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## Hell in the Pacific

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Lessons from the brokest country on Earth.

 [090429\\_TBM\\_nauru.JPG](#) [1]

The island nation of Nauru ranks as one of the more obscure world destinations. You have some sense of just how obscure from the [CIA's World Factbook](#) [2]. Although the Factbook is normally a fairly authoritative source for information on countries, it lists Nauru's population at around 14,000. This is wrong: The latest census, from the end of 2006, counted 9,275 Nauruans. The *Central Intelligence Agency* doesn't know how many people live in Nauru. And, frankly, almost certainly doesn't care. Nauru is that out of the way.

If you're one of the small number who've been following the Pacific island's history over the last years—though unless you are journalist [Jack Hitt](#) [3], it's highly unlikely you have been—you'll know it hasn't always been this way for Nauru. At one time, Nauruans had one of the world's highest per capita incomes, with at least one [importing a Lamborghini](#) [4] to an island on which there is basically no place to go. Then things went very wrong.

There are some good economic lessons in this. Though not necessarily the ones that you expect.

The key to Nauru's brief period of financial greatness was phosphate, an important resource for the production of fertilizer that is derived from the accretion of thousands of years of bird droppings. Nauru's coral reef, located 1,500 miles from Papua New Guinea, attracted vast flocks of birds who left millions of tons of phosphate. This has been mined since the turn of the century. It supported the population of the island, as well as workers from other Pacific nations, from 1968, when Nauru secured its independence from Australia and nationalized the mines, until the 1990s.

Then the phosphate ran out. This has to count as one of the longest anticipated depletions of natural resources in history. As far back as the 1920s, scientists had noted that changes in migratory patterns had left Nauru with fewer birds than would account for all that phosphate. And the destruction of their habitat by mining meant fewer birds still. Not that they ever stood a chance: People can mine phosphate a lot faster than any number of birds can make droppings.

Where this was going was clear early in the century. "A worked out phosphate field," as *National Geographic* described it back in 1922, "is a dismal, ghastly tract of land, with its thousands of upstanding white coral pinnacles from ten to thirty feet high, its cavernous depths littered with broken coral, abandoned tram tracks, discarded phosphate baskets, and rusted American kerosene tins." By the late 1990s, most of Nauru was a

"worked out phosphate field." The island had been hollowed out.

To prepare for this, Nauru had built up a national trust fund that at one point amounted to \$1 billion-plus. It didn't last. There were bad real estate bets, there was embezzlement, and there was even, as Jack Hitt detailed [in this story](#). [5] a comically disastrous investment in a short-lived London musical. By the time the phosphate was gone, so was most of the money.

From there, things got worse. The country's infrastructure broke down: For a while in 2003, Nauru lost all contact with the outside world—even its own diplomats—until Australia got wind of the situation and sent in phone technicians. One of the bright spots in the island economy, an effort to turn Nauru into a banking haven for the kinds of folks for whom the Cayman Islands weren't enough, dimmed in a worldwide crackdown. The other, an Australian refugee detention center, is now empty and mothballed.

Nauru Air's one airplane was repossessed. Fourteen hundred or so nationals of Kiribati and Tuvalu (some of whom had been working on Nauru for more than a generation) begged to be repatriated. Nauru's Chinese workers left when, [as the Asian Development Bank grimly reports](#) [6], "the demand for restaurant services declined with Nauru's falling incomes."

Even *Afghanistan* has Chinese restaurants. This sounds as if it's the end of the line. The endgame of three decades of prosperity: an island almost entirely hollowed out and strip-mined and a nine-hole golf course on the Pacific shore that's now too expensive to maintain.

Except it wasn't, quite. It turned out that there was a little more phosphate to be mined, and production resumed, on a small scale, in 2006. By sometime this year, that phosphate will be exhausted. But, wait: There's actually more still. The remainder, though, is buried underground, harder to extract, and won't bring anything like the bird-dropping glory days of the 1980s (though it could provide a nice little side business in crushed rock, according to [this fantastically detailed report](#) [6] from Australian Broadcasting Corp.).

The secondary phosphate deposits could provide a new stream of income for Nauru for the next 20 years. But while phosphate prices now are at a high, the secondary deposits won't come close to giving Nauru the per capita income it had in the 1980s. And it will barely put a dent in Nauru's debt, which runs at about \$1 billion Australian—or about 27 times Nauru's current GDP. That, by the way, would be the equivalent of \$386 *trillion* for the United States.

So what's Nauru doing now? With the help of the Asian Development Bank, the country is [setting up a new trust fund](#) [7] for the future phosphate revenues.

I called Nauru's United Nations ambassador, Marlene Moses, who is based in New York and so seemed to be by far the most accessible Nauruan official, to get all this sorted out. I was hoping she would be able to explain why the very same strategy that failed so miserably before was going to work now. Why would a second trust fund be any better than the first? Was it just that Nauru would avoid investing it in theatrical productions?

Unfortunately, she hasn't been taking my calls—or the e-mails that I've been sending to Nauru's U.N. address. (It is pretty cool, though, that writing to "nauru" at the U.N. gets you to the ambassador's mailbox.) Her assistant tells me she's busy chairing a committee at the United Nations, finishing a report, and "preparing for a trip overseas." So we don't have an official Nauruan explanation of the economic strategy.

But we can make some guesses. The hope of many resource-rich countries, which have all been setting up

"sovereign wealth funds," is that they will be able to take today's income and turn it into a perpetual stream of income for the future. This, on the face of it, sounds reasonable. But it's not. In essence it's a bet that you can securitize enough of your earnings to keep your country comfortable forever.

This will never turn out to be true. The first impulse is to see the story of Nauru as an extreme example of the natural resources curse—the tendency of countries rich in resources to vastly underperform in virtually every other area. It is that. But it's more than that, too.

It's a cautionary lesson in the perils of failing to reinvest in the economy. There is no country in the world, not Nauru and not the United States, that can possibly sustain itself indefinitely on the proceeds of yesterday's economic successes.

There is no substitute for economic growth. Making some really bad investments was clearly one of the Nauruans' big mistakes. But over the long run, neither a big, well-managed trust fund nor a small, badly managed one will survive in the face of a shrinking economy. Whether you are talking about the U.S. automakers' enormous pension plans or the sovereign-wealth hopes of the Middle East, shrinking production will eventually catch up with you. There's no practical way to cover all the liabilities of the future with the profits of the past. You don't have to be a religious believer in Murphy's Law to know that sooner or later, something will go awry.

The most effective use of the money that a country or a company earns today is to use it to ensure its continued vitality in the future. Without that, whether the endgame takes 20 years, 50, or 100, the end will always be in sight, and probably closer than anyone thinks.

In a surprisingly good [story about Nauru from Al Jazeera](#) [8] last month, the country's financial minister, Kieran Keke, promised that the reforms put in place in Nauru "will stamp out the corruption and mismanagement that occurred in the past" and bring a "bright future for Nauru." Well, maybe. But for those who look at Nauru from abroad, the right lesson to take isn't about corruption or mismanagement. Those will always be with us. It is about growth. An economy with a plan for growth can tolerate many sins of mismanagement, while the lack of growth will obliterate any number of good intentions. Any country whose only plan for the future is husbanding the profits of the past will sooner or later end up in the same spot, buffeted by events as certainly as a strip-mined coral reef is battered by the waves.

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