



REPUBLIC OF NAURU
EUROPEAN COMMISSION

JOINT ANNUAL REPORT 2007

EXECUTIVE SUMMARY

The Country Strategy Paper and National Indicative Programme (NIP) for the Republic of Nauru was signed and provides for an indicative financial allocation of € 1.8m for the “A” Envelope, and € 0.5m for the “B” envelope. The NIP addendum to the 9th EDF, signed by the NAO and European Commission confirmed the NIP allocation. The focal sector is Renewable Energy, implemented under a multi-country program, REP-5 project.

The Country Strategy paper for 2002-2007 identified the energy sector as the strategic sector for European Union Cooperation. The financial allocation is set out in the table below.

Total Allocation	2.3 million Euro
A envelope total	1.8 million Euro
85% allocated to the energy sector	1.53 million
15% allocated to non state actors	0.27 million
B envelope total	0.5 million Euro

Nauru is a small Pacific island state situated just south of the equator and 3000 km east of Australia. It has a surface of roughly 21 km² and a population of approximately 11,000. Post independence, Nauru’s government became very wealthy through the exploitation of its mineral resource, phosphate. When world prices began to fall the government borrowed heavily to support high levels of government spending eventually leading to an economic crisis in the early 2000’s. Nauru has now stabilised this crisis situation by drastically cutting government expenditure which has been achievable with recent political stability

In 2005 Nauru adopted its long term plan for recovery in the form of the National Sustainable Development Strategy 2005-2025 (NSDS).

Nauru is one of five Pacific ACPs (with FSM, Marshall Islands, Niue and Palau) in the Multi-country programme “Support to the Energy Sector.” Given the need for energy efficiency, consideration should be given to continuing this focus for the next programming phase. The Governments of Italy and the Republic of China are also active in this sector.

In October 2005 the Government of Nauru requested assistance with disaster preparedness in regards to drought and the Regional Pacific multi- country programme on disaster preparedness, currently being prepared, should deliver this support to Nauru. The allocation under the B envelope was transferred to SOPAC to undertake disaster preparedness with focus on drought risk management. In May 2007 SOPAC performed scoping mission for this project. The financing proposal for the project has since been approved.

1. Update on Political, Economic and Social Situation

1.1 Update on the Political Situation

Political stability was achieved in 2005 following the election of President Scotty’s government in October 2004.

Nauru undertook a constitution review process in 2007. A constitutional convention has been concluded and the recommendations from the convention are currently tabled with the Parliament of Nauru. Once Parliament has approved the recommendations, it is anticipated that a referendum will be held in the very near future.

In November 2005 the Government of Nauru launched its National Sustainable Development Strategy 2005-2025. The strategy entitled, 'Partnership for Quality of Life' commits the government and people of Nauru to a long term reform process. Development of the strategy included a comprehensive programme of community consultation. Ongoing community understanding and support to the reform process is fundamental if political stability is to be maintained throughout the many difficult adjustments ahead.

In November 2005 the Government convened its first meeting of donor partners at which the government presented its NSDS and demonstrated its commitment to transparent engagement with civil society, the wider Nauruan community, donors and regional organisations. Nauru followed this initiative by hosting a second meeting for donor partners on the 26th of July 2007.

In 2006 - 2007 Australia's package of assistance to Nauru was reduced to AUD \$18 million. Australia's support to Nauru will be reviewed in 2008. While the MoU was originally developed as an outcome of the establishment of the Australian processing centers, the financial assistance actually covers social expenditures (essential drugs, education infrastructure, etc) and fuel import. Australia also funds a number of key government in-line positions including the Secretary for Finance, the Secretary for Health and the Police Commissioner. As provided for under the bilateral MoU, the Government of Australia takes close account of Nauru's progress in achieving economic and governance reforms.

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

Women still have no representation in the Parliament and are grossly under-represented at the higher levels of government service.

1.2 Update on the Economic Situation

The financial situation of Nauru remains fragile.

The Budget speech for 2007-08 includes the following table which provides useful summary information in AUD \$'000-

	2005-06 Actual	2006-07 Actual	2007-08 Estimate	2008-09 Projection	2009-10 Projection	2010-11 Projection
Revenue	24,422.1	24,248.0	24,695.4	17,263.6	17,284.2	17,334.2
Expenditure	-21,594.1	-22,934.0	-24,675.0	-17,229.1	-17,178.9	-17,178.9
Budget Balance	2,828.0	1,313	38.4	34.5	105.3	155.3

The Government reported a surplus budget for the financial years 2005-06 and 2006-07. The expected surplus for this current financial year is small, but maintains the Government's commitment to balance its budget.

The 2007-08 fiscal year saw the continued increase in phosphate exports, which are now running at a rate of approximately 500,000 tonnes per annum. World phosphate prices have increased significantly in recent times, so there is much confidence that phosphate revenues will continue to grow through 2008-09. Ronphos is estimated to return approximately \$4.4 million in dividends to the Government in 2008-09.

In 2007-08, the Nauru Rehabilitation Corporation continued development work towards the mining of secondary phosphate. Economic reserves of secondary phosphate are estimated to be up to 20 million tonnes and should provide for a secure stream of revenue into the future. Sustained phosphate exports will provide a stream of income to landowners and government, and will maintain employment opportunities for Nauruans.

The Nauru Rehabilitation Corporation and Ronphos are looking to develop other export opportunities. The Nauru Rehabilitation Corporation is currently in negotiations with a foreign company to export crushed coral, and indications are that this could be a lucrative export industry, with projections showing revenues of around \$3-4 million per annum. The first trial shipment of aggregate left in April 2008 bound for Majuro.

In 2004-05 the Government commenced a major economic reform programme which has focused on the areas of the public sector reform, instrumentality reform, financial sector reform and budget reform.

Legislation has been passed to fight money laundering and the financing of terrorism including the Anti-Money Laundering Act 2004, the Counter Terrorism and Transnational Organized Crime Act 2004, the Mutual Assistance in Criminal Matters Act 2004, and the Proceeds of Crime Act 2004. The Government is currently working on setting up the appropriate administrative structures to effectively implement this legislation and has sought outside technical assistance to do so. Nauru is now removed from the FATF 'blacklist' and the United States has lifted the application of section 311 of the USA Patriot Act.

In October 2006, Nauru was removed from formal monitoring by the OECD FATF. Nauru attended the OECD's Asia Pacific Group (APG) on Money Laundering Annual Meeting as an observer and, in July 2007, the Annual Meeting of the APG approved Nauru's application for full membership status. Nauru is attending the 2008 Annual Meeting of the APG.

In April 2008, the US Treasury withdrew its previous Advisory 21 and Advisory 21A, which warned banks and other financial institutions of the need for enhanced scrutiny of transactions involving Nauru. This was further recognition of the success of Nauru's financial sector reform program.

The government has dominated the economy over the last decade. Currently 1,200 of Nauru's 10,000 population are employed by Government. The Government's large role in the economy has essentially seen a crowding out of private sector opportunities in the past. However, there are many factors that hamper private sector growth in Nauru including lack of banking and insurance facilities, unreliable service provision (power and telecommunications infrastructure in Nauru is very poor), Nauru's geographic isolation and limited reliable access to work markets and a lack of skilled human resources.

The provision of offshore financial services has greatly decreased in its importance, notably in view of the need to implement legislation in line with Nauru's commitment of 3 December 2003 towards the OECD to increase compliance with the principles of transparency and effective exchange of information for tax purposes. In this regard, Nauru participated in the last meeting of the OECD Global Forum on Taxation and contributed to the 2006 assessment of its tax system. Australia and New Zealand are currently negotiating Taxation Information Exchange Agreements with Nauru.

Since the Bank of Nauru (BON) became insolvent in the late 1990's, no commercial banking facilities are available on Nauru. Establishing any commercial banking facilities was made much harder for Nauru when it was black-listed by the FATF in 2004. However, since then, Nauru has worked hard to implement international standards to combat money laundering and terrorist financing. This hard work resulted in Nauru's removal from the FATF blacklist in 2005, its promotion to observer and priority observer status with the Asia-Pacific Group on Money Laundering (APG) in 2005 and 2006 respectively, and finally its recent admittance as a full member of the APG in July 2007. Nauru continues to work hard to meet international standards to combat money laundering and terrorist financing.

In March 2008, the Government engaged a consultant to conduct a study into the feasibility of establishing a commercial bank on Nauru. The study found that it could be feasible to establish a commercial bank, and recommended further actions.

In late 2006, the Government of Nauru produced, drawing on an ADB report into the Nauru Utilities sector, a strategy for the reform of its Utilities sector. The strategy is focused on the medium term, and particularly on the restoration of reliable power supply and financial sustainability of the Utilities sector. Critical to the implementation of this strategy will be the roll-out of electricity prepayment meters to residential consumers – which is to be funded by the EU under the REP5 program of assistance to Nauru. These meters will contribute to the financial sustainability of the sector, particularly as purchases of diesel for the power station represent a significant proportion of total government expenditure.

1.3 Update on the Social Situation

The NSDS includes an analysis of the application of the Millennium Development Goals to Nauru which is reproduced at the end of this report.

Infrastructure on Nauru is in a very poor state. Major investment in water, sewerage, power generation, power distribution, schools and hospitals, port, phosphate mine, telecommunications and transport are required.

Health is dominated by diabetes – it is estimated that more than 80% of adults are diabetic. Education is troubled by high levels of truancy and educational standards are low. Human resources in both sectors are scarce and under-skilled.

Water is also a scarce commodity on Nauru with the island dependant on desalination plants with several houses having roof-top rain water collection facilities. Consequently Nauru is very vulnerable to drought as evidenced in early 2006.

Migration opportunities are limited. Very few Nauruans will qualify as preferred migrants to Australia, New Zealand, Fiji or further a-field and without a massive re-prioritisation of resources into education the outlook for emigration is very limited.¹ However, Nauru was recently successful in providing 70 locals as fruit pickers (unskilled labour) to New Zealand for an average period of 3 months each. It is hoped that this exercise will be repeated in the future years. In addition the Government of Nauru has taken the initiative to accredit its tradesmen in Australia thereby creating an opportunity to access the labour market both regionally and in Australia and New Zealand.

The people of Nauru face a difficult adjustment to the dramatically different circumstances. This challenge is being met by an increasingly active civil society in particular the emergence of women's groups which are organised to improve local conditions.

See Annex I for an analysis of the Global Millennium Goals applicability to Nauru.

1.4 Update on the Environmental Situation

In 1998, the Government of Nauru adopted the National Environmental Management Strategy (NEMS) and National Environmental Action Plan (NEAP) to respond to immediate challenges arising at date. In 2005, the GoN's NSDS clearly identified *the rehabilitation of mined out lands for livelihood sustainability*. However, concrete actions to improve the environment in real terms at the community level are few. Nauru's major environmental risk is the mined-out phosphate lands that cover almost 90% of the island after strip-mining of the phosphate had left behind a barren landscape of deep pits and tall pillars and the removal of natural vegetation and topsoil from over 70 percent of the land area which has made most of the island uninhabitable and barren. Key environmental issues, in light of these are: limited access to sustainable safe drinking water and sanitation, inadequate access to sustainable clean renewable energy sources and land degradation.

Degradation of topside (inland) through phosphate mining limits the degree of land being available for agricultural activities in support of food security. The lack of knowledge of the environment and the need for protection severely hinders environment promotion efforts. As a result, there is a continued widespread use of environmentally unsustainable practices.

Housing and building arrangements are based on ownership of land plots leading to congested living and the clustering of several land uses including homes, cesspits, water wells, shops, planting plots, animal pens and sports field on one plot of land. Waste management is minimal – including human, water, household and industrial. A legislative review of all environment legislation is also a priority for GoN.

2. Overview of past and ongoing cooperation

The Country Strategy paper for 2002-2007 identified the energy sector as the strategic sector for European Union Cooperation. The financial allocation is set out in the table below.

Total Allocation	2.3 million Euro
A envelope total	1.8 million Euro
85% allocated to the energy sector	1.53 million

¹ ADB September 2005

15% allocated to non state actors	0.27 million
B envelope total	0.5 million Euro

Renewable Energy Programme (REP5)

In July 2005 the Financing Agreement for the Renewable Energy Programme (covering also Marshall Islands, Micronesia, Niue and Palau) was signed by the Secretary General of the Pacific Island Forum Secretariat. Tender specifications for pre-paid meters and photovoltaic panels were drawn-up in July 2007, and contracts let in October with expected supply and installation in the first quarter of 2008. The first national programme estimate was signed in October 2007.

NSA Programme

The NSA component in accordance with the NAO request has been merged with the main allocation for the REP – 5. The amendment to the financing agreement has been duly signed.

Utilisation of Envelope B

Nauru has decided to utilise its 'B' envelope funding through a multi-country disaster preparedness programme, to be implemented by SOPAC. This project is planned to be commenced in mid of 2008 with a time frame of four years.

Other instruments

The 9th EDF Pacific Regional Indicative Programme funded and extended a number of existing projects to the six new Pacific ACP countries, including Nauru. These consisted of:

Pacific ACP Regional Economic Integration Programme (PACREIP)

Development of Sustainable Agriculture in the Pacific (DSAP)

Pacific Regional and OCT Fisheries Programme (PROCFISH)

Plant Protection Programme (PPP)

Pacific Regional Initiatives for the Development of (basic) Education (PRIDE)

Reducing Vulnerability in PACP States – SOPAC

Development of Fisheries in the Pacific (DEVFISH)

Pacific Environmental Information Network (PEIN)

3. Assessment of Performance Indicators

Indicators were collected and refined during the duration of the programme and by ex post evaluation by the ROM in August 2007.

4. Donor Co-ordination of Harmonization

No Member State has in-country representation in Nauru. In recent years MS involvement has been limited to studies. Other donors provide an important source of funding and technical assistance in the various sectors.

Nauru has a number of bilateral donors including Australia, New Zealand, Japan, Republic of China (Taiwan), Republic of Korea, India, Singapore, Malaysia. Nauru's multilateral partners include the Asian Development Bank, United Nations Development Program (GEF),

European Union, United Nations Agency such as the FAO, UNESCO, UNESCAP, World Health Organization, and the Pacific Islands Forum Secretariat and its CROP agencies.

The Aid Management Unit (AMU) under the Ministry of Finance was established by the Government of Nauru in its efforts to centralize all development assistance received by Nauru. The Development Planning and Policy Division (DPPD) also under the Ministry of Finance is responsible for ensuring a development planning framework exists. Both units were established in November 2005 in order to fully maximize development assistance for the development of the country.

The European Investment Bank

Emphasis has been laid by EIB upon making funds available as widely as possible in the Pacific region through lines of credit to local financial institutions. Additional regional funding instruments such as loan guarantees to support smaller operations, which might also target Nauru, are being developed. A special focus will be on the renewable energy and environmental sector.

In Nauru the EIB seeks to identify suitable partner institutions. If a line of credit is being considered in Nauru, a window for micro-finance will make a significant contribution by giving borrowers access to the small scale financing they need to start and maintain income-generating businesses.

5. Dialogue in Country and with the NAO and NSAs

Nauru is a relatively new member of the ACP group having joined on signature of the Cotonou Agreement in June 2000. Neither the EU nor its member states has permanent representation in Nauru; since April 2006 the country has been served by the EC Delegation in Suva. Accordingly, opportunities for political dialogue have been few, mainly taking place on the margins of regional meetings such as the annual Forum meeting, or during the course of periodic missions to the country. In 2007 Delegation's desk officer for Nauru visited twice the Country. Relations between the EU and Nauru are cordial with no contentious issue to note.

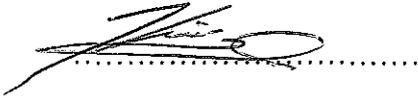
6. Conclusions

With the NSDS completed, the challenge for Nauru now is implementation of the strategies. The formulation of Ministry corporate plans will clearly define the Ministry objectives and strategies how they would support the NSDS goals. The same applies to the development of sector plans. Having clearly defined sector priorities and strategies as articulated in the National Sustainable Development Strategy will also identify the linkage between sector objectives and national priorities. With clearly stated sector goals and Ministry objectives, this will promote stronger vertical and horizontal coherence.

Results in the focal sector have yet to be realised. Tenders for the supply and installation of PV equipment and prepaid meters were only launched in 2007 with equipment delivery not expected until late 2007. Over the last year the PMU personnel for the REP-5 project has undergone significant change, significantly the replacement of the manager. It is hoped that such changes will bring about a timelier implementation of the programme. With amendment to the REP-5 Financing Agreement all the "A" envelope of Nauru has been committed.

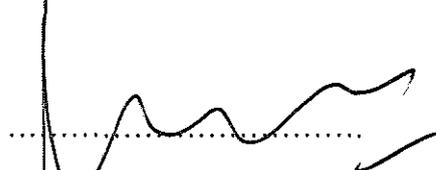
Signatures:

The National Authorising Officer



Date: 17/11/08

The Head of Delegation



Date: 10/7/08

7. List of Annexes:

Annex I – General Economic Indicators and MDGs

Annex II – EDF 9th Financial Situation

Annex III - Indicative Timetable for Global Commitments

Annex I - Basic Statistics reported in the NSDS and MDG

Land size	21 sq km
Number of islands	1
Population	10,065 (Nauruan 7,600)
Population Density	495 per sq km
Population Growth Rate	0.14%
Dependency	0.14%
Dependency Ratio	0.78
GDP per capita (US\$)	1400 ²
Real Growth of GDP per capital	NA
Major industries	Mining, Fishing licenses
Government Employment (as % of total formal sector employment)	42%
Unemployment Rate	22.7%
EEZ	320sq km
Budget Deficit (% of GDP)	18%
Proportion of Labour force in Subsistence	2%
Adult Literacy Rate	95%
School Attendance Ratio	59%
Life Expectancy	55 (men 53, women 58)

Millennium Development Goal and Targets: Assessment of Progress

Goal 1: Eradicate extreme poverty and hunger

Target 1: Halve, between 1990 and 2015, the proportion of people whose income is less than a \$1 a day.

Nauru: Nauru currently does not have statistics of people's level of income. While Nauru has a close system of extended family where income is transferred amongst family members the low general wage of \$140 per fortnight often spread among multiple families means it is likely there are some Nauruans with income less than \$1 per day.

Target 2: Halve, between 1990 in 2015 proportion of people who suffer from hunger

Nauru: Hunger is an increasing problem, but there are no statistics to support this

Goal 2: Achieve universal primary education

Target 3: Ensure that, by 2015, children everywhere, boys and girls alike, will be able to complete a full course of primary schooling

Nauru: Compulsory and free education is provided to year 10 or up to the age of 15 years 9 months. Attendance for primary schooling is between 60-70%

Goal 3: Promote gender equality and empower women

² Monetary GDP only.

- Target 4: Eliminate gender disparity in primary and secondary education, preferably by 2005; and all levels of education, no later than 2015
- Nauru: There is no gender disparity in the education system. The ratio of girls to boys at Primary Education is 1.02 (late 1990s)

Goal 4: Reduce Child Mortality

- Target 5: Reduced by two thirds, between 1990 in 2015, the under-five mortality rate
- Nauru: Nauru Statistics on child mortality are fairly well under control. Well- Baby clinics run a support programme for mothers. The under- 5 mortality rate is 30 per 1,000 live births (2001).

Goal 5: Improve maternal health

- Target 6: Reduced by three quarters, between 1990 in 2015, the maternal mortality ratio
- Nauru: Birth control is increasing as means of improving maternal health. Well- woman clinics exist to assist improve maternity care. Infant's mortality rate is 25 per, 1000 live births (2001).

Goal 6: Combat HIV/AIDS, malaria, and other diseases

- Target 7: Have halted by 2015 and begun to reverse the spread of HIV AIDS
- Nauru: Nauru is financially assisted with other countries through external assistance to prevent HIV/AIDS.
- Target 8: Have halted by 2015 and begun to reverse the incidence of malaria and other major diseases
- Nauru: Major global diseases such as malaria, leprosy and TB are not issues in Nauru, but so- called western diseases such as diabetes remains high at 3.1 per 1,000 people.

Goal 7: Ensure environmental sustainability

- Target 9: Integrate the principles of sustainable development into country and programmes and reverse the loss of environmental resources.
- Nauru: Environmental policies and strategies have not been implemented. Also, sector ministries do not integrate environmental concerns into their planning. Effective rehabilitation of mined-out phosphate lands has not yet started. A reef conservation strategy does not exist and sustainable practices are difficult to implement with an inadequate land based domestic food supply. A survey of reef resources was completed 2005.
- Target 10: Halve by 2015 the proportion of people without sustainable access to safe drinking water
- Nauru: Fresh water is available from rain and well water, but desalinated water is no longer available. Constant supply is unreliable due to periodic droughts and quality is questionable. Water use management does not exist. Poor waste management threatens to contaminate the water lens.
- Target 11. Have achieved by 2020 a significant improvement in the lives of at least 100 million slum dwellers.

Nauru: Living conditions have deteriorated with multiple family units living under one household and sharing facilities and amenities sufficient for one family only. Housing and building regulations exist but are not implemented. The land tenure system prevents planned land use and encourages random building by landowners.

Goal 8: Develop a global partnership for development

Target 12: Develop further an open, rule based, predictable, non –discriminatory trading and financial system (includes a commitment to good governance, development, and poverty reduction, both nationally and internationally)

Nauru: Nauru has legislated significant reforms to the financial system to make it robust (able to deal with international money laundering and proceeds of crime) and able to attract offshore institutions. The Government is including new corporate governance arrangements for its SOEs.

Target 13: Address the special needs of the least develop countries (includes tariff- and quota- free access for exports, enhanced programme of debt relief for and cancellation of official bilateral debt, and more generous official development assistance for countries committed to poverty reduction).

Annex II 9th EDF Financial Situation

Pipeline and absorption capacity

The whole of the A envelope should be committed by 2006/2007. The B envelope depends on progress made with the multi-country disaster preparedness programme being developed by SOPAC and IRCS.

9 th EDF NIP All figures in € million	2005	2006	2007	2008 estimate	2009 estimate
<u>Commitments:</u>					
Renewable energy	1.53	0	0.27	0	0
B envelope	0	0	0.5	0.5	0
<u>Disbursements:</u>					
Renewable energy	0	0.1	0.6	2.0	0
B envelope	0	0	0	0.1	0.4
<u>Total payments</u>	0	0.1	1.37	2.3	0.4
<u>Total payments cumulative:</u>	0	0.1	1.37	2.3	0.4

Proposal for revision of strategy

No change of strategy for 9 EDF is foreseen.

Preparation for next programming exercise 2008-2013

The European Commission and the Nauru Government jointly recognize that there may be important environmental issues which may become an essential part of the development agenda of the country. Issues related to the reliable provision of water and sanitation, sustainable management of solid waste, coastal protection, ecologically sustainable tourism, and renewable energy can certainly play a crucial role in the future partnership.

Further details will be elaborated in 2007, once the 10th EDF programming exercise is launched and negotiations formally begin. Consideration will be given for the most efficient implementation modalities, including continuing the 9th EDF approach grouping several countries under a same initiative, this could apply also to a future NSA programme.

Annex III:

Indicative timetable for global commitments

	Indicative allocation	2008		2009		2010→	
		1	2	1	2	1	2
1st FOCAL SECTOR – RENEWABLE ENERGY AND/OR WS&S	M € 2.3						
- Project 1 : MULTI-COUNTRY PROGRAMME	M €		2.3				
	M €						
2nd FOCAL SECTOR – NONE	M €						
- Project 1	M €						
- Project 2	M €						
NON FOCAL SECTORS	M € 0.40						
- Institutional support for non state actors.	M €						
- Technical cooperation facility	M €	0.40					
- Contribution to regional programmes	M €						
-<optional> Support for EPA	M €						
-<optional> Support for Governance	M €						
-Other	M €						
Total Commitments:	M €						
Total Cumulative Commitments :	M €	0.40	2.3				