

YAP STATE FINANCES- ROCK SOLID IN THE LAND OF STONE MONEY

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The conventional wisdom in the Pacific is that the small island nations in the world's largest ocean are poorly run, have little basis for a sound economy and that future prospects are limited. Various explanations are given ranging from the recent colonial past to time immemorial cultural practices. The inability of governments to constrain their appetites to conform to their real economies and real revenues draws the most attention and is frequently given as evidence of Pacific Islander inability to deal with modern state realities. In response, the negative effects of globalization are offered as the basis for understanding recent difficulties.

Yap State in the Federated States of Micronesia (FSM) offers us an example of a Pacific Island jurisdiction that manages its public finances well. The Asian Development Bank's annual outlook report notes that Yap, as the only state government in a strong fiscal position in the FSM, "has been able to achieve an impressive fiscal record and high standard of public sector management." (ADB, 2003, p. 3) Yap's experience has been discussed widely and sometimes overstated as a model of public sector finances. As has always been so true in the past, Yap responds to its own rhythms. Economically, politically and culturally, it is out of the mainstream not only of worldwide trends, but even Pacific island trends.

This paper explores factors within the Yapese cultural context that can be attributed to that government's financial management success. By understanding their budgetary conditions, political structure, how they make decisions and what has authority in their lives, we will get closer to knowing why Yap's finances are rock solid in this land of fabled stone money. We will also review the impact of these financial practices on the relationship between Yap proper and the outer islands of Yap state.

Budgetary Conditions

Yap is the rare Pacific island government that lives within its means. It does not have natural resources, a vibrant private sector economy and it does not have a population or bureaucracy that is especially well-educated in comparison to other states in the FSM. It does have a solvent state government that has invested and profited from a steady stream of assistance and has managed to sustain budget surpluses every year. It holds a substantial investment portfolio that is sometimes referred to as a “trust fund.”

The actual fiscal condition of Yap has reached legendary proportions and has been the subject of attention and explanation in the past few years. In actuality, Yap’s financial condition is healthy due to some very unique circumstances and the long-term outlook is not necessarily positive. For the past few years, Yap has been able to save funds and invest them in a portfolio that is similar to other Pacific Islands like those of the Government of Guam retirement fund. The process of managing the money utilizes many of the same techniques and advisers as nearby islands. (Robert Ruecho)

The investments are made possible by budget surpluses that have been identified at the following levels by auditors:

1999 - \$2.9 million (all amounts are in U.S. dollars)
2000 - \$4.3 “
2001 - \$3.7 “
2002 - \$1.6 “

The total value of the investment portfolio is, however, the subject of some disagreement. Maria Laaw, Yap State Director of Administrative Services identifies the value at \$56 million today. In contrast, Yap State Legislature Finance Committee Chair, Clement Mulalap identifies the value at some \$10 million less. Regardless of the total value of the investment portfolio, the total value of the money saved and invested is a little over 350% of the total annual operating budget. There are not many governments in the world that can boast of a bank account that is equal to three times their annual budget.

The funds are kept in a pooled investment fund managed by the Federated Development Authority (FDA) which includes investments from the FSM national government and the other three states. Some of the funds

from the funds from the first Compact of Free Association are restricted by that arrangement with the United States, but the earnings are unrestricted.

The contours of this enviable fiscal record have to be understood in the context of two factors in the financing of government services and the pattern of expenditures. The bulk of Yap's income comes from the Compact of Free Association with the United States. This is true for the entire FSM where Compact funds accounted for nearly 70% of government revenues and the majority of economic activity in each state except for Pohnpei. (ADB, 2002) In 2002, Yap received \$7.6 million from Compact funds in a total state budget of \$11.9 million. (Deloitte and Touche, 2003)

Yap's locally generated revenue is approximately \$2 million per annum and their share of FSM revenue sharing is \$1.5 million. External assistance in the form of Compact assistance doubles this locally generated revenue and provides a more balanced view of the real financial and economic conditions in Yap. Furthermore, Yap is one of four fairly autonomous states within the Micronesian federation. As such and despite its smaller population than Chuuk or Pohnpei, it receives a disproportionately higher share of the total compact funding. Deciding state shares of compact funding is one of the major political and fiscal arrangements in the FSM and the process is well underway for the new Compact funds.

Comparing Yap to other Pacific Island entities without such a healthy cash infusion from external sources is perhaps unfair. However, comparing it to other states within the FSM is certainly more to the point. No other state, not even Kosrae (which also gets a disproportionate share of compact funds) has an investment portfolio. All of the other three state governments regularly run deficits and have come under criticism for their fiscal policies.

This raises the second major consideration relative to the cost of public services. Yap continues to provide public services at much lower costs due to its lower minimum wage. Resisting the temptation to politically appease a government work force, Yap continues to maintain an 80-cent per hour minimum wage for its government work force. Moreover, there is no minimum wage for the private sector. Compared to Pohnpei's minimum wage of \$2.00 per hour, it is easy to see how Yap can get greater value for its expenditures, hold the line at budget time and have enough left over for investment.

The question, which then arises in Yap's economic and political climate requires much more than financial data. Yap is only an hour away from Guam where young people can freely go and earn a U.S. minimum wage of \$5.15 per hour to work in a hotel. They could also go to the national capital and almost triple their wages. The ability of Yap to keep a political and social consensus about government spending that doesn't lead to massive out migration or major political dissension is the real miracle. To understand this, we have to look at the totality of how decisions are made in Yap and by whom.

Exceptional Political Leadership

Given Yap's unique fiscal condition in the island Pacific and especially within the FSM, it is important to recognize decisions made by political leaders that actually held the line when they could have done otherwise. As is the case with assigning responsibility for remarkable decisions in the recent past, the record is not clear-cut.

Under the Compact of Free Association, Yap is currently under the administration of its fourth governor. John Mangafel, Petrus Tun, Vincent Figir and Robert Ruecho have all held the mantle of Yap's chief executive and depending upon whom you speak to, individual governors were assigned more credit than others for the frugal approach to Yap State finances. Regardless of who was in office, it is widely recognized that Yap's inherent conservative nature and decision-making process made certain decisions likely. (Mulalap, Tacheliol, Laaw, Chieng, Haglelgam)

Governor Tun is given credit for the much repeated saying in the Yap bureaucracy, "If you don't have a dollar, you don't spend it." (Mulalap) During his term in office, Yap as other FSM states faced the prospect of the step-down decrements in compact funding and confronted the reality that the economy was experiencing minimal growth. Given, these conditions, technical assistance experts from the Asian Development Bank recommended dramatic cutbacks in the government work force. The process of cutbacks began under Tun's term and was completed under Figir. The experts recommended that the workforce be cut back by 35% before the year 2000 and Yap State exceeded its goal. The work force fell to a historical low of 650. (Raigital)

In its first confrontation with dramatic political turmoil due to budgetary shortfalls, Yap's political leadership bit the bullet and no one paid a political price. The Yap State Legislature was very cooperative in devising and implementing the plan to shed government employees and participated in forcing the retirement of workers. The philosophy of the Yap State Legislature according to Senator Clement Mulalap, Chair of the Finance Committee for the past eight years, is "We don't spend what we don't have." In fact, he remarks, good politics in Yap is not to spend money. Even given this philosophy the work force has increased to 850 today.

Not spending what you don't have is noteworthy for government leaders, but not spending what you do have is even more remarkable. The availability of the investment funds has not led to a flurry of pork barrel capital improvement projects or spending. A sports complex was built from the funds and that project has been completed. A "southern road project" is being completed and it is anticipated that there will be a draw down next year to complete the funding of that project. (Laaw, Clement)

But there are discordant voices regarding the projects. Former FSM President Haglelgam from the outer islands of Yap notes that the capital improvement projects are both in the main island of Yap. There has been no funding of projects in the outer islands. The Compact funds are distributed on the basis of the population and 40% of Yap lives in the outer islands, but receives none of the capital projects. He asserts that part the financial success of Yap has been done at the expense of the residents of the outer islands. (Haglelgam)

In April 2004, Typhoon Sudal hit Yap. Although Yap's proximity (particularly the outer islands) to the Marianas Islands puts it within striking distance of typhoons, it is rare that a typhoon directly hits Yap. Under the free association agreement with the United States, Yap is eligible for Federal Emergency Management Agency (FEMA) assistance and it was significant.

But despite the widespread damage, the shortage of water and the interruption of public services, no political leader in the weeks subsequent to the typhoon suggested spending the investment funds. Under most political scenarios in the world, various voices in the legislature would have been raised that this is the rainy day that rainy day funds are supposed to take care of. Instead, the political leaders concentrated on working with the traditional leaders and village elders to ensure that resources were being fairly

distributed. One group of village leaders reportedly turned down Red Cross assistance to only five families because all suffered during the typhoon. Yapese values regarding resources and their distribution were starting to assert themselves. (Chieng)

If there is a tradition of political leadership that only seeks what is needed, it is also a function of a political constituency that is fairly undemanding. Even with common knowledge about the investment funds and the damage of Typhoon Sudal, there was no outcry about dipping into the funds. Senator Sabino Sauchomal, Yap Legislature floor leader, reports that the public asks only general questions about assistance. (Sauchomal)

Several months down the road, the political leaders of Yap have decided to spend \$1.5 million of the investment funds to satisfy Yap's matching share for FEMA. Instead of arguing that the matching share should be reduced or eliminated (as so often happens in Guam and other U.S. jurisdictions), the consensus decision was to use the funds in a limited and collective way. No individual was given any funds directly and Yap's willingness to pay their matching share will certainly be a story shared in the FEMA bureaucracy and the U.S. federal government.

This practical and frugal attitude was always a feature of Yap political leadership according to Hilary Tacheliol, former Lt. Governor of Yap. He remembers that even in the Trust Territory of the Pacific Island days, Yap district always sent the smallest delegation to Washington D.C. and got the most projects because they only asked for what they needed. (Tacheliol)

The source of this practicality and frugality is based on a conservative cultural tradition that continues to envelop life in Yap. That tradition continues to sustain itself because of a decision-making process that is slow, deliberate and involves a mixture of traditional and modern leadership that seems natural in Yap.

Traditional Decision-Making

To understand the background of these fiscally prudent political decisions by the holders of formal state authority, we have to understand the decision-making process in Yap. Authority in Yap is vested in a chief executive, legislative body and court system that seem very familiar to Americans. The state itself is divided into the main island of Yap and the

outer islands. The outer islanders are not ethnic Yapese, but they are culturally and historically bound to Yap in a complex system of relations that rely on a sense of place in a social order and propriety in social and political relationships.

In order for this system to continue to be mediated successfully, the traditional relationships and traditional forms of authority must be brought forward into the modern world. Accordingly, Yap is the only state in the FSM that has two Councils of Chiefs (Pilung and Tamol) that wield significant authority. They can veto legislation in areas that they decide affect custom and tradition and there is no recourse for the State Legislature. (Tamanaha, BZ, 1988) There is much discussion about bringing this into line with the rest of Micronesia by amending the Constitution to add the phrase “except as otherwise provided by law” to the authority of the Chiefs. (Chieng). It may happen with this year’s Constitutional Convention, but there appears to be little open disagreement with the role of the chiefs.

In actual practice, the Chiefs rarely exercise formal power. However, they continue to represent in actual practice their influence in the decision-making process in Yap, which is dependent upon consensus building. In some fashion, they are consulted and their agreement is given indirectly in most major decisions. Almost all highly educated government bureaucrats and officials discuss the process of decision-making as deliberately “slow” and “indirect.” (Saucholmal, Chieng) Noted anthropologist Don Rubenstein remarks, “It isn’t the chiefs who run the government, but everybody in Yap knows who has power and they are all comfortable with it.”

The practice of real consensus-decision making requires certain behaviors that are in abundance in Yap. Yap officials remark that no one wants to look like they are behaving “contrary to the general consensus” (Laaw) and no one is in a hurry to get ahead of others in proposing “new ideas.” (Sauchomal). The way a new idea gets proposed is for someone to suggest it in an “off hand manner,” with the full knowledge that it takes many, many meetings to finalize things. Unlike other FSM states, there is no tradition of “bucking authority.” (Sauchomal). Behaving in a reticent manner contributes to the consensus building process and consulting with traditional leaders in an indirect way ensures its continuity. (Rubenstein)

There is the begrudging admission that the time it takes to arrive at a consensus is frustrating and sometimes “holds us back,” but it has been

“helpful” for the most part. (Laaw). Charles Chieng of the Yap Community Action Program opines that the younger generation is not as content with the current state of affairs in Yap. As the population changes, there will be changes with both the decisions and the decision-making process.

The consensus process may also be masking some discontent by outer islands. Haglelgam asserts that the interests of the outer islanders are routinely ignored by the political leadership of Yap. In addition to having no capital improvement projects, the request to purchase a new field trip ship was denied. The former Yap Senator and FSM President believes that the outer islander representatives in the legislature are “being placated by personal privileges granted to them. He thinks that the Chiefs are too conservative to do much. The younger generation and the outer islanders may provide the energy for dramatic change in the future.

Cultural Continuity

Until that time comes along, the traditional character and culture of Yap continues to shape the kinds of decisions that are being made. Yapese, explains Senator Sauchomal, are “by nature, very conservative, intensely personal, guard privacy and private property strongly.” This conservative nature is manifested in a frugality, which is atypical in other Pacific islands.

The cultural modesty, attention to privacy and frugality all seem to work together in Yap. The bank loan default rate is the lowest in the FSM and when the Bank of Hawaii branch closed in Yap, there were still individual saving accounts totaling over \$10 million. (Raigetel). Senator Mulalap states that Yapese character is guided by the saying “if you don’t save for a rainy day, you will get in trouble.” Based on the typhoon experience, the rainy day still hasn’t arrived.

Some argue that it is easy to save money when you don’t need to spend it and the reality is that the subsistence economy is alive and well in Yap state. The need for cash is diminished by the continuing participation in subsistence agriculture and although consumer goods are increasingly available, there is no strong demand for them. The availability of a few products at the Yap Coop seems to meet the needs of most of Yap’s citizens.

Between the cultural conservatism and the participation in traditional economic activities, the people of Yap do not expect much from a modern state government. In the typhoon that destroyed over 35% of the homes and affected 100% of the population, people did not look to the government for help. They went to their extended families and their village leaders. (Chieng) In this environment, political leaders are not pressured to expend resources and the traditional conservative, decision-making process continues with few changes.

Yapese Rhythms

At the beginning of the 20th century, the eventual demise of the Yapese people was predicted by a number of observers. At the time, it was felt that Pacific islanders were on borrowed time and that the most stubborn and resistant to change islanders (like Yapese) were the ones who were going to disappear. Their inability to adapt and change quickly was seen as a weakness.

At the beginning of the 21st century, we must examine the continuing strength and vitality of those cultures that are innately conservative as they make political and economic decisions that globalization and external change impose upon them. In the case of Yap, it appears that their style of deliberation, their inherent conservatism and resistance to change has allowed them to make political and economic decisions that sustain the essential character of their society.

Many of the circumstances surrounding their good financial fortune cannot be replicated in other places. It is the rare place that has 70% of their operating revenues generated from external sources. But it is also the rare place that routinely saves money in the midst of the most difficult financial situations. As has always been the case with Yap, the Yapese have defied definition, responded to their own rhythms and offered a sense of hope for small groups of peoples everywhere. You can chart your own course in your own way and for your own people.

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