



REPUBLIC OF NAURU

2014-15 BUDGET

BUDGET PAPER 2

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FOR THE INFORMATION OF HONOURABLE MEMBERS
ON THE OCCASION OF THE BUDGET 2014-15

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PART 1: The Economic Outlook

With the re-opening of the Regional Processing Centre (RPC) in September 2012 Nauru has experienced dramatic economic growth. The growth of local employment opportunities on the RPC has resulted in labour market pressure, including salary rates and competition for skills in short supply. At the time of the budget preparation the RPC employs about 1500 of which 790 are local Nauruans or up to 15% of the labour force. Job growth in the other parts of the economy is also occurring. The Government as an employer has had to respond to these labour market pressures. .

According to the March quarterly figures CPI recorded a 7.6% increase on the December 2013 quarter and is now estimated at around 5.3% on an annual basis. Previous expectations for growth of about 8% into 2014-15 may now be conservative. In part this growth has been driven by the impact of the large-scale payments to Nauruans during the past year with local consumer demand taking up some of the previous RPC driven capital investment. Prices for tobacco and alcohol increased with the imposition of increased excise charges during the year and there is also some evidence of increased volume in these products. Given this and the amount of cash now present from debt repayment and full employment, inflation could accelerate into 2015.

While the short-term growth prospects are positive, there are some risks in the medium to longer term. Phosphate production is likely to decline in the absence of advances in extraction methods and finite supply. The RPC is dependent on a 5-year agreement with the Australian Government and there is an apparent slowdown in the number of new refugees arriving. Processing of refugees will pick up and must change the nature of the arrangements and the number and status of refugees on Nauru. Fishery revenue has grown strongly in the past year but has limited upside with limits on the number of vessel days now almost reached and climate patterns beginning to turn.

It is important to Nauru's long term future to begin immediately in this environment to set aside reserves for the long term if it is to avoid the mistakes of the past reliance on a narrow resource base and to take advantage of windfall gains. A Trust Fund is part of this but developing some cash reserves to cushion fiscal shock or make provision for infrastructure replacement is also a sensible fiscal strategy.

The port is the major vulnerability for almost all economic activity, with recent equipment failures inhibiting import and export activity and imposing very high short term costs on shippers and thus the community at large. Even refurbishing the port will expose the economy to potential major disruption to fuel, food and export movement. Utility services remain unreliable and exposed to ageing equipment, poorly maintained infrastructure in both the electricity and the highly power dependent reverse osmosis water supply system. These risks are exacerbated by the potential for further increases in population at RPC and, in the near future, the general community itself as refugees make the transition to the community.

As part of its risk mitigation strategy the Government has placed the port facility at the top of its list of economic priorities. Next, the government is committed to maintaining a tight fiscal stance and exploring a small number of options for shifting spending to infrastructure and skill building investment while restraining the lock in of recurrent expenditure to very slow growth rates.

Pacific economies while benefiting from post GFC rebounds have begun to soften and now appear to be stuck in a range around 5%, with little impetus and still some underlying political uncertainty. Some economies are responding to major disasters and other economies continuing to battle capacity and other constraints to economic expansion. In Nauru the main local source of growth is in the Fisheries sector, with more active management of the fishery and the vessel day's scheme in particular resulting in a more stable revenue floor and an ability to seek a premium on the base price for fishing days at least in the near term.

Economic outlooks for the two largest economies in Oceania (Australia/New Zealand) play a significant role in underpinning economic growth of the Pacific island economies. Australia is now forecast to go below trend as the mining investment phase winds down and growth rates are now forecast to decline to about 2.7% in 2014-15, putting pressure on unemployment rates and the new Government balancing tight fiscal policy with a need not to inhibit growth.

On the other hand New Zealand growth forecasts have recently been upgraded partly because post-earthquake construction is increasing and fostering growth in domestic demand and export growth. Australia remains the largest donor to Nauru with \$30m annually expected to continue over the near term, including some direct budget support. New Zealand continues to support the education and justice systems. Taiwan provides direct budget support and other project support in the community.

Overall the Asian region is forecast by the IMF to continue to grow at around 5½% through 2014 and 2015 although there are some signs that the rates in China and Japan could face challenges in meeting expectations.

Nauru's limited and volatile revenues from non-donor sources like fisheries license revenue and phosphate related payments continue to be difficult to forecast with accuracy, and are both subject to factors and influences that are beyond the control of the Government. Phosphate revenue in 2013-14 is expected to be in the area of \$US61m, with a small increase in 2014-15 to around \$US65m. Fishing revenue showed substantial growth to around \$21m and is expected to settle in the region of \$18m for the next two or three years

The Government continues to aim to broaden Nauru's economic base, which will insulate against the volatile and limited nature of current revenue streams, although some initiatives are proving slow to develop.

The demand for power and water has increased significantly due to the re-opening of the Regional Processing Centre (RPC) and as purchases of new white goods and other household improvements seem to be growing following the Ronwan payouts and pay out of other accrued liabilities to Nauruans. This is placing cost pressures on the Government and Nauru Utilities Corporation to meet this increased demand and the system remains vulnerable to outages.

Reforms aimed at improving efficiency in the operations and management of SOEs are continuing and this ultimately should lead to better performance and improved service delivery.

In the areas of public financial management, the Nauru Revenue Office and the Customs administration have been combined to form the Nauru Customs and Revenue Office (NCRO) within the structure of the Ministry of Finance. Recent staffing initiatives however should bring improvements in management of government revenue and increasing effectiveness of revenue collection. The Government will introduce taxation reforms this

year commencing with an employment tax and to be followed by a business income tax in 2015. The customs tariff will also be reviewed this year and updated to be consistent with 2012 WTO standards. The Ministry of Finance will be undertaking a review of the effectiveness of border collections and revenue leakage in order to firm up the revenue base.

The Financial Management Information System (FMIS) is now providing the Government of Nauru with improved capability to meet its financial management and accounting requirements. This system recently was upgraded to meet Nauru's particular financial management requirements. The system however remains under some pressure, particularly as staff turnover has required constant training and renewal. A concentrated support program will commence in the first quarter of the 2014-15 year to address these concerns, add some modules and strengthen the system so that it will support a move towards better integration of plans and budgets and a more robust Medium Term Expenditure Framework.

In the first quarter of 2013-14 the Government signed off on a new Procurement Agent Contract as a major step in implementing new Procurement rules pursuant to the Public Finance (Control and Management) Amendment Act 2012 and its related Regulations. This initiative has been supported by DFAT and is mandated to cover public procurement by all public authorities including SOEs. There have been some implementation challenges and resistance from some entities but it is anticipated that recent staffing and other changes, together with a renewed training program will see more of the expected benefits accrue to the Government. The operation of the procurement agency arrangements will be subject of a formal review in Q2 of 2014-15.

Negotiations for arrangements for a new banking service provider on Nauru continued during the year although progress was slower than expected. While many new account holders were taken on, the actual model of the banking service provision is not yet finalised. This is expected to occur in the first quarter of 2014-15.

Nauru Trust Fund

With the technical assistance provided by the ADB the Government of Nauru has continued to make progress in the establishment of the Nauru Trust Fund to accumulate, preserve, grow and mobilise capital for development. The Government will continue to put aside and invest a proportion of Government windfall revenue to the new long term Trust Fund. The Government provided \$2,500,000 in the 2013-14 budget as an initial payment to the Fund, from the ADB's Asian Development Fund grant. It has since taken the opportunity provided by solid revenue flows and lower than expected expenditure to make available an additional \$2,500,000 and this will be paid to an appropriate financial investment vehicle by end June 2014.

Nauru will continue to progress discussions with key partner governments in order to achieve a truly international agreement on the Trust Fund whereby no single party or Government can unilaterally withdraw monies from the Fund or change the Articles of the Fund. Work on the governance and administration of the Fund will be undertaken that will see the Fund fully operational this year. The Government intends to take opportunities from recent windfall revenue growth to continue to add to the Trust Fund as an important element of its long term plans to protect the Nauruan economy into the future. In this regard, a further \$5m has been set aside in the 2014-15 budget as the Government contribution to the Fund for next year.

Private Sector

Development of the private sector is one of the primary goals of the National Sustainable Development Strategy (NSDS). The NSDS emphasises the importance of the promotion and development of small and micro enterprise (SME) businesses and to ensure a more active private sector through strengthening the general business and investment environment.

The Government in 2014-15 will continue work to develop an Implementation Strategy for the Private Sector which sets out the path in which the private sector, development partners in particular DFAT, and the Government need to take to achieve its goals. These include greater investment in technical and vocational education to meet the skills needs of the private sector and leveraging off opportunities afforded by the RPC and Transfield's role as a certified TVET training authority in some areas.

Nauru's infrastructure roadmap, Nauru Economic Infrastructure and Investment Plan (NEISIP) has been formulated with the assistance of the Asian Development Bank (ADB). A review of the infrastructure sector was undertaken in March 2013. The review concluded that the infrastructure projects were being undertaken and that it was necessary to also develop Master Plans to assist in planning and implementing the NEISIP. These Master Plans would also assist donors to plan their assistance programs better. Any infrastructure development will have a trickle-down effect on the private sector. Small Business Development is being supported by UNDP and Taiwan.

The most important activity the Government can undertake to facilitate the growth and consolidation of private sector contribution to the economy is to address the issue of the port operations. The government has nearly finalised arrangements for the engagement of technical assistance in the form of a port operations manager who can work with the harbour master and other interested parties to develop a strategic management approach to restoring and redeveloping port capacity and reducing bottlenecks that inhibit import and export activity.

The Government will continue to explore other ways to build a vigorous business and investment environment through major developments and improvements in the infrastructure sector.

Australian Regional Processing Centre

The Regional Processing Centre (RPC) expanded operations in 2013-14 and now houses some 1100 asylum seekers and employs some 790 Nauruans. Nauru is currently imposing a visa charge on each asylum seeker while on Nauru. The current visa charge is \$1,000 per asylum seeker per month.

The flow on effect of the RPC is also providing additional income to the Nauru Utilities Corporation (NUC). Additional water supplies are being sold to the RPC as well as electricity and fuel. Businesses in Nauru are also benefiting through various contracts let by the RPC for the provision of food and laundry services and ancillary services.

The Government is finalising a new 5 year agreement on RPC with the Australian Government as refugees are processed and resettled in the community there will be pressure on local education and health facilities and the utilities services. These issues are being addressed as part of the negotiations on the 5-year agreement.

Eigigu Corporation is also a substantial beneficiary of the RPC activity with contracts with DIBP among others for provision of bulk accommodation.

PART 2: Economic Statistics

Good infrastructure development, better education, better health, a stable economy, good economic relationship with other economies and good planning are good determinants of economic growth in the long-run for most economies including Nauru.

The completion of the Household Income and expenditure survey and subsequent analysis during 2012/13 and 2013/14 has produced various economic information that highlights the changes in expenditure consumption patterns of households since 2006. Where the results have shown some significant changes in spending behaviours of household as a result of the improvement in the country's economy. The survey has provided the new baselines and benchmarks for economic statistics and has provided sufficient data for a second poverty analysis report to be produced later throughout 2014 calendar year. Other subsequent reports to be produced will be on communications, health, housing, agriculture & fisheries, food security and labour force and transport among others. Recent work with the assistance of various technical agencies such as SPC, PFTAC, NZStats and ABS have been undertaken to establish benchmarks for economic statistics, linked to measures on National Accounts (GDP) and Balance of Payments (BOP) to produce a more robust data collection framework for timely economic statistics in these areas. The second stages is to establish the new Consumer Price Index basket (CPI) that is to be used in price surveillance for the monitoring of inflation. This work is concurrently being undertaken by the bureau and expected to be finalised by September.

The average annual per capita expenditure for the average Nauruan person was found to be AUD\$3,151. The distribution can be seen below (Chart 1)

Chart 1 – Distribution of average annual per capita consumption expenditure for an average Nauruan person

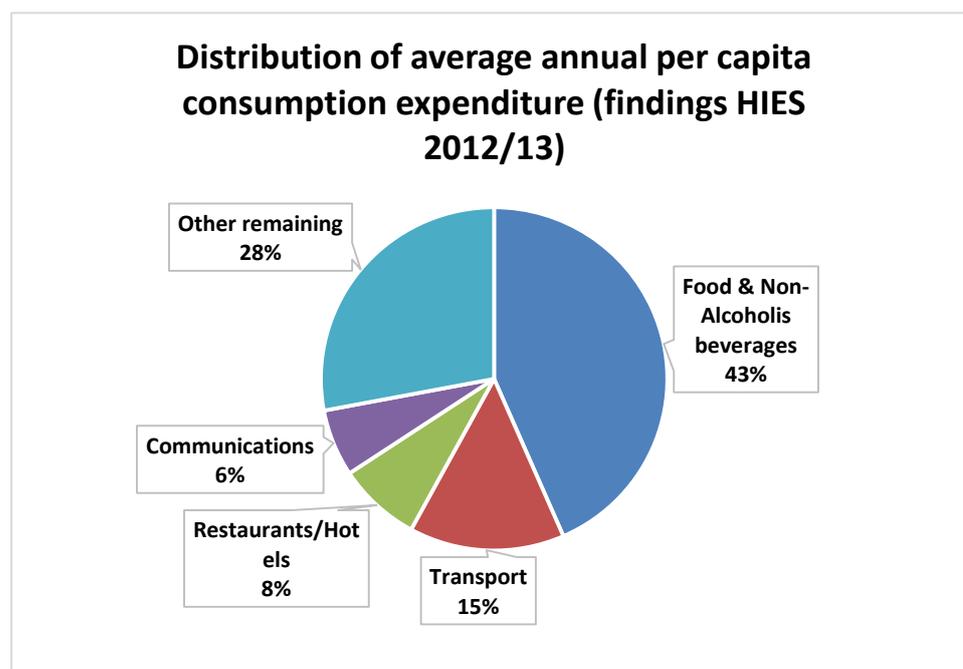
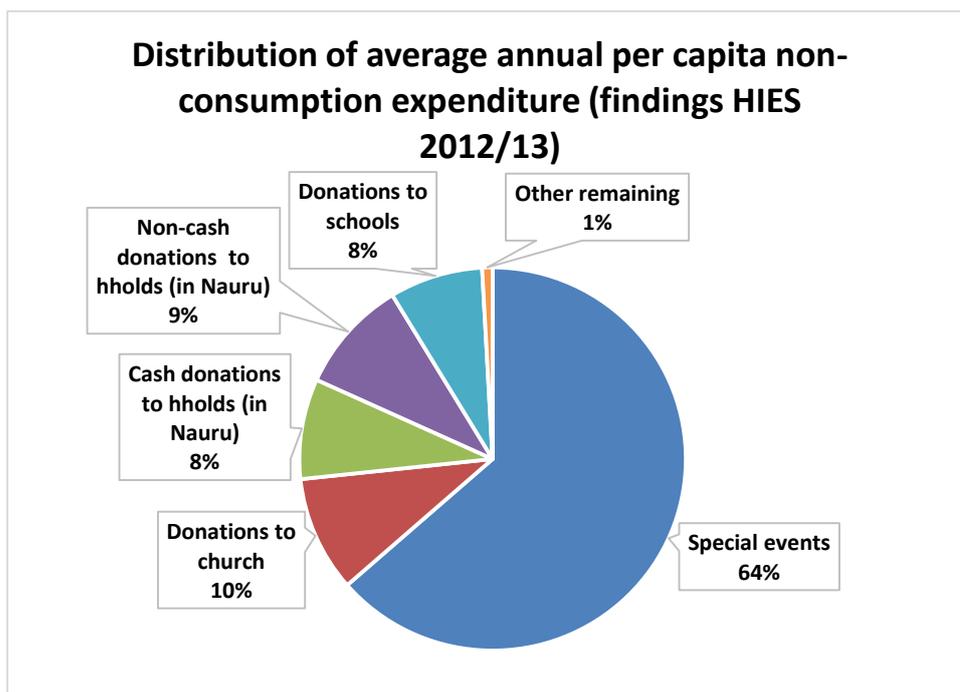


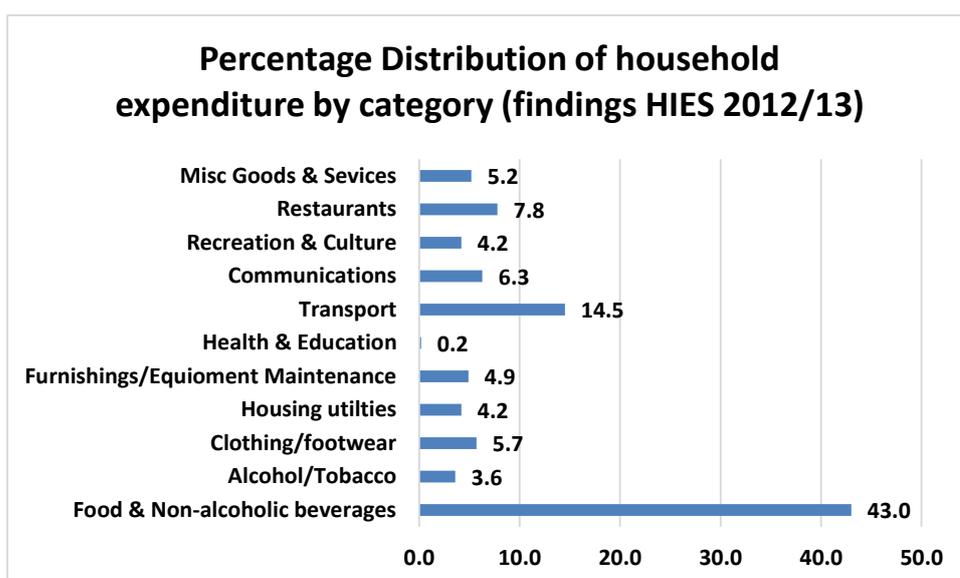
Chart 2 – Distribution of average annual per capita non-consumption expenditure for an average Nauru person



Investment and savings on house construction and major modifications registered as the least priority for the average Nauruan person.

The average household on Nauru in terms of consumption (or expenditure) consumes on average 43% on food and non-alcoholic beverages. Transports features high with 14.5%, and restaurants (take-away services) at 7.8% and high up is communications with 6.3%. These are indicative of the spending patterns of households as collected by the survey. Necessities like food and beverage remain high as a priority item. Health and education were not with a combined proportion of less than one per cent.

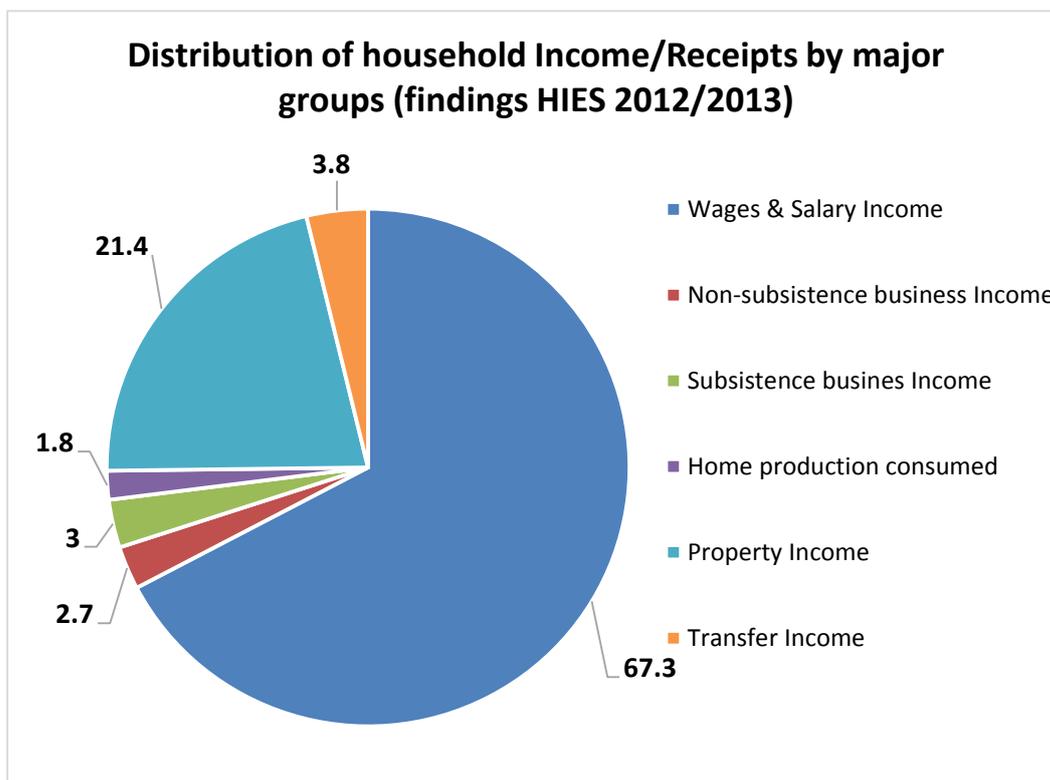
Chart 3 – Percentage distribution of household expenditure by category



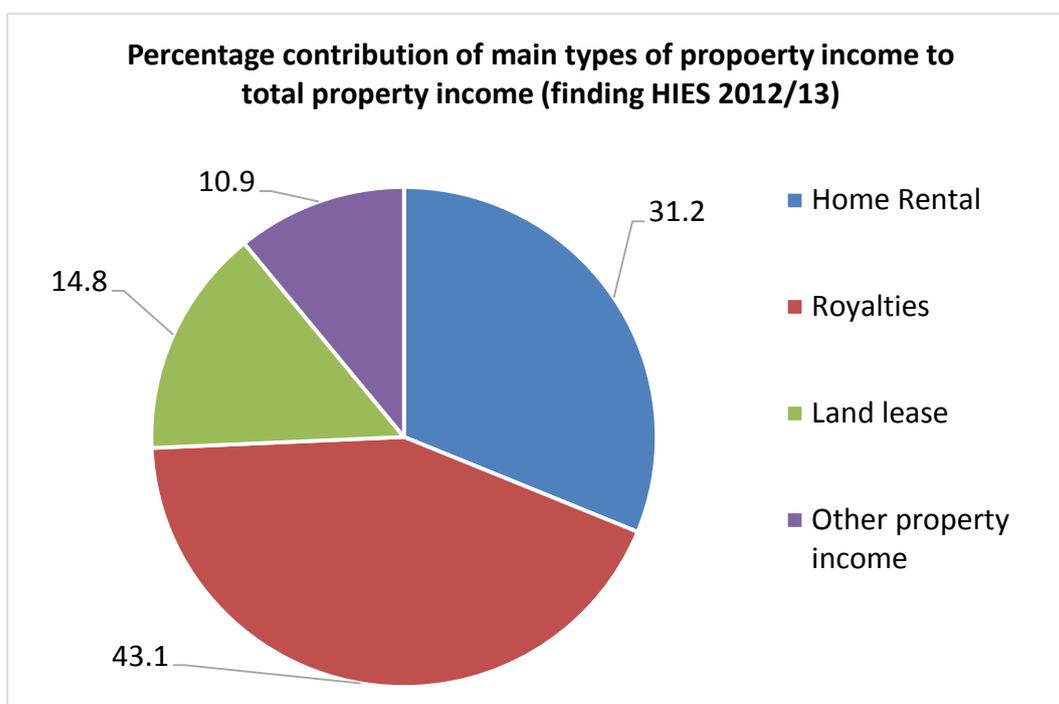
Per capita household income per annum for the average Nauruan household is estimated at AUD\$3,662 a year of which employment income accounts for 74% (AUD\$2,739)

Distribution of household income shows income from wages & salary as the key income source for the average household in Nauru. Property income not surprising was the second major source of income with its linkages to phosphate land ownership and dwelling rentals on the island. The remaining sources were barely larger than property income and represented approximately under 10 per cent of income.

Chart 4 – Distribution of household income/receipts by major groups



The total annual property income was estimated to be approximately just above AUD\$8m, representing a proportion of total household income of 21.4%. The major source was royalties at 43.1%, then home rental at 31.2%. The growth in home rental income can be attributed to recent high demands on property housing as a result of the introduction of the RPC. Subsequent shortages of housing for RPC expatriate workers has caused high demands causing rates to escalate rapidly.



National Accounts

In mid-2004 (FY2003/2004) National Accounts compilation was resumed, the annual value of Nauru’s gross domestic product (GDP) per capita was estimated to be USD 3,500. This estimate was made in line with the standards and recommendations in the UN’s System of National Accounts, and so is comparable with estimates made elsewhere using the same system. However, there are a number of features of the Nauru economy which needed to be taken in mind when comparing this figure with other PICTs. The most significant consideration is how to treat the RPC in the national accounts framework depending on it either being a domestic or foreign entity. There will be very significant impacts on how the gross domestic product derived and the per capita estimates.

National Accounts was last reviewed in March this year 2013 from FY2009/2010. Following the household income and expenditure survey in 2012/13 the national accounts will be rebenchmarked. The proposed review of the outputs and rebenchmarking are currently underway and implemented by the bureau with the assistance of national account experts from the *Pacific Technical Assistance Centre* (IMF/PFTAC), *Australian Bureau of Statistics* (ABS), and *Secretariat of the Pacific Community* (SPC).

Some of the key findings of the HIES review were;

The provision of financial intermediate services could not be identified in Nauru. There is no formal bank currently operating in the country at the time of the survey and loans are provided by individuals who do not accept deposits. Consolidating all local transactions under the arrangement with Bendigo Bank will need to be further investigated. As a result, financial intermediation services estimates could not be compiled.

Imputed rents estimates need to be reviewed because they have been distorted by high expectations of owners due to high rents paid by expatriates. Further investigations will be needed to determine if rents could be better measured by differentiating between a market for expatriates and a market for locals. No expenses could be identified for intermediate

consumption of owners of dwellings including owner-occupiers. Further analysis will be needed on this matter. Expenses on taxis and buses reported in the HIES could be used to compile production estimates for these transport activities therefore need further investigations.

NRC expects declining production and has experienced reductions in manpower, similarly with RonPhos. Operational costs are forecasted to increase to sustain high to sufficient production yields, however, it maybe be difficult to maintain with the tighter reporting conditions required by the government of Australia against the annual rehabilitation funding from the NACOS fund, diminishing manpower and depreciation of capital assets.

The Australian Dollar weakened against the US dollar from 0.97 in 2012, to 1.03 in 2013 then 1.09 in 2014. Given that constant prices take only volumes into account, a huge decline in constant prices is expected. But on the other hand the current prices will grow much higher due to a loss in market value of the AUD. It can be noticed that as the AUD starts getting closer to the USD, constant price growth is expected to start to narrow. The significance of the USD is the negotiated currency used for sale of processed phosphate rock.

Chart 5. Proportion of GDP by Industry 2003, 2008, 2012 at current prices

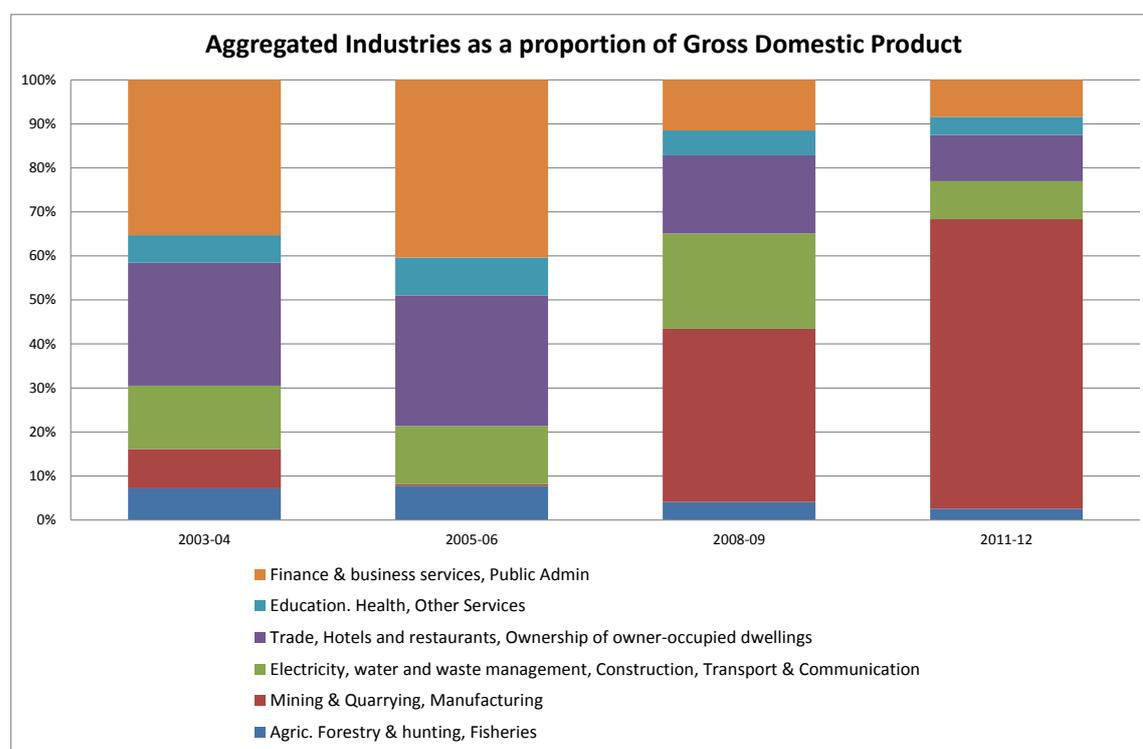


Chart 5 above shows aggregated industries as shares of total gross domestic product. *Mining, Quarrying and Manufacturing* has experienced the most significant growth over the period from 2003, to seizing production in FY2005/2006 and the latest year 2011/2012. By 2008/2009 the share of GDP for these industries increased to 40 percent of GDP, and by 2011/2012 it represented a majority proportion with almost 70 percent of total GDP. Prior to the ceasing of operation in 2005/2006 during 2003/2004 the total share of GDP for this industry was approximately just less than 10 percent. The rest of the industries showed decreases with the most noticeable being in the *Finance & Business Services, Public Administration* industry with shares of GDP showing decreases by more than three quarters which can mostly be attributed to the reduction of the national salary scales under reform policies, and the ceasing of all government financial institutions due to FATF blacklisting.

Trade, Hotels & Restaurants, Ownership of Owner-occupied dwellings began in 2003/2004 with a total share of GDP of almost 30 percent but by 2011/2012 the share dropped to one-third of GDP. The trend in shares of GDP were similar for the remaining aggregated groups falling approximately by half or two-thirds in proportions. The groupings of the aggregates were mostly for convenience but some attempt was made to group similar industries together.

Strong revenue performance in smaller Pacific economies occurred in 2013, while larger economies have struggled. For the second consecutive year, fishing license revenues are exceeding budget targets, particularly in Nauru, due to increased price of a fishing day under the Parties to the Nauru Agreement (PNA) Purse Seine (PS) Vessel Day Scheme (VDS) and are expected to continue in 2014 and possibly into 2015 calendar years.

Public investments to support the infrastructure development will continue to drive up debt levels and slow progress on fiscal consolidation adding to fiscal pressures in future years.

Growth remains driven by the expansion of the Australian Regional Processing Centre (RPC), which currently accommodates about 1,100 refugees. The RPC employs about 800 Nauruans and is now the second largest employer of the national labour force after the government.

Negotiations with the Bendigo and Adelaide Bank of Australia to establish an Agency bank in Nauru are being finalised. Nauru has not had a bank or other financial institution since the Bank of Nauru closed in 2002. The government has already commenced disbursement of A\$85-90 million in proceeds from the liquidation of the Nauru Phosphate Royalties Trust to over 5,000 Nauruan landholders. Financial literacy education is necessary to ensure this one off windfall contributes to the long term benefit of the recipients.

A fiscal surplus of A\$0.4 million was realized for FY2013 (ended 30 June) compared with the budgeted deficit of A\$4.3 million. This was due to higher-than-expected revenues from visa fees and fuel sales associated with economic activity generated by the RPC. Dividends and royalties from phosphate mining are projected to be lower by 15 to 20 percent in FY2015. Phosphate exports are projected at 513,000 metric tons in FY2014 and current tracking shows that if yields remain consistent this projected amount may likely to be met.

As Nauru is unable to borrow, achieving this spending increase is contingent on achieving revenue targets. Visa fee payments are expected to raise A\$19 million, but whether this is achieved is dependent on external factors that may be beyond the government's control.

Consumer Price Index (CPI)

The All Groups CPI Series (Chart 3) depicts historical data over the past 6 years with two measuring components. The "*Quarterly change*" represents the percentage movements for the All Groups CPI from one quarter to the other. While the "*Change since base period*" depicts the percentage change since the CPI base period (August 2008) to the corresponding quarter.

i. Quarterly change

On a quarter-by-quarter basis the historical series reported two most noticeable outliers with December 2009 quarter posting the lowest decline (down 5.6%) and March 2014 quarter posting the highest (up 7.8%). The event where the CPI plummeted in December 2009 was attributed by the decelerated index of Food, Alcohol & Tobacco and Transport &

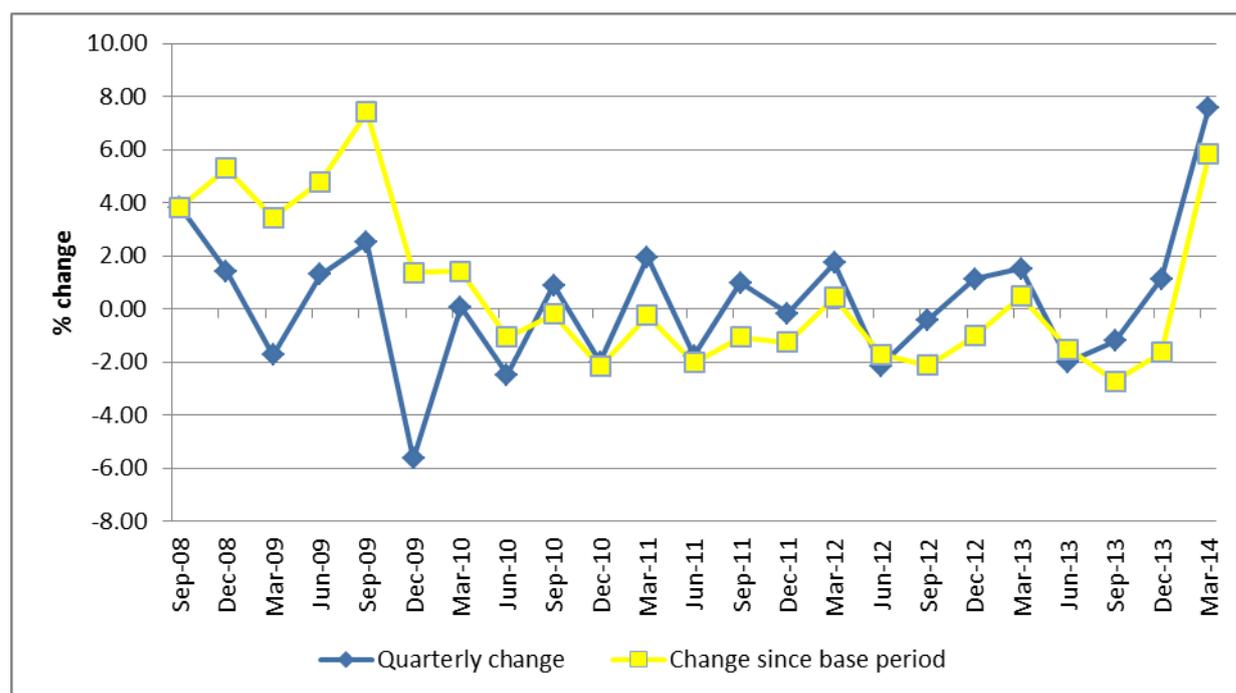
Communications. Declining rice contributed towards the falling of the Food index and the slight decrease of beer contributed to the drop of the Alcohol & Tobacco index. In Transport & Communication, mainly the discounted airfares for the festive period influenced the decline.

As stated above for the March 2014 surge, the spike for Alcohol & Tobacco was attributed towards the rise of beer and cigarettes. While in the Household operations, the impact was mostly for rise of refrigerators and freezer and spike in petrol and diesel influenced the increase for the Transport & Communications.

ii. Inflation change since base period

In comparison to the quarterly changes there is no significant difference between the two trend lines where the proportion of change is very similar. However, between the base period September 2008 and June 2010, inflation was much higher when observing the base period against the quarterly observation and vice versa for the remainder of the series. The resurgence for the All group index for March 2014 matched the peak inflation recorded in September 2009 where the inflation in rice also peaked. This time, Alcohol & Tobacco is the main contributor for the current upsurge.

Chart 6. CPI Historical Trend



In the annual comparison between current period and March 2013 the annual change of the CPI posted a significant increase of 5.3 percent as a result for increases of three of the seven main CPI groups.

As illustrated in Chart 6 above, Alcohol & Tobacco index lead the increase with 52.2 percent. Within Alcohol & Tobacco index the surges for cigarettes (up 52.4%) and beer (up 51.5%) both drove the index upward.

Likewise Transport & Communications also posted positive values of 8.9 percent. Similarly to the contributors to the rise in the monthly observations for Transport &

Communications, petrol (up 19.8%) and diesel (up 12.2%) were also the main contributors to index growth.

Household operations posted the smallest yet important increase of 1.4 percent. Within Household operations the main contributors were traced to dishwashing liquids (up 90.4%), television (up 70.4%), light fitting (up 54.6%) and freezer (up 12.8%).

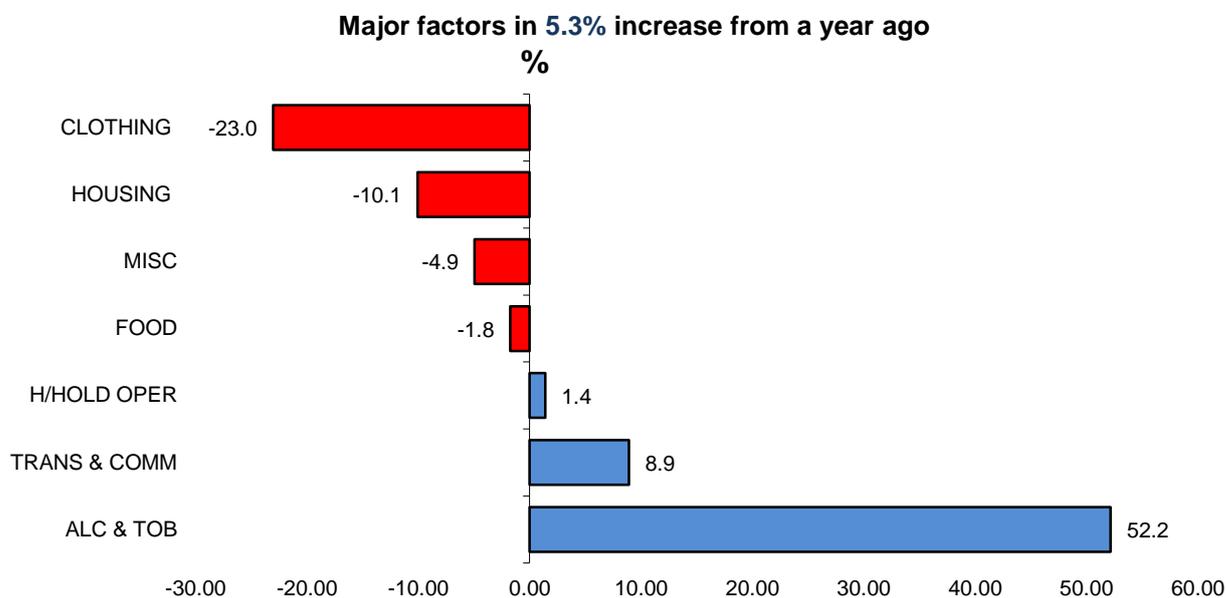
On the contrary, the Clothing index posted the highest decline with 23.0 percent and this was influenced by deflated prices of ladies mumu dress (down 42.9%), baby nappies (down 24.6%) and t – shirts (down 1.4%).

This was followed by the Housing Index with 10.1 percent. Contributing to the deflated Housing index was the falling prices of paint (down 18.9%), floor tiles (down 16.3%), 4x2 timber (down 15.8%) and cement bag (down 3.3%).

Next was the Miscellaneous index which decreased to 4.9 percent. Within the Miscellaneous group the impact was traced to exercise books (down 46.7%), blank CD-R (down 7.9%) and deodorant (down 3.5%).

Food index posted the smallest decrease with 1.8 percent. The deceleration was mainly attributed to the following items: potatoes (down 38.7%), 1kg tuna (down 33.3%), butter (down 19.8%), onions (down 18.2%), tea (down 13.3%) and cooking oil (down 12.9%). Other smaller contributors were evidence for sugar (down 7.9%), rice (down 5.5%), coffee (down 5.3%), soft drinks (down 3.6%), corned beef (down 3.6%), tinned sardine (down 3.2%), eggs (down 1.9%) and 2kg chicken (down 1.8%).

Chart 7. CPI Annual % change for March 2014 Quarter



Trade Statistics

According to the Asian Development Bank Pacific Monitor exports remain weak, but show signs of improvement. Merchandise exports to Australia from the Pacific fell by 13.4% (y-o-y) in January–August 2013. Papua New Guinea (PNG) continued to account for about 90% of total Pacific exports to the country, but slower economic growth in Australia and lower international prices depressed the value of petroleum exports. Growth in imports from Australia remained flat during the first 8 months of 2013 compared with a year ago. Thus, the Pacific’s balance of trade with respect to Australia worsened from a surplus of A\$307 million in January–August 2012 to a deficit of A\$32 million in the same period of 2013.

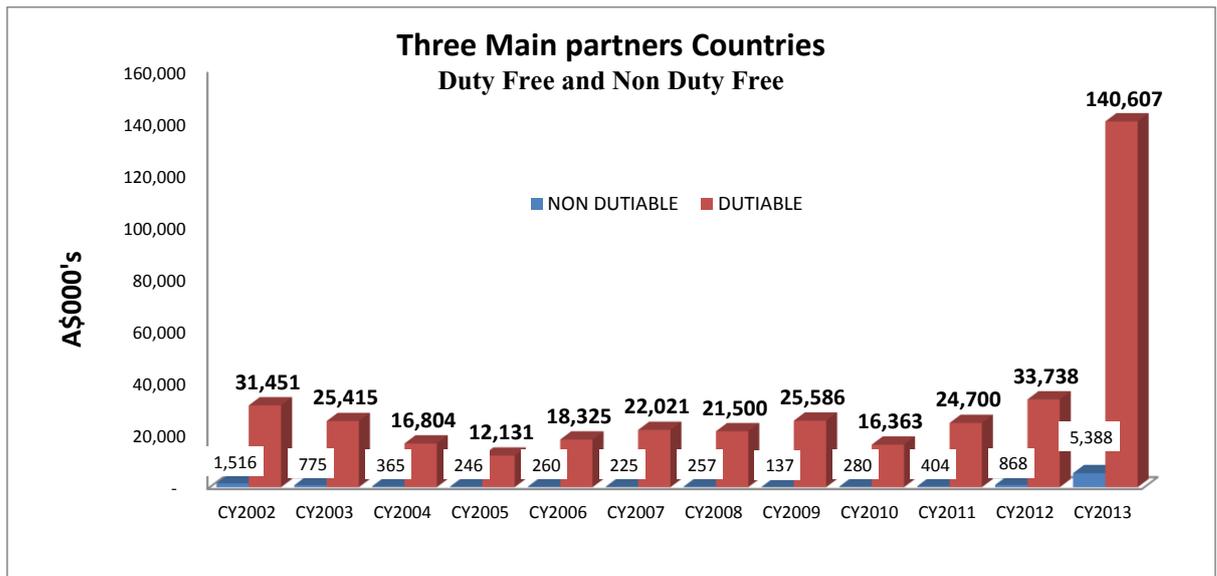
Pacific exports to New Zealand increased by 1.9% in January–August 2013 compared with the same period in 2012. A sharp midyear rise in phosphate exports from Nauru more than offset declines in food exports from Fiji and PNG. With Pacific imports from New Zealand (excluding transshipped goods) rising by 2.5% (y-o-y) in the first 8 months of 2013, the region’s trade deficit relative to New Zealand widened to NZ\$592 million from NZ\$577 million during the comparable period in 2012.

Trade statistics is one of the main economic indicators in monitoring sustainable development. It depicts the resilience of economies in terms of self-sufficiency in production, consumption, income and overall welfare at the country level.

Modernising Customs office with sufficiently adequate resources and training to facilitate proper capturing of trade statistics still needs to be prioritised by government.

With the lack of national trade data, the bureau has opted to use secondary sources to accommodate data gaps through the use of mirror trade data which are shown below (Charts 8&9). Chart 7 shows the value of merchandise imports by dutiable and non-duty goods from its primary trading partners namely Australia, New Zealand and Fiji. It is evident that imports for the last 3 years have increased. 2013 showed a large increase showing a growth of over 400% from the previous year, which can be attributed to introduction of the Regional Processing Centre. Increases in money supply through the disbursement of various payments has prompted increases in spending by households and raising demands on imports. The main driver pushing increasing imports is evidently construction materials which are directly related to RPC ongoing activities from FY2012/13, while major capital investments in imported motor vehicles were the mainstay of household expenses. Non-dutiable merchandise imports such as fruit, vegetables product and water remain very low among imported commodities. Revenue to be collected from merchandise duties is expected to be higher than usual for the consecutive years 2013/14 and 2014/15.

Chart 8. Nauru's Duty free and Non duty-free imports from Australia CY2001 – 2012.

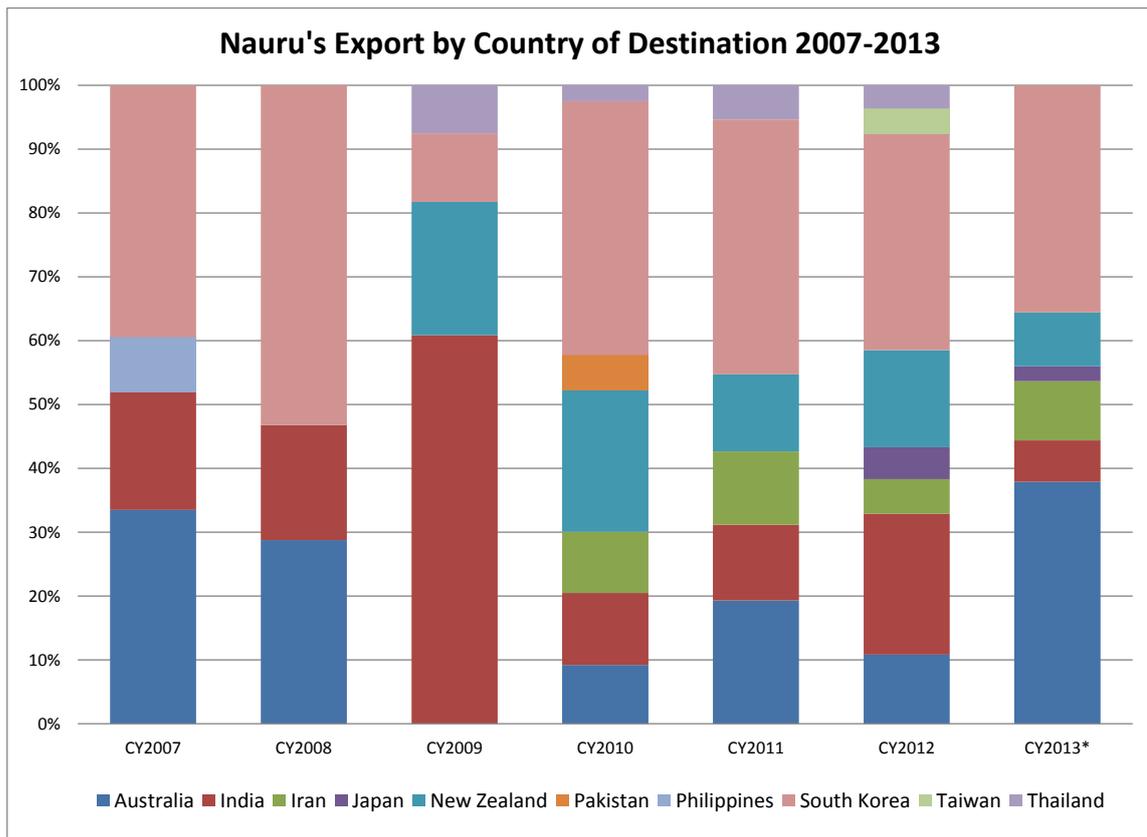
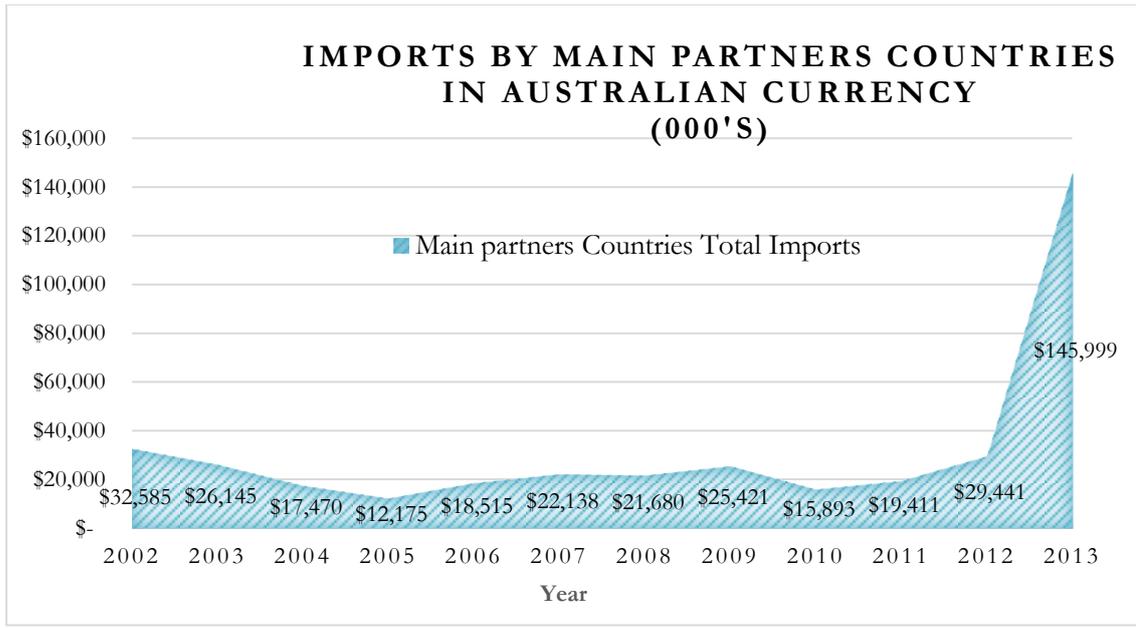


Australia remains the primary supplier of Nauru's material needs and supplies as shown in Chart 9 below. The substantial growth in imports from Australia and other trading partners will have a direct impact on out flow of cash money. Gross imports from Australia has grown by a magnitude of 5, or a growth of more than 400 per cent and dutiable imports as seen in chart above increased four times as much compared to the previous year by more than 500 per cent. It should be expected that revenue on imports should reciprocate and reflect this increase, unless current import policies and relations with the RPC administration are restrictive.

Chart 9. Imports value by primary trading partners, CY2002-2012

Chart 10 below show the latest export figures by main exporting partners with a growing demand from the Asian region in particular South Korea. This is a result of the transition of the mining sector with an improved infrastructure and increased productivity. These increasing values however will decline soon with primary mining sources exhausted unless the scoping for secondary mining determines otherwise.

Chart 10. Exports value by primary trading partners, 2012

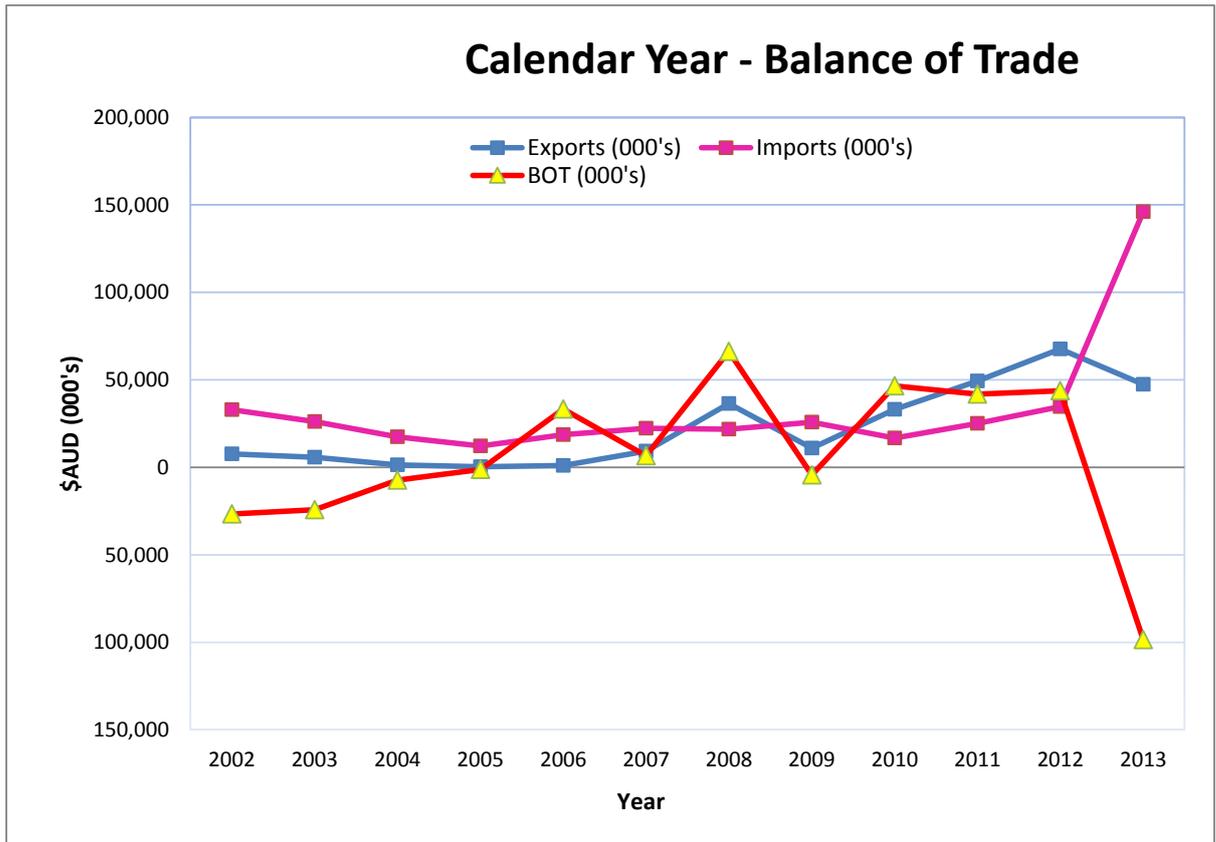


The slowing down of exports income and loss in surplus from pacific islands overall against Australia is visible and shows a wide negative trade balance in Nauru's trade from the previous year. Nauru's Balance of Trade determines the health of the economy and its relationship to the rest of world. The balance of trade depicted in Chart 11 returned a

surplus of AUD\$38 million in 2012 following surpluses in 2010 and 2011. It was anticipated in the last budget paper 2013/14 that trade deficits would likely re-emerge as the economy recovers and more demand on imports increases. The inclusion of Fiji's re-exports to Nauru were the primary cause of the spikes in 2006 and 2008. Part of these re-exports consists of second-hand motor vehicles with origins in Japan, as well as fabrics, construction materials, mechanical spare parts, dairy products and mineral water. Yields in phosphate exports are expected to keep declining overtime so renewed focus on an alternative income source will be needed.

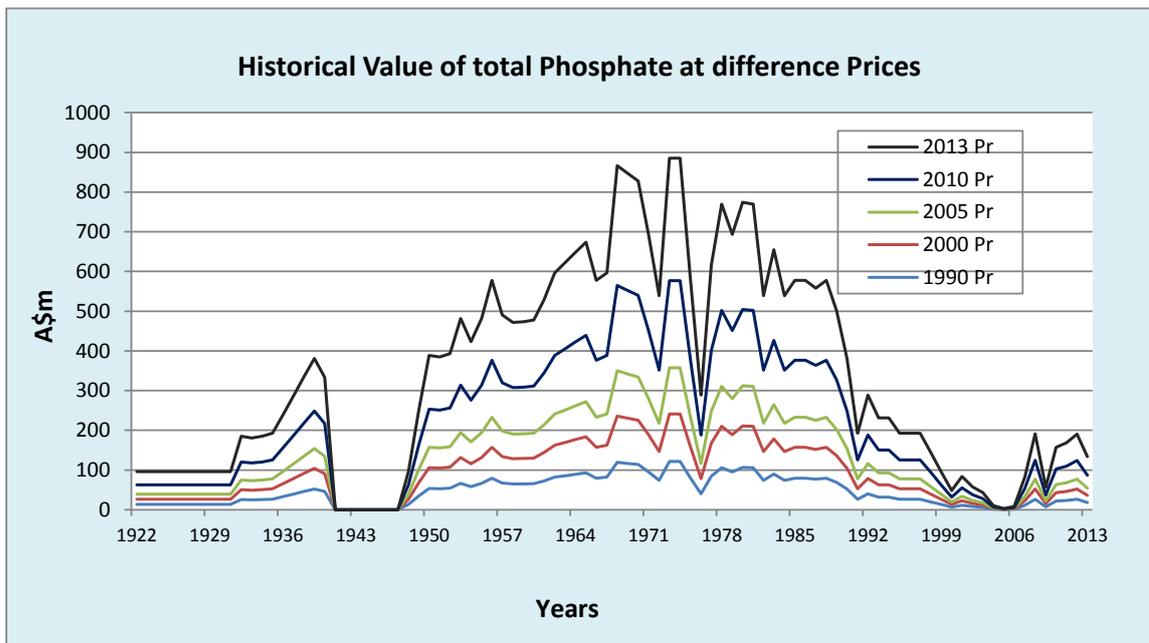
According to Asian Development Bank's Pacific Monitor the weak global growth is impacting the Pacific largely through lower commodity prices. Subdued global demand is keeping international commodity prices low—adversely affecting agriculture, mineral, and forestry export revenues of some Pacific economies.

Chart 11. Exports value year-on-year by primary trading partners, 2012



Note available imports figures are only for Australia, New Zealand and Fiji.

Chart 12. Historical Value of Total Phosphate Export at constant and current prices



Despite recent rebounds in the industry, estimated income revenues of phosphate remain relatively low in recent years, with the latest years showing decline and is expected to continue.

Labour Force Status

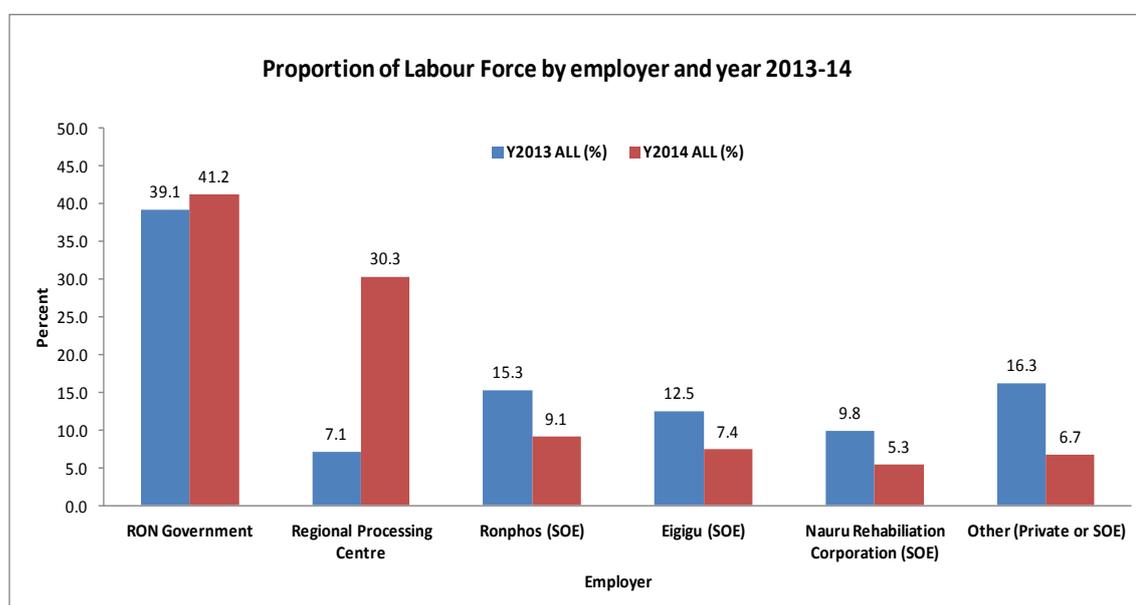
Labour Force Administrative Sources 2013-2014

Table 1. Proportion of Labour Force by Employer and Year 2013-14

EMPLOYER	Y2013 ALL (%)	Y2014 ALL (%)	Y2014 LOCAL (%)	Y2014 EXPAT (%)	Percentage Increase/ Decrease
RON Government	39.1	41.2	37.8	3.4	8.5
Regional Processing Centre	7.1	30.3	16.3	14.0	12.9
Ronphos (SOE)	15.3	9.1	8.8	0.3	-0.1
Eigigu (SOE)	12.5	7.4	7.0	0.4	-0.1
Nauru Rehabilitation Corporation (SOE)	9.8	5.3	5.2	0.2	-0.4
Other (Private or SOE)	16.3	6.7	5.4	1.3	-1.6
TOTAL		100.0	80.4	19.6	15.8

Sources: Derived from administrative sources

Chart 13. Proportion of Labour Force by Employer and Year 2013-14



In Table 1 and Chart 13 above are related in terms of actual and percentage figures. It shows that labour force in RON Government has increase to 44.1 percent in year 2014 updates compared to year 2013 which was 39.1 percent, whereas in year 2014 only, shows 37.8 percent in local population compared to a 3.4 percent in expatriate workers, mostly engaged with teaching staff at Education Department and nursing staff with the Health Department.

The RON Government overall percentage growth shows a positive increase of 8.5 percent. The positive increase at RON Government is reflected from creation of new jobs mostly at the Justice Department and Nauru Police Force in relation to the workforce development for Regional Processing Centre since the establishment of new sections.

The job opportunity at the Regional Processing Centre rapidly increase of 30.3 percent in year 2014 updates compared to the previous year 2013, which was 7.1 percent. It also shows in year 2014 updates the local population experienced a 16.3 percent have overtaken the number of expatriate workers at 14.0 percent, which the expatriates used to be higher when there was only one campsite.

There are currently three settlement campsites allocated in separate locations for asylum seekers. The rapid increase in the local population at RPC may also reflect the impact with the decrease in labour force towards the three main SOEs as listed above in Table 1 and Chart 13. The impact may also reflect the labour force in the private sector and other related SOEs and other subsistence work. The strong increase in labour force at RPC is most likely reflected from high salary rates and wages offered including unskilled recruitments and medium level recruitments through higher level recruitments.

According to percentage wise in above Table 1 and Chart 13 also shows that labour force at Nauru Rehabilitation Corporation, Ronphos and Eigigiu Holdings are experiencing a decrease between years 2014 compared to year 2013 results. The local population continues to outnumber the expatriate workers in each of the three main SOE. Each of the three main SOE shows a negative growth in the overall percentage.

The labour force in the private sector and other SOEs shows an assumption of 6.7 percent decrease in year 2014 updates compared to the previous year 2013, which was 16.3 percent. The local population engaged with other employers' shows a much higher of 5.4 percent than in expatriates which was 1.3 percent. The decreasing impact in subsistence work as most market vendors and most local fishermen and most private caterers tend to cease subsistence activity and acquire job opportunities at the RPC.

Labour Force Projections

The working age population by the national standard is observed to be between the ages of 15 years and 60 years (the retirement age) for Nauru.

Labour Force is defined in the census consisting both Employed and Unemployed.

- Employers
- Self employed
- Employees
- Unpaid work
- Subsistence work
- Unemployed
- Other paid employment

Employed population as define in the census consists of the following;

- Salaries/profit
- Subsistence

- On leave and sick leave

Unemployed population as define consists of the following;

- Population working age looking for work and available for work
- Not in Labour Force: Population defined as Pupil attending school 15yrs +
- Home duties/care,
- Do not want to work,
- Too old/disabled

Table 2. Labour Force Participation populations, 2002 to 2014/15

WORKING AGE (15+)	Census Y2002	Census Y2006	Census Y2011	Projections Y2014/15		
				Male	Female	Total
Total Population	10,065	9,086	*10084	5,470	5,337	10,807
Labour Force	3,280	4,106	3,952	2677	1673	4349
- Unemployed	746	1,567	906	553	407	960
- Employed	2,534	2,539	3,046	2124	1266	3389
Not in Labour Force	996	1,109	2,223	724	1,712	2488
Working Age population	4,276	5,215	6,175	3413	3424	6837

Note: *Including Total Persons in Institutions

Table 3. Labour Force Participation rates (%)

WORKING AGE (15+)	Census Y2002	Census Y2006	Census Y2011	Projections Y2014/15		
				Male	Female	Total
Labour Force Participation Rate	76.7	78.7	64.0	78.4	48.9	63.6
Unemployment Rate	22.7	38.2	22.9	20.7	24.3	22.1
Employment Rate	77.3	61.8	77.1	79.3	75.7	77.9
Inactivity Rate	9.9	12.2	22.0	13.2	32.1	23.0

Sources: Census 2002, Census 2006, Census 2011 provisional tables,
Projections for year 2014 based on rates from the Census 2011 provisional results

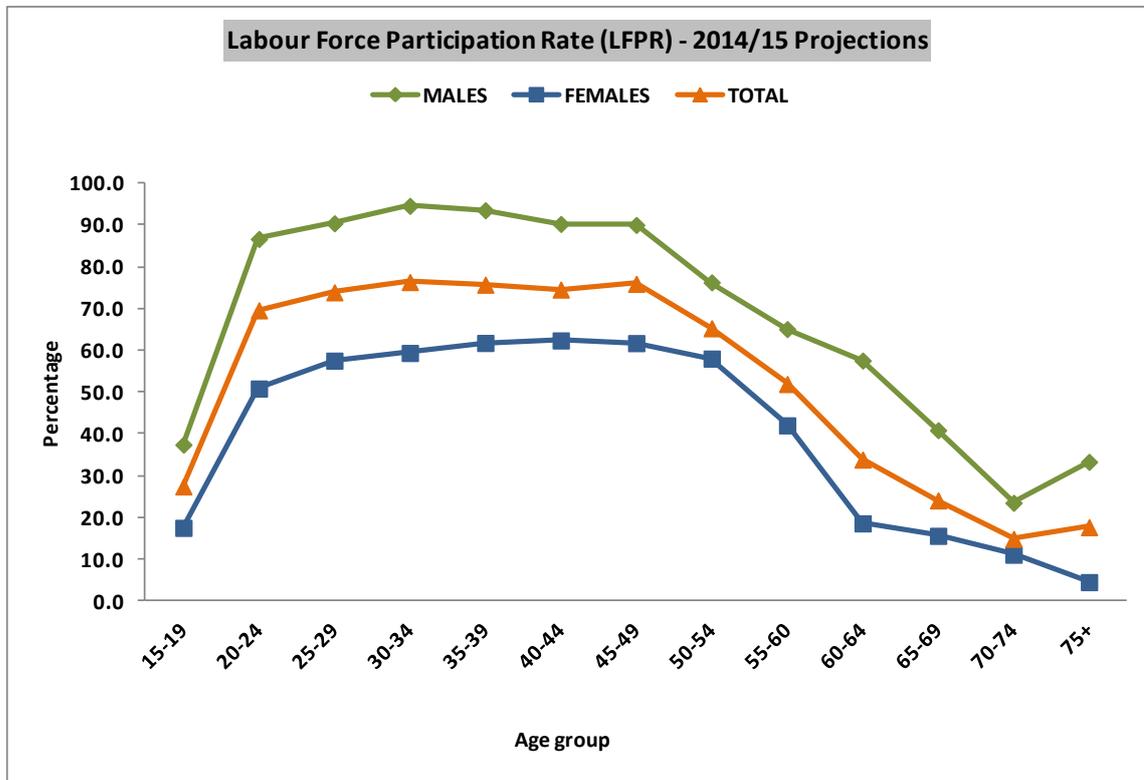
In Table 2 and 3 above are related in terms of actual and percentage figures. The Labour Force participation in Table 2 and 3 shows approximately 64 percent in 2011 and only 63.6 percent in 2014/15 projections. Unemployment rate was 22.1 percent in 2014/15, compared to 22.9 percent in 2011. The employment rate shows no significant change occurred between 2011 (77.1%) and 2014/15 (77.9%), which will, remain steady.

Inactivity rate also known as Not in Labour showed approximately 22 percent in 2011 and 23.0 percent in 2014/15 projections. The increase in “Inactivity Rate” between 2011 and 2014/15 will continue to show a steady increase compared to the previous results between 2006 and 2011 which mentioned from previous census reporting due to two factors; firstly in 2006 there was a significant drop in population due to the repatriation of Non-Nauruan workers and their families which were previously captured in the 2006 mini-census. Most of these Non-Nauruan households consisted of families who have stayed in Nauru for

more than two generations. The second factor is the unavailability of jobs that has led to some loss in confidence for job seekers.

According to 2014/15 projections the **Labour Force Participation Rate (LFPR)** will be higher for males (78.4%) than for females (48.9%). The same case with the **employment rate** will show a higher rate for males (79.3%) than for females (75.7%). The **unemployment rate** will be higher for females (24.3%) than males (20.7%).

Chart 14: Labour Force Participation rates (LFPR) by age and sex (%)



In Chart 14 above shows the LFPR and the general pattern usually show a low participation rates for the population 15-19 years which explains the population of the particular age group attending school or tertiary studies, or seeking job. The pattern shows that most men will engage to the labour force at the age of 30-34 while most females at the age of 40-44. The pattern continues to show that the results will begin to decrease at age of 50-54 leading to the retirement age 60 years and over.

The pattern shows that the result of population aged 60 years and older are in the labour force which explains that older people continues to be economically active supporting themselves or the household by producing goods for their own consumption. The labour force participation rate shows that males were dominant than for females at all ages.

Economic Activity

- ***Economically Active:*** All population and all ages engaged in the labour market or available to be engaged in the labour market or economic activities.
- ***Economically Inactive:*** All persons not classified as employed or unemployed within the working age population plus outside the working age population and also persons listed in the institutions.

Table 4. Economic Activity – 2002 – 2014/15

WORKING AGE (15+)	Census Y2002	Census Y2006	Census Y2011	Projections Y2014/15		
				Male	Female	Total
Total Population	10,065	9,086	*10,084	5,470	5,337	10,807
Economically Active	3,280	4,106	3,952	2,677	1,673	4,349
Economically Inactive	6,785	4,980	**6,132	2,793	3,664	6,457

Note: * Including Total Persons in Institutions

** Including Total Non-eligible working age persons and Total Persons in Institutions

Table 5. Economic Activity by proportion

WORKING AGE (15+)	Census Y2002	Census Y2006	Census Y2011	Projections Y2014/15		
				Male	Female	Total
Total Population (%)	100	100	100	100	100	100
Economically Active (%)	32.6	45.2	39.2	48.9	31.3	40.2
Economically Inactive (%)	67.4	54.8	60.8	51.1	68.7	59.8

Sources: Census 2002, Census 2006, Census 2011 provisional tables,

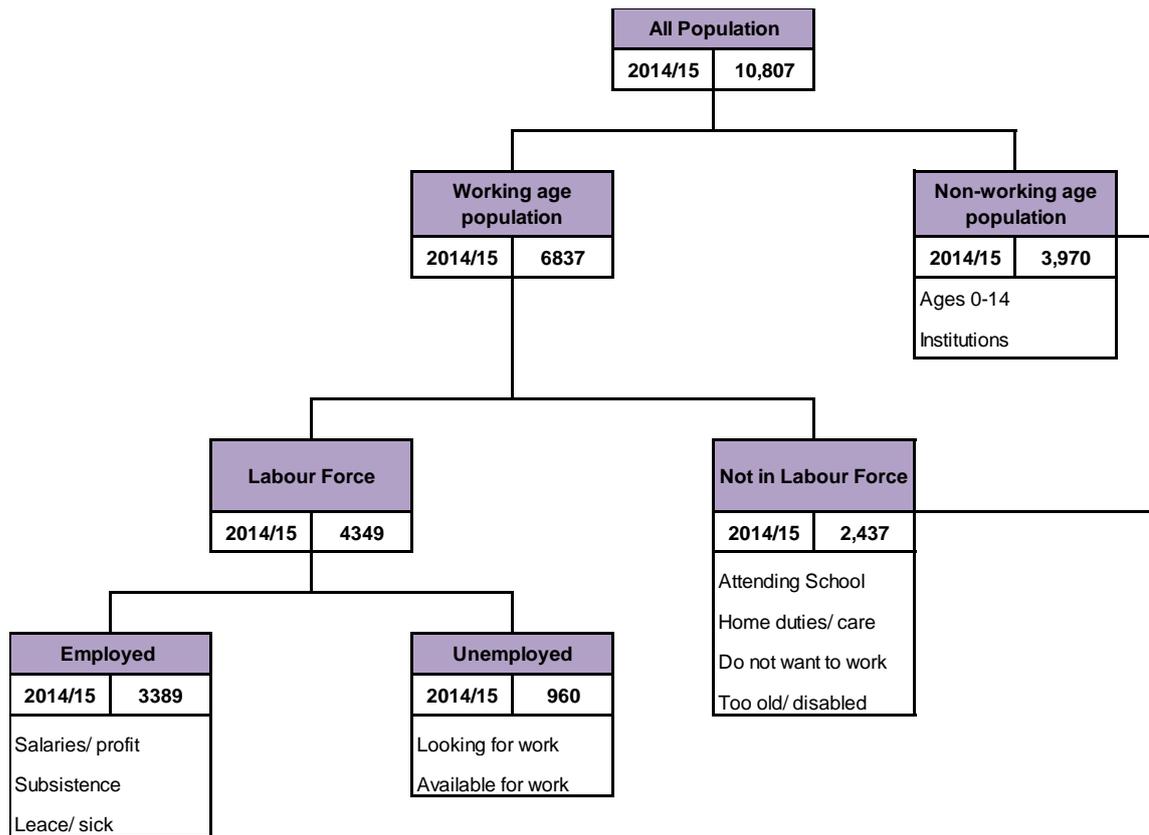
Projections for year 2014/15 based on rates from the Census 2011 provisional results

Table 4 and 5 are related in terms of actual and percentage figures. Economically active is calculated from the Labour Force population size by whole population size including all ages as the result shows a stable increase of between 39.2 percent in 2011 and 40.2 percent in 2014/15 projections. Economically inactive is calculated from Not in Labour Force population size by whole population size including all ages as the result shows 60.8 percent in 2011, compared to a steady change of 59.8 percent in 2014/15 projections.

As mentioned in previous census reporting between Census 2006 and 2011, the cause is most likely reflected by job seekers, particularly the types of unskilled jobs which continue to become scarce, as most of Nauruans who are currently within the Labour force are unskilled.

The Government continues to provide and encouraged the youth population through program known as Staff Training and Student Internships, which involves placing school leavers for longer term work placements. The Youth Affairs Training Program is also another reference that targeting our youths with work attachments as both program mentioned above are contribution to the employment workforce development program.

Chart 15. Labour Force Structure



Sources: Projection for year 2014/15 based on rates from the Census 2011 results

In Chart 15 above shows the Labour Force structure to provide a clear picture of relationships. The 2014 population projections show all people total of 10,807. The structure show two separate directions for Working- age population at 15 years and over, total of 6,687 and Non-Working population total of 3,970. The Working age population are people may be available or not available to work. Non-working age population are people between the age 0-14 years of age and people listed from the institutions. Nauru institutions are considered as the prison, hotels, hospital and the Catholic mission quarters.

The structure further show two separate directions for Labour Force total of 4,349 and Not in Labour Force total of 2,437. Not in Labour Force structure represents pupil attending school, home duties/care, do not want to work and too old/ disabled. Labour Force has a subset of Employed total of 3,389 and Unemployed total of 960. Employed representing pupil receiving salaries/profit, engaged in subsistence activities and on formal leave whereas Unemployed representing pupil still seeking job and available for work as previously stated above.

PART 3: Public Sector Reform

Financial Management Information System

The new computerised integrated Financial Management Information System (FMIS) was implemented in 2011. The Department of Finance began to process payments directly on the system in 2011-12 and has continued to develop the system applications in 2013-14, particularly with the payment process and the use of the system for monitoring and

reporting on revenue and expenditure within year.

Departmental reports for actuals as well as commitment items are now accessible live on the system to enable departments to better track and manage their spending.

The roll out of the FMIS to other departments continued in 2013-14. The system requires considerable effort to embed the electronic processes and reduce those processes still relying on paper systems outside of the FMIS. This embedding of the system will require support in training, some system enhancement, and the production of financial instructions that reinforce good public finance principles using the FMIS. This system embedding is an on-going process which, with the required support, will progressively improve the quality of financial information. There is still signs of coding errors and delays in posting revenue that suggest substantial very basic user retraining is required,

During the first half of 2014-15 the Ministry of Finance will engage specialist support as required to address data integrity issues. This will also deliver high intensity training and mentoring of key MoF and line ministry users. The Government will purchase additional licenses and modules and make more effective use of the chart of accounts structure to support more effective links between strategic and annual planning and budget execution. This work is a prerequisite to further steps on the adoption of a Medium Term Expenditure Framework (MTEF) and the Road Map for Financial Management Reform.

State Owned Enterprises

The Government recognises the need to improve performance of the SOE's. It has been gradually restructuring SOEs' management structure with the assistance of ADB. Ronphos was restructured in 2011-12. Ronphos and Our Airline are presently the only SOEs making a contribution to the Budget through its own business activities. In 2013-14 Ronphos contributed a total of about \$5.3 m through Royalties, dividends and a special payment of \$1m towards the Bank of Nauru debt reduction. It is expected along with the Our Airline and NUC to contribute significant dividends and royalty payments in 2014-15.

Proper recording and tracking of company assets is an essential aspect of effective company management. Asset management is required to satisfy financial reporting requirements, and to safeguard company assets. This responsibility includes protecting assets from misappropriation, misuse, damage and deterioration. Proper management of company assets also allows for maintenance scheduling and renewal and assists in making replacement decisions. The new management structures for both Ronphos and NUC will facilitate in better management of SOE assets. The Government commenced similar reforms with other SOE's progressively in 2013-14 focusing on NRC and will continue this work in future years, with an objective of obtaining fully audited financial statements and a better picture of the government's exposure to SOEs

Public Service Reform

The Government undertook a review of the public service structures and reward system in 2013-14 through the provision of technical assistance from DFAT. The review is aimed to improve capacity in the Public Service to ensure that the Public Service is structured in the most effective way, to meet the demands for more effective and efficient delivery of key public services to the people of Nauru. It will also identify a way of rewarding and structuring the Public Service in a more competitive labour market and provide a basis for a concentrated program of developing skills and capacity to match the demands of a more

productive public service. It is understood that the review will also trigger the possibility of developing and implementing a performance management system as part of the overhaul of the public service.

The Government will be considering the recommendations of the review in the first quarter of the 2014-15 financial year and developing an implementation strategy for the medium term.

Public Sector Financial Management and Budget Reform

Nauru has taken important steps over recent years to improve its resource management, accounting and reporting systems. One of the most significant measures has been the implementation of a new FMIS over the period since 2011. The new systems have considerably improved the management of Government procurement processes, the recording of commitments against line ministry budgets, and the capture of revenue data. The new systems have also provided a more comprehensive classification of fiscal data and the production of a range of ministry and donor budget execution reports. However considerable challenges remain.

The Government has not produced comprehensive annual whole of government financial statements since 1998/99. The government now intends to put in place a new annual whole of government fiscal reporting system with the intention of producing the first set of annual fiscal statements for 2013/14. A significant impediment to this objective is the fact that the Government does not maintain a formal fixed asset register, and there is no consistent, unified system for recording the acquisition, movement and disposal of its assets. Rather, the fixed assets records that exist are found in various documents, reports and studies and are not consolidated into a single government database suitable for maintaining proper accounting and fiscal reporting records.

In support of this reform initiative, the Government requested assistance from PFTAC to review the existing fixed asset accounting and management framework and provide advice on the development of key elements of a strengthened fixed asset management framework, including the development of formal systems for asset classification, asset recognition, fixed asset accounting, asset stocktaking, fixed asset valuation, fixed asset reporting and asset life cycle management. The mission was undertaken in February 2014 and initial work on developing an assets register has begun.

The basis of the FMIS is Technology One Financials. Technology One Financials is a commercial suite of financial management applications with a significant international client base. The Government implemented the Technology One applications in 2011. The applications are used to support some of the core financial functions of government: budgeting, accounts payable and payments, bank reconciliation, accounts receivable and financial reporting. DFAT funded technical assistance in 2012-13 for the upgrade of the FMIS. The upgrade included the systems and accounting controls of the FMIS and an instructions procedures manual.

The manual is now in place and will form the basis for further developments of proper Finance Directions under the Public Finance Act and better integration with the procurement reforms of 2013.

The new procurement procedures require all departments and State Owned Enterprises to procure general items (for purchases over \$3,000) through an appointed Government procurement agency. This will ensure that the Nauru Government realise better value of its

purchases. Implementation commenced in September 2013 and a Resident Office of the Procurement Agent is established. Implementation has been slower than expected and some resistance has been encountered but is expected that a more concentrated effort and renewed direction that all major procurement including by SOEs should realise some gains. The Procurement arrangements are to be reviewed in September 2014. A training needs assessment and training implementation strategy should be in place early in 2014-15, under the contract with the procurement agent.

A fully functional FMIS is crucial to the success of progress in this area, particularly in relation to that part of the Road Map relating to development of a Medium Term Expenditure Framework. While progress in the past year has not been as rapid as hoped, the Ministry of Finance now has restaffed some critical positions, will be getting specialist support for the FMIS and should now be able to take some important steps that will integrate Financial Directions and FMIS Operating Manual, to bring about improved financial performance and oversight of SOEs; and enhanced PFM regulatory framework.

With additional support also now available in the Revenue and Customs offices; enhanced revenue management systems and revenue flows and taxation reforms will also be undertaken and an active training program implemented. This will have the effect of reducing leakage in revenue collections and also provide the base for introduction of fiscal and taxation reforms over the next one to two years.

DFAT have created a Performance Monitoring Assessment Group (PMAG) to assist Nauru to improve its monitoring and reporting efforts. This Group comprises representatives from DFAT, PFTAC and ADB and will report regularly on progress or any special technical assistance that may be required.

PART 4: State Owned Enterprises

Currently only Ronphos and Our Airline contribute to the budget revenue line from its business activities while Our Airline collects and remits passenger departure tax. More emphasis is being placed by the Government on SOE's to provide adequate financial reporting in the interests of transparency and accountability. The people of Nauru are entitled to have financial information on corporations that serve and benefit the community and the Government is entitled to expect a return on the investments already made in their SOEs. .

This section provides a brief overview of the objectives and financial expectations of the SOEs in 2013-14.

Ronphos

The broad business strategy of Ronphos Corporation is to maximise return to the shareholder through vigilant management and to contribute to the growth of the Nauru economy now and into the future.

The Ronphos objectives in the coming year include:

- The design, fabrication and commissioned installation of upgraded phosphate rock drying facilities, which among other things will greatly reduce dust emissions.

- To continue the debt reduction strategy and achieve a positive net asset valuation as part of a strategy to place Ronphos on a sound financial footing consistent with international accounting standards.
- Begin the removal of redundant plant and equipment as an early stage of the restitution of its legacy footprint.
- To efficiently manage the operational costs of the Corporation
- To maintain growth in volume consistent with the capacity of secondary mining and rehabilitation activities, and to continue research into options that will support effective commercial partnerships
- Maintain best price options and strategies for price making and new channels to market in a highly competitive market place.

Ronphos is expected to generate phosphate sales of \$US65.4 million during 2014-15 compared to phosphate sales for the 2013-14FY of US\$61.3 million. Production and export targets have been set at a realistic level based on recent performance and a review of the lands planned for mining. Buyer demand for Nauru phosphate remains strong although recent market trends are softening and supplies from China in particular come on stream. Subdued economic conditions in traditional high users of phosphate including India and the US persist. Ronphos plans to continue a combination of well-targeted capital expenditure, efficient operations, ensuring no new liabilities and a re-organisation of debt repayments by Ronphos. However, it is expected that selling price rather than production volumes will be the most significant determinant of Ronphos revenues.

Nauru Rehabilitation Corporation

NRC's immediate priority throughout 2013-14 was to increase profitability by increasing operating revenues and decreasing operating expenses. In 2014-15 NRC will initiate development projects and continue to increase profitability. This follows a review of revenue sources and operating costs carried out under the direction of the new CEO.

Wherever possible the financial return for existing commercial agreements will be maximised and specific financial return for services without commercial agreements will be introduced. New agreements will be introduced for on-island businesses for disposing of their solid waste at the landfill and for the upgrade and ongoing maintenance of mine haul roads that are used by non-mining traffic.

The expired RadCA funding will be replaced with funding defined by a new agreement and drawn from the residual funds in the NACos trust account.

New arrangements will be underpinned by a new Five Year Plan, a cornerstone of which is a five year budget forecast to be reviewed at least annually as part of the normal budget cycle and the intention to move towards a medium term strategic outlook.

NRC is forecasting total revenue in the order of \$20.3 million for 2014-15 and a total surplus of approximately \$2.2 million although this is highly sensitive to actual mining related outcomes. Capex and operating expenses are forecast to be in the order of \$18.0 million. Income from services functions still forms a relatively small proportion of total revenue and is subject to some risk of slow payment for services.

Eigigu Holdings Corporation

For the new financial year 2014-15, Eigigu continues to shift its direction and outlook from its traditional low-cost community-targeted services, to streamlined and profitable operations, which are aimed at ensuring the viability of Eigigu as a full commercial enterprise. In 2014-15 Eigigu proposes to operate profitably with the Menen Hotel and the Supermarket contributing the majority towards profitability. The Menen Hotel will continue to benefit from the RPC and ongoing demand for accommodation.

The Eigigu's construction arm will continue refocusing on more viable activities. These activities include renovations to the Civic Centre, construction of additional rooms at the Menen Hotel, construction of houses and modifications to the Department of Health.

Our Airline

Nauru Air Corporation, trading as Our Airline, operates three Boeing 737-300 aircraft in compliance with the regulatory requirements of the Australian Civil Aviation Safety Authority (CASA).

The re-opening of the offshore processing centre on Nauru has seen a marked increase in both the services provided and the number of passenger movements. This coupled with the increase in Australian Department of Immigration and Border Protection (DIBP) has allowed Our Airline to achieve a second successive surplus.

The key challenges that face Our Airline in the budget and subsequent years remain predominantly those of the past years including:

- Vulnerability to the externalities of the Australian policy on Offshore Processing
- Uninterrupted supply of fuel on Nauru at competitive prices
- Increasing maintenance costs
- Increasing regulatory requirements resulting in increases in overheads

Our Airline's strategic outlook is to consolidate its operational strength and remain open to maximise current opportunities while maintain tight control on its fixed operating costs and maintenance in compliance with regulatory requirements. This will enable OA to be in a position to identify and take advantage of emerging business opportunities and support economic growth in Nauru, for example by acquisition of a dedicated freighter and in turn to leverage opportunities for additional charter services.

For 2014-15 Our Airline is planning to achieve some \$58m in revenue of which about 90% is expected to flow from passenger related services, which are near capacity and include block capacity agreements with some major clients. It is expected that at this level the Government will receive about \$800,000 in departure taxes, which are collected and remitted by Our Airline.

PALCo&YALCo

Pacific Aircraft Leasing Holding Corporation (PALCo) and Yaren Aircraft Leasing Holding Corporation (YALCo) are the entities which own the two Boeing 737-300 aircraft, VH-INU and VH-NLK respectively, which are leased to and operated by Our Airline.

PALCo's aircraft, VH-INU, was originally financed through a commercial loan with NPRT which has since been repaid in full with interest, by refinancing with the Exim Bank of

Taiwan. Through an annual grant from the Republic of China (Taiwan) the aircraft loan was fully repaid in 2012. YALco obtained a commercial loan from Getax Pacific Finance Company Ltd (Samoa) in 2008 and this loan was fully repaid in May 2011. All charges have been released and this aircraft is now fully owned by Nauru without any debts or encumbrances. In 2013-14, both aircraft will continue to be leased to Nauru Air Corporation.

Nauru Utilities Corporation

The provision of electricity to the community has shown growth in revenue from domestic, industrial and Government users during the 2013/14 year. In 2014/15 NUC is expecting to earn \$5.3 m of the estimated \$6.9 m in revenue from the supply of electricity. The provision of water is expected to generate income of \$1.0 m and the tank farm operation \$0.5 m.

As part of the SOE reform program the Government is seeking expressions of interest in the privatisation of the provision of fuel and any financial implications of this will be assessed at the mid-year budget review.

The NUC continue to focus on strengthening and improving essential services to meet the energy and water needs of Nauru. It intends to address infrastructural issues and capacity constraints that often effect corporate performance. The primary objective for the coming year at the Nauru Utilities Corporation is to ensure business growth and that reductions in business losses are achieved through ongoing investment in existing but dilapidated infrastructure. The intention is to ensure Nauruans have access to reliable and sustainable energy and quality water services.

PART 5: Debt Management

In the Budget year just completed, the Government appropriated approximately \$20 million for Debt Repayment and added another \$3.96 million in the Supplementary Budget. By the end of the FY 2013-14 it is anticipated that the government will have reduced the Pending salary debt to below \$5 million.

Nauru's Debt Situation

Nauru's debts are divided into debts owed overseas; debts owed within Nauru to individuals and other organisations outside of government; and inter-entity debts owed between entities within the public sector in Nauru.

Strategies for Reducing Debt

Nauru can only pay its debts by generating budget surpluses. Although the Government plans to generate small surpluses, will continue to take the opportunity afforded by either slow expenditure elsewhere in Government or the effect of the windfall payments from the RPC to explore options for faster debt reduction in order to assist with the task of creating fiscal space in future years. The Government of Nauru will continue to prioritise and organise debt repayments, with a view to further reducing the overall level of debt owed. As in the past two years, a schedule of debt repayments is maintained in 2014-15, showing the timing of repayments and amounts to be repaid to creditors in the new financial year. Provided revenue is received in line with budget estimates, the repayment schedule will be adhered to with creditors being paid accordingly.

PART 6: Finance Sector Reform

During 2013-14 the Government continued detailed negotiations with Bendigo Bank with the objective of establishing a Community Based branch of the Bank on Nauru. These negotiations continue although they are now focussed more on developing an Agency model of operation. It is hoped that the branch will be operating early in the new financial year.

During 2013-14, as part of the overall strategy to deepen the financial system on Nauru, Bendigo Bank personnel made several visits to the island and signed up over 2000 new account holders and issued them with bank access cards. This was part of the strategy associated with the payout of Ronwan payments via EFT to these or other predominantly Australia based accounts. During the year four automatic teller machines (ATMs) were installed and began operating on the Island. While there have been some teething problems mainly to do with maintaining cash supply to the ATMs, it is clear that this facility is important to Nauruans. With further progress of the Bendigo bank agency, the government will be able to consider more actively paying salaries of civil servants and payments for local purchases by EFT. The capacity to make EFT payments of this nature will be part of the additional support to be given to improve the operation of the FMIS in the Ministry of Finance and will have substantial benefits for efficiency and productivity in the Public Service.

PART 7: National Sustainable Development Strategy

The National Sustainable Development Strategy (NSDS) articulates the high-level development goals of the Government of Nauru and outlines the strategies and activities that will be required to achieve those goals. The NSDS remains very relevant and central to Governments development agenda. It also places emphasis on future intentions and required actions that the Government would need to undertake in order to achieve the NSDS objectives.

The NSDS review did not take place during the financial year 2013-14 as originally planned due to the national elections. However it is intended that NSDS will be updated and reviewed fully during the FY2014-15.

One part of the review will be to transform the NSDS into an Operational Development Strategy (ODS), which can translate to a realistic, costed framework for Nauru's sustainable development. The NSDS review in 2014-15 year will be extensive and will especially detail the achievements and progresses made towards the national goals as well as provide a revised version to include practical monitoring and evaluation guides of the NSDS for the way forward.

Social sector:

There has been several key advancements made within the Education sector but there remains a persistent issue of student attendance levels. The development of an attendance / truancy policy from the Education Act is in progress and yet to finalize implementation; Teacher Development and training for ECE teachers is still a key priority in Education. Thus skills capacity from expatriate teachers recruited from Australia/ region for the implementation phases of the QCE in Secondary level is necessary; the new TVET Learning Village is progressing and anticipating to commence classes in 2015; development and implementation of new curriculum across the school levels has been successfully integrated with core subject curriculums in their second year; proactive initiatives

undertaken regarding the training and recruiting of current and new teachers to ensure the quality education delivery and retention of staff in schools.

The Department of Health had undertaken a review in early 2014 which carry on the strengthening of the Health systems; The review main objectives were: the efficiency and effectiveness of health service delivery and the management of the health sector in Nauru; the Ministry of Health and Medical Services Strategic Plan (2010-2015) and associated monitoring and evaluation arrangements; and the quality of support to Nauru and to suggest possible opportunities for improvement. Some of the key recommendations from this review included: strengthening management of NCD, human resource development, and health information management.

Furthermore the Health sector completed a job evaluation exercise, which will help assess the efficiency and effectiveness of the current staff and the adequate supply of drugs and other medical consumables. These were maintained despite the recent fire that destroyed the entire pharmacy centre. The Action Plan for NCD SP 2014-2018 is in place; house inspections and clean up campaigns ongoing including a focus on waste management programs. Child immunization rates were achieved and maintained above 80% due to an ongoing work regarding the Development of FLE in school program in collaboration with DOE and UNFPA.

Other Social sector strategies

- Community sports promoted by Epon Karamen (EK) several sports courts have been refurbished,
- National Community Based Organisation (NCBO) is operating but needs to be further integrated with Government development process;
- Women in development have scheduled initiatives that are drawn from the four UN Women programs in the Pacific
- Youth are continuing bridging education for life skills.

Cross-Cutting sector:

The Chief Secretary Department's Corporate Plan was developed in 2009. However the development of Corporate Plans for other Ministries is yet to be implemented. Notable achievements for the department include

- The Student Internship Program which is showing promising outcomes;
- In-house training workshop with the Civil Service College of Singapore on Public Service Governance & Administration coordinated by HR&L is being undertaken and proving beneficial thus far;
- The review of the government's salary was initiated across the public sector and is currently ongoing with results expected in the 14-15 year;
- Twelve family units and twenty one single units for expatriate staff are now available at the Meneng as a result of the successful Meneng Hotel project

Significant progress has also been made in the environment sector. A national water resource management policy was developed and implemented

- groundwater/brackish was a new initiative from CIE in collaboration with NUC; guidelines for optimal use of groundwater resources developed;

- assessment of water demand during drought periods is completed and the results will assist guide the development of water related policies while international events are utilized to promote water conservation issues;
- improvements to water catchment and infrastructure revamped and maintained (e.g. installation of guttering and downpipes and renovation of existing water tanks);
- the National Solid Waste Management Strategy was finalized and implemented and the Solid Waste Management Strategy Action Plan was updated and the Solid Waste Advisory Taskforce was established;
- hazardous waste management strategy was developed;
- the National Action Plan which was endorsed by Government is an important enabling document for rehabilitating mined areas,
- the rapid biodiversity survey was conducted on Nauru;
- the National Adaptation Program of Action (NAPA) developed; plans underway to construct sea walls in vulnerable areas;
- implementation of the Integrated Island Biodiversity project and the Ridge to Reef Project commenced;

Economic sector:

In the economic sector some of the advancement made includes:

- Finance department has been structurally reorganised into the following divisions, Treasury, Planning and Aid, Revenue and Customs, and Statistics. Customs is now incorporated in Finance and with expert engagement of key Deputy Secretaries in these divisions;
- Finance anticipates the strengthening of broad based revenue systems.
- Furthermore for Treasury and Planning continued strengthening of public finance management is ongoing; for instance introducing Medium Term Budgeting Framework (MTBF) which is an important step to achieve a more effective and strategic management of public finances; significant progress achieved with financial data management and reporting using the FMIS;
- Plans for customs modernization and taxation reforms; finance staff capacity development remain a priority;
- New procurement process through an independent procurement agent is operational but further consolidation of process is envisaged
- Arrangements to establish some banking services on Nauru are well underway; insurance services are being offered by a foreign insurance service provider. Significantly initial progress is being made for the Nauru Trust Fund, for sustainable capital growth that will benefit Nauru over the long term..

Also in Fisheries there has been significant revenue collection and the Parties to Nauru Agreement (PNA) have reinforced their sustainable fisheries management. The fish market facility (funded by Japan GGP) will be completed in 2014 will provide private sector led of small commercial fisheries; also the aquaculture holding facility expected to be operational in 2015 and will re-establish local fish livestock for food security or commercial purposes. Finally in Fisheries; Illegal-unregulated-unreported (IUU) is ongoing and importantly to highlight the fining from an illegal fishing has been recorded.

In brief for other Economic sector activities progress; due to the RPC activities the business investment environment has provided opportunity for micro, small and medium enterprises

(MSME) to flourish, thus Government and Private-Sector Organisation will consolidate from this opportunistic environment for long-term sustainable private sector growth.

Infrastructure sector:

In regard to progress on the Infrastructure sector; it should be noted that the infrastructure sector in Nauru has received considerable support from development partners to an average amount of about \$13-\$14 million per year. Moreover from the National Economic Infrastructure Strategic Investment Plan (NEISIP) review in 2013 it is encouraging to note that 5 out of the 12 priority investments are currently underway, including the supply of navigational aids for the Airport (NZ-MFAT), preparation of an energy roadmap (GIZ/IRENA/SPC), rebuilding of the new hospital and implementation of the Learning Village Project (AusAID). The review also suggests adding one additional priority investment, which is to start preparations and land acquisition for a new landfill for Nauru because the current dumpsite is expected to be full within the next 2-3 years.

Energy sector remains to be a priority area in the infrastructure sector, NUC with developing partners (Australia, EU and ADB) planned for 2014-2017 to commission two new and more efficient power generators to provide more reliable and efficient energy supply. In terms of power distribution – main support from EU under EDF 10th is progressing well.

From 2014 the Government of Nauru has indicated that sustainable economic development of Nauru will be directly supported by the development of Ports, thus GoN has indicated its intention to commence necessary negotiations and processes with developing partners to assist in ports redevelopment project.

Improving essential Infrastructure sector will continue to be Nauru's priority area; the fire at the hospital in 2013 was a setback but the GoN plans to rebuild hospital as soon as possible with developing partners. Water and Sanitation plans are earmarked and managed by the department of CIE, also Waste and Sanitation plans to be coordinate appropriately with NRC and Eigigu sharing roles respectively. Furthermore the increase population tied RPC activities will certainly strain Nauru's infrastructure sector hence key priority activities are closely managed by the GoN.

Part 8 Nauru's Development Partners

Australia

Under the Pacific Partnership for Development (PPD) Government of Australia (GoA) will continue with the Government of Nauru (GoN) for developmental programs in the following five priority areas;

- i) strengthening the public sector management,
- ii) increase private sector growth,
- iii) improving health
- iv) improving education services, and
- v) power, water and infrastructure.

Significantly in the early parts for the financial year 2014-2015, implementation of development activities are appropriated from the preceding bilateral allocation to Nauru's PPD for 2013-14, which was approximately \$8.4 million of programmable funding from a total of \$20.7 million GoA development assistance.

Moreover programmable funds were only delivered in the fourth quarter of FY2013-14, the main reason for this delay of funds for 2013-14 was that the GoA did not want to increase the un-necessary risk of significant amount of unused funds for development programs in the Operational Account, by committing new additional funds.

There were many factors influencing the development programs implementations progress in 2013-14 programs and the development program managers in these priority areas will be practical in 2014-2015 in expending these development funds to gain the essential outcomes for Nauru's sustainable development.

However; there will be opportunity in 2014-15 to work with GoA to proceed and negotiate new funds for new 2014-15 developmental programs. Republic of China, Taiwan

Republic of China (Taiwan)

In the calendar year 2013, the Republic of China (Taiwan) committed an estimated \$9.3 million in direct financial support to GoN, the Republic of China (Taiwan) is the second largest developing partner to Nauru, and ROC-Taiwan generally provides assistance to Nauru in the following areas;

- i) General Budget Support
- ii) Nauru Overseas Missions
- iii) Grass Roots projects
- iii) Loan repayments to ROC banks

In 2013, about 44.4% of Taiwan assistance was directed at helping GoN overcome debt with Exim Bank and ICDF. Moreover, \$150,000 was channelled to support of operations of Nauru's Overseas Missions namely; United Nations, New York Mission and Taiwan, Taipei Mission. An estimated \$4.1 million was directly paid as General Budget Support.

In 2014, RoC-Taiwan will continue to commit the same level of financial support of \$9.3 million to Nauru, whereby similar expenditure programs will be directed at; budget support, Nauru Overseas missions, Grass roots projects and debt repayments. All the aforementioned figures are in US currency.

Russia

The bilateral engagement between the Republic of Nauru and Federated States of Russia will be further strengthen, with Nauru having prioritised the development of ports in 2014 will be seeking further support from Russia. In 2014, Russia has supported Nauru's role in chairing the Alliance of Small Island States (AOSIS) by allocating \$400,000.

Russia will continue to offer educational scholarships for the upcoming academic year in 2015 and there is possibility of provision of essential specialised medical doctors to be engaged in Nauru's health sector.

Japan

The Government of Japan will continue its development assistance to Nauru in the following traditional areas of financial support namely; Non-Project Grant Aid (NPGA) and Grassroots Grant Project Aid (GGP).

In 2013 there were two GGP programs; firstly in the area of private sector growth which will be completed in 2014, a fish market facility at Anibare Boat Harbour. Secondly, in area of environmental climate change sector by providing Water from solar-purifying panels in selected schools, this project will also be completed in 2014. Furthermore in 2014, GGP program will further implement community solar-water pump, which was successfully implemented in earlier GGP programs.

The NPGA program with Government of Japan (GoJ) commenced in 2005, GoN has successfully utilised this annual funding of an estimated AUD\$1 million to procure diesel fuel to ensure power generation intended to provide rapid support to Nauru with economic opportunity. The GoN has to set aside counterpart funds usually equivalent to the value of the grant aid; these funds with consultation with GoJ can be further used for economic development of Nauru.

New Zealand (NZ AID)

Two core areas that New Zealand finances under its development program to Nauru are Justice and Education. New Zealand provides approximately \$1.8 million (\$NZ2.3 million) annually to these sectors.

The Justice Grant Funding Arrangement (GFA) was renewed under the new Nauru Law and Justice Sector Improvement Initiative Phase 2 Program (NLJS) which came into effect on January 2014. This arrangement is providing Nauru Justice Sector at total of \$3.2 million AUD and involves the funding of key in-line Justice positions, vital office equipment, training and development for the sector, and other capacity development programs.

Under the GFA the Government of New Zealand continues to provide assistance to the education sector and this GFA was also renewed earlier in 2013. Continued support in the education sector will ensure Nauruan standards of education are competitive in the region and will form a path to higher educational opportunities overseas. Under the new agreement, funding is directed for the continued implementation and improvement of the Department's administrative duties, providing a safe and conducive learning environment as well as improve system and human resource performance management through the recruitment of a school support team to build the capacity of local teachers.

In addition to the above areas, NZ provided funding for the fisheries sector including training and capacity development, equipment upgrades, and construction of the milk fish aquaculture facility which is near completion.

Asian Development Bank (ADB)

The indicative total provisional ADF resource available for Nauru; in 2014–2017 is approximately \$2.56 million. For 2013–2014, the ADF allocation was \$0.85 million. For 2015–2016, the provisional allocation is \$0.71 million. For 2017-18 and 2019-20 an indicative allocation of \$0.7 million per year is assumed, of which \$0.44 million is brought forward to the COBP period. The final allocation for 2014–2017 will depend on the available commitment authority as well as annual country performance reviews. ADB will also provide technical assistance (TA), at an indicative average of \$0.3 million per annum.

A \$5 million Electricity Supply Security and Stability project, co-financed by the European Union, is planned for 2014 following a recently completed TA project to develop the capacity of the utilities corporation. A second phase of TA for institutional strengthening of the Nauru Utilities Corporation is also planned for 2014.

Furthermore, there are a number of technical assistance and grants planned for; PFM reform (2015-17), strengthening implementation of NSDS (2015) and strengthening of financial inclusion (2016) are highlighted.

ADB is currently discussing a proposal to combine Asian Development Fund (ADF) and Ordinary Capital Resources for lending. Nauru, as an ADF grant-only recipient would continue to receive ADF grants under this proposal. Nauru is likely to be a major winner from this proposal as ADF grant-only countries will receive a minimum allocation of \$3 million per year, a large increase from Nauru's current allocation of approximately \$1 million every two years

European Union (EU)

Continuing from 2014, Nauru is currently accessing up to \$1.7 million under the 10th European Development Fund for the energy sector. EU's assistance focuses mainly on energy efficiency, energy distribution and developing and promoting the use of renewable energy technologies.

Support to NUC is therefore the largest activity under the current EDF 10. A major component of this funding will be given to improving Nauru's power distribution grid through the recruitment of a long term and short-term technical assistance to assess the power distribution system and to procure spare parts to upgrade the system.

Indicative programming for EDF 11th has commenced with similar envelope available to Nauru for Energy sector; Nauru has planned to procure under EDF 11th, an efficient power generator to replace in-efficient and 'high-repair' current power generators. Furthermore it is envisaged with strengthen of public finance systems in Nauru that EU will be considering flexible direct budget support to the GoN, this work is in early stages.

United Nations (UN) Agencies, Funds and Programmes

The various United Nations Agencies, Funds and Programmes continue to provide development assistance to Nauru, including in through regional programmes and in partnership and coordination with other development partners.

UN Joint Presence Office

Since 2010 there is UN Joint Presence Office in Nauru. The role of the office is to lead in-country facilitation and coordination of the work of UNICEF, UNFPA, UNDP and UNWOMEN, in addition to other broader UN coordination. By second half of 2014 a Nauru national will take over managing the office, from the current international staff.

UNFPA – United Nations Populations Fund

The Biennium Work Plan 2014-2015 was confirmed by MHMS in early 2014. It streamlined all resources through the MHMS, whilst other Ministries also implement the work. The support to MHMS implemented work is closely coordinated with UNICEF and WHO. The overall budget for the two years is USD 566.828

UNICEF – United Nations Children's Fund

The draft Work Plan for 2014-2015 has been discussed with government counterparts, MHMS and MoHA, and presented in late May to DFAT to facilitate formal confirmation. It proposes continuing its work with MHMS (in close coordination with UNFPA and

WHO) and starting a work with the newly established Family and Community Services Division of MoHA. The funding is in 2014 USD119,900 and in 2015 USD55,000. The work is in two main areas:

- Pregnant women, mothers and children equitably benefit from improvement of neonatal, child and maternal survival, health and nutrition; and
- Child Protection situation analysis and related CRC reporting requirements completed. Also a Child Protection situation analysis report launched.

UN Women – United Nations Entity for Gender Equity and Women Empowerment

At present, UN Women's main contribution in Nauru is by hosting the UN Joint Presence Office. In April 2014 UN Women opened up a dialogue with Nauru through DFAT by sharing the organization's regional programming approach for the next 4 years and to ascertain the regional programme initiatives that would be of greatest interest to the government, and most relevant to the Nauruan context. The proposed initiatives are drawn from the four UN Women programs in the Pacific:

- Advancing Gender Justice in the Pacific (AGJP),
- From Policy to Action: Ending Violence against Women and Girls in the Pacific” (EVAW)
- Women's Economic Empowerment (WEE)
- Increasing Community Resilience through the Advancement of Women to address Climate Change and Natural Hazards (IREACH).

UNDP – United Nations Development Program

Support from UNDP is in numerous areas, and includes various partnerships.

The Second National Communication reporting managed by DCIE is in its final steps. The remaining funding for second half of 2014 is AUD15,000.

The Hon. Speaker of Parliament confirmed the Parliament Support Project in May. It was created in partnership of Nauru Parliament, Victoria Parliament and UNDP. The purpose of it is to contribute to strengthened oversight capacity in Parliament and strengthened capacity in the Parliament Secretariat. It is a one-year initiative, with total budget from UNDP of USD 75,800, in addition to substantial in-kind contribution from Victoria Parliament.

A comprehensive biodiversity programme, “Ridge to Reef”, is in its final months of preparations. The programme includes conservation of biodiversity, sustainable land and water management, strengthening of governance and institutions as well as knowledge management. The programme is to be implemented over 4 years. The total costs will be USD 6 million with indicative financing including a GEF funding of 3 million, and Australian DFAT USD 1.2, in addition to in-kind contribution from EU, UNDP as well as DCIE.

Technical assistance is given in other areas, including on the implementation of Nauru's household energy survey. This is in partnership with SPC and the Government of Nauru. Technical assistance is also provided on the EU funded climate change and migration project that UNESCAP is leading on.

UNEP – United Nations Environmental Program

The general objective of the “Island Biodiversity Programme of Work” is to contribute to the implementation of the Convention of Biological Diversity’s Island Biodiversity Programme of work by supporting an integrated ecosystem approach to biodiversity conservation management at local level. Funding from GEF Trust Fund is USD 350,000, and in-kind funding from NRC is USD 631.030. The project duration is 1 March 2012 until 28 February 2015.

UNESCO – United Nations Educational, Scientific and Cultural Organisation

The Nauru National Commission for UNESCO receives support from UNESCO. This includes funding of USD17.000 in 2014. The support includes Education for All reporting, as well as Mother Language Day Celebrations.

UN ESCAP – Economic and Social Commission for Asia and the Pacific.

ESCAP facilitates the Pacific Climate Change Migration Project, the long name is: Strengthening the Capacity of Pacific Island Countries to Manage the Impact of Climate Change to Migration. The initiative has a regional aspect and national implementation in Tuvalu, Kiribati and Nauru.

In Nauru, there are 4 main national actions: (1) improve data and analysis of labour migration; (2) Gain an understanding of the attitudes of communities and individuals on migration, through community consultations and a survey; (3) Develop and begin implementation of evidenced-based national strategies on climate change induced migration and relocation and (4) Enhance national capacity to effectively participate in regional, bilateral and global schemes on migration.

This initiative from June 2013 to June 2016 and the total value is USD 3.1million. This includes both the contribution from the EU and in-kind contributions from ESCAP, ILO and UNDP. The project activities in Nauru make up about USD 0.6million - however, this value also includes a portion of the salaries of the staff working at the regional level.

Other Donors

There are a number of other development partners who continue to assist Nauru on its path towards sustainable development. Assistance rendered by these development partners comes in a vast array of assistance, from provision of technical and financial assistance, capacity building or aid in-kind.

The Council of Regional Organisation of the Pacific (CROP) agencies have also made significant impacts in offering their expertise in managing regional projects that Nauru has and will be involved in and building capacity through the provision of workshops and trainings in country or in other Pacific Island countries. The CROP agencies also provide technical assistance at the request of recipient countries including Nauru in key sectors including agriculture, water, energy, law and justice, education, health and environment.

Nauru has recently engaged with a number of new partner countries such as Turkey, Azerbaijan, Israel, Italy, Germany and the United Arab of Emirates (UAE). The GoN aspires to continue to strengthen its relations with its existing development partners and to build new links to other non-traditional development partners.