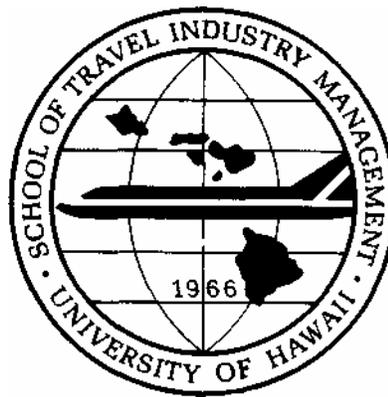


TOURISM DEVELOPMENT IN THE FEDERATED STATES OF MICRONESIA



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EXECUTIVE SUMMARY

1.0 Introduction

In the Pacific region and elsewhere in the world, tourism represents a major alternative for small island nations searching for industries to increase their economic base, expand foreign exchange earnings, and enhance the standard of living for their people. While tourism is expected to grow moderately in the next decade for Pacific island destinations as a whole, the impact will vary among the islands according to the stage of development. In order to address outstanding current and future policy issues related to tourism development in the Pacific region, the Pacific Islands Development Program (PIDP) of the East-West Center initiated the "Multinational Corporations in the Pacific Islands Tourism Industry" research project in 1987. To conduct the study, PIDP contracted the School of Travel Industry Management (TIM) of the University of Hawaii-Manoa (UHM) to analyze ten Pacific island destinations grouped by geographical proximity and selected for criteria based on visitor arrivals and levels of development. This study covers the Federated States of Micronesia (FSM).

2.0 General Overview

The Federated States of Micronesia (FSM) encompass most of the island groups which form the Caroline Islands Archipelago. Discovered by European explorers in the 16th century, the Carolines were claimed by both Spain and Germany toward the end of the 1800s. Spain eventually gained control and administered the islands from 1885 to 1898. Germany purchased the Carolines from Spain in 1898, and German administration extended to 1914 when Japan seized the islands at the beginning of WW I. American administration began in 1947 when the Carolines became a part of the Trust Territory of the Pacific Islands, a Trusteeship established by the United Nations following WW II. In 1965, the various island groups comprising the Trust Territory formed the Congress of Micronesia, an initial step toward self-government. With the subsequent establishment of the Future Political Status Commission by the U.S. Congress, negotiations began toward attaining the political relationship of free association with the U.S. Three of the six districts of the Trust Territory-Pohnpei, Truk, and Yap in 1978 approved a constitution creating the Federated States of Micronesia, and after further negotiations executed a Compact of Free Association with the U.S. which became effective November 1986.

Covering more than a million square miles of the Western Pacific, the FSM encompasses more than 600 small islands, with a total land area of 271 square miles and a population of 94,500. Truk is the most populous state with 47,700 residents, followed by Pohnpei (28,800), Yap (11,300) and Kosrae (6,700). Population growth has been rapid in all of the states, and since 1980 the national rate of growth has averaged 3.6 percent per annum. In some areas of the nation, particularly in Truk state, high population density has become a matter of concern.

Agriculture and fisheries, largely at the subsistence level, represent the largest sector of the economy, accounting for about 42 percent of the national GDP of S 106.5 million 1983. Government services (\$31.5 million) and wholesale and retail trade, (\$12.7 million) accounting for 30 and 12 percent of GDP, respectively, were the second and third ranking sectors. The FSM economy is characterized by several fundamental imbalances. The public sector dominates the economy, accounting for more than half of all money sector employment. Imports (\$58.5 million in 1983) far exceed exports (\$3.6 in 1983), resulting in a large balance of payments deficit which is offset by U.S. government expenditures. In 1983, the \$67.5 million in U.S. assistance amounted to about 76 percent of total private consumption in the FSM.

Based on 1980 census data, the estimated labor force of the FSM was about 25,100, of which about 5,500 (22 percent) were unemployed. With respect to education, school attendance is compulsory through grade 8 (or age 15). It is estimated that about 90 percent of the FSM elementary age population is enrolled in school, but at the secondary level enrollment totals only about 45 percent of the population ages 15-18 yrs. because of a lack of teachers and facilities. Total enrollment of FSM students in post-secondary institutions has been roughly estimated at 5,700, mostly in U.S. institutions outside of Micronesia.

3.0 Tourism Development Assessment

The FSM tourism industry is relatively small with only 14,740 visitor arrivals in 1987. Visitor arrivals among the states vary with Pohnpei (5,670) and Truk (5,060) attracting the largest number in 1987, followed by Yap (2,140) and Kosrae (1,870). Compared with 1980, total FSM visitor arrivals have increased 34 percent, representing an average annual growth rate of 4.3 percent. The principal tourism markets of the FSM are the U.S and Japan, the former accounting for about 60 percent and the latter about 25 percent of total international visitor arrivals. Roughly 5 percent of all visitors come from Europe, and the remaining 10 percent came from other Pacific islands and Asian countries. Roughly a third of all visitors come to the FSM on government or private business with most of the balance coming for pleasure purposes.

A projected average annual growth of 10 percent in non-Micronesian visitor arrivals during the period 1988-1995 is believed reasonable, assuming government action to relieve identified growth constraints. The projected number of non-Micronesian visitors in 1995 is 31,600, with arrivals by state as follows: Kosrae (4,000), Pohnpei (12,200), Truk (10,800), and Yap (4,600). Continental Air Micronesia is the only airline providing regularly scheduled international service. Utilizing the Boeing 727, seat capacity in mid-1988 was about 28,400 on the 12 flights per week entering and departing the FSM. Four of the 12 flights originated in Guam and served only Pohnpei and Truk, while Yap and Kosrae had more limited capacity. Although there is no firm evidence that limited seat capacity constrains the number of visitors to the FSM, there is little doubt that future growth will depend on increasing capacity. Expensive regular air fares discourage travel to the FSM, and therefore any action which results in lowering average fares is likely to increase the number of visitors to the FSM.

4.0 Tourism Resources Assessment

The nation's 16 hotels included a total room inventory of 272 units in mid-1988. Relative to the 226 room inventory in 1980, there has been a 20 percent increase or 46 additional units. No statistics on occupancy rates are available, but estimates made for 1985 indicate that overall, average annual occupancy rates have been below 60 percent. To accommodate projected growth in both non-Micronesian (10 percent per annum growth) and Micronesian (5 percent per annum growth) visitors, a modest net increase of about 60 hotel room units is projected for 1995. With the projected growth in visitors, an increasing proportion can be expected to demand higher quality accommodations which should result in the replacement of the existing room inventory with newly constructed units.

While each of the states has identified sites which can be developed into scenic, historic, or recreational attractions for visitors, very few have been developed. Most potential sites are inaccessible or difficult for tourists to find, are not maintained, or not made known to tourists through the availability of informative brochures. Handicrafts and other local products of interest to tourists are also in short supply. The infrastructure in each of the states currently is insufficient to support sustained growth in tourism. Water

and sewerage systems in particular are substandard, and defects together with insufficient capacity act to increase the incidence of diarrheal, cholera, and other diseases related to contaminated water. These diseases may directly affect visitors with a potentially harmful impact on the industry. Increased capacity and improved service will also be required in electrical power systems, roads, and airport terminal facilities, the latter primarily in regard to Truk and Yap.

5.0 Economic Assessment

The economic benefits associated with visitor expenditures include the generation of employment, income, export earnings, and government revenue. Additionally, growth in tourism brings increased diversification in the economy and improved infrastructure. Visitor expenditures in 1985 were estimated to be \$3.4 million, and direct tourism sector employment totalled about 400. While estimates of government tax revenue generated by tourism have not been made, a part of the \$3.4 million visitor expenditures accrues to the national and state governments through the payment of income, gross revenue, import and hotel room taxes. Diversification in the economy is illustrated by the business activity generated by visitor expenditures, indirect economic benefits are realized through multiplier effects which occur as visitor spending flows into other sectors of the economy. To the extent import leakages are minimized, multiplier effects are greatest in generating indirect employment, income, and tax revenues. Import leakages may be reduced by promoting the domestic production of goods and services consumed by visitors.

Economic costs also are associated with tourism development. In the FSM, the potential costs which are likely to be most significant are the risk of unproductive government investment in tourism and loss of domestic control of tourism development to foreign investors. Unproductive investment occurs when government invests in costly projects which subsequently are underutilized or do not effectively serve their original purpose. Loss of control of development to foreign investors may result in economic losses when operating policies emphasize employment of foreigners, repatriation of profits, and market control which ties services to subsidiary companies.

6.0 Social and Cultural Assessment

The potential adverse impact of tourism development on traditional values and lifestyles is of great concern in the FSM. The pace and scale of development, control of land, expectations and interests of tourists, and lack of knowledge about tourism and the skills needed to work in the industry are among the specific concerns. It is generally agreed that tourism growth should be gradual and that development should emphasize smaller scale, lower density resort/hotel facilities. Although foreign investment is regulated and land cannot be owned by non-citizens of the FSM, foreign investors may obtain long-term leases to privately owned land. There is a dilemma in that outside capital is needed to develop tourism and achieve a sustained rate of growth, but in encouraging foreign investment, residents may lose control of land use. In regard to dealing with tourists and understanding what is involved in developing the tourism sector, community awareness programs are not currently available. Industry employee training, occupational as well as cross-cultural, is also limited.

7.0 Government Tourism Policy Assessment

National government tourism development policy has been expressed in the First National Development Plan, 1985-1989, prepared in 1984. Tourism objectives, policies, and development strategies are summarized in the National Development Plan as one of 18

sectoral plans. National policy supports the gradual and controlled expansion of tourism with national and state development efforts to be integrated and carefully planned. The type of tourism development sought is one based on inherent natural, cultural, and historic attractions of the FSM, and marketing is to be aimed at attracting tourists most likely to appreciate and respect the type of attractions promoted. While growth constraints, problems, and concerns are briefly mentioned, the sectoral plan was not intended to fully address these issues. Yap is the only state which has prepared a comprehensive tourism development plan. The Yap State Comprehensive Tourism Plan is consistent with the policies contained in the National Development Plan in presenting detailed recommendations emphasizing small-scale tourism which minimizes impact on traditional culture.

The relatively small, capital short private sector of the FSM places a heavier burden on government to support economic development. Since the tax base is correspondingly small, the FSM depends heavily on external resources which come primarily from U.S. Compact funding. The national government receives Compact funds and other foreign assistance distributing the majority of funds to the state governments. Currently, there are no means for tracking the level of support and the particular objectives of tourism development expenditures for the nation as a whole. To effectively plan and administer an integrated tourism development program in the FSM, this function must be performed. The heavy dependence on external capital also underscores what is needed with respect to tourism. The burden of constructing hotels and other facilities which directly serve visitors essentially is borne by the private sector, and there is need for private foreign investment in tourism. Both national and state government currently are involved in the regulation of foreign investment in tourism which poses some problems to foreign corporations. The problems of determining and coordinating government incentives for tourism and creating a favorable climate for foreign investment illustrate the need for a national/state organizational structure which delineates the respective roles of each level of government and provides for the linkages needed to effectively promote tourism development.

8.0 Summary and Recommendations

International Travel Access

Increased air carrier seat capacity and especially reduced air fares would stimulate tourist travel to the FSM. The addition by Air Micronesia of twice weekly, special reduced fare flights to Pohnpei and Truk from Guam appears to have had this effect. In conjunction with growth in hotel accommodations, the introduction of air charter service dedicated to specific hotels would introduce an element of competition which in turn is likely to have a positive effect on fares and capacity. It is recommended that the FSM National Government (FSMNG):

- Request Air Micronesia introduce special reduced fares on flights originating in Honolulu.
- Encourage and support hotel developers and industry to obtain charter service from U.S. or Japanese airlines.

Facility Requirements

In the 1988-1995 period, projected growth in visitor arrivals will create the demand for additional hotel rooms. With increased development, tourists will expect higher quality accommodations which will generate new construction to replace the existing inventory as well as add new units. An estimated 130-190 new units are projected. That portion of existing inventory not needed for hotel use could be converted to long-term residential use. Additional visitor attractions also are needed. Relatively few identified scenic, historic and

other sites are available to tourists. It is recommended that FSM State Governments (FSMSG):

- Implement policies designed to encourage and facilitate the conversion of a part of the existing accommodations inventory to long-term rental units.
- Set specific annual targets for the number of identified sites to be developed, implement maintenance programs to keep all developed sites accessible and attractive, and make available to visitors up-to-date brochures which locate and explain sites.

Infrastructure

There are major shortcomings in infrastructure needed to support tourism, particularly with respect to water and sewerage systems. IN some areas such as Moen, limited water resources may constrain future growth in tourism. It is recommended that FSMSG:

- Identify water, sewerage and other infrastructure projects in their tourism development master plans and describe the benefits of each project in terms of eliminating or mitigating existing problems.
- Implement infrastructure standards to be incorporated in zoning and land use controls applicable to future resort zoned land.
- Prohibit the construction of hotels on land not zoned for such uses, and identify environmentally sensitive areas which cannot be zoned for resort use.

Market Segments

It is estimated that U.S. and Japanese markets account for about 85 percent of all visitors to the FSM on pleasure and business. Statistical data on visitor arrivals are weak because available data are not processed and because of defects in the forms and procedures used to collect the statistics. Information on purpose of visit and other characteristics is largely lacking. Along with the collection of better statistical data, market research is needed to identify market segments having the most potential for travel to the FSM. It is recommended that the FSMNG:

- Redesign the forms and procedures used to collect and compile visitor statistics so that adequate data can be obtained on relevant visitor characteristics.
- Undertake or contract for market research to identify and refine specific segments of the Japanese and U.S. travel markets which have the greatest potential for growth in travel to FSM> Lower priority should be given to assessing the potential of other Asian countries to contribute to tourism growth in the FSM.
- Enter into joint marketing and promotion programs with the Northern Marianas and Guam which promote the diversity of travel attractions in the region. The objective of joint programs is to capture a larger part of the segments of the Japanese market who longer vacations and are interested in adding new destinations to their travel package.

Appropriate Scale of Tourism

Given expressed concern about potential adverse effects on culture, limited land, and fragile ecosystems, small-scale tourism development is appropriate for the FSM. Single projects of more than 100 units generally should be discouraged, and for specially planned

and zoned resort areas consisting of multiple projects, a limit of about 300 units would be appropriate. For Kosrae and Yap, a mix of development which includes smaller hotels and village based guest accommodations may be more appropriate in light of greater concern in these states for maintenance of traditional culture. It is recommended that the FSMNG and FSMSG:

- Define the scale and character of tourism development that is desired and incorporate appropriate criteria in both development master plans and state zoning and land use controls applicable to resort zoned land.

Protection of Natural and Human Environment

Simultaneous with the planning and promotion of growth in the FSM tourist industry, government must provide for explicit policies and guidelines for hotel and other tourism facility development. Resort building densities, sewage treatment and disposal regulations, building design standards, and other facility-related regulations should be implemented before significant growth has occurred. One of the most significant functions of the state tourism master plans is the identification of specific areas in which tourism facilities could be built. It is recommended that the FSMSG, with the coordination and technical assistance from the FSMNG:

- Implement land use policies and controls which specifically address environmental and socio-cultural concerns.
- Identify specific areas within each state where resort and hotel zoning would be permitted.
- In cooperation with private developers and land owners, purchase land which is to be zoned for resort use, negotiating long-term lease rent and land use conditions to be made a part of state leases to hotel developers.

Foreign Investment

Because the FSM is a capital-short area with respect to both private and government sources of funding, foreign investment will be needed to meet tourism growth objectives. An explicit policy statement on foreign investment should be included in the national tourism master plan, and guidelines clarifying the terms and conditions for tourism investment projects approval should be issued. Investors should only have to obtain approval from the national government. With input from FSMSG and industry, it is recommended that the FSMNG:

- Include a policy statement in the national tourism master plan which encourages foreign investment in accordance with specific tourism investment guidelines.
- Issue foreign investment guidelines which are applicable in all states of the FSM. Amend Public Law No. 2-5 to reflect national government jurisdiction in issuing foreign investment permits.

Reducing Leakages

The economic benefits of tourist spending are enhanced to the extent domestically produced goods and services can be substituted for those which otherwise would be imported. In effect, this reduces the amount of visitor spending that would "leak" out of the FSM to pay for imports. Another source of leakages is the repatriation of profits and interest on foreign investment. To the extent joint ventures between domestic and foreign investors can be formed, a larger share of profits and interest are likely to remain in the FSM. It is recommended that FSMSG:

- Establish task forces to identify specific import substitute commodities and services which can be supplied by domestic firms to tourism sector establishments.

It is recommended that the FSMNG:

- Assess the feasibility of providing tax or loan program incentives to encourage domestic-foreign investor joint ventures in the tourism sector.

Strengthening Intersectoral Linkages

The task forces recommended for reducing import leakages must be organizationally positioned to work effectively with the tourism industry. While commodities and services would be supplied by other FSM sectors such as agriculture and manufacturing, linkages would need to be formed between these sectors and the tourism industry. It is recommended that FSMNG:

- Include an import substitute task force within each of the state tourist advisory boards or tourist commissions.

Protecting Traditional Cultures

Each of the states has a distinct traditional culture. Promoting a moderate pace of tourism growth together with smaller scale hotel/resort projects should minimize the impact on traditional culture. Foreign investment guidelines and state land use controls also would contain provisions that would minimize adverse cultural impacts. Within local communities, land tenure can be a particularly sensitive culturally related issue. Since the state would be the party issuing long-term leases to investors, individual projects should be reviewed with respect to the need for special conditions. It is recommended that FSMNG:

- Insure that proposed tourism projects are reviewed with respect to possible adverse sociocultural effects and impose conditions when necessary, including lease covenants which developers must meet to obtain land use approvals.

Public Awareness of Tourism Development

Public support of tourism development will be necessary to achieve sustained growth in the industry. The development of public education programs should closely follow the completion of state tourism development master plans since the goals and objectives, policies, and analysis contained in the master plans form the basis of the education programs. With technical assistance from the FSMNG, it is recommended that FSMNG:

- Develop and implement public education programs which inform the general public and industry employees of the goals and objectives, benefits, and costs of tourism, and of the interests and expectations of tourists.

Industry Training

Industry training, including the education programs noted in the previous recommendation, are needed not only to assure visitor satisfaction, but also to promote personal job satisfaction and enhance benefits to residents. It is recommended that the FSMNG:

- Provide financial and technical assistance to the states to develop occupational and cross-cultural training programs for tourism industry employees, utilizing the College of Micronesia's (COM) continuing education centers in the states and the Community College of Micronesia (CCM) facilities in Pohnpei.
- Coordinate the organization and implementation of institutional training projects involving trainees from two or more states.

It is recommended that FSMSG:

- Work with tourist industry to develop and implement on-the-job employee training.
- Promote and coordinate industry participation in institutional training projects offered by COM continuing education centers.

Administration of Tourism Development

To effectively promote and support tourism development, the plans, policies and programs of the national and state governments dealing with tourism should be consistent, each contributing to an environment which facilitates the growth and development of private sector tourism activities. This requires a clear delineation of national-state responsibilities, along with appropriate administrative structures at each level of government. The national government would have primary responsibility for: visitor arrivals; foreign aid/technical assistance; relations with regional/international tourism organizations; bilateral agreements affecting tourism; private foreign investment; regulation of foreign corporations; nationally focused marketing/promotion; post-secondary training provided by COM; collection/compilation of tourism-related government expenditure/revenue data (national and state); and facilitating interstate tourist travel. The states would be given primary responsibility for: development/maintenance of tourism sites; zoning and land use controls; marketing and promotion of state tourism; regulation of tourism establishment standards; environmental protection; public utilities/services; public transportation, roads, and parks; public health and sanitation. Shared or joint national-state responsibilities would include: planning and research; public education; business development loans; airport and harbor facilities; and education and training.

In terms of organizational structure at the national level, a National Tourism Office (NTO) would constitute a division within the Department of Resource and Development (R&D), with a staff director reporting directly to the R&D director. To carry out the functions of the NTO (detailed in Appendix A), a three-person professional staff, including the director, would be needed. Private sector participation would occur through tourist industry representation on state advisory boards and tourist commissions, and at the national level by a tourism development board. At the state level, organizational structure should reflect relative size and complexity of the industry. In Kosrae and Yap, planning and administrative functions would remain in the R&D Department. In Pohnpei and Truk, which have larger more diversified industries, the organization structure would include a visitors bureau (or commission, as in Pohnpei) primarily responsible for marketing and promotion and a State Tourism Office which consolidates all other functions and would be situated in one of the executive departments. In these states, industry participation would be through the visitor's bureau. At the national level and in the States of Pohnpei and Truk, funding budgeted in support of tourism development has not been adequate to accomplish objectives contained in the First National Development Plan. It is recommended that the FSMNG:

- Enact a Tourism Development Law which defines the respective functions and responsibilities of the national and state governments and the organizational structure to administer national responsibilities.
- Provide for a distinct budgetary allocation in the state executive budget to operate the NTO.

It is recommended that FSMSG:

- Enact State Tourism Development Acts that are consistent with the provisions of a National Tourism Development Law, and which establish an organizational structure appropriate to the level of tourism development in the state.
- Provide a specific budget allocation in the state executive budget to operate the state tourism offices.

National Development Objectives

Tourism development objectives which are ultimately adopted in the national tourism development plan should reflect the potential in each state to attract and accommodate tourists from overseas markets and the level and quality of tourism activity that is desired in each state. In the delineation of national-state responsibilities, the states would have a strong role in determining the type of tourism to be developed, while national planners would have primary responsibility for the analysis of international travel trends, overseas markets, air service capacity and costs, and other significant factors bearing on growth potential. It is recommended that the FSMNG:

- Prepare a national tourism development master plan which reflects state goals and objectives and input with respect to state tourism growth potential. In developing the national master plan, state tourism planning should be assisted and guided by analyses and projections prepared by the NTO with respect to economic and technical factors for which the NTO compiles and analyzes the basic source data. It is important that national policies and plans reflect industry input which can be provided directly from the National Tourism Development Board and indirectly via state policies and master plans.

It is recommended that FSMSG:

- Prepare state tourism development master plans which are based on state analyses of industry growth potential, taking into account carrying capacity, local community support, and the analyses and projections supplied by the NTO. Policies and plans reflect the input of tourist advisory committees/commissions which represent the industry.

Appendix A - Role of Federal Government in Tourism Planning and Development

Tourism is inherently an international industry as most revenue is generated by visitors from other countries. Air service, customs and immigration, and international business transactions are associated activities which are responsibilities of the national (federal) government, as is interstate commerce. While the national government obviously must have a role in tourism development, the large degree of autonomy accorded the states

in the FSM's federal system of government has brought into question which responsibilities the national government is to perform and how coordination and integration of planning and promotion are to occur. The FSM Constitution provides guidance in delineating national-state responsibilities together with the legal-administrative functions that have been assumed by the national government since the country became independent. Appendix A reviews those responsibilities and functions which are judged to be primarily national and those which would be within the purview of the states. Once the national and state governments have reached agreement on the delineation of tourism development responsibilities, administrative structures are needed to carry out these responsibilities and to promote tourism development. National and state organization structures, including the mechanism for industry participation, are addressed in Appendix A. Legislation in the form of a Tourism Development Act is recommended as the vehicle for defining and endorsing the respective roles of the national and state governments in the administration of tourism development.