitated. The accountable entity for the compact also oversaw the construction of staff housing in support of the clinics. Additional health-sector assistance strengthened the national infrastructure to support the response through construction of a reference lab, blood transfusion center, student dorms, and improved health waste management standards.
- **The Private Sector Development Project (\$23M)** increased access to credit, reduced transaction costs and enhanced participation of women in the formal economy, and provided support to essential components of the Government of Lesotho's major policy reform program to attract foreign investment and stimulate growth of Basotho-owned companies. The project established a commercial court and registered four credit providers, and issued 3,200 smart debit cards. The project also reinforced a more inclusive private sector by supporting the passage of the Land Act, which resulted in 26,000 women having registered land, supporting the Legal Capacity of Married Persons

Act by ensuring gender equity in land ownership and land transactions, and training and public awareness in gender equality.

MCC is employing some key lessons learned through the 2008 compact, including coordinating with other donors and stakeholders early, considering sustainability up front, and identifying government champions early. Since the development of the 2008 Compact, MCC has further improved its compact development process to include an analysis of the constraints and root causes to the betterment of compact design. The Government of Lesotho has fully committed to this process.