



REPUBLIC OF NAURU

DEPARTMENT OF FINANCE

MEDIUM TERM DEBT STRATEGY  
2023-28

Release date: November 21, 2022  
Cabinet Resolution Reference: 090/2022

Treasury Division  
Department of Finance

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# 2023-28 MEDIUM-TERM DEBT STRATEGY

## INTRODUCTION

This document outlines the Government of Nauru's Medium-Term Debt Strategy for the period 2023-28 continuing on from the Medium-Term Debt Strategy for the Fiscal Year 2022-23 in line with the Government's 2022-23 Fiscal Strategy. It is based on all available information to Treasury as at 31 May 2022.

## MACROECONOMIC AND FISCAL OUTLOOK

With the international economy entering a pronounced slowdown amid threats from COVID-19 variants and a rise in inflation and debt, small economies like Nauru have performed well with continued support from bilateral partners and donor funding. Nauru has been very fortunate to have avoided any COVID-19 cases until very recently, and to be insulated from the down-turn in tourism and trade that has affected many of its neighbours. The key economic indicators in the 2022-23 Budget as shown in Table 1 have been used in formulating the 2022-23 Medium Term Debt Strategy.

**Table 1: Key Economic Indicators**

Item	2019-20	2020-21	2021-22	2022-23
Real GDP Growth (per cent change)	0.7	1.6	0.9	2.6
Nominal GDP (\$A million)	171	179	184.5	189.6
Consumer prices (period average, per cent change)	0.9	1.2	1.4	1.7

(Source: IMF World Economic Outlook April 2022)

The International Monetary Fund (IMF) has acknowledged Nauru's success in deploying containment efforts rapidly and comprehensively to until June 2022. Nauru's medium-term outlook is highly uncertain, given its dependency on the future of the Regional Processing Centre (RPC). Current agreements between Nauru and Australia are short term, and the possibility of extension beyond June 2022 will be through enduring capability arrangements. The risks posed by the rapid spread of the Omicron variant indicates that the pandemic will likely continue to disrupt economic activity in the medium term.

The 2022-23 Budget Aggregate Estimates as shown in Table 2 have been used in formulating the 2022-23 Medium-Term Debt Strategy.

**Table 2: 2022-23 Budget Aggregate Estimates**

Description	2020-21		2021-22	2021-22	2021-22 YTD	2021-22	2022-23	
	Preliminary	Actual	Approved Budget	2021-22 Supp Bills	Revised Budget	Actual & Commitment	Projected Actual	Approved Budget
	\$	\$	\$	\$	\$	\$	\$	\$
Revenue	271,469,525	244,123,361	244,123,361	94,150,942	338,274,303	282,314,559	322,645,213	233,504,185
Expenditure	279,843,596	244,023,361	244,023,361	93,954,487	337,977,848	235,122,536	264,329,223	232,954,731
Balance	-	8,374,071	100,000	196,455	296,455	47,192,023	58,315,990	549,454

## GOVERNMENT LOANS AND PUBLIC DEBT LEVELS

The following provides details of the loans contracted by the Republic of Nauru and their status in terms of debt outstanding and loans to be disbursed.

### RONPHOS

The Republic of Nauru acting by and through its Ministry/Department of Finance (the “Borrower”) signed a loan agreement on 16 October 2018 with the Export-Import Bank (EXIM) of the Republic of China (Taiwan). The US\$5 million aggregate principal amount has been used to support the Republic of Nauru Phosphate Corporation (RONPHOS) in its purchase of mining equipment for extraction of secondary phosphate. While the loan is for RONPHOS, with a subsidiary loan agreement between the Republic of Nauru and RONPHOS dated 14 November 2018, the primary loan is in the name of Republic of Nauru and therefore is classified as central government public debt and recorded in the public debt register (in accordance the international debt classifications).

The primary and subsidiary loans have the same terms and conditions. The primary loan is recorded as central government debt. The subsidiary loan agreement is an SOE loan (between RONPHOS and the Republic of Nauru) and therefore recorded as a financial asset. For the period to 31 December 2022, the loan will be serviced by the Republic of China (Taiwan) under the annual grant. From a recording and accounting perspective, all inter-related transactions under the primary and subsidiary loans will be recorded and funded from the Republic of China (Taiwan). Beyond 2022, the loan and subsidiary loan will be subject to further negotiation with the Republic of China (Taiwan).

### NAURU AIRLINES

The Republic of Nauru acting by and through its Department of Finance (the “Borrower”) signed a loan agreement on 28 December 2021 with the Export-Import Bank (EXIM) of the Republic of China (Taiwan). This will provide a facility in the maximum aggregate amount of US\$24.95 million to Support the Nauru Airline Aircraft Fleet improvement program.

The Republic of Nauru will firstly enter a loan agreement for US\$13.46 million for the purchase of the first replacement aircraft and to enter a separate loan agreement for \$11.49 million for the purchase of the second Replacement Aircraft when it is identified in the future.

Under the loan agreement, there is a promissory note for a maximum of US\$24.95 million from EXIM to Republic of Nauru through the Department of Finance (the Borrower), which is required to meet all loan payments. There is no subsidiary loan agreement. Both Nauru Leasing Corporation and Nauru Air Corporation will mortgage the aircraft thereby providing a guarantee or collateral against the loan. This means the aircraft will be registered in the name of EXIM.

The date for the drawdown of the first tranche of US\$13.346 million was on 16 May 2022. The primary loan will be recorded as central government debt (in accordance the international debt classifications). For the period to 31 December 2022, the loan will be serviced by Republic of China (Taiwan) under the annual grant. From a recording and accounting perspective, all inter-related transactions under the primary loan will be recorded and funded from the Republic of China (Taiwan) annual grant. Beyond 2022, the loan will be subject to further negotiation with Republic of China (Taiwan).

## PUBLIC DEBT LEVELS

Prior to 2021, Nauru was assessed at being at high risk of debt distress due to significant external legacy bond obligations, and significant domestic liabilities related to the Bank of Nauru Liquidation. Implementation of the Debt Action Plan has utilised windfall Government revenues to resolve all external legacy debts and progress resolution of the Bank of Nauru liquidation, as well as addressing SOE payment arrears. The total Government debt stock (gross debt) estimated as at 30 June 2022 is set out in Table 3. The net debt estimated after including financial assets (i.e. cash and deposits, Nauru Trust Fund investment, lending to SOEs, and equity in Nauru Airlines Corporation) as at 30 June 2022 is set out in Table 4.

<b>Australian Dollar (A\$'000)</b>	<b>2019-20 Actual</b>	<b>2020-21 Actual</b>	<b>2021-22 Estimate</b>
<b>Total External and Internal</b>	<b>183,536.5</b>	<b>49,653.9</b>	<b>59,742.0</b>
<b>As a share of GDP</b>	<b>107%</b>	<b>28%</b>	<b>32%</b>
<b>External</b>	<b>131,226.9</b>	<b>8,594.4</b>	<b>25,515.9</b>
<b>As a share of GDP</b>	<b>77%</b>	<b>5%</b>	<b>14%</b>
Government External Debt	128,296.6	5,664.1	24,015.9
Informal Liabilities (Payment Arrears)	2,930.3	2,930.3	1,500.0
<b>Internal</b>	<b>52,309.6</b>	<b>41,059.5</b>	<b>34,226.2</b>
<b>As a share of GDP</b>	<b>31%</b>	<b>23%</b>	<b>19%</b>
Bank of Nauru Liquidation Creditors	51,950.9	41,059.5	34,226.2
Informal Liabilities (Payment Arrears)	358.7	-	-
Notes:			
1. Table reflects unaudited results and may change			
2. Numbers as at 30/06/2022 reflect an estimate and may change			
3. This table could be extended by adding past and future years			

The net debt shows that the financial assets are significantly higher than GON debt to the extent that the estimated net debt as at 30 June 2022 is AUD 291.6 million, equivalent to 122 percent of GDP.

<b>Australian Dollar (A\$'000)</b>	<b>2020-21 Actual</b>	<b>2021-22 Estimate</b>
<b>Liabilities in net debt</b>		
Bonds	-	-
Loans	5,664.1	24,015.9
Other liabilities (BON & arrears)	43,989.8	35,726.2
<b>Total Liabilities in net debt</b>	<b>49,653.9</b>	<b>59,742.0</b>
<b>Assets included in net debt</b>		
Cash and deposits	102,215.3	150,490.2
Investments (NTF)	166,608.0	195,236.0
Lending to SOEs	6,364.1	5,656.1
NAC equity (EXIM)	-	19,059.8
<b>Total Assets included in net debt</b>	<b>275,187.4</b>	<b>351,382.3</b>
<b>Net Debt</b>	<b>(225,533.5)</b>	<b>(291,640.3)</b>
<b>As a share of GDP</b>	<b>126%</b>	<b>122%</b>

In the recent 2021 IMF Article IV mission report, it was assessed that debt is sustainable under current policies, which is a significant improvement from the 2019 Debt Sustainability Analysis when debt was assessed as unsustainable. Two key factors contributed to this improvement: firstly, the

settlement in March 2021 of the long-defaulted external debt (yen bonds); and secondly, reductions in domestic debt inherited from the liquidated Bank of Nauru. A continuation of sound fiscal and public debt policies, which is expected in the baseline, will help maintain public debt sustainability.

To maintain debt sustainability, the IMF indicated that continued sound fiscal and public debt management policies are needed, as well as policies to generate and diversify economic activity. Importantly, the IMF noted that the Government of Nauru (GON) was transparently reporting details of domestic and external debt which began in the 2021-22 budget. It was further noted that the GON was working towards strengthening debt management and monitoring arrangements, including management of fiscal risks, with assistance from the ADB.

The GON agreed with the IMF's analysis and assessment that Nauru's debt is sustainable. The GON through the Department of Finance (DOF) emphasised the commitment to responsible debt management and noted the actions that were being taken toward reining in debt levels since Fiscal Year 2020, including resolving the long-standing external debt to Firebird in March 2021, the ongoing Bank of Nauru (BON) liquidation payments to individuals and the Nauru Phosphate Royalties Trust (NPRT), and resolving accounts payable arrears for Eigigu Holdings. The DOF stressed that repayment and servicing of the planned EXIM loan to upgrade the Nauru Airlines fleet would be met by committed budget support from Republic of China Taiwan.

## DEBT ACTION PLAN

The resolution of BON debts is progressing with assistance from the Australian-based business advisory firm, Cor Cordis. The government continues to make ongoing payments when budget funds permit. There have been 37 payment batches to BON claimants totalling \$2.595 million up to March 2022. The current position as at the beginning of May 2022 showing the account status is set out in Table 5.

**Table 5: Account Status of Bank of Nauru Claimants**

<b>Account Status</b>	<b>Scenario 5.3 Balance \$</b>	<b>Treasury 7 May 2021 Balance</b>	<b>Calculated Balance \$</b>	<b>Net Variance \$</b>	<b>No.</b>
Closed Accounts <sup>#</sup>	10,431,775	(5,230)	(5,191)	(39)	7,732
Active Accounts	26,162,064	20,980,739	21,127,048	(146,309)	2,935
T.B.A. Closed / Active <sup>*</sup>	631,033	16,155	(161,157)	177,312	100
<b>Total private sector accounts</b>	<b>37,224,873</b>	<b>20,991,665</b>	<b>20,960,700</b>	<b>30,965</b>	<b>10,767</b>

<sup>#</sup> Includes +/- \$10 variance (Now Closed) - Net Variance total \$38.55

<sup>\*</sup> Zero treasury balance does not reconcile to calculated balance.

<sup>\*\*</sup> 505 accounts fully paid in the \$0 -\$100 range totalling \$22,939 were removed from BON Master

The revised budget for BON repayments in Fiscal Year 2021-22 is \$5.85 million. For Fiscal Year 2022-23, it is estimated that the BON repayment will amount to \$1 million which will depend on the GON fiscal and liquidity position. The GON plans to make available funding to NPRT with a 5 percent Ronwan capital re-distribution from balances available from the BON liquidation.

## COSTS AND RISKS OF PUBLIC DEBT

### COST-RISK MATRIX

An important component of the Medium-Term Debt Strategy is to assess the costs and risks of the public debt portfolio. The cost-risk matrix in Table 6 sets out the risk indicators for the GON debt portfolio for the estimate of debt outstanding as at 30 June 2022 and therefore, does not include the second tranche of the Nauru Airlines loan.

**Table 6: GON Debt Risk Indicators**

<b>Risk Indicators (for year ending 30 June 2022)</b>		<b>External Debt</b>
Total Public Debt (in million AUD)		24.016
Nominal Public Debt as % of GDP		13%
PV of Public Debt as % of GDP		12%
Interest Payment as % of Government Revenue		0.06%
Cost of Debt	Interest Payment as % GDP	0.08%
	Weighted Average Interest Rate (%)	2.66%
Refinancing Risk	Average Time to Maturity (ATM) in years	5.63
	Debt Maturing within 1-year (% total debt)	4%
Interest Rate Risk	Average Time to Refixing (ATR) in years	0.39
	Debt Refixing within 1-year (% total debt)	100
	Fixed Rate Debt (% of total debt)	0
FX Risk	Foreign Currency Debt (% total debt)	100

### EXCHANGE RATE RISK

The GON has significant exchange rate risk as 100 percent of the external debt portfolio is denominated in US dollars, whereas the Government's budget and reporting currency is Australian dollars. For example, if the US dollar appreciates against the Australian dollar, the cost of servicing external debt will increase. However, this risk is mitigated by the Republic of China Taiwan budget support grant that is used to meet the debt service principal and interest obligations of the GON.

### INTEREST RATE RISK

The GON has significant interest rate risk as 100 percent of the debt portfolio has the interest payment set by a spread to the 6-month floating US dollar interest rate. Interest rates have begun to increase in 2022 as the US Federal Reserve began raising the Fed Funds rate in March and is expected to raise the rate further over the next two years, possibly by more than 2 percent. The impact has begun to take effect immediately as the 6-month LIBOR rate has risen from 0.34 percent at the beginning of January to 2.07 percent as at 20 May 2022. The impact of the rise in 6-month LIBOR on the projected interest cost in Fiscal Years 2022-23 and beyond can be seen in Table 7. As with the exchange rate risk, interest rate risk is mitigated by the Republic of China Taiwan budget support grant that is used to meet the debt service interest payment obligations of the GON.

Table 7: Total Government External Debt Service

Instrument	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28
	Projected						
<b>Original Currency</b>							
Samurai Bond Series B (JPY millions)	-	-	-	-	-	-	-
Principal Payments	-	-	-	-	-	-	-
Interest Payments	-	-	-	-	-	-	-
Samurai Bond Series C (JPY millions)	-	-	-	-	-	-	-
Principal Payments	-	-	-	-	-	-	-
Interest Payments	-	-	-	-	-	-	-
EXIM Bank China Ronphos (US\$'000)	569.3	592.2	603.9	586.1	567.7	549.7	531.6
Principal Payments	500.0	500.0	500.0	500.0	500.0	500.0	500.0
Interest Payments	69.3	92.2	103.9	86.1	67.7	49.7	31.6
EXIM Bank China - Aircraft TR#1 (US\$'000)	-	1,504.6	1,473.0	1,439.5	1,406.9	1,374.3	1,342.3
Principal Payments	-	1,121.7	1,121.7	1,121.7	1,121.7	1,121.7	1,121.7
Interest Payments	-	383.0	351.3	317.8	285.2	252.6	220.6
EXIM Bank China - Aircraft TR#2 (US\$'000)	-	644.3	1,271.4	1,242.7	1,214.9	1,187.1	1,159.8
Principal Payments	-	478.8	957.5	957.5	957.5	957.5	957.5
Interest Payments	-	165.5	313.9	285.2	257.4	229.6	202.3
<b>Australian Dollar (A\$'000)</b>							
Samurai Bond Series B	-	-	-	-	-	-	-
Principal Payments	-	-	-	-	-	-	-
Interest Payments	-	-	-	-	-	-	-
Samurai Bond Series C	-	-	-	-	-	-	-
Principal Payments	-	-	-	-	-	-	-
Interest Payments	-	-	-	-	-	-	-
EXIM Bank China - Ronphos	806.2	838.5	855	830	804	778	753
Principal Payments	708.0	708.0	708.0	708.0	708.0	708.0	708.0
Interest Payments	98.2	130.5	147.1	121.9	95.9	70.3	44.7
EXIM Bank China - Aircraft TR#1	-	2,130.6	2,086	2,038	1,992	1,946	1,901
Principal Payments	-	1,588.3	1,588.3	1,588.3	1,588.3	1,588.3	1,588.3
Interest Payments	-	542.3	497.5	450.0	403.9	357.7	312.4
EXIM Bank China - Aircraft TR#2	-	912.3	1,800.3	1,759.7	1,720.3	1,680.9	1,642.3
Principal Payments	-	677.9	1,355.8	1,355.8	1,355.8	1,355.8	1,355.8
Interest Payments	-	234.4	444.4	403.9	364.5	325.1	286.4
<b>Total:</b>	<b>806.2</b>	<b>3,881.5</b>	<b>4,741.2</b>	<b>4,627.9</b>	<b>4,516.4</b>	<b>4,405.3</b>	<b>4,295.8</b>
Principal Payments	708.0	2,974.3	3,652.2	3,652.2	3,652.2	3,652.2	3,652.2
Interest Payments	98.2	907.2	1,089.0	975.8	864.3	753.1	643.6

## LIQUIDITY RISK AND CASH BUFFER

The GON continued to build up cash balances over the third quarter of Fiscal Year 2021-22. At the end of the quarter, total funds were \$150.5 million as set out in Table 8. The cash buffer requirement of two months of adjusted expenditure was \$40.6 million. Total funds were significantly in excess of the recommended fiscal cash buffer, with \$40.1 million quarantined in separate cash buffer accounts.

Table 8: Government of Nauru Liquidity and Fiscal Cash Buffer Requirements

	TOTAL FUNDS (\$)		
	Requirement (\$)	As at 1 July 2021	As at 31 Mar 2022
Cash Buffer at 1 July 2021	37,743,821	102,215,345	
Cash Buffer 31 Mar 2022	40,587,770		150,490,229
<i>of which held in cash buffer accounts</i>		40,070,267	40,098,922

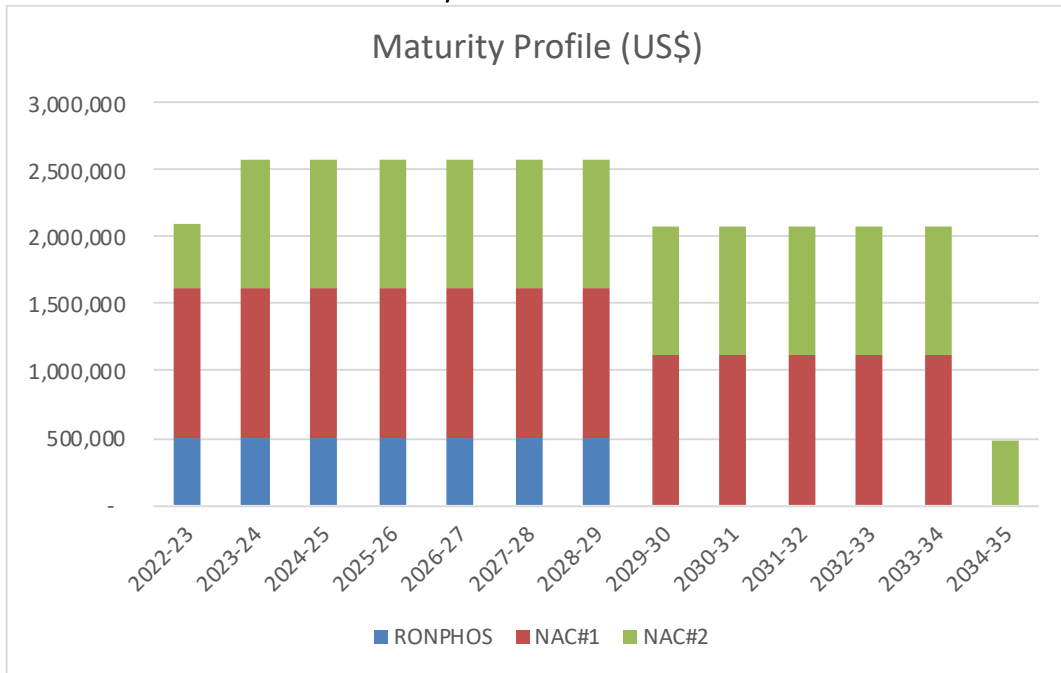
To mitigate liquidity risk, the GON will maintain a fiscal cash buffer with the strategy of continuing to build up the cash buffers up to the equivalent of two months adjusted expenditure, to ensure that Government has sufficient cash on hand to meet its bills as and when they fall due.



**ROLLOVER/REFINANCING RISK (MATURITY PROFILE)**

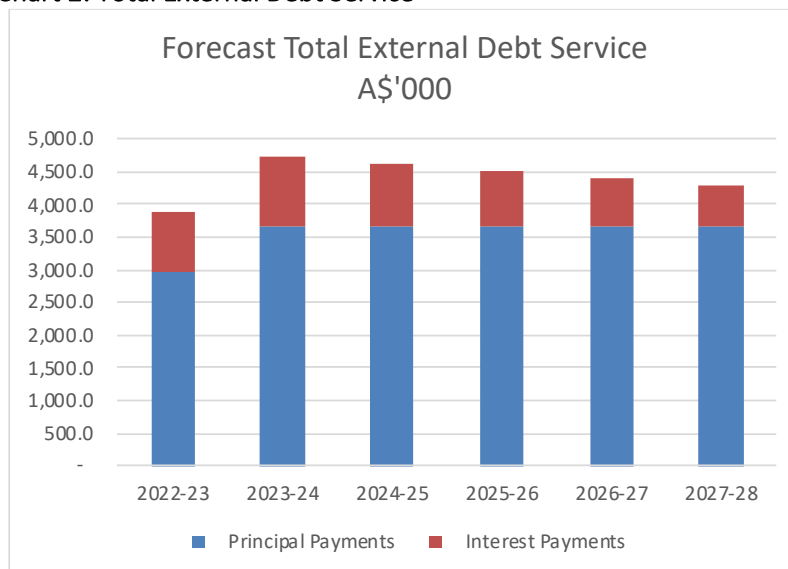
The GON has a low rollover or refinancing risk as the average time to maturity (ATM) of the debt portfolio is 5.6 years and with only 4 percent of the debt maturing in 1-year. Moreover, the debt portfolio has a smooth maturity profile as shown in Chart 1. It should be noted that the maximum payment due in any Fiscal Year is US\$2.6 million (A\$3.7 million).

**Chart 1: Government Debt Maturity Profile**



The graph of the total annual external debt service (principal and interest) out to Fiscal Year 2027-28 as set out in Table 7 is shown in Chart 2.

**Chart 2: Total External Debt Service**



## DEBT SUSTAINABILITY

As is stated on Budget Paper No.1, while the Nauru external debt level is still considered moderate to high, it is sustainable. The two key factors that contribute to this improvement are the settlement of the Firebird debt and some repayment of domestic debt related to the liquidation of the Bank of Nauru. This assessment is also confirmed by the IMF in the 2021 Article IV mission report.

The projected level of government external debt for the Fiscal Years 2021-22 to 2027-28 by loan in both original currency and Australian dollars is shown in Table 9. The debt as a share of GDP increases to around 20 percent in Fiscal Year 2022-23 when the second tranche of the Taiwan EXIM Bank loan is drawdown but falls back to 15 percent in Fiscal Year 2024-25. This and for subsequent fiscal years, the benchmark external debt to GDP of less than 15 percent will be met.

**Table 9: Total Government External Debt Outstanding**

Instrument	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28
	Projected						
<b>Original Currency</b>							
Samurai Bond Series B (JPY millions)	-	-	-	-			
Samurai Bond Series C (JPY millions)	-	-	-	-			
EXIM Bank China - Ronphos (US\$'000)	3,500	3,000	2,500	2,000	1,500	1,000	500
EXIM Bank China - Aircraft TR#1(US\$'000)	13,460	12,338	11,217	10,095	8,973	7,852	6,730
EXIM Bank China - Aircraft TR#2(US\$'000)	-	11,011	10,054	9,096	8,139	7,181	6,224
<b>Australian Dollar (A\$'000)</b>							
Samurai Bond Series B	-	-	-	-	-	-	-
Samurai Bond Series C	-	-	-	-	-	-	-
EXIM Bank China - Ronphos	4,956.1	4,248.1	3,540.1	2,832.1	2,124.0	1,416.0	708.0
EXIM Bank China - Aircraft TR#1	19,059.8	17,471.4	15,883.1	14,294.8	12,706.5	11,118.2	9,529.9
EXIM Bank China - Aircraft TR#2	-	15,592.3	14,236.4	12,880.6	11,524.7	10,168.9	8,813.0
<b>Total:</b>	<b>24,015.9</b>	<b>37,311.8</b>	<b>33,659.6</b>	<b>30,007.4</b>	<b>26,355.3</b>	<b>22,703.1</b>	<b>19,050.9</b>
<b>As a share of GDP</b>	<b>13%</b>	<b>20%</b>	<b>17%</b>	<b>15%</b>	<b>13%</b>	<b>12%</b>	<b>10%</b>

The debt sustainability indicators as at the end of the Fiscal Year 2021-22 and projected out to Fiscal Year 2027-28 are set out in Table 10.

**Table 10: Debt Sustainability Indicators**

	2021	2022	2023	2024	2025	2026	2027	2028
GDP	0.179	0.185	0.19	0.194	0.197	0.092		
(A\$'000)	179,000	185,000	190,000	194,000	197,000	200,000	203,000	206,000
External Debt	5,664.1	24,015.9	37,311.8	33,659.6	30,007.4	26,355.3	22,703.1	19,050.9
Exports	23,700.0	24,587.0	25,600.0					
Government Revenue	338,274.3	322,684.2	253,329.4	253,300.0	256,600.0	225,300.0	219,700.0	207,500.0
Government Expenditure	337,977.8	305,028.7	252,780.0	252,800.0	255,000.0	224,500.0	219,300.0	207,100.0
External Debt Service	4,898.4	806.2	3,881.5	4,741.2	4,627.9	4,516.4	4,405.3	4,295.8
PV External Debt	5,664.1	21,896.1	33,268.8					
Nominal External Debt-to-GDP	3.16%	12.98%	19.64%	17.35%	15.23%	13.18%	11.18%	9.25%
PV External Debt-to-GDP	3.16%	11.84%	17.51%					
PV of External Debt-to-Exports	23.90%	92.39%	129.96%					
PV of External Debt-to-Revenue	1.67%	6.79%	13.13%					
External Debt Service-to-Exports	20.67%	3.40%	16.38%	18.52%	18.08%	17.64%	17.21%	16.78%
External Debt Service-to-Revenue	1.45%	0.25%	1.53%	1.87%	1.83%	1.78%	1.74%	1.70%

As shown in Tables 9 and 10, external debt to GDP is projected to fall to below 15 percent in Fiscal Year 2025-26 and continue to fall below 10 percent by Fiscal Year 2027-28 (on the assumption of no new borrowing). This level is well below the internationally accepted threshold of 30 percent. Table 11 sets out the current debt sustainability ratios for Nauru as compared to the internationally accepted thresholds assuming that Nauru would be assessed as “weak” under the World Bank Country Policy Institutional Assessment (CPIA) methodology. It is important to note that Nauru is well below in three of the thresholds, but just below the PV of Debt-to-Exports threshold which will fall as

the three loans are repaid. The External Debt Service-to-Exports ratio is significantly above the threshold of 10 percent and will continue to be above the threshold for the entire period of the MTDS unless there is an increase in exports.

**Table 11: Debt Sustainability Indicator Thresholds**

<b>Nauru</b>	<b>2022</b>	<b>2023</b>	<b>Threshold</b>
PV of Debt-to-GDP	13.0%	19.6%	30%
PV of Debt-to-Exports	92.4%	130.0%	140%
Debt Service-to-Revenue	0.3%	1.5%	14%
Debt Service-to-Exports	3.4%	16.4%	10%
PV of Total Public Debt-to GDP	13.0%	19.6%	35%

## SOEs, GOVERNMENT GUARANTEES AND FISCAL RISKS

The performance of State-owned enterprises (SOEs) is a key fiscal risk for the 2022-23 budget, including the need to fund ongoing operations and capital investment. Several of the SOEs are years behind in preparing financial statements, and any data that may be available to undertake an assessment of performance, which are often based upon internal management reports, has not been audited. Some data can be years out-of-date and therefore considered to have a low level of reliability.

The focus of efforts by DOF to review the performance of SOEs has been on governance improvement rather than debt issues. The 2022-23 Budget Strategy and Outlook (Paper No.1) sets out the measures to strengthen SOE governance as well as the responsibilities of the Public Enterprise Monitoring Unit (PEMU) to monitor the performance of SOEs. Other than the loans from RONPHOS to GON, there are no recorded loans across the other SOEs.

### GOVERNMENT LOAN GUARANTEES

Nil

### FISCAL RISKS

The 2022-23 Budget Strategy and Outlook (Paper No.1) sets out the fiscal risks which are tilted significantly towards the downside. The key fiscal risks for Nauru relate to the Port Projects, fuel price increases, the uncertainty around the future of the RPC beyond December 2022, and the impact of COVID-19. While there are no fiscal risks directly arising from public debt due to the back-to-back grant funding from Taiwan, there is the risk that the interest cost on the loans outstanding will rise given recent increase in the Federal Reserve rate which is expected to continue to increase during the rest of 2022 and into 2023. If the grant is not increased to compensate, the annual grant will not change in AUD and there will be less grant funds available for other programs.

The 6-month USD LIBOR rate used in the MTDS 2022-23 and MTDS 2023-28 to calculate future interest costs is 2.06557 percent (which was the rate as at 20 May 2022). The rate has continued to increase and is currently 2.82657 percent. This adds a further \$350,000 to the annual debt interest cost. If the 6-month LIBOR interest rate was to rise by a further 2 percent, the interest payments would increase by around \$800,000 in Fiscal Years 2023-24 to 2027-28.

## DEBT STRATEGY FOR 2023-28

The Medium-Term Debt Strategy 2023-28 has been prepared in accordance with the Financial Instructions (Liabilities) approved by Cabinet in June 2021. The overall objective is to ensure that the financing needs of the GON for the medium term are met on a timely basis, with borrowing costs as low as possible and consistent with a prudent degree of risk.

The risks inherent in the GON debt portfolio have been identified (i.e. exchange rate, interest rate, liquidity, and refinancing or rollover risks) and measured as set out in the cost-risk matrix in Table 6. The mitigation strategy for each risk is outlined.

Consistent with Nauru's Medium-Term Fiscal Strategy to achieve macro-economic stability and inclusive economic growth with a commitment to fiscal responsibility, the GON's Medium -Term Debt Strategy is to target a 'low risk' IMF debt sustainability rating through:

1. Responsible fiscal policy settings with three fiscal responsibility ratios:
  - Budget balance must be positive as a share of GDP – that is, the budget must be in surplus
  - Personnel as a proportion of current expenditure must be below 30 percent
  - Fiscal cash buffer of three months adjusted non-RPC expenditure
2. No new public debt arrangements for the foreseeable future with the aim to maintain the debt to GDP ratio at sustainable levels over the medium term, i.e. benchmark external debt to GDP of less than 15 percent
  - if new debt is to be considered, it must be concessional – either a minimum 35 percent grant element, or supported by back-to-back grant funding that meet all principal and interest payments
3. Maintenance of the debt sustainability indicator ratios below the thresholds of:
  - PV of Debt-to-GDP: 30 percent
  - PV of Debt-to-Exports: 140 percent
  - Debt Service-to-Revenue: 14 percent
  - Debt Service-to-Exports: 10 percent
  - PV of Total Public Debt-to-GDP: 35 percent
4. Continued resolution of legacy domestic debt and liabilities where fiscal conditions allow
5. Maintenance of a liquidity cash buffer equivalent to a minimum of two months adjusted expenditure

The Debt Strategy is based on the assumption that the servicing of the EXIM RONPHOS and Nauru Airlines loans will be met by committed budget support from Republic of China (Taiwan) beyond the current agreement period to 31 December 2022, with the exception of the debt sustainability indicators which have been calculated without this support.