



# Country Operations Business Plan

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October 2007

## Federated States of Micronesia 2007–2009

Asian Development Bank

## CURRENCY EQUIVALENTS

The currency of the Federated States of Micronesia is the United States dollar.

## ABBREVIATIONS

|      |   |                                     |
|------|---|-------------------------------------|
| ADB  | – | Asian Development Bank              |
| ADF  | – | Asian Development Fund              |
| ADTA | – | advisory technical assistance       |
| COBP | – | country operations business plan    |
| CPS  | – | country partnership strategy        |
| CSPU | – | country strategy and program update |
| FSM  | – | Federated States of Micronesia      |
| GDP  | – | gross domestic product              |
| RETA | – | regional technical assistance       |
| SDP  | – | Strategic Development Plan          |
| TA   | – | technical assistance                |

## NOTES

- (i) The fiscal year (FY) of the Government and its agencies ends on 30 September.
- (ii) In this report, "\$" refers to US dollars.

|                         |   |
|-------------------------|---|
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## **I. CONSISTENCY OF THE BUSINESS PLAN WITH THE CURRENT COUNTRY PARTNERSHIP STRATEGY**

1. Since the preparation of the Country Strategy and Program Update (CSPU) 2006–2007 of the Asian Development Bank (ADB),<sup>1</sup> the Government of the Federated States of Micronesia (FSM) has experienced a tightening of the fiscal environment, due to stricter controls on the use of Compact of Free Association (Compact) funds, and reductions of \$800,000 annually in Compact grant assistance to FSM from FY2007. This reduction is offset by an equivalent contribution by the United States to the jointly-managed trust fund. The FSM Government (the Government) remains committed to implementation of the Strategic Development Plan 2004–2023: Achieving Economic Growth and Self-Reliance<sup>2</sup> (SDP), viewing this as the most appropriate means to address the current financial difficulties and create a sound foundation for sustained future growth. Implementation progress has been slow, due in part to capacity limitations and the Government's loose federation structure, which has made it difficult to forge a consensus for reform and to coordinate policies.

2. FSM's strained medium-term economic outlook and slow development progress increases the importance of the priority areas—good governance, inclusive social development and pro-poor economic growth—identified in the CSPU 2006–2007. In light of the level of assistance available for FSM, and the slow progress in implementing the CSPU 2006–2007 assistance pipeline, the Country Operations Business Plan (COBP) 2007–2009 acts to further tighten the strategic focus of the CSPU 2006–2007, while remaining consistent with it.

3. ADB's strategy in FSM for 2007–2009 will support the Government's twin SDP goals of economic growth and self reliance through (i) good governance, with a particular focus on economic management and accountability; (ii) ensuring inclusive social development; and (iii) promoting sustained private sector-led economic growth. This strategy contributes to ADB's overarching goal of poverty reduction, is fully consistent with ADB's Pacific Strategy 2005–2009, and supports FSM's continued economic and social development. A joint country partnership strategy (CPS) for FSM will be initiated in 2008. A draft CPS results framework is in Section VI.

## **II. INDICATIVE LENDING AND NONLENDING PROGRAMS**

### **A. Indicative Lending Level**

4. Currently, FSM is a Category B1 country with access to the Asian Development Fund. However, no new lending is currently proposed for 2007–2009. The assistance pipeline will be reviewed during the development of the CPS in 2008.

5. FSM has three ongoing loans.<sup>3</sup> Performance on all has been problematic and Loan 1816-FSM: Basic Social Services Project remains at risk. Loan 1873-FSM: Private Sector Development program has been closed. The single loan included in the CSPU 2006–2007

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<sup>1</sup> ADB. 2005. *Country Strategy and Program Update 2006–2007*. Manila.

<sup>2</sup> Government of the Federated States of Micronesia. 2004. *Strategic Development Plan 2004–2023: Achieving Economic Growth and Self-Reliance*. Pohnpei.

<sup>3</sup> ADB. 2000. *Report and Recommendation of the President to the Board of Directors on a Proposed Loan to the Federated States of Micronesia for the Basic Social Services Project*. Manila (Loan 1816-FSM); ADB. 2001. *Report and Recommendation of the President to the Board of Directors for a Proposed Loan to the Federated States of Micronesia for the Private Sector Development Project*. Manila (Loan 1874-FSM); and ADB. 2004. *Report and Recommendation of the President to the Board of Directors on Proposed Loans and Technical Assistance Grant to the Federated States of Micronesia for the Omnibus Infrastructure Development Project*. Manila (Loan 2099/2100-FSM and TA 4426-FSM).

pipeline did not proceed. During the November 2006 FSM Consultative Group meeting, ADB management indicated a desire to see the performance of the current lending portfolio in FSM improve before committing any further loans.

6. Sustained general government fiscal deficits have been noted by the International Monetary Fund to have raised the size of the fiscal adjustment needed to achieve self-sufficiency through the Compact Trust Fund by 2023.<sup>4</sup>

## **B. Indicative Nonlending Program**

7. Subject to availability of core technical assistance (TA) resources, ADB is considering indicative annual TA support for 2007–2009 at around US\$700,000. New TA during the period 2007–2009 will address improving: (i) economic management, planning and modeling; (ii) performance reporting in national and state departments; (iii) the effectiveness of selected public utilities; and (iv) information sharing between FSM's congress, state legislature and civil society. An indicative assistance pipeline for nonlending products for 2007–2009 is in Table 2. Additional information on the proposed nonlending assistance for 2007 is in Table 3.

8. To complement the TA program and leverage scarce TA resources, ADB will include FSM in regional TA (RETA) activities where feasible. ADB will also seek to coordinate and cooperate with FSM's other development partners, in particular seeking cofinancing opportunities.

## **III. SUMMARY OF CHANGES TO LENDING AND NONLENDING PROGRAMS**

9. Changes to the CSPU, formalized by this business plan, comprise (i) the removal from the pipeline of the loan for Solid Waste Management (\$8.00 million); (ii) the replacement of the associated advisory TA (ADTA) Capacity Building for Solid Waste Management (\$300,000) with an ADTA for Institutional Strengthening of Public Utilities in Chuuk, Kosrae and Yap (\$400,000); and (iii) the shifting of the \$400,000 from the ADTA Education and Health Sector Strategy to the ADTA Strengthening Economic Management and Planning. These changes reflect the delayed implementation of the Omnibus Infrastructure Project and the Basic Social Services Project, which meant the nature and timing of the proposed 2007 activities were no longer appropriate. These changes are consistent with ADB and Government discussions regarding the CSPU.

## **IV. INDICATIVE INTERNAL RESOURCE REQUIREMENTS**

10. It is estimated that a total of 21 person-weeks of professional staff inputs would be required for the processing of the nonlending program.

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<sup>4</sup> International Monetary Fund, *Staff Report for the 2006 Article IV Consultation, Federated States of Micronesia*. IMF Country Report No. 07/106, March 2007.

## **V. RESULTS-BASED MONITORING**

11. The CSPU 2006–2007 was not results-based and no road maps were developed. A results-based CPS will be developed in 2008. A draft CPS results framework consistent with this COBP is in Section VI; it will be further developed for the CPS to be prepared in 2008. There are no substantive changes in the key sectors or themes resulting from this COBP.

## VI. COUNTRY PARTNERSHIP STRATEGY RESULTS FRAMEWORK

| National Development Agenda   |   | Asian Development Bank Strategic Focus<br>Development Objective: Private Sector-Led Economic Growth  |   |   |
|---|---|--|---|---|
| SDP Strategy <sup>a</sup>   | Key Constraints   | Intermediate Outcomes  | Intermediate Indicators   | ADB Assistance Program  |
| <b>ADB Objective 1: Good Governance</b>   |   |  |   |   |
| Strategy 2: Good governance: Improving effectiveness and efficiency of government                                     | Poor national-state coordination/consultation processes<br><br>Loss of reform momentum  | <ul style="list-style-type: none"> <li>Decrease in extra-ordinary budget appropriations.</li> <li>SDP- and Compact-planned outcomes delivered in each year.</li> </ul>   | <ul style="list-style-type: none"> <li>Performance budgets developed.</li> <li>State and national budgets linked to SDP.</li> </ul>   | <ul style="list-style-type: none"> <li>TA 4961: Strengthening Economic Management and Planning</li> </ul>   |
| <b>ADB Objective 2: Inclusive Social Development</b>  |   |  |   |   |
| Strategy 4: Investing in human resource development   | Lack of government commitment to HRD  | <ul style="list-style-type: none"> <li>Capacity developed to manage and deliver quality basic social services in health and education.</li> <li>Improved HRD planning within Government public sector</li> </ul> | <ul style="list-style-type: none"> <li>Performance information management systems implemented and utilized in Departments of Health and Education.</li> <li>Long term public sector capacity building roadmap implemented.</li> </ul> | <ul style="list-style-type: none"> <li>Loan 1816(SF): Basic Social Services (2000)</li> <li>TA 4789: Implementation of Public Sector Capacity Building Roadmap (2006)</li> </ul>  |
| <b>ADB Objective 3: Pro-Poor Economic Growth</b>  |   |  |   |   |
| Strategy 3: Developing an outward-oriented, private sector-led economy<br><br>Strategy 5: Investing in infrastructure | Lack of effective government commitment to required reforms<br><br>Limited capacity to plan and manage infrastructure development | <ul style="list-style-type: none"> <li>Increase in small business enterprise start ups.</li> <li>Increase in commercial loans.</li> </ul>  | <ul style="list-style-type: none"> <li>SBDCs completed in each state.</li> <li>More than two banks using secured transactions registry.</li> </ul>  | <ul style="list-style-type: none"> <li>Loan 1874(SF): Private Sector Development Project (2003)</li> <li>Loan 2099(SF)/2100: Omnibus Infrastructure Development Loan (2004)</li> <li>Project: TA Capacity Building and Community Awareness Raising for Selected Public Utilities</li> </ul> |

ADB = Asian Development Bank, HRD = human resource development, SBDC = small business development center, SDP = strategic development plan, TA = technical assistance.

<sup>a</sup> Specific components of *Strategic Development Plan 2004–2023* that are supported by ADB's assistance priorities in the Federated States of Micronesia.

Source: Asian Development Bank

**Table 1: Indicative Assistance Pipeline for Lending Products and Services, 2007–2009**

| Sector<br>Project/Program<br>Name    | Targeting<br>Classifi-<br>cation | Thematic<br>Priority | Division | Year of<br>Project<br>Preparatory<br>Assistance | Total | Cost (\$ million) |       |        |       |        |                  |
|--------------------------------------|----------------------------------|----------------------|----------|---|-------|-------------------|-------|--------|-------|--------|------------------|
|                                      |                                  |                      |          |   |       | OCR               | ADB   |        | Total | Gov't. | Co-<br>financing |
|                                      |                                  |                      |          |   |       |                   | Loans | Grants |       |        |                  |
| Year Firm Loans<br>2007–2009<br>NONE |                                  |                      |          |   |       |                   |       |        |       |        |                  |

ADB = Asian Development Bank, ADF = Asian Development Fund, Gov't = Government, OCR = ordinary capital resources.

Source: Asian Development Bank

**Table 2: Indicative Assistance Pipeline for Nonlending Products and Services, 2007–2009**

| Sector<br>Assistance Name  | Responsible<br>Division | Assistance<br>Type | Sources of Funding |                    |        |                    | Total<br>(\$'000) |
|--|-------------------------|--------------------|--------------------|--------------------|--------|--------------------|-------------------|
|  |                         |                    | ADB                |                    | Others |                    |                   |
|  |                         |                    | Source             | Amount<br>(\$'000) | Source | Amount<br>(\$'000) |                   |
| <b>2007</b>  |                         |                    |                    |                    |        |                    |                   |
| <b>Law, Economic Management, and Public Policy</b>                               |                         |                    |                    |                    |        |                    |                   |
| 1. Strengthening Economic Management and Planning                                | PAHQ                    | ADTA               | JSF                | 400.00             |        | 0.00               | 400.00            |
| <b>Subtotal</b>  |                         |                    |                    | <b>400.00</b>      |        | <b>0.00</b>        | <b>400.00</b>     |
| <b>2008</b>  |                         |                    |                    |                    |        |                    |                   |
| <b>Multisector</b>   |                         |                    |                    |                    |        |                    |                   |
| 1. Institutional Strengthening of Public Utilities in Chuuk, Kosrae and Yap      | PAHQ                    | ADTA               | TASF               | 400.00             |        | 0.00               | 400.00            |
| <b>Law, Economic Management, and Public Policy</b>                               |                         |                    |                    |                    |        |                    |                   |
| 2. Develop a Medium Term Economic Framework                                      | PAHQ                    | ADTA               | TBD                | 500.00             | TBD    | 0.00               | 500.00            |
| <b>Water Supply and Sanitation</b>   |                         |                    |                    |                    |        |                    |                   |
| 3. Remedial Maintenance of Selected Wells in Chuuk                               | PAHQ                    | ADTA               | JFPR               | 900.00             |        | 0.00               | 900.00            |
| <b>Subtotal</b>  |                         |                    |                    | <b>1,800.00</b>    |        | <b>0.00</b>        | <b>1,800.00</b>   |
| <b>2009</b>  |                         |                    |                    |                    |        |                    |                   |
| <b>Governance</b>  |                         |                    |                    |                    |        |                    |                   |
| 1. Managing for Development Results – Enhancing the Accountability of Government | PAHQ                    | ADTA               | TBD                | 860.00             | TBD    | 0.00               | 860.00            |
| <b>Subtotal</b>  |                         |                    |                    | <b>860.00</b>      |        | <b>0.00</b>        | <b>860.00</b>     |
| <b>Total</b>   |                         |                    |                    | <b>3,060.00</b>    |        | <b>0.00</b>        | <b>3,060.00</b>   |

ADB = Asian Development Bank, ADTA = advisory technical assistance, JSF = Japan Special Fund, PAHQ = Pacific Operations Division, PARD = Pacific Department, TBD = to be determined, TASF = Technical Assistance Special Fund.

Source: Asian Development Bank estimates.

**Table 3: Summary Information on Proposed Indicative Nonlending Products and Services for 2007–2009**

| Project Name                                   | Description  |
|--|--|
| Strengthening Economic Management and Planning | <p><b>Impact</b><br/>The TA will support the implementation of the SDP and its goal of economic self-sufficiency through (i) advice to (a) develop short-term action plans in support of the SDP at the national and state levels, and (b) strengthen the performance-based budget process; and (ii) linkages between the budget and the national plan, which will facilitate the financing of these activities.</p> <p><b>Major Components</b><br/>Strengthening the implementation of performance budgeting at both the national and state levels through analysis of the existing situation and process(es), and advice to improve budget sustainability and budget monitoring. Supporting implementation of the SDP through the development of 3-year action plans at the national and state levels that are tied to budget processes and that facilitate the implementation of key priorities identified in the SDP. Capacity building among budget and planning staff. Where requested, advice on long-term adjustment and sustainable transition plans to improve the balance between government revenue and expenditure.</p> <p><b>Expected Outputs and Outcomes</b><br/>Strengthened budget management at the national and state levels. Where required, plans to move to sustainable budget positions. Budget and planning staff with greater capacity to undertake key tasks required by their positions. A series of 3-year action plans to facilitate implementation of SDP for the attention of both state and national governments.</p> |

SDP = Strategic Development Plan 2004–2023, TA = technical assistance.

Source: ADB. 2207. *Technical Assistance to the Federated States of Micronesia for the Strengthening of Economic Management and Planning*. Manila (TA4961-FSM, approved on 17 August 2007 for US\$400,000).

| Project Name                                    | Description   |
|---|---|
| Remedial maintenance of selected wells in Chuuk | <p><b>Impact</b><br/>Increase the potable reticulated water supply in Chuuk.</p> <p><b>Major Components</b><br/>Analyze the health status and equipment of the wells in Chuuk currently feeding the reticulated water supply and prioritize their refurbishment based on their likely pumping volumes, water quality, current equipment serviceability, and sustainability of maintenance requirements. Refurbish the wells in order of priority within the budget.</p> <p><b>Expected Outputs and Outcomes</b><br/>The expected outcome is an increase in the potable water pumped into the Chuuk reticulated water supply system on Weno, with a target of 1 million gallons per day. Outputs will include: a prioritized schedule of work to refurbish the wells on Chuuk that currently feed into the reticulated water supply network; refurbishment of wells pumping potable water into the reticulated system; repairs to existing pumping and chlorination equipment.</p> |

Source: Asian Development Bank