



CONGRESSIONAL NOTIFICATION TRANSMITTAL SHEET

This Congressional Notification outlines the Millennium Challenge Corporation's intent to negotiate a Millennium Challenge Compact with the Government of Lesotho.

The transmission of this notification to Congress on December 23, 2021, affirms negotiations concerning the proposed Lesotho Compact may begin on or after 15 days from the date of this notice.

Please find enclosed, the notification with supplemental information regarding the proposed compact.

If you or your staff would like to arrange a meeting to discuss the proposed negotiations with the Government of Lesotho, please contact Brian Forni at (202) 521-2631 or ForniBJ@mcc.gov.

Sincerely,

/s/

Aysha House
Vice President
Congressional and Public Affairs

Enclosure: As stated

**MILLENNIUM CHALLENGE CORPORATION
CONGRESSIONAL NOTIFICATION**

December 23, 2021

Pursuant to (i) section 7015(c) of the Consolidated Appropriations Act, 2014; (ii) section 7015(c) of the Consolidated Appropriations Act, 2019; (iii) section 7015(c) of the Further Consolidated Appropriations Act, 2020; and (iv) and section 610(a) of the Millennium Challenge Act of 2003, as amended (“Act”), this notification is to advise you that the Millennium Challenge Corporation (“MCC”) intends to commence negotiations with the Government of Lesotho (the “Government”) for a Millennium Challenge Compact under section 605 of the Act.

The proposed \$300,000,000 compact seeks to assist the Government of Lesotho in addressing the root causes of the country’s binding constraint to economic growth across three key sectors: health, agriculture, and access to finance. The MCC-Lesotho Compact will invest in effective policy planning, coordination and execution across four key projects: the Health Systems Strengthening Project (the “HSS Project”), the Business Environment and Technical Assistance Project (the “BETA Project”), the Market Driven Irrigated Horticulture Project (the “MDIH Project”), and the American Catalyst Facility for Development (the “ACFD Project”).

Projected Economic Justification for the Compact

Lesotho’s economy suffers from a vicious cycle that limits the prospects for private sector-led growth. The private sector is too small to demand quality public goods and services from a government that fails to coordinate on policy execution and instead delivers goods and services based on political and personal patronage, further weakening the confidence and ability for private sector growth. Each of the proposed projects has been designed to combat this structural constraint by either strengthening private sector actors in sectors not captured by patronage or by improving government coordination, capacity, and execution. The projects also incorporate lessons learned from MCC’s experience in the three sectors, including how best to increase the ability of structurally disadvantaged populations, particularly poor people, women, and youth, to access and benefit from compact investment. At this time, the expected overall economic rate of return (“ERR”) of this compact with strong inclusion components is 8.9 percent. Ongoing work is designed to identify additional benefits that could not yet be captured in the current calculation. Due to the national impact of the health project, as well as the reform-oriented nature of the compact, the compact is expected to benefit the entire population of Lesotho plus future citizens, approximately 2.5 million people.

Health Systems Strengthening (HSS) Project

The **HSS Project** will seek to support the Government to implement policy and institutional reforms that are expected to strengthen the health system in ways that indirectly improve the quality and efficiency of health service delivery. This investment is expected to result in improved health outcomes (reduced mortality and morbidity) and increased cost savings. The cost-benefit analysis explicitly incorporates the benefits of gender-based violence prevention and treatment expected to result from the investment. The project is expected to support the sustainability of PEPFAR’s hard-fought achievement in reaching HIV/AIDS epidemic control. Beneficiaries of the investment are expected to include all individuals accessing public primary health care services over the course of the evaluation horizon, roughly 2.5 million people. A substantial share of benefits is expected to derive from improved maternal and child health

outcomes, and therefore disproportionately accrue to women and children. The HSS Project ERR estimate is 15 percent.

Business Environment and Technical Assistance (BETA) Project

The **BETA Project** will address the binding constraint of access to finance by creating pathways to grow and support successful local companies, targeting structurally excluded groups like women and youth. In turn, these companies are expected to demand reliable services which will make job-creation investments possible. By stimulating an increase in firm-level profits and formal employment from the BETA pipeline, including for micro, small, and medium-enterprises owned by women and youth in remote rural areas, these businesses will participate in the public-private dialogue, which results in provision of critical services. The cost benefit analysis for the BETA has two main benefit streams – the increase in returns to factors of production (land, labor, capital) that can be attributable to the BETA Project, and the increase in gross domestic product (GDP) growth that results from major reforms flowing from the public-private dialogue component of the BETA. Based on estimates of typical firm size and household size, the total number of beneficiaries of the BETA Project is approximately 6,000. The BETA Project ERR estimate is 12 percent.

Market Driven Irrigation Horticulture (MDIH) Project

The **MDIH Project** targets food insecurity and the potential to increase public goods and services to vulnerable communities that have been neglected due to patronage systems and targets structurally excluded rural smallholders, and even further disadvantaged women and youth. The comprehensive design of infrastructure, human capacity development, financing, and institutional reforms supports the establishment of new, Basotho-owned small-scale enterprises, working alongside foreign and domestic investment by medium-to-large scale enterprises, while also working with key ministries in the Government to alleviate coordination and planning problems. The estimated ERR for the MDIH Project is 4 percent, but MCC anticipates that the project may generate additional benefits that cannot yet be captured in a traditional cost benefit analysis as described below. This is in part because the project incorporates lessons learned from previous MCC projects in the sector to better assure benefits reach structurally disadvantaged groups, including women, poor people, and youth:

- The project is targeted to highly vulnerable, subsistence farmers and investing in the overall food system. It is designed to generate direct investments targeted towards horticulture and diversifying the market as well as improving subsistence farmers' diets with the benefits of fruits, vegetables, spices and herbs, and other horticultural products. The project is expected to generate additional benefits beyond the direct intervention area (measured in the ERR) by supporting policy and institutional reforms to resolve government coordination problems, enhance transparent, secure, and sustainable access to land and water, and target enhanced inclusion of women and youth. The institutional reform activities are expected to generate some non-horticulture benefits that are difficult to quantify for ERR purposes. Finally, the project will include ecosystem service benefits, such as ground water recharge, pest control and ecotourism, amongst others. Due to COVID-19 delays, MCC expects to complete data collection to estimate benefits to rural land reform in early 2022, which is also likely to affect the project ERR.

- The project will require an experienced commercial anchor farmer that is capable of quickly producing high quality products for market. Such an anchor farmer would enhance the ERR performance post-compact, while working with smaller farmers to provide additional human capacity, financing support, and general sustainability for the program to grow beyond MCC's investment period.

There are important design aspects to the project that support broadening inclusion, including improving gender outcomes, building on lessons learned from previous MCC compacts. In the direct intervention area, MCC is collecting data to calculate additional benefits from a new approach as a result of the interventions that reduce barriers to women's entry into self-employment. A partial beneficiary analysis performed early in the design of the MDIH Project ensured that the sites chosen targeted poor farmers. The preliminary analysis suggests that the impact on poor and extreme-poor household beneficiaries is around twice their representative size as compared to Lesotho's national income distribution.

The MDIH Project's disproportional impact on poor people, targeted inclusion of women and youth in rural areas, and alignment with the Government's strategic priorities in the sector make it a compelling investment despite its currently atypical ERR. This comprehensive irrigated horticulture investment will support future growth opportunities related to the horticulture value chain that will serve to diversify Lesotho's export base and support more sustainable growth opportunities with greater resilience to climate change. The estimated number of direct beneficiaries of the project is 10,000. Furthermore, additional analysis finds that for every dollar of additional production due to the MCC intervention, there is another 23 percent of indirect benefits due to multiplier effects. Therefore, depending on the employment patterns outside of irrigated horticulture, the number of indirect beneficiaries could be an additional 2,300, for a total of 12,300 beneficiaries.

American Catalyst Facility for Development (ACFD)

The **ACFD Project** will leverage U.S. Development Finance Corporation ("DFC") funding to support private investment in Lesotho. MCC funds will be used to de-risk DFC-led private sector investments, particularly in the targeted areas of health, agriculture and access to finance. The ERR assessment and cost-benefit analysis excludes the ACFD Project as DFC will lead on identification of potential investments and MCC will coordinate to help identify potential investments that align with the constraints to growth identified in Lesotho by MCC as well as the timeline of the compact. The beneficiaries of the ACFD Project will be identified as specific investments are identified.

The expected overall compact ERR is 8.9 percent, which may increase as additional work is done on the cost benefit analysis. Due to the national impact of the health project as well as the reform-oriented nature of the compact, the compact is expected to benefit the entire population of Lesotho in addition to future citizens, approximately 2.5 million people.

PROPOSED LESOTHO COMPACT SUPPLEMENTAL INFORMATION

Overview

The compact seeks to grow, strengthen, and organize the private sector in Lesotho by improving health outcomes for a healthy workforce, investing in the horticulture sector, and supporting the creation and viability of private businesses unconnected to existing patronage systems. MCC expects that providing infrastructure and capacity building in a specific sector, promoting business development, and ensuring access to healthcare will contribute to broader, longer-term efforts to support private sector growth to create a constituency that demands more effective and efficient governance.

Background and Context

The Kingdom of Lesotho is a mountainous, landlocked country approximately the size of Maryland, surrounded by South Africa. Of its two million population, approximately 60% live below the poverty line. The country is highly unequal economically, with a GINI coefficient of 44.6, in the top fifth of countries. Poverty and economic inequality in Lesotho have many drivers, including the mountainous geography (poverty is highly correlated with remoteness from urban centers), high political instability, and pervasive gender discrimination.

Lesotho's political environment is characterized by an unusual degree of turnover and instability that has grown acute in the last decade. This turmoil contributes heavily to the constraint of ineffective governance in Lesotho and generates a political and governing class essentially focused on short-term self-interest to the exclusion of developing and implementing long-term, poverty-alleviating policy. Immediately prior to and following Lesotho's reselection by MCC's Board in December of 2017, the Thabane administration presided over a period of relative political calm in Lesotho. The Government made strides towards addressing needed political reforms, including establishing the National Reforms Authority. In May 2020 Prime Minister Thabane resigned, and the ruling coalition selected former finance minister Moeketsi Majoro as the new Prime Minister. Since that time, Prime Minister Majoro has endured a series of no-confidence votes, and his administration has focused chiefly on political survival, resulting in numerous ministerial shuffles. This dynamic is representative of Basotho politics, yet still reflects a period of comparative stability in contrast to the overt political violence of the hiatus period from 2015-2017.

This instability is further reflected in the challenges the government has had in passing key reform legislation like the Harmonization Bill, a law aimed at reconciling Lesotho's dual legal systems to cement equal civil and political rights for women across the whole of the national territory. The difficulty in passing the Harmonization Bill also reflects the pervasive gender discrimination that characterizes Basotho society and hinders social and economic development. Despite progress under the first compact, including passage of the Legal Capacity of Married Persons Act, which laid the groundwork for the Harmonization Bill, many laws, institutions, and social norms remain discriminatory, limiting women's economic participation and empowerment—most pervasively in rural Lesotho.

Compact Proposal Overview and Budget

The proposed compact program is summarized in the budget table below. The anticipated budget of the compact is approximately \$322 million, which includes up to \$300 million funded by MCC and a Government of Lesotho contribution of at least \$22 million. Of the total MCC funded amount of \$300 million, the budget includes a total of up to \$30 million in the form of Compact Facilitation Funding under Section 609(g) the Millennium Challenge Act of 2003, as amended, to be made available through the compact.

Lesotho II Compact Total Program Budget			
Component	Compact Facilitation Funds	Compact Implementation Funds	Total Program Funds
Health Systems Strengthening Project	2,099,000	73,306,000	75,405,000
Activity 1: PHC Service Provision	879,000	29,459,000	30,338,000
Activity 2: DHMT Reform	931,000	21,610,000	22,541,000
Activity 3: Digital Health	289,000	22,237,000	22,526,000
Market-Driven Irrigated Horticulture Project	13,877,000	104,745,000	118,622,000
Activity 1: Insitutional Reform	3,025,000	19,175,000	22,200,000
Activity 2: Irrigated Horticulture Support Services	4,890,000	24,220,000	29,110,000
Activity 3: Irrigation Infrastructure Development	5,962,000	61,350,000	67,312,000
Business Environment and Technical Assistance Project	4,500,000	57,500,000	62,000,000
Activity 1: Pipeline Development	2,000,000	27,000,000	29,000,000
Activity 2: Strengthening the Business Ecosystem	1,500,000	18,500,000	20,000,000
Activity 3: Financial Ecosystem Strengthening	1,000,000	12,000,000	13,000,000

American Catalyst Facility for Development Project	-	3,000,000	3,000,000
Activity 1: American Catalyst Facility for Development	-	3,000,000	3,000,000
Monitoring and Evaluation	200,000	2,800,000	3,000,000
Activity 1: Monitoring and Evaluation	200,000	2,800,000	3,000,000
Program Administration	9,586,000	28,387,000	37,973,000
Activity 1: MCA-Lesotho II Administration	7,686,000	18,267,000	25,953,000
Activity 2: Fiscal Agent	900,000	4,800,000	5,700,000
Activity 3: Procurement Agent	900,000	4,800,000	5,700,000
Activity 4: Audits	100,000	520,000	620,000
Total Compact Program Investment	30,855,000	291,418,000	322,273,000
MCC Funding	30,262,000	269,738,000	300,000,000
Government of Lesotho Contribution	593,000	21,680,000	22,273,000

Proposed Projects

The objective of the **Health Systems Strengthening (HSS) Project** is to improve the delivery of health services and management of the primary health care system in Lesotho resulting in improved health outcomes and reduced per unit treatment cost. The project includes three activities:

- *Primary Health Care Service Provision Activity* – This activity will support the Ministry of Health (MOH) to improve primary healthcare services from ministry-level management to clinic-level standards of care.
- *District Health Management Team (DHMT) Reform Activity* – This activity will expand health financial systems and management capacity to the district level.
- *Digital Health Services Activity* – This activity will work with the MOH and other stakeholders to ensure that health data systems are interoperable and protect sensitive personal information.

The objectives of the **Market Driven Irrigated Horticulture (MDIH) Project** are to increase: (i) rural incomes by stimulating growth in market driven irrigated horticulture; and (ii) women and youth participation in horticulture and their incomes related to horticulture. The project also incorporates lessons learned from previous MCC projects in the sector to better assure benefits

reach structurally disadvantaged groups, including women, poor people, and youth. The project's implementation is contingent upon the identification of one or more commercial anchor farmers who will collaborate with local smallholder farmers to improve and sustain best practices in horticulture and to provide a financially viable path for all project stakeholders to remain active in horticulture production after the end of the compact. The project is composed of three activities:

- *Institutional Reform Activity* – This activity will work directly with Government partners to ensure that irrigation has strong legal and policy frameworks to support the equitable and sustainable growth of irrigation throughout the country.
- *Irrigated Horticulture Support Services Activity* – This activity will help participants overcome the obstacles to sustaining irrigation schemes by providing relevant technical assistance and attracting experienced commercial farmers in the form of an anchor farmer or joint venture partnership to help leverage smallholder efforts and sustain the infrastructure investment.
- *Irrigation Infrastructure Development Activity* – This activity includes the development of up to 2,000 hectares of irrigated land at several sites still under study. Further feasibility and design work to be conducted prior to entry into force of the compact program will refine the size and location of the irrigation perimeters and identify measures for environmental and social sustainability. Commercial farmer investments are necessary to ensure economic justification and sustainability of the investment.

The objective of the **Business Environment and Technical Assistance (BETA) Project** is to stimulate an increase in firm-level profits and formal employment from a pipeline of BETA supported firms, including for micro, small, and medium enterprises owned by women and youth and in rural areas. These businesses will participate in the Public-Private Dialogue, which results in provision of critical services to improve the business enabling environment. This project is organized into three activities:

- *Pipeline Development Activity* – This activity will identify, build, and connect existing and new high-growth potential firms to direct technical assistance and business development services to support increased firm level profits and business maturation. This activity will provide grants to select women- and youth-owned businesses to purchase equipment and goods to facilitate business plan implementation.
- *Business Ecosystem Strengthening Activity* – This activity will strengthen the Public-Private Dialogue mechanism to increase private sector participation in policy decisions and improve delivery of critical services to improve the business environment.
- *Financial Ecosystem Strengthening Activity* – This activity will increase financing options for micro, small, and medium enterprises and large firms by structuring financing vehicles that address access to credit issues for firms across the size spectrum and building the capacity of financial sector actors to develop and deliver innovative financial products.

The compact program also includes a \$3 million allocation for **American Catalyst Facility for Development (ACFD)**. The purpose of this funding is to support blended finance transactions that will catalyze private investment into Lesotho. MCC and the Development Finance Corporation (DFC) have been in discussions for over two years about potential investments including a small-medium enterprise working and growth capital fund, agriculture sector

investments and projects in the health sector. These investment areas and potentially other areas by DFC have the potential to contribute to DFC's broader southern African region investment strategy, in line with MCC's mandate.

Policy and Reform of the Compact

The proposed compact program will require passage of several reforms that are important to the success of all projects. Three of the reforms aim to address gender equality issues and rights. This includes passage of the Harmonization Bill to close legal gaps that allow rural women to be treated as legal minors; adoption of key Inheritance Reforms to allow women and daughters to inherit land and assets from their parents or spouse; and the Counter Domestic Violence Bill which addresses gaps in legal protections for women by defining domestic violence, ascribing penalties, and outlining the responsibilities of ministries and police in responding. The Counter Domestic Violence Bill is directly linked to the planned gender-based violence interventions in the HSS Project. Finally, the proposed compact program will require passage of the Labor Bill which includes worker rights and health and safety requirements. All of these legal actions are in final form and are actively supported by donor institutions. The Government has committed to establishing an Investment Climate Cabinet Sub-committee dedicated to overseeing progress on the compact related reform commitments and is currently working on an action plan to achieve these reforms by entry into force of the compact.

The HSS Project is a reform project and will offer technical assistance and use results-based financing to achieve and incentivize reforms. Digital health technical assistance will offer the data and analysis tools required for the Government of Lesotho/Ministry of Health to make evidence-based technical and resource decisions. The activity descriptions explain the system, policy, and behavioral reforms the project will incentivize to improve the management and provision of high-quality primary health care services.

The MDIH Project requires extensive reforms in gender, land, and water in order to implement and sustain the project and establish a conducive environment for the Government to replicate the project. The reforms to be implemented during the compact are described in the Institutional Reform Activity as well as the Irrigated Horticulture Support Services Activity. There are several conditions precedent for the MDIH Project that include: gender equity reforms, labor reforms, and a Letter of Intent from experienced commercial farmers in the form of anchor farmers or joint venture partnerships that express their intent to participate in the irrigation infrastructure. The proposed compact program offers extensive technical assistance in achieving the reform agenda. Using remaining Compact Development Funds, MCC's counterpart office in Lesotho is offering assistance to the Ministry of Trade and Industry to revise their Business and Licensing Regulations in order to achieve the common goals of protecting and promoting small Basotho-owned businesses while also attracting large foreign direct investment particularly in the horticulture sector.

Several reforms will be pursued to ensure the success of the BETA Project. This will include the establishment of a public-private dialogue mechanism, development of policy, regulatory, and institutional framework for horticulture standards and certification and quality conformity, and assessment of the policy, regulatory, and legal reforms that could enable greater access to finance for micro, small, and medium enterprises by strengthening financial institutions.

Update and Sustainability of the First Lesotho Compact

The \$362 million Lesotho Compact concluded in September 2013 and invested in health and water security, as well as reforms to unlock stronger private sector development. Through the compact's health and water projects, MCC and the Government trained health practitioners in infection, prevention, and disease control, renovated over a dozen health centers, and built or rehabilitated infrastructure to provide clean water and sanitation services, including water reservoirs, pumping stations, latrines, and wetlands water retention structures. The private sector project led to improvements in the volume of land transactions, the time taken to conduct land transactions, and the number of women holding land leases.

The Government has contracted routine maintenance of the health clinics rehabilitated by the compact to ensure their sustainability. The proposed compact builds off this work in creating access by improving service provision. The Lesotho Land Administration Authority (LAA), established under the private sector project, continues to operate, as does the System for Open Land Administration land information system. Monitoring data shows there is continued demand for land transactions at the LAA, including first-time land leases and secondary transactions, and continued participation by women. The proposed compact will build off this work to overcome challenges faced in registering rural lands.