

Nauru: An Experiment

By Hannah Thomas

Nauru is an island country of less than 10,000 people, and with a landmass of a mere twenty-one square kilometers, tucked off the shore of Sydney, Australia. In October 2014, the nation found itself featured in *The Economist* for its imminent descent into bankruptcy.¹ In many ways Nauru can be used as a case study to understand the insufficiencies of democracy, if democracy is merely defined by elections and representation. Despite Nauru's democratic governance structure, which includes a unicameral parliament, elected representatives, and recognition of civil liberties, the country still faces multifaceted instability. Its democratic institutions fall short of helping to protect liberty and property as seen in Nauru's impending bankruptcy. Moreover, the entire country is an interesting case because unlike most failed democracies that can attribute failure to political, ethnic, or social violence, Nauru has none of these conflicts but is still at high risk of being a failed state. It is a democratic country that is confronting myriad social and economic problems that threaten its sovereignty and the legitimacy of its government—not too different from the political and economic challengers that arose in a nascent United States of America. Finally, the potential of other countries (which have more significant involvement in international markets) with such problems could be a threat to international stability. The following serves as an examination of the political, economic, and social implications of a small island state that finds itself confronting exceptional risks to national stability.

The political condition of Nauru can perhaps best be described as paradoxical. Freedom House accords Nauru the highest rating for being based on representation and free elections² as the country operates under a Westminster system bequeathed by its colonial rulers.³ Despite this “freedom,” Nauru is ravaged by government corruption. The system has generated numerous changing of the guards in the past decade alone which has resulted in political instability amidst allegations of political corruption, legislative stalemate, and no-confidence votes. In order to break

¹“Closing Down.” *The Economist*. October 04, 2014. <http://www.economist.com/news/asia/21621873-dismal-tale-one-remotest-nations-closing-down>

² *Freedom In The World 2014: Nauru*. Report. Freedom House. Accessed November 03, 2014. <http://www.freedomhouse.org/report/freedom-world/2014/nauru-0#.VDs7xPnF9aQ>

³ Australia. Department of Foreign Affairs and Trade. *Nauru's Country Brief*. Accessed November 03, 2014. http://www.dfat.gov.au/geo/nauru/nauru_brief.html

the legislative stalemate the government had to introduce legislation to bring the number of parliamentary seats to an odd nineteen.⁴

Nauru's unicameral Westminster system of government has very little checks and balances. The only accountability mechanism occurs when the government is pushed out through a no-confidence vote or popular elections. Moreover, 3 years as a time span for implementing policies is very short. Therefore, it is no surprise that the government's policies cater to the whims of voters. When a large sector of the economy is public, as in Nauru, political accountability is inextricably linked to economic decisions, therefore political risk is dependent on economic risk.

Historically, Nauru's economy was largely reliant on the fossilized droppings of seabirds, industrially known as phosphate deposits. Regrettably, the island's phosphate reserves were mostly plundered by colonial rulers. Despite this, when Nauru finally threw off the shackles of colonialism in 1968, the country was still financially sound.⁵ *The Economist* reports that, "After independence in 1968, phosphate exports briefly put Nauruans, per head, among the world's richest people."⁶ But the policies of successive governments failed at rehabilitating the land, diversifying their economy and investing wisely in the years of abundance. Initially, phosphate revenues contributed to robust economic growth. Australia and other colonial raiders also paid huge sums in reparations. However, the country's GDP growth peaked in 1981, and over the following three decades, Nauru's GDP in fact declined in many instances from the 1980s and through the 2000s. Only recently has moderate economic growth emerged.⁷ According to the Asian Development Bank, this growth is partly attributable to the regional processing center for people seeking asylum in Australia, referenced at a later point in this report.⁸ Ultimately, unsound investments abroad and at home depleted much of Nauru's phosphate wealth.⁹ This includes the purchase of an air fleet which was to be a national carrier and was instead used by presidents for personal reasons at the expense of paying customers who were left stranded at the airport.¹⁰

⁴ *Freedom In The World 2014: Nauru*. Report. Freedom House. Accessed November 03, 2014.

<http://www.freedomhouse.org/report/freedom-world/2014/nauru-0#.VDs7xPnF9aQ>

⁵ "Paradise Well And Truly Lost." *The Economist*. December 20, 2001. <http://www.economist.com/node/884045>

⁶ "Closing Down." *The Economist*. October 04, 2014. <http://www.economist.com/news/asia/21621873-dismal-tale-one-remotest-nations-closing-down>

⁷ Nauru: Country Profile. UN Data. Accessed December 02, 2014.

<https://data.un.org/CountryProfile.aspx?crName=Nauru>

⁸ Nauru: Economy. Asian Development Bank. Accessed December 02, 2014.

<http://www.adb.org/countries/nauru/economy>

⁹ "Paradise Well And Truly Lost." *The Economist*. December 20, 2001. <http://www.economist.com/node/884045>

¹⁰ "Paradise Well And Truly Lost." *The Economist*. December 20, 2001. <http://www.economist.com/node/884045>

Many of the poor economic policies of prior decades are inflicting contemporary consequences, and this is not strictly limited to depleted resource wealth. Nauruans do not pay taxes. Instead, they have increasingly become reliant on social welfare with schooling and medical fees paid for by the government. Housing, electrical and telecommunication services are all subsidized. Since the phosphate industry is state owned, 95% of employment in the country is in the public sector. When unemployment was at 90% in 2005,¹¹ the government told the people that the welfare society they were used to was no longer sustainable.¹² Today, an estimated one-third of the population is thought to be unemployed.¹³

Like many other small island states, Nauru is compelled to leverage its resources creatively. The government has taken to some unusual ways of filling their coffers, including serving as a haven for dubious characters who seek off-shore banking alternatives and selling citizenship. Nauru has also developed warm relations with Taiwan by recognizing their statehood and allowing them to have the distinction of the only embassy on its paradise in return for fiduciary loans at low interest rates.¹⁴ Regulations of bank start-ups are minimal and this has spun into a roaring business of crooks using Nauru as a venue for money laundering.¹⁵ In a highly publicized case, Nauru played an essential part in a trail left by money laundering crooks from Russia to the United States. Whatever the verity of the story, Nauru's international image was ultimately tainted due to its lax rules and refusal to ramp up legislation on offshore banking.¹⁶ These illegal activities might not represent a problem for other countries who can easily impose sanctions on Nauru; but for Nauru, fiscal ties with these countries are a necessity. As a small island nation, the country has limited economic options and the state of foreign relations bears significant weight. Now, the country is on the brink of economic collapse and the policies mentioned above are dysfunctional.

¹¹ *The World Factbook: Nauru*. Report. Accessed November 03, 2014. <https://www.cia.gov/library/publications/the-world-factbook/rankorder/2129rank.html>.

¹² "Paradise Well And Truly Lost." *The Economist*. December 20, 2001. <http://www.economist.com/node/884045>

¹³ "Closing Down." *The Economist*. October 04, 2014. <http://www.economist.com/news/asia/21621873-dismal-tale-one-remotest-nations-closing-down>

¹⁴ "Paradise Well And Truly Lost." *The Economist*. December 20, 2001. <http://www.economist.com/node/884045>

¹⁵ "Paradise Well And Truly Lost." *The Economist*. December 20, 2001. <http://www.economist.com/node/884045>

¹⁶ Jason Sharman. "A Study for the Pacific Islands Forum on Offshore Finance Centres in Forum Island Countries: Assessing the Impact of the Proposed US 'Stop Tax Haven Abuse' Act." <http://www.forumsec.org/resources/uploads/attachments/documents/FEMM%202008%20Offshore%20Finance%20Centres%20in%20FICs%20-%20Report.pdf>

According to the Australian government, the greatest growing source of revenue (5% increase in real GDP in 2011)¹⁷ today is the previously-referenced offshore processing center, used to house the boat-loads of refugees seeking asylum in Australia. In return for money, Nauru houses the refugees.¹⁸ Former president Marcus Stephen said that “Nauru's parliament would unanimously support the re-opening of the two detention centers on the island, which operated between 2001 and 2008”.¹⁹ Refugees, on the other hand, expressed their displeasure at being housed there instead of in refugee camps in Australia.²⁰

Aside from political and economic implications affecting the overall stability of the country, there are notable social factors at work. As referenced previously, Nauruans depend on the government for work and social welfare and they are used to a lifestyle of opulence including short work hours and access to imported goods. In fact, Nauru has been branded the “world’s fattest country” in an indictment against the lifestyle changes that came with phosphate prosperity— the shift from a traditional diet to an imported diet of soda, beer, spam and fast-food. The body index for men and women is 33.85 and 35.05 respectively. Obesity was ensued by related diseases: an estimated 45% of Nauruans are plagued by diabetes.²¹ This increases the government’s spending on social welfare and healthcare. It will definitely contribute to a low life expectancy, and undoubtedly has a damaging effect on the value of the country’s labor force. Society will eventually become riddled with problems that government policies will find hard to address.

Along with ill health, phosphate prosperity also gave way to a population that was less inclined to work.²² Education lost its value. In 2001, it was reported that only a third of children go on to secondary school. Education took a hit in 2001-2005, when the system came to a standstill because teachers were not being paid and schools stopped functioning. It is reported that, “In 2008, less than 9% of teachers in Nauru had a degree qualification. Half had only a basic certificate and

¹⁷ "Nauru: Economy." *The Commonwealth*. November 03, 2014.

<http://thecommonwealth.org/our-member-countries/nauru>

¹⁸Australia. Department of Foreign Affairs and Trade. *Nauru's Country Brief*. Accessed November 03, 2014.

http://www.dfat.gov.au/geo/nauru/nauru_brief.html

¹⁹ Alana Rosenbaum. "Nauru's President Quits Amid Corruption Allegations." *The Age*, November 2011.

<http://www.theage.com.au/world/naurus-president-quits-amid-corruption-claims-20111110-1n8qo.html>

²⁰ "Paradise Well And Truly Lost." *The Economist*. December 20, 2001 <http://www.economist.com/node/884045>

²¹ Joshua E. Keating. "Why Do The World's Fattest People Live On Islands?" *Foreign Policy*, February 08, 2011.

http://www.foreignpolicy.com/articles/2011/02/08/why_do_the_worlds_fattest_people_live_on_islands

²² "Paradise Well And Truly Lost." *The Economist*, December 20, 2001. <http://www.economist.com/node/884045>

over 30% had effectively no qualifications, being classified as trainees.”²³ Even if the government enacts policies to address the economic dysfunction, society will not be willing to change.

While Nauru exists under a democratic governance structure, there exist myriad elements with political, economic, and social dimensions which, coupled with a faulty unicameral parliamentary system, all contribute to the unstable and vulnerable position in which Nauru finds itself today.. Economic challenges are particularly intractable through the country’s political system because individual and social choices are reflected negatively in the political system. Like most countries endowed with natural resources, Nauru’s reliance on phosphates will not last forever. Most investors should refrain from investing in this phosphate industry because of the economic risks and the moral issues of contributing to the slow death of a failing state. Using Nauru as an example of the risk that comes with elections as a platitude of democracy, when issues like these are present in a more significant player in the international system, they can present both an economic and security risk. This begs the question: what should be done with Nauru and states that face similar issues?

One option has been illustrated in the case of Lanai, a Hawaiian island with 3,200 residents purchased in 2012 by Larry Ellison, founder of Oracle and one of the world’s richest people.²⁴ In fact, Nauruans are seeking a way out of the island entertaining the possibility of purchasing another island.²⁵ As Nauru runs out of money, it is also running out of ideas. One mutually beneficial solution for Nauru and investors (including sovereign funds) could feasibly be for an investor to buy the island. Nauruans will have the option of leaving to another country or seeking employment under the investor in what would no longer be their country. The investor would own that country and control much, if not all, of the island’s economic productivity. Admittedly, this is controversial; however, this experiment might lead to better yields than if Nauruans continue with the status quo. A “good” investor might turn Nauru around in a way that Nauruans were unable to do. This could lead to similar solutions for vulnerable “microstates” and those who have to suffer living in them.

²³ International Council For Open and Distance Education. November 03, 2014. http://www.icde.org/projects/regulatory_frameworks_for_distance_education/country_profiles/nauru/

²⁴ Jon Mooallem. "Larry Ellison Bought a Island in Hawaii. Now What?" *The New York Times*, Sept. 23, 2014. http://www.nytimes.com/2014/09/28/magazine/larry-ellison-island-hawaii.html?_r=0

²⁵ "Paradise Well And Truly Lost." *The Economist*. December 20, 2001. <http://www.economist.com/node/884045>

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