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A REPORT TO THE
POLITICAL STATUS COMMITTEE
CONGRESS OF MICRONESIA
ON
THE GENERAL ECONOMY AND
MINIMUM FINANCIAL REQUIREMENTS
TO SUSTAIN THE GOVERNMENT
UNDER VARIOUS POLITICAL SITUATIONS
AND STATUS

BY
WILLIAM H. STEWART
JULY, 1971

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I GENERAL ECONOMY

COMPILED BY WILLIAM H. STEWART

This text is to be used in conjunction with the Statistical Atlas of Economic Indicators of the Trust Territory of the Pacific Islands.

TRADE CHARACTERISTICS

Imports

The future balance of international payments should be of major concern to those who seek a more permanent political status than the Trust Territory. At the present time, Micronesia's import purchases requiring hard currency far exceed the area's export earnings. This potential balance of payments problem can be examined on the charts entitled, "Value of Imports and Exports" found on page 4 of the recently published Statistical Atlas of the Trust Territory. The excess of imports over exports in 1970 can be studied on the following table.

TABLE 1

1970 TOTAL PRIVATE (NON-GOVERNMENT) IMPORTS VS. EXPORTS

District	Imports	Exports	Payments Deficit	Ratio
Marianas	\$5,290,223	\$ 254,635	\$5,035,588	21 to 1
Yap	871,749	163,341	708,408	5 to 1
Palau	2,193,366	1,157,709	1,035,657	2 to 1
Truk	4,778,571	655,444	4,123,127	7 to 1
Ponape	2,156,209	623,621	1,532,588	3 to 1
Marshalls	5,630,200	1,321,253	4,308,947	4 to 1
Total TT (Minus Marianas)	\$15,630,095	\$3,921,368	\$11,708,727	4 to 1

The above figures do not include government purchases of supplies and equipment.

As can readily be seen, the economy is depending increasingly on imports. During 1970, for example, imported canned fish accounted for 13.7% of Micronesia's imported food bill; rice and sugar, both items which could be produced in the Trust Territory, accounted for 20.4% and 8.3% respectively, of the total food imports. These three items required hard currency in the amount of \$2.9 million to purchase 42.4% of all imported food which could be grown or caught easily in Micronesia. Beverage imports accounted for another \$4.0 million representing 36.5% of total food and beverage imports (milk, soft drinks, beer, etc.).

The total value of imported goods (not including services) by the private sector in 1970 was \$21.0 million of which about half (\$9.1 million) consisted of items of necessity, i.e., petroleum, oil and lubricants, building materials, boat parts, machinery and miscellaneous items (all other).

These goods were purchased largely as a result of the total Trust Territory Government payroll which in 1971 was \$20.6 million of which \$13.3 million was paid to approximately 6,400 Micronesian Government employees and the remaining \$7.3 million paid to 257 U.S. Civil Service and 410 contract employees. While no information is presently available as to the total number of Micronesians employed in the private sector, nor of total wages paid, it has been estimated that approximately 6,000 to 7,000 people (both Micronesians and non-Micronesians) were on private payrolls in FY 1970 earning wages totaling approximately \$6.8 million.

In terms of average imports per Micronesian employee, the following table indicates the expenditures on selected private sector imports:

TABLE 2
TOTAL ANNUAL IMPORT EXPENDITURES - FY 1970

Item	Total Import Value (Dollars)	Average Imports (1)	
		per Micronesian Wage Earner (Approx. Dollars)	Average Import Per Capita (Dollars)
Food	6,987,786	562	68
P.O.L.	3,214,388	258	31
Tobacco	937,691	75	9
Clothing-Textiles	1,550,651	124	15
Building Materials	2,312,256	186	23
Boat Parts	321,679	26	3
Machinery	1,582,696	127	15
Alcohol	1,066,788	86	10
Milk and Other Bev.	1,263,241	102	12
Misc. Imports	1,683,142	135	16
TOTAL	20,920,318	1,682	205

(1) Based on 12,436 employees of which 3,045 are in the Marianas.
(2) Based on population of 102,250.

The above figures are a bit misleading because not all items are consumed exclusively by Micronesians, nor do the figures indicate Trust Territory Government imports required to provide the necessary governmental services for area residents, i.e., fuel for electric generators, radar sets for ships, etc. Also, even though the government does import goods duty free (and thus not shown in the totals), it does purchase goods on the local market; for example, boat parts, machinery, etc., with the result that the per capita consumption figures may be a little high. However, in the absence of more reliable data, the above figures will have to suffice as estimates.

With the exception of trade goods valued at \$1.7 million⁽¹⁾ purchased by the population located on the outer islands, most of the imported goods are purchased in the district centers for some 36,443⁽²⁾ Micronesians plus 4,700 non-Micronesians⁽³⁾. Thus, it might be said that approximately \$19.2 million of privately imported goods are purchased for some 42,713 people and when sold represent an average annual per capita expenditure of \$450 per person. Unfortunately, the available statistics do not permit allocating the above consumption expenditure on a district basis other than by simple multiplication of the dollar figure by the district center Micronesian population. Table 3 depicts this calculation.

(1) Earnings on copra production on outer islands. \$110 per ton x 15,600 tons = \$1.7 million.

(2) Ebeye - Kwajalein population included = 4,500.

(3) Estimated to include 1,021 alien workers plus 550 non-Micronesian government workers x average 3 people per family = 4,713.

TABLE 3

ESTIMATE OF MICRONESIAN EXPENDITURES FOR THE PURCHASE OF PRIVATELY
IMPORTED GOODS (BY DISTRICT CENTER - FY 1970)

District Center	Population	Average Value Imports Per Person	Total Value Imported Goods Purchased by District Center Population (Mic
Saipan	10,034	\$450	\$4.5 million
Colonia (Yap)	593	450	0.3 "
Koror	6,270	450	2.8 "
Moen	5,056	450	2.3 "
Kolonia (Ponape)	2,825	450	1.3 "
Majuro	7,165	450	3.2 "
Ebeye (Not. Dist. Center)	4,500	450	2.0 "
TOTAL	36,443	--	\$16.4 million

Exports

The greater Micronesia's export earnings, the smaller will be its dependence on external grants-in-aid to purchase imports for consumption.

A review of the chart on page 4 of the Statistical Atlas will reveal that the imbalances in imports versus exports for each district varies considerably.

In the opinion of Professor Elbert V. Bowden,

"The standards of living and levels of services which have already been obtained represent only a halfway position in advancing toward the consumption levels which the youthful and educated political and business leaders of Micronesia have come to know and understand. They plan to continue to seek more improvement and involvement of more of their people in the modern, money economy. But the opportunities for development are not encouraging.

"There are a number of specific, local possibilities for economic development. Almost all of these possibilities involve the inflow of outside capital. Some offer opportunities for profitable businesses, but none are sufficiently large and promising enough to offer economic viability to Micronesia over the next two decades.

"After all the alternatives are surveyed, it becomes clear that there is no way that the local economy can become sufficiently productive to support the levels of consumption, infrastructure,

and government services which the people now know and demand. Large flows of goods into Micronesia from the outside without any return flow from Micronesia in exchange will continue to be essential over the foreseeable future. Given the realities regarding land ownership and private capital restrictions, existing living standards and standards of public services cannot be maintained.....certainly not expanded to meet the growing needs.....without continued grants from outside.

"With the living standards which Micronesians now know and require, economic viability for Micronesia is not possible in the foreseeable future. The United States has introduced and is teaching U.S. standards and values, and is moving toward establishing U.S. wage scales and other characteristics of the U.S. economy. The only realistic alternative to the shock of serious and painful depression in Micronesia is to continue the flow of unilateral transfers to support the government services, the labor force, and the economy.

"The history of external economic controls and supports in Micronesia throughout the past several decades and especially within the past few years, has resulted in the development of a unique kind of economically dependent society. Levels of consumption and services have been permitted to escape from the usual restraining influence of basic productivity. The old ways of getting along on what nature provides are a thing of the past;

yet the productivity necessary to support the new ways has not yet been developed. It will not be developed in the foreseeable future."(1)

The sector analysis on page 17 discusses Micronesia's potential export earnings and its ability to undertake an import substitution program.

(1) Source: "The Theory and Practice of Economic Development Planning in the Scattered Tropical Islands of Micronesia" by Elbert V. Bowden, August 27, 1969.

LABOR FORCE

"Micronesia's labor force is defined as that part of the population between the ages of 15 through 64 living in commercial and administrative centers, excluding students and a percentage of women. Using this definition, there were only 15,800 Micronesians available for the labor force in 1969. Because of Micronesia's geographic dispersion, cultural traits and the youth of its population, only about one-half of its inhabitants fall into the labor force because of age. After students, a small percentage of handicapped, disabled or migrants and a larger percentage of women are deducted, only 31,200 remain. Of these, approximately one-half live on the outer islands in the subsistence economy and are considered a secondary labor force. There was in 1969 an estimated immediate full-time labor force of approximately 15,800 individuals, 9,700 or 60% male. By 1976, the same process leaves us with a potential labor force of 35,000; 20,700 in the district centers and an additional secondary force of 14,400 in the outer islands."⁽¹⁾

Approximately 1,166 aliens entered the Trust Territory during FY 1969; 1,021 in FY 1970 and 1,332 in FY 1971. (This does not include Trust Territory Government employees, Peace Corps volunteers and other U.S. Government employees.) The majority were skilled construction workers. A breakdown follows of the alien labor entries.

(1) Source: Income-Employment in Micronesia -- June 18, 1970.

TABLE 4

GAIKEN WORKERS IN TEST TERRITORY BY INDUSTRY (JUNE 30, 1971)

Construction workers	611
Fisheries	380
Domestic	16
Cooks	16
Chefs	7
Barbers	7
Hostesses	2
Bakes	4
Survivors	15
Architects	11
Engineers	40
Teachers	15
Accountants	29
Waiter/Waitresses	12
Farmers	8
Seamstresses	3
Barenders	6
Musicians	2
Beautician	1
Other	<u>147</u>
TOTAL	1,332

WAGES

Total wages earned by Trust Territory Government employees represent at least 75%, if not more, of the total wages earned in Micronesia, the remaining wages being earned by individuals in the private sector.

"The wages paid to indigenous government employees, although somewhat below the wages paid to U.S. and other expatriate employees, are very high as compared with wage levels throughout the Far East and most of the world. The annual wage for labor, clerical, protective and domestic employees of the Trust Territory Government ranges from \$1,300 to \$2,700. For senior, professional and executive employees, the wage range is from \$3,800 to \$20,000. Most of the Government's 6,400⁽¹⁾ Micronesian employees are in the \$2,000 to \$3,000 wage bracket. These amounts are high by Asian standards, but are low when these wage earners are living by American standards.

"Virtually the only kinds of economic activities which can compete for local labor, given the government scale, are businesses which serve the recipients of these relatively high wages. The trade and service enterprises and a few businesses producing agricultural and fisheries products for local sale can enjoy prices high enough to support wages comparable to the Government scale.

(1) This figure is based on a 1970 analysis....the current pay plan when implemented will increase this average substantially.

"There is no realistic plan which could result in sufficient productivity development in Micronesia to support desired standards any time during this century. Through careful planning, proper direction, and efficient administration, economic viability may be developed in Micronesia over the very long range. But for the next two or three decades, the state of the Micronesian economy will be determined more by the size and pattern of the unilateral inflow of dollars and goods than by any other factor or group of factors."⁽¹⁾

(1) Source: "Development Economics for Micronesia," by Elbert V. Bowden, August 27, 1969.

EXISTING REVENUES

The combined revenues of the Trust Territory Administration (grants from the U.S. Congress) total approximately \$59.7 million. Other U.S. Government funding, i.e., wage payment of the Kwajalein military facility, the U.S. Coast Guard, Post Office, OEO, together with Micronesian government revenues add an additional \$14 million for a total of about \$74 million.

The graph entitled "1971 Trust Territory Government Allocations for the Total Budget of \$59.7 Million," depicts almost half the government budget being spent on wages and salaries.

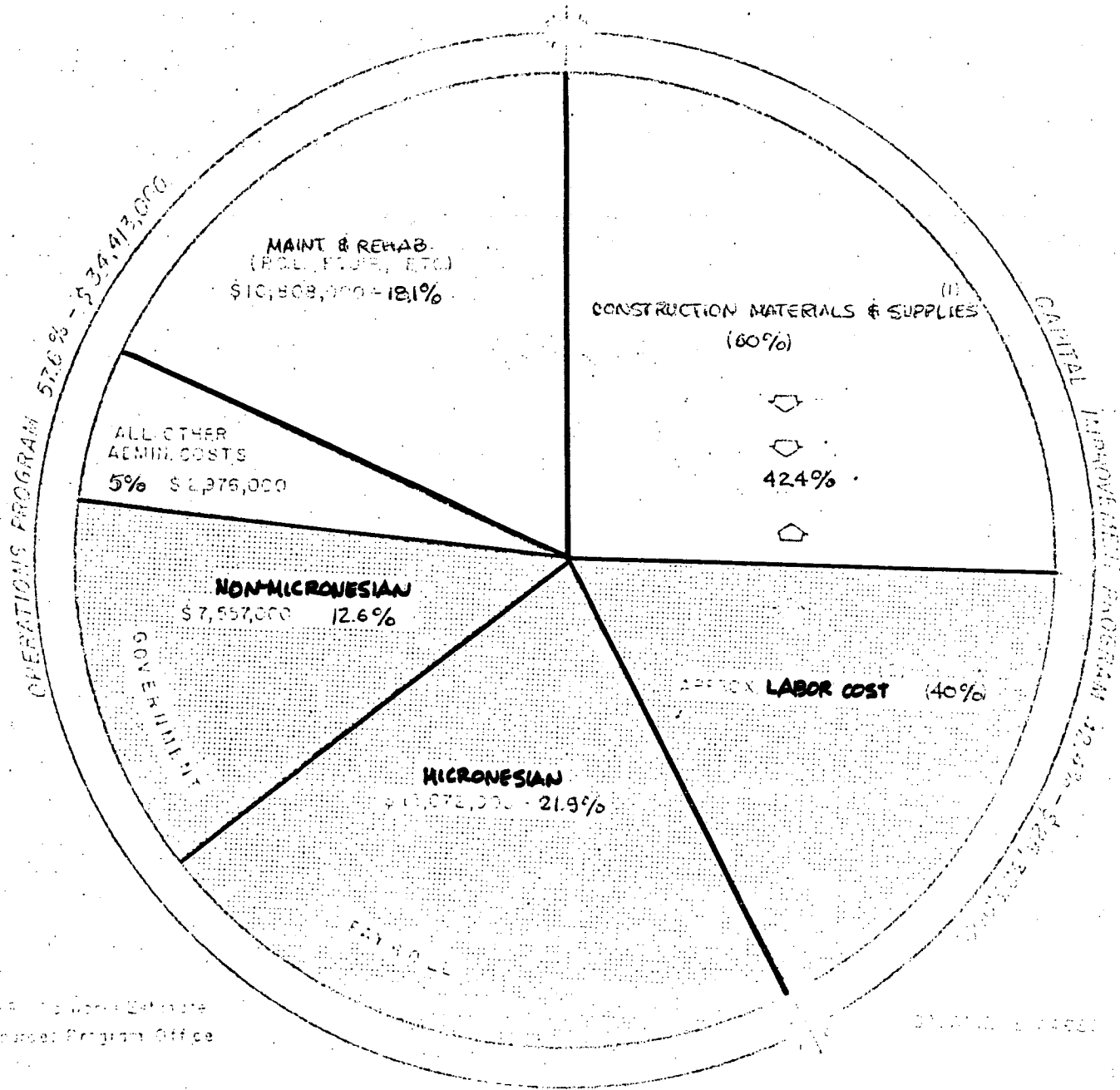
Trust Territory Administration grants have increased from \$6.5 million in FY 1962 to a FY 1971 level of \$59.7 million⁽¹⁾ for a per capita grant-in-aid of \$600. This is much more than the Federal Government is spending per capita for services for people in the United States.

-At the present time, 85% to 90% of the Trust Territory economic base is appropriated by the U.S. Congress. Wesley H. Hillendahl, Vice President of Bank of Hawaii, states, "that the private productive capital structure of the Trust Territory economy is almost inconsequential."

(1) During this period, per capita annual expenditures for health and education alone have increased from \$14 in 1962 to \$109 in 1970.

1971 TRUST TERRITORY GOVERNMENT ALLOCATIONS

FOR TOTAL BUDGET OF \$59,736,000.



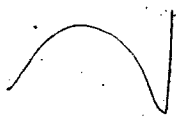
Washington, D.C. Estimate
 Central Program Office

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TAX REVENUES

A very rough estimate of tax collection has been calculated on the assumption that Administration funding is to be continued at present levels for the next five years and that such funding, i.e., infrastructure, EDFL loans, etc., will enhance and promote the growth and development of the private sector as anticipated in the section entitled, "Sector Analysis." Under no circumstances should the projected figures be interpreted to infer that the "Estimated Congress of Micronesia Revenues" shown on the graph could be anticipated under any other form of government structure.

Tax Revenues, Problems in Estimating

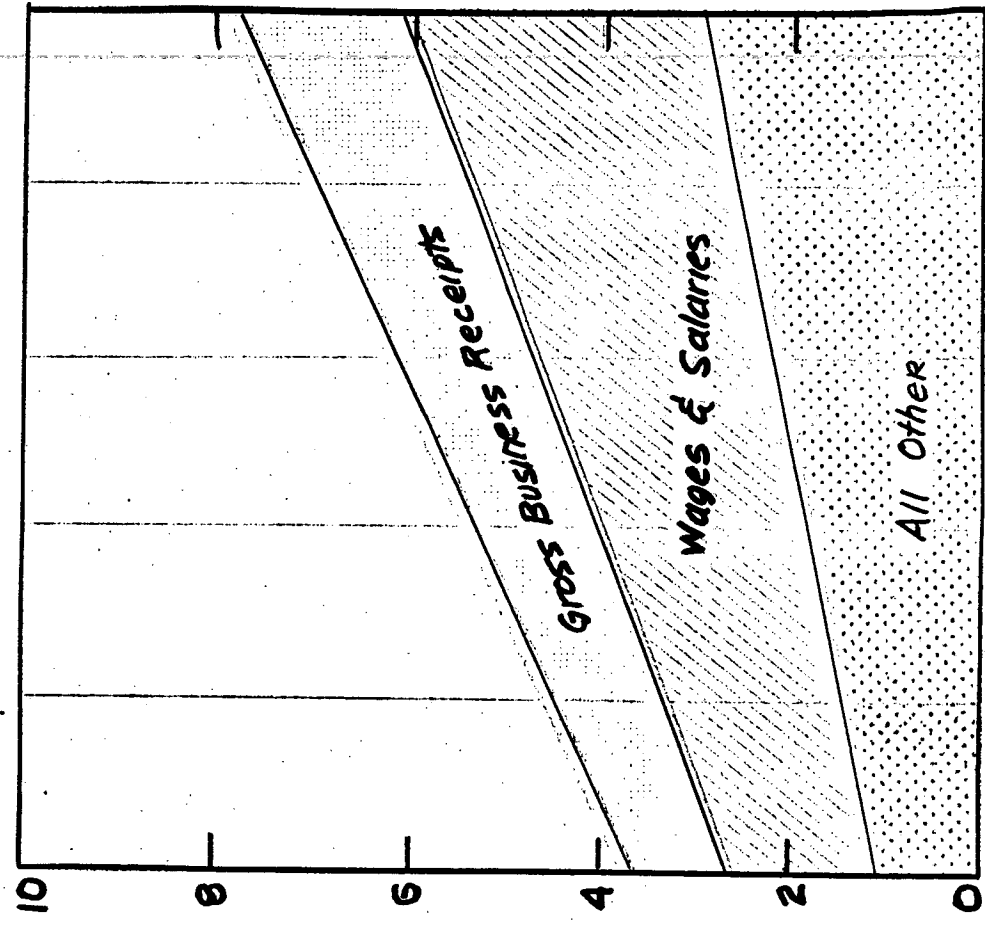
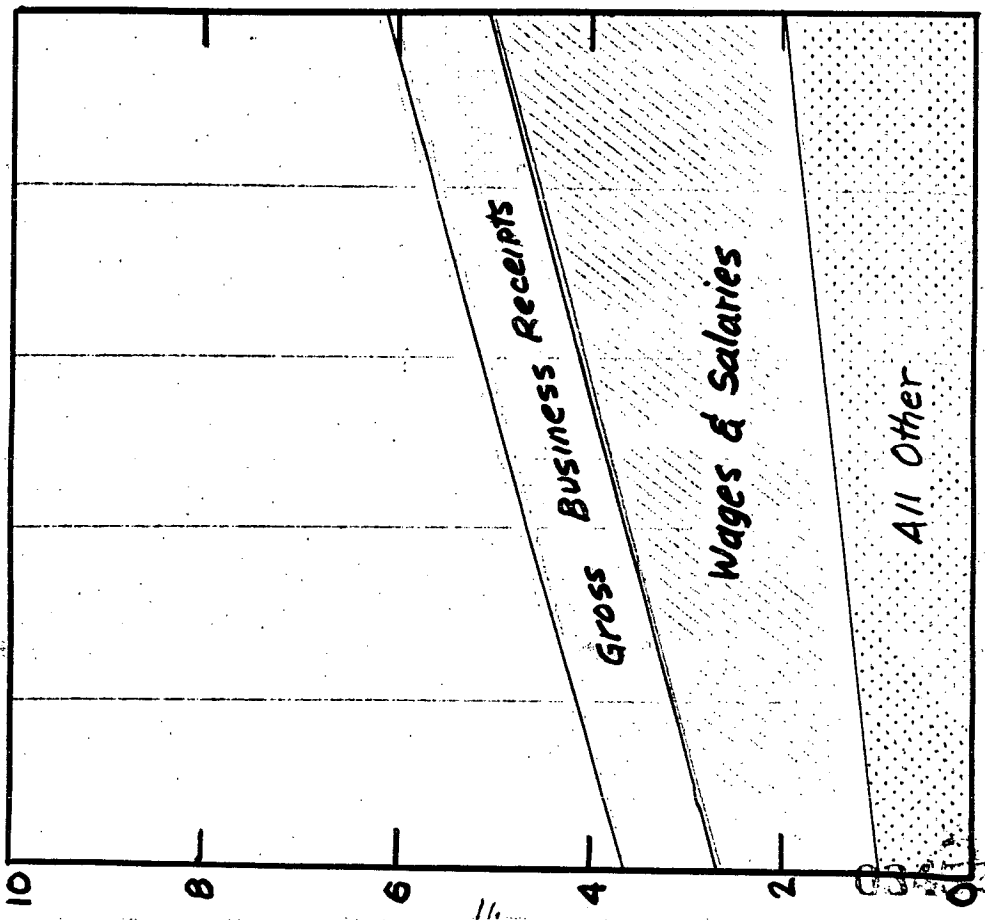


At this time, it is impossible to estimate total tax revenue based on an economy other than that presently existing. A figure for total revenue cannot even be guessed.....to do so in view of the importance of the imminent discussions relative to a possible different future political status would be to mislead and misinform representatives of both governments with serious consequences.

ESTIMATED CONGRESS OF MICRONESIA REVENUES

Current Rate Of Economic Growth Full Employment Rate Of Economic Growth

MILLIONS \$



1972 73 74 75 76 1977 1972 73 74 75 76 1977

II FOREIGN EXCHANGE DEVELOPMENT POTENTIAL

SECTOR ANALYSIS

Tourism

Under the assumption that the existing level of U.S. Government budget support can be maintained, i.e., \$60 million, the following development potential exists. The most immediate opportunities for economic expansion, for creating new employment opportunities, income and skills can be found in the tourist industry.

In FY 1971, about 32,000 visitors entered the Territory. By 1975, if accommodations, labor force and transportation facilities will allow.....82,000 travelers will visit Micronesia; by 1980, the number could reach 250,000, facilities permitting. Direct income from tourist expenditures alone could be between \$18 to \$20 million not considering the multiplier effect. *[leakage for imports]*

About 2,300 hotel rooms have been planned to accommodate the influx of visitors. This will require an additional investment of \$30 to \$55 million and about 2,600 hotel workers. This will place severe strains on Micronesia's labor force. Such investment can only be met by the private sector either through economic development loans or through foreign capital participation in development opportunities.

While the tourism sector holds great promise for growth, two points should be remembered: (1) The tourist economy is directly related to the economy of the market which it serves. Any economic

recessions in the market will directly influence the Micronesian tourist industry. Tourism consists of discretionary income expenditure and as such, it is the first area in which people will reduce spending during an economic slow down. (2) The impact of the so-called multiplier effect on the local economy has meaning only in those economies that are sophisticated enough to absorb and turn over the travel dollar expenditures. In other words, in an area that does not have night clubs, restaurants, elaborate transportation systems, attractions, etc., and where there is little activity outside the hotel or resort facility on which the tourist can spend his money, the flow of money into the economy does not occur in the same fashion that it does in more sophisticated economies.

Marine Resources (1)

At the present time, Japanese live bait skipjack vessels, operating out of Japan and fishing the waters surrounding the Territory, take approximately 30 to 35 thousand tons annually. The Van Camp boats operating out of Palau catch an additional 5,000 tons. An additional 50,000 tons of yellowfin tuna is caught in Trust Territory waters by long-line boats. With the exception of the Van Camp fishery in Palau, the tonnage of tuna harvested in Trust Territory waters is of no economic benefit to the Micronesians as it is processed and marketed from Japan. The value of the fish caught is depicted on page 24 of the Statistical Atlas.

(1) Source: Income and Employment Study, June 18, 1970.

It has been estimated that the ocean, lagoon and reefs of the Territory have a potential yield of marine products worth \$10 million annually and could employ over 1,500 islanders if these resources were properly utilized.

(1)

Commercial Agriculture

Most commercial agriculture is located within or on the periphery of the Commercial and Administrative Centers. Its development has been a reaction to the demands of these centers. With the exception of the Micronesian Development Company's livestock ranch, the sector is in an embryonic stage, characterized by small production units, family operated, with low levels of investment and technology.

The sector has the physical potential to produce commodities having an annual value of \$8 to \$10 million. A direct investment level of \$8 to \$10 million will be required to reach the full production potential. (2) See Appendix 4 and 5.

The sector must become more capital intensive and will require 1,300 workers with a per capita output of \$7,000 to \$9,000 versus the current per capita output of \$1,160. This will partially replace the current reliance on imported agricultural items which can be substituted by local production.

(1) Source: Income and Employment Study, June 18, 1970.

(2) It has been stated by competent observers that Japan, when preparing for war, subsidized agriculture and fisheries.

Subsistence Agriculture and Fishing

This sector is located outside the commercial and administrative centers situated on either outer islands or in isolated communities and handicapped in the participation of a money economy because of lack of transportation (i.e., roads, shipping, etc.).

Currently, this sector contains about half of the Territory's population. By 1976, projections show it will decline by about 10%. Approximately twenty-seven percent of Micronesia's population (27,400 people) are engaged in some form of productive endeavor (fishing, agriculture or copra production) in the subsistence sector.

Copra

Historical data for the production of copra can be examined in the Statistical Atlas by district for the period from 1961 to 1970 (pages 20 and 21). While much of the production is produced in the subsistence sector of the economy, it finds its way into the commercial sector as an important export item. However, copra production is declining as reflected in 1971 production valued at \$1.6 million for 10,687 short tons, a drop in earnings of 38.6% from 1970. The Agriculture Division estimates that copra production has the potential of being increased to 25,000 tons by 1975 for approximate earnings of \$4.5 million to \$5 million (before marketing costs, deductions, i.e., transportation, brokerage fees, etc.). See the Projected Value for Potential Copra Production in Appendix 4.

III EXISTING BUDGET ALLOCATIONS FOR CURRENT FIVE YEAR PLAN

The financial plan for the next five years for the Trust Territory Government has been shown graphically on page 23. This data has been derived from the Preliminary Operations Program and the Program Memorandum developed by the Program Office. The financial totals, shown by year for each district are more or less self-explanatory. It is worth noting, however, that once the infrastructure is in place, a funding level of about \$50 million will be required to operate the Government.

In interpreting the graph entitled, "Total Proposed Operations and Capital Improvements Budget for Maintaining Existing and Constructing Planned Government Social and Development Services," caution should be exercised in the omission of the Marianas District from the Trust Territory total. This omission, as requested by the Staff Director of the Political Status Committee, amounts to nothing more than a simple arithmetic subtraction. In the event of a Trust Territory Government structure other than that which presently exists, it is safe to assume that none of the figures which reflect the capital improvement programs, nor the operating and maintenance budgets for the districts, would have any meaning. This is because the movement of the Headquarters from the Marianas would entail substantial additional expenditures which have not been anticipated in the development of this five year budget in addition to the cost of reorganizing a new political administrative environment.

In summary, it must be clearly understood that the development potential described under the Sector Analysis is contingent upon the continuation of the programs which have been undertaken by the Trust Territory Government and in the provision of increased Government services through the planned capital improvement programs regardless of the final political status of the area.

THE COST OF FISCAL SELF-SUFFICIENCY

One of the difficulties to be overcome in estimating the cost of maintaining a government under a political status other than the present situation was to determine the level of public services and administration considered to be an acceptable standard. In the absence of guidance from the Status Committee of the Congress of Micronesia as to what would be considered an acceptable level for government programs, the writer communicated with the various department heads located throughout the Trust Territory Government and asked them to use their subjective judgment in developing a "bare-boned," minimal financial program developed under the most austere circumstances. The figures provided herein reflect the combined judgment of experienced departmental administrators and are furnished to provide a "bench mark" or "point of departure" relative to the cost of maintaining a markedly reduced level of government services as well as a halt in providing increased government infrastructure. In all services-----education, health, hospitals, water, sewer, power, transportation, communications, etc., American standards were modified when used as criteria.

The cost of maintaining and sustaining existing district community facilities cannot escape the basic recognition that the wide dispersion of Micronesia's six district centers requires tremendous duplication of government services resulting in high government

expenditures. Every district center must have a hospital, high school, sea port, airfield, radio station, electric generating facilities, etc.

Other than the Marshall Islands District, a large percentage of the money spent by the Trust Territory Government is spent for the maintenance of the six district centers on a combined population of approximately 36,500 to 47,600⁽¹⁾ Micronesians (there are one or two exceptions such as providing a Trust Territory vessel to call once a month at an outer island). This point may be examined graphically on the chart entitled, "Population Distribution" on page 28. Table 5 illustrates the "Percent of Trust Territory Budget Allocated for District Centers."

The graph on page 29 depicting the cost of operating the government at a minimal level must obviously be based upon Micronesian desires as to one of a number of alternatives to the kind of economic base they wish to cultivate, namely: (1) The maintenance of the status quo. (2) A return to an almost entirely subsistence economy. (3) A mixture of subsistence and commercial economy. (4) Continued "stimulated" economic growth with a view toward competing in the world market. Once this decision is made, the level of government services can be established and more realistic estimates as to what

(1) This population figure will differ with definition of district centers. A figure of 47,529 could be used as district center population if the citizens located on the periphery of the district centers are included. See the Population Distribution Map.

the cost of government could reasonably be expected to total under one of the above circumstances.

In the absence of any criteria as to the level of government the Micronesians would like to provide the citizens of the area, the calculations shown on the chart entitled "Estimated Projected Cost of Providing Government Services at a Substantially Reduced Level," page 29, were developed as a result of combining the considered judgment of individuals who have been involved in the administration of the various sectors of the government. It could be considered a "fall back" line ranging from approximately ~~\$25 million in 1972~~ to ~~\$43 million in 1982.~~

In the event of a reduction in present levels of grants-in-aid, substantial numbers of Micronesians would return to a subsistence way of life. Fewer Micronesians would be employed as wage earners and those so employed will be supporting more family members than is presently the case.

TABLE 5

PERCENT OF TRUST TERRITORY BUDGET ALLOCATED FOR DISTRICT CENTER
POPULATION AS COMPARED WITH THE OUTER ISLAND POPULATION

District	Percentage of Population		Percentage of 4 Year Budget	
	Dist. Center	Outer Island	Dist. Center	Outer Island
Marianas	<u>81.9</u>	18.1	87.2	12.8
Marshalls	35.5	<u>64.5</u>	46.8	53.2
Palau	45.3	<u>54.7</u>	94.4	5.6
Ponape	<u>69.8</u>	30.2	77.67	23.2
Truk	17.3	<u>87.2</u>	75.5	24.5
Yap	<u>63.3</u>	36.7	90.2	9.8
TOTAL	46% ⁽¹⁾	<u>54%</u> ⁽²⁾	<u>80%</u>	20%

Source: Planning Division - Public Works

(1) 47,629 people in District Centers. (This figure includes all of Ponape and Yap Islands population.)

(2) 54,621 people on outer islands.

IV INTERNATIONAL SOURCES FOR FINANCING ECONOMIC DEVELOPMENT

EXPORT-IMPORT BANK

AGENCY FOR
INTERNATIONAL DEVELOPMENT
(Dollar Loans)

AGENCY FOR
INTERNATIONAL DEVELOPMENT
(Foreign Currency I

PURPOSE

To promote U.S. exports through dollar loans and assistance to exporters by means of financing, guarantees and insurance.

Assistance in economic development; expansion of trade abroad for U. S. agricultural products.

TYPE OF ASSISTANCE

LOANS

Lends dollars only. Terms: for agricultural commodities--up to 12-15 months; for machinery and equipment, up to 5 years; for large jet aircraft, 7 years; project loans, 5-20 years (interest on project loans 5 3/4% per annum). Buy exporters' foreign dollar notes receivable up to 75 1/2% of invoice value without recourse on the exporter.

Lends in dollars. Terms 5 3/4% (15 years) to 3/4% (40 years), plus grace periods.

Lends in local currency local interest rate 3 to 10 years (15 years exceptional circumstances). Loans must be accepted in foreign country, and usually spent there.

STABILITY SURVEYS

Provides medium term political and credit guarantees to financial institutions in the United States. The institutions must assume the credit risks on the early maturities, which constitute 30 to 50 percent of the total financing. Cooperates with Foreign Credit Insurance Association in providing political and credit insurance for exporters.

On loans: guarantees are available although loan terms usually are too long and interest rates too low to interest most private No. investors. On investments: agency gives full or partial guarantees to U.S. investors.

GUARANTEES AND INSURANCE

EXPORT-IMPORT BANK	AGENCY <input checked="" type="radio"/> (1) INTERNATIONAL DEVELOPMENT (Dollar Loans)	AGENCY FOR INTERNATIONAL DEV. (Foreign Currency)
<p>WHO CAN BORROW</p> <p>United States private enterprises, foreign private enterprises and governments of friendly countries qualifying under the Battle Act.</p>	<p>Private enterprises in United States or in less-developed friendly countries; also governments or government entities of friendly countries, including development banks.</p>	<p>For business development private enterprises market expansion agricultural products enterprises of U.S. whose currency is</p>
<p>WHERE THE MONEY MUST BE SPENT</p> <p>United States</p>	<p>United States or borrowing country or other less-developed countries.</p>	<p>Recipient countries signed agreements States Department</p>
<p>PRIVATE PARTICIPATION IN AGENCY LOANS</p> <p>Eximbank encourages commercial banks and other private financial institutions to participate.</p>	<p>Welcomed, but see "GUARANTEES." No.</p>	
<p>DO PRIVATE CAPITAL FIRST</p> <p>Yes.</p>	<p>Administrator must take into account whether financing is available from other free-world sources on reasonable terms.</p>	<p>No.</p>
<p>MUST SHIP ONLY TO UNITED STATES VESSELS</p> <p>Yes, unless waived by Maritime Administration, which usually waives 50 per cent. No restriction where assistance is by guarantee or insurance.</p>	<p>Not less than 50% in U. S. vessels, more if desired; AID will pay freight only on cargo shipped in U. S. vessels.</p>	<p>Not applicable.</p>

Now being re-organized into Overseas Private Investment Corporation and International Development :

WORLD BANK

INTERNATIONAL DEVELOPMENT ASSOCIATION

INTERNATIONAL MONETARY FUND

INTERNATIONAL FINANCE CORPORATION

PURPOSE
To finance projects helping to build the foundations of economic growth in less-developed countries.

To finance economic and social projects in less-developed countries.

To promote stability of international exchange and expansion and growth of world trade.

To finance only private enterprises contributing to economic development of less-developed member countries.

TYPE OF ASSISTANCE

LOANS
Lends dollars and other currencies. Terms: 5 to 25 years, depending on project. Current rate: 5 3/4% per annum. Government guarantee required.

Terms may be varied. To date loans have been for 50 years without interest, with repayment in foreign exchange after a 10-year grace period. There is a service charge of 3/4% per annum on the outstanding balance.

Credits take the form of foreign exchange transactions (currencies of other member nations advanced in exchange for local currencies) which are to be reversed in a period of 3 to 5 years. Rates are 2 to 5 per cent per annum, plus a service fee.

Invests in or lends to any enterprise that makes a useful contribution to the economic development of a member country. It does not invest in undertakings that are government-owned or government-operated, or in public utilities or real estate development. Can now invest in capital stock.

GUARANTEES AND INSURANCE
Has authority to guarantee repayment of loans in whole or in part, but has never exercised it.

Can issue guarantees in lieu of loans, but has not done so to date.

Not applicable.

Can underwrite the subscription of capital issues.

TO WHOM CAN MONEY BE LOANED
Governments of member nations, including territories and political sub-divisions; political or private entities; public international or regional organizations.

Same as World Bank.

Governments of member nations.

Private companies in member countries.

WHERE CAN MONEY BE SPENT
Member countries, normally other than the one in which the project is located. Also Switzerland, by special arrangement.

Same as World Bank except that there is no special arrangement with Switzerland.

No limitations.

Member countries.

INTERNATIONAL AGENCIES, CONT'D

	WORLD BANK	INTERNATIONAL DEVELOPMENT ASSOCIATION	INTERNATIONAL MONETARY FUND	INTERNATIONAL FINANCE CORPORATION
Commercial banks and other financial institutions welcomed.	No.	No.	No direct participation, but agreements between Fund and member nations serve to encourage private sources to lend to those countries.	Welcomes financial part by financial institutions trial partners in ment ies.
MUST SEEK PRIVATE CAPITAL FIRST	Yes, and other public capital.	Yes, and also World Bank.	No.	Yes.
MUST SHIP ONLY IN UNITED STATES VESSELS	No.	No.	Not applicable.	No.

OTHER SOURCES OF POSSIBLE FINANCIAL ASSISTANCE

(1)

UNITED NATIONS
DEVELOPMENT PROGRAM

(1)

JAPAN

PURPOSE To assist in the economic development of less developed areas through the United Nations Industrial Development Organizations.

PURPOSE

TYPE OF ASSISTANCE

GRANTS

TECHNICAL INVESTMENT
FEASIBILITY SURVEYS

GUARANTEES AND
INSURANCE

EDUCATION
TRAINING

Underdeveloped member nations.

LOANS
GRANTS
STIPENDIUMS

World-wide procurement.

PRIVATE PARTICIPATION IN
INDUSTRY LOANS

STIPENDIUMS PRIVATE CAPITAL FIRST

STIPENDIUMS ONLY IN UNITED STATES
STIPENDIUMS

No.

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None informed members of the status committee should complete these sections.

APPENDIX 1

ECONOMIC DATA IN THE TRUST TERRITORY

An analysis of any economy must necessarily be based upon reasonably accurate statistical measurements of the various segments of that economy. For reasons which have never been clear to the writer, the collection of statistics of the type and quality required to make informed decisions relative to the Trust Territory economy, have never been undertaken on a serious, continuing and sustained basis. Recent comments on this subject from a variety of sources are worth noting.

From the Robert R. Nathan Report dated December 1966:

"Statistics of the kinds usually available to the economic development planner regarding such basic and essential characteristics as population size, characteristics, and distribution; the labor force and its industrial and occupational composition; wages and incomes; kinds and sizes of economic activities by major sectors; availability, location and present use patterns of various kinds of resources; and other such basic elements are largely unavailable for the Trust Territory. The lack of these basic data severely limits the precision with which conclusions and projections can be made. The serious limitations of information and data, and the rapid rate of change which now characterizes political, economic, and social conditions in Micronesia preclude accurate projections and forecasts for any extended future time period. In fact, it is impossible to know precisely what situations exist even today rendering projections into the realm of tomorrow even more treacherous."

The former Chief of Economic Development as recently as April, 1970, in a report for Kusaie wrote: "A repeated plea is again offered: the decision making process needs to be supported by (1) the systematic gathering of economic and social data; (2) its analysis, and (3) informed, flexible forward planning. Without accurate, adequate basic data which is required for monitoring of change, economic policy cannot be intelligently framed. Problems cannot be fully understood nor solutions anticipated."

The U.N. Report itself states, "although data furnished by local authorities are checked against previous reports, some sources of error cannot be controlled."

..... "Want to advise that 1/2 to 1/3 of all businessmen in Palau (my estimate) fail to have been reported in the past."

- Steele Holman, July 6, 1971.

..... The 1970 fish catch for Palau District was not reported for inclusion in the U.N. Report. This in itself is amazing as Palau is the site of the Marine Resources Division.

We are constantly called upon to provide economic data in the form of import/export data, individual and corporate income, etc., all of which in a developed, sophisticated, technological society are available as a result of reporting requirements imposed by law on the various sectors of the economy. For instance, the legal requirement to report "value added through the manufacturing process" in the U.S. Census of Manufacturers, or rental income reported to U.S. Census of Housing and wages and salaries reported to Bureau of Internal Revenue, assessed valuation of property, etc.

To date, none of the above have ever been collected by the Trust Territory Government, indeed, the only economic statistics collected have been those data which appear in the U.N. Report.

A cursory review of any economic analysis of the Trust Territory will reveal a statement relative to the dire shortage of measurement tools. A few examples follow:

- We do not know the population of Micronesia.
- We do not know the number of people engaged in subsistence agriculture.
- We do not know the number of businesses in Micronesia (other than those reported to Social Security and those are not complete).
- Information relative to individual district imports to, or exports from, the U.S., Japan, or any other country are not available at Headquarters.
- There is no accurate picture of visitor entries by district.
- We do not even know, nor can we find out, how the budget was allocated (in terms of total funds) to the six districts in past years.

Thus, in full consideration of the limitations mentioned above, the attached comments are provided on the economy of the Trust Territory.

TABLE

A COMPILATION OF AVAILABLE INCOME AND EMPLOYMENT STATISTICS

(DATA SHOWN REFLECTS TOTALS FOR FY70)

Item	COL. 1		COL. 2		COL. 3	
	MICRONESIAN No. Employees	\$ Payroll	NON-MICRONESIAN No. Employees	\$ Payroll	MICRO & NON-MICRO No. Employees	
Territory Gov.	6,400	13,300,000	550	7,300,000	6,950	20
Dist. - Munic. - District	(913 Mar)	(2,100,000 Mar)	(47 Mar)	-	(960 Mar)	(2
Private Sector				(1)		
				1,352,741	6,000-7,000	6
District Legislature				(332,319 Mar)	(1,400 Mar)	(1
and Staff						
		411,650				
		(113,700 Mar)				
S. Government						
		627				
		(131 Mar)				
		Unknown				

According to the Social Security Administration, this total excludes all wages in excess of \$750. per
Includes U. S. Government employees of Weather Bureau, OEO, etc.

Source: U. N. Report, Social Security Administration and T. T. Finance Office.

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APPENDIX 2

FACTORS INFLUENCING ECONOMIC GROWTH VIEWED AS RELATED TO A WESTERN
CONCEPT OF ECONOMIC DEVELOPMENT

(What the United States Negotiators may Cite)

- The islands, geographically isolated, physically separated, make for difficulty in marketing products in Micronesia, i.e., high shipping tariffs.
- Lack of physical infrastructure.
- Lack of indigenous capital as well as institutions for savings and capital accumulation. (The saving of money is not a habit of a subsistence culture.) Extended family system requiring the wage earner to share his earnings with other family members.
- Uncertain political status.
- Island culture which has not placed a high value on individual gain.
- Present attitudes regarding land ownership. (Mortgage on land as loan collateral not permitted.)
- Limited mineral, human and financial resources. (Land neither abundant nor fertile.)
- Unexpected climatic conditions resulting in high insurance, possible disruptions in production, raw material delivery.
- Lack of commitment as to overall, area-wide policy relative to economic development, e.g., Micronesians not too convinced of the advantages of the "American concept" of private enterprise.

- No natural source of fuel or power.
- No apparent comparative advantage (over other areas) in any particular economic endeavor.
- Lack of industrial sophistication (marketing, production, and managerial).
- Labor - small numbers, low levels of training, and productivity in relation to high wages, lack of mobility and low labor market standards.
- Lack of pest free warehouses, including cold storage, (a necessity between shipments), is an effective obstacle to economic development.
- Small indigenous market.

(What the Micronesian Negotiators could Cite as
Impediments to Economic Growth)

- Burdensome legal restrictions on foreign (American) investment discourages joint venture investment (PL 3C-50) as does the "most favored nation" clause in the Trusteeship Agreement.
- U.S. tariff restrictions on Trust Territory exports, i.e., canned fish.

APPENDIX 3

IMPORT SUBSTITUTION

SELECTED PROBABLE BUSINESS ENDEAVORS WHICH MERIT PRE-INVESTMENT INVESTIGATION AND ANALYSIS FOR ADAPTATION IN ONE OR MORE DISTRICT CENTERS.

FOOD

Potato, banana, breadfruit chips (packaged)

Banana puree, flakes and flour

Ice Cream

Poultry farming -- eggs, dehydrated and fresh

Bakery

FEED FERTILIZER

Seaweed (agar)

Animal feed (fish meal)

Poultry feed (blood-bone meal)

AGRICULTURAL PROCESSING

Small canning facility

Hydroponics

Lyophilization (agricultural, seafood, meat)

Dairy products, i.e. (dried, powdered, condensed milk, butter, etc.)

Frozen food packaging

Vegetable dehydration (i.e., onion flakes.)

SERVICE - TOURISM

Automobile tire recapping

Laundry - dry cleaning

Wet-cell batteries

Bowling alley

Drive-in theater

Hotels (10-20 room)

Warehousing

Marina

CONSTRUCTION

Saw mill

Concrete Pipe

Soil building blocks

MANUFACTURING

Furniture

Small boat hulls (fiberglass)

Outboard motor assembly

Leather-plastic sandals, belts, wall etc.

Block ice

Carbon dioxide plant

Portable freezing units
(Small boats)

Molder wood products (pulverized
coconuts)

Handicrafts

Ceramics

Printing shop

Galvanizing sheet

Solar water heaters - solar cookers

Shirts - dresses (cotton)

MISCELLANEOUS

Wind driven generators

MARINE

Shark skin tanning

Lobster (rearing from fry)

Fishing (Skip-jack tuna, sardines,
sea turtle, clams, crabs, mackerel,
reef fish, etc.)

Trepang, Mother-of-pearl culture,
mother-of-pearl, trochus.

TROPICAL FRUIT

Papaya - papain (meat tenderizer)
Papa preserves, jam, marmalade,
pickles, pate candy, canned
and frozen papaya.

Sugar cane, sugar, bagasse (wall
board), candy molasses (cattle feed)

Shredded or grated coconut, package
charcoal briquetting, coir for car
and handicrafts mats, canned heart
palm.

Avocado, mango, star apple, manioc
pineapple.

CITRUS FRUIT

Corn, tomatoes, egg plant, melons,
green vegetables and root crops.

Rice-ramie, pepper, cocoa-chocolat

OTHER

Bee keeping

APPENDIX 4

ECONOMIC BASE DATA FOR POLITICAL STATUS COMMITTEE

PROJECTED POTENTIAL ANNUAL COPRA PRODUCTION VALUE (EXPORT)

Year	MARIANAS	MARSHALL	PALAU	PONAPE	TRUK	YAP	TOTAL
1972	\$ 20,000	\$1,400,000	\$ 50,000	\$ 680,000	\$ 700,000	\$150,000	\$3,000,000
1973	\$ 30,000	\$1,500,000	\$ 60,000	\$ 750,000	\$ 800,000	\$160,000	\$3,300,000
1974	\$ 40,000	\$1,580,000	\$ 70,000	\$ 810,000	\$ 830,000	\$170,000	\$3,500,000
1975	\$ 50,000	\$1,760,000	\$ 80,000	\$ 910,000	\$ 920,000	\$180,000	\$3,900,000
1976	\$ 60,000	\$1,910,000	\$ 90,000	\$1010,000	\$1040,000	\$190,000	\$4,300,000
1977	\$ 70,000	\$2,000,000	\$100,000	\$1040,000	\$1090,000	\$200,000	\$4,500,000
1978	\$ 80,000	\$2,100,000	\$120,000	\$1120,000	\$1170,000	\$210,000	\$4,800,000
1979	\$ 90,000	\$2,200,000	\$130,000	\$1150,000	\$1210,000	\$220,000	\$5,000,000
1980	\$100,000	\$2,230,000	\$140,000	\$1200,000	\$1400,000	\$230,000	\$5,300,000
1981	\$110,000	\$2,250,000	\$150,000	\$1250,000	\$1500,000	\$240,000	\$5,500,000
1982	\$120,000	\$2,320,000	\$160,000	\$1350,000	\$1600,000	\$250,000	\$5,800,000

APPENDIX 5

ECONOMIC BASE DATA FOR POLITICAL STATUS COMMITTEE

Projected Potential
ANNUAL FRUIT AND VEGETABLE PRODUCTION VALUE (EXPORT)

Year	MARIANAS	MARSHALL	PALAU	PONAPE	TRUK	YAP	TOTAL
1972	\$ 300,000	\$ -0-	\$ 10,000	\$ 24,000	\$ 5,000	\$ 1,000	\$ 340,000
1973	\$ 562,000	-0-	\$ 25,000	\$ 48,000	\$ 10,000	\$ 5,000	\$ 650,000
1974	\$ 630,000	-0-	\$ 35,000	\$ 70,000	\$ 15,000	\$ 10,000	\$ 760,000
1975	\$ 685,000	-0-	\$ 50,000	\$ 100,000	\$ 20,000	\$ 15,000	\$ 870,000
1976	\$ 750,000	-0-	\$ 65,000	\$ 120,000	\$ 25,000	\$ 20,000	\$ 980,000
1977	\$ 800,000	-0-	\$ 85,000	\$ 150,000	\$ 30,000	\$ 25,000	\$ 1090,000
1978	\$ 855,000	-0-	\$ 100,000	\$ 180,000	\$ 35,000	\$ 30,000	\$ 1200,000
1979	\$ 910,000	-0-	\$ 125,000	\$ 200,000	\$ 40,000	\$ 35,000	\$ 1310,000
1980	\$ 925,000	-0-	\$ 150,000	\$ 250,000	\$ 45,000	\$ 40,000	\$ 1420,000
1981	\$ 965,000	-0-	\$ 180,000	\$ 280,000	\$ 50,000	\$ 45,000	\$ 1530,000
1982	\$ 1135,000	-0-	\$ 200,000	\$ 300,000	\$ 55,000	\$ 50,000	\$ 1740,000

(Confidential)

E. B. Mihalj
May 21, 1971

Alvin
to

The First Position Papers - Suggested Topics

I. Economic - General

The aim here is to develop a set of statistical breakdowns of Micronesia's economic position. I suggest that, if possible, a sub-set also be made showing the situation for the five districts, minus the Marianas. The units should include:

- Stewart*
1. A table(s) or graph(s) showing the total cost, in the 1972-82 period, of maintaining existing and planned social and developmental services; of maintaining these services at a substantially reduced level (50 percent less places in schools, or a 50 percent reduction in health care facilities); of increasing the level of these services at a conservative rate, e.g., five percent per annum.
 2. National income estimates for the 1972-82 period. This would be based in turn on
 3. Projections of growth in key sectors: tourism, fisheries, copra, etc. at varying levels of private and public investment
 4. Projections of official (as opposed to private) external capital requirements needed; first, to make these investments and second, to close the gap between likely domestic revenues (at current tax rates) and total fiscal requirements.

This is a job for a magician. The existing data simply isn't that good; and the number of variables is staggering. I do think though that Bill Stewart can come up with a good indication of what it will cost Micronesia to go off on its own or, to put it differently, of how much Micronesia would require from the U.S. or other sources to sustain the

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present and alternative spending patterns. Bill should do his best with such subordinate issues as the cost of maintaining the government, but with a rapidly decreasing number of American officials.

II. External Capital

Stewart

The Micronesian side can legitimately take the stand that the post-trusteeship state will require infusions of official external capital for at least ten years. Moreover, it can legitimately argue that the magnitude of these requirements is a function almost exclusively of American spending and investment patterns during the trusteeship (size of bureaucracy, scope of services, etc.). The projections developed above should give a rough estimate of how large that infusion must be. I would stress that this will hold true whether Micronesia becomes independent or is associated.

A separate paper, therefore, should tackle two questions.

- * 1. How much will Micronesia need?
- * 2. How and where will it get that amount?

The first question is difficult, but the answer is at least simple to express. Given varying growth rates of exports and given varying investment and spending patterns in Micronesia, the requirements will be X or Y or Z.

The second paper is far more complex. It should explore what the Micronesian side could ask of the U.S. And it should explore the alternative possibilities. To elaborate

From the U.S. The U.S. can put money into Micronesia in a variety of forms. Which of these are the best bets from the Micronesians in

point of view? The possibilities, at first glance, are:

1. Outright subsidy or grants. The U.S. would, in the course of negotiations, agree to a schedule of grants for, say, five years with a commitment of renewal thereafter on the basis of future negotiations.

2. A grant and loan package. The former would be intended for government operations, the latter for capital investments likely to increase exports, i.e., pay for themselves. This is a dangerous route and should be travelled on warily.

3. Tariff preferences for Micronesian exports, particularly fish and tropical fruits. The U.S. could be asked, simultaneously, to use its good offices to get Micronesia preferential access to the Japanese market.

4. Rent from use of military facilities. Presumably, this would be in conjunction with grants (and perhaps loans). The issue is: should such rents be seen as part of the assistance Micronesia needs to dig itself out of the hole the U.S. put it in; or as an additional item--a bonus. I tend to the latter, certainly as a negotiating tactic.

5. Technical assistance. Micronesia will need specialized manpower for some time, particularly if the economy moves. Such manpower comes high--and in foreign exchange. The U.S. might supplement its grant with manpower assistance.

6. A guarantee from the U.S. to use its good offices to get Micronesia special treatment from the international financing organizations. This too should be looked at with great caution.

This brings us to the alternatives to financing by the U.S.

1. United Nations agencies. The most that can be expected here is technical assistance, some of it quite good, plus some pre-investment survey work. The experience of Fiji and Western Samoa is an indicator that not much can be hoped for from the U.N. in financial terms.

2. Asian Development Bank. A fair prospect. The ADB is now aiding Western Samoa on a project basis. This institution is run on rather businesslike terms and assistance can only be expected if Micronesia has projects of clear commercial feasibility. The ADB will not give budget support.

3. World Bank. The IBRD is a very useful institution, but its loans come at nearly world prices. Again, the commercial pay-off must be quite obvious. The International Development Association, a component of the Bank, lends at concessional rates, i.e., lower rates. But these are still loans. The day may come when this is a desirable approach, however. Are there projects ready for support and with what would repayment be made?

4. Other governments. If Micronesia becomes independent, it can enter the competition for grant and loan funds from both western and eastern countries. The competition, it should be realized, is fierce and the funds severely limited relative to demand. Moreover, aid is given with some political purpose. This can be handled, primarily by taking from a variety of sources and thereby cancelling out the so called strings. This is a tough game to win. A projection of likely funds from such sources is almost impossible. An associated Micronesia would not have access to this kind of aid.

5. Commercial credit. This form of capital comes at a high cost. The cost is worth it if the project is right. If not handled gingerly, each use of such credit can be disastrous. Many countries in the world today have such high debt service costs from past loans that their current and near-term future exports are heavily mortgaged.