

REPUBLIC OF NAURU  
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## 1. Executive Summary

Nauru is a tiny Central Pacific nation of 21km<sup>2</sup> and populated by about 11,000 people. In 1975 it was the second richest country in the world (measured in GDP per capita) due to the abundance of phosphate mined on the island. However, phosphate exports fell from 2 M tonnes in 1980 and 926,000 tonnes in 1990 to a mere 5,000 tonnes during the first 10 months of 2004. The revenues of the past were not well invested, and today Nauru is practically bankrupt and dependent on outside support.

Nauru's current economic situation is grave and there are very limited opportunities for economic growth. Nauru has few resources; some phosphate remains but mining would require significant and costly repairs to infrastructure. Other possibilities are fishing, some limited tourism, very limited agriculture and some private development for general construction/maintenance and possibly local manufacture.

Nauru's current national budget is effectively supported by the government of Australia. In late 2001 under the 'Memorandum of Understanding for Cooperation in the Management of Asylum Seekers and Related Issues' Australia committed a total of \$41.5 million to Nauru. The MOU was renewed in 2004 in which Australia committed a further AUD \$29 million. One other source of income is fishing licenses issued to China, Japan, South Korea, Taiwan and the United States of America.

In addition to this drastic loss of income there has been a long period of neglect including of social sectors and infrastructure. All infrastructure except the government buildings are in a very poor state of disrepair. Many subsistence skills including fishing have been lost and will need to re-learned. The education and health sectors have deteriorated and suffer from a chronic shortage of skilled staff. Widespread illiteracy is reported amongst young people Lifestyle diseases, truancy in schools and low educational attainments are symptomatic of the neglect of the social sectors.

Basic services are being supported by the government of Australia including electricity and drinking water; for the later Nauru is dependant on two reverse osmosis plants. Nauru has only one square kilometre suitable for food production so is dependent on shipping and air services for the provision of food and other supplies, notably from Australia. There is no operating bank.

From a total "welfare-state", the country and its population will have to face the harsh reality of a world in which they will have limited resources and thus limited wealth. In 2004 the government put in place an austerity budget and with support from the government of Australia is addressing key reforms. Even so the political crisis necessitating a general election in October 2004 is indicative of an overall lack of nationwide commitment to the adjustments that are required following loss of the phosphate revenue and near bankruptcy of the country.

Nauru joined the ACP group in 2000, when it became a signatory to the Cotonou Agreement. The 9th EDF allocations are €1.8 million for the A-envelope and €0.5 million for the B-envelope. The CSP/NIP was signed on 17 August 2003. The area of concentration is the energy sector, in particular the promotion of new and renewable sources of energy, which has been allocated 85% of the A-envelope.

## **2. Update on Political, Economic and Social Situation**

Nauru's short history of European contact is informative. Germany and the United Kingdom first mined for phosphate in 1907. In 1920, a League of Nations mandate named Australia, New Zealand and the United Kingdom as co-trustees of Nauru, with Australia the administering power and phosphate mining was taken over by the British Phosphate Company owned jointly by the trustees. During World War II Nauru was occupied by Japanese forces. The population was then 2000 and 1200 Nauruans were shipped to the Federated States of Micronesia, where 463 died of starvation. In 1947 Nauru was placed under United Nations Trusteeship, with Australia the administering power on behalf of the co-trustees; Australia, New Zealand and the UK. The British Phosphate Company continued mining until 30 June 1970, when control passed to the Nauru Phosphate Corporation (NPC). Nauru became self-governing in January 1966 and an independent state in January 1968.

In August 1993 the Governments of Australia and Nauru signed a Compact of Settlement which ended litigation by Nauru against Australia in the International Court of Justice over rehabilitation of phosphate land mined before independence. As part of the settlement Australia paid Nauru \$57 million in cash and agreed to provide \$50 million over a period of twenty years (paid in annual instalments of \$2.5 million indexed at 1993 values) for projects to be undertaken under a Rehabilitation and Development Cooperation Agreement. Since 2001 the government of Australia has provided considerable support to Nauru through a series of Memorandum of Understanding.

The President is elected by and responsible to Parliament and is both head of government and head of state. The Nauruan Parliament consists of eighteen Members of Parliament (MPs), who are elected every three years by resident Nauruan citizens over the age of twenty. Nauru is divided into fourteen districts, which are grouped into eight electoral constituencies. There are no formal political parties in Nauru. Candidates stand as independents, contesting elections on the basis of personal or family ties. Loose and fluid alliances develop in Parliament, usually on the basis of extended family ties. Government is formed by a coalition of like-minded parliamentarians, with a majority of at least ten votes. At its first sitting, Parliament chooses a Speaker and a Deputy Speaker, before proceeding to elect the President from among the remaining members. The President then appoints four or five members of Parliament to form the Cabinet.

### **2.1 Update on Political Situation**

Following independence, Nauru's political system was very stable. Hammer DeRoburt, the island's traditional tribal chief, served as President for most of the period from 1968 to 1989 (in 1977 he briefly lost the Presidency to Bernard Dowiyogo). However, from January 2003 to June 2004 Nauru had six Presidents. The current Ludwig Scotty government first came into power in May 2003 but its reforms did not suit other members of Parliament and Rene Harris was returned as President following a vote of no confidence in August 2003. Ludwig Scotty regained the Presidency on 22 June 2004, following a vote of no confidence against Harris. President Scotty appointed a young, pro-reformist Cabinet and affirmed his intention to address the long-term issues facing Nauru.

On 30 September 2004, President Scotty declared a state of emergency, dissolved Parliament and announced a general election would be held on 23 October 2004. This action was

prompted by a stalemate in Parliament over the Speaker's suspension of the Health Minister blocking the Government's attempts to present its budget before supply ran out on 30 September 2004. President Scotty's government received strong support from the electorate and in October 2004 the reformist budget was passed.

In May 2005 Nauru shifted its diplomatic allegiance from China to Taiwan after three years of recognizing mainland China. Previously, Nauru recognized Taiwan from 1980 through 2002.

Women still have no representation in the Parliament and are grossly under-represented at the higher levels of government service and in the NPC, which is the next largest employer.

## **2.2 Update on Economic Situation**

Economic indicators for Nauru (such as GDP, inflation and GDP growth) are not available.

Nauru's current national budget is effectively supported by the government of Australia. In late 2001 under the 'Memorandum of Understanding for Cooperation in the Management of Asylum Seekers and Related Issues' Australia committed a total of \$41.5 million to Nauru including fees associated with Nauru hosting their asylum seeker processing centres on behalf of the Government of Australia and development aid for health and education, essential power, water and ports infrastructure. The MOU was renewed in 2004 in which Australia committed a further AUD \$29 million including for the deployment of in-line finance and police officials to Nauru whilst continuing support of basic services. Australia continues to support a small scholarship scheme and pays AUD \$2.5 million per year to the Rehabilitation and Development Cooperation programme under the Compact of Settlement signed in 1993 by Australia and Nauru to end litigation by Nauru against Australia in the International Court of Justice over rehabilitation of phosphate land mined before independence.

The main objectives of the in-line finance team funded by the Australian government is to develop a viable, sustainable, balanced budget; determine the net worth of the country; work on the removal of Nauru from the FATF of non-cooperative countries, and come to the subsequent establishment of a commercial Bank and public diplomacy. The 2004 budget aims at broadening the tax basis and has introduced salary saving measures, which would be necessary but unpopular with the general population, hence the need for public awareness raising on the general financial situation.

Determining the "net worth" of the country is a difficult task as there are no recent audit reports available at all, neither of Government Expenditures, nor of the semi-independent public corporations like the Nauru Phosphate Corporation. Determining where assets are is the more difficult exercise (the liabilities will not fail to turn up) given the complexity and non-transparency of the trust-fund constructions plus the total absence of reliable past information and may take until end 2005 or later.

Working in removing Nauru from the FATF-list of non-cooperative nations is the other main assignment of the finance team. Legislation is being introduced aiming at satisfying basic requirements. Most of this is still on paper, the problem is implementation, especially with complicated matters like the creation of a Financial Intelligence Unit. In its 2004 report, FATF welcomes Nauru's efforts to eliminate shell banks but requires additional steps to ensure previous shell banks are no longer operating before FATF will consider removing sanctions.

### **2.3 Update on Social Situation**

There are no publicly available studies on the current social situation however anecdotal evidence indicates a number of concerning trends.

There are indications that young people are opting out of formal education by not going to school. This is attributed to a lack of parental value for education and lack of parental control. Schools are in a poor state of disrepair. Students still attend the government's one secondary school although it is almost derelict. The government of Australia pays an additional salary to teachers to encourage them to attend and teach. Non state actor representatives report very high levels of illiteracy amongst young people. An increase in teenage pregnancy, alcohol abuse and thieving by young men is also reported. Unemployment generally and particularly among the youth is a key issue facing Nauru and experience from other parts of the Pacific show a link between youth unemployment and social unrest.

There are also reports of elderly and young children experiencing hunger with families facing shortages of food and cash. It is vital to start activities such as small scale fish farming, gardening and placing of fish aggregating devices to increase local food production. Even here there are difficulties with individuals living on leased land reporting that food they have grown in small garden plots is removed by the landowners. Improving the social situation of Nauru may take even more concerted effort than that given to its economic situation.

Nauru's migrant worker community are particularly affected. Living in sub-standard even derelict and overcrowded accommodation many families from Kiribati, Tuvalu, China and the Philippines have not been paid for over a year and do not have the means to return to their home countries. Their skills are however still key to the people of Nauru. The Kiribati and Tuvalu communities fish in the reef waters to feed their families and sell fish to Nauruans. Many also work in the small shops and restaurants which still eke out an existence on the island.

### **3. Development Agenda of Nauru**

The National Policy Objectives and development strategies for the medium term are set out in the Nauru Development Plan (2002-2006). Recommended priorities for reform include (i) addressing the structural budget deficit through expenditure reduction, improvements in revenue collection, and new revenue measures; (ii) restructuring the trust funds; (iii) overhauling arrangements for the management of public finance and public enterprises; (iv) reassessing arrangements for the provision of air services by Air Nauru; and (v) re-establishing commercial banking services. The government which was elected in May 2003 committed to return to the fiscal and financial reform program initiated in 1998. The high priority areas identified in the 2004 budget speech are public service salaries, education and health. All government officials receive a salary of just AUD \$100m per fortnight.

### **4. Overview of past and ongoing cooperation**

Nauru joined the ACP group in 2000, when it became a signatory to the Cotonou Agreement. There is therefore no record of past cooperation. The Country Strategy Paper was signed on 17 August 2003.

#### **4.1 Focal sectors and macroeconomic support**

The 9th EDF NIP foresees an allocation of €1.8 million for the A-envelope and €0.5 million for the B-envelope.

The 9th EDF NIP Focal sector is Support to the Energy Sector, especially the identification and use of new and renewable sources of energy 85% of the A-envelope (€1.53 million) has been allocated to the focal sector. As such Nauru is one of the countries addressed by the '*Support to the Energy Sector in five ACP Pacific Islands*' Project which should be operational toward the end of 2005.

There is no real power utility in Nauru, the production and distribution of electricity (as well as of drinking water) to its citizens has traditionally been a side business of the Nauru Phosphate Company.

Electricity tariffs in Nauru are extremely cheap and do not cover the costs of production and distribution. Despite extremely low tariffs there appears to be a very poor discipline concerning the payment of electricity bills. There is thus no incentive to reduce consumption and excessive use or even waste of energy is widespread. One possibility is to use the EC renewable energy programme for the procurement and installation of a prepaid metering system for electricity. The main alternative to demand side measures under the renewable energy programme would be the installation of solar panels. One study carried out in 2002 estimated that the installation of PV with a capacity to produce 100kW peak would cost roughly EUR 800,000 and would save some 60 tonnes of diesel per year. At the present moment it would appear that the saving potential with a comparable investment would by far outweigh the power production capacity of a PV installation, but that will have to be determined during the start-up phase of the programme. Furthermore, institutional reforms are also necessary, if not a precondition, particularly the organisational separation of power production from NPC.

#### **4.2 Projects and programmes outside focal sectors**

There are no projects and programmes outside focal sectors.

#### **4.3 Utilisation of Resources for Non State Actors**

Of the 1.8 million Euro in envelope A, 15% i.e. 0.27 million Euro is allocated to NSAs for '*projects in the area of income generation and employment, in particular concerning Women in Development, Youth Development and training and other employment generating areas and social areas.....including capacity building*'.

There are few functioning NGOs apart from the National Council of Women which is given some support by the government's Department of Women's Affairs. NIANGO – Nauru Association of NGOs existed in the past but is now defunct. Most NGOs are run by people also employed as government officials. Churches are active in the social sector but to a limited extent.

A new development resulting from the current financial crisis is the formation of community based groups headed by unemployed women. These groups are crossing family barriers bringing different families living in the same area together to address immediate needs. The Cabinet Secretary highlighted this as a new phenomenon in social organisation for Nauru which traditionally organises in family groups.

A workshop was held in December 2004 attended by over 50 non-state actor groups which identified the need for training to support the development of NSAs and for projects in women and youth development in particular in the area of micro-enterprise. There are a number of implementation problems which need to be resolved including the lack of banking facilities. The Australian government works through a local entrepreneur as a sort of clearing house. The key programming priority for 2005 is the finalisation of a financing agreement for the NSA programme.

#### **4.4 Utilisation of Envelope B**

Nauru is situated near the equator and is therefore outside the “cyclone belt”. Unlike other Pacific island countries it is therefore less likely to need support from the B-envelope for post-disaster rehabilitation. It was therefore suggested to use Nauru’s B-envelope under the 9<sup>th</sup> EDF (EUR 500,000) to mitigate adverse effects of instability in export earnings to support activities in the focal sector of the A envelope. The FLEX procedures are now being addressed by the authorities in Nauru.

#### **Regional Cooperation**

Regional cooperation programmes address some of the key needs of Nauru’s development including food production (DSAP); education (PRIDE) and fisheries.

#### **9<sup>th</sup> EDF**

The regional allocation amounts to €29 million and includes three focal sectors “Economic Integration and Trade” (€9 million), “Human Resources Development” (€8 million) and “Fisheries” (€5 million) and a non-focal sector, for extension of the 8<sup>th</sup> EDF programmes to the 6 new ACP countries (€7 million).

#### **Regional Economic Integration Programme (REIP) - €2.2 million**

The programme aims to assist the region in strengthening its capacity to implement PICTA (free trade area among the Pacific island countries), negotiate trade agreements with developed partners (eg. EPA), participate in multilateral trade negotiations (WTO) and assist the private sector in addressing supply-side constraints. The Financing Agreement was signed in February 2004 immediately followed by the recruitment of TA. A mini-work programme was approved for the period July to December 2004 to cover the recruitment phase and to commence implementation of project activities.

#### **Human Resources Development (HRD) – PRIDE (Pacific Regional Initiative for the Development of Education) - €8 million**

The objective of the programme is two-pronged: to assist Pacific island countries (PICs) in develop a sector-wide strategy for Education and subsequently to finance the implementation of some parts of that strategy. An education planning workshop was held in Nauru in November 2004 and the resulting Education Plan will be presented to the government in early 2005.

#### **Fisheries - €5 million**

This section comprises two projects:

##### **a) Extension of PROCFISH to the 6 new ACPs - €1.997 million**

The Financing Agreement was signed in February 2004 followed by the recruitment of TA and implementation of some activities. The objective of the project is to assist Pacific ACP countries better manage their in-shore fishery by providing basic information on in-shore fish

stocks. The project undertakes a comparative analyses of reef fisheries in the Pacific ACP countries. This provides scientific information to governments including local communities ensuring effective management of the resource. The 2005 work plan includes in-country field work in all the new Pacific ACP countries.

b) DEV FISH, a project to be managed by the Forum Fisheries Agency (FFA) in collaboration with the Secretariat of the Pacific Community (SPC) - €3 million. A financing decision was made in December 2004 with the Financing Agreement to be signed in March 2005. Implementation should commence immediately thereafter.

The objective of the project is to increase benefits received by PICs from the sustainable use of marine resources by increasing the capacity to directly participate in the tuna fishing and processing industry, and through the reinforcement of national and regional policies and strategies in the sector.

#### **Non-focal sector - €7 million**

The non-focal sector is mainly composed of the extension of 8<sup>th</sup> EDF Natural Resource projects to the 6 new Pacific ACP countries including Nauru. All such extensions have been approved and implementation has commenced as per the table below.

PROJECT	EURO Millions	EDF SOURCE	STATUS
SPC/DSAP ext.	1.981	9th NF	Approved. FA signed in Feb 2004
SPC/PPP ext.	1.512	9th NF	Approved. FA signed in Feb 2004
SOPAC ext.	2.55	9th NF	Approved. FA signed in Feb 2004
SPREP/PIEN ext.	0.56	9th NF	Approved. FA to be signed in March 2005.

#### **4.5 8<sup>th</sup> EDF and balances of previous EDFs**

This is not applicable to Nauru.

#### **4.6 Other instruments**

There are no other instruments. Community budget-lines and STABEX are not applicable to Nauru.

### **5. Programming Perspectives for the coming year**

The key programming priority for 2005 is the finalisation of a financing agreement for the NSA programme and start-up of the energy programme.

### **6. Dialogue in Kiribati with National Authorising Officer and Non State Actors and Donor Coordination**

#### **6.1 Dialogue in Kiribati with National Authorising Officer and Non State Actors**

There have been a series of missions to Nauru all of which have included discussion with the NAO who is the Permanent Secretary for Foreign Affairs. The Head of Delegation mission to Nauru in September 2004 was preceded by a mission of the Delegation's rural development adviser and the Kiribati and Nauru programme adviser. In October 2004 the Delegations' energy adviser carried out an assessment of the energy situation and in December the programme adviser and desk officer from Brussels conducted a consultative workshop with NSAs. Communication outside of missions proves problematical.

A workshop held in December 2004 attended by over 50 non-state actor groups identified the need for training to support the development of NSAs and for projects in women and youth development in particular in the area of micro-enterprise. There are a number of implementation problems which need to be resolved including the lack of banking facilities. AusAID works through a local entrepreneur using it as a local clearing house. The key programming priority for 2005 is the finalisation of a financing agreement for the NSA programme.

## **6.2 Donor Coordination**

The Pacific Forum Secretariat has staffed a “Foreign Aid Management Unit” in the Ministry of Foreign Affairs. Donors now active in Nauru are Australia, ADB, Taiwan and the European Commission. Nauru plans to hold a donor coordination meeting in November 2005 in Fiji. The energy sector is a main concern for both ADB and AusAID since it constitutes an enormous drain on donor resources (at the moment exclusively financed by AusAID). ADB and AusAID are jointly sending a three person team to Nauru to identify ways to split the water and power production components from the NPC and to reduce the dependency from diesel oil imports. There is good liaison with the European Commission 5 Country Renewable Energy Programme.

## **7. Conclusions**

Nauru is in a serious economic condition and can currently only survive with outside support.

Even though the accurate financial situation of Nauru cannot be determined at this stage, it is very evident that the country is virtually bankrupt. From a total “welfare-state”, the country and its population will have to face the harsh reality of a world in which they will have limited resources and thus limited wealth. This will imply a total change of mentality.

Following the clear support for Nauru from Pacific Island Leaders the European Commission has taken steps to accelerate its cooperation programme. A crucial obstacle is the implementation mechanism, as there is no banking system in place. The orientation of our programmes remains very valid; both energy and NSA-support are crucial and are complemented by regional programmes.