

Budget 2012 & Streamlining Workshop

External Factors Affecting the College

External Factors

- FSM Economy
- Migration Trends
- ECE-12 Enrollment Patterns
- College Readiness of HS Graduates
- US Military Recruitment
- JEMCO & IDP Issues

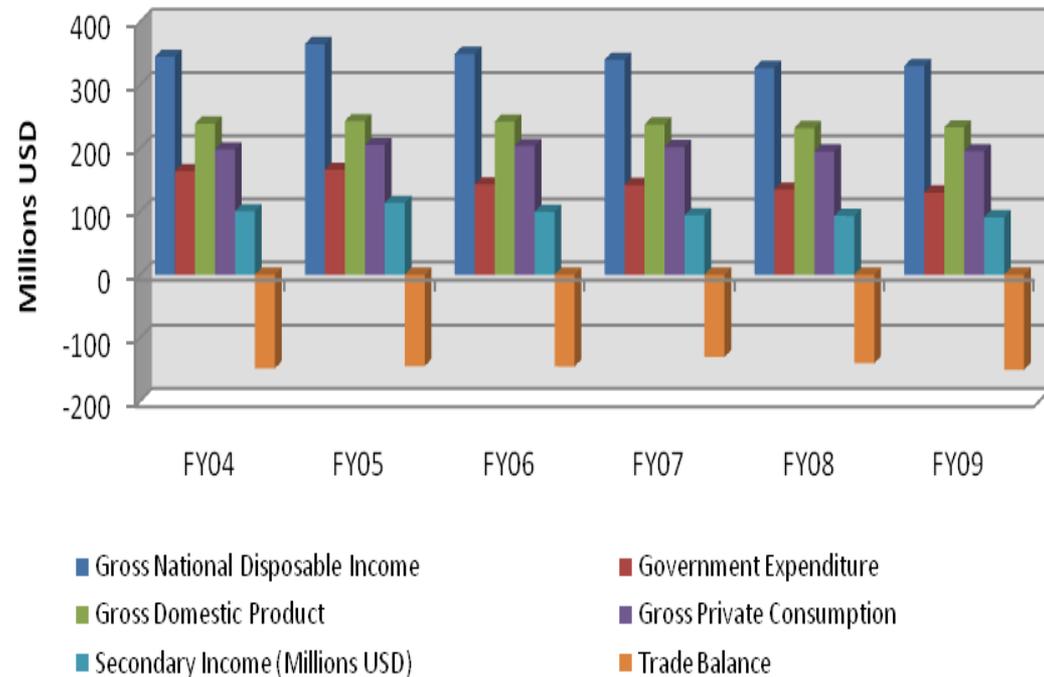
The Economy of the FSM

Based on FSM Presentation to JEMCO September 2010

Macroeconomic Indicators

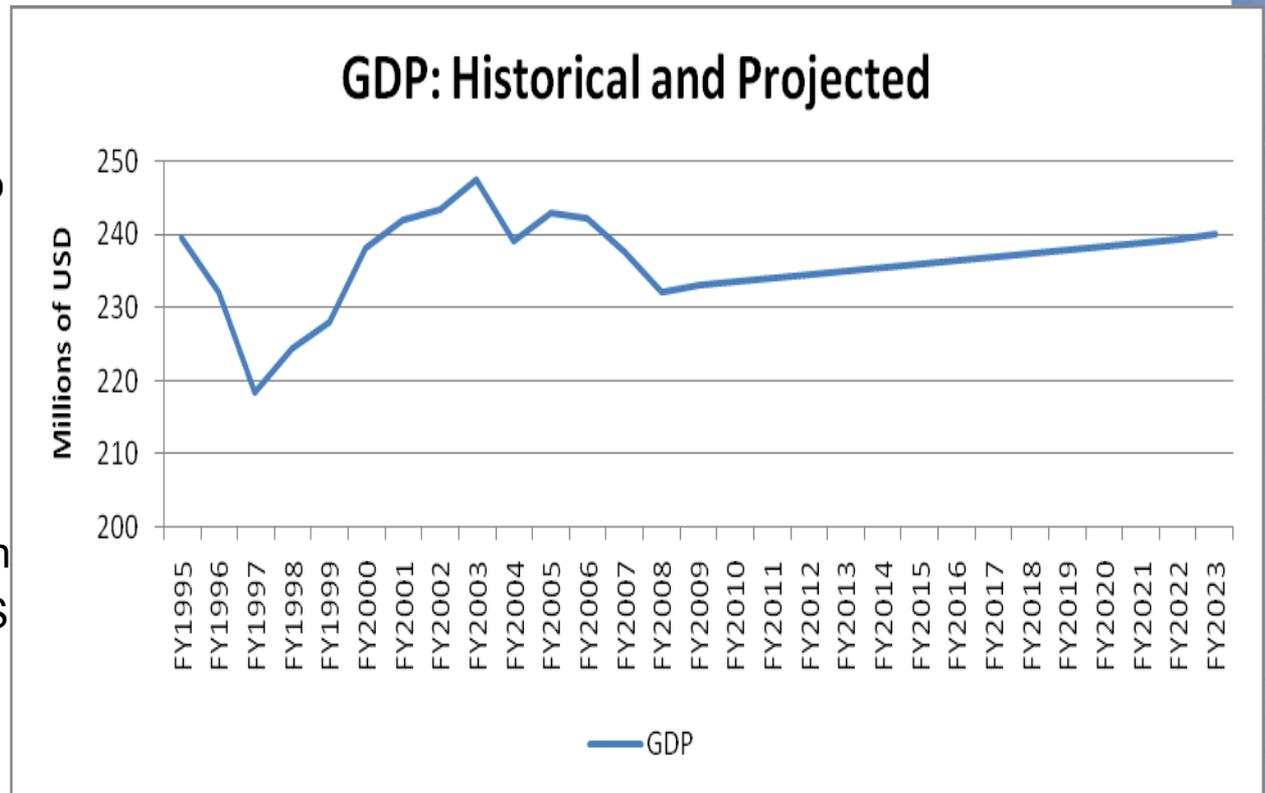
- GDP Stagnant
- Gov't Expenditure Down
- Trade Deficit Up
- Large Secondary Income
- Consumption Up

Real Series Macro Indicators



GDP Projection

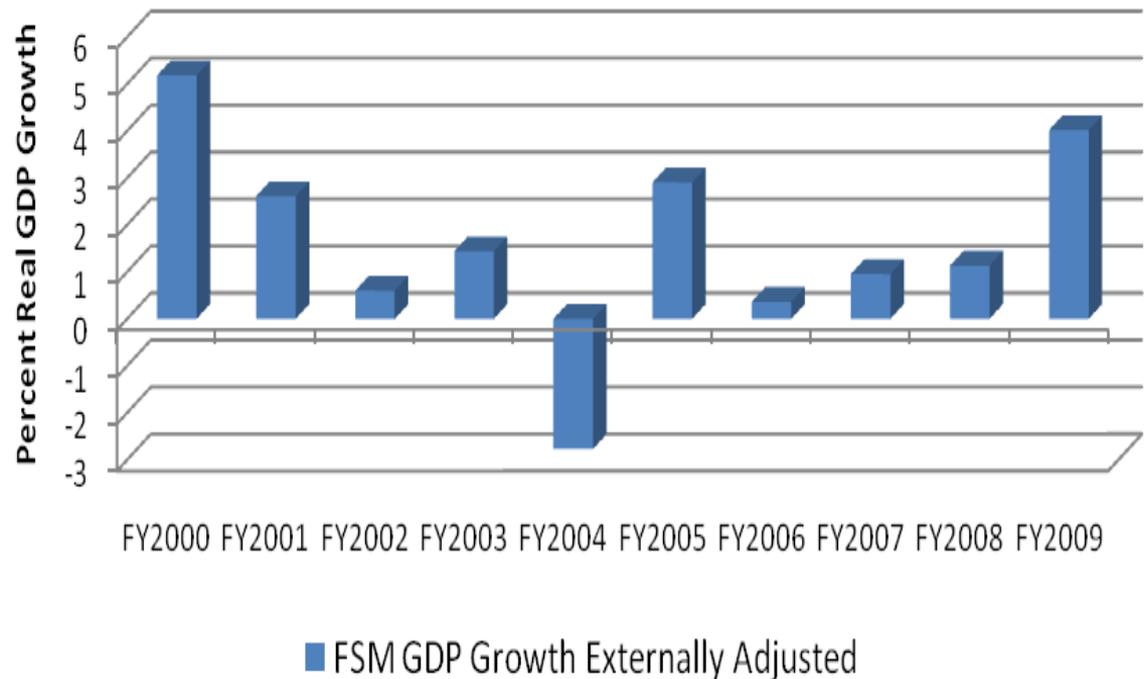
- GDP will continue to stagnate over the remainder of the Amended Compact period without substantial policy changes – from both the FSM and the US



GDP as an Indicator

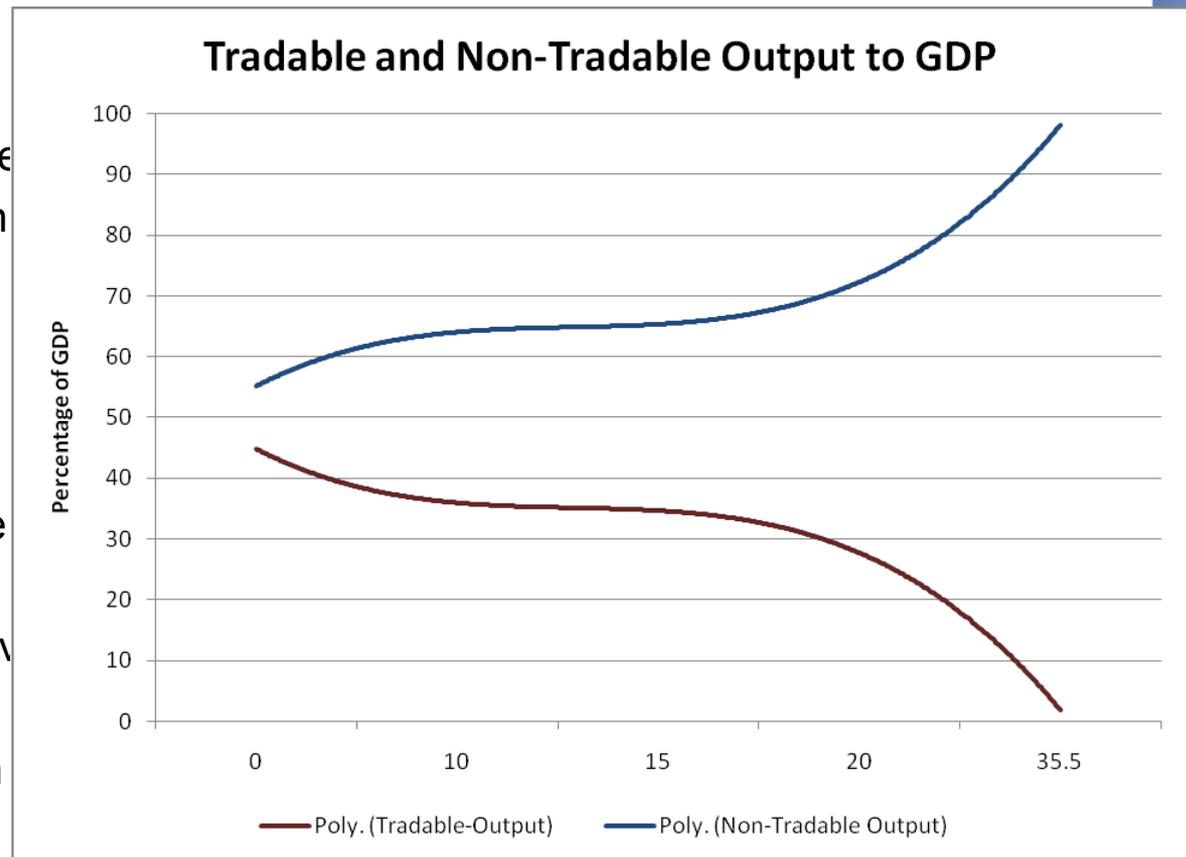
- GDP may not be a good indicator of economic progress in the FSM.
- Changes in CPI and external grant levels account for 40% of all fluctuation in the GDP growth rate.
- “Stripping” these out presents a much more optimistic picture of economic growth in the FSM.

FSM "External Shock" Adjusted GDP Growth



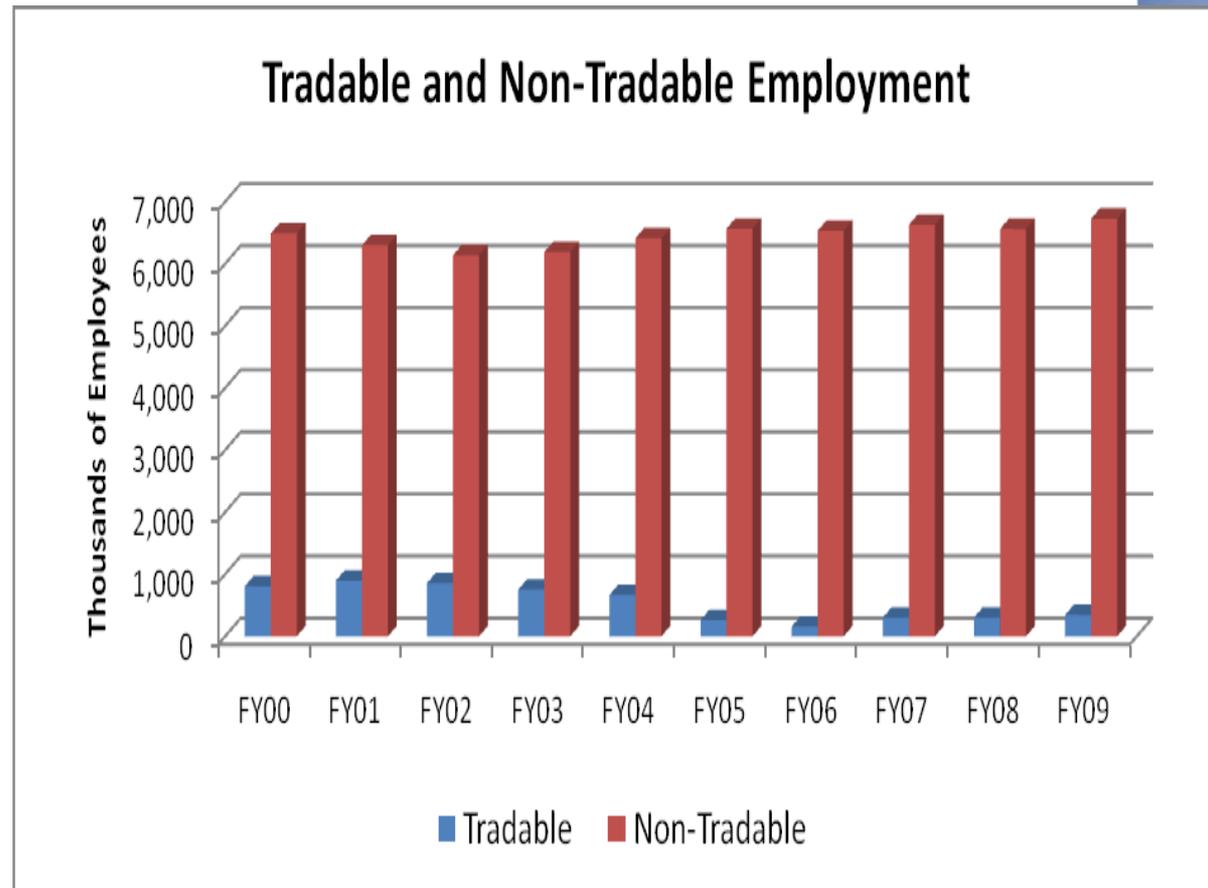
Dutch Disease

- Following Arellano et al (2009) it appears that the FSM suffers from “Dutch Disease” induced by the Amended Compact.
- Dutch Disease is the transfer of productive factors from the tradable to non-tradable sectors due to a change in relative prices brought on by changes in consumption patterns.



Labor in the FSM

- Private sector employment is up 3% from FY2008 to FY2009.
- Although FY2009 also saw a 14% jump in the employment level in the tradable sector, from 302 to 344, tradable sector employment is still less than 5% of total private sector employment.
- This discrepancy is a vibrant manifestation of the Dutch Disease



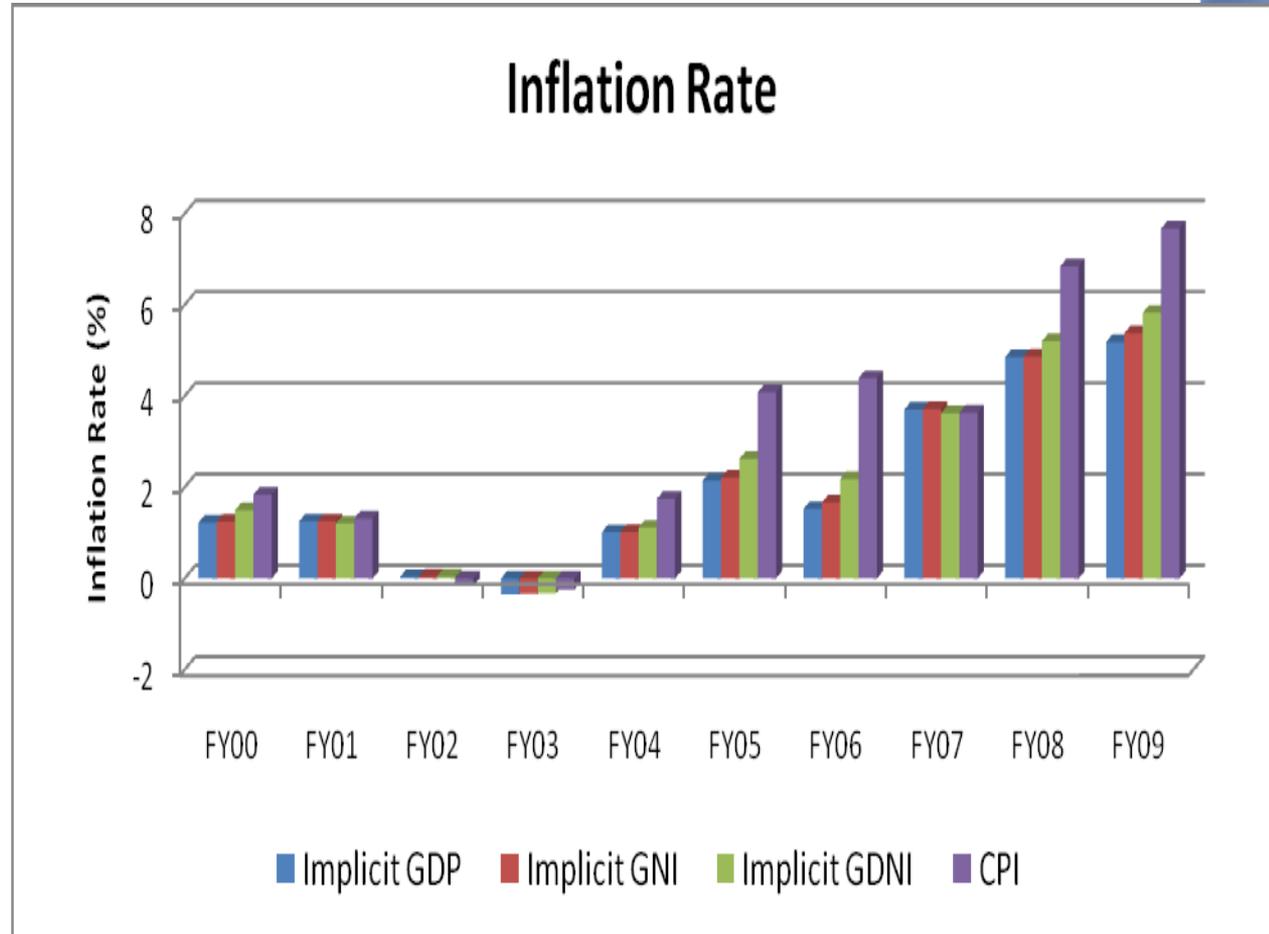
Prices in the FSM

- Price levels have averaged 5% increases from FY07-FY09.

- In response to the global economic downturn, inflation rates should subside in FY10.

- From 1999Q4 to 2008Q1 non-fuel tradable goods increased by 12.4% while the price of non-tradable items increased by 33.2%.

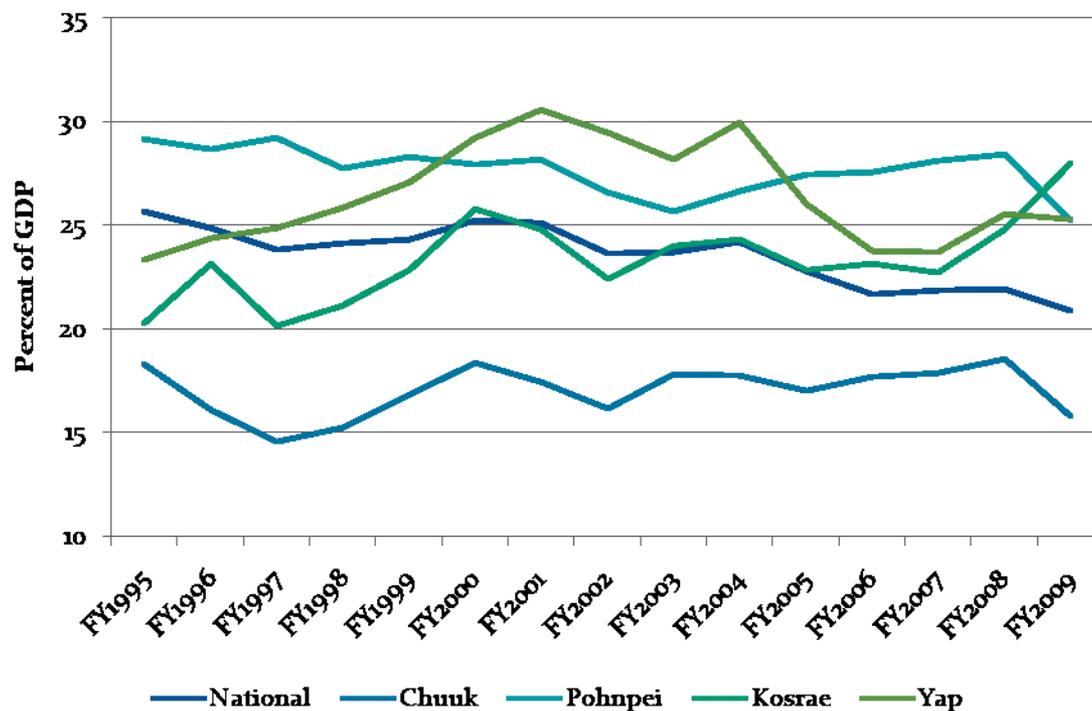
- Although price shocks increase the relative price of tradable goods and service, they cannot be viewed as a solution to the Dutch Disease problem.



Private Sector in the FSM

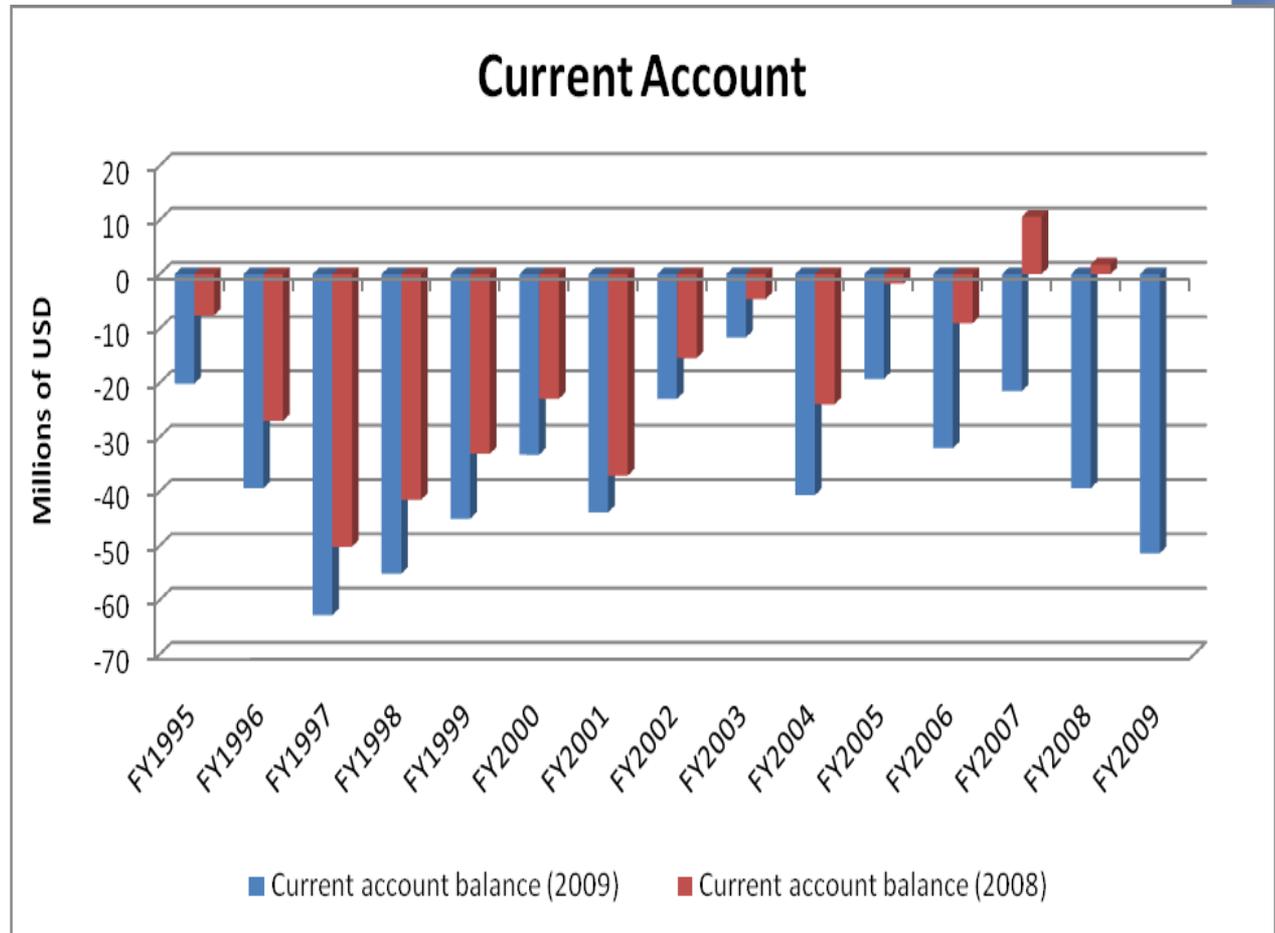
- The combination of these factors has resulted in continued infirmity for the private sector in the FSM.
- Private sector output has accounted for less than 25% of GDP since FY1995

Private Sector Output as Percentage of GDP



Why does the tradable sector matter?

- Revised balance of payments (BOP) data shows that the FSM has been running a significant current account deficit.
- In the absence of infusions to the capital account, this position is unsustainable in the absence of increased income transfers or increased production.



Why does stagnation persist?

- The lack of sustained economic development in the FSM can be attributed to three broad factors.
 - Internal Policies
 - Government expenditure that encourages consumption, rather than investment, distorts prices and induces the “Dutch Disease.”
 - Government policies and practices discourage foreign direct investment (FDI).
 - Lack of Economic Infrastructure
 - The FSM lacks the energy, transportation and communications infrastructure to support domestic production or attract FDI.
 - Insufficient Investment in the Private Sector
 - Domestic savings, and domestic commercial banks, provide insufficient capital for private sector development.

What can be done in the context of the Amended Compact to turn the tide?

IDF Performance

- The US can extend the time to submit a proposal for authorization of \$40 million to revitalize the Investment Development Fund (IDF) to provide a base of capital for private sector development.
- IDF underperformance is largely due to the politically-influenced state sub-accounts. The private sub-account has performed within development bank levels.

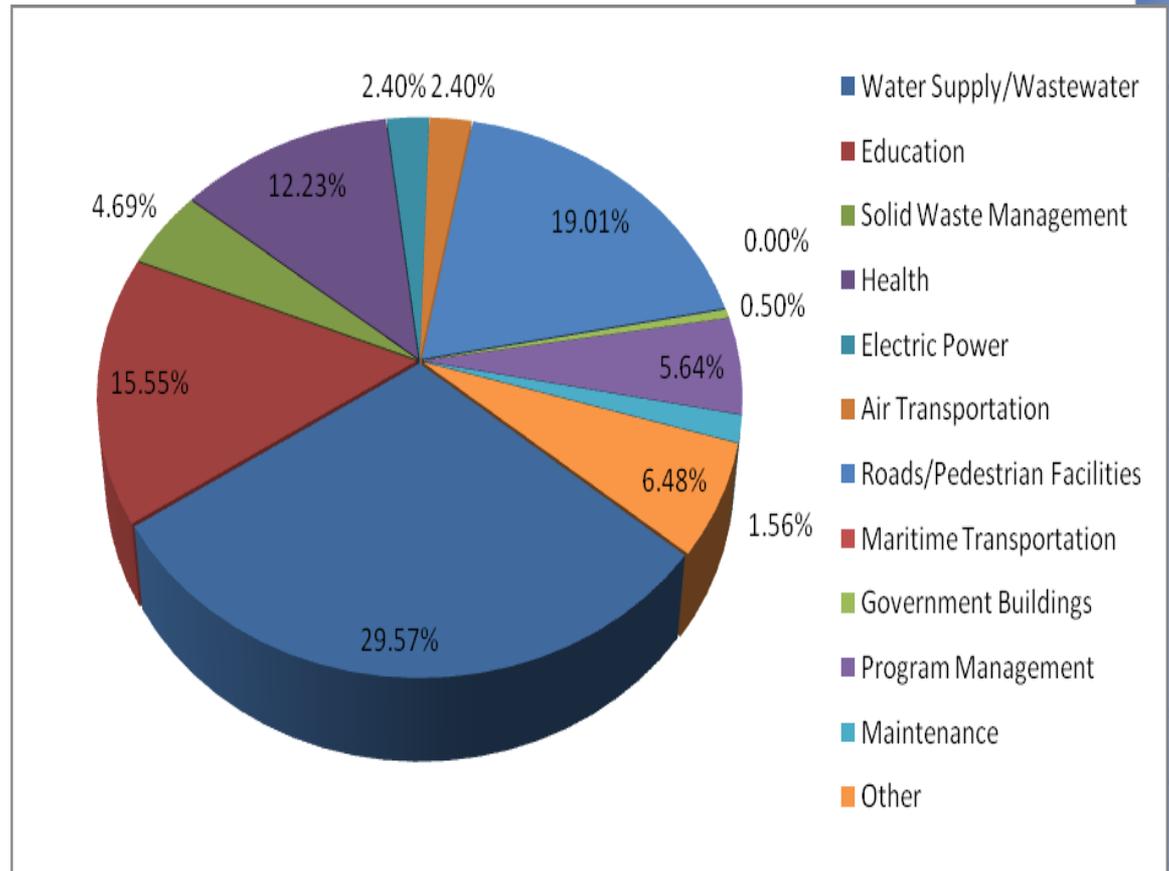
Sub Account	Number	Amount	Active	Default	Balance
Pohnpei	2	838,881	0	2	914,325
Chuuk	3	3,982,131	0	3	3,852,920
Kosrae	2	3,695,115	1	1	2,999,937
Yap	3	2,447,389	0	3	2,530,878
Private	12	14,153,824	8	4	9,506,432
Total	22	25,117,340	9	13	19,804,493

Develop an Appropriate Institutional Environment

- The FSM, perhaps with US technical assistance, seeks to undertake comprehensive studies to identify ways to increase the effectiveness of sector expenditures, particularly in health and education.
- It is no secret that the FSM faces political difficulties in passing institutional reforms that would facilitate economic development.
- Rather than using Amended Compact conditionality under the Fiscal Procedures Agreements (FPA) to “micro-manage” expenditure level decisions it would be useful if JEMCO applies broad conditionality to help facilitate institutional reform.
- Projects funded by a renewed IDF authorization could be limited to those states that have adopted an appropriate foreign investment regime.

Funding for Economic Infrastructure

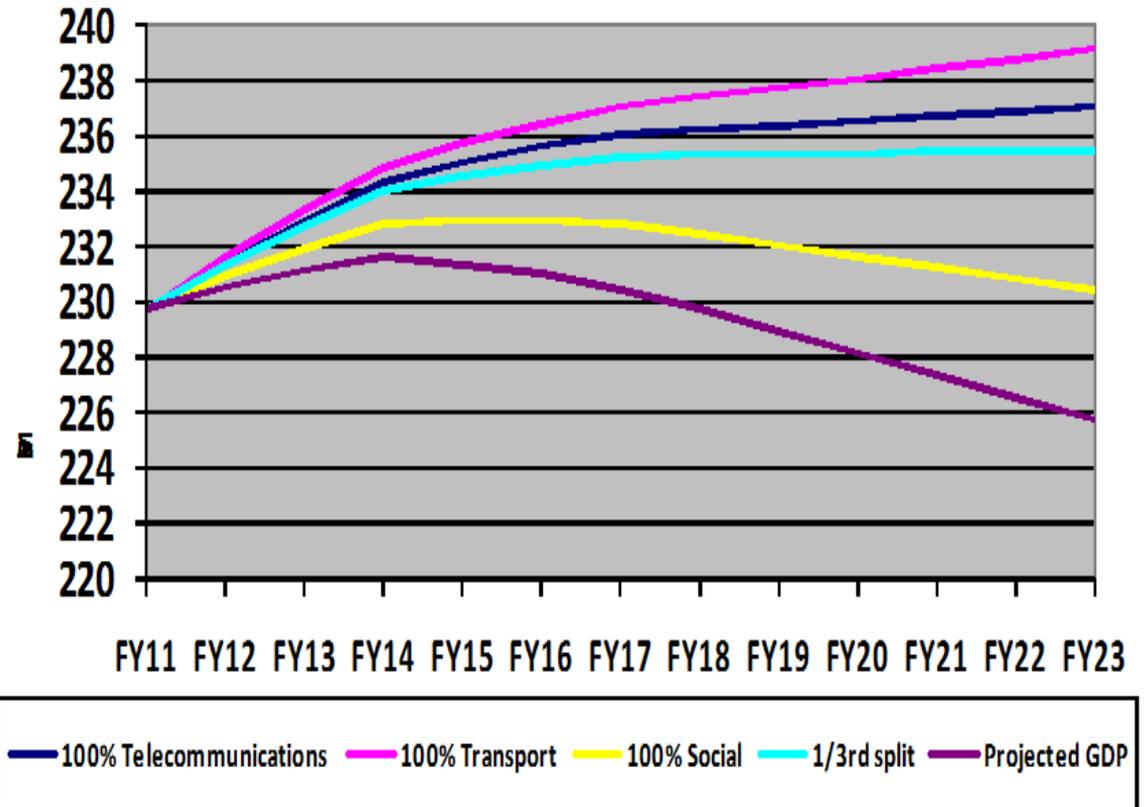
- Of the \$262 million worth of currently approved infrastructure projects, only 22% are economic infrastructure projects.
- Economic infrastructure (energy, transportation, communications) contributes more to the underlying growth rate than social infrastructure alone.
- Allocating 2/3rds of the remaining infrastructure would help put in place an inviting business setting.



Infrastructure Growth Rates

- Economic infrastructure (energy, transportation, communications) contributes more to the underlying growth rate than social infrastructure alone.
- Granting equal consideration for economic infrastructure for remaining grant would help put in place an inviting business setting.

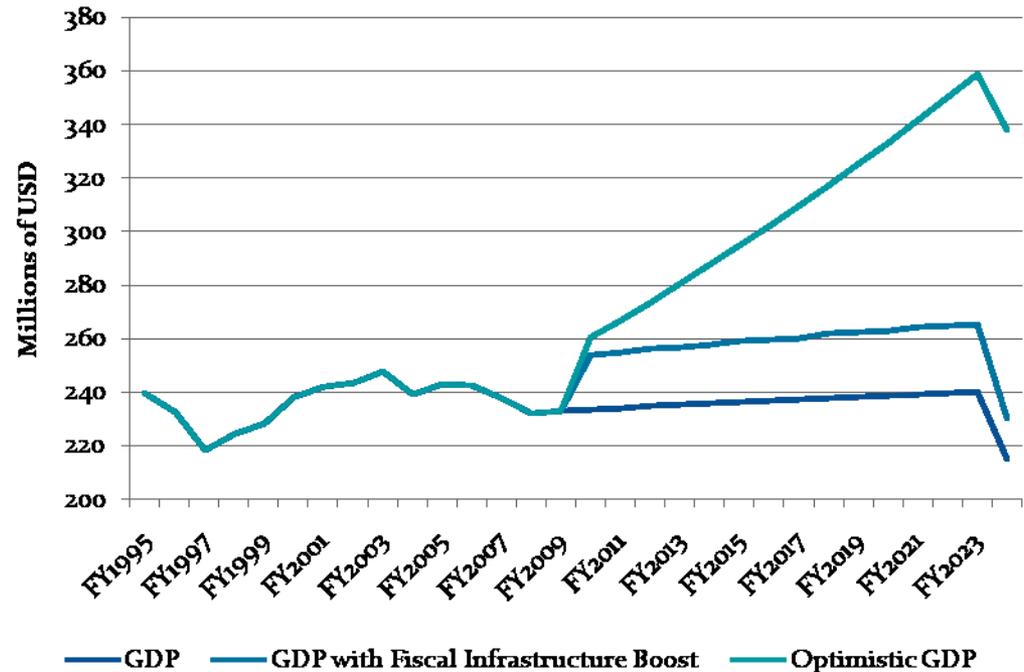
Real GDP Projections Via Types of Infrastructure Spending



FSM Economy in the Long Term

- With the appropriate policy adjustments the FSM can outperform current GDP projections over the remainder of the Amended Compact period.
- However, due to systemic under-funding of the Compact Trust Fund, the FSM will experience a significant recession in FY2024, even under the most optimistic growth projections.

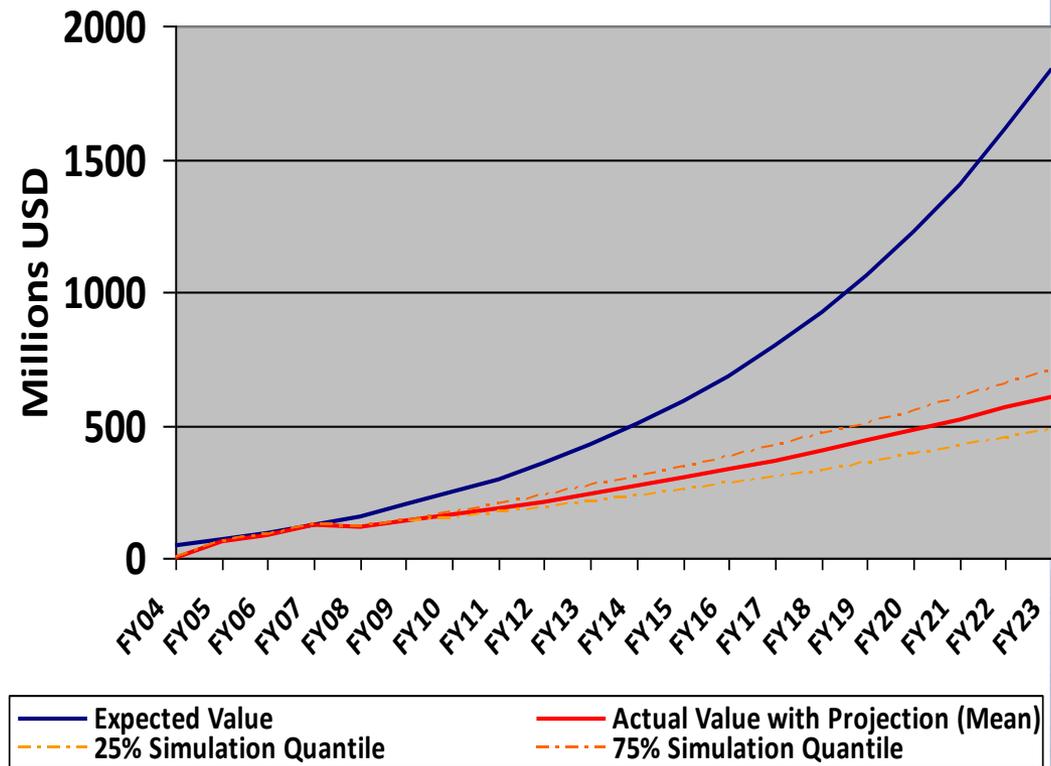
Real GDP Projections



The Compact Trust

- The Compact Trust is currently some \$55 million, or 40% below, its expected value.
- The Trust growth path was never realistic- based on assumptions of roughly 12% annual growth.
- Under a plausible growth strategy the Trust will have a terminal value of \$984 million, some \$850 million below the projected valued.
- Assuming optimistic growth, the Trust would still need additional annual contributions of \$12.5 million to avoid recession in Fy2024.

Actual and Expected Trust Fund Performance



Trust Fund & the College

- Trust funds based on compact sector grants
- Trust fund never intended to cover/replace PELL grant, SEG, or other US grants

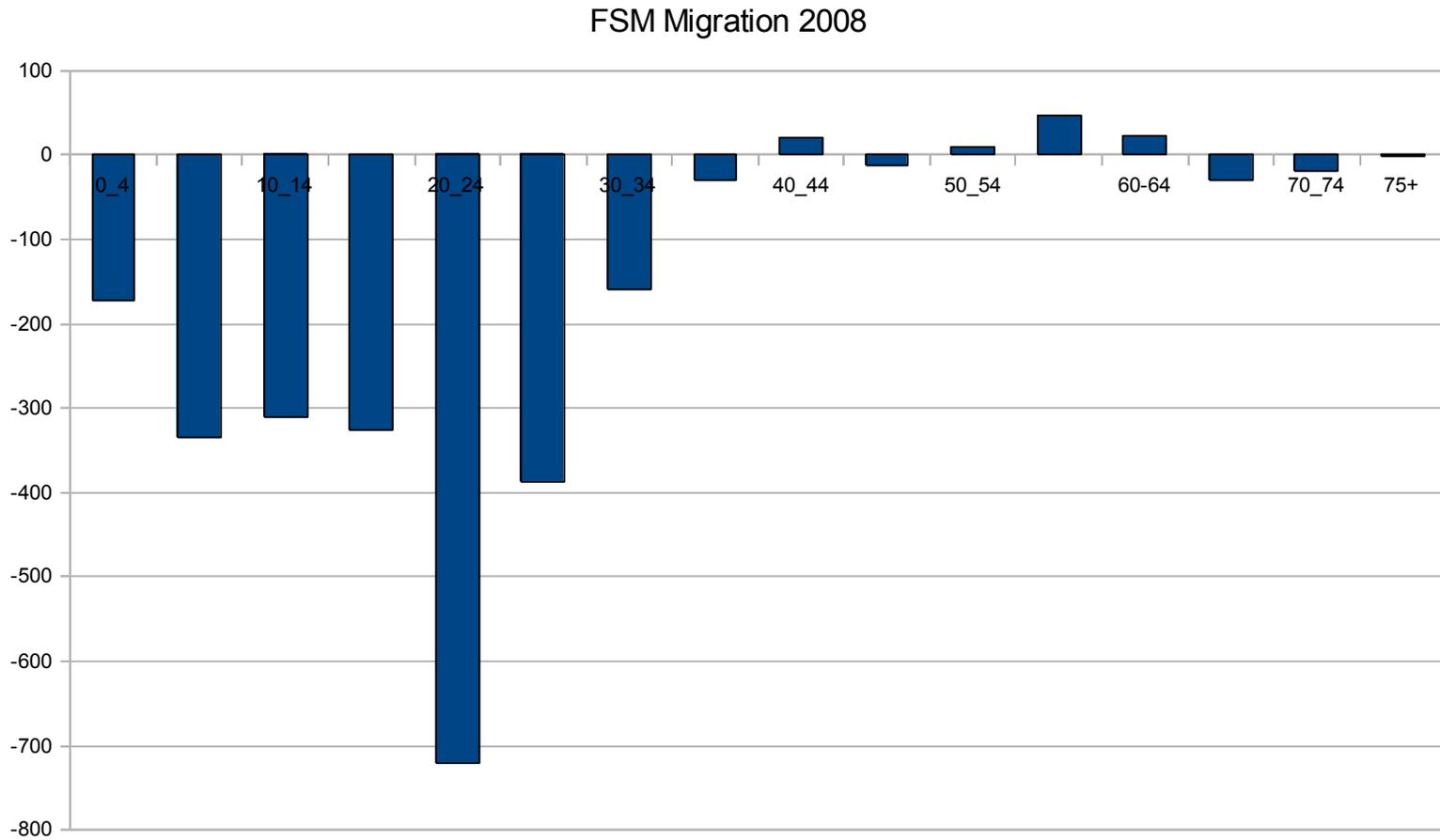
Conclusion

- Implementation of the Amended Compact has not coincided with an improving macroeconomic situation in the FSM.
- In order to move forward the FSM needs to work with the US to ensure the most productive use of remaining Amended Compact sector grants.
- Economic self-sufficiency can only be achieved with private sector development, which requires:
 - Institutions
 - Infrastructure
 - Investment
- Even under optimistic growth projections, the FSM will still face a significant recession in Fy2024 due to the underfunding of the Compact Trust. Addressing this inevitability should be a priority for both the FSM and the US.

Migration Trends

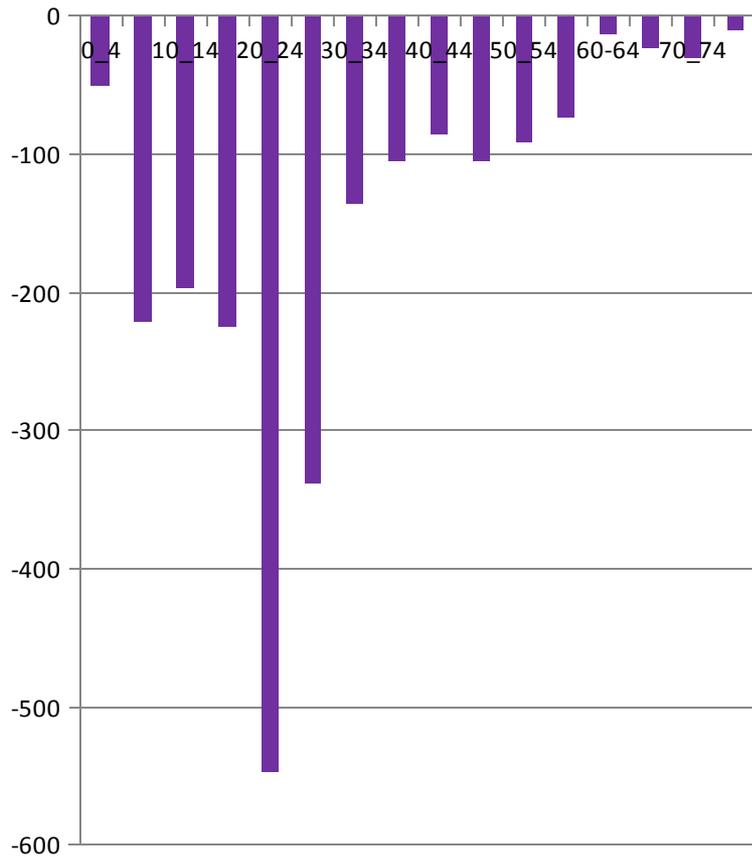
Data from FSM Statistics

FSM Migration 2008

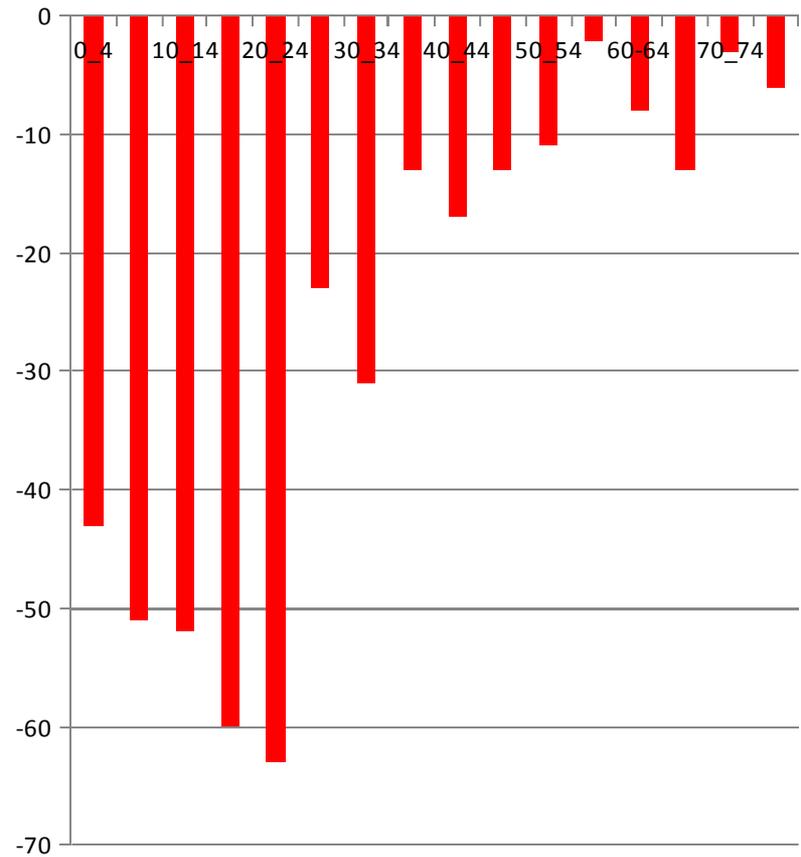


Chuuk & Kosrae 2008

Chuuk Migration Trends 2008

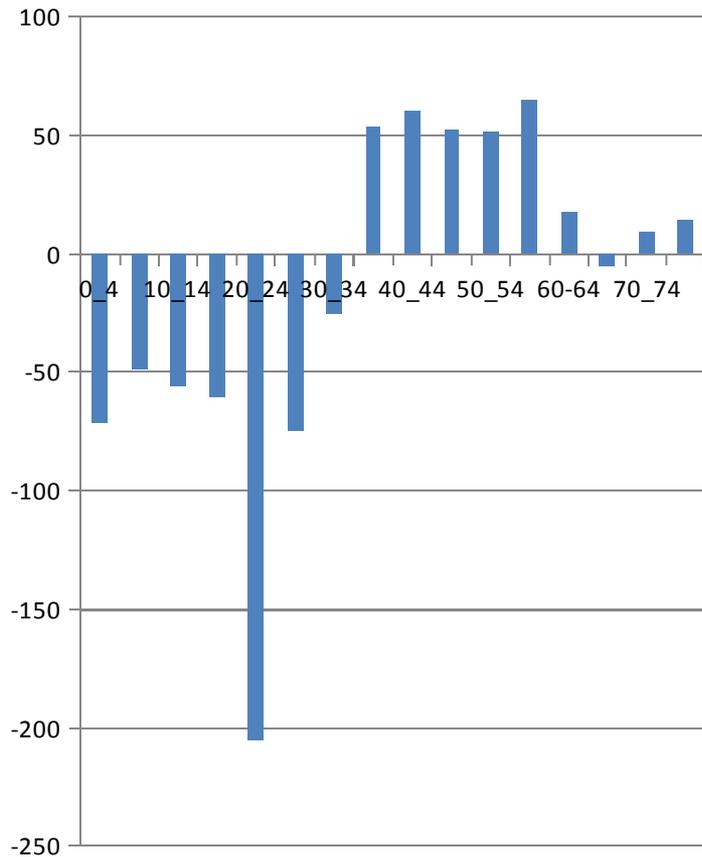


Kosrae Migration Trends 2008

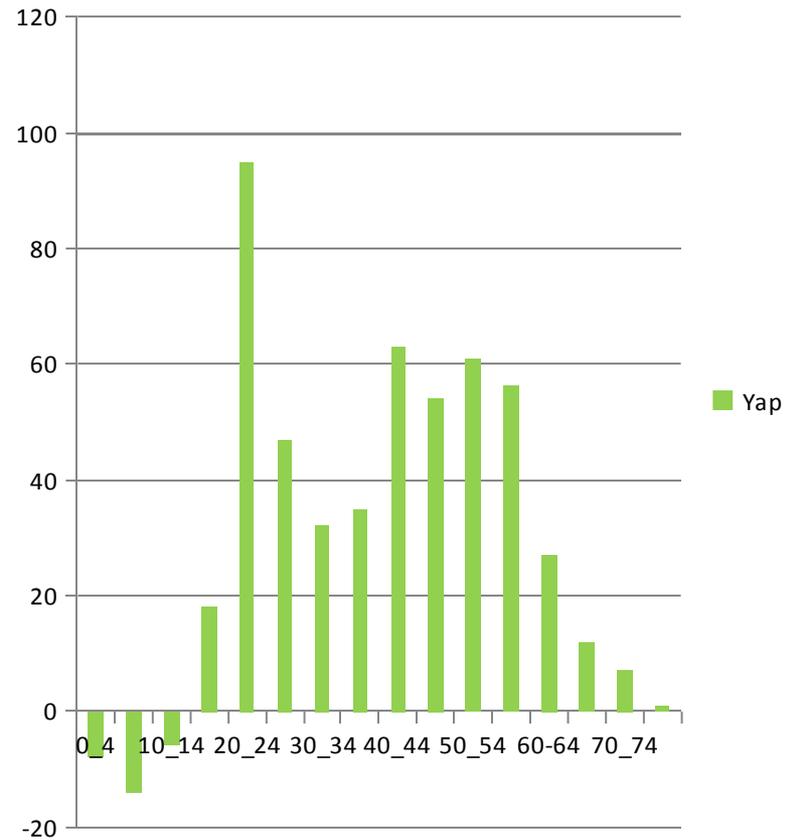


Pohnpei & Yap 2008

Pohnpei Migration Trends 2008

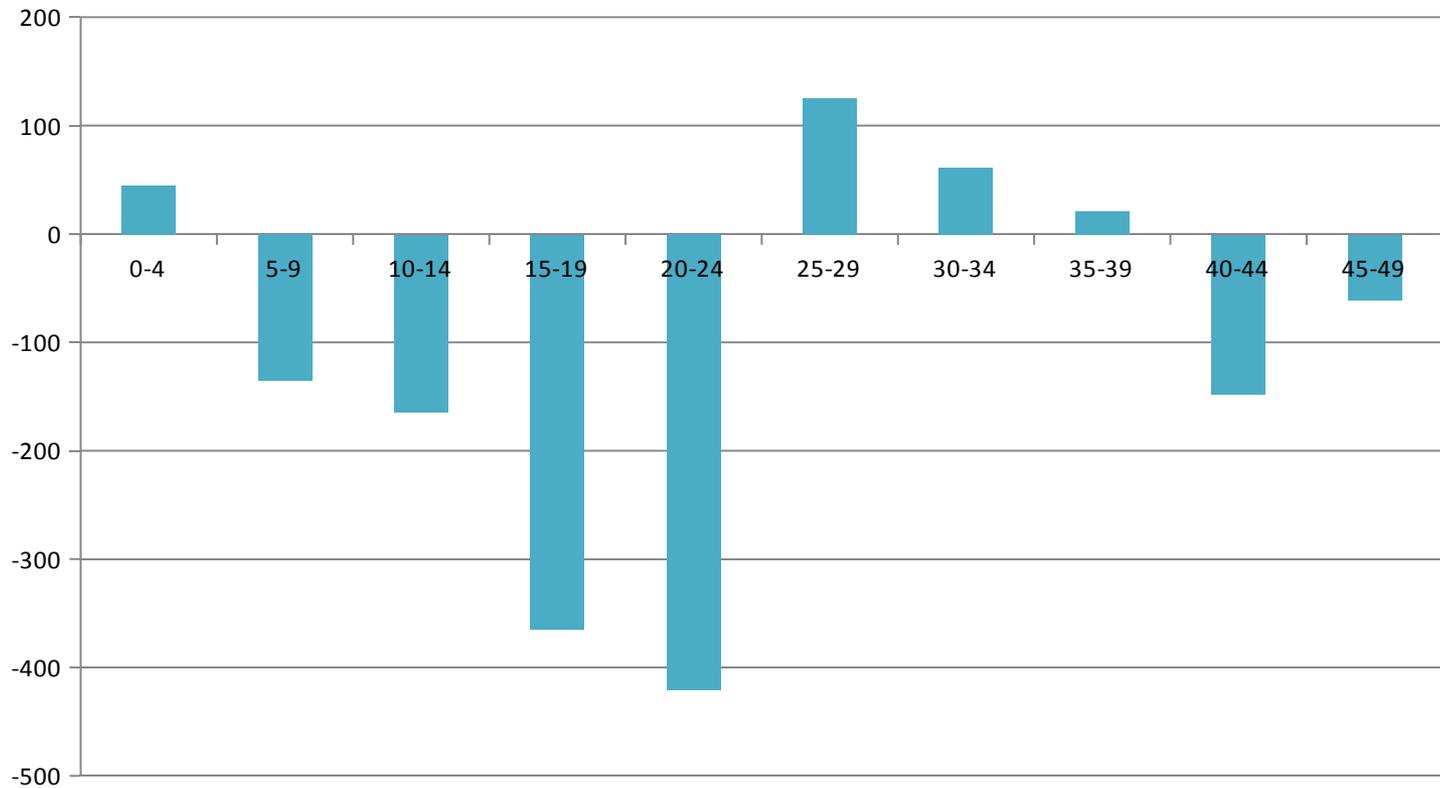


Yap Migration Trends 2008



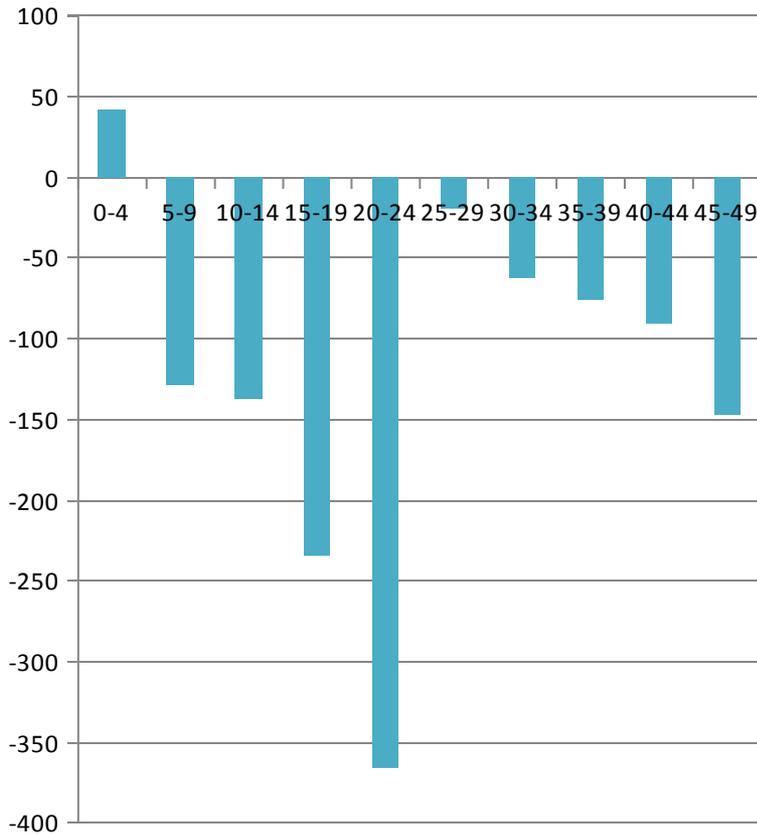
FSM Net Migration 2009

FSM Migration Trends 2009

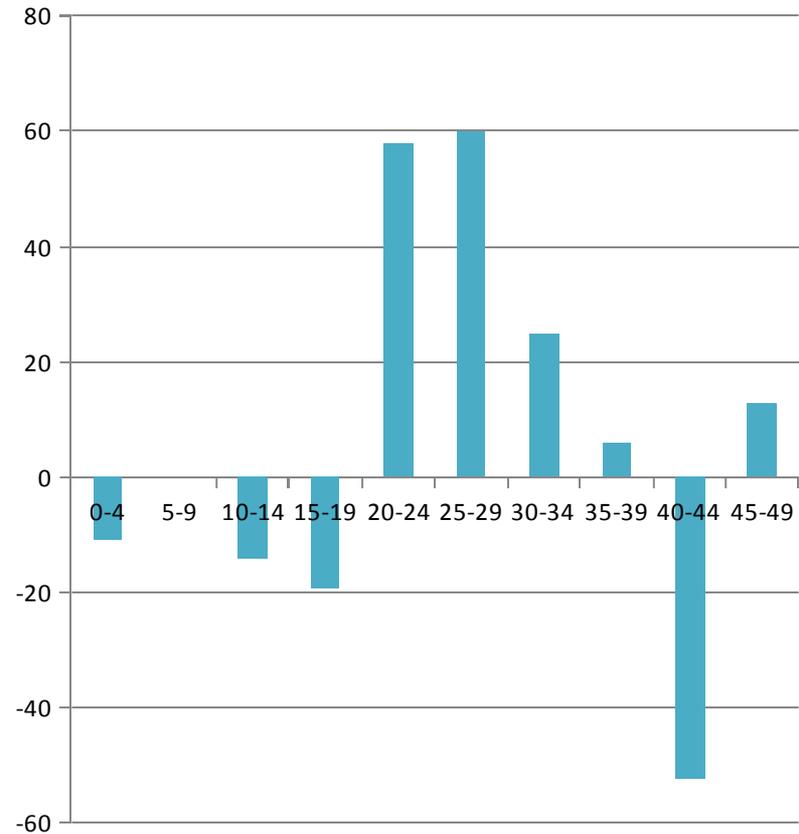


Chuuk & Kosrae 2009

Chuuk Migration Trends 2009

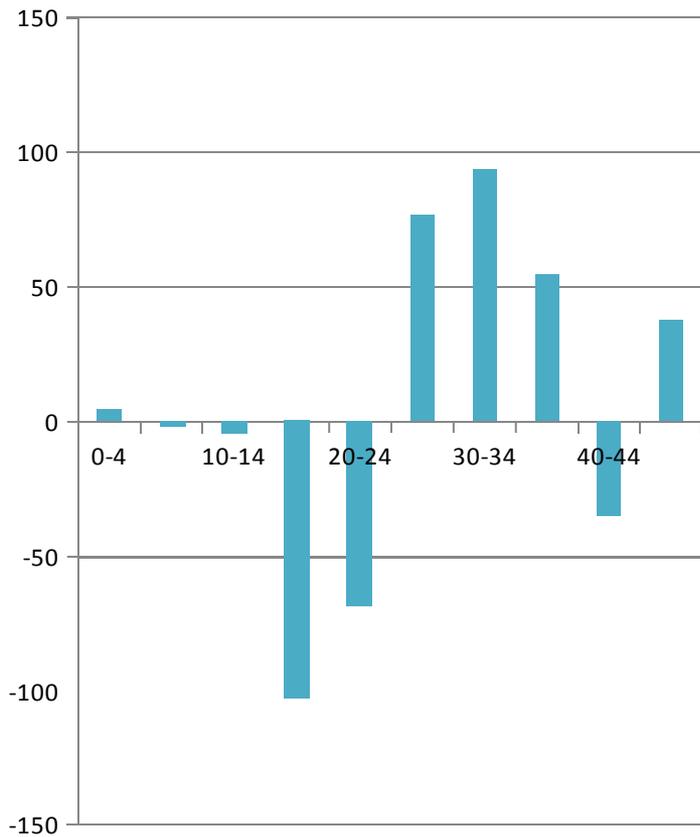


Kosrae Migration Trends 2009

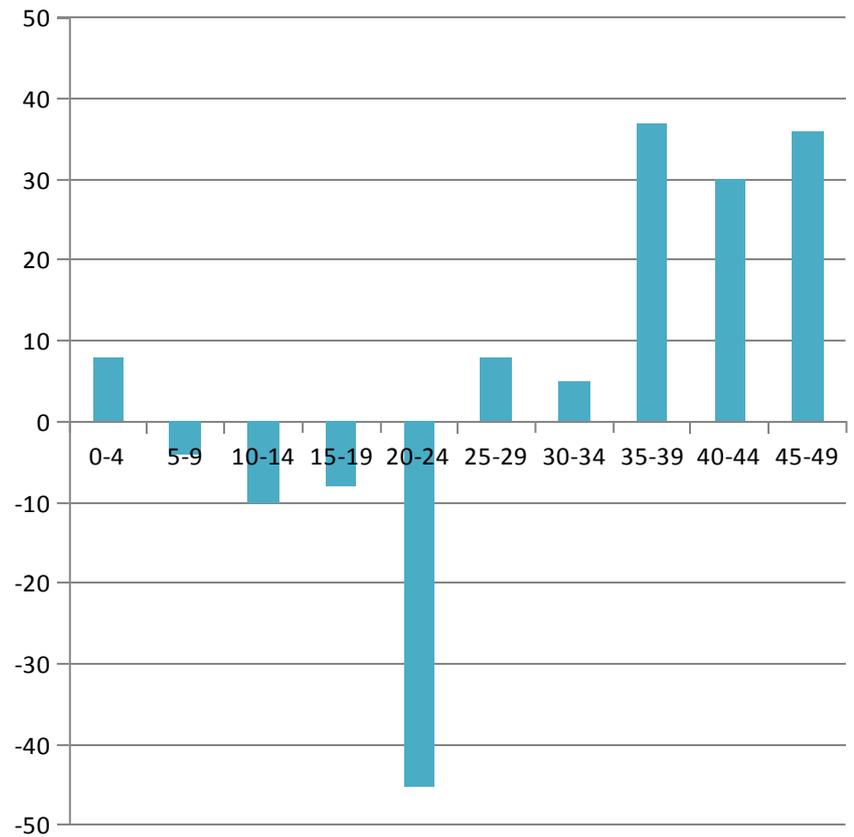


Pohnpei & Yap 2009

Pohnpei Migration Trends 2009



Yap Migration Trends 2009

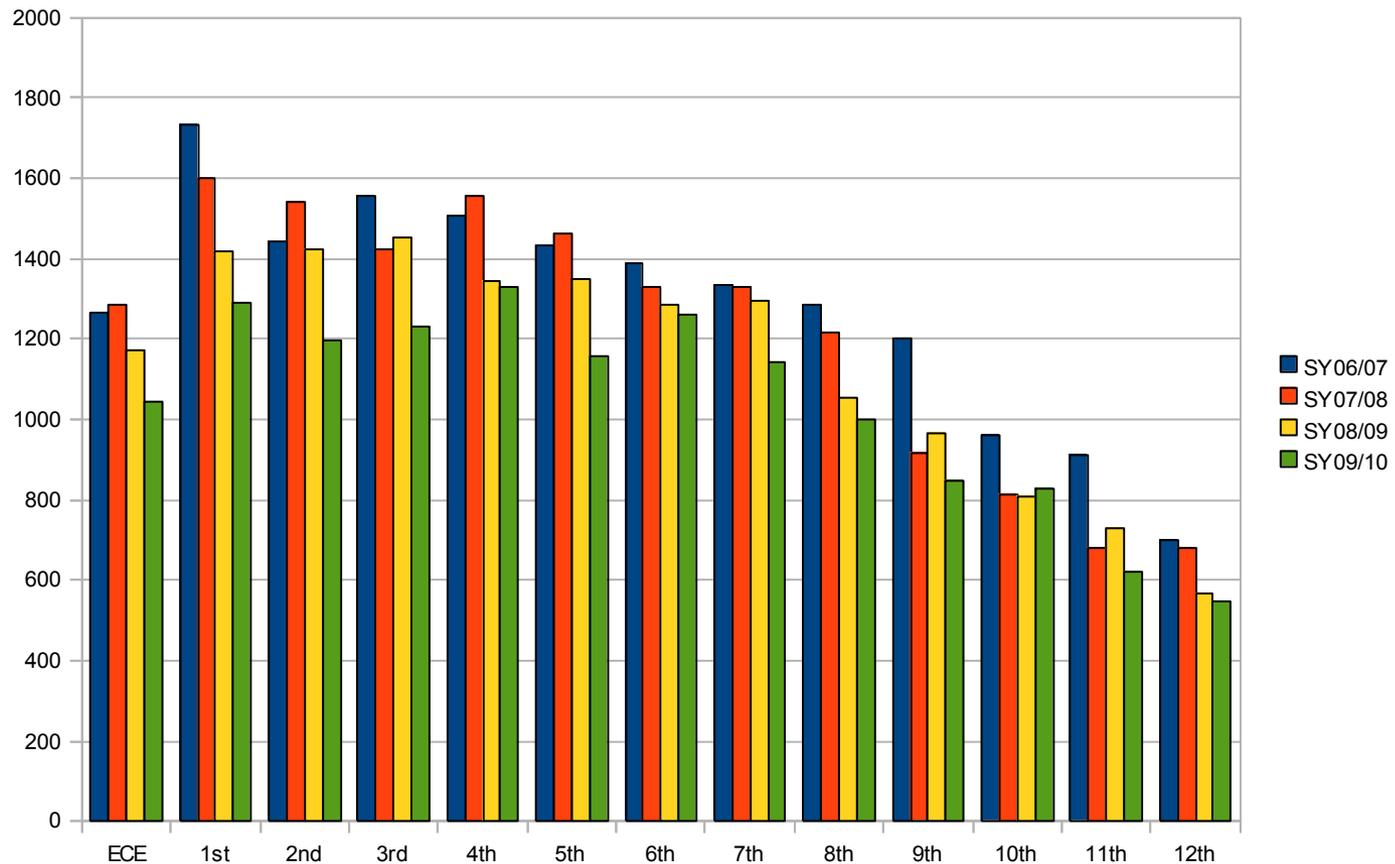


ECE – 12 Enrollment

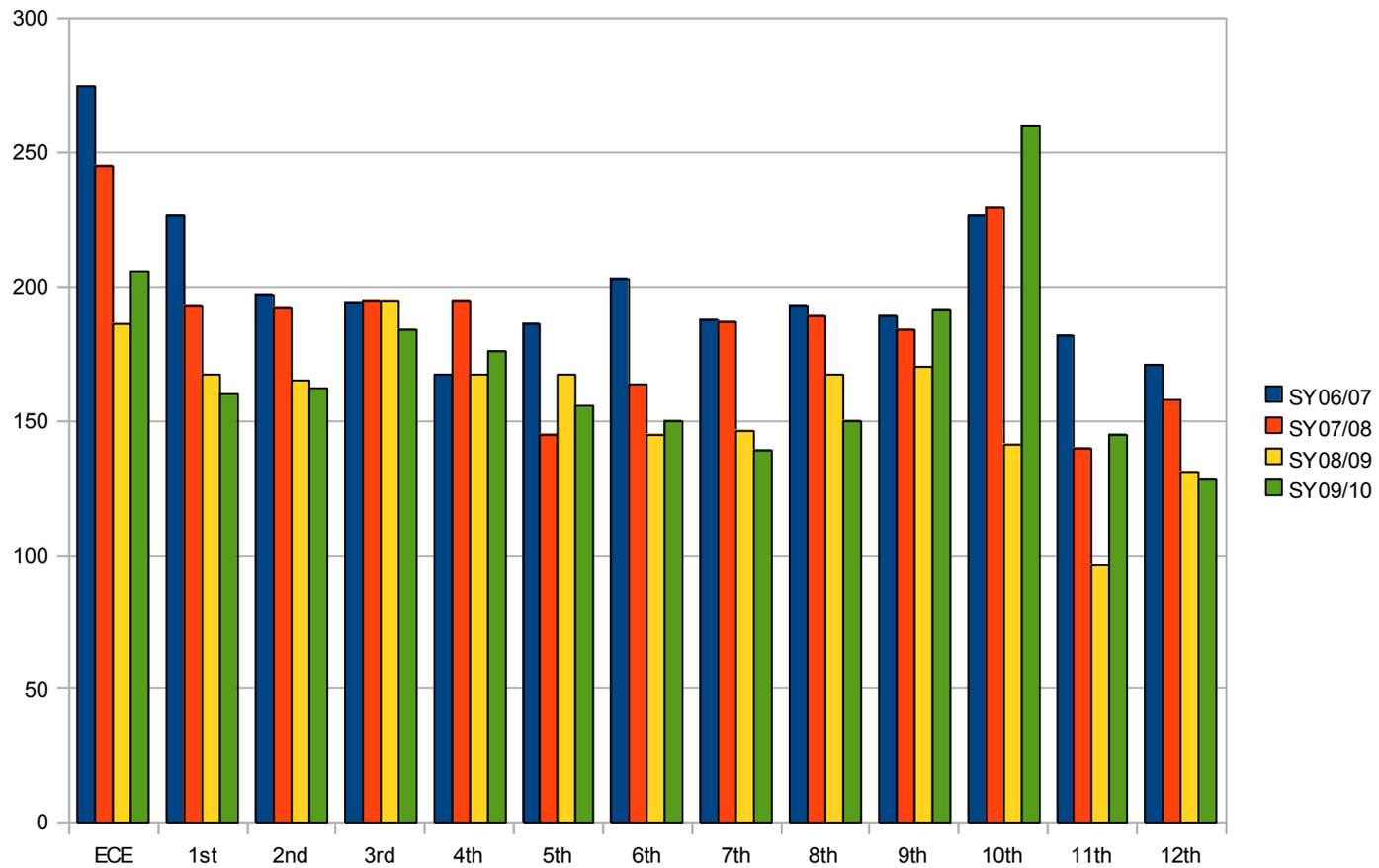
Data from FSM NDOE

Chuuk Enrollment Trends

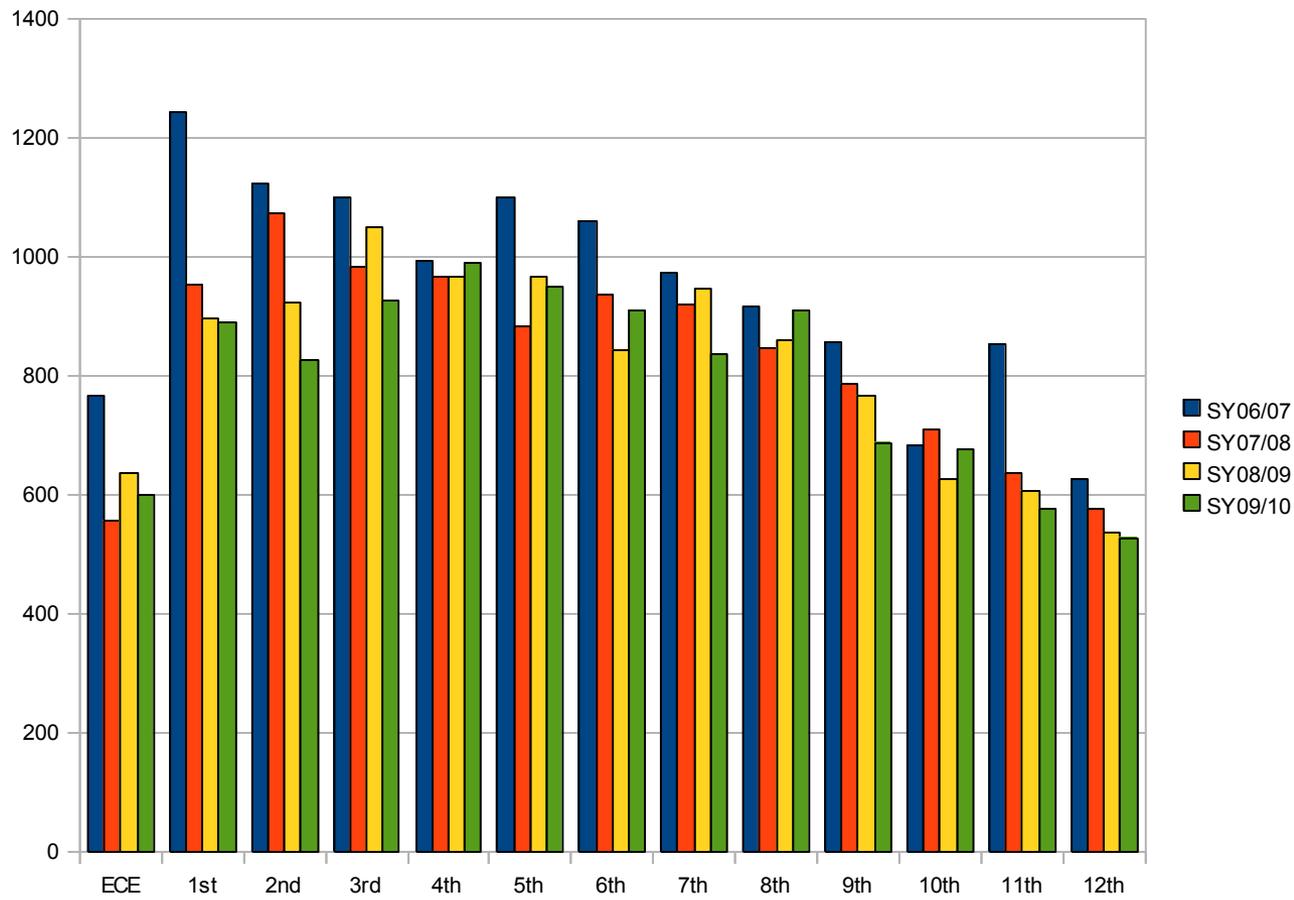
Chuuk ECE - 12 Enrollment Trends



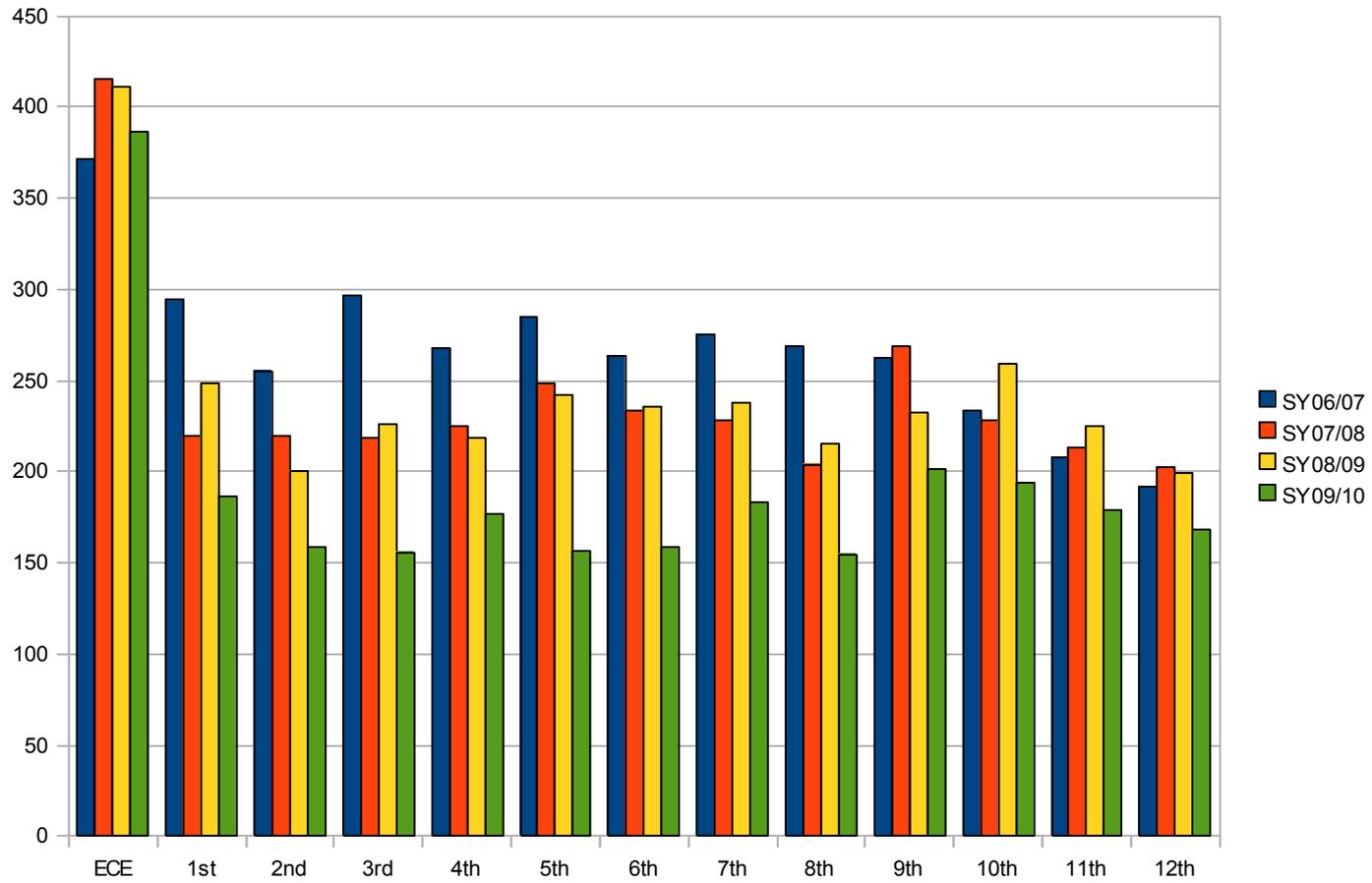
Kosrae Enrollment Trends



Pohnpei Enrollment Trends



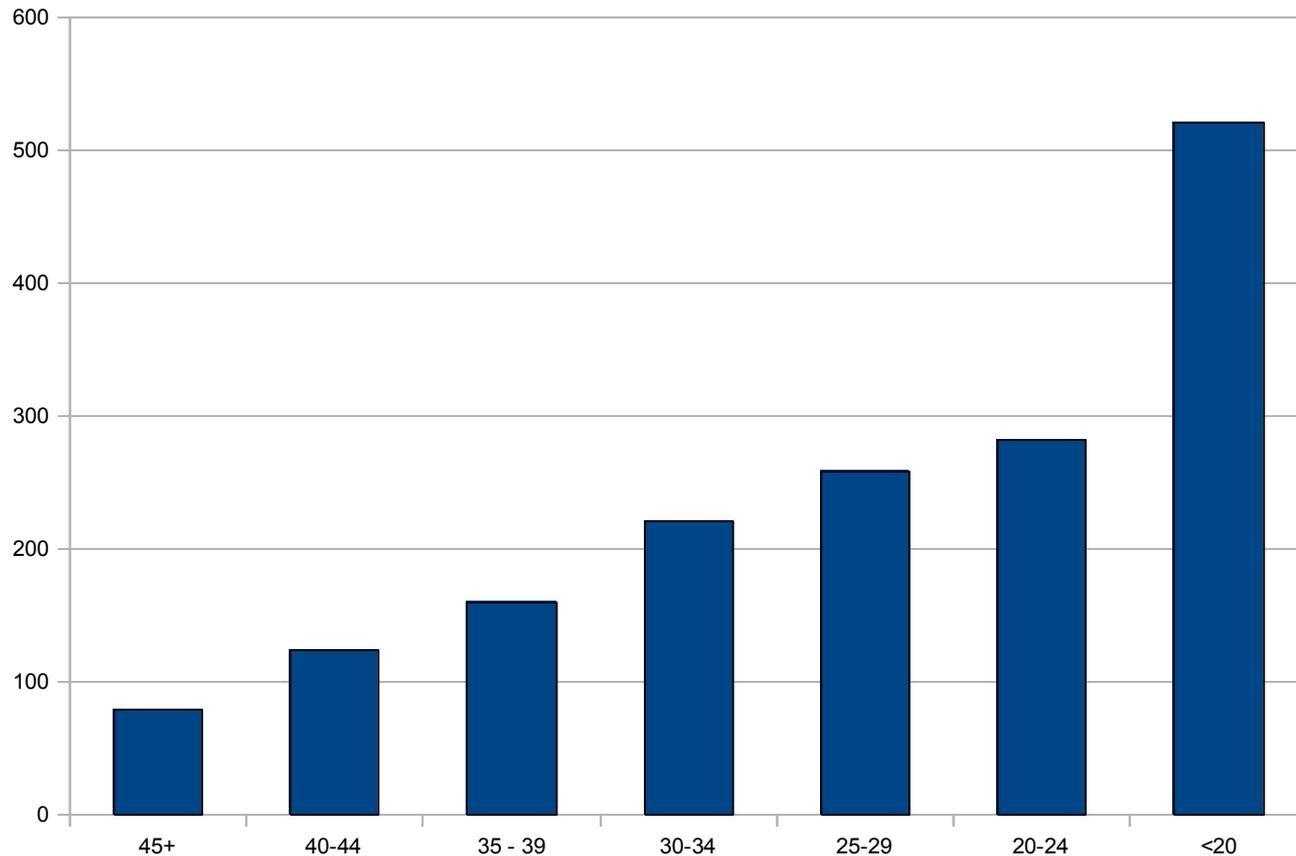
Yap Enrollment Trends



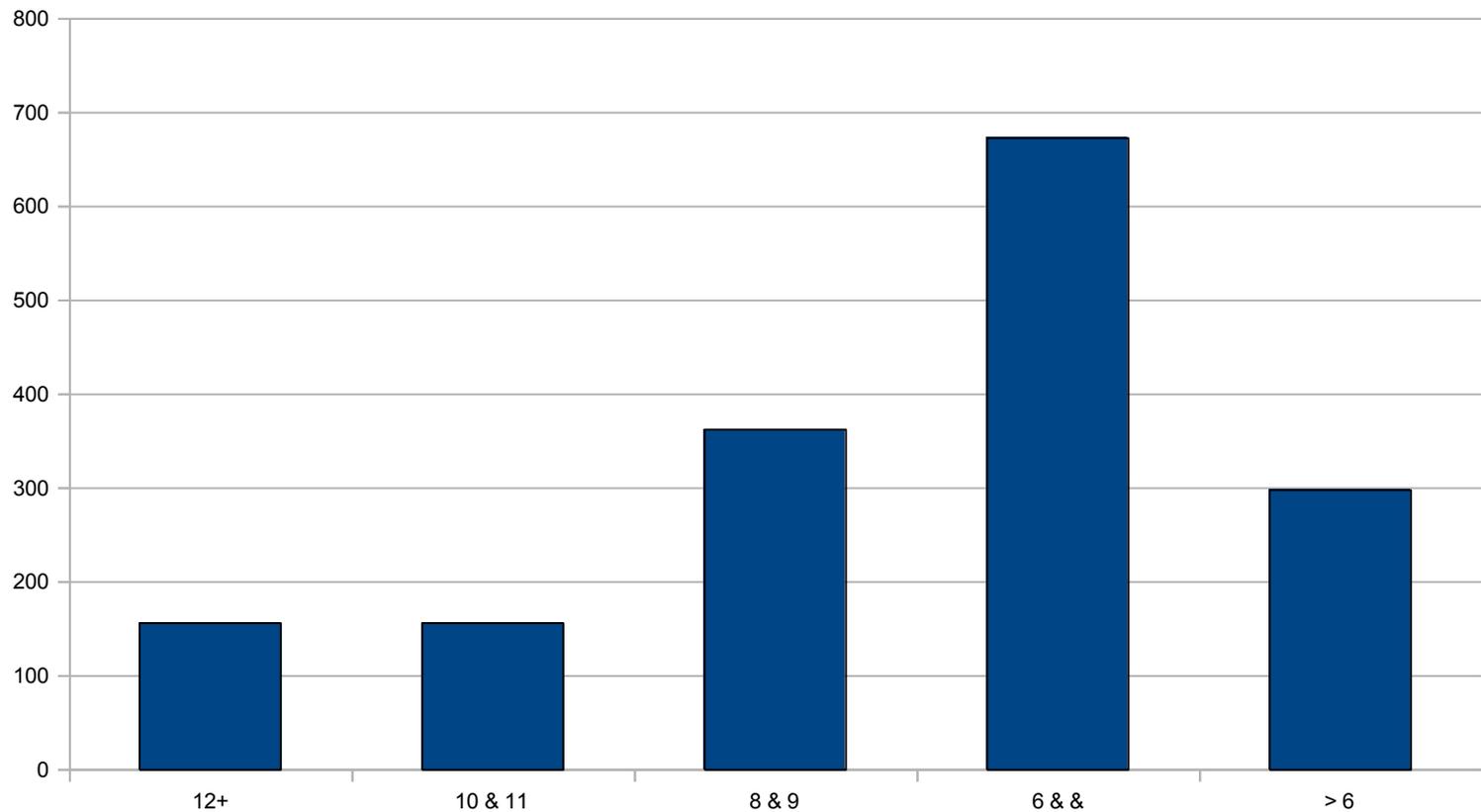
**College Readiness of HS Graduates SY
09/10 – COMET Data
(regular testing)**

COMET Essay Distribution

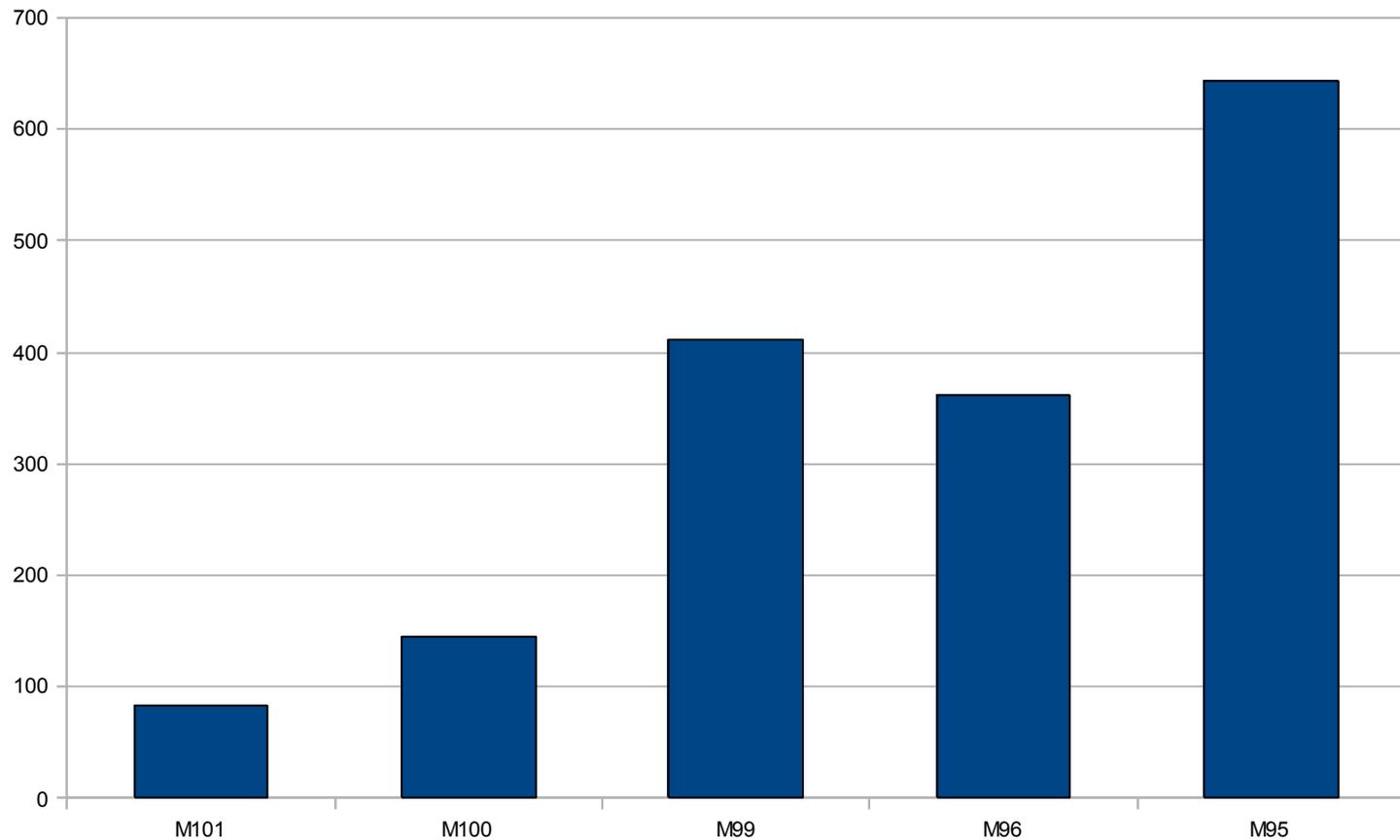
COMET Essay Distrubtion 2010 (regular)



COMET GE Comprehension 2010 (regular)



COMET Math Placement 2010 (regular)



US Military Recruitment of FSM Citizens

Some Issues

- FSM Army Recruitment – Higher per capita than any US State
- Reasons
 - See the world
 - Steady paycheck
 - Pay for college
- Approximately 1000 – 1500 FSM citizens in US military
- Military - hope for upward movement

IDP & JEMCO

Resolution JEMCO 2010-5 Infrastructure Program Management

JEMCO further resolves that Compact-funded design and associated preliminary engineering work for the following College of Micronesia projects: 1) Chuuk Campus - College of Micronesia Phase 1; 2) Chuuk Campus - College of Micronesia Phase 2; 3) National Campus - College of Micronesia Student Center; 4) Pohnpei Campus – College of Micronesia Vocational Center and Classroom Building; shall be suspended until the FSM submits and the JEMCO accepts the Western Association of Schools and Colleges (WASC) - approved College of Micronesia restructuring plan.

FSM PMU Planning

- PMU planning for national share of IDP (non college)
 - Sekere bridges ~\$800K
 - Mufti-function building at Palikir ~\$3M
 - Outer Island Airfields ~\$5M
 - 4+ years of IDP funding in the about projects - Other?
- **Issue – 1) How much additional IDP funding will be available for the college?**
2) Impact on current plans?

Resolution JEMCO 2010-6 Special Grant Terms and Conditions

e) A sum of \$20,000 (from the \$3,800,000 provided to the College of Micronesia) shall be allocated to support agriculture extension activities. The specific activities shall be submitted in project-based format to the Office of SBOC and Office of Insular Affairs for review and concurrence prior to the release of funding (\$20,000).