
USAID Graduation: Sharpening the Policy on When and How to End Assistance



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Summary

WHEN A NATION receiving USAID assistance reaches certain success thresholds—measured in, for example, per capita gross domestic income, infant mortality rate, and total fertility rate—the Agency theoretically will conclude its assistance. USAID calls this graduation. But the concept is fraught with controversy. 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.

During 1997–98 a team from USAID’s Center for Development Information and Evaluation (CDIE) reviewed Agency experience with concluding concessional assistance to a country or sector when that entity is viewed as no longer needing USAID assistance; it is ready to graduate. The team posed two questions: *When is a USAID-supported country ready for graduation? And, How should the Agency structure, manage, and implement a country graduation?* It reviewed how USAID has answered those questions as manifested by its policy and operational decisions over the past decade. This Highlights summarizes the lessons that team drew from its review regarding how the Agency might better direct and manage the graduation process.

Official USAID rationale for assistance uses broad, flexible criteria based on need, global importance, for-

ign policy, and quality of commitment and partnership. Most people the study team interviewed suggested 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.

A set of clearly defined and consistently applied measures of development need would allow 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.

USAID has an institutional reluctance to end aid unless driven to it by budget difficulties. Instead, from the moment USAID enters a country, Agency and host-country officials should think about when and under what conditions assistance will end. 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. 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.

A graduation sequence could proceed as follows: A methodology is used to identify graduation candidates. Next, even before the Agency works out the process for graduating a country, USAID determines, on the basis of U.S. policy objectives, the legacy it wants to leave behind. Finally, the mission develops and implements a country-specific strategy.

USAID appears to be working two separate and uncoordinated activities regarding graduation. One is the on-again–off-again work of Agency 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.

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.

There is confusion and concern in the Agency about whether the term “graduation” 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, such as the cessation of bilateral concessional assistance.

Moreover, there is disagreement over whether “graduation” means 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. The benefits of this assistance must be weighed against the opportunity cost of not assisting other countries.

Background

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, or ADCs. The issue was first analyzed in the Bureau for Latin America and the Caribbean, which had developed a policy for such 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 ADCs argued for a more nuanced approach to phaseout and postphaseout cooperation. In the late 1980s a working group on policy toward ADCs 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; and sophisticated, responsive, stable political institutions that allow peaceful change and promote public welfare. The group’s suggestions were never adopted, but an internal discussion about graduation thresholds continued.

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 when making decisions 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 (Democracy, Education, Environment, Humanitarian Aid, Population and Health, and Economic Growth and Agricultural Development) 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.

The ‘When’ Question: Criteria and Decisions

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, foreign policy, and quality of commitment and partnership. A broad policy is understandable given the budget constraints and shifting foreign policy objectives within which USAID must operate. But most people the study team interviewed suggested 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 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 analyze 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. 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.

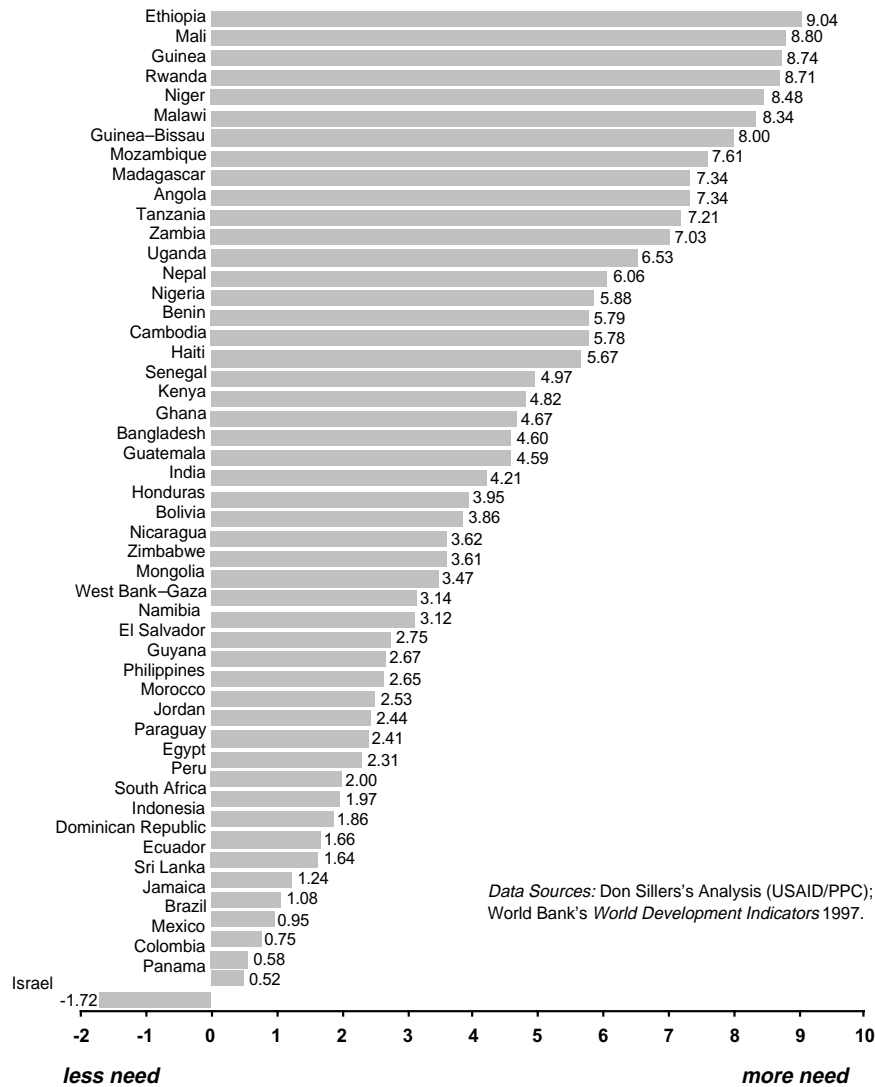
Experience in the Bureau for Eastern Europe and the New Independent States illustrates one step toward a clear, documented graduation process at the bureau level. ENI has a well-developed process and appropriate indicators, but the countries it serves have for the most part higher per capita income and more developed infrastructure and social indicators than the average USAID sustainable development country.

Most USAID bureaus have used various socioeconomic indicators as a way to identify graduation candidates. The Bureau for Program and Policy Coordination has developed an index of country need for development assistance based on three indicators: per capita gross domestic income, total fertility rate, and infant mortality rate. Values are assigned each indicator, and an overall need score is calculated (see figure, next page). The index has no formal standing in the Agency but is concise and easy to interpret.

The three indicators (income, fertility, and infant mortality) 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 improve only slowly over time. (In a crisis, though, they can worsen rapidly.) Because of the slow rate of improvement 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

Composite Need Scores

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



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

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.

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. It is desirable that mis-

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

sions and USAID/Washington prepare an exit strategy that is broad and flexible yet definitively begins transition toward terminating assistance. All actors should be apprised of critical short- and long-term goals and their own responsibilities.

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.

Currently, a great disparity exists, among regional bureaus, in standards 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. An African country that graduates is generally nowhere near as developed as a Latin American graduate. Such 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 in the community of 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.

The 'How' Question: Transition Strategies And Mechanisms

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 USAID works out the process for graduating a country, the Agency 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.

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, such as the cessation of bilateral concessional assistance.

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.
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 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. It is use-

The Portugal Luso–American Development Foundation

Some important lessons about developing foundations as a postpresence mechanism emerge from USAID’s experience with the Luso–American Development Foundation. 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.

ful 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 to set up an endowment. But missions not already so endowed face a much tougher prospect.

■ 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 should augur well for ownership and effectiveness.

3. A *binational commission* has the advantage of committing high-level involvement from a range of governmental entities on both sides. This mechanism reduces USAID’s role, visibility, and (typically) staff demands. 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.

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. 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 transfer of *resources* 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.

- An endowment will allow USAID to help graduate or near-graduate countries develop assistance programs for less developed countries.

- The Agency could restrict postgraduate relationships to a few countries where the potential for a substantial postassistance 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.

Conclusions

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 impeded the process of deciding when and how to graduate countries or sectors.

Though graduation would logically be the end result of all USAID's development work, actual graduation is almost uniformly resisted within the Agency. *We can always find more to do in countries*, goes the thinking. 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. That bureau's countries rank higher by and large on a range of socioeconomic indicators than most

developing countries throughout the rest of the world. It is better able to make aid short-term in nature and to emphasize helping countries undertake social, political, and economic transformation toward free-market-based democracies.

Indicators of country socioeconomic status are useful for ranking countries' need for *assistance*. No matter which indicators are

used and how they are weighted, the rank ordering of countries as candidates for *graduation* does 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. The Agency should encourage early and frank discussions with stakeholders about the decision and the process. Such an approach will clarify responsibilities and provide USAID staff with valuable information on the interests and capabilities of counterpart organizations.

The Agency has created several different types of transition mechanisms within graduation strategies to maintain a postassistance relationship with the host country. These mechanisms have different levels of

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USAID involvement and different demands on funds. The type of postassistance relationship specified in the graduation strategy should guide the choice from among them. The country graduation strategy should clearly specify the rationale and nature of the post-assistance relationship between USAID and the host country—even if that relationship is *no* relationship.

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 gross domestic income and similar indicators would mark the transition to a new stage. At that point, 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 with a corresponding emphasis on mutual benefit through trade, investment, and the exchange of ideas.

Lessons Learned

1. USAID staff will have more productive discussions of "graduation" if the term is given a single clear definition. There is confusion and concern in the Agency about the term, particularly over whether it refers to cessation of USAID's *in-country presence* or the cessation of all U.S. bilateral *concessional economic assistance*. Defining it as, for example, the cessation of bilateral concessional assistance would be useful.

2. From the moment the Agency enters a country, USAID and host-country officials should think about when and under what condition assistance will end.

The Agency needs clear guidelines and policy directives on when to terminate assistance.

3. Choosing a threshold level—whatever the indicator—for graduation eligibility is the operational question of interest in formulating a graduation strategy. Lack of a policy has impeded the decision-making process.

4. A set of clearly defined and consistently applied measures of development 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 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 postassistance relationship between USAID and the host country. Transition mechanisms have different levels of Agency involvement and different financial demands. The choice from among them should be guided by the type of postassistance 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 that have a stake should be included. USAID should encourage early and frank discussions with these other stakeholders.

7. 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.

This Highlights, by Michael Hopps of Conwal Incorporated, summarizes the findings of USAID Graduation: Recent Experience and Outstanding Issues, by Frank D. Martin, John Eriksson, and Stephanie McNulty, Center for Development Information and Evaluation, USAID Evaluation Special Study No. 81. This report and the individual country Impact Evaluations can be ordered from USAID's Development Information Services Clearinghouse, 1611 North Kent Street, Suite 200, Arlington, VA 22209; telephone (703) 351-4006; fax (703) 351-4039; e-mail docorder@dec.cdie.org. To access from the Internet, key in www.info.usaid.gov. Click on Publications/Partner Resources, then on USAID Evaluation Publications.
