

# Bilateral Aid to a Small Island Developing State: The Case of the Federated States of Micronesia

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## Abstract

Most of the world's Small Island Developing States (SIDS) are heavily dependent on foreign aid. Since many factors affect the volume of aid, SIDS constantly encounter unpredictable funding for both development and fiscal needs. This study argues that recipient countries may be able to predict the trends of aid by systematically organizing historical and current data; identifying determinants; analysing trends in the international aid community; and examining relations among provider countries. It examines the case of the Federated States of Micronesia (FSM) and addresses three central questions: 1) who are the significant and emerging bilateral aid providers? 2) what is the history of bilateral relations with each significant provider before and after the FSM became a nation? 3) what are the main determinants of aid giving? The study finds that the main determinants are strategic alliance and regional stability. The findings also suggest that significant providers will continue to provide aid to the FSM although the shares of aid volume may be changed.

**Keywords:** foreign aid, aid determinants, aid donors, small island developing states, Micronesia

**Subject classification codes:** economic assistance, small developing island countries

## Introduction

The world's Small Island Developing States (SIDS) share similar challenges: they are geographically small and remote; they have a narrow resource and export base; and they are exposed to global environmental challenges, external economic shocks, impacts from climate change, and frequent and intense natural disasters (Sustainable Development Goals Knowledge Platform, 2019). Because of these challenges, most of these states are heavily dependent on foreign aid. SIDS are vulnerable to other countries' foreign aid decisions, which consist of many influential factors such as international relations among aid providers, bilateral relations with providers, multilateral relations with inter-governmental and non-governmental agencies, and aid providers' domestic politics. The recipient countries constantly encounter these unpredictable circumstances and it's difficult for them to make long-term development plans.

This study argues that recipient countries may predict the trends of aid flow by systematically organizing historical and current data; identifying determinants; analysing trends in the international aid community; and examining relations among provider countries. It examines countries that provide development aid to the FSM. Since the study focuses on providers' intentions and their national interests, multilateral aid providers will not be discussed.

This study also examines current and emerging aid providers in a descriptive way and uses available numeric data to illustrate and support the descriptions. The data is extracted from reliable sources, such as the Organisation for Economic Co-operation and Development (OECD); however, there may be discrepancies among data provided by other intergovernmental organizations, non-governmental organizations, aid provider agencies, and partner agencies for multiple reasons: different fiscal years are provided, what was included varied; and there were differences in the use of constant dollars or current dollars, exchange rates, time of disbursement, etc. Nonetheless, these discrepancies do not undermine the general findings of the study because

the study discusses the historical background, diplomatic relations and determinants of aid of the current and emerging providers.

### **The Case in Micronesia – The Federated States of Micronesia**

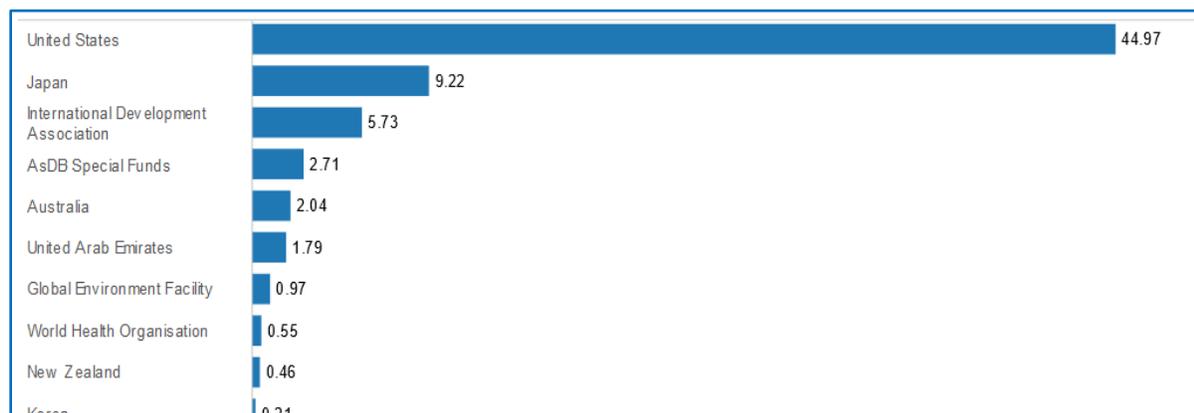
The four states of the Federated States of Micronesia - Pohnpei, Chuuk, Yap and Kosrae each are home to unique peoples and cultures but they share similar colonial era and wartime experiences, as well as similar vulnerabilities to natural disasters and economic challengers. After World War I, these islands were governed by Japan under the South Pacific Mandate by the Leagues of Nations. After Japan was defeated in World War II, the United Nations entrusted the islands to the United States under the Strategy Trusteeship. The stated goals of the Trusteeship were to help the islands in Micronesia move towards autonomy (Yeichy, 2019, p. 176).

In 1965, the Congress of Micronesia was established. The Congress consisted of all Trust Territory islands: the Marianas (except Guam), Palau, Yap, Chuuk, Pohnpei, Kosrae and the Marshall Islands. The establishment of the Congress intended “to assert control over the process of economic development through a series of legislative initiatives” (Hanlon, 1998, p. 142). They tried to look for consultation beyond the Trust Territory government and prepared for negotiations with the U.S. about the future political status of Micronesia. The negotiations began in 1969. After years of negotiations, the Marianas, Palau and the Marshall Islands broke away and negotiated with the U.S. both multilaterally and individually. After a 1978 plebiscite, this left Pohnpei, Yap, Chuuk and Kosrae in the Congress of Micronesia. The Congress of Micronesia chose a freely associated status with the U.S. and eventually became an independent country - the Federated States of Micronesia. The Federated States of Micronesia (FSM) was established in 1979 and became fully independent in 1986. In the same year, the FSM signed the Compact of Free Association with the United States. After the long negotiating period and eventual emergence as an independent nation, the FSM became part of the new Pacific in which sovereign governments are the primary actors, just like other countries established after the trusteeship dissolved. Among these small island developing states, development aid is a vital resource to the nation.

### **Significant and Emerging Aid Providers**

According to the OECD, the top ten aid providers to the FSM in 2015-16 were the United States, Japan, International Development Association (World Bank), ADB Special Funds (Asian Development Bank), Australia, United Arab Emirates, Global Environmental Facility (multilateral institution), World Health Organization (United Nations agency), New Zealand and Korea. China is another significant aid provider; however, China is not on the chart because it is not an OECD member and its aid data (as a provider) is not tracked by OECD.

Figure 1. Top Ten Donors of Gross ODA for Micronesia, 2015-2016 average, USD Million



Source: OECD (2017), Aid at a Glance charts, OECD-DAC, <http://www.oecd.org/dac/financing-sustainable-development/development-finance-data/aid-at-a-glance.htm>

### Bilateral Relations with Aid Providers

There are four significant bilateral foreign aid providers to the FSM: United States, Japan, Australia and China, and three emerging providers: Korea, New Zealand and United Arab Emirates.

Table 1. Diplomatic Relations with Aid Donor Countries

	Diplomatic relations established on	Country ambassador	FSM Ambassador
Significant and providers			
United States	November 3, 1986	Resident	Resident
Australia	July 6, 1988	Resident	
Japan	August 5, 1988	Resident	Resident
China	September 11, 1989	Resident	Resident
Emerging aid providers			
New Zealand	June 30, 1988	Non-Resident (Hawaii)	
Korea	April 5, 1991	Non-Resident (Fiji)	
United Arab Emirates	September 14, 2016		

Source: Countries with which the Federated States of Micronesia has established diplomatic relations. Information retrieved from <http://www.fsmsgov.org/diprel.html>

## **United States**

The United States is the largest aid provider to the FSM, and certainly the most influential one. The U.S. funding is so substantial that it almost doubled the total of all funding provided by other aid providers and multilateral agencies. The U.S. influenced Micronesia even before the FSM became a nation. In 1944, when the American troops landed in Micronesia during WWII, they brought in great quantities of foodstuffs and supplies that immediately brought relief to the islanders. One islander described “a short time later some amtracs landed and brought a great deal of food onto the islet. They brought perhaps a thousand dollars’ worth of food and left it there (Poyer, 2001, p. 239). That was the first time Micronesians received humanitarian assistance from the U.S.

## **Under Strategic Trusteeship**

After WWII, the Micronesian islands were placed under American administration through the United Nation Trusteeship Council in 1947. The UN-US Trusteeship was an arrangement affecting the colonies of those countries defeated at war. The former Japanese mandate, including three archipelagos: Mariana Islands (except Guam), Caroline Islands and the Marshall Islands, were entrusted to the U.S. Under Chapter XII, Article 76 of the Charter of the United Nations, the basic objectives of the trusteeship were “to promote the political, economic, social, and educational advancement of the inhabitants of the trust territories, and their progressive development towards self-government or independence...” (United Nations, 2018). The goal of the trusteeship was that the nations would gain self-government or independence one day. There were 11 territories in the UN Trusteeship system: 7 were in African and 4 were Pacific Islands areas.

Nevertheless, the U.S. insisted upon the region’s strategic importance. As the Japanese had fought hard in the Pacific area to protect their homeland, the U.S. also saw that Micronesia could serve as a buffer against attacks from Asia. During the Japanese Mandate period, Japan fortified the islands in preparation for potential threats from the U.S. The essence of the strategic thrust was the right of denial by the U.S. for any third-party nation to again build military installations in the island. Unlike other colonial countries, such as Germany and Japan, whose main purpose was economic exploitation, America's interest in Micronesia was its strategic location.

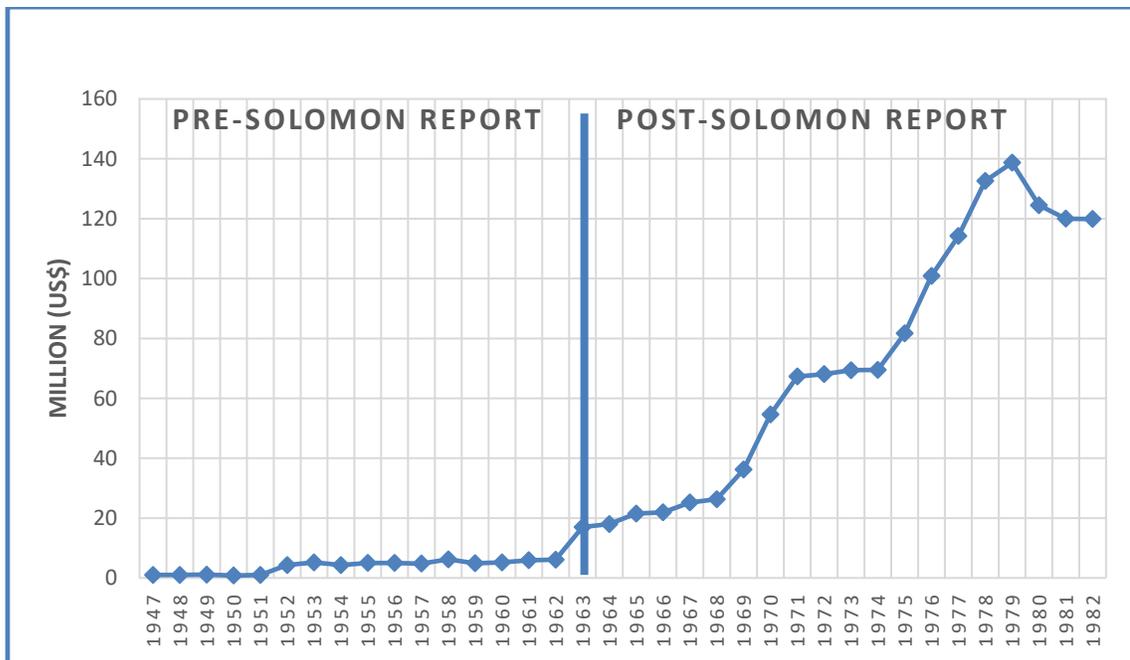
To deny access to Micronesia by other countries, the U.S. sought a “double guarantee” from the U.N. (Lake, 1999, p. 147). The Strategic Trust that was created by the U.N. provided the U.S. with near-total control over Micronesia. There were three major differences between an ordinary trust and a strategic trust. First, the strategic trust “allow[ed] the administering power to fortify the territory and to close parts of it at will for security purposes” (p.147). Second was the location of the U.N. control. Instead of the General Assembly, the Security Council became the location of the U.N. control and that permitted the U.S. to exercise its veto power (p. 147). Last was that strategic trust specified “that the state ‘concerned’ would have final authority regarding any alteration in the status of the territory” (p. 147). As Hanlon describes in the *Remaking Micronesia*, “the document’s [Trusteeship Agreement] terms and conditions reveal just how extensive was American license to control and direct” (Hanlon, 1998, p. 52).

In 1961, the U.N. sent a Visiting Mission to survey the progress in Micronesia and found that the progress in both political and economic development was unsatisfactory. The U.S. had not met the goals indicated in Chapter XII, Article 76 of the Charter of the U.N. In “Our ‘Colonial’ Problem in the Pacific”, Jacobson (1960) identified one of the reasons for the unsatisfactory

development was the security restrictions. Not only foreign investment and alien labor were prohibited, foreign vessels were not allowed to come close to the islands.

**Transition to a Freely Associated State.** The U.S. assumed the islands would eventually gain self-government or independence, although what form that would take was unclear. To ensure a favorable vote in plebiscite and to achieve rapidly minimum but satisfactory social standards, two strategies were implemented: the U.S. sent many Peace Corps volunteers to Micronesia and provided substantial aid to the islands (Dibblin, 1990, p.171-172). The following chart demonstrates the dramatic changes after the 1960 UN visiting mission issued its critical report. Prior to that, the level of subsidies was low and basically flat. In 1963, the U.S. subsidies almost tripled from the year before and reached 17 million dollars. The subsidies continually increased and tripled again in 1970 when they reached 54 million dollars. The subsidies hit the highest level in 1979 and were over 138 million dollars (Schwalbenberg, 1994, p.97). Nonetheless, the aid was not focused on economic development, but on social services, such as education and health services (Hezel, 1984). Besides large amounts of aid, the U.S. government also brought in a large number of federal programs.

Figure 2. United States Aid to Micronesia during Trusteeship



Source: Data extracted from Schwalbenberg, H. M., & Hatcher, T. (1994). Micronesia trade and foreign assistance: Contrasting the Japanese and American colonial periods. *The Journal of Pacific History*, (1), 95-104.

**The Compact of Free Association.** The first Compact of Free Association was signed between the U.S. and the FSM in 1982 and became effective in 1986. The Compact itself is of indefinite duration, however, under Article III, section 213, the economic provisions would expire

after 15 years, in 2001, and the Compact stipulated that negotiations for the renewal of the Compact begin by the 13th year, in 1999. Since the Compact itself would not be expired, the extension of the economic provisions was made under an amended compact act signed in 2003. The economic provisions were extended for 20 years and will expire in 2023. In the original compact, grant assistance was provided in a step-down pattern. The U.S. provided US\$60 million from Year 1 to Year 5, US\$51 million from Year 6 to Year 10, and US\$40 million from Year 11 to 15.

The Amended Compact. The FSM government established the Joint Committee on Compact Economic Negotiations (JCN) in 1997 to handle the negotiation process with the government of the United States. The JCN began its negotiations with the representatives from the United States in 1999 in Honolulu. After years of negotiations, the economic provision in the Amended Compact agreement was finalized in 2003. The Amended Compact provides annual grant to 2023. The Joint Economic Management Committee (JEMCO) was established under the amended Compact. Its functions are: to monitor the funding operations and activities, to review development plan, audit, performance and other reports, to approve grant allocations and changes, and to evaluate and comment on the outcomes (U.S. Embassy, 2018). It consists of five members: three representatives from the U.S. and two representatives from the FSM. The FSM receives a fixed total, \$92.7M, with the annual grant gradually decreasing while the trust fund contribution gradually increasing. The amended provisions provide approximately 45% more funding in total than the original compact, and the goal of the trust fund is to provide a source for the FSM after the provision expires. The funds from the Trust provide for part of the government's operational expenses after the amended economic provision expires in 2023. The FSM Government is also required to contribute to the Trust Fund. However, the FSM Government has not maintained its contribution. The fiscal year 2016 Annual Report indicated that the FSM contributed US\$30.30 million in 2004 but has not contributed any since then.

## **Japan**

Japan is the second largest aid provider to the FSM. It is historically and culturally linked to Micronesia. After World War I, the League of Nations transferred the colonies and territories of the defeated German nation to the allied powers. The Micronesian islands, including the Caroline Islands, the Marshall Islands and the Mariana Islands except Guam, were charged to Japan as a mandate by the Council of the League of Nations (Harris, 1932, p. 691)

Unlike Germany, the former colonizer of Micronesia, the Japanese government was very ambitious about developing the islands. In 1922, Japan established the Nan'yo-cho, a civilian South Seas Agency. The Japanese government extensively developed education and health care programs, but also intensively promoted economic development and immigration of laborers from Japan, Okinawa and Korea. Under the Japanese Empire, the economy in the islands prospered. According to Poyer, by the late 1920s, the mandate began to turn a profit for Japan (2001, p.19). After 1922, Japanese workers, businessmen and government officials migrated to the Micronesian islands. Purcell concludes that the reasons for the successful economic development in Micronesia under the Japanese Mandate were efficient administration, modern technology, well-defined objectives, adequate communication, public works facilities, and improved roads. Most important was the "aspirations [for] a higher standard of living, and [this] increased dependence on a money economy" (Purcell, 1967, p.211).

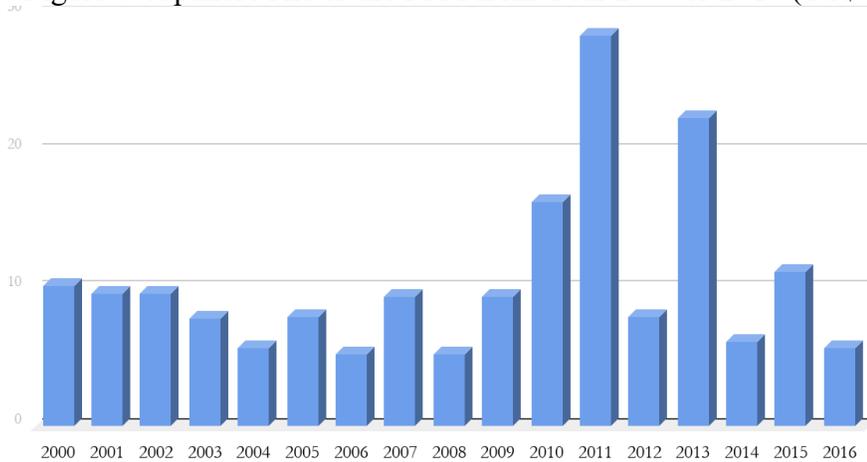
After Japan was defeated by the U.S. in WWII, the surviving Japanese were repatriated to Japan by the U.S. military (Komai, 2001, p. 230). However, many Japanese preserve feelings of friendship with Micronesians and are interested in the island and may have relatives there.

### *Diplomatic Relations*

The FSM government opened a liaison office in Japan on 1984. On August 5, 1988, the two countries officially established diplomatic relations. The liaison office was upgraded to a full embassy in May 1989. The FSM's first ambassador to Japan was Mr. Masao Nakayama, whose father was Japanese (Pearce, 1991, p. 36). After twenty years of relations, in 2008, the first Japanese resident ambassador, Shoji Sato was officially stationed in the Japanese Embassy in the FSM (Government of the Federated States of Micronesia, 2018).

The embassy also gets small-grant funding to help the FSM. The Japanese ODA focuses on large scale infrastructure projects. Figure Three shows that the quantity of Japanese aid fluctuates from year to year but it's not necessarily an indication of unpredictable funding. It could be the large-scale infrastructure projects weren't able to be completed in a single year, therefore, the funding was disbursed in uneven patterns.

Figure 3. Japanese Aid to the FSM from Year 2000 to 2016 (US\$ million)



Source: Data extracted from OECD 2008-2018 annual report: Geographical distribution of financial flows to developing countries: Disbursements, commitments, country indicators.

### *The Determinants of Japanese Aid*

#### **Former Colonies**

Japan's colonial relations with the Micronesian islands began under the Japanese Mandate and ended when the islands were placed under the U.S. Strategic Trusteeship. As of now, the FSM is still culturally linked to Japan. There are a number of descendants of the former Japanese migrants living in the FSM. However, the former colonial relationship doesn't appear to be the

strongest factor when Japan determines whom to give aid to. The top ten recipients of Japanese aid are Asian and Middle East countries that do not have colonial ties to Japan.

### **Economic Interest**

The indicator of economic interests as a determinant is tied aid, which is the procurement of goods and services are restricted to the provider countries as a condition of aid (Ali, 2015, p.125). In the case of Japanese aid, all infrastructure projects funded by the Japan International Cooperation Agency (JICA) must awarded to Japanese companies. Even consulting contracts are likely to be awarded to Japanese consultant firms because the awarded consultant firms work with the project implementing firms during the project cycles.

### **Food Security**

The FSM's EEZ covers close to 3 million sq. km. of ocean of the Pacific Ocean and is one of the richest fishing grounds in the western and central Pacific (Tarte, 1998, p.90). Japan consumes a high volume of tuna that can be divided into three types: dried fish (Katsubushi) for soup base, sashimi and canned. The FSM's EEZ provides about 70% of total tuna consumption to Japan. Maintaining reliable and promising relations with the FSM is crucial.

### **Australia**

After the FSM became an independent country in 1986, it first established diplomatic relations with the United States. Two years later, on July 6, 1988, it established diplomatic relations with Australia, which was the sixth country to exchange diplomatic relations with the FSM. The Australian Embassy was opened in November 1989 in Pohnpei, FSM. The Australian Embassy in the FSM is also responsible for the diplomatic mission to the Republic of Palau, the Republic of Marshall Islands, the Territory of Guam, and the Commonwealth of the Northern Mariana Islands.

#### *Development Aid Policy*

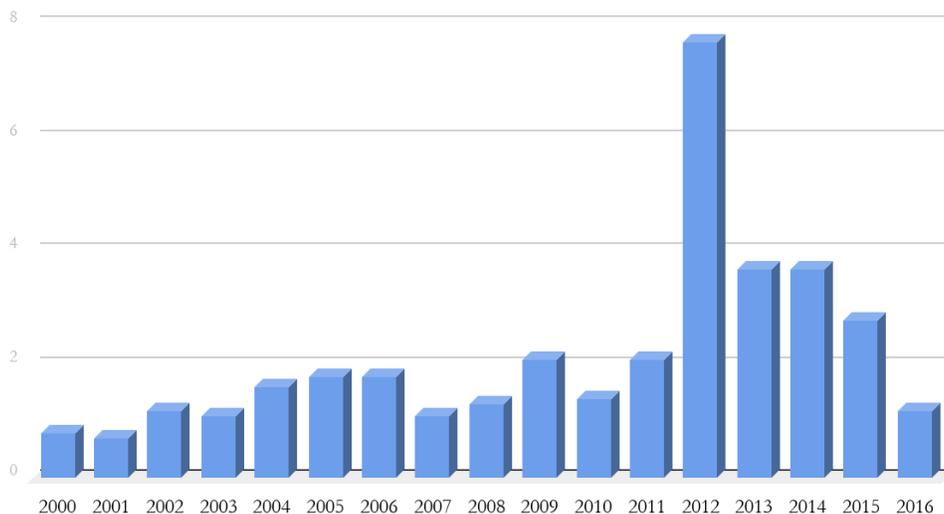
Australia's geographic location and its history have shaped its foreign aid policy. Barratt identified the importance that regionalism plays in Australia's aid patterns (2008, p.162). She believes the isolation from other developed countries makes Australia more vulnerable. One of the major factors in its aid giving pattern is geographic proximity. Therefore, Australia pays special attention to the developing countries in the Pacific and East Asia, especially countries that are close to Australia, have large populations, and are considered politically unstable, for example Papua New Guinea and Indonesia. Australia's aid strategy has not changed much over time, although practices have. The 2006 AusAid White Paper was explicit in linking Australia's security with poverty reduction in the near region of Southeast Asia and Southwest Pacific (Hameiri, 2008, 357). In 2011, AusAid stated in its website that the objective of Australia's aid program is to assist developing countries to reduce poverty and achieve sustainable development, in line with Australia's national interest. Currently, AusAid no longer exists and the embassies oversee the aid programs. One of Australia's strategies in choosing aid programs is to pursue national interest and extend its influence (Australian Government, 2018).

Australian scholars label Australia as neo-liberal and this worldview influences how Australian government gives aid. Hadiz defined neoliberalism as an idea that the “most efficient allocation of resources is achieved by a natural and self-regulating market driven by its own internal laws” (2006, p.67). To extend this idea to politics and international relations, neo-liberalism focuses on the rules and norms that citizens of aid-giving states are socialized to accept by working through international institutions (Devetak, 2007, p. 391).

### *Development Aid*

Prior to fiscal year 2010-2011, Australia appropriated a single allocation to Micronesia as a whole. The aid to Micronesia is divided among the three island states based on their populations. Starting from fiscal year 2010-2011, the government of Australia signed individual partnership agreement with the FSM, the Republic of the Marshall Islands and the Republic of Palau respectively. On August 4, 2010, the FSM and Australia entered a Partnership for Development. The Partnership expired in 2015, as the intention of the partnership agreement was to make progress towards fulfilment of the Millennium Development Goals by 2015 (Partnership for Development, 2010). The Aid Investment Plan (AIP) replaced it in 2016. Despite the name changed, the Aid Investment Plan is similar to the Partnership for Development.

Figure 4. Australia Aid to the FSM from Year 2000 to 2016 (US\$ million)



Source: Data extracted from OECD 2008-2018 annual report: Geographical distribution of financial flows to developing countries: Disbursements, commitments, country indicators.

### *The Determinants of Australian Aid*

#### **Regional Stability**

As discussed in the Australian aid policy, Australia is a developed country which is not only surrounded by developing countries, but also far away from other developed countries.

Regional security and stability are the top determining factor. As an Australian analyst at the Australian Strategic Policy Institute once stated, Australian aid is a long-term investment in Australia's national security.

## **China**

The FSM officially established diplomatic relations with China in 1989 and the FSM agreed that the People's Republic of China is the only legal Chinese Government (People's Daily New, 1989). The then FSM President John Haglelgam made the first official visit to China since the two countries established diplomatic relations on November 2, 1990 (People's Daily New, 1990a) and the two countries signed an Economic and Technical Cooperation Agreement, in which China agreed to provide untied aid to the FSM (People's Daily New, 1990b).

Among all significant aid providers, China is unique in many ways. First, China is the only developing country which is an aid provider and yet also an aid recipient. The experience of being simultaneously an aid provider and an aid recipient contributes to its unique behaviors. China provides foreign aid to other developing countries under the United Nations Development Program for South-South Cooperation, which encourages "developing countries working together to find solutions to common development challenges" (United Nations Office for South-South Cooperation, 2018).

Second, Chinese aid motivated from the start by ideology and it's still influencing its decision today. During the 1950s when China was in the desperate poverty, it still provided aid to Korea and Vietnam to help them counter any forms of imperialism (Zhang, 2006, p. 59).

Third, China is ruled by one party, the Communist Party. Its government administrators are not accountable to voters. As Elizabeth Feizkhah, an Australian official, said in an interview, "China has freedom of action that Australia, New Zealand and the U.S. simply do not have" (2001, p.22). From a recipient perspective, the freedom is not a bad thing. For example, China built residential houses for the FSM President, Speaker and the Justices in early 2000s. China also contributed one million dollars into the FSM trust account in 2009 and in 2010. These contributions would be more difficult for a democratic country to justify for the "development" purpose.

Fourth, Chinese aid is controversial because the traditional aid providers claimed that Chinese aid is undermining their painstaking work on reform supported by good governance and accountability (Hanson, 2008. p.17). Traditional aid providers use tied aid as a tool to combat corruption and bad governance which inhibit development. However, the interpretation of good governance is dominated by traditional aid providers, such as the U.S. and Australia. China is not intentionally promoting corruption and bad governance, but it has a different understanding of good governance.

Fifth, China is not a member of the Organization for Economic Cooperation and Development (OECD) as an aid provider; therefore, it was difficult to track Chinese aid. Hanson (2009) describes Chinese aid as "secretive aid". Recently, the circumstances have changed. A team from the Research Lab of William and Mary College analyzed Chinese aid using a dataset tracking Chinese aid from 2000-2014. However, data on Chinese aid to the FSM is not included.

*The Determinants of Chinese Aid*

**Economic Interest**

As with Japanese aid, China is interested in providing infrastructure projects to the FSM. The projects were awarded only to Chinese construction companies, with Chinese construction workers working on the projects and using building materials imported from China.

**Strategic Alliance**

The FSM is the only freely associated state in the Western Pacific that has diplomatic relations with China. The Republic of Palau, the Republic of the Marshall Islands have diplomatic relations with the Republic of China (ROC) aka Taiwan. Therefore, the FSM is an important strategic partner for China in the Western Pacific.

Table 2. The Determinants of Aid Giving

	<b>U.S.</b>	<b>Japan</b>	<b>Australia</b>	<b>China</b>
Economic interest		<b>X</b>		<b>X</b>
Food security		<b>X</b>		
Former colonies	<b>X</b>	<b>X</b>		
Regional stability	<b>X</b>	<b>X</b>	<b>X</b>	
Strategic alliance	<b>X</b>			<b>X</b>

**Emerging Aid Providers**

New Zealand, Korea and the United Arab Emirates are the emerging aid providers to the FSM. The volumes of aid are comparatively small, but they are consistently providing ODA to the FSM. If the FSM development plans align with their national interests and development policies and goals, these countries will potentially become significant aid providers to the FSM.

**New Zealand**

New Zealand is the ninth top donor to the FSM. The aid is provided through the North Pacific Development Fund (NPDF), which covers funding to the FSM, the Republic of Palau and the Republic of the Marshall Islands (New Zealand Foreign Affairs & Trade, 2018). The top ten New Zealand aid recipients are neighbouring island states in the Pacific, for example, Vanuatu, Solomon Islands and Papua New Guinea. The pattern demonstrates that regional stability is the most important factor in determining whom to give to.

## **Korea**

Korea is the tenth top donor to the FSM. However, the volume of Korean aid is very small and variable. The aid was between US\$100,000 to US\$300,000 a year. Korean aid focuses mainly on Asian and African countries. In the Pacific region, Korean aid is focused on Fiji and the Solomon Islands (Korea International Cooperation Agency, 2018). However, the issues Korean aid tackles in the Pacific are climate change and natural disasters, which also concerns the FSM. Korean could potentially increase its aid if the FSM can demonstrate its commitment on these issues.

## **United Arab Emirates**

The FSM established diplomatic relations with the United Arab Emirates (UAE) in 2016. The UAE gave the FSM US\$1.78 million in 2015 and US\$1.79 million in 2016 (Ministry of Foreign Affairs and International Cooperation, 2015 & 2016). Their development goals have aligned with the United Nations Sustainable Development Goals (SDGs) in 2016.

## **Implication**

U.S. funding overshadows aid from other provider countries. With the current fiscal status in the FSM, if the U.S. does not extend economic provisions to the FSM, the FSM must search for other aid providers. According to providers' patterns of behaviour, one or multiple aid providers will step in for many reasons. Among all the factors, regional security is one of the top determinants for providing aid. This study implies that if the U.S. withdraws development aid, which is a vital source of funds for the FSM, other developed countries will fill the void and step in to be the lead aid provider. The following section discusses implications for the FSM and the aid provider countries.

## **Federated States of Micronesia**

The FSM is still heavily dependent on foreign assistance. Negotiation of economic provisions to the country after 2023 must be started soon. If the U.S. decides not to amend or extend these provisions, the FSM will have to seek foreign assistance with other provider countries. A number of provider countries will be interested filling the void. However, it will be extremely challenging for the FSM. Transition phases are almost guaranteed to be problematic and complicated. First, individual providers may approach and negotiate with individual states or political leaders. Diverse opinions or decisions may further divide the country. Third, since no country will be able to completely replace the U.S., the FSM may likely have to deal with multiple providers. Since each provider has its own ideology, agenda, domestic politics and policies, the FSM may be pulled in different directions, which will make long-term development planning even harder.

## **United States**

The U.S. will likely amend or extend economic provisions to the FSM. The expiration for economic provisions is not equal to the expiration for the termination of the Compact of Freely

Association Agreement. Because of the government funding deficits, however, the FSM will still have to approach other providers. In the three freely associated states, the FSM is the only state that has diplomatic relations with China. Both the Republic of Marshall Islands and the Republic of Palau have diplomatic relations with the Republic of China (Taiwan). If the U.S. steps down as the FSM's lead provider, it will give China a chance to increase its presence in the western Pacific. The U.S. may not want to see a non-ally country step in as a lead provider.

### **Australia**

If in case the U.S. steps down from the lead provider position, for the sake of regional security, Australia may substantially increase its aid to the FSM. The U.S. is their ally and is currently the FSM's lead provider, while Australia is the lead aid provider in the southern Pacific. There is no reason for these allies to overlap their efforts in one region. Nonetheless, if the U.S. is no longer the lead provider, Australia concern for regional security gives it the strongest reason to step in. However, domestic politics has major effect on international relations. An increase in the volume of aid does not mean the funding will go to areas the FSM targets, nor will be able to meet all its needs.

### **Japan**

Although both regional stability and food security are the determinants of aid from Japan, Japan has comparatively less incentive to step in to become the lead provider in the FSM if the U.S. decides not to extend economic provisions. According to the pattern of Japanese aid flow, Asia is more crucial than the region of Oceania. For food security there is no obvious reason to believe that the lead provider country, whoever assumes the role in the future, will prohibit Japanese to fish in the FSM's EEZ as long as Japanese fishing vessels comply with international and local laws and regulations.

### **China**

Of the three freely associated states in the western Pacific, only the FSM has diplomatic relations with the People's of Republic China. The other two freely associated states have diplomatic relations with Republic of China (Taiwan). It's much easier for China to increase its aid to the FSM, because policymakers in China do not have to seek electoral approval. Furthermore, China has very lax policies on the sectors it funds. However, because of the characteristics of Chinese aid: the fluctuation of aid flow; over-emphasized infrastructure and construction projects; and a lack of consistent aid policies, the FSM may not be truly benefit from the aid in the long term.

### **Conclusion**

Fulfilling aid providers' agendas does not have happen at the expense of the partner. A win-win situation is possible, and the partner is key. To be more precise, the partner's national government is key. The partner's national government should proactively manage the relationship and partnership, making certain the national development plan and national policies are implemented as planned, and ensuring that local needs are met.

### **Anticipating the Future**

The economic provisions of the Compact of Free Association will expire in 2023. The FSM and the U.S. will soon negotiate whether or not to extend the provisions beyond 2023. It is likely the U.S. will continue to provide substantial grant and financial support to the FSM. However, in case the U.S. decreases its financial support of the FSM, it is optimistic to say that other ODA providers, such as Japan, Australia, New Zealand, Korea and China, will fill the void because of the FSM's geographic importance.

Studies on foreign aid are important for developing countries, especially the SIDS that are highly vulnerable to external factors; however, studies in this area are scarce. Studies that focus on the impact of aid providers' agendas on their partners' policymaking; factors that influence the distribution of aid among national governments, state governments and local communities; and the inclusiveness and participation of local communities in development planning can be useful evaluation tools when negotiating foreign aid agreements.

These studies will provide a more complete and clearer picture of the effectiveness of development aid. Like other aid-dependent developing countries, SIDS' government operations and development depend on various external factors such as unpredictable aid flows, changes in diplomatic or international relations, as well as uncertainty of aid providers' domestic politics. This case study is significant because it demonstrates that by systematically examining aid determinants, aid flows and trends of aid providing countries, recipient countries may foresee problems and seek solutions in advance. The findings of such examinations allow recipients' countries to manage aid providers and aid received; to expand development goals; and to improve development plans.

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