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USAID Graduation

Recent Experience And Outstanding Issues

by

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THE RECORDS, DOCUMENTS, and ideas behind USAID's analyses and decisions regarding graduation of countries from its assistance programs are spread throughout the Agency, its personnel and former employees, and beyond—to individuals and organizations who have collaborated with USAID on graduations. In its effort to compile the record, the study team interviewed more than 75 persons, all of whom gave graciously of their time. We are grateful for their generosity. Without it the study could not have been completed.

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Summary

When a nation receiving USAID assistance reaches certain thresholds—measured in, for example, per capita income, infant mortality rate, and total fertility rate—the Agency theoretically will conclude its assistance there. USAID calls this graduation. But as we will see in the following pages, the concept is fraught with controversy—including arguments over its very meaning.

USAID and its predecessor agencies have always had ambiguous criteria for terminating assistance. This is in part because the situations of countries receiving U.S. assistance over the years have varied greatly. Although a favorable balance of payments may have been reason enough to graduate a country such as the Netherlands (the first to graduate from assistance under the Marshall Plan), that alone would be insufficient cause to graduate a country still suffering extreme poverty today.

This study reviews the Agency's experience with concluding concessional assistance to a country or sector when it is regarded as no longer needing the support. USAID has made several attempts to develop guidelines for the graduation decision. The various methodologies used historically have been neither compiled for comparison nor distributed throughout the Agency. This enterprise attempts to accomplish both those tasks for the first time.

The study poses two questions: *When is a USAID-supported country ready for graduation?* And, *How should the Agency structure, manage, and implement a country graduation?* The study goes on to review how USAID has answered those questions as manifested by its policy and operational decisions over the past decade.

When to Graduate

Since the early 1980s, USAID officials have debated which indicators and criteria to use when deciding to terminate traditional bilateral assistance. Discomfort with reliance on per capita income alone as a threshold, as well as the problems inherent in permanently terminating bilateral assistance, led the Agency to explore alternative policies and strategies for managing U.S. interests in advanced developing countries. In the late 1980s a working group on policy toward advanced developing countries recommended that before USAID would terminate bilateral assistance to a country that the country have attained the following: steady economic growth; diversified, export-oriented industry leading that growth; productive employment for a growing majority of its labor force; a well-trained and educated human resource base; the institutional ability to adapt, develop, and use advanced technology; and sophisticated, responsive, stable political institutions that allow peaceful change and promote public welfare.

In the early 1990s, as the Agency expanded its presence to the former Soviet Union and Eastern Europe, the debate switched from a strategy for advanced developing countries to one of "engagement and disengagement." With tighter budgets the Agency spread itself thin, jeopardizing its accountability and effectiveness. Decisions about when to terminate aid were not necessarily tied to the successful development of a country. In 1993 the USAID Administrator announced that 21 field Missions would close.

Since 1993, USAID has tended to divide countries into four categories—humanitarian, full, limited, and exit—defined by U.S. direct-hire presence and the number and nature of Mission strategic objectives. In 1996, USAID undertook a management exercise to discuss budget allocations over the following 10 years in relation to the Reinventing Government exercise. The Agency publicly committed to a broad and flexible set of criteria, rather than need- or performance-based criteria, when deciding whether to graduate countries.

Downsizing under Reinventing Government prompted a new approach to deciding to terminate or alter bilateral assistance. USAID began to emphasize progress and performance in its six sectors rather than overall country progress. In theory, as sectors achieve their goals and meet certain thresholds, they gradually close out and the Mission downsizes. When all sectors have achieved their goals, and the corresponding programs are sustainable, then a country can continue along its development path without USAID assistance.

Two bureaus—Latin America and the Caribbean, and Asia and the Near East—have the most extensive experience in terminating assistance at the sector level. The Bureau for Latin America and the Caribbean has graduated a number of sectors from country portfolios, although it has no formal sector graduation policy. The Bureau for Asia and the Near East emphasizes sectoral graduation rather than country graduation, an approach based on the belief that countries develop at different rates across various sectors.

The standard measures of development status all confirm that USAID regional bureaus do not have the same country profile of preparedness for graduation. The recent Agency practice of requiring a quota of graduates from each region produces a group of countries with such huge socioeconomic differences that those differences outweigh the similarities. An African country that graduates is generally nowhere near as developed as a Latin American graduate. This type of grouping makes it impossible to design a standard approach to graduation.

Individuals interviewed for this study stressed that the decision to terminate assistance should ideally be a participatory process involving USAID, host-country government officials, representatives from civil society, and other donors.

How to Graduate

A graduation sequence could proceed as follows: A methodology is used to identify graduation candidates, some or all of which are then selected to graduate. Guided by U.S. policy objectives, USAID determines what it wants to leave behind. Finally, the Mission develops and implements a country-specific strategy. The strategy may include several phases with changing emphases; it may include a phase between closing a Mission and concluding concessional assistance.

USAID's legacy in a graduation country may have two characteristics. First, every country will have whatever heritage (research centers, for example) the Agency projects leave behind. Second, over the final five years before a country is slated to graduate, USAID may set up institutions (such as foundations or business associations) that have not already evolved from the Agency's portfolio in that country.

USAID had funded 35 or so *endowments* through 1996, most of them designed to strengthen the viability of existing local organizations. But despite the specific intent of these endowments to sustain organizations, the Agency did not, until recently, make this a deliberate component of its strategy to graduate a country from concessional assistance.

Binational foundations manifest a binational character in the structure of their governance and their programs. Some, but not all, binational foundations subscribe to the principle of mutuality of contribution and benefit. When USAID has funded such organizations, always through an endowment, they have typically been part of a transition or graduation strategy.

A number of *binational commissions* between the United States and other countries also have emerged over the past 20 years. They may concentrate on a specific issue or on a broad range of subjects. As opposed to binational foundations, binational commissions entail formal bilateral agreements and usually require high-level official involvement from both nations. The relationship of binational commissions to a strategy of transition from USAID concessional assistance has not been as close as in the case of binational foundations.

USAID's Bureau for Europe and the New Independent States, while using approaches similar to the other bureaus', is treated separately in this study, owing to the special characteristics of its programs: a limited assistance time frame and a strategic emphasis on transition to free-market-based democracies.

Sector-Specific Strategies And Mechanisms

Sectoral graduation strategies offer the possibility to do graduations a step at a time, concluding assistance sequentially on the basis of sectoral development progress. Examples include sectoral graduation strategies for economic growth in Indonesia and for population, health, and nutrition in Indonesia and Morocco. USAID's Bureau for Asia and the Near East has evolved a graduation strategy of concentrating on sectors rather than on an entire country.

New Approaches and Tools

The study discusses two new approaches and one recently expanded tool. The first approach, setting up *strategic partnerships*, aims to maintain programs in countries where the Agency no longer has a presence, with nongovernmental organizations managing the programs under contract or assistance arrangements. The second approach involves maintaining linkages with institutions in countries where USAID is about to conclude or already has concluded bilateral assistance through *regional mechanisms*. Every USAID regional bureau—particularly Africa, and Latin America and the Caribbean—has pursued this in one form or another, though the recent and rigid "out is out" policy has sometimes made this difficult. Under the 1998 Foreign Assistance Act, the *Development Credit Authority* allows the Agency to use development assistance or Support for East European Democracy Act funds to cover the subsidy costs of direct loans or loan guarantees used for certain development purposes. This authority may well complement the other elements of a middle-income country graduate strategy.

Conclusions

1. There is confusion and concern in the Agency about the very term "graduation." One source of confusion is whether the term applies to cessation of USAID's *in-country presence* or the cessation of all U.S. bilateral *concessional economic assistance.* Agency staff will have more productive discussions of graduation if the term is given a single clear definition.

2. USAID needs clear guidelines and policy directives on when to terminate assistance. From the moment the Agency enters a country, USAID and host-country officials should think about when and under what condition assistance will end.

3. Lack of a policy has had deleterious effects on when and how the Agency graduates countries. Choosing the threshold level—whatever the indicator—for graduation eligibility is the operational question of interest in formulating a graduation strategy.

4. A set of clearly defined and consistently applied measures of development need would enable the Agency to put candidates on the table for graduation. Whether these countries would be selected for graduation would depend on the importance of the other foreign policy objectives in light of their assessed needs. USAID could make an important contribution to this essentially political decision by informing the decision-makers of the countries' abilities to sustain development without concessional U.S. assistance.

5. A country graduation strategy should clearly specify the rationale and nature of the post-assistance relationship between USAID and the host country. Transition mechanisms have different levels of Agency involvement and different demands on financial resources. The choice from among them should be guided by the type of post-assistance relationship specified in the graduation strategy.

6. Efforts to manage the graduation decision and process by keeping it in-house as long as possible could backfire. Host-country governments and other institutions and organizations have a stake. Early and frank discussions with these other stakeholders should be encouraged.

7. The work initiated in the Bureau for Latin America and the Caribbean on strategies for advanced developing countries is worth resurrecting. That bureau's paradigm identified stages in the development cooperation relationship at which per capita gross domestic product and similar indicators would signal the host country's readiness to move to a new stage. At that point, the Agency would transfer ideas, technology, and expertise to a wide range of individuals and organizations in the host country, so it could pursue and develop growth strategies without continued USAID assistance.

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Introduction

A TEAM with USAID's Center for Development Information and Evaluation undertook this study. It reviews USAID experience with concluding concessional assistance to a country or a sector when that entity is viewed as no longer needing USAID assistance or when USAID can no longer afford to provide it. The study draws lessons from this experience regarding how the Agency might better direct and manage this process.

Scope

USAID can terminate a program and depart a country (close out) for one of three reasons: the country's government is not a good development partner; its democratically elected government is overthrown by the military; or it no longer needs USAID assistance. This study is concerned solely with cases in which the country no longer needs USAID support; it is ready to graduate.

The question of when to graduate is implicitly related to the R4* process. Graduation is a special case in which the R4 system concludes that the country allocation should be zero because the country no longer needs foreign aid. (Countries may also get a zero allocation in the R4 process because they are poor development partners. This, however, is flunking out, not graduating.)

Regional bureaus have been working for several years on indicators, indices, and criteria to determine development need. USAID's Bureau for Program and Policy Coordination (of which CDIE is a component) and Management Bureau carried out a development needs assessment in 1996. The latter work was a budget-driven effort to identify, among other things, graduation candidates. A starting point for this CDIE study is a review of the work done by the regional and central bureaus. The various methodologies have neither been compiled for comparison nor distributed throughout the Agency. This enterprise attempts to accomplish both those tasks for the first time.

This study does *not* review USAID experience with countries where concessional assistance has been terminated because the

*R4, shorthand for Results Review and Resource Request, is USAID's process for reporting on its in-country programs and proposing future funding levels.

country's economic and governance policies are deemed inimical to sustained development (a poor partner) or where aid has been terminated because a country opposed a U.S. foreign policy (in the United Nations, for example). It is important to distinguish these as separate reasons for ending concessional assistance from those of need and affordability.

The second chapter of the study examines the criteria and processes USAID uses to determine *when* assistance should conclude. It then reviews the actual decisions made to terminate aid to countries and sectors in light of these criteria and processes. The chapter closes with the study team's observations on the issue of when to graduate.

Chapter 3 reviews *how* USAID has managed the transition from concessional assistance in situations where aid is concluded for reasons of country need or USAID budgetary constraints. The chapter examines several strategies or mechanisms the Agency has used and supported to facilitate a smooth transition from concessional assistance and ensure sustainability of the objectives it has helped achieve. That chapter concludes with the team's observations on how to graduate.

The final chapter draws conclusions from the observations and offers recommendations where the evidence and lessons are clear. It does not repeat all of the observations found at the conclusions of chapters 2 and 3. Readers in a hurry should look at those sections and all of chapter 4.

The annex reviews the policies and experience of other donors (the World Bank and several bilateral donors) with respect to *when* they conclude concessional assistance to a country and *how* they manage the process.

Methodology

Our team reviewed a wide range of documents: country and sector assistance strategies, project and activity descriptions, evaluative reviews and studies, databases, and oral histories from retired USAID Mission directors. We conducted group and key informant interviews with Agency staff in all bureaus and with selected representatives of nongovernmental and other donor organizations. Documents reviewed are listed in the bibliography.

A Word About Terminology and 'Graduation'

The term "graduation" provoked a mixed reaction from virtually everyone interviewed for this study, particularly when it applied to a *country*, as opposed to a *sector*. Although some see the graduation concept as a necessary part of USAID's lexicon, many others believe the term is bankrupt and should be dropped. One reason is confusion over its use, which has included application to USAID's ending its direct-hire presence in a country as well as to terminating financial aid. Another reason, voiced by many interviewees, is that the cooperating country may find the term condescending. A third reason is that graduation conveys a sense of *finality* when, as will be seen in the next chapter, assistance has in fact been resumed in a number of "graduate" countries—whether for reasons of global issues or other foreign policy concerns.

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The 'When' Question: Criteria and Decisions

USAID and its predecessor agencies have never been precise or especially systematic about establishing criteria and thresholds for concluding U.S. concessional assistance based on country need, despite several attempts throughout the Agency's history to develop guidelines for the graduation decision. This chapter reviews some of the criteria suggested and used in USAID over the years to assess a country's ability to sustain economic progress without U.S. concessional assistance. The sources of these criteria derive from legislation and elsewhere in the international development community, as well as from processes within USAID itself. The chapter presents decisions made by the Agency to terminate aid to a country or sector and compares these with selected need-based criteria. It then compares the graduation paradigm with current thinking on assistance transitions in various parts of the Agency.

Conceptual, Legislative, And Agency Context

The Need-Based Paradigm

USAID's criteria for terminating assistance have been ambiguous partly because the situations and capacities of countries receiving U.S. assistance over the years have varied greatly. For example, the first European country to graduate from assistance under the Marshall Plan, the Netherlands, did so because there was no longer any balance-of-payments justification for continued aid. Although the balance-of-payments position may be an adequate criterion for ending concessional assistance to a country with the human and institutional capacities of the Netherlands, it is not adequate for a country so lacking in these capacities that balance-of-payments "equilibrium" coexists with extreme poverty. The complexity of determining the need for foreign aid in a systematic way across countries, combined perhaps with a sense of a lack of urgency for such a policy, halted previous efforts to define a graduation policy.

Per capita income (or per capita gross national product) came to be a measure of country need for development assistance with the emergence of varying degrees of aid concessionality, ranging from 100 percent grant terms to loans at terms near or equal to those of international capital markets. A further refinement has been to adjust per capita GNP figures, denominated in U.S. dollars, for differences in purchasing power—the so-called purchasing-power parity, or PPP, adjustment. But the unadjusted figure, derived by exchange rate conversion, continues to have significance because the World Bank still uses it to determine eligibility for its various lending instruments (for further discussion of the Bank's approach, see annex).

Owing to the ambiguities inherent in interpreting per capita GNP figures, whether or not PPP-adjusted, country need can be approached from a different angle—namely, how a country's creditworthiness is rated in commercial capital markets. A relatively high rating conveys access to these markets at fairly favorable terms and a diminished need for concessional assistance. Few less developed countries are even rated by investor services such as Moody's; of those that are, fewer still make "medium grade," let alone "upper medium grade" or "high quality." However, six of the seven countries selected for graduation in 1993 were rated by Moody's, with three earning a medium grade.

Several documents of an enabling or strategic nature for USAID might be expected to provide guidance or criteria for concluding concessional assistance for a country. But they do not. They provide, at best, markers from which criteria could be derived. These documents include the Foreign Assistance Act; the current USAID Strategic Plan; and the recently issued Organization for Economic Cooperation and Development/Development Assistance Committee strategic document *Shaping the 21st Century: The Contribution of Development Cooperation*. Reacting to criticism of the graduation concept and term at public meetings on the draft USAID strategic plan, Agency management decided to delete explicit reference to *graduation* in subsequent versions of the plan. The term appears in a brief section of the "Managing for Results" chapter of USAID's 1996 *Agency Performance Report*. Although at one point this section refers to "establishing thresholds, or 'graduation points,'" it elaborates no further. Rather, most of the discussion is on "ensuring that the institutions, programs, and objectives the Agency supports will be sustainable once assistance is phased out" and "designing exit strategies to ease the transition from USAID-assisted interventions to locally self-sufficient systems and results" (USAID 1997a, 6–8). The language emphasizes the *how* question rather than the *when* question.

Extension to Sectors

Efforts to broaden the measure of development status beyond per capita income have generally involved the inclusion of widely accepted indicators of health or social status. USAID's 1997 Strategic Plan sets forth performance goals that express the Agency's broad development goals in its six program areas over the next 10 years. The plan outlines both specific targets and overall trends (USAID 1997d). The performance goals are adapted from the Development Assistance Committee's resolution to achieve certain levels of development in the next century, as documented in *Shaping the 21st Century* (Development Assistance Committee 1996b, 2). Several of the indicators of success at the country level used informally by USAID may also be viewed as need-based indicators for termination of programs in specific sectors.

For example, the population, health, and nutrition sector has developed targets and corresponding indicators to measure them. The strategic plan outlines five goals and indicators: three related to population growth and two to health and nutrition. Those involved in developing the population, health, and nutrition targets debate to what extent the most standard indicators of progress reflect long-term, sustainable change. In other words, at what point do these indicators reflect the point at which progress is sustainable without USAID assistance? A discussion of two of these indicators highlights the advantages and disadvantages of each in terms of its applicability to graduation thresholds.

First, the USAID strategic plan states that one performance goal is reducing the fertility rate by 20 percent in 10 years. The indicator that measures progress toward this goal is *total fertility rate*, or the number of children that would be born to a woman were she to live to the end of her childbearing years and bear children in accordance with prevailing age-specific fertility rates. Total fertility rate is determined by contraceptive prevalence, the extent and level of education of women and girls, and, to a lesser extent, variables such as degree of urbanization, family income, and factors that affect the age of marriage. The Agency chose this measure of success because it is widely measured, well defined, and straightforward. Currently, USAID countries have an average total fertility rate of 4.0. A rate between 2.0 and 3.0 is generally considered an appropriate long-term goal.

Another indicator that many population, health, and nutrition officials advocate using to measure this goal is the *contraceptive prevalence rate*, or the percentage of women who are practicing, or whose sexual partners are practicing, any form of contraception, usually measured for women from ages 15 through 49. Most population, health, and nutrition officers believe that if this rate rises above 65 percent, then under certain conditions (such as local government and private sector involvement) progress made by USAID population activities can sustain itself. Contraceptive prevalence rate is a more intermediate measure of progress toward controlling population growth that is often easier to obtain than total-fertility-rate data. However, Agency economists and other social scientists hesitate to use this measure because it is only one component of total fertility rate and perhaps less indicative of sustained progress. Many family planning experts counter that all these variables tend to be associated with contraceptive prevalence, thus contraceptive prevalence rate remains a useful indicator. Clearly, one of the problems in sorting out the real causes of a total-fertility-rate decline is the high degree of association between the likely causal factors.*

Second, USAID's strategic plan states that in the next 10 years the Agency will try to reduce mortality rates by 25 percent in the categories of infants and of children under 5. To measure progress toward this goal, the Agency chose under-5 mortality rate (U5MR), or the probability that a newborn baby will die before reaching age 5, if subject to current age-specific mortality rates. U5MR is well defined, with reported data for almost every country in the world. U5MR in countries with a USAID presence is about 99 per 1,000 live births. Generally, it is believed that when the U5MR reaches about 50, progress in the sector is sustainable.

*For more information on both indicators see USAID 1997d, 36–37, and World Bank 1997, 41.

Another common indicator used to measure similar gains is the *infant mortality rate*, defined as the number of infants that die before reaching 1 year of age (per 1,000 live births). Infant mortality data were used heavily in the past and are more widely recognized than U5MR. However, infant mortality rate may not capture the full effects of programs that address the causes of morbidity and mortality of children (such as diarrheal diseases, respiratory infections, and malnutrition) that generally appear in the first few years of life. Thus U5MR is considered a better measure of long-term and sustainable development (USAID 1997d; World Bank 1997).

In both instances, USAID chose the indicators that capture the long-term, more nuanced, representation of progress toward performance goals in population, health, and nutrition. A remaining issue: to what extent does consensus exist regarding the threshold for each indicator? Additionally, the Agency should carefully think through the relationship among these performance goals, the corresponding indicators, and sectoral graduation.

In addition to indicators that measure broad-based progress toward USAID's performance goals, sector specialists are developing results measurement tools at the program level as part of the R4 process. Although standard indicators are important to measure program effects and progress toward broad goals, few demonstrate at what point assistance can conclude. Several offices in the Agency support methodological research in host-country institutional capacity and commitment to continue programs after USAID exits a country.

The Global Bureau's population, health, and nutrition office has begun to develop such indicators in the form of three activities. First, the Communication, Management, and Training Division is funding the Family Planning Management Development project to analyze the institutional sustainability of program achievements at the organizational level, owing in part to concerns that arose during graduation processes. One component of the project assesses local-level organizational sustainability. To achieve this goal, an NGO called Management Sciences for Health has developed a toolkit, which it has posted on the Internet.* A second activity, an evaluation project funded by the Policy and Evaluation Division, analyzes two sustainability indicators—program and outcome. Program measures the national level effort to ensure contraceptive access, while outcome measures the sustainability of changed fertility rates by analyzing longer term fertility trends. The two activities reflect population, health, and nutrition efforts to link sectoral progress with a measure of sustainability. Third, in 1995 the Global Bureau's Office of Population began funding development of a financial sustainability assessment tool through the Population Technical Assistance project. The tool attempts to assess the financial sustainability of national family planning programs. The tool remains in draft form.

The population, health, and nutrition sector's success in developing measures of sustainable progress is due in part to the fact that in some ways it is conceptually relatively straightforward to quantify and interpret PHN indicators, and in part due to this sector's long history of data collection efforts (much of

*Its address is http://erc.msh.org/toolkit/orgsus.htm.

which is USAID supported). These factors, combined with overall program success, have resulted in many graduations in the PHN sector. This experience has led the Center for Population, Health, and Nutrition to begin examining the question of institutional sustainability through exercises such as the Family Planning Management Development project and the evaluation project. PHN's progress is a model of how to decide when to conclude assistance at the sector level. This is a promising area for future work.

Europe and the New Independent States Transition Paradigm

When eastern European nations jettisoned their former systems of governance and economic organization in the late 1980s and early 1990s, most countries of central and eastern Europe ranked higher on a range of social and economic indicators than most developing countries. This was also true of several new independent states that had been part of the former Soviet Union. However, the contrast was less marked, and some of the new countries (e.g., some in Central Asia) manifested indicators in the same range as low-income countries elsewhere in the world. Those considerations underpin the paradigm for USAID assistance to countries in the Bureau for Europe and the New Independent States. Namely, aid should be relatively short-term in nature and emphasize helping countries undertake social, political, and economic transformation toward free-market-based democracies.

There are special legislative frameworks for the ENI countries: the Support for East European Democracy Act (commonly known as the SEED Act) for central and eastern European countries and the Freedom Support Act for the new independent states. Although the legislation itself does not specify a time frame for concessional assistance, a period of 10 to 15 years seems to have emerged out of the legislative history and discussions involving the White House (including the Office of Management and Budget), the State Department, and USAID.*

The ENI Bureau, in consultation with State and OMB, has developed a systematic method to assess the progress of each country in its transition to a free-market-based democracy, to decide when to terminate assistance. The approach consists of regular meetings with representatives from the State Department's Country Coordinator Office, the ENI Bureau (specifically the Office of Program Coordination and Strategy), OMB, and the Mission. The graduation date is set when participants agree that the programs and institutions reach a sufficient momentum and level of results to complete their transition without USAID. After the date is set, the Mission writes a closeout R4 and a strategic plan, as directed by the bureau's operating procedures.

To inform these decisions, the bureau has developed a process to determine at what point programs are sustainable. Two formal factors (country performance and program performance) and two informal factors (strategic importance and political influence) are

*The legislation is couched in general terms. The SEED Act requires the provision of "assistance to eastern European countries which have taken substantive steps toward institutionalizing political democracy and pluralism."

analyzed to determine the amount and length of assistance (Conly 1997, 2). Although the latter factors cannot be systematically measured, the bureau tracks program performance through the R4 process. It monitors country performance through the monitoring country progress report.

First, the monitoring country progress report analyzes country performance in two steps. Data primarily from the European Bank for Reconstruction and Development, Freedom House, and the World Bank are reviewed to track progress toward democratic and economic reforms and to set proposed benchmarks for graduation. While the ENI Bureau documents do not specify thresholds for terminating aid, countries that rank near the top of economic policy reform and democratic freedoms are considered "obvious candidates for earlier graduation" (USAID/ENI 1997, 52). Second, ENI assesses indicators of macroeconomic sustainability, such as growth in real gross domestic product (GDP), labor productivity, integration into the world economy, and social sustainability such as poverty, human development, and unemployment rates. This is one of the Agency's few documented attempts to monitor the sustainability of country reforms.*

One problem the bureau experienced in 1997 was that monitoring program results through the R4 process was less operationalized than monitoring overall country performance. ENI Missions incorporate several of the 11 broad strategic objectives outlined for the region into their country portfolios. However, few indicators were developed to gauge progress at the individual activity level, with the exception of democracy and governance strategic objectives (civil society, rule of law, and local governance). One example of democracy and governance's progress toward measuring program impact is the nongovernmental organization sustainability index, which gauges the strength of the NGO sector in Europe by analyzing five aspects: the legal environment, organizational capacity, financial viability, advocacy experience, and public image (USAID 1997c). The bureau addressed this problem during the 1998 R4 cycle by encouraging the teams that develop strategic objective indicators to develop criteria for graduation.

ENI encourages Missions to include in their strategic plans the graduation thresholds that, if attained, indicate the objective has been achieved. Additionally, program objective teams have been tasked with developing criteria and thresholds to gauge successful completion of the strategic objective. Information from three sources—country progress monitoring reports, team progress reports, and Mission R4 reports—are used to inform decisions about graduation.

Although the ENI experience is the most successful attempt within the Agency to formulate a graduation policy, the process appears neither problem free nor necessarily applicable to other bureaus. ENI has a well-developed process and appropriate indicators, but the countries for the most part have higher per capita income and more developed infrastructure and social indicators than the average USAID sustainable development country. However, there may be much to learn from the process that applies to other regions with

*For a detailed description of methodology and actual data see USAID/ENI 1997, 3–50.

countries further along the development continuum.

USAID Decisions

Policy Framework

Since the early 1980s, USAID officials have debated which indicators and criteria to use when making decisions to terminate traditional bilateral assistance. Discomfort with reliance on per capita income alone as a threshold, as well as the problems inherent in permanently terminating bilateral assistance, led the Agency to explore alternative policies and strategies for managing U.S. interests in advanced developing countries. The issue was first analyzed in the Bureau for Latin America and the Caribbean, which had developed a policy for advanced developing countries before the rest of the Agency began to look at the issue systematically. Eventually, the issue was addressed Agencywide as proponents of a policy for advanced developing countries (ADCs) argued for a more nuanced approach to phaseout and postphaseout cooperation. In 1987 and 1988, a working group on policy toward advanced developing countries met to discuss the issues involved in terminating bilateral assistance and developing ties with these countries. Among their recommendations was a suggestion by the Bureau for Program and Policy Coordination's Office of Policy Development and Program Review to agree on target thresholds that could indicate successful and sustained development. Specifically, the working group recommended that before USAID would terminate bilateral assistance to a country that the country have

Steady economic growth

Diversified, export-oriented industry leading that growth

Productive employment for a growing majority of its labor force

A well-trained and educated human resource base

The institutional ability to adapt, develop, and use advanced technology

Sophisticated, responsive, stable political institutions that allow peaceful change and promote public welfare (Callison 1987)

The group's suggestions were never adopted, but an internal discussion about graduation thresholds continued. In 1988, the Bureau for Program and Policy Coordination circulated a paper on USAID policy toward ADC countries. The piece suggests that to be designated for ADC Programs, countries must have four things: a viable education system, effective institutions, an appropriate and functioning policy framework, and a strong, sustained record of broad-based economic growth (Callison 1988, 12). Although a set of criteria corresponding with these four was developed and recommended, none was ever adopted officially.

In 1991, the Bureau for Program and Policy Coordination acknowledged that the lack of official Agencywide policy toward ADCs had led bureaus to develop conflicting programs and strategies. To rectify this situation, PPC circulated “Draft AID Guidelines for Middle-Income Country Programs and Strategies.” The guidelines reflect the movement toward recognizing per capita PPP estimates as a better indicator of sustained economic growth than nominal per capita income converted to dollars at official exchange rates. The guidelines state that “any recipient with a PPP per capita exceeding 10 percent of the U.S. PPP per capita will be expected to contain one or more [middle-income country] programs as part of its portfolio, unless there are compelling arguments that this indicator fails to reflect the level of development” (Sines 1991, 2–3). The Bureau for Program and Policy Coordination’s official position on terminating or changing bilateral assistance to advanced developing countries was to recommend making these decisions on the basis of simple, discernible criteria (PPP) instead of the more complex formula recommended by the earlier ADC working group.

In 1992 the debate switched from an ADC strategy to one of “engagement and disengagement.” According to interviews and documents reviewed, the Agency’s involvement in many more countries (owing to USAID’s presence in the former Soviet Union and a movement to democratize in Africa) coupled with tighter budget constraints caused the Agency to be spread too thin. That jeopardized its accountability and effectiveness. Decisions about when to terminate aid were not necessarily tied to the successful development of a country. As an Agency official noted,

> To date, decisions about initiating, expanding, decreasing, or terminating AID development programs are often made on an individual basis by regional bureaus, without reference to a common set of questions or criteria. In addition, where decisions are made to initiate or terminate assistance programs, these are generally taken on political, rather than development grounds. [Morfit 1992, 1]

A movement to formulate a flexible yet explicit disengagement policy was proposed by the Bureau for Program and Policy Coordination strategic planning office. The approach argued for resource allocation decisions based on need and performance. The countries were separated into five levels of development: basic, accelerated, steady, preparing for graduation, and postgraduation. The minimum eligibility threshold recommended by the strategic planning office took into account “satisfaction of U.S. legal requirements for aid; meeting a ‘floor’ definition of need (per capita income, social indicators); and demonstrating a basic willingness to undertake political and economic reform.” Thus, a more nuanced understanding of host-country commitment to sustain programs emerged officially as part of the debate regarding when to terminate development aid.

Although discussions about when to terminate assistance were revisited for a span of 15 years, no Agencywide policy emerged. The failure to adopt a formal policy was the result of three factors. First, every attempt to set thresholds or standards for a country to receive or stop receiving aid was criticized for not addressing the political context of development assistance. Critics argued that political factors such as foreign policy priorities are not explicitly recognized in policies that stress thresholds and indicators of development. Second, officials in regional bureaus argued that the different development contexts in each region demand a flexible approach to making these decisions. Third, most graduation decisions grew out of budget cuts rather than some assessment of development level or need; therefore, thresholds were seen as useless. Indicators generated some theoretical interest, but political and budgetary concerns usually rendered discussions about indicators and thresholds academic.

Mission Closeouts

In 1993, in an effort to reform and restructure the Agency, the USAID Administrator announced the closing of 21 Missions. The closeouts fell into three categories: graduates, small country programs, and countries that were inconsistent or unreliable development partners (USAID 1993). Seven of the 21 countries were officially designated as graduates: Argentina, Botswana, Chile, Costa Rica, Thailand, Tunisia, and Uruguay. Though some of the research from the earlier exercise in engagement–disengagement was used to decide that those seven countries could sustain development achievements, official thresholds were not part of the public justification.

One particularly contentious feature and legacy of these closeouts was USAID's so-called out-is-out policy, which directed the Agency not to undertake any new activities in these 21 countries. This policy was a hurdle to offices struggling to formulate graduation strategies. It made regional bureaus more reluctant to exit a country, as this meant severing ties with the country definitively. The policy has also had a chilling effect on using Agency resources to tap expertise in exit countries for the benefit of countries with ongoing programs.*

Recent Changes In Policy Framework

In early 1996, a USAID official summed up the decision-making policy with regard to graduation:

> [A] combination of objective country data (higher levels of per capita income, more widespread education, growth-supporting policies, and similar indicators) and professional judgment are used to develop a set of contingencies for dealing with different budget scenarios. [Sillers 1996]

In other words, a specific formula for graduating a country from development assistance did not exist, nor had officials explicitly addressed the issue since the engagement–disengagement exercise. However, two recent trends have led USAID to once again reexamine its policy toward graduating countries.

First, USAID's involvement in eastern Europe and the former Soviet Union placed the Agency in countries "with levels of real income and human development well above the threshold at which USAID would normally view graduation as appropriate" (Sillers 1996). Because the programs are explicitly transitional, the Bureau for Europe and the New Independent States developed procedures to guide country graduation as well as the date-setting process discussed earlier in this chapter.

To date, ENI has graduated three countries—the Czech Republic, Estonia, and Slovenia—owing mostly to their rapid and suc-

*The out-is-out policy is being reviewed by a group of officials from the Bureau for Program and Policy Coordination who have been tasked with drafting the Agency's formal policy on programs in nonpresence countries.

cessful political and economic transformations. Five more (Poland, Hungary, Latvia, Lithuania, and the Slovak Republic) are scheduled to graduate in the next four years. The most recent monitoring country progress report observes that three clusters of countries emerge from the data, differentiated by progress toward economic and democratic reforms. The first cluster comprises obvious graduation candidates (countries with the highest ranking of economic policy reform and democratic freedom) such as countries in the northern tier of central and eastern Europe (USAID/ENI 1997, vi–viii). While country monitoring is typically used for annual budgeting decisions, this clustering suggests that monitoring has also served to identify countries that can sustain their progress toward reform and are hence graduation candidates.

The date-setting process seems to be working as well; participants are communicating, and the process has some degree of flexibility. For instance, because the Czech graduation proved problematic, USAID monitored the progress of upcoming graduates more closely. After officials confirmed that Latvia, Lithuania, and Slovakia were experiencing political and economic slippage, State Department and USAID officials reconsidered graduation, and the dates were pushed back a year to allow for greater success.

A second trend affecting decisions on when to terminate assistance is the rise of global issues—problems that affect all countries, demand coordinated action, and affect U.S. interests. Examples include global environmental concerns, population growth, and transitions to democracy in developing countries. Global concerns often affect countries that no longer need USAID concessional assistance but are still in a path of development. To address such worldwide problems, these countries must be reengaged. For this reason, global activities in such countries will be at odds with the out-is-out policy and the Agency's traditional graduation paradigm.

For example, officials in the Bureau for Latin America and the Caribbean recognize that were it not for global environmental issues, USAID should have stopped concessional assistance to Brazil, a country with relatively high social and economic indicators of development. However, in 1990 the United States launched its Global Climate Change Program to address important climate change issues in strategically important countries such as Brazil. In 1996 the program expanded to open up new possibilities for environmental management programs, such as renewable energy and biodiversity conservation. Global concerns seem to have been one of the influencing factors in the decision to continue to fund activities in Brazil.

These developments, combined with lessons learned from previous debates about USAID policy toward more advanced countries, have led the Agency to try to address more systematically the question of determining at what point a country no longer needs concessional assistance. An opportunity to learn from these changes and experiences arose in 1996 when USAID reexamined its presence in developing countries as part of its Reinventing Government process.

Reinventing Government II Experience

Since 1993, USAID has tended to divide countries into four categories—humanitarian, full, limited, and exit—defined by U.S. direct-hire presence and the number and nature of Mission strategic objectives. In 1996 the Agency undertook a management exercise to discuss budget allocations over the next 10 years in relation to the Reinventing Government exercise. Most of the decisions regarding which category a country falls into were made during the two phases of the restructuring exercises, Reinventing Government I and Reinventing Government II. According to a letter from the Administrator to the Office of Management and Budget, "the restructuring decisions made in the spring of 1996 . . . were largely budget driven and not based on poor results or the relatively advanced development status of the recipient countries" (Bradford and Byrne 1996, 3). However, tough decisions had to be made about reallocating scarce resources. According to the same letter, USAID considered four criteria when making the decision to reduce the size of, close, or graduate a Mission: 1) need and level of development, 2) global programs, 3) U.S. foreign policy, and 4) quality of partnership, commitment, and performance. Thus the Agency publicly committed to a broad and flexible set of criteria, rather than need- or performance-based criteria, when deciding whether to graduate countries.

The process and outcome of the exercises were either confidential or rarely documented; therefore, it is difficult to discern which countries were placed on a graduation track as a result of this exercise. The Administrator's letter states that eight countries (not including ENI) were to be put on the graduation track starting in 1999, but the countries were not disclosed publicly. The official "list" of closeout countries (available to the public through USAID's legislative and public affairs office) does not include any new, non-ENI graduate in 1997–99. Because these decisions are subject to change, the Agency refuses to publicly commit to graduating countries after fiscal year 1999. On the one hand, this tendency to keep these decisions confidential and close to the top of the Agency may ensure flexibility in times of crisis or if a country's development indicators change drastically. On the other hand, this tendency indicates a lack of transparency regarding decisions that affect the Agency and the countries where it works.

After the exercise was completed, some familiar questions remained unanswered. In one public Reinventing Government II memorandum, Agency economists from the regional bureaus wrote, "Can USAID set graduation [progress] criteria to make program termination more routine in an era of declining resources?" The Bureau for Program and Policy Coordination and Management Bureau never formally responded, and some regional bureaus realized the need to think more systematically about issues related to deciding when to terminate concessional assistance. The next two subsections explore the different bureaus' country and sector graduation policies that evolved during and after the Reinventing Government II exercise.

Country and Bureau Decisions

No regional bureau has explicitly developed thresholds that determine country resource allocations. Regional bureaus have recently debated or discussed the issue of when to graduate a country from bilateral assistance as part of a budget-induced downsizing exercise. To determine when a country can sustain development without bilateral assistance, the Bureau for Latin America and the Caribbean informally uses four filters: per capita income, global interest, sector-specific issues resulting from earmarks, and foreign-policy or political issues. Africa Bureau has developed a system for ranking countries by both need and economic performance.

After Reinventing Government II, the Bureau for Latin America and the Caribbean conducted an internal exercise to give analytical rigor to the decision-making process when allocating scarce resources within the bureau. The exercise reviewed countries' ability to pursue effective growth strategies or to develop such strategies without continued USAID assistance. Four of what were then the Agency's five strategic objectives and their suggested indicators were joined with data from the Pan-American Health Organization, Unesco, UNICEF, the World Bank, and the World Health Organization to develop indicators to signal where performance results and sustainable development needs justified extending aid. The bureau recognized that while widespread problems may exist, graduation is appropriate in countries that have the institutional and policy framework to ensure future progress. However, the LAC internal exercise was never adopted as policy, and LAC Bureau's formal strategy is to "reduce the number of strategic objectives and to consolidate and prioritize their remaining projects and activities" (Fischer 1996, 10).

The bureau's experience with country graduation decisions represents an approach typically taken by a bureau in a region characterized by sustainable, long-term development assistance strategies. Faced with budget cuts, the bureau considered a number of informal factors in deciding where to make those cuts. In no instance did the bureau examine progress and decide that program impact determined that USAID assistance was no longer necessary.

Sector Decisions

Another approach to making decisions to terminate or alter bilateral assistance is to emphasize progress and performance in what are now USAID's six sectors instead of overall country progress. In theory, as sectors achieve their goals and meet certain thresholds, they gradually close out and the Mission downsizes. When all sectors have achieved their goals, and the corresponding programs are sustainable, then a country could continue along its development path without USAID assistance. The development of sector level strategies at the bureau level was prompted by Reinventing Government II downsizing and meeting targets set by the R4 process.

Two bureaus—Latin America and the Caribbean, and Asia and the Near East—have the most extensive experience in terminating assistance at the sector level. The Bureau for Latin America and the Caribbean has graduated a number of sectors from country portfolios, although it has no formal sector graduation policy. In the LAC case, some country programs are kept open to absorb earmark funds. In this sense the bureau may have inadvertently concentrated on sector-level assistance that terminated after a few years. However, no formal sector-specific graduation strategy or experience has been documented. Specific sector closeouts in the bureau include the population sector in Colombia and Chile (before the entire Missions closed), democracy and governance–related activities in Panama and Jamaica, and a bilateral trade activity in Guatemala. The bureau plans to graduate Mexico's and Brazil's population activities and the Dominican Republic's and Ecuador's child survival activities in the year 2000. However, every sector graduation took place in unique contexts for a variety of reasons, and no clear strategy for exit emerges.

The Bureau for Asia and the Near East has emphasized sectoral rather than country graduation. The ANE approach rests on the belief that countries develop at different rates across various sectors. When faced with budget cuts, officials used the data generated during R4-cycle strategic objective reviews to inform their decisions regarding which Mission to close or downsize. During Reinventing Government II, the decision was made to graduate three sectors in two countries: Indonesia's economic growth strategic objective; Indonesia's population, health, and nutrition strategic objective; and Morocco's PHN strategic objective. Although actual decisions were based on budget concerns rather than consistently applied thresholds, the bureau is beginning to envision a sectoral graduation strategy that combines the country progress and performance data, and standard indicators such as per capita income, with some measure of country commitment and the institutional capacity to sustain the progress.

In sum, *graduation decisions appear to be made in reaction to budget cuts.* They do not seem based on development thresholds or consistent criteria. Evidence suggests that regional bureaus have been more systematic when graduating sectors. This may stem from the R4 process, which formalizes discussions about sector progress.

Comparing Decisions And Criteria

The Agency's efforts to identify indicators or measures suitable for identifying countries for graduation was discussed earlier. This section uses a popular set of these indicators to characterize countries and examine the characteristics of those that have been chosen for graduation.

The Bureau for Program and Policy Coordination has developed an index of country needs for development assistance. The index has no formal standing in the Agency, but it has been used to rank countries during several decision-making exercises. The index uses three indicators: PPP-adjusted income per capita, infant mortality, and total fertility. Each indicator is scaled by establishing maximum and minimum scores. The maximum score (the most severe need) is set equal to the value of the worst-off country. The minimum score is set equal to the average indicator values of five comparator countries that are viewed as graduates or near-graduates from concessional development aid on the basis of need.

The countries are Chile, Colombia, Costa Rica, Malaysia, and Thailand. Chile, Costa Rica, and Thailand have in fact graduated from bilateral concessional development assistance. Malaysia was never a significant U.S. bilateral aid recipient and now receives little concessional assistance from any source. The scale is then normalized on the 0–10 range, with 10 indicating the greatest need. Using the weights of 50 percent for income and 25 percent each for infant mortality and total fertility, an overall need score is calculated. The overall need score is also set on a scale of 0–10.

FIGURE 1 CAN BE FOUND AT THE END OF THIS DOCUMENT.

The Bureau for Program and Policy Coordination need index was not developed explicitly to study the graduation issue. Nonetheless, it carries the implication that at some level the need score suggests a decline in the requirement for development assistance. The PPC-prepared scores, using 1995 data, are shown at left. Figure 1 does not suggest any obvious threshold value as an indication of readiness for graduation. The incremental increases in the need scores are small throughout the entire range. (European and NIS countries are generally excluded from the analysis in this section, as their criteria for graduation differ from those relevant to the other geographical bureaus.)

As an index, the need score is concise and easy to interpret. But it may obscure important differences in the underlying indicators. Another way to present the indicator values is with development triangles, a visual aid used frequently in World Bank publications. To convey a quick representation of the development situation in countries of interest to us, a comparison triangle was constructed using the three development indicators from the Bureau for Program and Policy Coordination analysis just described. The five comparator countries used to construct the need index are the basis of the comparator triangle, figure 2.

Grouping countries by geographical region suggests that graduation is a more pertinent concept in some regions than in others. Figure 3 (following page) shows the frequency distribution of need scores by region and the average development triangle for each need score. The shaded area of each triangle is the average for the countries with that score. The triangle frame is the graduate comparator country triangle. The closer the shaded area to the triangle frame, the closer the country comes to matching the three need-indicator values of the five graduate comparator countries.

The issue of graduation from USAID assistance on the basis of being less needy has greater urgency for the Bureau for Latin America and the Caribbean, considerably less urgency for the Africa Bureau, with the Bureau for Asia and the Near East in between. Figure 4 (see page 19) presents the compa-

FIGURE 2 CAN BE FOUND AT THE END OF THIS DOCUMENT.

rable data for the Bureau for Europe and the New Independent States.

Earlier sections of this report described the Agency's past decisions on graduation. The left side of figure 5 (see page 20) presents the development triangles for the countries selected for graduation in the 1993 and 1996 decisions. Whereas the countries selected in 1993 are quite similar to the com-

FIGURE 3 CAN BE FOUND AT THE END OF THIS DOCUMENT.

FIGURE 4 CAN BE FOUND AT THE END OF THIS DOCUMENT.

parator country triangle, the countries selected in 1996 show much wider variation among themselves and none of them comes close (South Africa being the closest) to matching the graduate comparator country triangle. At the low end, Zimbabwe's triangle is less than 20 percent of the area of the comparator triangle. In the period 1993–96 the profile of countries deemed ready to graduate changed dramatically. For comparison, the right side of figure 5 shows the 14 countries in figure 1 with the lowest need scores.

Figure 5 and the preceding discussion suggest that budget issues may inordinately influence the Agency's concept of graduation.

Budget reductions such as USAID experienced in the 1990s must be dealt with by reducing or eliminating country programs, leading to termination or exit within a relatively brief period. Graduation, as discussed within the Agency, is a slower deliberative process.

FIGURE 5 CAN BE FOUND AT THE END OF THIS DOCUMENT.

USAID staff have based their analytical work on graduation on the notion of objectively verifiable indicators of readiness. The Agency's approach to graduation will be clearer and more rigorous if it is developed independent of current budgets and not as an adjustable yardstick responding to changes in funding levels.

Conclusions

Some conclusions regarding when to terminate concessional assistance emerge from discussions with USAID officials and review of Agency documents.

Currently, decisions about when to terminate aid appear driven by political and budgetary concerns, not standard development thresholds. Official USAID rationale for assistance uses broad, flexible criteria based on need, global importance, quality of commitment and partnership, and foreign policy. Although a broad policy is understandable given the circumstances under which USAID operates, most interviewees offered that a more objective set of criteria underpinning a rational graduation policy would benefit the Agency's credibility, make it more accountable, and make decisions more transparent. Although Agency staff have attempted to develop overall indicators of country progress, most work has been at the individual sector or subsector program level. Interviewees expressed the need to also analyze both host-country institutional and organizational commitment and capacity to sustain USAID-initiated programs after graduation.

As a development agency, USAID can distinguish between its developmental (need) objective and the other objectives for delivering assistance. A set of clearly defined and consistently applied measures of development need would enable the Agency to put candidates on the table for graduation. Whether these countries would then be selected would depend on the importance of the other foreign assistance objectives in light of their assessed need. USAID could make an important contribution to this essentially political decision by informing the decision-makers of the countries' abilities to sustain development without concessional U.S. assistance.

Previous efforts to produce a graduation policy have failed. USAID has an institutional reluctance to end aid unless driven to it by budget difficulties. The Agency needs clear guidelines and policy directives regarding when to terminate assistance. From the moment USAID enters a country, Agency and host-country officials should think about when and under what conditions assistance will end. The ENI experience illustrates one step toward a clear, documented graduation process at the bureau level. In the past, Missions received unclear messages and guidance from Washington before, during, and after the date-setting process. That led to strained working relationships with host-country counterparts.

The development indicators presented in this Special Study (per capita GDP, infant mortality, and total fertility rate) are examples of socioeconomic development that could inform a discussion of a country's preparedness for graduation. Whether this or another set of indicators is used, it is worth noting that these indicator values increase only slowly over time. (In a crisis, they can decline rapidly.) Because of the rate of increase in the indicators, graduation candidates do not pop up unexpectedly. They are easily identifiable. Once a short list of candidates is drawn up, an interagency group could determine whether there are country-specific reasons to continue assistance. Absent a justification for continued aid, the candidate could then be selected for graduation with enough lead time to permit the orderly design and execution of a graduation strategy or plan. Monitoring implementation of the graduation plan would fall naturally within the R4 process. The R4 review could also take the lead in identifying candidates for sectoral graduation if the Agency chooses to formalize the sectoral graduation concept.

Some of the work done by USAID staff has led to the notion of "institutional capacity" as one type of graduation criterion. Though this concept has intuitive appeal, no one yet has come up with a good measure of it. Until the measurement problem is solved, institutional capacity cannot be compared across countries or assessed over time in a single country. It would be premature to include institutional capacity as a (or the) graduation criterion until the term has a firmer analytic content. Proponents of an institutional capacity approach to graduation would have to confront the position that improving economic and social indicators combined with declining aid dependency is a prima facie case of adequate institutional capability.

Timing is important. When undertaking graduation discussions, the mere act of setting a date can make a difference in the experience. The date needs to be flexible enough to accommodate setbacks and changes, yet firm enough to satisfy development partners and placate host-country doubts. For example, population, health, and nutrition officials in Morocco set a date and then developed a two-phase strategy. In recognition that unforeseen problems likely would arise, the second phase was left open. USAID needs to commit to a graduation plan immediately after the date is set, at high levels in Washington and the Mission, and convey this commitment to the host country at appropriately high levels. Missions and USAID/Washington need to prepare an exit strategy that is broad and flexible yet definitively begins the transition toward terminating assistance. Critical short- and long-term goals and responsibilities of all actors should be spelled out clearly.

Decisions regarding when to terminate assistance—incorporating criteria used as well as graduation experiences—must be well documented and evaluated. The process should be transparent and publicized within the Agency. Resources should be allocated to evaluate the overall experience and success of a Mission before it closes, to present a clear history of Agency experience and offer lessons from successes.

The standard measures of development status all confirm that USAID regional bureaus do not have the same country profile of preparedness for graduation. The recent Agency practice of requiring a quota of graduates from each region produces a group of countries with such huge socioeconomic differences that their differences outweigh their similarities. These types of groupings make it impossible to design a standard approach to graduation.

Interviewees pointed out that the decision to terminate assistance should be a participatory process involving USAID, host-country government officials, representatives from civil society, and other donors. Although the

Agency's process often combines input from a number of U.S. government agencies, it tends to exclude private voluntary organizations (PVOs), the private sector, and the host country's governmental representatives. This has led to considerable tension, especially among U.S.–based PVOs—which are directly affected by decisions to close out activities and entire Missions. Wider participation in the process could offset problems that result when host-country partners do not immediately accept that USAID is leaving and could improve communication between the Agency and the PVOs affected.

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The 'How' Question: Transition Strategies And Mechanisms

THE QUESTION OF HOW the Agency should graduate a country has two parts. What is the process of graduation? And what should USAID leave behind?

A graduation sequence could proceed as follows. A methodology is used to identify graduation candidates, some or all of which are then selected for graduation. Next, even before the Agency works out the process for graduating a country, USAID determines, on the basis of U.S. policy objectives, what it wants to leave behind (its legacy). Finally, the Mission develops and implements a country-specific strategy (the process). The strategy may include several phases with changing emphases; it may include a phase between closing a Mission and concluding concessional assistance.

USAID's legacy in a graduation country may have two components. First, every country, whether a graduate or an "exit" country, will have whatever legacy the USAID projects have left behind. For example, the Agency has supported agricultural research in many countries throughout the world. The host-country research centers are staffed with graduates of American universities. The researchers maintain contact with American research institutions. These linkages have built up over a decade or more. Presumably, the graduation process would protect this type of linkage.

The second way to a legacy is in the country-specific graduation strategy. USAID currently has countries slated for graduation within the next five years. Five years is ample time to develop linkages or (perhaps) set up institutions that have not already evolved from the Agency's portfolio in that country. Examples here are foundations, commissions, host country–American business associations, alumni associations, and the like. This chapter looks in detail at attempts to build legacies during the final years of USAID programs.*

Endowed Local Organizations

Most of the approximately 35 endowments that had been funded by USAID by 1996 were intended to strengthen the viability of existing local organizations. (These differ from foundations with a mandated binational board of directors, which are discussed in the following section.) An important objective in virtually every case of Agency support for an endowment was enhancing sustainability of the organization. But there are relatively few cases where such support was a deliberate component of a strategy of transition to conclusion or graduation from concessional assistance.

Among local organizations endowed as explicit components of a transition process, the Korea Development Institute and Korean Institute of Science and Technology, established in the 1970s, are early examples. Both endowments were funded with local currency. In the case of KDI, this was in the range of $70 million. The original intent of these endowments was to create two institutions independent of government that would continue contributing to Korean development. Although not explicitly designed to further U.S.–Korean linkages, that did in fact result over time, as such U.S. organizations as the Harvard Institute for International Development established linkages with KDI.

A more recent example is an endowment established in 1993 for Profamilia, the Colombian affiliate of the International Planned Parenthood Federation. Profamilia is the largest family planning services provider in Colombia, accounting for 65 percent of all services offered. USAID capitalized the endowment fund with $6 million. The fund is managed by a U.S.–based investment bank and overseen by a three-member board.

Profamilia's transition strategy also calls for increased cost recovery and diversification of services. These measures, along with income from the endowment, are expected to ensure its viability as USAID phases out support for population activities in Colombia. The country is viewed as one of Latin America's population success stories, with contraceptive prevalence rates having reached 65 percent of couples of reproductive age.

Binational Foundations

As the name implies, binational foundations manifest a binational character in the structure of their governance and their programs. Some but not all binational foundations subscribe to the principle of *mutuality of contribution and benefit.* When USAID has funded such organizations, always through an endow-

*It is important to distinguish between *organizational structures,* such as binational foundations and commissions, and *funding instruments,* such as endowments and sinking funds. Whereas foundations are typically grant-making organizations supported by endowments or other funds managed by their own directors or a separate board of trustees, endowments may also be established to enhance the financial security of other types of organizations. An endowment usually refers to an invested fund that has been set aside for a specific purpose. The purposes may be supported only from the income generated by the invested funds, with endowment principal maintained intact. This arrangement is sometimes called a perpetual endowment. The principal of an endowment may also be disbursed according to an agreed schedule, in which case the invested fund is called a sinking fund. (See Horkan and Jordan, 2, 12.)

ment, they have typically been part of a transition or graduation strategy. The following four subsections discuss the experience of USAID-supported binational foundations in Costa Rica, Portugal, and Thailand and plans for a new one in Zimbabwe. Each of the first three has been a key component of USAID's transition strategy for concluding concessional assistance and has been considered a post-assistance means to maintain bilateral development-related linkages. Each example has at least one unique characteristic that bodes well for future performance or poses special challenges.

Costa Rica–USA Foundation For Mutual Cooperation

The Costa Rica–USA Foundation, or CRUSA, was established in San José, Costa Rica, in January 1996. Three months later, a bilateral agreement between Costa Rica and the United States established an endowment for the foundation. By mid-1996, the endowment's estimated worth was $12 million. Over time its value is expected to range between $30 million and $50 million. The sources of these funds include the remaining balances in substantial local currency trust funds that had been managed or overseen by the USAID Mission.

CRUSA's creation preceded by nine months the conclusion of USAID presence and concessional assistance in Costa Rica. It was the keystone of the Agency's graduation strategy. CRUSA's programmatic mandate is relatively broad: to "support sustainable development through technical cooperation, training, and technology transfer between the United States and Costa Rica, and to provide the Costa Rican government with access to specialized assistance required for the continuing improvement of its policies, structure, and service delivery systems." The initial emphases, which may be modified by majority vote of the board of directors, are on 1) reform of state institutions and structures (with great weight given to decentralization), 2) environmental policies and natural resource management, 3) trade liberalization and enhancement of Costa Rica's international competitiveness, and 4) technological developments in strategic areas.

CRUSA is governed by an "assembly of founding members" and a five-member board of directors. The founding members, five Costa Ricans and five Americans, were selected by the Costa Rican president and the U.S. ambassador, respectively. Subsequent vacancies of the founding members are filled through election by remaining members, subject to the condition that equality of numbers between the two nationalities be maintained. On the five-member board, two directors are appointed by the Costa Rican government, another by the U.S. ambassador; the remaining two are elected by founding members. A local private bank manages investment of the endowment fund under a trust agreement, and the foundation receives the difference between the previous year's earnings and the inflation rate.* The board meets at least quarterly to review assistance requests screened by a small executive staff.

Although CRUSA is operational, it is still too early to assess its performance. However, its design contains five noteworthy features likely to have a bearing on its effectiveness.

*This maintains the real value of principal. The endowment agreement provides that under "extraordinary circumstances, the Founders and the Board of Directors, by unanimous consent, may authorize the disbursement of previously capitalized interest as approved in the annual and financial and operating plans."

1. CRUSA is relatively amply endowed with local currency. At first this seemed problematic in light of the Costa Rican government's oft-repeated statement that a foundation based on mutuality of interest should also have a dollar contribution. In fact, two USAID Mission directors lobbied USAID/Washington vigorously for a dollar contribution but were turned down on grounds of budget constraints. The Costa Rican government was persuaded to accept a totally local currency–funded endowment in return for gaining access to a local currency fund held in the Central Bank that had been generated by previous USAID assistance. This fund amounted to about $20 million and was applied to such public sector restructuring elements as severance pay for laid-off government employees.

2. Although the restriction to local currency funds initially was perceived as a limitation, CRUSA was also seen as a means to absorb the large balances of outstanding local currency resources, as well as an opportunity to continue the technology exchange between the United States and Costa Rica. Few other Missions have access to the magnitude of local resources available to USAID/Costa Rica.

3. The stature and quality of the founding members has set a tone for high-quality operations. Persons with demonstrated capability and high integrity were selected. An additional qualification for the choice of U.S. members was that they had demonstrated a genuine and likely continuing interest in Costa Rica.[*] This, in the view of one USAID officer involved in creating CRUSA, helps offset the risk of having provided the founders considerable discretion regarding disbursement policy and use of funds. Continuing U.S. influence is also ensured by the requirement that the numbers of U.S. and Costa Rican "founding" members remain equal.

4. Once the CRUSA endowment was established and the local currencies transferred, all USAID monitoring and oversight responsibilities ceased.[†]

5. Though the views of other stakeholders—including the main opposition party—were sought informally in the development of CRUSA, the main interlocutor was the government in power. This is perhaps understandable, but at least one USAID officer involved at the time would have preferred a broader Costa Rican political consensus behind CRUSA to ensure its sustainability.

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[*]The U.S. members are Norman Brown, president emeritus of the Kellogg Foundation; Thomas Buergenthal, professor of law at George Washington University and honorary president of the Inter-American Institute for Human Rights; Franklin Chang–Díaz, NASA astronaut; Thomas Lovejoy, adviser on biodiversity and environmental matters, Smithsonian Institution; and Francis McNeil, former U.S. ambassador to Costa Rica.

[†]It is unclear why the Costa Rica–USA Foundation does not come under USAID Policy Determination No. 21, "Guidelines: Endowments Financed With Appropriated Funds." PD 21 requires a 5- to 10-year USAID oversight period for endowments financed with appropriated funds. The difference in Costa Rica may be because the substantial portion of the local currency trust funds were reflows from domestic loans made with local currencies generated by USAID assistance. Further, the agreement between the Mission and the Costa Rica government was not a grant or a cooperative agreement but a "mutual disposition of these funds." Finally, "ownership" of the local currency funds was a somewhat sensitive issue between the Mission and the Costa Rican government.

A senior officer of the USAID Mission during the period of the transition has provided some conclusions from the experience that bear on the ability of a Mission to effectively plan and implement a strategy for concluding concessional assistance. Those lessons follow:

1. Although morale of the Mission's Costa Rican foreign service national staff plummeted after announcement of the conclusion of the official bilateral program and closure of the Mission, the foreign service staff adjusted quickly and came to be a significant asset in planning and implementing the transition strategy. A key contribution to maintaining the loyalty and productivity of foreign service nationals during the transition period was the Mission's decision to use a significant portion of the local currency resources for a training fund. A large number took advantage of the program, many by completing university degrees. Again, the substantial local currency resources under the Mission's control eased the transition.

2. A chief obstacle to an orderly transition, one that created problems in the Mission's relationship with the Costa Rica government and Costa Ricans in general, was rigid instructions from USAID/Washington that accelerated the pace of closure and prohibited, at least initially, Costa Ricans' participation in regional training programs and support to regional institutions that happened to be located in Costa Rica. This was under the out-is-out policy that since 1992 has dominated the Agency's approach to the conclusion of programs and Missions.

3. The CDIE/Latin America and Caribbean Bureau review of the Costa Rica Program was underfunded, owing to a decision by the bureau that providing the initially requested $200,000 for the review, rather than the $50,000 actually provided, would invite reproach from some quarters of Congress. Even though the resulting study was informative and insightful, its coverage and usefulness were limited by this funding shortfall.

4. Changing Mission leadership three times during the transition process made it more difficult to maintain effective counterpart relationships and to rebuild and maintain Mission morale.

Portugal: Luso–American Development Foundation

The Luso–American Development Foundation (LADF) was established in 1985 through an endowment funded by the government of Portugal with funds generated by USAID Economic Support Fund grants as part of a base-rights agreement. Its establishment was a conscious element of a strategy of transition from USAID concessional assistance. LADF seeks to promote economic and social development in five areas: science, technology, culture, education, and commerce.* Early in the process, LADF chose to invest conservatively in Portugal and the United States to balance both countries' interests. The foundation favors projects that promote cooperation among Portuguese organizations and between Portuguese and U.S. organizations. The board's astute investment of endowment funds has caused the original grant to grow to more than $150 million.

*For more information about the foundation's projects and activities see the Internet site www.flad.pt.

LADF is a private entity under Portuguese law. U.S. influence on LADF programming and policies, along with the foundation's binational character, has declined over time. In 1988 the prime minister signed a law that restructured the foundation to give it greater autonomy. Control over the board of directors has been the focal point for debates regarding the appropriate level of government control. The decline highlights the larger issues behind the creation of all foundations: should the foundation be a mechanism for the host country to take control of the U.S. legacy, or should it be a way to maintain a U.S. influence in the graduated country?

In recent years the foundation has been criticized on operational and functional grounds. Critics argue that overhead is too high, reporting has been inconsistent, and too many expenditures have been unjustifiable. Some say the foundation has not been the catalyst originally envisioned for developing a sustainable relationship between U.S. and Portuguese institutions. However, recent reports from the U.S. embassy in Lisbon suggest much of this controversy has died down.

Some important lessons about developing foundations as a postpresence mechanism emerge from the LADF experience. First, a clear objective for the foundation should be defined at the outset. Will the foundation be a mechanism to promote long-term development or to promote government interests abroad? Second, careful attention must be given to how the board is selected and who is chosen for it. Who will appoint the members? How much control will the United States want over the long term? Finally, it is important to plan ahead. According to the final USAID representative, setting up the foundation and closing the Mission proceeded smoothly. Discussions were going on about Portugal's graduation seven years before the Mission closed, and the strategy was designed five years in advance.

United States–Thailand Development Partnership

The United States–Thailand Development Partnership (USTDP) was the last component of a USAID/Thailand transition strategy. The first attempt to fashion an explicit graduation strategy for the USAID/Thailand program occurred during the last half of the 1980s. This period also marked the commencement of Thailand's remarkable accelerated economic growth. The USAID Mission organized an off-site workshop composed of senior Mission staff and outside experts on Thailand. The workshop recommended, as a core element of a transition strategy, a "Thai–U.S. Partnership Foundation," to be endowed with funds provided by the U.S. and Thai public and private sectors. However, implementation planning for the proposed foundation encountered two obstacles:

1. The hoped-for use of new appropriations or tapping reflows from previous loans (PL 480 food aid loans) as a major source of endowment funding was blocked by executive branch objections and by congressional prohibitions against endowments funded with appropriated dollars.

2. Although USAID/Washington endorsed the effort, the embassy preferred the planning to take place without the participation or knowledge of Thai counterparts.

Since, unlike USAID/Costa Rica, the USAID/Thailand Mission had no local currency trust funds at its disposal, the first obstacle virtually eliminated the possibility of establishing an endowment. The second obstacle created unfortunate tensions in the relationship between the Mission and one of its counterpart agencies in the Thai government when the news of "USAID graduation plans" inevitably leaked to Thai government counterparts. The signing in mid-1990 of a memorandum of understanding between the prime minister's office and the visiting USAID Administrator helped ease these tensions. The memorandum committed both the Agency and the Thai government to promote expanded private, public, and professional collaborations, or "partnerships," between Thai and U.S. organizations. These partnerships were viewed as collaborations that would continue beyond the conclusion of the concessional assistance program.

A junta's assumption of power in late 1991 resulted in suspension of the USAID program. With the restoration of democracy in late 1992, active planning for implementation of the partnership concept continued. This culminated with the July 1993 signing of the U.S.–Thai Development Partnership project. The partnerships supported under the project stressed supporting Thai capacity to slow the spread of HIV/AIDS, and identifying and implementing sustainable solutions to environmental management and critical infrastructure problems. Twenty-five partnerships between Thai and U.S. organizations were to be supported through provision of resources to identify, plan, nurture, and "enhance the development" of joint ventures in the two subject areas—but not for implementing the activities or ventures themselves. Including three budget amendments between July 1993 and August 1994, a total of $9.1 million was obligated for the project, which had originally envisioned a total USAID contribution of $20 million. A joint proposal of the Kenan Institute of the University of North Carolina business school and Chulalongkorn University in Bangkok won a competitive bid to manage the partnership project. The joint entity is known as the Kenan Institute Asia.

A formal Thai Bilateral Graduation Strategy was issued in February 1994 by the Bangkok-based East Asia Regional Support Mission (which at the time included responsibility for the Thai bilateral program). The strategy proposed closing out all bilateral projects, except the partnership project and the Housing Guaranty Programs, by the end of fiscal year 1995. The partnership would close at the end of 1996, and the housing guaranties would close at the end of 1998. However, the strategy document expressed serious concerns that a proposed recision would eliminate an additional $10 million USAID contribution to the partnership project and threaten the project's viability.

Within two years—just before the September 1996 termination of the Thailand Mission and program—the USTDP-cum-partnership project was transformed into an endowed foundation, the Kenan Foundation Asia. Two factors made this possible: first, expansion of authority in fiscal year 1993 by the Congress to permit the establishment of endowments with appropriated dollars, and second, the creative hard work and goodwill of individuals at the Kenan Institute, the USAID Mission and USAID/Washington, and in the Thai government.

The foundation was established in August 1996 with the signing of a cooperative agreement that calls for a minimum total endowment of $10.5 million, with three contributors—USAID, the Thai government, and the Kenan Charitable Trust—each providing $3.5 million. The Thai government and Kenan Trust contributions are being provided in two disbursements, whereas the USAID contribution was provided as a lump sum. A group of U.S. banks manages the endowment fund. The foundation has a board composed of prestigious Thais, including former prime minister Anand Panyarachun (as its chairman) and U.S. Ambassador to Thailand William Itoh.

One issue particularly relevant to USAID's role is the extent of its oversight responsibility. With the closing of all operations in Bangkok in September 1996, this responsibility shifted to the regional bureau in Washington. Although Policy Determination No. 21 on Endowments specifies a USAID accountability period for dollar-appropriated endowments of 5 to 10 years, depending on the track record of the endowed organization, it is not clear how this would apply to an organization such as the Kenan Foundation Asia or the USTDP.

Six fundamental conclusions can be drawn from the USAID perspective on the Thailand graduation experience:

1. U.S. strategic foreign policy concerns can have a dominant influence over decisions to conclude or not conclude a concessional assistance program.

2. The congressional liberalization that permitted the creation of endowments with appropriated dollar funds was crucial for the USTDP.

3. Even though the total size of the endowment is fairly small, the three-way contribution from the U.S. public sector, U.S. and Thai private sectors (raised by the Kenan Institute), and the Thai government is unique in USAID's experience with endowments thus far. It implies a high degree of ownership, which bodes well for sustainability. However, the long USAID–Thailand relationship and its economic attractiveness to potential private contributors certainly facilitated both the Kenan Institute's ability to coax contributions and the Thai government's willingness to make them.

4. Attempting to prevent government counterparts from learning about Mission graduation strategizing is apt to backfire, as it did in Thailand. However, high-level interest and support, as demonstrated by the Administrator's July 1990 visit to Thailand, can help ameliorate counterpart concerns about graduation.

5. The Mission directors most intensively involved in establishing the United States–Thailand Development Partnership attest that the most demanding aspect of their work—in both time and energy—was keeping Washington "on board and on track" with the concept and with what was needed to implement it.

6. Accountability and oversight responsibility for endowments remains an unsettled issue for USAID.

The Kenan perspective on the Thailand experience offers five additional conclusions:

1. The USTDP's main *strengths* are clear objectives (especially to assist Thailand's development by helping create sustainable and mutually beneficial linkages between U.S. and

Thai organizations); a flexible response capacity (including the ability to go beyond mere funding by also providing information, contacts, and advice); the requirement that recipients put up a share of their own funds (usually a 50–50 match is sought), an essential prerequisite for screening and commitment; and the stability provided by the "endowment nature of the funding," which attracts and permits the retention of high-quality staff.

2. The main *challenges* include communicating effectively to the wide variety of potential Thai and U.S. partners (including those "accustomed to more traditional USAID programs" and those who "do not normally like to get involved in government programs"); identifying nongovernmental organizations that are prepared to provide matching funding; and attracting sufficiently high-quality and *sustainable* proposals from the Thai and U.S. sides.

3. Things Kenan Institute interlocutors wish had been *in place at the beginning* include more consensus-building with the Thai government to get greater government "ownership" of the USTDP; less stringent funding criteria for HIV/AIDS projects (where it was much more difficult to find market-oriented and self-sustaining ventures than for environment proposals); and broader definitions of subject areas for funding, to include public health and education and training, not just HIV/AIDS.*

4. Input from, and links with, the United States–Asia Environmental Partnership have been important to the USTDP. (A public–private initiative under leadership of USAID, US–AEP seeks to promote a "clean revolution" in Asia.) This has included the provision of funds for a vital staff person, support for urban infrastructure projects, and links with the US–AEP network of expertise, resources, and programs. Likewise, the Kenan Institute believes these have contributed significantly to the success of US–AEP programs in Thailand. However, the institute also believes the effectiveness of coordination and the potential for joint activities with US–AEP could be improved and expanded, and hopes the new US–AEP leadership will make this possible.

5. Among the lessons learned and observations are the following: a) the best and most sustainable proposals are those with strong interest and backing on the part of the Thai partner; b) a "partnership" program such as USTDP's must be anchored in a programmatic NGO or university with a "standard of operation," a sound track record, and, ideally, an endowment of its own (such as the Kenan Institute); c) the design phase must pay close attention to the tax structures of the partner country and the United States; d) the initial connection of the Kenan Institute Asia and the USTDP with the prestigious Chulalongkorn University in Bangkok helped raise the profile in Thailand, but a continuing strong institutional tie—difficult from a managerial point of view—was not maintained; and e) the strong support of entities such as the Kenan Charitable Trust and the University of North Carolina, and the ability of USAID to get congressional approval for contributing appropriated dollars to an endowment, were crucial—since it is, as the Kenan Institute puts

*In point of fact, subject areas eligible for funding were subsequently broadened to include education and public health more broadly defined, as well as environment.

it, “nearly impossible” to get corporate funding for a basic endowment.

Inasmuch as no field work was undertaken for this study, it was not possible to draw conclusions about the USTDP from the perspective of the Thai public or private sectors.

Zimbabwe–American Development Foundation

Pursuant to the Reinventing Government II decisions discussed in the previous chapter, the USAID program in Zimbabwe is scheduled to conclude in 2003. The program’s nearly 20-year history has been marked with fairly sharp political ups and downs in the bilateral relationship between Zimbabwe and the United States (Herrick 1997). As also shown in the previous chapter, although Zimbabwe’s economic and social indicators, as well as its institutional capacities, are significantly above average for sub-Saharan Africa, they fall far short of such indicators prevailing in countries in other regions where the United States has concluded assistance for reasons that included less need for concessional assistance as a significant consideration (e.g., Costa Rica and Thailand). For example, note the sharp disparity between the development triangle shown for Zimbabwe in figure 5 of chapter 2 and the graduate comparator triangle.

A critical element in the USAID/Zimbabwe strategy is to establish and endow a foundation, which, in the words of summary activity descriptions, would serve as a “hallmark of the evolving and mature relationship of official U.S. assistance in Zimbabwe.” However, these same descriptions admit that although the Zimbabwe government has made initial progress in moving to a liberalized, market-driven economy, the transition is far from complete. The continued exclusion of “traditionally marginalized groups” from access to economic opportunity and policy-making is also cited. Moreover, Zimbabwe is recognized as a “fragile democracy which needs to strengthen many of the fundamental aspects and institutions required for a free and strong civil society, thereby increasing economic opportunities” (USAID Activity Data Sheet).

The proposed Zimbabwe–American Development Foundation (ZADF) is intended to continue addressing these issues after the USAID program concludes by providing support to Zimbabwean NGOs actively engaged in increasing opportunities for participation in the private sector and political processes in that country. A particular emphasis of ZADF will be to increase the access to economic and governance resources (e.g., the justice system) of Zimbabwean small and microenterprises.

The foundation is also seen as the main funding mechanism for a strategic partnership within a new “special objective” for the USAID/Zimbabwe Country Strategic Plan: 1997–2003 (USAID 1997b). The special objective calls for “increased opportunities for participation in the private sector and political processes.” Though the strategic plan sees ZADF as the main instrument for accomplishing the objective, indicating that “there are no current plans for any other strategic partnerships beyond the ZADF,” the possibility of others is not ruled out. Grants awarded by ZADF are expected to range from $2,500 to $100,000 each.

The operational plan proposes identifying a U.S. private voluntary organization or foundation as a "lead organization" to manage the tasks involved in establishing ZADF, and to provide ZADF supervision, training, and monitoring as it gains experience. ZADF is to be endowed with $20 million, half of which is to be provided by USAID over three years, and half of which is to be raised from private sources in the United States and in Zimbabwe. The lead organization is also to be charged with raising this latter $10 million over an estimated three to five years. In addition to its $10 million contribution to the endowment, USAID is also providing a grant of $2.5–2.8 million to the lead organization for technical assistance to ZADF, to support ZADF start-up tasks and for seed grants to NGOs over an initial two to three years.

The Zimbabwe–American Development Foundation is expected to have "distinctive American ties through its founding and funding by the U.S. government, U.S. foundations, private voluntary organizations and other nongovernmental organizations, and through its approaches to development problems that draw on U.S. values, technology, and collaboration" (USAID Activity Data Sheet). The endowment principal of $20 million is to be maintained intact, and ZADF will use the endowment's net investment income to make grants to Zimbabwe NGOs "organized for public benefit and involved in promoting economic growth and democratic pluralism in Zimbabwe" (USAID/Zimbabwe 1997, 2).

Since the process of establishing ZADF, including selecting the lead organization, is still going on, it is impossible to assess ZADF's performance. However, some observations about the strategy and the challenges that lie ahead are worth noting:

A major assumption of the strategy is that the linkages between the United States and Zimbabwe, particularly in the private and NGO sectors, are sufficiently diverse and deep that the matching contributions totaling $10 million for the ZADF endowment can be generated. Several people interviewed within and without USAID questioned this assumption. Staff of the Kenan Institute Asia observed that even for Thailand, a country with wider and deeper linkages to the United States than Zimbabwe (including a substantial Thai community in the United States), an intensive, time-consuming effort was required to raise $3.5 million. They felt that raising $10 million from the private sector for ZADF would be extremely difficult, if not impossible.

Several USAID staff members have questioned the proposed *substantive* scope for ZADF.* The criticism is that the scope is too broad, particularly the addition of the democratization–governance–civil society component. These areas are deemed too difficult, complex, and sensitive to try to address in Zimbabwe at this stage and in the

*Two or three staff members of the Bureau for Program and Policy Coordination and one Africa Bureau staffer criticized the broad ZADF scope, pointing out that the democracy and governance components were initiated only *after* the decision had been made to phase out the program in 2003 and to establish the development foundation.

closing years of the USAID program. Rather, in the view of these critics, major if not exclusive weight should be given to the small and microenterprise economic access objective.

It would appear no *host* government contribution to ZADF will materialize—an indication that mutual "ownership" of ZADF probably will be narrower than that of the United States–Thailand Development Partnership.

Another major assumption is that the Zimbabwe government will not interfere with ZADF's operations. The USAID country strategic plan points out that legislation governing NGOs has been challenged in the courts as too restrictive and as giving the Zimbabwe government too dominant a role. While citing a recent court ruling in favor of NGOs, the country strategic plan admits that "in the sensitive political development area, government interference is a potential problem" (USAID 1997b, 43).

USAID oversight could be an issue. The country strategic plan envisions that the Agency would continue to monitor ZADF progress and compliance with agreement conditions and covenants, but that "after 7 to 10 years of solid operations, the fund would be turned over completely to the ZADF to continue in perpetuity." Thus, USAID's oversight responsibility would continue several years beyond the Mission's closing and the program's conclusion.

The country strategic plan contemplates additional strategic partnerships. This suggests that the Mission may fear its support to ZADF will not by itself be enough to achieve adequate performance in the programmatic results indicators it proposes monitoring.* However, just what those partnerships might be and how they would mesh and be consistent with ZADF—and, more important, with the 1997–2003 time frame and strategy for conclusion of the assistance program—are not indicated.

Binational Commissions

A number of binational commissions between the United States and other countries have been created over the last two decades. They may study a specific issue, such as the border zone between the United States and Mexico, or a broader range of subjects. In contrast to binational foundations, binational commissions entail formal bilateral agreements and usually require high-level official involvement from both countries. The relationship of binational commissions to a strategy of tran-

*Among the many indicators the country strategic plan identifies are these seven: credit to USAID-assisted groups, production and employment by targeted groups, percent of population reporting participation in civil society, number of independent sources of media, the Freedom House index on human rights and civil society, frequency of dissemination of budget and procurement information, and some measure of senior elected officials reporting civil society or NGO influence in their legislative and policy decisions. Also specified are relatively general "institutional results" for ZADF, including a "demonstrated ability to leverage additional funds for program activities (e.g., through cofinancing) and for augmentation of the endowment corpus" (USAID 1997b, 45–46).

sition from USAID concessional assistance has not been as close as in the case of binational foundations. An early example of a binational commission is the U.S.–Japan Friendship Commission. It was established on the U.S. side almost 50 years ago by an Act of Congress that provided for an endowment funded by reflows of U.S. loans to Japan after World War II for the reconstruction of the Ryukyu Islands.* Grants are made to both American and Japanese citizens and organizations that make proposals meeting criteria in five programmatic areas, such as education, business, and culture.

The U.S.–Spain Joint Commission was established as part of a strategy of transition from annually appropriated concessional economic aid. However, the commission, short-lived by design, was funded by a specific military base rights agreement related to an Economic Support Fund grant. The Omani–American Joint Commission, created in 1980, was unique in that it was created as a joint Omani– and U.S.–staffed institution to administer the USAID program. In point of fact, it operated more like a traditional USAID Mission, although the joint structure facilitated gradual transfer to greater Omani management. The commission and staff phased out in 1996, after the expiration of the second bilateral agreement.

The United States–South Africa Binational Commission, inaugurated 1 March 1995, meets twice a year in locations that alternate between the United States and South Africa. Vice President Al Gore and South African Deputy President Thabo Mbeki serve as cochairmen (South Africa Binational Commission 1998). The Commission has six committees: Agriculture; Sustainable Energy; Science and Technology; Trade and Investment; Human Resources Development and Education; and Conservation, Environment, and Water. The committees are for the most part chaired by the relevant U.S. department secretaries and South African ministers. One exception is the Human Resources Development and Education Committee, which has been chaired on the U.S. side by USAID Administrator Brian Atwood. However, reportedly because of South African concern for parallelism in committee leadership, the U.S. education secretary was to have assumed that committee's chairmanship as of the February 1998 binational commission meeting.†

The Commission's envisioned goals include

- Promoting the bilateral relationship between the United States and South Africa through a working partnership at the highest levels of government

- Cooperation between the two countries by establishing permanent and vigorous institutional partnerships

- Identifying U.S. expertise to help South Africa meet its reconstruction and devel-

*The experience of this commission was drawn on in the late 1980s for planning a joint U.S.–Thai foundation. However, the position of the Treasury Department and the Office of Management and Budget at the time was that both the creation of an endowment and the use of loan reflows would again require special legislation.

†The Clinton administration canceled the meeting, owing to the Iraq crisis.

opment program goals and to explore areas for cooperation based on shared values and experiences

Building upon and expanding the involvement of both private investors and NGOs in strengthening U.S.–South Africa ties

At least one staff member in USAID's Africa Bureau sees the Commission as an opportunity to thoughtfully fashion a post-assistance relationship with South Africa with more adequate lead time than other graduation cases, such as Zimbabwe's, which have been expedited for budget reasons. Budget constraints have been at least part of the rationale for the 2003 deadline for concluding concessional assistance to South Africa as well. In South Africa's case, the Commission (unlike the Zimbabwe–American Development Foundation) has already been functioning for nearly four years. The networks of private sector and civil society institutions in South Africa are considerably more developed than in Zimbabwe, as are already existing institutional ties between the United States and South Africa. A major challenge, according to the same staff member, is how to bring about a closer relationship between the still substantial but rapidly declining U.S. bilateral assistance program (about $70 million in fiscal year 1998) and the emphases of the Commission.

Transition Endowments In the ENI Region

The Europe and new independent states region is treated separately, because of the special characteristics of its programs: a limited assistance time frame and a strategic emphasis on transition to free-market-based democracies (for a more in-depth discussion, see chapter 2). This section will discuss the USAID/Poland "graduation plan" (a proposed Polish–American Foundation) and a proposed regional approach (the Baltic–American Partnership Fund).

USAID/Poland Strategy

In May 1996, USAID/Poland issued a strategic plan for conclusion of the economic assistance program: *Poland in the Year 2000: USAID Graduation Plan*, or the Poland 2000 Plan. As the title implies, the proposed graduation date is 2000, just 11 years after the program began with the inception of the Support for East European Democracy Act in 1989. Although that date made Poland one of the earliest country programs in the region, an 11-year life span is less than a quarter of those for Costa Rica and Thailand. As previously explained, a basic rationale for the short time frame for countries within the Bureau for Europe and the New Independent States is that in several dimensions their stage of socioeconomic development *before* World War II, though perhaps not as advanced, was clearly closer to that of Western European countries than to most of the less developed countries of Africa, Asia, and Latin America.

These comparisons provide some context for understanding recent debate in USAID/Washington regarding Poland and broader ENI transition strategies. The Poland plan points to impressive economic reforms, private sector–led economic growth, and the reentry of Poland into private international capital markets. However, it also points to remaining challenges, such as inflation still in the double-digit range, underdeveloped financial institutions, wide regional disparities, and a per capita income (adjusted for purchasing power) less than a third of the European Union average.

Nonetheless, in view of the 2000 graduation date and an expectation that program resources will decline sharply from the 1989–95 annual average of about $140 million, the plan proposes a considerably narrower strategic emphasis for the program's final five years. From an earlier strategy that had included 10 of the 11 ENI Bureau strategic objectives, the Poland 2000 plan examines three:

> The private sector is stimulated at the company level.
>
> A competitive, market-oriented private financial sector is developed.
>
> Local government is effective, responsive, and accountable.

Of these, the dominant strategic objective is the third—local government. The plan argues that strengthening the nascent institutions of government and civil society at the local level is the key to sustaining Poland's transition to a free-market democracy, as well as to reducing regional disparities. The plan also observes that this last objective is not receiving adequate support from other donors.

The Poland 2000 plan devotes some attention to post-assistance mechanisms or linkages. It identifies several Polish-to-U.S. institutional linkages under each of the three strategic objectives and proposes nurturing them over the remaining years of the program, with the expectation that they will sustain themselves beyond 2000. An endowment derived from reflows of the Polish–American Enterprise Fund is now a subject of interagency study.

Other enterprise funds have been established with USAID support in eastern and central Europe. The largest of these, the Hungarian–American Enterprise Fund, has moved more slowly and with a less successful track record than its Polish counterpart; therefore, it would be several years before this fund could generate profits and reflows adequate to establish an endowment.

The Baltic–American Partnership Fund

Although most country programs in Eastern and Central Europe are to be phased out over the next three years, the ENI Bureau has identified the nascent stage of civil society as a weak link in the chain of support for the sustainability of free-market democracies throughout the region. This has led to a recent regional initiative intended to nurture and strengthen civil society in the period beyond conclusion of the country assistance programs.

The Baltic–American Partnership Fund, authorized by ENI in March 1998, is to be endowed with $15 million, half of which is to come from the Support for East European Democracy (SEED) Act through USAID/ENI and half from the Soros Open Society Institute. The partnership fund will provide grants to nurture civil society in Estonia, Latvia, and Lithuania. The USAID contribution is expected to be drawn down over 10 years (as a 10-year sinking fund), but BAPF is to have the authority to seek other funds so it can continue beyond this period. Since BAPF will be a new organization, USAID/ENI expects to maintain active oversight over the entire 10-year drawdown period.

The endowment fund is designed as a 15-year sinking fund. USAID will monitor the foundation's operation closely for its first five years. The intended sinking fund approach has been questioned in some quarters of USAID/Washington. The sinking fund seems to call into question the vision of an endowed foundation as a continuing post-assistance mechanism. However, the ENI Bureau has successfully argued that the Baltic–American Partnership Fund's useful life is limited to accomplishing the objective of nurturing civil societies, and so, in accordance with USAID Policy Determination No. 21 on Endowments, "preservation of the endowment principle is neither necessary nor desirable" (Steele 1998).

Other Transition Endowments

The Center for Development Information and Evaluation study of endowments also identifies the Ecological Trust Fund in Panama as part of a graduation strategy. This fund was established in 1995 with $8 million from USAID, $15 million from the government of Panama (consisting of reflows from a previous Agency project), and $2 million from The Nature Conservancy, an international nongovernmental organization. Despite Panama's contribution, the binational character of the governance and programming of the fund is unclear, except that one area of emphasis is the Panama Canal watershed. The CDIE study also describes endowment funds set in seven countries under the 1990 Enterprise for the Americas Initiative. However, the EAI was not established as a part of a graduation strategy but for debt reduction purposes. As a quid pro quo, Argentina, Bolivia, Chile, Colombia, El Salvador, Jamaica, and Uruguay each agreed to establish a local currency endowment fund to support environment and child survival programs.

Sector-Specific Strategies And Mechanisms

The following sections describe and analyze the evolution of *sectoral* graduation strategies for economic growth in Indonesia and for population, health, and nutrition in Indonesia and Morocco. As indicated in chapter 2, the Bureau for Asia and the Near East has evolved a graduation strategy of centering on sectors, rather than on an entire country. The bureau has adopted a sector-by-sector approach, recognizing that it is being forced—partly by budget constraints—into phasing out programs in such countries as Indonesia, Morocco, and the Philippines, even when the conditions for overall "fully sustainable development" have not yet been met. The approach also accounts for the fact that development does not proceed in parallel across all sectors simultaneously. The Indonesia and Morocco experiences illustrate that the strategy for transition to phaseout is at least as important as the role and significance of post-assistance mechanisms. Although the latter has attracted attention in the case of Indonesia's economic growth, this aspect has received little notice in the population, health, and nutrition cases—perhaps because they are phased, with the second phases to cover the period 2000–05.

Revised Strategy For Economic Growth In Indonesia

The USAID/Indonesia Mission and the Bureau for Asia and the Near East decided in 1996 to zero in on graduation in the economic growth and population, nutrition, and health sectors. However, the approach chosen for each sector was different, so we will discuss them separately. In the case of the economic growth sector, the decision was to base the Mission's strategy during 1996–2001 on what the Mission saw as two obstacles to continued success: international trade and domestic competition. Graduation from the sector was planned for 2001. This timetable has been put on hold in view of the current economic crisis afflicting Indonesia. The USAID economic growth strategy, before the event, identified some of the factors behind the current crisis:

> The substantial trade barriers which remain and restrictions on domestic competition promote rent-seeking behavior and favor monopolistic and oligopolistic positions which are neither economically efficient nor equitable in terms of market access. [USAID/Indonesia 1997a, 1]

The purpose of this discussion is not to detail the rationale for, or the substantive content of, this strategy but to describe an approach that the Mission identified to facilitate the transition to graduation. The approach involves the provision of grants to create or reinforce linkages among a number of U.S. and Indonesian institutions interested in improving the Indonesian economic policy framework. The summary of the *Revised Strategy for Economic Growth Activities* expressed this component of the strategy:

> Several "sustainability products" from the partnerships are expected by the end of the fiscal year 2001: a series of financially self-supporting partnerships between Indonesian and U.S. public and private entities gave weight to economic policy and regulatory issues; these linkages are expected to encompass think tanks and research entities in both Indonesia and the United States which have a *particular mutual interest* in trade, investment, and competition issues as they affect the two countries. [USAID/Indonesia 1997a, 4 (emphasis added)]

Contrary to what might be inferred from this passage, the Mission did not necessarily envision that every one of these partnerships would survive beyond graduation. However, there was an assumption that something like a minimum critical mass of them would survive. The summary document concludes:

> The need for economic change in Indonesia, as well as U.S. economic interest in the country, will obviously not end as we enter the new millennium. However, by the end of fiscal year 2001, we will test the hypothesis that the value of the partnership relationships which have been developed is worth more than the USAID grant funds which have nurtured them. What we foresee is the continued strengthening of economic ties be-

> tween the two countries as private groups and key public institutions continue to engage in the exchange of ideas and technical expertise aimed at eliminating barriers to economic efficiency and fostering mutually beneficial growth. [USAID/Indonesia 1997a, 7]

The Mission dubbed the modality for nurturing these linkages the U.S.–Indonesian Partnership for Economic Growth, or PEG. The Mission states that it had conducted several surveys of "customers related to the formulation of this economic growth strategy" and found "strong interest in maintaining a mutual dialog on key elements of economic policy reform." The strategy is careful to point out that the linkages it plans to nurture should not be characterized as "institutional development":

> Great strides have been made in creating [in Indonesia] a set of public institutions which have an internal coherence and an ability to respond and cope with the problems at hand. Concomitantly, USAID no longer possesses the resources needed to mount major projects aimed at institutional development in the economic field. These factors dictate a move to other modalities of assistance that rely more heavily than ever on policy rather than on institutional change. These modalities will rely more heavily on linkages between institutions with a sustainable, mutual interest in improving the economic framework which makes possible strong commercial and financial ties. [USAID/Indonesia 1997a, 8]

These are the conceptual and experiential underpinnings for the "transition" aspect of the USAID/Indonesia economic-growth graduation strategy. Whether this strategy is completely valid, in light of the now full-blown Indonesian economic crisis, may be arguable. For example, "institution building" with regard to accountability and transparency in the financial and regulatory sectors may still be a serious need in Indonesia, a need that USAID might have some comparative advantage in helping meet. But that question goes beyond the terms of reference for this study.

Population, Health, and Nutrition Graduation in Indonesia

The PHN graduation strategy received approval in April 1997 as a "Transition Plan for USAID/Indonesia's Assistance in Population, Health, and Nutrition." In contrast to the economic-growth graduation strategy, the PHN strategy envisions two phases: from 1996 to the beginning of fiscal year 2000, and from 2001 to 2005. The essence of the plan is that by the beginning of 2000, USAID will have completed its objectives and ceased funding all activities in the family-planning and reproductive health area but that essential activities in HIV/AIDS and health care financing may continue beyond that point—depending on the outstanding needs and staffing and financial resources available to the Mission at that time (Koek 1997; USAID/Indonesia 1997b).

There was protracted disagreement between the Mission and Washington, and *within* Washington, about the specific timing of these phases. Budget considerations ultimately became the determining factor. One observer noted that the 18 months it took to reach a decision on the strategy, the time frames selected, and the lack of clarity about some aspects of the strategy led to confusion and some loss of USAID credibility among partners—Indonesian government counterparts, other donors, and NGOs. Though they felt reasonably confident about the phaseout period eventually chosen for family planning and reproductive health, they had little clarity about what the second phase would look like. For example, it was unclear how or to what extent post-assistance linkages in family planning and reproductive health could be nurtured. In contrast to Colombia, government in Indonesia has been dominant in family planning. Phase I of the Indonesia PHN strategy calls for improving the sustainability and service delivery capability of family-planning-related NGOs, as well as strengthening the strategic planning capacity of the Indonesian government entity responsible for family planning services.

According to the Mission's Transition Plan, by 2000 even HIV/AIDS and health financing projects directly supported by the Mission will have ended. USAID-supported activities during phase II will be

> limited to key "development cooperation" activities deemed necessary to overcome a global challenge or to complete the final transition. Resources for these activities are expected to be minimal, and management and funding of these activities would be provided through the Global or Asia and the Near East Bureau. They would be implemented by Global Bureau [Cooperative Agreements], and monitored in Washington, with limited technical backstopping from USAID direct-hire staff assigned to Jakarta." [USAID/Indonesia 1997b, iv]

Criteria used to support activities in phase II will be a

> more limited variation of the criteria used for phase I. They include degree to which the activity is required to achieve full sustainability; global impact; feasibility within limited time frame; USAID comparative advantage; and minimal management requirements. [USAID/Indonesia 1997b, iv]

Thus, there would appear to be more work necessary for phase II on several fronts, including substance, sources and volume of funding, and sources and extent of management. For example, these passages fail to make clear whether USAID population, health, and nutrition staff will continue in Jakarta after phase I. One area in the text suggests there will be no staff in Jakarta; another refers to "technical backstopping from USAID direct-hire staff assigned to Jakarta." The trip report summarizes the principal issues:

> Initially, (2000–04/5) there will probably be a need for some sort of programmatic assistance, particularly in HIV/AIDS and health care financing. As Mission staff levels reduce further, this kind of assistance will have to be implemented by Global Bureau projects, or some other USAID/Washington mechanism. What kind of on-the-ground support would these programs require? What kind of Indonesia-dedicated staff would be required in Washington? . . . Indonesian officials have indicated a need for some kind of continued relationship with USAID after assistance has ended. This is not a role that can be filled by embassy staff, as it requires knowledge of the development and technical com-

munity and of development-related issues. One of the Indonesian officials we met with also made it very clear that while there may be a role for nongovernmental organizations, *NGOs could not act on USAID's behalf when we pull out.* In many developing countries, NGOs are not as appreciated as they are in developed countries and cannot get access to the government. [Koek 1997, 5–6 (emphasis added)]

The head of the Indonesian government family-planning program indicated, "No, we don't need your money, but we want the technical relationships." The trip report continues:

> Some of the functions to be carried out in a post-assistance relationship include: "Interact with government and technical ministry officials; represent the U.S. government and be familiar with development issues and programs. Function as a window to international donor and technical meetings and community. Facilitate a relationship between host country institutions and U.S. private organizations and/or universities. Support for resident experts to share experiences back and forth." Exactly how this relationship could be manifested or implemented is as yet undefined. Would it require an in-country presence? What kind and at what level? What kinds of mechanisms should be developed to facilitate this? Options for implementing a more equal partnership with developing country counterparts after assistance has ended would be tremendously useful for Missions developing transition/phaseout plans.

USAID/Morocco's Population and Health Transition Plan

Over the last several years, the USAID/Morocco Mission has developed a "Transition Plan for Achieving Sustainability in Family Planning and Maternal and Child Health." This followed a signal from Washington in autumn 1994 that the USAID/Morocco program had been identified for a transition to phaseout. Though discussions had begun in fiscal year 1989, the Mission argued successfully for a phaseout in population and health rather than a full closeout. "Sustainability" in the transition plan is thus defined:

> The ability of the health system (public and private) to produce high quality [family planning and maternal and child health] information, products, and services that are sufficiently well valued by the population so that adequate national resources are committed to ensure their continued delivery. [USAID/Morocco 1997, 2]

The plan, as with Indonesia's population, health, and nutrition plan, is divided into two phases: a bilateral phase, which completes bilaterally funded assistance by the year 2000; and a postbilateral phase, which may include activities funded through USAID/Washington mechanisms (USAID/Morocco 1997, 4). The first phase is to run 1996–99, and the second phase 2000–05. The plan goes on to observe that each phase will entail different financial resource and staffing requirements, with phase II requirements expected to be less than phase I on both counts. Plans for phase II continue to evolve and were to be finalized in January

1999. The following narrative describes some issues USAID/Morocco struggles with while planning to close its PHN sector. There is the same ambiguity as in the USAID/Indonesia PHN plan regarding in-country direct-hire staffing in the second phase. Though it is stated that "bilateral funding" will conclude at the end of phase I, the following statements are made with regard to staffing:

> Since achieving sustainability is a labor-intensive endeavor, staffing levels should be maintained through the end of the decade (phase I) to ensure that sufficient management oversight is in place. [U.S. direct hire] and [foreign service national personal services contractor] levels decline significantly after FY 99. . . . While it is too soon to define the exact staffing configuration that will be required for phase II, it is expected that a combination of USDH, FSNs, and NGOs in Morocco, coupled with USAID/Washington expertise, will be needed.

The expectation in both the Indonesia and Morocco cases, apparently, is that resident Mission staff will continue to be required even though all funds are coming from Washington. The ambiguity on behalf of both Missions may reflect the desire to maintain flexibility during the transition process.

The substance of phase II in the USAID/ Morocco plan is unclear; however, it is expected to evolve as the end of phase I approaches. Though "intermediate results" are specified for the end of phase I, goals for the end of phase II apparently have not been determined.

The Bureau for Asia and the Near East initially perceived the experience of Tunisia in phasing out USAID population assistance during 1988–90 as a model for phaseout in Morocco and Indonesia as well. But the model soon came to be viewed as not particularly positive. First, there was general agreement (at least among population, health, and nutrition officers) that the Tunisia PHN graduation was done in a somewhat preemptory fashion. Second, whereas there was confidence at first about the sustainability of Tunisian progress (given the relatively high levels of contraceptive prevalence at graduation), alarms sounded when the classic population and health indicators did not continue to perform. Furthermore, during a USAID employee's temporary-duty visit to Tunisia in 1992, some members of the Tunisian government and the United Nations Population Fund expressed interest in resuming USAID assistance because other donors were unable to provide the type of contraceptive assistance that the Agency had formerly provided. An observer described the problem:

> The implementation capacity of the government had been overestimated in USAID's graduation decision; also it was incorrectly assumed that the private sector (for-profit and NGO) would step forward with service delivery if the policy environment were right. This did not happen—and it should not be surprising in situations where the government has dominated programs and where the private sector has had little previous involvement in family-planning implementation or in the planning for transition from USAID assistance.

The situation in Morocco, and to a lesser extent in Indonesia, is similar. To date, little attention has been paid to the private sector's role. The Moroccan government has tended either to be in a state of denial about the USAID phaseout or to assume that another donor will fill the vacuum USAID leaves. The Bureau for Asia and the Near East, noting the steady progress in Morocco of population and health indicators (contraceptive prevalence, total fertility, infant mortality, under-5 mortality), concluded that the country could continue progressing on its own. However, the Global Bureau expressed concern about the "fragility" of progress in Morocco and that the fruits of USAID investments might be lost.

Although commodity assistance will not continue in phase II, it appears that capacity-building assistance will. Given that the decision to phase out of PHN in Morocco is a reality, it seems that technical assistance to strengthen such functions as procurement and standards setting and enforcement would be critical during both phases. The Moroccan minister of health reportedly appealed to the assistant administrator for the Bureau for Asia and the Near East to reestablish assistance after 2000, with a stress on policy and technical dialog more than financial aid.

There has been progress on at least three other fronts critical to sustainability:

> The Mission communicated with the World Bank and the European Union about assuming some USAID activities as it phases out. For example, one of USAID's phase I objectives is to achieve maternal mortality reduction in a pilot activity. The European Union has expressed strong interest in a follow-on activity. Further discussions with other donors will continue.
>
> After first resisting, the Moroccan government has agreed to permit and encourage increased participation of for-profit health and family planning practitioners. The initial results of a pilot training program, in which the government bestowed its seal of approval on graduate private practitioners, are positive.
>
> With no line item in the Morocco budget for contraceptives, mobilization of domestic resources for program sustainability has been a major concern. The Moroccan government has agreed to set up a pilot project for contraceptive cost recovery, a concept that had been resisted on legal and cultural grounds.

To date, there has been little thinking about some kind of postpresence mechanism. The only NGO with a relatively broad base is the Family Planning Association of Morocco, but this is considered insufficiently broad to provide an adequate foundation for an endowment.

Two overarching lessons come out of both the Indonesia and Morocco experiences so far:

1. Adequate time for transition to phasing out of a sector such as population, health, and nutrition is essential. Particularly in Morocco, the full extent of both phases, until 2005, will probably be necessary. And carefully designed and implemented pilot and capacity strengthening activities will be essential to make the most of this time frame.

2. High levels of the host government need a clear, high-level expression of the decision to phase out from USAID/Washington—and perhaps from elsewhere in the U.S. government. The lack thereof was a problem in both Indonesia and Morocco, with the result that time was wasted, confusion was sown, and initial planning and design tended to be carried out only on one side when it might have been undertaken jointly.

The Proposed 'Strategic Partnership' Approach

The clearest articulation within USAID of the "strategic partnership" approach was issued in a 15 January 1997 working paper by an intra-agency franchise working group and entitled "Implementation of USAID programs in Nonpresence Countries by Nongovernmental Organizations." The private voluntary organization community sees the strategic partnership as relevant to graduation strategy in view of the partnership's potential to facilitate the transition to graduation. The franchise working group observed that

> A part of the Agency's strategy for maintaining programs in nonpresence countries consists of country programs managed entirely by NGOs under contract or assistance arrangements (grants and cooperative agreements). The establishment of a new and expanded relationship with NGOs is endorsed. This new relationship is defined by an empowerment of NGOs to undertake USAID development initiatives in countries where no Agency employee may be stationed. [USAID/Franchise Working Group 1997, 1]

This document replaced a term—"franchising"—that had been used previously to convey the concept.* As explained in the working paper:

> In describing this relationship with NGOs, the working group concluded that the term "franchising," while stimulating innovative thought regarding outsourcing and privatization possibilities, may pose an obstacle in that different interpretations of the word may give rise to widely differing expectations. Therefore, with respect to USAID's reengineered program operations, this relationship with the NGO community is characterized as a "strategic partnership" and program implementers can also be referred to as "strategic partners." Therefore, for the sake of clarity these terms are used [later], rather than the terms "franchise" and "franchisee."

The paper spells out two significant characteristics of strategic partnerships:

> NGOs are defined broadly to include all nongovernment business and civil society—that is, for-profit firms, institutions of higher education, private and voluntary organizations, and other nonprofit entities.

> A strategic partnership is envisioned to implement a part of a USAID strategic objective or, in some countries, an entire strategic objective.

*The franchising concept was first introduced by Larry Byrne, then assistant administrator of the Management Bureau, at an April 1995 meeting with the leadership of the Advisory Committee on Voluntary Foreign Aid.

However, the working paper goes on to note:

> The difference lies in the degree of authority the NGO is expected to exercise over the implementation process. The NGO will agree to achieve specific results. In many cases, after selection, the partner will be responsible for leading and coaching the strategic objective and the results package teams. Within the scope of the contract or assistance arrangement, the NGO will exercise discretion over the management of activities, and it will be able to decide which intervention, or set of interventions, is most effective and to make funding allocation choices accordingly.

Two additional working paper observations deserve mention:

1. Though the strategic concept would appear to apply *in principle* to any country from which USAID had decided to withdraw its direct-hire presence, the working group thought the best candidates for strategic partnerships would be countries expected to graduate from USAID assistance over the next 5 to 10 years.

2. A strategic partnership would be entered into for a limited period (e.g., two or three years), and it would require appropriated USAID funding; that is, it would constitute a potential postpresence mechanism, not a post-assistance mechanism. However, a strategic partnership could appropriately be viewed as a potential mechanism for transition to graduation in two stages—that is, from postpresence to post-assistance.

Although members of the Advisory Committee on Voluntary Foreign Aid (ACVFA) appreciated the conceptual and operational clarifications incorporated in the early 1997 working paper, they continued at year's end to have several concerns about how the concept would work in practice. Concerns and recommendations (Storck 1997) included the following:

> USAID needs to consult with partners before and during the closeout process (and field guidance should address this).
>
> The Agency should now implement strategic partnerships in countries already slated for closeout, rather than wait for issuance of the next list.
>
> Criteria for strategic partnerships should be broadened beyond what was perceived as a singular emphasis on technical expertise in the USAID strategic objective sector in the 1997 working paper.
>
> Related to the previous recommendation, the Agency needs to identify the comparative advantages of different USAID partners, in order to achieve broader and more strategic goals (including U.S. foreign policy goals), in addition to sectorally based strategic objectives.

A related issue is the extent to which a strategic partner could assume a policy dialog role with the host government. The January 1997 working paper appears to condone such dialog, provided it is "limited to the technical area, the USAID results framework, and the specific set of results that is being implemented by the strategic partner in the nonpresence country." This construction seems inconsistent with the suggestion in the last point, cited earlier by the ACVFA, that USAID partners take on broader and more strategic goals, including foreign policy goals. Closely associated is the issue of representation, although here there seems a greater convergence of views, with both USAID and ACVFA members agreeing that the strategic partner should not be asked to represent USAID, thereby blurring the distinction between the private voluntary organization and the U.S. government.* Another consideration is the attitude of at least a few host governments about dealing with NGOs. A technical relationship may be palatable, but the quotation from an Indonesian government official in the earlier section on graduation in that country ("We don't need your money, but . . .") suggests that a policy dialog relationship with an NGO strategic partner might not be palatable to some host governments.

Since mid-1997, ACVFA leadership has been pressing USAID to identify two or three pilot countries where the strategic partnership concept could be made operational. ACVFA leadership agrees with USAID management that the graduation process deserves good management, and it sees the strategic partnership approach as an important element in a well-managed graduation process. ACVFA leaders have also suggested that the United States combine maintaining a strategic partnership in a country without a USAID Mission with placing a development attaché in the U.S. embassy there. This would be one way to resolve policy dialog and representation issues. The development attaché would take on such functions considered outside the strategic partnership mandate. As of early spring 1999, there had been no further action with respect to the strategic partnership concept. The Bureau for Policy and Program Coordination has been charged with the responsibility of further considering the strategic partnership approach in connection with its continuing development of Automated Directives System 205 on USAID and nonpresence countries.

Notwithstanding its introduction under the label of franchising three years ago, the strategic partnership concept has yet to become reality. It is true that the Agency historically has turned to private voluntary organizations to administer programs for humanitarian reasons in countries from which it has decided to withdraw government-to-government assistance, as well as all or most direct-hire presence, because it has judged the country a poor development partner. However, as suggested earlier, what distinguishes the strategic partnership from previous reliance on private voluntary organizations or NGOs in nonpresence countries is that the partnership is deemed a strategic steppingstone to graduation. Since 1995, a series of interchanges about the strategic partnership approach have occurred between USAID and ACVFA, involving correspondence; memoranda; reports; meetings between ACVFA leadership and USAID, including the Administrator; and ACVFA subcommittee and full committee

*Another related issue concerns functions the Office of Management and Budget identified in its Circular A–76 as "inherently governmental." These functions, delineated in an annex to USAID/Franchise Working Group 1997, deal with matters such as entering into financial arrangements on behalf of the U.S. government and supervising U.S. government employees. However, they also include "conduct of foreign relations" and "selection of program priorities."

meetings. The frequency of these interchanges generated high expectations for the strategic partnership concept on the part of the U.S. private voluntary organization community, expectations that have turned into growing impatience and frustration with the long gestation period.

Regional Approaches

Every regional bureau, as well as the Global Bureau, has pursued, in one form or another, maintaining linkages with institutions in countries where USAID is about to conclude, or already has concluded, concessional bilateral assistance through regional mechanisms. Regional projects have been a significant feature of USAID strategies in the Africa and the Latin America and Caribbean regions for a decade or more. Programs emanating from these strategies have not concentrated on countries about to graduate. Under budgetary and other pressures to phase out bilateral programs, regional programs are being reviewed as potential instruments to maintain some development linkages in graduate countries. However, under the strictest interpretation of the out-is-out policy of the last few years, regional and global activities have encountered difficulties in supporting involvement of individuals or institutions from countries where USAID has phased out.

Two other regional bureaus have developed regional activities that have not met resistance within the Agency on grounds of conflicting with the out-is-out policy. The Bureau for Europe and the New Independent States' regionally endowed foundations were described in a previous section. The other initiative is the United States–Asia Environmental Partnership, developed in the Bureau for Asia and the Near East. The balance of this section briefly describes that partnership and discusses its relevance as a mechanism for facilitating graduation and for maintaining development linkages in graduate countries.

United States–Asia Environmental Partnership

The United States–Asia Environmental Partnership (US–AEP) is an interagency program, led by USAID, with the active involvement of the U.S. Environmental Protection Agency and the Foreign Commercial Service of the U.S. Commerce Department. It was established as a presidential initiative in 1992 to help address environmental degradation and sustainable development issues in Asia and the Pacific by mobilizing U.S. environmental experience, technology, expertise, and services (US–AEP 1998; Bando 1997). US–AEP activities fall under the following program components:

- Fostering and disseminating "clean technology" and environmental management
- Developing urban environmental infrastructure
- Establishing a policy framework to sustain a "clean revolution"

The Environmental Exchange Program supports these activities with business and technology exchanges, and fellowships.

US–AEP seeks to be a catalyst for private- and public-sector initiatives to apply U.S. environmental technology and expertise. It works through Asians and Americans, nonprofit organizations, professional associations, private businesses, and government agencies to stimulate direct technology transfer, develop networks and long-term relationships, disseminate information, identify financial aid vehicles, provide grants and fellowships, and organize business and technology exchanges. Integral to US–AEP's operations is its cadre of local market experts, or US–AEP environmental technology representatives, who staff technology cooperation offices in 12 cities in 10 Asian countries. Technology representatives are not direct-hire USAID employees but a mix of American and local national people with contacts, experience, and expertise in the field. They act as environmental experts, brokers, or matchmakers, and as problem solvers. Offices are currently in Bangkok, Chennai (formerly Madras), Colombo, Hong Kong, Jakarta, Kuala Lumpur, Manila, Mumbai (formerly Bombay), New Delhi, Seoul, Singapore, and Taipei.*

Among the accomplishments reported by the US–AEP are

- The transfer of an initial US–AEP investment of $72 million and partner investments of $263 million

- About $1 billion worth of U.S. private-sector environmental equipment and services to Asian public and private sectors

- The participation of over 2,500 Asians and Americans in the technical and business exchanges and in fellowships intended to match Asia's environmental problems with appropriate U.S. environmental technology and expertise

- More than 3,000 trade leads generated by US–AEP technology representatives in Asia that have been matched with more than 1,800 U.S. environmental firms in the US–AEP database

The US–AEP program has drawn considerable positive notice from U.S. industry and the Congress. This attention sparked a proposal in mid-1997, strongly supported by the Administrator, to globalize the program to other regions. Two options were developed: centralize all similar activities into one office in the Global Bureau, or encourage other regional bureaus to develop similar programs but coordinate them through an interbureau oversight team and draw on technical support from the Global Bureau. The regional bureaus reportedly favored the second option, or something like it, to maintain a regional character and identity for each program. The Administrator issued a decision in January 1998 agreeing to an approach along the lines of the second option. Regional bureaus will take primary lead, but a coordinating committee chaired and supported by the Global Bureau will provide Agencywide coordination (Atwood 1998).

Although the US–AEP program was not consciously designed as a mechanism to facilitate graduation, it clearly has that potential and has to a certain extent been playing that role. It is concentrated in graduate and near-graduate countries for logical programmatic reasons.† The lower-income countries of South Asia, such as Bangladesh and Nepal, are not yet considered to provide sufficient market potential to justify placement of a US–AEP environmental technology representative.

*A U.S. Senate move in 1997 to authorize the establishment of a US–AEP technology cooperation office in China (the so-called Baucus Amendment) was rejected by the House.

†Neither USAID nor its predecessor agencies ever administered bilateral concessional assistance programs in Hong Kong, Malaysia, or Singapore.

By contrast, as noted earlier in the section on the United States–Thailand Development Partnership, there has been a complementary match between the activities of the US–AEP and the USTDP in Thailand.

A recent US–AEP director saw the program as a critical component of a USAID graduation strategy. While expressing that program results have been extraordinary—generating rare outside praise for USAID, as well as envy from within the Agency and on the part of other donors—the director also observed that the approach is labor-intensive and that the environmental technology representatives and their small staffs play a crucial role. He acknowledged that some portion of US–AEP success has "ridden the wave of Asian economic growth" and that the current economic crisis in the region could slow US–AEP down a bit. But he also noted that the program has been unable to meet demand. He would have liked stronger and more consistent support from senior leadership in the Bureau for Asia and the Near East over the years, particularly in the direction of ensuring "seamless relationships" with Mission bilateral programs in the region, which have varied from Mission to Mission.

The US–AEP commissioned an independent panel's five-year review,* published in June 1997. Although it identified a number of "insufficiently realized" areas, the review was generally favorable to the US–AEP, concluding that it had correctly defined a critical problem and had put in place a significant and mutually beneficial means (for both Asia and the United States) for addressing it. Among several thematic issues the review explored was presence versus nonpresence (Bando 1997, 18–21). It observes that "US–AEP is working in many countries long since graduated from development assistance" and then asks: "Is it appropriate for USAID to continue development activity in those countries?"

The review clearly concludes that USAID support for US–AEP objectives and approaches in these nonpresence countries is appropriate. Justifying this conclusion, the review cites a vision for U.S. foreign policy articulated by Secretary of State Madeleine Albright when she identified four groups of countries:

> The first is the largest group, and that is what I would call those who see the advantages of a functioning international system, *who understand the rules*, who know that a rule-of-law system works, that diplomatic relations can go forward. . . . The second are the newer evolving democracies who would very much like to be part of an international system and obey the rules but who may not have all the resources, capacities, or systems yet to fully participate in it. The third group are what we have called the rogue states. The fourth group are basically the failed states. Now, a long-term goal for the United States and for other countries, in order to make our citizens prosper, is to try to get everybody into the first group, which means to see that the new democracies have the ability to participate properly. [Bando 1997, 9]

The five-year review sees in this formulation "a new goal or end game for

*The panel consisted of Amit Bando, principal investigator, and review members David Angel, Richard Blue, Kurt Fischer, George Heaton, and Lyuba Zarsky.

nation–states in the development process, one that is *no longer defined by GDP but rather by adherence to the norms of the emerging international system"* (Bando 1997, 9).

In the context of the presence versus nonpresence theme, the five-year review concludes:

> Looking back at the Albright formulation of new foreign policy approaches, Asia is not yet a full member of the new international order. Important normative differences exist between most of the Asian countries (not including Japan) and Organization for Economic Cooperation and Development countries with regard to important aspects of economic, social, governance, and ecological management. These differences constitute an important development agenda, rationalizing USAID's engagement in each of the seven nonpresence countries in Asia." [Bando 1997, 20]

In effect, the review is suggesting a new paradigm for development cooperation between the United States and other countries, a paradigm in which the conveyance of ideas and values is paramount. This also suggests a corollary new paradigm for *graduation*, measured not by GDP per capita (adjusted or unadjusted for purchasing power), infant mortality rates, and other socioeconomic indicators, but measured by *accession to full membership in the international system with a capacity to shoulder all its responsibilities as well as enjoy its benefits.*[*]

The Development Credit Authority

The fiscal year 1998 Foreign Assistance Appropriations Act provides that up to $7.5 million of development assistance, Economic Support Fund, and Support for East European Democracy (SEED) Act funds may be transferred to cover the "subsidy costs" of direct loans or loan guaranties used for any of the development purposes delineated in the Foreign Assistance Act. This authority is called the Development Credit Authority. The subsidy cost of any activity under the DCA is not expected to exceed 30 percent. Thus, grant funds transferred would leverage more than twice as much in additional loan funds from private sources. Based on experience with USAID's Housing Guaranty Program (renamed the Urban and Environmental Credit Program), an average 1:7 leverage factor for sovereign risk loans seems likely.[†]

Those in USAID (from the Global Bureau) who have been most closely involved in the development of the DCA view it as an attractive part of a country graduation strategy and package. They see it as a useful transition mechanism from highly concessional assistance. They also note that the recipient of a subsidized DCA loan does not have to be a central government. It may be a municipal government, or even a private entity provided the entity is ratable in terms of risk.

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[*] A similar approach was forcefully articulated by John Sullivan, executive director of the Center for International Private Enterprise of the U.S. Chamber of Commerce. He envisions graduation as a transition from *resource transfers* to financing the exchange of *concepts and ideas.*

[†] There is a one-in-eight chance that the country will default; therefore, $1 can be leveraged to obtain an additional $7 of resource flows.

Conclusions and Lessons Learned In USAID Graduations

There is confusion and concern in the Agency about the very term "graduation." One source of confusion is whether the term applies to cessation of USAID's *in-country presence* or the cessation of all U.S. bilateral *concessional economic assistance.* Agency staff will have more productive discussions of graduation if the term is given a single, clear definition.

Transition Strategy

1. A smooth and constructive transition from concessional assistance requires careful planning and is labor-intensive and time-consuming. Graduation decisions should be made with sufficient lead time to allow orderly planning and implementation. The recent out-is-out policy combined with budget-induced urgency has not permitted adequate time for sound graduation transition planning and implementation.

2. A clear understanding between Washington and the field regarding transition strategy, including the time frame, is essential.

3. The transition is likely to be fraught with misunderstandings and tensions when the host government is not consulted during transition planning and when it does not receive a clear message regarding the transition strategy from USAID leadership.

4. Transition planning must give attention to the institutional capacity of the private sector and nongovernmental organizations as well as public sectors.

Transition Mechanisms

Different mechanisms have been tried or at least proposed to facilitate transition. Each has its own advantages and disadvantages.

1. *Institution-to-institution linkages* on an individual basis between U.S. and recipient country institutions have probably evolved naturally as a part of USAID assistance in many cases, without this being seen as a deliberate "transition to graduation" strategy. (An example is the Korean Development Institute with the Harvard Institute for International Development.) The Revised Strategy for Economic Growth Activities in Indonesia represented a conscious attempt to establish and strengthen such linkages as part of a multiyear graduation transition strategy in the economic growth sector in Indonesia. It is useful to keep in mind the distinction between linkages developed during decades of USAID project assistance (for which most costs have already been incurred) and linkages built specifically as part of the graduation process (for which future appropriations will be required).

2. An *endowment* provides stability and continuity of funding over a number of years. However, generating a given annual level of program and administrative funds requires an endowment fund 15 to 20 times as large. Thus, in a sense endowments are expensive; they have a high opportunity cost.

> It is one thing for a USAID Mission with large local-currency trust funds that can be tapped, such as existed in Costa Rica, to set up an endowment. But Missions not already so endowed face a much tougher time.

Promoters of endowments must be realistic about the prospects of raising complementary funds from private sources.

A strong programmatic managing institution for an endowment that also has a financial stake in it would appear to contribute to the effectiveness of an endowment approach.

Similarly, a contribution by the recipient government to the endowment, as in Thailand, should augur well for ownership and effectiveness.

Although USAID Policy Determination No. 21 delineates some guidelines for Agency monitoring of endowments, a significant degree of uncertainty remains, as illustrated by the Thai case.

3. A *binational commission* has the advantage of committing high-level involvement from a range of governmental entities on both sides. One characteristic of binational commissions is that USAID's role and visibility may become relatively insignificant. However, to the extent USAID maintains a prominent role in a binational commission, staff demands could be intense.

4. A *strategic partnership,* to the extent it is part of an explicit transition strategy, has the advantage of being time-limited in nature. However, this mechanism, in which a U.S. private voluntary organization or other NGO manages a sectoral activity in a nonpresence country, has yet to be practiced. It is not clear that USAID and the U.S. private voluntary organization community, as represented by the Advisory Committee on Voluntary Foreign Aid, have resolved their mutual concerns about this approach.

One issue that cuts across transition mechanisms is the extent of continuing influence of the U.S. government on policy issues of interest. In the case of *endowed foundations*, retaining such influence requires special efforts to maintain significant U.S. presence and stature on governing bodies, such as has been ensured for the Costa Rica–USA Foundation, or an effective U.S.–linked managing institution with a clear substantive mandate and close ties to official and private Americans, such as the Kenan Institute in Thailand. However, when the mandate is far reaching and the requirements for U.S. participation minimal, as in the case of the Portugal Luso–American Development Foundation, the scope for U.S. influence becomes correspondingly smaller. Almost by definition, binational commissions retain significant U.S. influence.

This concern has led some to argue that a postpresence program, and even a postassistance mechanism such as an endowment, should be accompanied by an officer in the U.S. embassy designated as a development counselor or development attaché. This officer would serve to take up policy issues that an NGO-managed strategic partnership or endowed foundation could not (or could not as effectively).

Does "graduation" mean termination of all bilateral assistance? This is perhaps the most basic issue in determining *how* to graduate. An endowment, used as a graduation mechanism, may be viewed simply as a way of buying a *continuation* of concessional assistance *after* graduation. In this case, an endowment obscures the continuation of assistance. Under this format, there is no USAID *presence* in an endowed graduate country but the country receives (prepaid) *assistance.* The benefits of this assistance must be weighed against the opportunity cost of not assisting other countries.

These arguments have been made for continuing concessional assistance after graduation:

> The United States and the partner country have a strong mutual interest.
>
> There will be a shift from resource transfers to exchange of ideas. The corollary of this notion is that little in the way of *financing* would be required—just enough to continue to nurture the exchange of significant ideas of mutual interest.*
>
> Institutions and individuals in the graduate country could be tapped to help nongraduate ("sustainable development") countries in the *region*.

Such a relationship will allow USAID to help graduate or near-graduate countries develop assistance programs to other less developed countries. This *south–south* approach apparently is being promoted as a graduation strategy by Japanese bilateral assistance.

The Agency could restrict postgraduate relationships to a few countries where the potential for a substantial post-assistance relationship based on mutual interest is great. This implies selection of a few relatively large countries, such as Brazil, Egypt, Indonesia, Mexico, Russia, South Africa, and Thailand.

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*John Blackton has proffered this view, labeling endowments inappropriate as they tend to emphasize dollars rather than ideas. John Sullivan espouses a similar philosophy, stating that USAID should "graduate country programs from dollars to ideas and institutions." Sullivan favors the creation of "policy think tanks" in near-graduate countries.

4 ~ Conclusions

THIS SPECIAL STUDY documents that although much thinking has gone into the concept of graduation, it has not come to fruition in the form of Agency policy. Lack of a policy has had deleterious effects on when and how we graduate countries.

Though graduation would logically be the end result of all USAID's development work, actual graduation is almost uniformly resisted within the Agency. Graduation, despite its implication of laudable socioeconomic progress, carries the reality of an aid cut off. As such, it is a subject (and a decision) held closely within USAID's senior levels. The Agency appears to be working two separate and uncoordinated activities regarding graduation. One is the on-again–off-again work of USAID staff to think through issues related to advanced developing country assistance and graduation. The other is the high-pressure, budget-induced graduation decision-making that has taken place in the 1990s. Only in the Bureau for Europe and the New Independent States does one find an integration of analytical work and graduation decision-making. Sectoral graduation is also taking place in the absence of Agency policy and is subject to the same issues.

Indicators of country socioeconomic status are useful for ranking countries' need for assistance. However, though different combinations of indicators will highlight different aspects of the country profile, the rank ordering of countries as graduation candidates will not change significantly. Choosing the threshold level for graduation eligibility—whatever the indicator—is the operational decision of interest in formulating a graduation strategy.

The termination of U.S. foreign aid is always sensitive, regardless of its rationale. Efforts to manage the process by keeping it in-house as long as possible can backfire. Host governments and other institutions and organizations have a stake in the process. Early and frank discussions with stakeholders about the decision and process should be encouraged. Such an approach will clarify responsibilities and provide USAID staff with valuable information on the interests and capabilities of counterpart organizations.

A country graduation strategy should clearly specify the rationale and nature of the post-assistance relationship between USAID and the host country. It is not axiomatic that the graduation strategy include the creation of new institutions to perpetuate a USAID relationship.

The Agency has created several different types of transition mechanisms (institutions) within graduation strategies to maintain a USAID relationship with the host country. To the extent possible (given the recent creation of most of these initiatives), the advantages and disadvantages of these various mechanisms are presented in this report.

These transition mechanisms have different levels of USAID involvement and different demands on financial resources. The type of post-assistance relationship specified in the graduation strategy should guide the choice from among them.

The work initiated in the Bureau for Latin America and the Caribbean on strategies for advanced developing countries is worth resurrecting. The thinking there is congruent with a new graduation paradigm along the lines of Secretary of State Madeleine Albright's formulation. This paradigm does not rule out the traditional indicators but involves *stages* in the development cooperation relationship, in which per capita GDP and similar indicators would mark the transition to a new stage, where the transfer of ideas, technology, and expertise would predominate through a wide range of individual and organizational contacts, with a heavy, but not exclusive, emphasis on business contacts. Development cooperation in this later stage would serve a catalytic, matchmaking function, much along the lines of the United States–Asia Environmental Partnership and the United States–Thailand Development Partnership, with a corresponding emphasis on mutual benefit through trade, investment, and the exchange of ideas.

Annex

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Policies and Experiences Of Other Donors

THIS ANNEX reviews information on the policies and approaches of selected other donors with respect to how they determine *when* to conclude concessional assistance to a country and what approaches they use in addressing *how* to conclude assistance. It discusses the roles of the World Bank and the Development Assistance Committee (DAC) of the Organization for Economic Cooperation in setting standards for eligibility for concessional assistance and what countries donors may count as recipients of Official Development Assistance. Information provided through direct contacts with representatives of Canadian and Danish bilateral programs and with World Bank staff supplements this discussion. The U.S. representative to the DAC and the DAC secretariat also furnished information about policies and approaches employed by other bilateral donors. The authors believe the picture painted in this section would be essentially the same had time permitted direct contact with additional donors.

Criteria Employed For Graduation

The World Bank

The World Bank's graduation policy is of interest for two reasons. First, as the largest single source of concessional economic assistance, the implications of Bank policy for its own portfolio are noteworthy. Second, DAC follows Bank policy closely in determining which countries are on the so-called DAC list, which, in turn, has implications for determining what counts as Official Development Assistance.

With the establishment of the "soft loan" International Development Association window several decades ago, the Bank has had to set eligibility criteria for the more concessional IDA terms. From the outset, the sole criterion has been per capita GNP, expressed in

U.S. dollars. This criterion is adjusted for inflation annually. Although the Bank's board of executive directors has discussed using alternative criteria—such as purchasing-power-parity adjusted GNP per capita, or supplementary criteria such as infant mortality—each suggestion has been rejected. Board members favor the easy-to-understand Atlas GNP per capita criterion, despite its conceptual limitations. Given the political and economic implications of a change in the rules of the game, the weight of the precedent of the originally established method is heavy.

By the early 1980s, the Bank had started using a per capita GNP criterion to suggest a benchmark that would signal a country's imminent suitability for graduation from the less-concessional World Bank terms. The phrase "suggest a benchmark" is employed deliberately here. The benchmark is not a hard and fast determinant of graduation. Given the relatively low degree of concessionality of the hardest World Bank terms, one might ask why this is an issue. In addition to the fact that some concessionality is better than none, being a World Bank borrower normally entitles a country to Bank nonlending services, including analytical work, technical assistance, and training. Continued access to these services after graduation would entail the payment of a fee for them. As noted by a Bank staff member:

> Chile has been graduated de facto, although it is below the benchmark. Argentina continues to borrow, even though it's above the benchmark. The driving sentiment that always wins out is that we like above all to lend, and then we like to provide nonlending services, and we like to cease relations least.

Another consideration is the overall demand–supply relationship for World Bank funds. In the words of the same Bank staff member:

> In the 1970s and 1980s, one could argue that lending to rich countries like Argentina, Chile, and Poland would have deprived others of [World Bank] funds. Thus, graduation policy was a relevant issue. But today the demand for [World Bank] funds is much weaker in relation to supply, so graduation is no longer imperative to ration scarce resources.

These characterizations bring out an essential difference between the environment for graduation for a donor such as USAID and one such as the World Bank—namely, the difference between the relatively scarce grant resources of USAID and the less scarce, less concessional loan resources of the Bank. As it has every year for the last several decades, at the end of May 1997, the Bank designated five revised "guidelines," or thresholds, to mark the dividing lines between five operational categories of lending terms (see table 1). These dividing lines apply for the Bank fiscal year 1998, which began 1 July 1997.

From Bank fiscal year 1997, when the per capita GNP guidelines were measured in 1995 U.S. dollars, to Bank fiscal year 1998, when the guidelines were measured in 1996 U.S. dollars, two countries were moved into "Category V," World Bank Graduation: St. Kitts–Nevis and Uruguay. However, as suggested earlier, this does not necessarily imply graduation from access to World Bank lending.

Table 1. Operational Categories of Lending Terms	
Category	Bank FY98 GNP per Capita Guidelines (1996 US$)
I. Civil works preference and World Bank terms	Less than or equal to $785
II. Blend of IDA terms and 20-year World Bank terms	Less than or equal to $1,505
III. 17-year World Bank terms	$1,505 to $3,115
IV. 15-year World Bank terms	More than or equal to $3,116
V. World Bank graduation	More than $5,435

Even a country that has graduated from access to the most nonconcessional World Bank loans is still a member of the World Bank and participates in its board deliberations. It also has access to Bank research results and its promulgation of "best practices." The Bank, as noted before, has on occasion provided nonlending services to graduate countries on a fee-for-service basis. A special program for cost-reimbursable technical assistance was established after the oil shocks of the 1970s and 1980s for several "World Bank–graduated" Persian Gulf states, but this has rarely been used, especially in recent years. Chile has recently paid for some Bank "nonlending" services. In recent years, under President James Wolfensohn, "knowledge management" activities and networks have been established in the Bank, to which graduated countries as well as current borrowers are being linked.

The Development Assistance Committee

The Development Assistance Committee employs 10 quantitative criteria, the most important of which is GNP per capita in relation to World Bank categories, for helping to guide decisions regarding which countries remain in part I of the DAC List of Aid Recipients. GNP per capita is the most important because it is the only criterion for which thresholds have been established.* DAC member countries provide the vast majority of both bilateral assistance and financial support to

*The other criteria are ratio of agricultural output to gross domestic product, life expectancy at birth, gross school enrollment ratio (primary, secondary, and tertiary), female-to-male gross enrollment ratio, total fertility rate, ratio of Official Development Assistance to all resource flows to a country, ratio of bank credit to GDP, ratio of total external debt to GDP, and sovereign credit ratings on government bonds in foreign currency (or Moody's ratings). These are explained in Development Assistance Committee 1996b.

multilateral assistance institutions. These countries may count as Official Development Assistance only that aid they provide countries named on part I of the DAC list,* called "Aid to Developing Countries and Territories (Official Development Assistance)." Part II is "Aid to Countries and Territories in Transition." The per capita GNP and other criteria are guides only for discussion among DAC members. Any DAC member can delay a decision to place a country into a three-year track to graduation. One reason for this three-year holding pattern is that the DAC list is reviewed but once every three years. Even at the end of the three-year waiting period, DAC members can delay graduation of a country already in the holding pattern, but this can be done only by consensus of the DAC membership (Development Assistance Committee 1996c).

The critical categories in the DAC list are

> The *upper-middle-income countries* (as defined in GNP per capita terms by the World Bank) that also lie *above* the World Bank threshold for graduation from Bank terms. DAC calls these Schedule B, or "Development Threshold Zone Countries."
>
> Countries that still receive assistance from DAC member countries but are also *high-income countries* (as defined in GNP per capita terms by the World Bank). DAC calls these Schedule A, or "High-Income Countries."

The DAC list decision process can be illustrated by referring to the decisions taken at the 2 December 1996 DAC meeting, which was devoted to the triennial review of the DAC list. At this meeting 10 countries and 7 territories were shown to be in schedule B, that is, *upper-middle-income countries* with per capita GNPs above the 1992 eligibility threshold for World Bank loans ($4,715). DAC members agreed to place four of these "development threshold zone countries" (two countries and two territories) into the three-year graduation track. However, the objection of at least one DAC member was enough to prevent the other 13 candidates in schedule B from being elevated to the three-year track to graduation. Meeting minutes in some cases reveal reasons given by a member or members (in some cases more than one member objected to a given elevation); in other cases, no reasons are provided. In some cases, the reasons bore a relationship to the other nine DAC quantitative criteria guidelines; in other cases they did not. The stated reasons include 1) being small island states "vulnerable to external shocks and natural disasters," 2) declining per capita incomes, 3) high population growth, 4) a rising external debt ratio, and 5) a weak industrial base.

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*To be counted as Official Development Assistance the aid must also have a minimum specified degree of concessionality. The DAC list and the definition of ODA also have significance for those donor nations concerned about trying to meet the UN target that a donor country should contribute at least 0.7 percent of its GNP to ODA. Some nations, such as the United States, have neither accepted nor paid much attention to the UN target. But other nations, especially those (Canada, the Netherlands, the Nordic countries) that have approached or exceeded the target, follow it closely.

The two countries and two territories elevated by DAC in December 1996 to the three-year graduation track were the Republic of Korea, Libya, Gibraltar, and the British Virgin Islands, respectively. Those remaining in schedule B—but by at least one DAC member objection not elevated to the three-year track—include Antigua–Barbuda, Argentina, Bahrain, Barbados, Malta, Oman, Saudi Arabia, Seychelles, Aruba, French Polynesia, Montserrat, Netherlands Antilles, and New Caledonia (the first eight being countries and the last five being territories). The four three-year track countries and territories are to be graduated from part I of the DAC list into part II on 1 January 2000, unless the DAC members, at their 1999 triennial review of the DAC list, agree by consensus that an exception should be made.

The December 1996 DAC meeting agreed unanimously that three countries (Cyprus, Israel, and Taiwan) and four territories (Bermuda, Cayman Islands, Falkland Islands, and Hong Kong) in schedule A (high-income countries, according to the World Bank dividing line of a GNP per capita of $8,355 in 1992) should be graduated to part II of the DAC list as of 1 January 1997.

In sum, the DAC list graduation process is a deliberately prolonged process in which quantitative indicators, especially GNP per capita and the World Bank thresholds, play a role, but one in which there is also ample opportunity for delaying graduation beyond what the GNP per capita thresholds alone would indicate.

Other Bilateral Donors

Little information was obtained about specific graduation criteria other bilateral donors used in their own programs. A number of donors employ a country assistance allocation approach that, if followed, would suggest graduation criteria. Generally, the relatively smaller (in absolute terms) DAC donors try to concentrate their concessional assistance on anywhere from 5 to 25 "core" low-income countries. In some cases, this is more rhetorical than real. In others, donors also provide up to half their aid to a larger group of countries beyond the core countries, a policy intended to strengthen trade and investment relationships. This is sometimes provided on less concessional terms, employing mixed credits. For example, Denmark has since 1989 emphasized 20 to 25 core, or program, countries (Olsen and Udsholt 1995, 9–11). One of the criteria for selecting these countries is that their GDP per capita be less than two thirds of the World Bank limit for longer term (17-year) credits ($1,855 in 1994). The Danish bilateral assistance budget for these program countries has ranged between 55 and 65 percent of the total. The balance has been spent on a wide range of other countries, as well as on asylum seekers in Denmark. Pressures for spending outside the program countries emanate from Danish business interests arguing that their best export markets are not low-income countries in sub-Saharan Africa but rather some of the fast growing East and Southeast Asian countries. The introduction by Denmark in 1993 of a mixed credit scheme for a wider range of countries has satisfied some criticism from the business community of the "program country approach." Outside of the aid agency Danida, other Danish government bodies (including Parliament) and some nongovernmental organizations tend to see aid as flexible funds that can be used to "reward" promising development trends in individual countries. The

Canadian International Development Agency has debated the issue of graduation criteria internally for years, but actual decisions to terminate or not terminate assistance are usually made on other grounds. About five years ago a CIDA statistician undertook an analysis of various quantitative indicators that might inform graduation decisions, but this has been shelved and never used. CIDA is developing an approach to graduation for Baltic and central European countries.

'How' to Graduate: Strategies and Mechanisms

It would appear that other donors have not paid as much systematic attention to the "how" question as USAID has (or at least not as much as individual bureaus and field Missions of USAID). The Canadian International Development Agency has debated the question of how to maximize the "returns" from its development investment in a country, even after its assistance program winds down. One tangible example of an attempt to do this has been in Thailand, but the approach differed greatly from USAID's. CIDA provided initial core funding to a nongovernment think tank, the Thailand Development Research Institute. CIDA's goal was to create a self-sustaining institution that would remain visible and viable after the official bilateral program concluded. But CIDA also gave high priority to Thai ownership and influence in the new institution. Accordingly, CIDA, in contrast to the United States–Thailand Development Partnership, did not insist on visible Canadian identity in the Thai think tank.

Japan has supported "south–south cooperation" in advanced developing countries, including Singapore and Thailand. The following passage from the Ministry of Foreign Affairs *Official Development Assistance Annual Report: 1995* makes an explicit tie to graduation.

> Some developing countries are on the way of "graduation," and they are gradually stepping up to be an aid donor. "Partnership Programme" supports these developing countries' efforts. The program is aiming at increasing the number of third country training programs which are implemented in the countries concerned with the Japanese cooperation and the share of cost covered by the countries themselves. The program also includes the idea of technical cooperation through jointly dispatching experts to other developing countries.

The Know How Fund (KHF) is bankrolled by the United Kingdom's bilateral assistance program and is a mechanism for providing technical aid, training, and institutional development support for the countries of central and eastern Europe and Central Asia. To measure these countries' progress, it uses indicators similar to those used by USAID's Bureau for Europe and the New Independent States. Both KHF and the ENI Bureau use the economic transition indicators developed by the European Bank for Reconstruction and Development. However, both KHF and the World Bank see accession to the European Union as the appropriate criterion for graduation of central and eastern European countries from concessional assistance. These criteria are rigorous. They include stringent requirements with respect to price stability and internal and external debt, as well as in areas such as privatization and institutions that ensure transparency and accountability in the public sector. These are more stringent than the criteria used for graduation in USAID's ENI Bureau.

Do we see systems in other donor organizations that could serve as models? The policies and practices of other donors reviewed for this study show surprisingly little thought given to the questions of *when* or *how* to graduate. Exceptions are the DAC country list criteria and the World Bank thresholds. But these criteria are applied with great flexibility. The World Bank experience suggests that graduation may be a more important issue for institutions such as USAID, which offer a high degree of concessionality, than for those with a low degree of concessionality. The Japanese bilateral program is apparently paying some attention to helping near-graduate countries become aid donors on their own.

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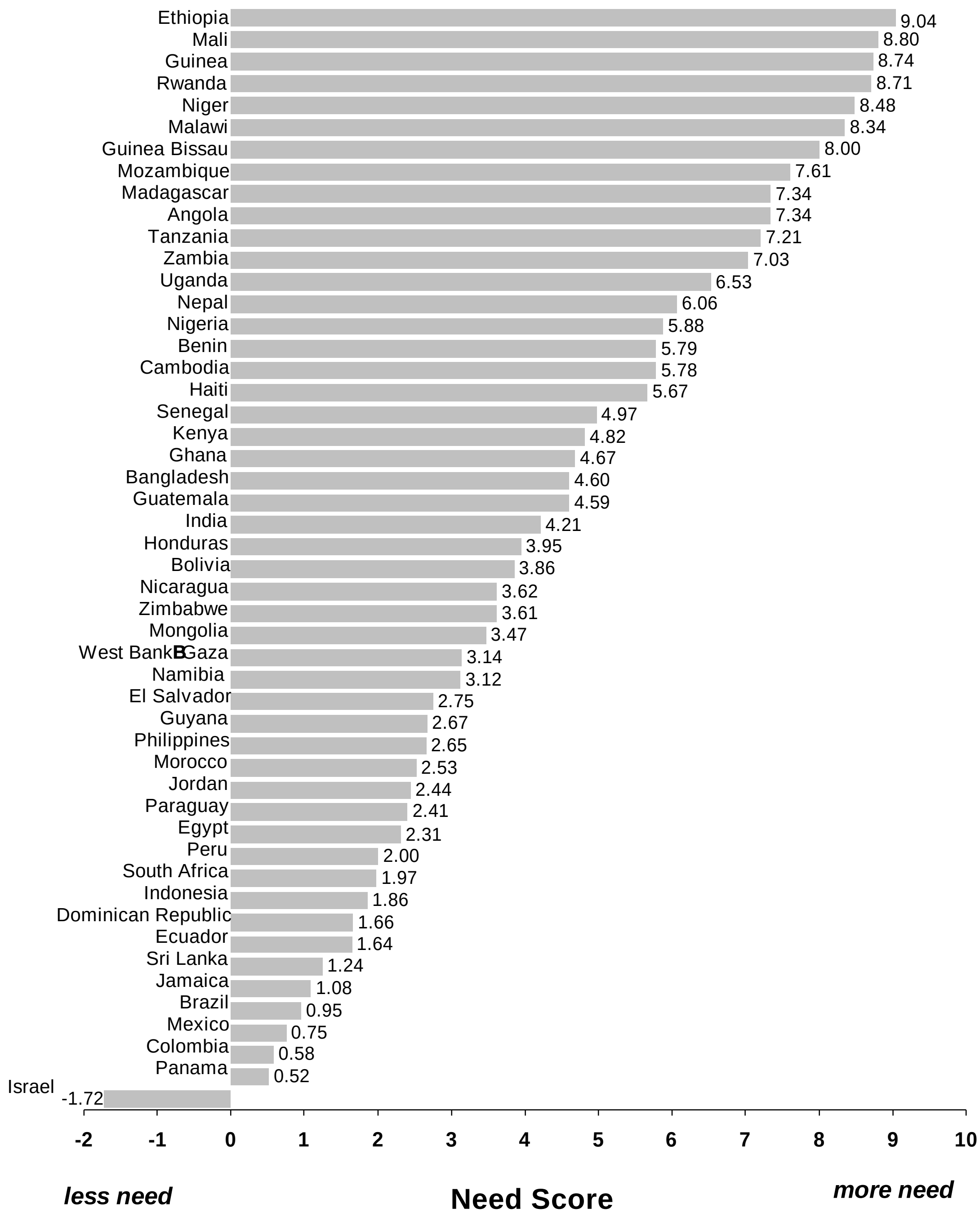
Figure 1.
Composite Need Scores

Ranked from highest to least need.1995 data.
Does not include eastern Europe and the new independent states.



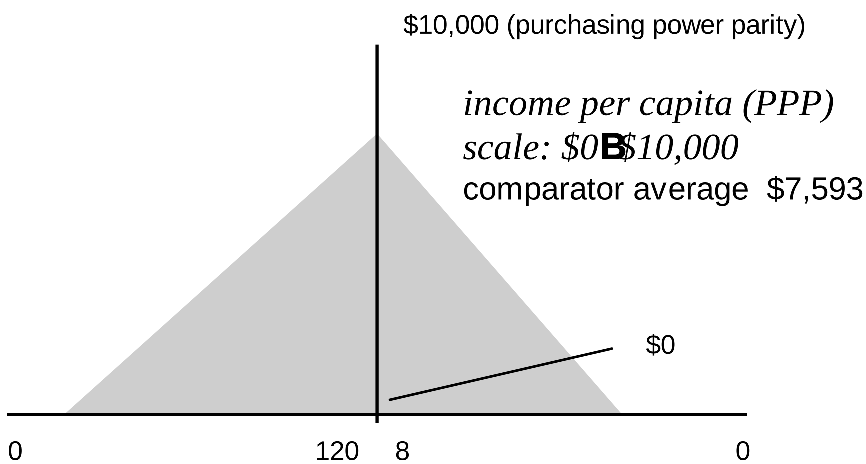
Data Sources: Don Sillers's Analysis (USAID/PPC);
World Bank's *World Development Indicators* 1997.

Graphics: USAID/PPC/CDIE/DI/ESDS.

Figure 2.
Comparator Country Averages

Chile, Colombia, Costa Rica, Malaysia, Thailand

Gray area determines comparator's average for each scale.



infant mortality
scale: 0B120 deaths
per 1,000 live births
comparator average 18.6

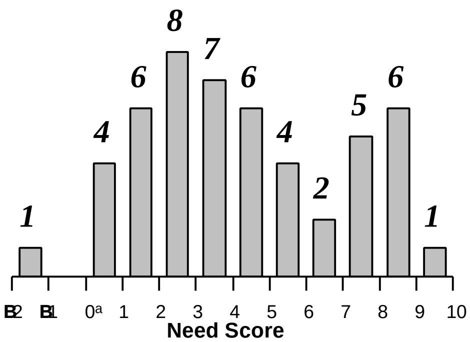
total fertility
scale: 0B8 births
per woman age 15B49
comparator average 2.7

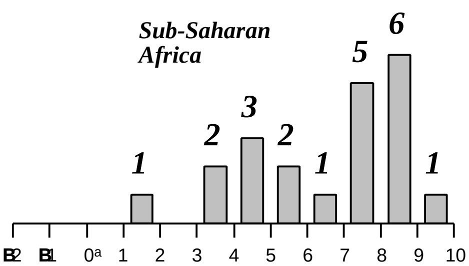
Figure 3.
Distribution of Need Scores

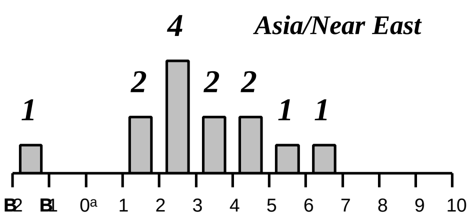
Total Need Scores, 1995 (PPP Income per Capita, Infant Mortality, and Total Fertility)

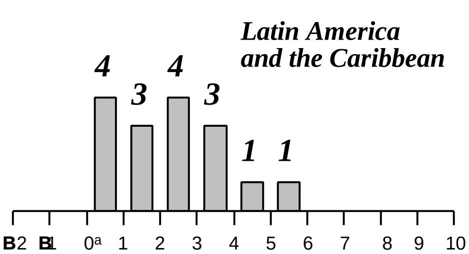
Number of countries.

All Countries (non-ENI)





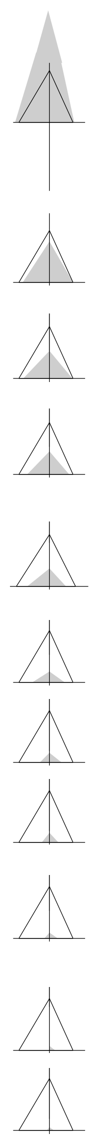




[a]Comparators (score=0): *Chile, Colombia, Costa Rica, Malaysia, Thailand*

Development Triangles

Indicator average
(see figure 2)



Country Distribution

less than B1
Israel

B1 through 0
none

0B1
Brazil, Colombia, Mexico, Panama

1B2
Dominican Republic, Ecuador, Indonesia, Jamaica, South Africa, Sri Lanka

2B3
Egypt, El Salvador, Guyana, Jordan, Morocco, Paraguay, Peru, Philippines

3B4
Bolivia, Honduras, Mongolia, Namibia , Nicaragua, West BankBGaza, Zimbabwe

4B5
Bangladesh, Ghana, Guatemala, India, Kenya, Senegal

5B6
Benin, Cambodia, Haiti, Nigeria

6B7
Nepal, Uganda

7B8
Angola, Madagascar, Mozambique, Tanzania, Zambia

8B9
Guinea, GuineaBBissau, Malawi, Mali, Niger, Rwanda

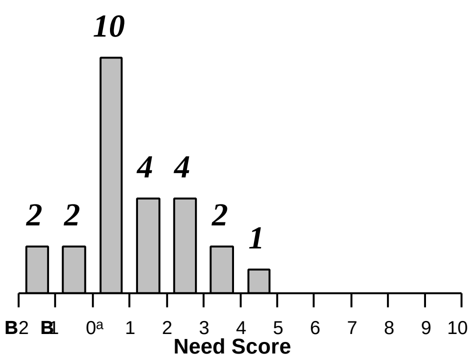
9B10
Ethiopia

Data Sources: Don Sillers's Analysis (USAID/PPC); World Bank's *World Development Indicators* 1997.

Graphics: USAID/PPC/CDIE/DI/ESDS.

Figure 4.
Distribution of Need Scores
Total Need Scores, 1995 (PPP Income per Capita, Infant Mortality, and Total Fertility)

Eastern Europe and the New Independent States
Number of countries

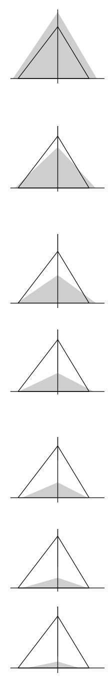


[a]Comparators (score=0): *Chile, Colombia, Costa Rica, Malaysia, Thailand*

Data Sources: Don Sillers's Analysis (USAID/PPC); World Bank's *World Development Indicators* 1997.

Graphics: USAID/PPC/CDIE/DI/ESDS.

Development Triangles
Indicator averages
(see figure 2)



Country Distribution

less than B1
Czech Republic, Slovenia

B1 through 0
Hungary, Poland

0B1
Belarus, Bulgaria, Croatia, Estonia, Latvia, Lithuania, Macedonia, Romania, Russia, Slovak Republic

1B2
Armenia, Kazakhstan, Moldova, Ukraine

2B3
Azerbaijan, Georgia, Turkmenistan, Uzbekistan

3B4
Albania, Kyrgyz Republic

4B5
Tajikistan

5B6
none

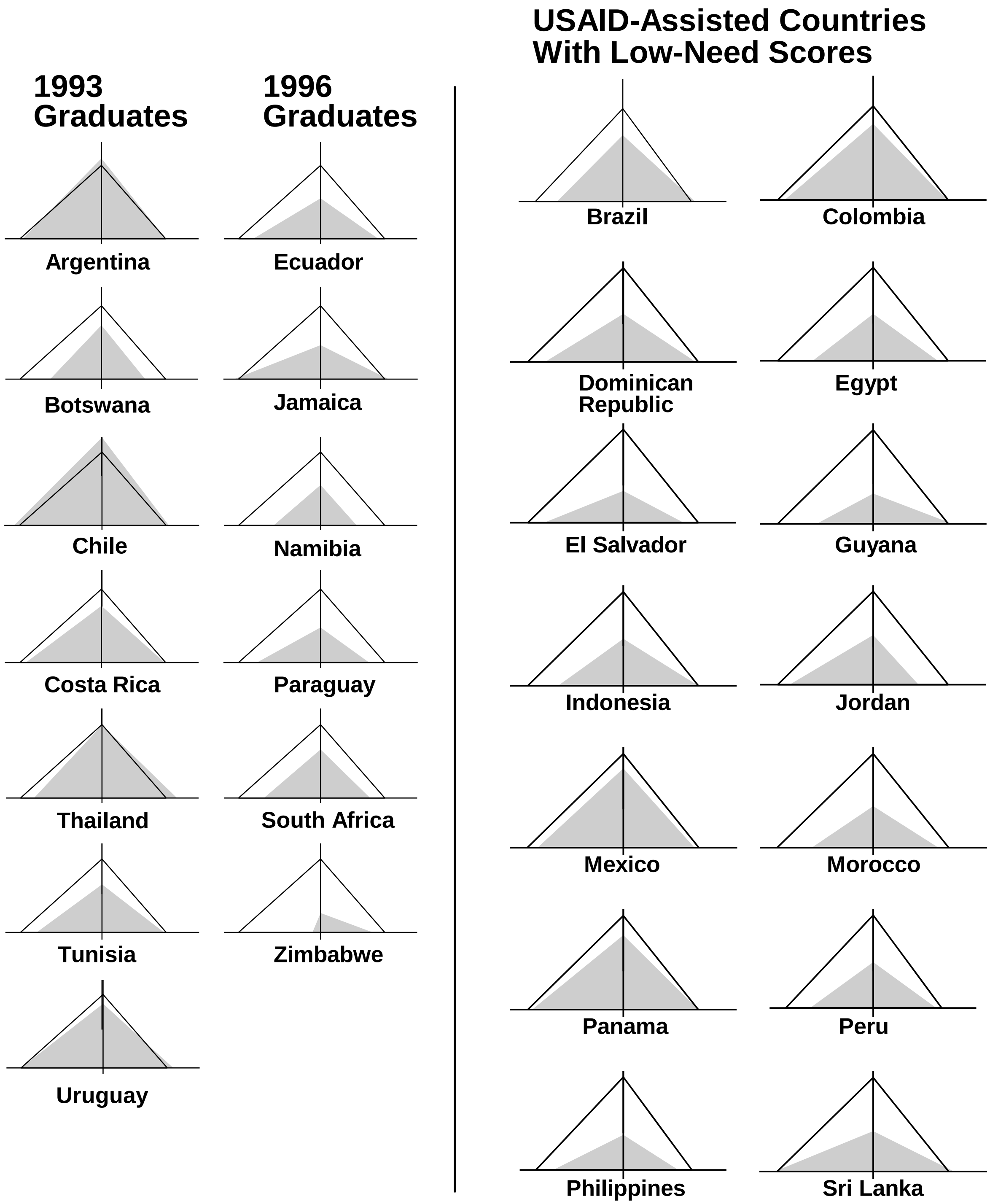
6B7
none

7B8
none

8B9
none

9B10
none

Figure 5.
Development Triangles
Selected USAID Graduates and Assisted Countries



Data Sources: Don Sillers's Analysis (USAID/PPC); World Bank's *World Development Indicators* 1997.

Graphics: USAID/PPC/CDIE/DI/ESDS.