MILLENNIUM
CHALLENGE CORPORATION
UNITED STATES OF AMERICA

CONGRESSIONAL NOTIFICATION TRANSMITTAL SHEET

We wish to notify you that the Millennium Challenge Corporation intends to provide assistance to the Government of Lesotho to facilitate the development and implementation of a Millennium Challenge Compact.

If you or your staff would like to arrange a meeting to discuss this assistance, please contact Dan Petrie at (202) 521-3583 or PetrieDB@mcc.gov.

The attached notification is being sent to the Congress on February 10, 2020. The assistance may be provided and funds obligated on or after 15 days from the date of this notification.

In addition to the enclosed notification, we have attached supplemental information regarding the planned assistance.

Sincerely,

Emily Davis
Vice President
Congressional and Public Affairs

Enclosure: As stated

MILLENNIUM CHALLENGE CORPORATION
CONGRESSIONAL NOTIFICATION

February 10, 2020

PROGRAM:	Eligible Countries
APPROPRIATIONS CATEGORY:	Fiscal Year 2019 Program Funds
OBLIGATION AMOUNT:	$3,960,000

Pursuant to section 7015(c) of the Department of State, Foreign Operations, and Related Programs 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 $3,960,000 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 compact, further design activities and develop implementation strategies.

SUPPLEMENTAL INFORMATION - SECTION 609(G) ASSISTANCE 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, leading to "jobless growth" for less skilled workers and highly unequal economic outcomes.

Lesotho shares a high youth unemployment rate with several other African countries. Like its comparators, Lesotho 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 is the result of 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 Opportunities 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 Lesotho's poverty rate was 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, and it 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.

Compact Eligibility and Constraints Analysis

In December 2015 and 2016, MCC's Board of Directors deferred a vote on Lesotho's selection for a compact due to concerns about the government's commitment to the rule of law and accountability following a period of unrest in late 2014.

Thereafter, in December 2017, 2018, and 2019, in recognition of the concrete steps taken by Lesotho to address MCC's rule of law concerns and implement Southern African Development Community recommendations concerning constitutional, parliamentary, judicial, security sector, and public service reform, MCC's Board selected Lesotho as eligible to develop a second compact. In selecting Lesotho, MCC's Board directed MCC to continue to monitor government stability; progress on the reforms process; commitment to accountability and the rule of law; and proper maintenance of the assets of the first compact. At present, Lesotho continues on its reform

path, and, in Fiscal Year 2020, passed 17 out of 20 indicators on MCC's scorecard, including both hard hurdles.

During the current compact development process, Lesotho has continued to be a strong partner for MCC, and has demonstrated an early commitment to inclusiveness and transparency. Lesotho committed $2.1 million to funding a professional compact development team in 2018, and has continued to finance staff and development activities to date. From February to May 2018, Lesotho conducted a constraints analysis to identify the key factors inhibiting economic growth. That analysis identified two primary constraints: (i) poor health related to HIV/AIDS and (ii) ineffective policy planning, coordination, and execution. Together with MCC, Lesotho identified strategic approaches to address both constraints. MCC plans to conduct further due diligence and feasibility studies on two potential projects: (1) Improving Capital Investment Planning and Execution and (2) Health Systems Strengthening.

Summary of Potential Compact Projects

The proposed compact projects will focus on the following objectives:

1. *Improving capital investment planning and execution.* MCC will seek to combine support for reforms to government service provision with capacity building and targeted infrastructure assistance. Potential activities may include the following:
    - Sector-specific process reforms to create a functioning and equitable rural land registration system and improve capital investment planning and execution;
    - Catalytic assistance for irrigation infrastructure to increase the availability of serviced land in specific locations and support high-value horticulture; and
    - Developing and supporting an Impact Investment Fund and Technical Assistance Fund to support private investment in Lesotho's productive sectors and develop a pipeline of businesses unconnected to the existing patronage system.

   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 public service delivery.

2. *Improving the health landscape by strengthening the health system.* MCC will seek to fund a combination of activities to address the high disease burden of working-age persons in Lesotho. To address the effectiveness of the health system, MCC proposes strategic and integrated interventions in governance, financing, and service delivery within the health sector. Potential activities may include the following:
    - Institutional reforms to support fiscal de-concentration and data-driven accountability;
    - Institutionalize the Ministry of Health's ability to use district- and facility-led quality improvement initiatives;
    - Improve evidence-based decision-making by strengthening health information systems; and

- Institutionalize policy related to improved service delivery: Village Health Workers, mobile clinics, preventative health promotion and gender-based violence.

MCC is closely coordinating with the President's Emergency Plan for AIDS Relief (PEPFAR), the United States Agency for International Development, the Centers for Disease Control and Prevention, and other donors that are leading health and HIV/AIDS activities in Lesotho.

Assistance to Develop the Compact Proposal

The proposed assistance, in addition to funds previously notified on November 2, 2018, will be used to assist the Government of Lesotho to further develop the proposed compact. These funds will be used to initiate further study of the governance and health systems in Lesotho, initiate feasibility studies and detailed designs for assistance in public service delivery, and support the core 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 approximately $362.6 million Lesotho Compact began in 2008 and ended in September 2013. By Compact closing, 1,041,422 people benefited from the projects. The 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 U.S. government partner, PEPFAR. The objectives of the three projects and their major outcomes are listed below:

- **The Water Project ($148 million)** upgraded and expanded water systems to increase water supply to domestic and industrial consumers in selected urban and rural areas. It also aimed to enhance rural livelihoods through improved watershed management. Major achievements of this project included 208 water retention structures constructed with 180 people trained in alternative livelihoods in wetlands areas; 164 kilometers of pipes laid; construction of 5 pumping stations and 175 water systems; and over 29,000 pit latrines built; construction that was incomplete at the end of the Compact was ultimately completed post-Compact with Government of Lesotho funding.

- **The Health Project ($144 million)** aimed to mitigate the negative economic impacts of poor maternal health, HIV/AIDS, tuberculosis and other diseases by strengthening health care infrastructure and human resources. Access to health facilities increased through the 138 clinics that were built or rehabilitated under the Compact; these facilities included staff housing. Additional health assistance included the construction of a reference lab, blood transfusion center, and student dorms, and supporting improvements to health waste management standards.

- **The Private Sector Development Project ($23 million)** aimed to increase access to credit, reduce transaction costs and enhance 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 issued nearly 12,000 smart debit cards to expand access to financial services in rural and remote areas. The project also aimed to broaden participation in the private sector by supporting the passage of the Land Act, which may have contributed to the increase from 3,200 women holding land titles at the beginning of the Compact to over 26,000 women having registered land at Compact end; supporting the Legal Capacity of Married Persons Act, which was intended to increase gender equity in land ownership and land transactions; and providing training and public awareness related to gender equality.