

N A U R U
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1. Executive Summary

Nauru is a coral island of only 21 km², with an exclusive economic zone of 320,000 km² in the central Pacific, and has a population of about 12,000.

The political situation has been marked by considerable uncertainty in recent years, with successive changes of government and president. The current President, Mr. Ludwig Scotty, was re-elected by MPs less than a year after he left office after losing a confidence vote in August 2003. He is the 6th President of Nauru since January 2003.

The economic and financial situation continued to deteriorate, as the phosphate reserves, the main natural resource, have become nearly exhausted. A complete collapse of the economy has only been averted by continuing donor support, particularly Australia's humanitarian and development assistance. In 2001, Nauru signed an agreement with Australia to accommodate more than 1,000 asylum seekers on the island, as part of Australia's so-called "Pacific Solution" to curb illegal immigration into Australia, in return for millions of dollars of aid.

Nauru remains on the OECD's Financial Action Task Force (FATF) money-laundering blacklist. In late 2003, following a commitment to improve transparency and establish effective exchange of information on tax matters with OECD countries, it was however removed from the OECD list of tax havens.

With the near depletion of the phosphate reserves and offshore investment revenues, the people of Nauru are facing an uncertain future. With the government and the Nauru Phosphate Company (NPC) no longer able to meet salary expenses and to absorb the increasing number of young job market entrants, youth unemployment has risen to an estimated 35%, impacting severely on standards of living.

The country is plagued by frequent fuel, power and water shortages while the cost of living has increased. The education and health sectors have deteriorated and suffer from a chronic shortage of skilled staff. Lifestyle diseases, truancy in schools and low educational attainment are symptomatic of the neglect of the social sectors.

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. The implementation of the programme has not yet started.

2. Nauru's National Policy Agenda

2.1 National Objectives

The National Policy Objectives and development strategies for the medium term are set out in the Nauru Development Plan (2002-2006).

The government which was elected in May 2003 committed to return to the fiscal and financial reform program initiated in 1998. 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. A National Economic Forum was held in October 2003. The consultations that preceded the Forum demonstrated general support among the population for the National Economic Forum. The government expressed commitment to consider the recommendations of the Forum. That government itself lost power in June 2004 and the reformists have regained control.

3. Update on the political, economic and social situation

3.1 Political Situation

The political situation has been marked by considerable uncertainty in recent years, with successive changes of government and president. The Government which was elected in May 2003 was overturned in August 2003 and the momentum for reform reversed. Another motion of no-confidence resulted in June 2004 in yet another change in government. The very loose political alliance without real foundation in a party-system and hence absence of party politics make the political situation in Nauru very volatile. The situation is further complicated by the fact that there are nine members of parliament on either side of the 18-member house, resulting in frequent stalemates. The current President, Mr. Ludwig Scotty, was re-elected by MPs less than a year after he left office after losing a confidence vote in August 2003. He is the 6th President of Nauru since January 2003.

3.1.2 Human Rights

Since 2001, Nauru is hosting an Australian immigrants processing centre, as part of Australia's so-called "Pacific Solution" to curb illegal immigration into Australia. The centre, funded by Australia, held approximately 300 asylum seekers at year's end, down from 700 at the end of 2002 and 1000 in 2001. Most of the detainees, from Iraq, Afghanistan and elsewhere, were intercepted in 2001 on their way to Australia. In 2003, Nauru continued to allow Australia to station refugee detainees, while their cases were being investigated by Australian immigration officials, in coordination with the UNHCR, to see if they would be deported back to their country of origin or allowed to enter Australia.

Australian human rights organisations continue to express concerns about poor living conditions and alleged arbitrary detention of the asylum seekers and protested that journalists, human rights activists, doctors and lawyers were denied visas to visit the asylum seekers.

3.2 Economic Situation

ECONOMIC AND SOCIAL INDICATORS

ECONOMIC INDICATORS	
GDP (000 A\$, PPP, 2001 est.)	60,000
GDP per capita (A\$, current, 2001 est.)	5,000
Government expenditure (current A\$ - FY 2004 est.)	40 million
Government revenues (current A\$ - FY 2004 est.)	18 million
Total exports (fob A\$ - 2002)	18 million
Total imports (cif A\$ - 2002)	31 million
Total exports to the EU (2000)	€ 0.3 million
Total imports from EU (2000)	€ 4.1 million
Fishing access revenue (2000)	€ 4.9 million
External debt (A\$ - 2002)	33 million
POPULATION AND SOCIAL INDICATORS	
Population (2004 est.)	12,000
Population growth rate (% change, 2004 est.)	1.87
Birth rate (over 1000, 2004 est.)	25.61
Death rate (over 1000, 2004 est.)	6.95
Total Fertility rate (births per woman, 2004 est.)	3.29
Infant mortality rate (per 1,000 live births, 2004 est.)	10.14
Life expectancy at birth (2004 est.)	62
Adult literacy (%)	95
Primary school enrolment (%)	96
Secondary school enrolment (%)	34
Child malnutrition (% under 5 years)	0
Population with access to safe water (%)	100
Population with access to sanitation (%)	97
Human Development Index	0.7
Human Development Ranking	103
Human Poverty Index. (1998)	12.1

Statistical data for Nauru in general and in particular in relation to economic and social indicators are extremely poor. A large part of the economic and social information presented here has been extracted from the ADB publication “Asian Development Outlook 2004”.

Since 1906, the economy has revolved around the phosphate industry. Sales of the rich phosphate deposits (at the time reputedly the richest deposit in the world) provided Nauru with a level of income and prosperity unparalleled in the Pacific Islands. In the 1980’s phosphate exports averaged 1.58 million tons per year, by the 1990’s exports had fallen to 0.5 million tons.

In 2003 the economic and financial situation continued to deteriorate, as the phosphate reserves, the main natural resources, have become nearly exhausted. At the current level, revenues from phosphate production do not cover operating costs, and royalty and dividend payments have been delayed. Phosphate exports were at a virtual standstill in most of 2003 following strikes, sabotage and other

disruptions in production and shipping. With the decline in phosphate revenues, borrowing against trust fund assets administered by the Nauru Phosphate Royalties Trust (NPRT) has represented the government's main revenue source. The total value of NPRT assets has declined from an estimated A\$1.3 billion in 1990/91 to an estimated A\$300 million today, and stems from poor investment decisions and other bad management. The remaining NPRT assets are now almost fully, and relatively expensively, mortgaged. The size of the budget deficit for the last three fiscal years is unknown. FY 2003 (ended 30 June 2003) provided for a deficit of A\$15.2 million, though the actual budget deficit is expected to have been much higher. In FY 2004, expenditures are estimated at A\$40 million and revenues at A\$18 million.

A complete collapse of the economy has only been averted by continuing donor support, particularly Australia's humanitarian and development assistance linked to Nauru's agreement to host asylum-seekers. Australia's assistance has been essential in maintaining water and power supplies as well as education and health services with additional assistance from international organisations. Australian assistance for the period 2003 - 2005 is expected to reach A\$22.5 million.

Both ADB and AusAID have provided assistance to the government to lay the groundwork for improved performance. More recently, assistance has been provided for economic management, the reform of the budget system, the reestablishment of banking services, and the restructuring of the Nauru Phosphate Royalties Trust (NPRT). However, this assistance has had little impact due to a lack of political commitment to change and the very limited technical capacity available in the bureaucracy.

The medium-term outlook remains very bleak, particularly in the light of the government's lack of commitment to confront the drastic structural changes essential for reversing the economic decline and bringing back political stability. The promised assistance package from Australia relieves some of the most immediate pressures. The package also includes provisions for Australian personnel serving in line positions, including an Australian Secretary of Finance, with a clear mandate to address key economic and financial reforms. Agreed tasks also include auditing and assessing the remaining assets of the trust funds and beginning a restructuring of these assets.

Measures to reduce the structural budget deficit are needed. With the steep decline in the value of the NPRT, few options remain for the government to fund future budget deficits. The failure to reduce expenditures – particularly the public sector wage bill – and to address revenue shortages through taxation and cost recovery remains a particular concern. Currently the revenue base is very narrow. Few opportunities exist to develop agriculture and service industries targeting the local market, or to expand revenues from licensing of foreign fishing vessels.

3.3 Social Situation - Achievements in the social sectors

With the near depletion of the phosphate reserves and offshore investment revenues, the people of Nauru are facing an uncertain future. With the government and the Nauru Phosphate Company (NPC) no longer able to meet

salary expenses and to absorb the increasing number of young job market entrants, youth unemployment has risen to an estimated 35%, impacting severely on standards of living.

The country is plagued by frequent fuel, power and water shortages. The lack of access to quality health services, safe water and housing are areas of concern. Education and health sectors have deteriorated and suffer from a chronic shortage of skilled staff. Lifestyle diseases, truancy in schools and low educational attainment are symptomatic of the neglect of the social sectors.

3.3.1 Human Development

Nauru's Human Development Index ranking has slipped to a medium level in recent years as GDP per capita has fallen. With no minimum education requirements for employment in the government, education has remained a neglected sector. UNESCO estimated public expenditure on education at 7% of total public expenditures. Nauruans are not particularly encouraged to go to schools. Very few have attained college degrees or gone abroad for higher education. Years of "welfare state" governance sustained by high phosphate earnings has led to a lifestyle of luxury and leisure, as there was no perception of the need to be educated or to learn vocational skills.

As far as the MDG are concerned, Nauru has a low life expectancy and low education indicators, compared to per capita GDP. The quality of education is poor and secondary enrolment rates are low. There is a significant increase in lifestyle diseases and health indicators show little or no improvement.

3.3.2 Poverty Assessment

The government has not established a definition of poverty nor poverty line to determine the incidence of poverty, the intensity and severity of such poverty. Although the Human Poverty Index was relatively low in 1998 (12.1), the considerable downsizing of the government and NPC, which constitutes 95 percent of all employment, has resulted in a significant drop in household incomes and unemployment. Government policies have recognized and are concerned about the disadvantaged people, those with low incomes or insufficient subsistence production, those with poor health status and education as well as the fragility of the atoll environment in which people live. With limited skills and educational attainments, Nauruans rendered jobless are likely to find difficulty in securing immediate alternative employment. The situation is further aggravated by limited emigration opportunities.

3.4. Achievements in cross-cutting issues

3.4.1 Gender Issues

While women play an important role in family matters, they 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. This trend is likely to continue while the social system remains led by a Council

of Chiefs. However, increasing numbers of girls are enrolling in school and the truancy among the female students is significantly lower than that among male students. As a result, women seem to be benefiting more from the education system.

The government is aware of the need to increase employment opportunities for women and to enhance to a medium level their participation at higher levels of government. There is a Women's Affairs Office to promote professional opportunities for women.

3.4.2 Environment

Phosphate mining has seriously affected the environment of Nauru. The strip-mining methods employed in the extraction of phosphate for some 90 years have devastated the country. The natural vegetation and phosphate-rich top soils have been removed from over 70 percent of the land area, leaving a wasteland at the centre of the island, thus preventing the dispersal of a rapidly-increasing population from the coastal fringe, heightening land pressures and disputes around that fringe, and possibly causing microclimate deterioration.

3.5 External Environment (Regional and International Developments)

Offshore Finance

Nauru remains on the OECD's Financial Action Task Force (FATF) list of Non-Cooperative Countries and Territories on Money Laundering. Sanctions have been imposed since December 2001 which have hurt the economy. To comply with the FATF recommendations, the government revoked all banking licences issued by the Bank of Nauru, enacted legislation eliminating its offshore shell banks, and passed an anti-money laundering act and new banking legislation.

In late 2003, following a commitment to improve transparency and establish effective exchange of information on tax matters with OECD countries, Nauru was however removed from the OECD list of tax havens.

Regional Cooperation

In August 2001, Nauru hosted the Pacific Islands Forum where the leaders from the region signed the *Pacific Agreement on Closer Economic Relations* (PACER), which includes all member countries of the Pacific Forum. As a first step under PACER, Forum members initiated a free trade agreement, the *Pacific Island Countries Trade Agreement* (PICTA), which applies to the 14 Forum Island Countries (FICs, excluding Australia and New Zealand), and entered into force in 2002. Once ratified by at least six FICs, PICTA will start removing most tariffs on trade between member countries by 2010, and removing all tariffs by 2016. Nauru is a signatory to PICTA.

Donor Co-operation

In the present economic and social situation, the country is almost completely dependent on Australian support.

Under a Compact of Settlement between the governments of Australia and Nauru in 1993, Australia provided a one-off payment of A\$57 million into a trust fund for Nauru. Australia is providing a further A\$2.5 million a year (indexed for inflation) for 20 years under the Rehabilitation and Development Cooperation Programme for jointly agreed activities.

In 2001, reflecting Canberra's approach to asylum seekers processing, Australia agreed to a further package of development assistance and committed a total of A\$41.5 million under this package to Nauru in 2001-02 and 2002-03. This assistance is additional to the bilateral programme. In 2002-03, Australia provided A\$3.5 million in bilateral and regional assistance and expects to provide A\$3.9 million in 2003-04. A new package of assistance is being negotiated for 2003-04.

4. Overview of past and on-going 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.

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

4.1 9th EDF NIP Focal sector : 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.

a) Results

As not only Nauru, but also four other new Pacific ACP States (the Federated States of Micronesia, the Marshall Islands, Niue and Palau) have targeted the energy sector, especially the identification and use of new and renewable sources of energy, as the focal sector of the 9th EDF NIP, a single Financing Proposal was prepared for the programme activities to be implemented in the five Pacific Island States. The overall cost of the five States programme will be € 11.41 million. The financing will be from the 9th EDF NIPs of the five States, with the contributions proportional to the NIP allocation for the renewable energy sector for each country. The programme will be implemented at a sub-regional level. The implementation period will be 3 years.

In Nauru, the objectives are to improve the overall efficiency of the energy sector and, where justified, to increase power production through renewable energy. This will allow allocating more resources to sustainable development, reducing local pollution and environmental risks associated with current energy generation practices. The Nauru component amounts to € 1.53 million.

b) Progress in activities

In December 2003, the NAOs of the five ACP States agreed to the Financing Proposal, which is scheduled to be presented to the EDF Committee in September 2004. The Financing Agreement is expected to be signed soon afterwards.

The programme will commence with a six-month start-up phase, which will be followed by three Programme Estimates (all to be signed within three years of the date of the global commitment). The first eighteen months will be an inception phase, during which a series of preparatory actions and studies will be carried out related to the detailed assessment of new and renewable energy development opportunities and to the design of projects proposal, including tender documents, to be financed within the programme. Studies will also include global energy efficiency assessment and the preparation of related action plans.

4.2 Utilisation of Resources for non-state actors (NSA)

Non-State Actors have been allocated 15% of the A-envelope (€ 0.27 million). The programme still needs to be identified. The aim will be to find alternative sources of employment in the light of declining opportunities in the phosphate industry and the future (proposed) retrenchment of workers in the public sector. There is also the need to address the high rate of youth unemployment.

The dialogue with the NSA and the preparation of the NSA programme is hampered by the fact that the Commission has no permanent representation in the country. This is expected to change in 2004 with the opening of a Commission office in Kiribati, which will also cover Nauru.

4.3 Utilisation of Envelope B

Nauru, like the other Pacific Island countries, is vulnerable to natural disasters such as cyclones and tidal waves. Every year the region is hit by several cyclones. The funds available in the B-envelope (€ 0.5 million) will therefore be used primarily for the purposes of emergency and/or reconstruction, in case of a natural disaster. Should no such needs occur until the last year of implementation of the Energy Support Programme, and provided the implementation of the programme is progressing according to expectations, these funds will be used to complement the programme's allocation of € 1.53 million.

4.4 Dialogue in country with the NAO and non-State actors

By the end of 2003, the contacts of the Commission with the Nauru Authorities remained sporadic. In-country dialogue with the NAO is hampered by the absence of a permanent representation of the Commission in the country. The same can be said for the NSA. This will change in 2004 with the opening of a Commission office in Kiribati, which will also cover Nauru.

4.5 Regional EC Co-operation

The 9th EDF 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), plus a non-focal sector to extend the 8th EDF programmes to the six new ACP countries (€ 7 million). The Regional Strategy Paper (RSP) was signed in 2002.

Regional Cooperation is handled mainly by the FORUM Secretariat and the EC Delegation in Fiji. Whereas Nauru should benefit from the recently signed 9th EDF projects, effective participation of Nauru, and ensuing benefits from these regional projects, cannot yet be assessed.

5. Programming perspectives for the following years

5.1 Integration of new EC/EU policy initiatives and commitments

Under the EU Energy Initiative for Poverty Eradication and Sustainable Development, support has been requested by the Pacific Forum and other regional partners for two priority activities: (1) Support for the development of national energy policies and strategic action plans, to be executed by SOPAC, and (2) Support for human resource development within national electricity utilities (PPA). Both activities will deliver benefits at the national level and will support and complement the focal sector of the NIP of Nauru.

6. Conclusions of the joint annual report

The EC dialogue with the Nauru authorities has been limited. The opening of a Delegation sub-Office in Kiribati to also cover Nauru should improve the dialogue. Whereas during 2003 this dialogue concentrated on the contents and signature of the CSP and NIP, the dialogue should now shift toward the finalisation of 9th EDF Non State Actors proposals as well as the main planned intervention in renewable energy/energy efficiency.

Despite the difficult political and economic situation it was decided to maintain the focus of the A envelope on renewable energy/energy efficiency, but the practical approach will have to be adapted to the situation of Nauru.

The NSA-initiative has yet to be prepared and it is not expected that a financial commitment will be taken in 2004.

Coordination with the main donor, Australia, will be essential in the implementation of the Nauru National Indicative Programme.

Annex 1 - Chronogram of activities (9th EDF)

Title	Amount (in € million)
5-country renewable energy Programme	1.53 (from Nauru NIP, plus allocations from the other countries' NIPs)
Support to NSAs	0.27
Total	1.8

Annex 2 – 9th EDF indicative timetable for commitments and disbursements

<i>All figures in € million</i>	2004 (estimate)	2005 (estimate)	2006 (estimate)	2007 (estimate)
<u>Commitments:</u>				
Renewable energy	0	0.3	1	0.23
NSA	0	0.1	0.1	0.07
<u>Disbursements:</u>				
Renewable energy	0	0.05	0.3	0.8
NSA	0	0.0	0.1	0.1
<u>Total payments</u>	0	0.05	0.4	0.9
<u>Total payments cumulative:</u>	0	0.05	0.45	1.35

ANNEX 3: MDG indicators selected by the EU

Indicators	(%)			
	1990	1995	2001	2002
Impact indicators				
1. Proportion of population below \$1 per day	NA	NA	NA	NA
2. Prevalence of underweight children (under 5 years of age)	NA	NA	NA	NA
3. Under-five mortality rate X 1000 live births (Infant mortality rate)	NA	30% 25%	30% 25%	NA
Outcome				
4. Net enrolment ratio in primary education	NA	81% ¹	NA	NA
5. Primary Completion Rate	NA	NA	NA	NA
6. Ratio of girls to boys in Primary	NA	1.04 ²	NA	NA
Secondary	NA	1.06	NA	NA
Tertiary education	NA	NA ³	NA ⁵	NA
7. Proportion of births attended by skilled health personnel	NA	NA	NA	NA
8. Proportion of 1 year old children immunised against measles	NA	99% ⁴	95%	NA
9. HIV prevalence among 15-24 year old pregnant women	NA	NA	NA ⁶	NA
10. Proportion of population with sustainable access to an improved water source	NA	NA	NA	NA

¹ 1998 total - girls 82.4% - boys 79.6% - pupil/teacher ratio 22.5

² 1998 data - Gross enrolment ratio – 53.9% - Female 55.6% - Male 52.3%

³ 1997 proportion of women in National Parliament 6%

⁴ 1997 data

⁵ 2000 illiteracy rate 5%

⁶ 2000 death rate Malaria 13/100.000 – Prevalence of TB 34/100.000 – 2001 TB cases 100, 2000 cured 25