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Statement Before the

Senate Committee on Foreign Relations

"Modernizing Development Finance"

A Testimony by:

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Introduction

Chairman Corker, Ranking Member Menendez, and distinguished members of the committee, thank you for asking me to testify before you today. It is a privilege and an honor.

I want to recognize the incredible work of dozens of staffers on this committee, HFAC, a number of key congressional offices, the team at OPIC, and at the White House who have made this all possible. I also want to single out Senator Coons and his team for their leadership on this important issue.

Currently, I hold an endowed chair at the Center for Strategic and International Studies (CSIS), researching how we might use American soft power and influence around the world. I served in the Bush Administration at USAID and worked for a time at the World Bank Group after starting my career in investment and commercial banking. I have been working and writing on the issue of development finance for more than 15 years.

I am submitting a series of my reports and articles published by CSIS, *Forbes*, and *Foreign Policy*—for the record. Let me make several key points with my time today.

Evolved Development Finance and the BUILD Act

My message is: this Committee and Congress should approve the BUILD Act for four reasons:

1) The world has changed. The developing world needs more American investment and more private investment generally.

2) China is currently filling the void created by a lack of funds. A new Development Finance Corporation (DFC) can be part of the answer but it cannot be the full response of the United States to the China challenge. Frankly, China is eating our lunch around the world, especially in Southeast Asia, Africa, and Latin America. China offers quick financing and no questions asked infrastructure projects in these places. We cannot change China's policy, but we can have a better offer than China. This new DFC is part of that better offer.

3) Foreign assistance is still a necessary component of U.S. development, but ODA and aid will not be enough, or the right type of funds. Confronting poverty requires more investment capital. The Addis Ababa Financing for Development Conference of 2015 saw foreign assistance as a "catalyst" and put a greater emphasis on other forms of financing including private financing. The phrase that was adopted was "from billions (in foreign assistance) to trillions (in the form of private investment, taxes collected, local private savings, etc.)." The challenges we face are going to be bigger than the billions that we can mobilize through foreign aid. We need to move from billions to trillions. For example, in 2016, total global ODA amounted to $142.6 billion.[1] However, meeting

[1] http://www.oecd.org/dac/development-aid-rises-again-in-2016-but-flows-to-poorest-countries-dip.htm

infrastructure investment needs in Asia alone will equal $1.7 trillion over the next 25 years.[2]

4) The new DFC can help with a series of national security and foreign policy challenges better than the current set of development finance instruments that the United States has at its disposal. Someone once said, "the best social program is a job." Illicit drugs, refugees, drug financed gangs, terrorists, and human trafficking all can be partially addressed with projects by this new DFC. We have a youth bulge in places such as Africa, the Middle East, and the Northern Triangle of Central America, where a possible demographic dividend could be harmed by lacking economic growth. These young people could be customers for American goods and services or they could be sources of danger for us and our allies. The key differentiator is meaningful work. In places such as Afghanistan, getting power, growing licit crops, and starting new companies are directly linked to the security of our troops. In many post-conflict situations, having alternatives to being a soldier or a member of a militia is dependent on real economic alternatives.

The Overseas Private Investment Corporation (OPIC) is a powerful development finance agency, but one that operates with outdated instruments and authorities. OPIC is in need of a refresh to allow it to fully compete in today's world. Our allies, such as Japan and the UK, have DFIs and want to work with OPIC but given OPIC's limitations it can be difficult to work in a coordinated way with OPIC. The current Senate version of the BUILD Act provides several important improvements to OPIC, allowing the new DFC:

1) To make equity investments,
2) To provide technical assistance,
3) Increases the ability to take smart risk using local currency loans, first loss guarantees, and provision of small grants,
4) Raises the spending cap on the DFC's investments to $60 billion, more than doubling OPIC's current $29 billion funding cap.
5) Provides a 20-year authorization,
6) and creates a preference for American investors, rather than a requirement. This is important in contexts such as Afghanistan where we need American soft power but where it is almost impossible to get credible American investors to go due to security or the absence of legal and regulatory frameworks.

I am encouraged to see that the BUILD Act includes a strong preference for the new DFC to work in lower-income and lower-middle income countries. There will be times where the new DFC should make investments in poorer parts of wealthier emerging markets, but the emphasis should be on poorer, more conflict affected countries.

I was also encouraged by the inclusion of the potential for future enterprise funds which are an underutilized tool of the United States, and a complement to the new Development Finance Corporation. The United States should update enterprise funds to the 21st century and we should

[2] https://www.forbes.com/sites/danielrunde/2017/04/05/we-shouldnt-be-eliminating-opic-we-should-be-putting-it-on-steroids/#1cdcf0173156

use enterprise funds much more often. A future round of enterprise funds should be considered as an important supplement to the new DFC.

Recommendations

Having said all of this, this bill could benefit from some small improvements that can happen in the normal markup process.

My suggestions for improvement are related to more explicit institutional linkages, or "jointness" between USAID and the new Development Finance Corporation. Legislation should require regular secondments/rotations among USAID, MCC, the new DFC and perhaps other agencies. When USAID reaches for finance tools, they should understand the breadth of what the new DFC can do. When the new DFC is thinking about an investment that might lead to reform of a sector like the telecoms, the DFC needs to understand what USAID can do.

The Congress should make explicit that it expects USAID to continue to work on "private sector development" –a central part of USAID's bread and butter work. USAID's relationships, expertise and long-term engagement in a country make it uniquely positioned to create the investment environment which enables DFC success. USAID will need to continue to work with and support the private sector, in partnership with host country regulators, across an industry, through chambers of commerce, or with particular companies. For example, the massive investments by DFIs in the telecoms sector in Africa and Afghanistan required changes in the rules about how many cell phone companies could operate and under what rules of the game. These changes to the rules of the game were often done by agencies such as USAID or the World Bank Group. USAID has done much of the work to "set the table" to enable investments by DFIs such as OPIC. USAID will need to continue to be able to "set the table" in a wide number of ways for future DFC investments.

Here are some specific additional improvements for your consideration:

First, when it comes to the Development Credit Authority, "If it ain't broke, don't fix it." The Development Credit Authority has been tremendously successful as a part of USAID. It ought to remain at USAID. If that is not politically possible, the person who runs the DCA office and its function needs to know USAID. The best way to ensure this would be to make the new office director dualhatted as a USAID and DFC employee, and by making the office director role a regular USAID foreign service slot.

Second, the position of the Chief Development Officer at the DFC should also be "dualhatted" accountable to USAID and the new DFC. The Chief Development Officer should also be a regular rotation slot for the USAID foreign service.

Third, I think the new DFC is going to need a small cadre of full time investment officers overseas. These investment officers should be embedded in USAID missions and should work as part of the USAID mission team.

Fourth, I would also urge the Committee to give the new DFC the capacities to support *early stage* investments, many entrepreneurs cannot get access to this type of investment which requires higher risk tolerance and more patience.

Conclusions

This is not your grandparents' developing world—it is richer, freer, and has far more agency than it did 40 years ago. If we do not meet the hopes and aspirations of our friends and allies, they will take their business to the Chinese. At the same time, a number of our national security challenges require private sector solutions as part of our response. Rather than look at many developing countries as simply recipients of aid, we must look at them as emerging or even emerged partners who desire a deeper relationship built around trade, investment, and economic growth. We should not let this moment pass. With some small tweaks, the BUILD Act, when passed, will be the most important piece of international development legislation in more than a decade.

Thank you for the opportunity to testify before the Committee on this important topic, I look forward to your questions.