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## Developing an Export

C.L. Cheshire



## Introduction

Over the past fifty years, successive Micronesian governments have labored to achieve economic self sufficiency. Since the Compacts of Free Association were established in the late 1980's, the island states that make up the Caroline and Marshall islands have tried to meet this challenge through a variety of export development initiatives. In addition to developing a local tuna industry, Micronesians have attempted to establish an aquaculture industry (giant clams, trochus, sponges, black pearls, and hard and soft corals). They have worked to wring profits from the region's traditional export, copra, and have constructed two coconut soap factories. Rather than reduce Micronesia's dependency on foreign aid, however, these efforts have been, for the most part, a drain on its aid funds. The challenge of developing a thriving export industry to achieve self-sufficiency still remains.

For an export industry in Micronesia to be truly Micronesian, it needs to be locally owned and operated. Some commentators, however, have suggested there is no export in Micronesia because there is insufficient business experience to develop a locally owned export industry. As the argument goes, successfully exporting a locally manufactured product is more complicated and requires a different set of business skills than those possessed by local business owners. This argument overlooks the considerable business experience and expertise that is in Micronesia. There are several large diversified service and retail businesses in Micronesia that employ scores of employees and have annual sales in the hundreds of thousands or even millions of dollars. These businesses can be viewed as an important asset in a strategy to develop a locally owned export industry in Micronesia.

Others have argued that the reason various export development initiatives have not been successful in Micronesia is its geography and scant natural resources. Micronesia, with its small, remote islands, simply cannot compete in the global marketplace with countries like Indonesia and the Philippines, with their large local markets, cheap labor, and well developed infrastructure. Yet, one can also argue that had Micronesians focused on producing export

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Island Topics #37  
Running Time: 37:10

A presentation of the terms of the re-negotiated Compact of Free Association: What the Marshalls will receive and what it hopes to achieve in the next 20 years.



view Micronesian export as a secondary concern until there is sufficient freight volume to justify providing more service. But until there is a transportation system in Micronesia that supports export development, export development in Micronesia will continue to struggle. Government can play a role in helping Micronesia break out of this chicken and egg predicament by identifying the transportation exporters need to get their products to market. Once this is done, they can begin to explore with the various members of the region's transportation industry how these services can be provided.

## Conclusion

The keys to developing a Micronesian export industry are:

- Select products that are geographically, economically, technologically and culturally appropriate and commercially competitive.
- Capitalize on the business experience that already exists in the region by removing barriers and creating incentives for local business people to invest in export development.
- Limit government's role in export development to providing technical assistance, low interest loans and economical, efficient export infrastructure (transportation, communication, utilities, etc.).

There is nothing new here. All of the pieces needed to construct an export industry in Micronesia already exist. What has been missing in the past has been a way to assemble these pieces so that they add up to a successful Micronesian export industry. This proposal suggests that the way to do this is to first recognize which of the region's natural resources are economic opportunities and then to create the incentives and the means for those best able to develop and exploit those opportunities: the local Micronesian business people.



products where Micronesia possesses a competitive advantage, the results may have been different. Tahitians, for example, who are no less geographically challenged than Micronesians, were able to transform their abundance of black lip oysters into a multi-million dollar black pearl industry that they now dominate. Pohnpei, for a short time, marketed a successful pepper product that was unique to Pohnpei and was sold not simply as pepper but as "Pohnpei Pepper". The product was admittedly a high end, niche product without a large volume of sales, but the potential of the product was barely tapped before production ceased. Likewise, Yap betelnut is prized throughout the region and could also be developed as an export product. All of these examples suggest that given the right products and the right development strategy, Micronesia, too, could develop a competitive export industry.

This paper is a proposal for an alternative export development strategy for Micronesia that is organized under the following three headings: product, team, government support. The purpose of organizing the proposal this way is to examine those aspects of export development that are particularly significant for Micronesia but are often overlooked in the standard approaches to developing an export industry.

## Product

One can find example after example of export products such as fresh tuna, Kosrae limes, coconut soap and giant clams that make economic sense (ie, a good market and a price that exceeded the cost of production and delivery) and resource sense (an abundance of natural resources such as coconuts and tuna to make high value products such as coconut soap and sashimi grade fresh tuna), but did not succeed in Micronesia for reasons that have little to do with economics and resources.

In contrast, the list of successful export products from Micronesia (products that actually produced a profit for local producers) is very short: copra, betelnut, and reef fish. All of these products were "low tech" with low start-up costs. All were relatively



easy to ship. The market was readily accessible; there was a fairly simple distribution chain to connect producers with end users and demand was consistent and in line with the available supply. And most important, local Micronesians willingly produced these products consistently over an extended period of time. In summary, all of the products that succeeded “fit” Micronesia *geographically, economically, technically* and *culturally*. Those that failed did not.

## Geography

Geography affects product viability in Micronesia in several ways. On a small remote island, the business developer has only a small local market that is quickly saturated with product. To get beyond the local market requires exporting, and the closest export markets can only be reached by sea or by air. The one airline that serves all of Micronesia (Continental) has limited space for freight. Moreover, there is no guarantee that this space will be available. Producers of fresh limes in Kosrae have repeatedly brought their produce to the airport to ship it to Pohnpei only to learn that there was no freight space.

For almost all fresh products like limes and tuna, surface carriers are not a viable alternative because they are too slow. Those products that can be shipped by surface carriers must be shipped in container loads. LCL (less than container load) space is expensive and is often unavailable. This means that the local producer has to increase production to 20,000–30,000 lbs. of product per month if the shipping rates are to be affordable. Furthermore, the schedules and routes for surface carriers reflect the fact that most of their business comes from goods delivered to Micronesia rather than goods being exported from Micronesia. Thus, a local producer often has trouble finding a vessel that will stop to make a backhaul to the U.S.

mainland. Increasing production from a few thousand pounds a month of local sales to 20,000 to 30,000 pounds a



tuna, which is abundant in Micronesia and is a high end specialty product with a high profit, did not meet this criteria. The cost of providing a chartered jet to transport the fresh tuna to Guam from the FSM ultimately proved to be prohibitively high as the volume of tuna shipped from the FSM declined.

4. The product needs to be something that Micronesians can and will produce. This cannot be easily determined since Micronesian managers and owners play a decisive role in motivating employees. But where training is required, the proposal for the venture must show that the training is readily available at a price that is consistent with the projected profitability of the business. Given the high cost of training in Micronesia, this criterion should be given close attention.
5. The technology required to produce, package and ship the product must be appropriate for Micronesia. It must not only be able to operate reliably and efficiently in Micronesia, but it must also be maintainable in Micronesia at a cost that is consistent with the revenue projected for the sale of the product.

A final requirement for an export development loan is that the applicant must show that the venture has adequate technical support. As noted above in the discussion of the export development team, local owners/operators need the support of technical assistance to set up production systems, train employees, identify markets, contact buyers and make initial sales. This kind of technical assistance requires those providing the assistance to be actively involved in the business. It also requires the owner to follow up the assistance with the necessary investments in personnel and equipment to ensure that what is recommended is implemented.

*Explore Ways to Improve Micronesia’s Transportation Infrastructure:* The single greatest barrier to export development in Micronesia is the lack of transportation dedicated to supporting export development. Currently, the only airline serving the whole region is primarily a passenger carrier, and the only surface carrier that serves all of Micronesia is set up to bring goods into Micronesia rather than take goods out. The current transportation industry in Micronesia will continue to



export development loan should be more stringent than other development loans. In particular, the requirements should include a high equity contribution on the part of the owner and the owner should be required to show that he has other sources of income to cover the operating costs of the export venture until it can show a profit. Hence, it is almost essential that the loan applicant have another business or substantial personal assets with which to support the development of the export business. Making ownership of a profitable business a requirement for obtaining an export development loan is appropriate for another reason: it demonstrates that the manager knows how to make a profit and knows how to manage and motivate a Micronesian workforce.

Another appropriate requirement for an export development loan is that the product must not only be feasible, but also competitive. There are many ways to assess the relative competitiveness of a product or a business. The following five criteria should be taken into consideration in evaluating a Micronesian export product:

1. There must be a strong market demand for the product, and the product must have a high profit margin. Given the high costs of producing and transporting Micronesian products, niche products with high profit margins like Pohnpei pepper, marine sponges and black pearls are more likely candidates for export development than commodity products like limes and bananas unless the latter can be marketed and sold as specialty products as well.
2. There must be a competitive advantage in producing the product in Micronesia. Geography has given Micronesia so many competitive disadvantages that one rarely hears of any of the region's natural advantages. But the abundance of clean, accessible lagoons for growing marine aquaculture products gives Micronesia a competitive advantage over other producers of marine products whose marine habitats have been compromised by the pollution from over development.
3. The product must fit the existing transportation infrastructure rather than require its own separate transportation system. Sashimi grade



month of export sales is very hard to do overnight. It may be no harder, though, than convincing a shipping line to change its route and schedule just to pickup a single container once a month.

Given the uncertainties of shipping, the product must be hardy: it must have an indefinite shelf-life and be immune to the effects of delay. This requirement automatically eliminates many fresh products or forces the producer to develop an expensive, and often elaborate, transportation system to get the fresh product to market. For example, fresh tuna requires its own jet airplane or tank ship (for shipping live fish); bananas require refrigerated containers and equipment to retard the ripening process until the bananas reach their destination.

## Business Economics

Business economics have also been a limiting factor in the history of product development in Micronesia. The commercial banks have been better than business developers and development banks in identifying these limits. Commercial bankers have recognized that products that have high start up costs and require highly leveraged loans (80% debt to 20% equity) leave the business with a debt burden that the business usually cannot support. But this has not prevented business and development advisers from helping their clients to apply for these loans, nor has it prevented the development banks from making these loans. Yet, the poor performance of these loans speaks for itself.

Recently, the Asian Development Bank has been critical of some export industries, like aquaculture, because the length of time required to generate an income is so long. While this should not eliminate agriculture and aquaculture products as possible export products, it does highlight the need for a developer to have sufficient financial resources of his own to cover the costs of product development until the product becomes profitable.

The product also must have a competitive advantage by being produced in Micronesia. It is not enough just to be able to produce a product in Micronesia; the product must be able to



compete in a global market. What constitutes a competitive advantage, however, is not always apparent. It is just as easy to overlook a competitive advantage as it is to see an advantage where none exists. For example, Micronesia's remote atoll lagoons have often been dismissed as commercially un-developable because they are so remote, possess few developable resources and have so little commercial infrastructure. Now, however, they are being seen as excellent sites for open ocean aquaculture because they are pristine and relatively inexpensive to develop. On the other hand, Micronesia's often touted "cheap" labor continues to be mistakenly viewed as a competitive advantage.



## Technology

The technology needed to produce a potential export product is another component of the export business that must fit its Micronesian environment. Too often business planners are content to assume that because a piece of equipment worked well in another part of the world, it will also work well on a remote island in Micronesia. But can this outside technology be supported in a remote environment? Something as common and "low tech" as an outboard motor must be maintained regularly. This maintenance requires a certain amount of expertise that is not always locally available. Outboard motors also have parts that wear out and must be replaced. These parts must be ordered from factories and suppliers that are usually several hundred miles away and often do not ship to Micronesia. On many of the remote islands in Micronesia it is difficult just to communicate with suppliers. As a result, an outboard motor may sit for months before anyone can repair it. If the motor and the boat are essential to the business, this part of the business suffers. The issue here is not whether a specific kind of technology is appropriate for the job, but whether it is appropriate in a remote Micronesian location. To determine whether a particular technology

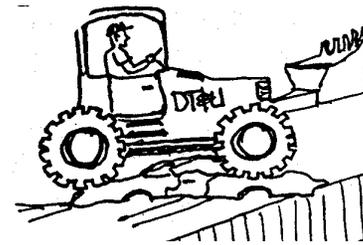


3. Finally, government funded technical assistance could speed up export by attracting several private businesses to invest in export development or by helping them to be successful once they have made their initial investment. The market study recently completed by the Pacific Business Center to find sponge buyers for Pohnpei's sponge growers was designed to help all of the sponge farmers on Pohnpei, not just one of them. No single sponge farm on Pohnpei is large enough to supply the potential demand for sponges by itself. The more sponge farmers that take advantage of the Center's market study, the sooner Micronesia will be recognized as a significant supplier of natural sponges. In the absence of government funded technical assistance, however, the government and the rest of Micronesia will have to wait for a private business owner like Ramsey Reimers at RRE to slowly develop an export industry by himself.

### *Provide Access to Low Interest Financing for Export*

*Development:* Previous business development programs in Micronesia have been supported by development loan programs with relatively low interest rates (9%) and low owner equity (20%) requirements. Making loans available for export development could be an attractive incentive to encourage business owners to look at export as a way to grow their business.

This does not mean that Micronesian governments should make export development loans easy to obtain. Making it easy to qualify for a business development loan has not significantly lowered the barriers to business development. Export products, because they take more time to produce a profit, are particularly poor candidates for excessive financing. For example, by the time a new aquaculture farm can produce an exportable product that is accepted by foreign buyers, it will be swamped with debt from the original loan and the accumulated interest on the loan. Consequently, the requirements for an





## What Can Government Do?

What can the state and national governments in Micronesia do to stimulate the development of a locally owned export industry in Micronesia? Micronesian governments have already taken an important first step by getting out of the export business themselves and exploring ways to privatize many of the government sponsored export ventures. The governments in Micronesia can also take the following steps to lower the barriers to export development.

*Provide Technical Assistance:* Most of the business development assistance in Micronesia has been directed at those who are not in business, but would like to be. Classes, workshops and loan programs have been funded by governments in Micronesia to assist potential Micronesian entrepreneurs start their own businesses. But no assistance has been provided to existing businesses to help them expand into export. Such an assistance program is needed for a variety of reasons:

1. Local retailers who have been successful running their own businesses in Micronesia are in the best position to develop and manage a local export business. They know how to manage and motivate a local Micronesian workforce. They know how to develop a new product or service. They know how to make a profit. But local managers and owners lack the technical expertise to identify potential export products, install efficient production systems, find foreign buyers, and complete sales abroad.
2. All of the requisite expertise and experience needed to establish and operate an export business is costly to obtain. The expense of acquiring this expertise and experience is a major barrier keeping local retailers from developing products for export. By providing existing businesses with technical assistance in market analysis, product development and oversees sales, Micronesian governments would be lowering this barrier.



is appropriate in Micronesia, one must recognize how much outside support is required, estimate the costs of this support, and include them in the project budget.

A similar caution applies to training. In those cases where the technical expertise required to operate and maintain a piece of essential equipment is lacking, there is a tendency to gloss over this lack of local “fit” with the promise “we will provide training.” Too often what the training can accomplish is overestimated while the cost of the training is underestimated. When the training takes too long or costs too much, it does not occur. The result is an inadequately trained staff or one that must be replaced by outsiders who possess the necessary skills. This latter scenario defeats the whole purpose of creating a local economy: that is, to create jobs for Micronesians.

## Culture

A cultural or social fit is also essential for a successful Micronesian export product. It has been assumed that unemployed Micronesians will take just about any job offered to them. But this assumption has been shown repeatedly to be incorrect. Just because a person is technically “unemployed” does not mean that the person needs or wants a job. Many of the “unemployed” are active participants in the subsistence economy and so receive many of their basic needs from the extended family. The reciprocal obligations that come with membership in an extended family in Micronesia can take up much of a person’s time. In fact, a person who wants a job may not be able to take and keep one because of the demands placed on him or her by the extended family.

Several export development projects like commercial fishing, agriculture, handicraft production and even tourism have been promoted in Micronesia on the grounds that they fit the local culture. The promoters have argued that since Micronesians have traditionally fished, planted gardens, produced handicrafts and hosted each other on a regular basis, they will be equally adept at



doing all of these same activities commercially. This argument fails to recognize how much commercialization changes an activity. The obvious differences between the traditional subsistence activity and its commercial counterpart are completely overlooked. Yet the importance of these differences is evident in the difficulty of getting Micronesians to work on commercial fishing boats; the numerous unsuccessful attempts to develop a local handicraft industry; and the absence of sustainable commercial agriculture, even on islands that have excellent soil and abundant rainfall.



Why the transition from traditional to commercial has not been as smooth and rapid as some expected is a question too complex to answer here. Part of the answer, though, is that most commercial activities, regular nine to five jobs, are too inflexible to accommodate the many traditional obligations that take precedence over the desire for a cash income. Also, commercial activity is often too impersonal and the benefits are too indirect. When a Micronesian fishes for subsistence, for instance, he goes out on a daily basis and catches fish which he either takes home to eat or gives away to someone he knows. Subsistence fishing is far more personal and the rewards are far more immediate than commercial fishing, where the fisherman is required to be away from his family for weeks at a time and receives wages that are paid out at the end of the season. Subsistence fishing and commercial fishing are, socially and culturally, two very different activities. The same can be said for growing food and producing handicrafts. The benefits from these subsistence activities are personal, social and immediate. These are qualities that, more often than not, are missing in most commercial employment. In the end, what is needed is an awareness of the fundamental differences between the two economies and the development of management strategies that take into account those differences and address them in the commercial workplace.



For one thing, export is not where local business owner/operators have a competitive advantage. Their advantage lies in local retail where they can use their knowledge of local markets. Export is more expensive to get into and requires a different kind of expertise and experience. To get into export, a business owner/operator needs to be able to manufacture a product consistently to specifications set by foreign buyers. He needs to know who his foreign buyers are and who his foreign competitors are. It is possible to acquire this information through first-hand experience, training programs and by hiring outside experts. But gaining experience and attending training programs take time and cost money. Hiring outside experts is also expensive. Some outside experts who are very qualified in their field can be ineffective because they lack sufficient knowledge of Micronesia.

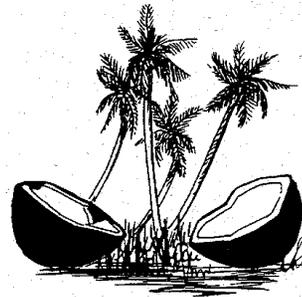
A second reason local business owners/operators have not ventured into export is because, until recently, there has been no pressing need to do so. There have been easier alternatives in the local market for expanding and diversifying their businesses. Local business owners have been able to grow by expanding their general stores into construction companies, apartment buildings, hotels and other services. This has been possible because there has been sufficient money in the local economy from government payrolls and government purchasing and government contracts to insure enough sales to keep the large diversified Micronesian businesses going.

Finally, government's lack of success in developing export products has tended to discourage private business owners from getting into export. The business community in Micronesia is conservative and generally takes a "wait and see" approach to developing new businesses. Seeing how much export ventures can cost, how difficult it is to become competitive, and how much work is involved in finding buyers has only made private business owners more reluctant to spend their own money to get into exporting Micronesian products.



effective when they have become directly involved either in setting up and refining the production system (as in the case of the two coconut soap factories and the sponge farms in Pohnpei and the giant clam hatchery in Kosrae) or in actively marketing the product (as in the case of RRE's giant clams in Majuro and the pearl farm on Nukuoro atoll in Pohnpei).

But experts can only do so much. They must rely on local owner/operators to implement the recommendations that the experts make. For example, Kaselel, the coconut soap manufacturer in Pohnpei, and its sister company, Afata in Chuuk, benefited from the input of production experts from Indonesia who greatly improved the consistency and quality of their coconut soap. Unfortunately, there was not an equally successful marketing effort to find buyers for the improved product. A similar situation exists for Pohnpei's sponge farmers. With the help of Dick Croft at PATS, several farmers have successfully grown commercial sponges, but none of the farmers have been able to export them because they did not know how to contact buyers. In contrast, RRE in Majuro, with the help of various aquaculture experts, successfully grew its first giant clams for the aquarium market in 1996, but it was not until 1999 that RRE was able to find buyers in Canada and the U.S. RRE sent representatives to attend several trade shows where they met several potential buyers. Now, RRE has the enviable problem of having more orders for its giant clams than it can fill.



## Government Support

If there are commercially viable export products in Micronesia and there are local business managers who are able to develop and manage a locally owned Micronesian export industry, and there are several development programs ready to provide technical assistance, why have the local business owners in Micronesia never built on their success in the local retail market and developed some of Micronesia's obvious export products?



## Team

A typical export business employs people who produce products, people who market and sell the products and people who oversee the whole operation. Looking back at the various attempts to develop an export industry in Micronesia, one finds that all of these positions were identified and people were hired to fill them. Nevertheless, almost all of the export ventures in Micronesia failed: because production was inconsistent both in respect to quantity and quality or because the markets disappeared or could not be reached competitively; or because the managers, whether expatriates or local managers, failed to find a way to manage effectively. To prevent the same failures from being repeated over and over again, we need to assess what is required to develop and manage a successful export business in Micronesia.

## Local Owners

The most important position that must be filled in any Micronesia business is the position of owner/operator. To succeed in Micronesia, the owner/operator must be a business person who understands that the business must make a profit in order to be a success. Government initiated businesses may start with the goal of making a profit, but they also have other goals such as creating local employment and utilizing local raw materials. In Micronesia these other goals have led governments into the difficult position of trying to make a profit from tuna and copra with a local workforce. When they have failed, the political consequences of admitting their failure have been weighed against the benefits of cutting losses by closing the business. For a business owner, who is spending his own money, business decisions like cutting losses are more obvious. These decisions are also easier to make since they are made in private with little risk of public embarrassment.

Building an export industry with local business owners allows us to tap into the energy and diversity of the local business community. Businesses in Micronesia have had to diversify in order to grow. To grow a business in Micronesia, the owner/operator must



be constantly diversifying into new products and services because small islands with small populations have small markets. One business owner in Micronesia, for instance, started with a stevedoring contract and diversified into construction, sand dredging and manufacturing concrete blocks. Another started as a travel agency and car rental and added a multi-unit apartment building, followed by a twenty-five room hotel and restaurant and dive shop. This same growth strategy has been used by Robert Reimer Enterprises in Majuro in the Marshall Islands, which went from general retail to hotels and bottled water production to aquaculture. Aquaculture development requires a large upfront investment and takes a long time to produce a positive income, but when aquaculture is developed within the context of an existing diversified business, the upfront investment is significantly reduced. This is because the business owner can use the personnel, facilities and cashflow from his other businesses to support the development of the aquaculture venture.

Although the strengths that business experience and business assets bring to an export development project are crucial, they are probably not as important for the success of the venture as local ownership. A local owner, even if he or she is an expatriate, has a place in the local community and with it local connections and support that translate into local authority and power. This fact is important, because eventually any business success in Micronesia will be challenged by local rivals. For example, family members will question whether or not the business owner really owns the land that the business is on so that they can claim ownership themselves and take over any of the business assets that happen to be on the land. Landlords will seek to “renegotiate” the terms of the lease or rent agreement, thereby raising the rent or the lease payment to a point where the business owner must either close the business or pay the landowner a rent that makes the landowner a virtual partner. Rivals can also use political influence to undermine or even shut down a successful business for the purpose of starting a similar business of their own. When these inevitable challenges occur, it is important that the business owner have sufficient local authority to confront them. It is even better if the local owner has so much local authority that no one is willing to mount any challenge at all.



Another benefit of local ownership is that many of the larger locally owned businesses in Micronesia are family businesses. As such, the owner is able to draw on his/her traditional authority within the family to obtain the cooperation and support of his employees who are, for the most part, family members. It is one thing to stay home from work when the manager is a stranger; it is a different matter entirely to skip work when the owner is your father or your uncle. This is true everywhere, but it is more significant in Micronesia where one’s place in one’s family is a primary concern.



Most family owned businesses in Micronesia, though, must employ individuals outside of the family who have no obligations to the business apart from their responsibility to their job. Consequently, traditional family authority can take a local business owner only so far. To go beyond this, any business owner in Micronesia must understand and appreciate what motivates his/her Micronesian employees. From my discussions with several successful business owners in Micronesia, no simple rule or single set of guidelines has emerged on how to motivate Micronesian employees. All of the business owners I have spoken to have indicated they had to work this out for themselves. Even though every solution was different, all of the owners emphasized the importance of knowing their employees personally and understanding how the local culture makes demands on them.

## Technical Assistance

Micronesian business owners who want to develop a Micronesian export industry usually lack experience producing a product, as well as the necessary contacts and connections in markets outside of Micronesia. Consequently, production and marketing expertise must be brought in from outside the business. All of the export development projects in Micronesia—from tuna to coconut soap to sponges and giant clams—have benefited from experts from a variety of development programs. These experts have been most