



CONGRESSIONAL NOTIFICATION TRANSMITTAL SHEET

We wish to inform you that the Millennium Challenge Corporation intends to provide assistance to the Government of Timor-Leste to facilitate the development and implementation of a Millennium Challenge Compact.

If you or your staff would like to arrange a meeting to discuss the planned assistance, please contact Jennifer Belair at (202) 521-3880.

The attached notification is being sent to the Congress on February 8, 2019. The assistance may be provided and funds obligated on or after 15 days from the date of this notification.

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

Sincerely,

/s/

Karen Sessions
Vice President
Congressional and Public Affairs

Enclosure: As stated

**MILLENNIUM CHALLENGE CORPORATION
CONGRESSIONAL NOTIFICATION**

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| PROGRAM: | Eligible Countries |
| APPROPRIATIONS CATEGORY: | Fiscal 2019 Program Funds |
| OBLIGATION AMOUNT: | \$7,380,000 |

Pursuant to section 7015(c) of the Department of State, Foreign Operations, and Related Programs Appropriations Act, 2018, as carried forward by the Continuing Appropriations Act, 2019, as amended, and section 610(a) of the Millennium Challenge Act of 2003, as amended (the "Act"), this is to advise that the Millennium Challenge Corporation ("MCC") intends to obligate up to \$7,380,000 to provide assistance under section 609(g) of the Act to the Government of Timor-Leste for the purpose of facilitating the development and implementation of a Millennium Challenge Compact with MCC.

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

SUPPLEMENTAL INFORMATION - MCC 609(G) ACTIVITIES FOR TIMOR-LESTE

Background

Timor-Leste is the world's second youngest democracy, occupying the eastern half of the island of Timor at the end of the Indonesian archipelago. It is home to a population of 1.3 million comprised primarily of Malayo-Polynesian and Papuan communities.

In 2002, Timor-Leste voted for independence from Indonesia in a referendum that had substantial support from the United States and the international community. When the Indonesian military pulled out, nearly all public infrastructure—including health clinics, schools, roads, ports and airports, water and sanitation systems, and government facilities—was destroyed. As the country emerged from its violent, twenty-year struggle for independence, the Timorese faced enormous development needs as they began to build their country. There were severe shortages of human capital and exceptionally weak governing institutions. Few Timorese had access to formal education and an even smaller number had any government experience. Extreme poverty and hunger were widespread, and conflict and violence consistently threatened to break out, creating a culture of instability.

Today, Timor-Leste has a democratically-elected government that is committed to economic development. Since independence, the country's economy has been shaped by the discovery of oil. Timor-Leste's sovereign oil-wealth fund grew to nearly \$10 billion within a decade, which the country used to rebuild the electric grid and expand access to basic infrastructure like roads, showing the government's commitment to development and reform. Health indicators have also improved significantly due to improvements in access to health facilities. While Timor-Leste has made important strides in human development, private investment has remained flat and growth of the non-oil sector has been stagnant since 2011. The legal and regulatory framework necessary to enable business development and growth is also extremely nascent. Going forward, private sector-led growth that is enabled, but not driven, by the government will be critical for sustaining Timor-Leste's social and economic progress.

Timor-Leste currently faces a historic moment of political uncertainty and transition. Over the last two years the country has experienced three national-level elections. For the first time in Timor-Leste's history, the President dissolved Parliament and called early elections in February 2018. In May 2018, a new, fragile, governing coalition emerged victorious. At this moment of democratic maturation, the Timorese have remained peaceful in the face of this uncertainty.

Compact Eligibility and Constraints Analysis

Following the MCC Board's selection of Timor-Leste to develop a compact in December 2017, the country has shown continued strong performance on the MCC scorecard, passing 14 out of 20 scorecard indicators for fiscal year 2019. In particular, the country has shown significant improvement in scores on political rights, civil liberties, and control of corruption. Timor-Leste has shown strong resolve and commitment to an inclusive and transparent development process to identify investments that will drive poverty reduction through economic growth. In 2016, the government committed staff and resources to conduct the constraints analysis to identify the key factors inhibiting economic growth. That analysis identified four primary constraints: (a) uncompetitive real exchange rate (Dutch disease); (b) ineffective public financial management;

(c) a weak business enabling environment; and (d) low human capital attributed to poor nutrition outcomes and lack of skilled workers.

In October 2018, MCC and the Government of Timor-Leste held a root cause analysis workshop to discuss key challenges to economic growth. In November 2018, the Government of Timor-Leste submitted two concept notes for MCC's consideration that prioritized addressing the core problems of child stunting and a lack of skilled workers underlying the human capital constraint, while recognizing the importance of improving the business environment for investments in a more skilled, healthier workforce to generate significant and sustainable economic returns for the country. MCC will work with the Government of Timor-Leste to develop project proposals advancing this strategic approach. MCC currently projects that the MCC Board of Directors will consider a fully-developed compact program for Timor-Leste in fiscal year 2020.

Summary of Proposed Project Interventions

Potential compact projects may focus on the following core objectives:

- **Reduce the prevalence of stunting.** Potential activities include (a) community-based programming to improve nutrition practices and behaviors; (b) water and sanitation infrastructure, operations, and maintenance; (c) capacity and skills development for service delivery; (d) increasing women's empowerment and economic opportunities; and (e) building capacity and improving policymaking in relevant institutions.
- **Improve the skills of the Timor-Leste labor force to support private-sector led growth.** Potential activities include (a) training new and in-service secondary school teachers in revised curricula; (b) developing a functioning labor assessment system to target education investment to in-demand skills; and (c) testing and incorporating new materials and approaches into formal and continuing education.
- **Reduce the riskiness of business transactions by building the foundation of the commercial legal environment.** Potential activities include (a) developing channels for commercial dispute resolution and enforcement of decisions; (b) enacting required legislation or regulations governing business contracts and their enforcement; and (c) building the relevant skills of agencies and firms engaged in commercial contracts and dispute resolution.

Assistance to Develop the Compact Proposal

In order to assist Timor-Leste to further develop the proposed compact, MCC intends to fund preparatory activities for each of the potential projects listed above. Specifically, funds would be used for integrated feasibility studies, private sector analysis, environmental and social planning and assessment documents, and labor market analysis that MCC will need to conduct before compact approval. Funding these activities reflects MCC's commitment to preparing projects in a comprehensive manner, prior to compact signing, to reduce implementation risk and increase confidence in the economic justification and technical feasibility of the proposed projects.

Update and Sustainability of the Timor-Leste's Threshold Program

In September 2010, MCC's Board of Directors approved Timor-Leste's proposal for a \$10,496,000 threshold program. The Timor-Leste threshold program was funded by MCC with implementation supervision provided through the United States Agency for International Development (USAID). The program worked to tackle corruption through an integrated approach involving a number of key institutions and actors and improved access to immunization services through the creation of a more effective community health system. The program began on February 1, 2011, and concluded on March 31, 2014.

The Fostering Transparency Initiative (FOTI) accounted for \$6,961,340 of the total threshold program budget. The program worked to reduce corruption and emphasized building human and institutional capacity. FOTI assistance delivered a broad suite of activities to build corruption-fighting capacity that included coaching and mentoring to enhance the government's capacity to investigate corruption crimes. The components were also effective in increasing the audit capacity of staff in the Office of Inspector General and developing principles of procurement and trainings on public procurement that were rolled out nationwide. The program resulted in legislative victories, including amendments to the country's law for preventing and combating money laundering and the financing of terrorism, and passage of a law creating a Financial Intelligence Unit, which was established in September 2014. These measures were unanimously approved by Parliament.

Timor-Leste's immunization coverage was among the lowest in Asia. The capital city Dili had even lower coverage (43.4 percent) than the national urban average. Administrative and official immunization coverage rates in infants were among the lowest in the Southeast Asia region. The Imunizasaun Proteje Labarik (Immunization Protects Children or IPL) program assisted the Ministry of Health in improving immunization coverage and strengthening routine immunization services. The program provided support, facilitation and funding for the Ministry of Health to conduct micro-planning sessions at the 35 community health centers in its seven focus districts (covering approximately two-thirds of the national population). IPL raised the national average of DTP3 and measles vaccination in infants from 67.5 percent to 81.5 percent in those districts. The program's tools and approaches were viewed positively at all levels with beneficiaries who were directly involved in the intervention at subdistrict and village levels being most appreciative of the collaborative approach of the program.