

# PNG economic survey 2015-16

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THE UNIVERSITY OF PAPUA NEW GUINEA



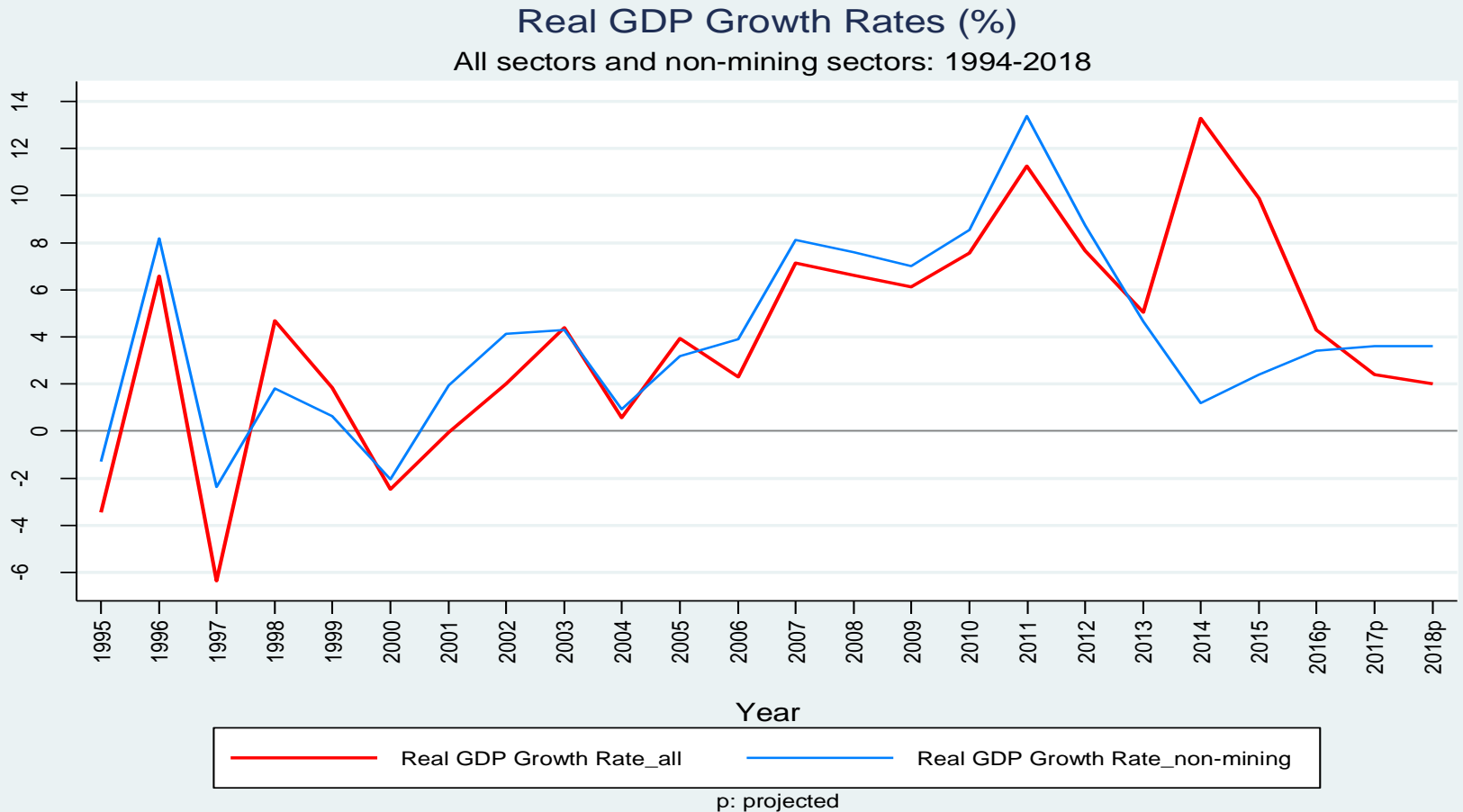
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# Introduction

- Joint project of Division of Economics, School of Business and Public Policy, UPNG and Development Policy Centre, Crawford School of Public Policy, ANU
- Provides a survey of key economic developments
- Focus this year on economic growth, macroeconomic developments and structural policy response

# Economic Growth

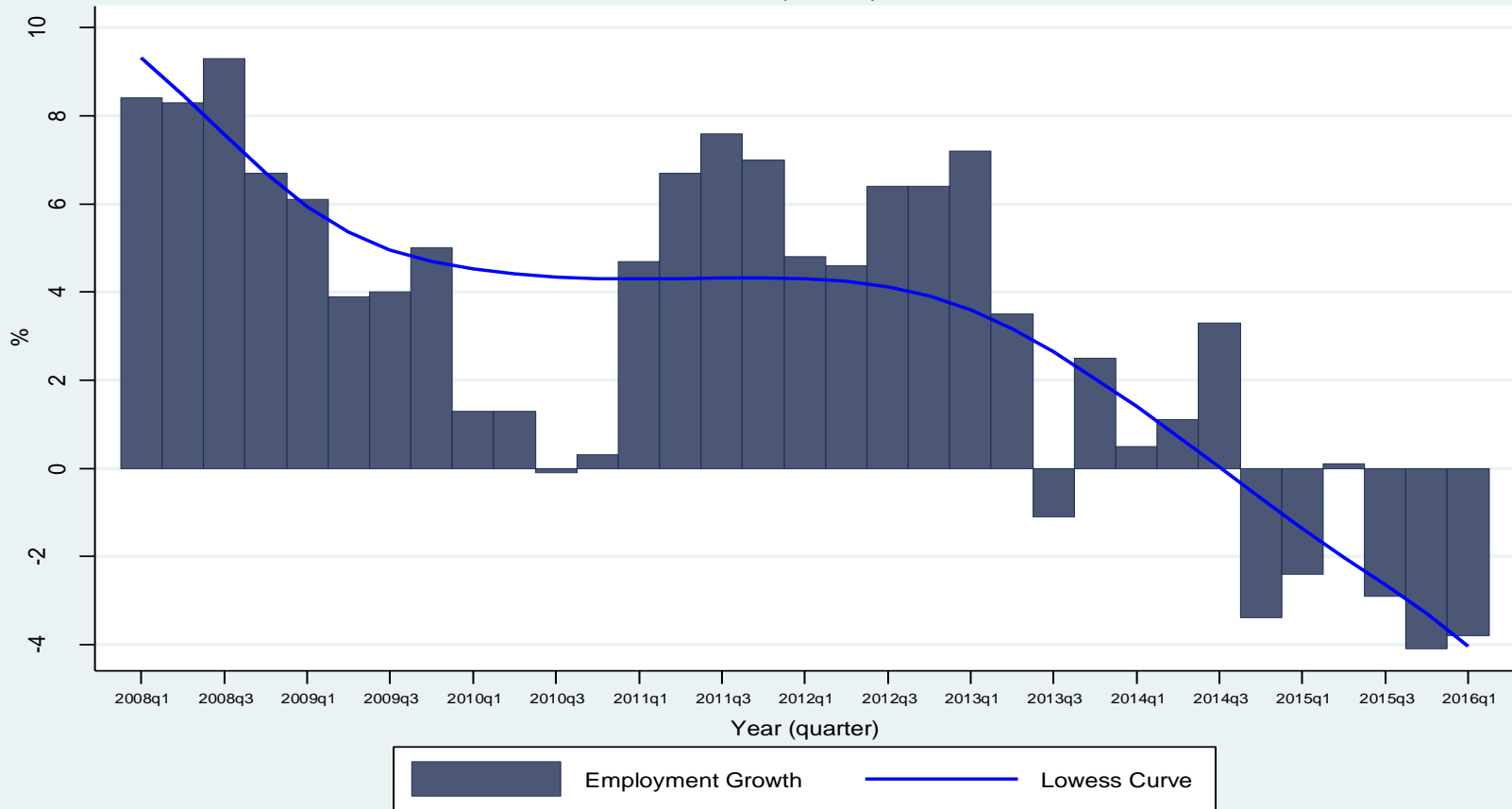
# PNG's growth slowdown



Source: NSO/Treasury/BPNG

# Employment growth negative since 2014 Q4

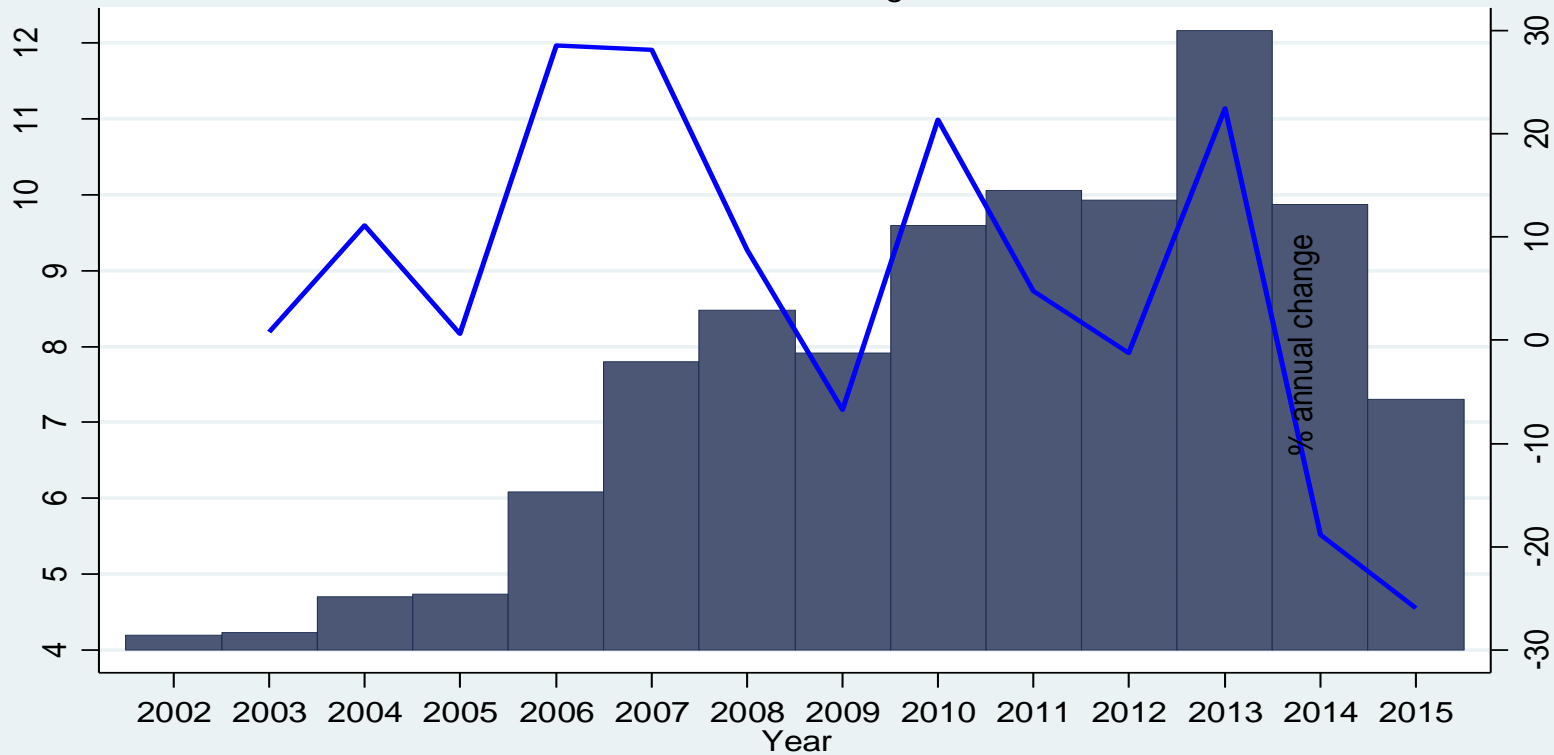
Formal sector employment growth (quarterly, year on year)  
2008q1:2016q1



Source: QEB Statistical Tables, BPNG

# Imports down below 2007 levels

Goods import in Papua New Guinea  
Value and % annual change: 2002-2015

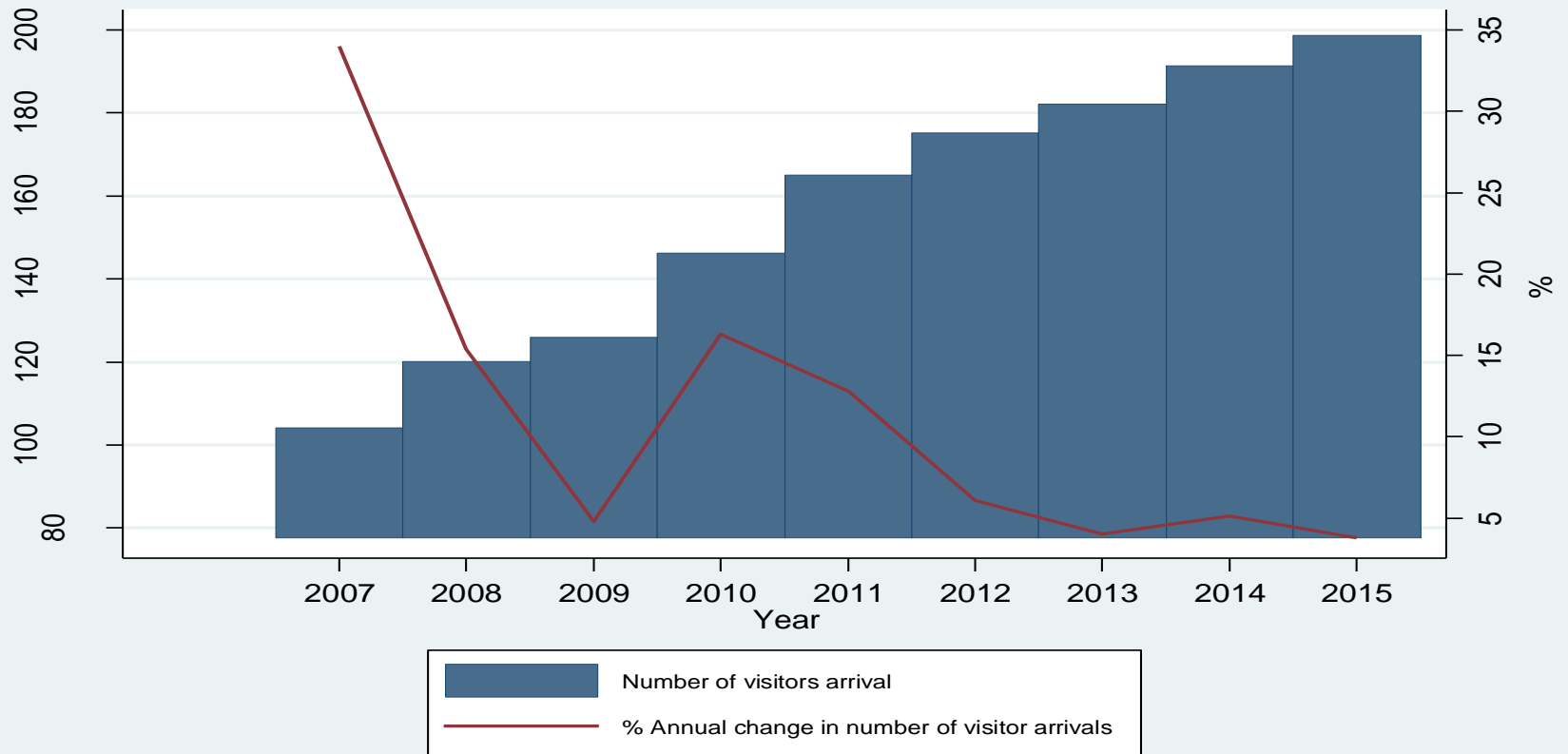


■ Import value for goods      — % annual change in import value of goods

Source: QEB Statistical Tables, BPNG

# Visitor arrivals still growing, but slowly

Visitor Arrivals in Papua New Guinea  
Numbers and % annual change: 2007- 2015



Source: PNG Tourism Promotions Authority (PNG-TPA)

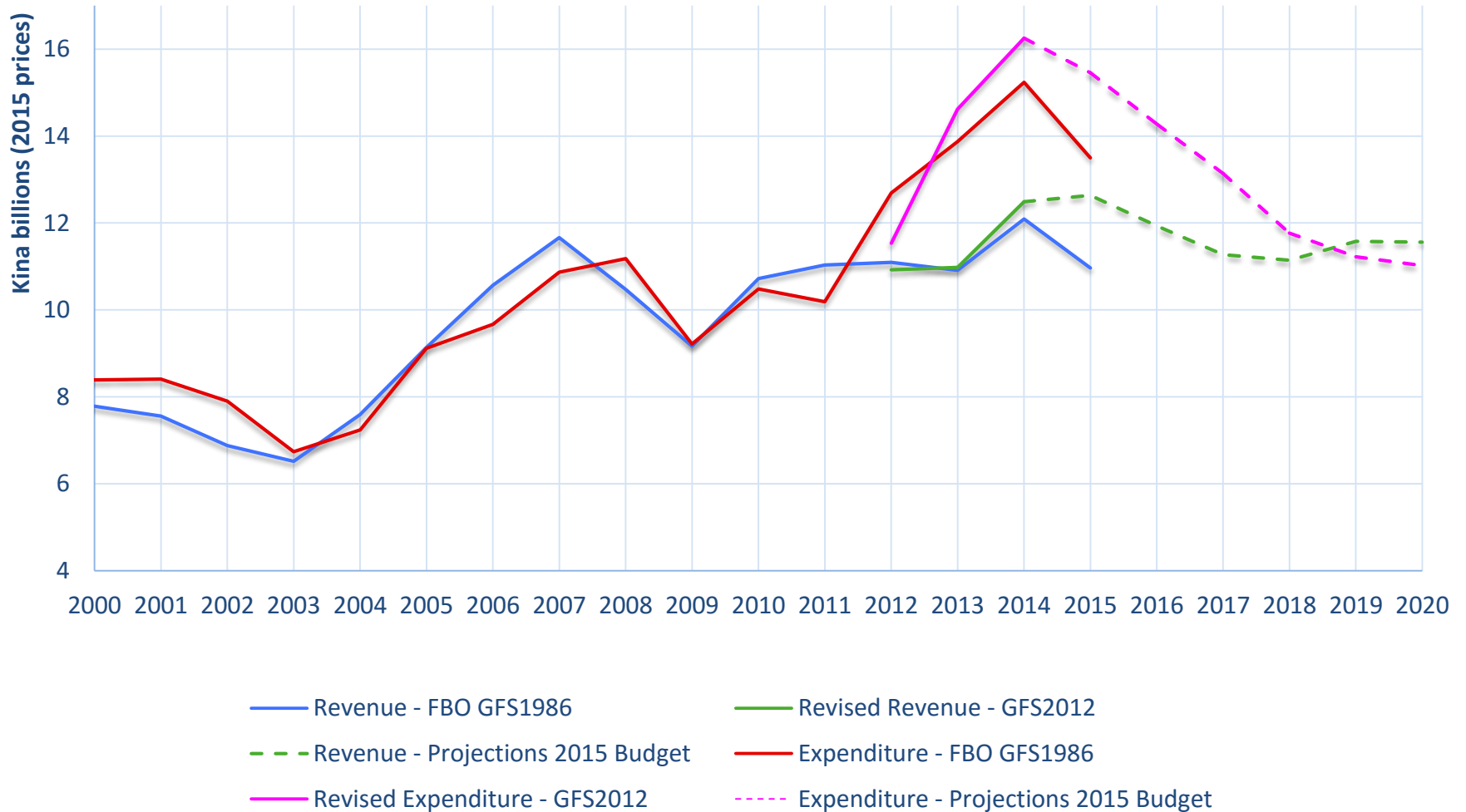
# Growth summary

- Overall, the indicators suggest a sharp slow down in domestic economic activity.
- Even if GDP growth is still positive, many indicators are suggestive of an economic recession in PNG.
- A key challenge for the government is therefore how to stimulate the economy through its macroeconomic tools which is the subject of the next section.



# Fiscal Developments

# Expenditure has outpaced revenue



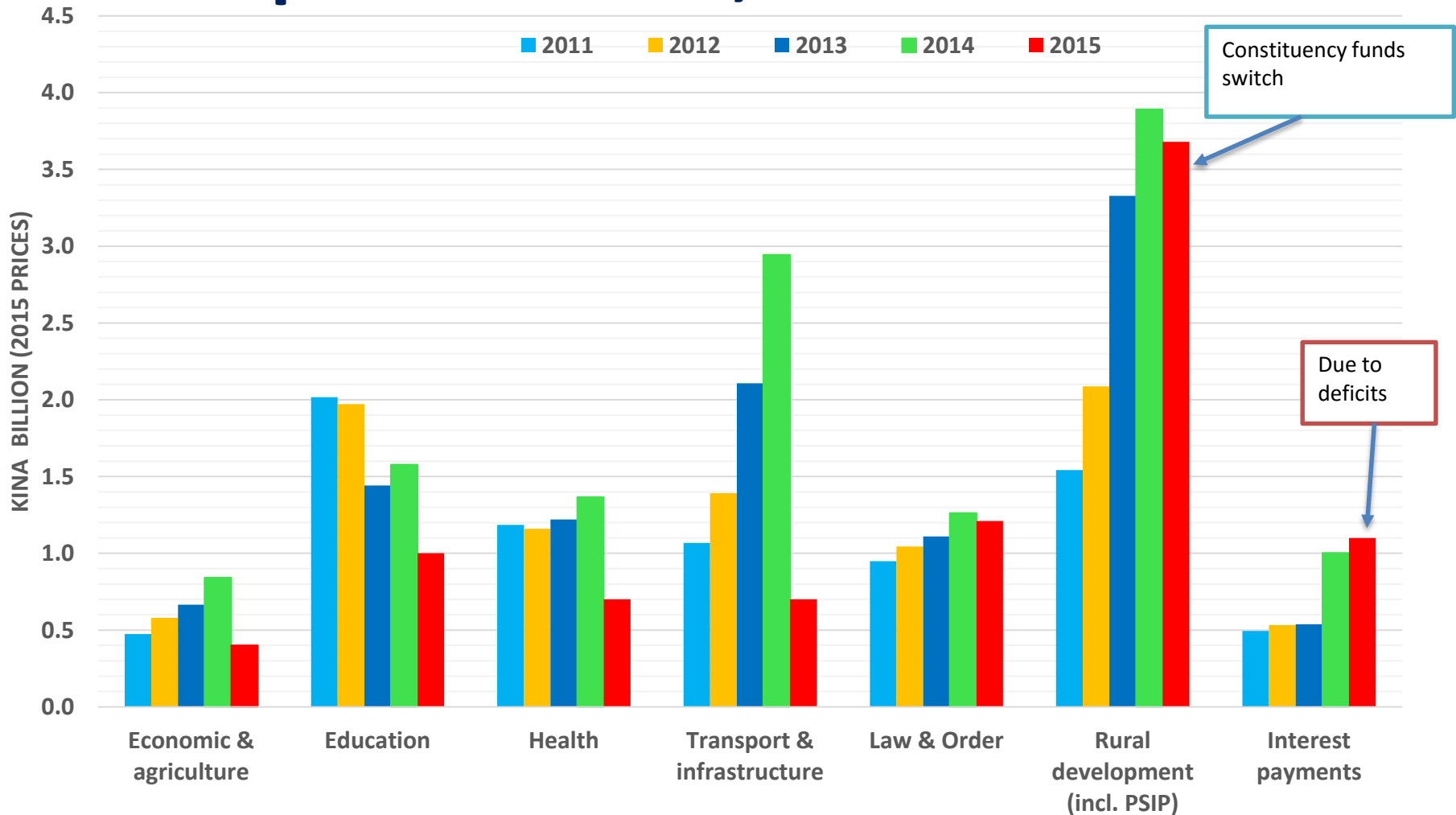
Source: Treasury

# Both mineral and economy-wide taxes have fallen



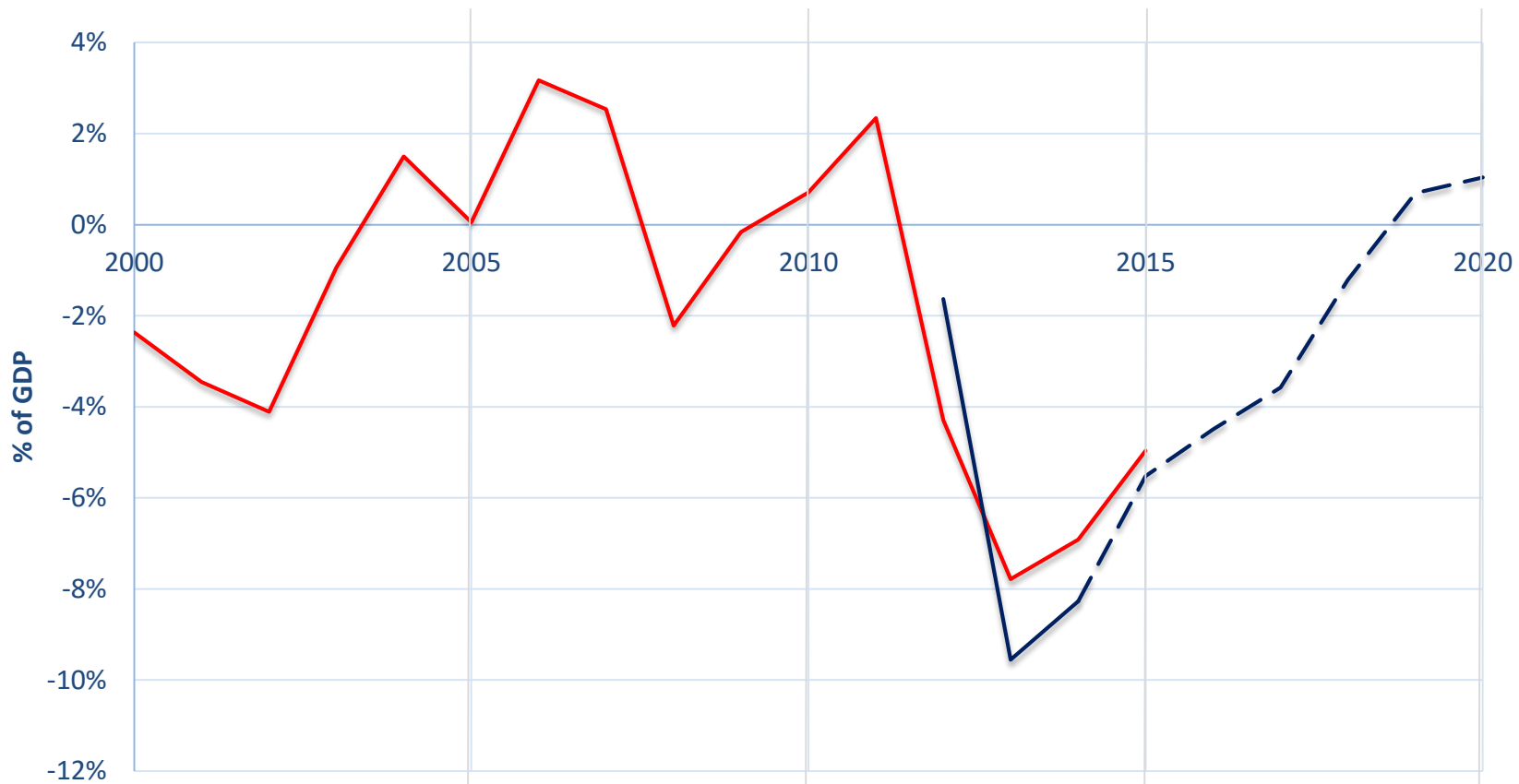
Source: Treasury

# Harsh cuts to critical services, reprioritization, 2013 vs 2015



Source: BPNG and Treasury

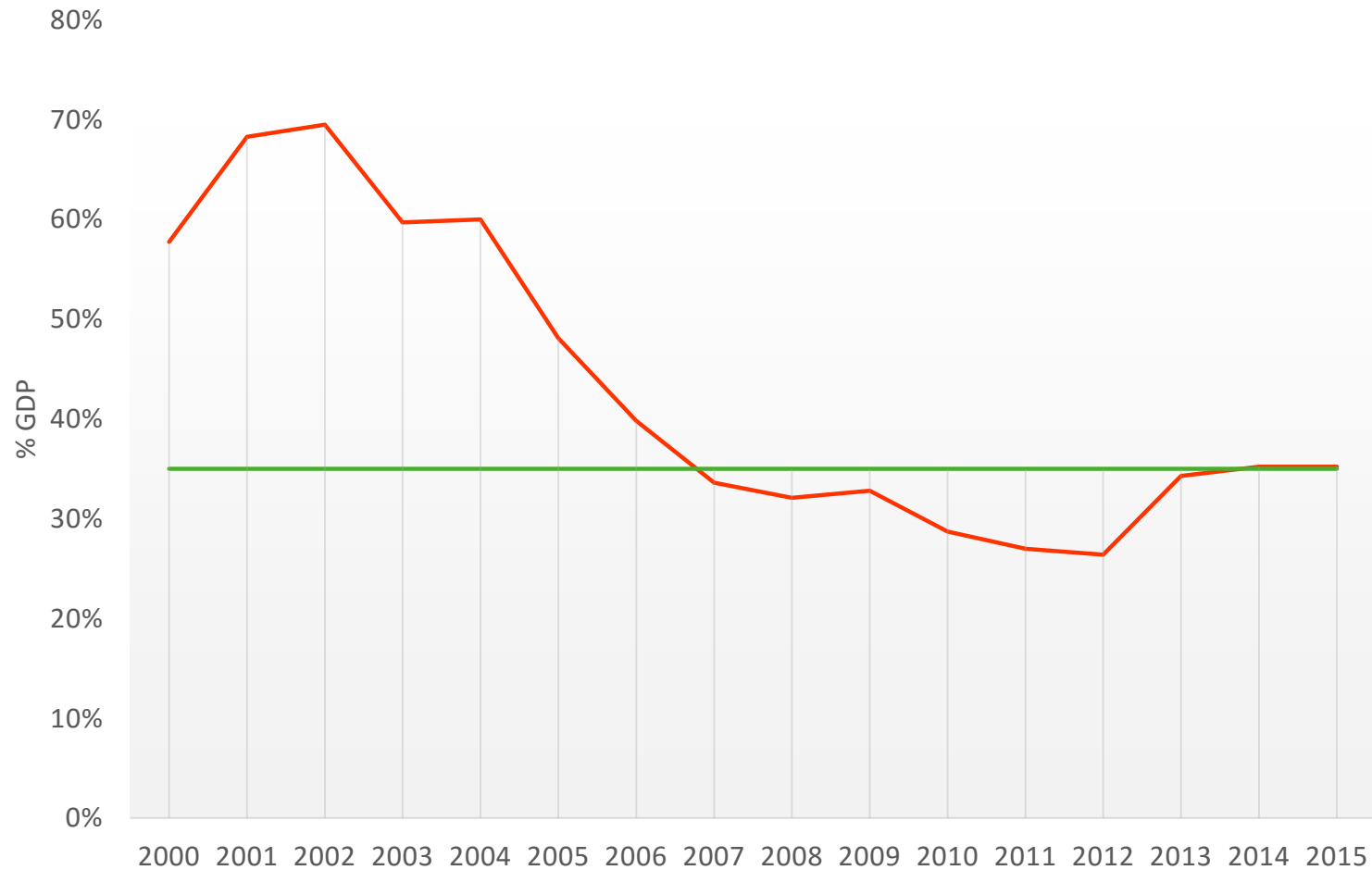
# Fiscal deficits are very large



Source: Treasury

— GFS1986 — GFS2012 - - Projections

# Debt is rising and borrowing difficult



Source: Treasury

— Debt/GDP - actuals — Revised FRA limit

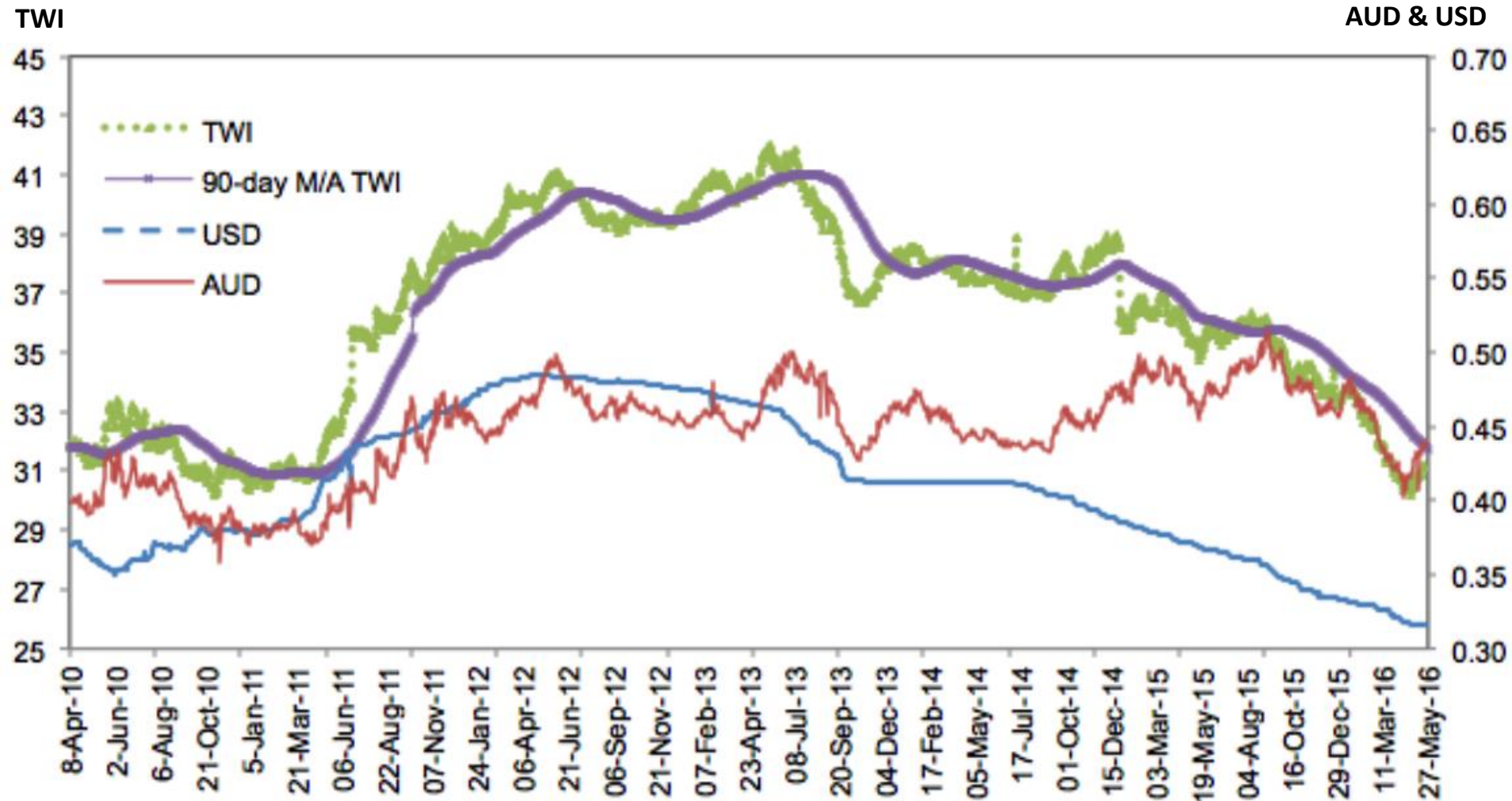
# Fiscal Policy Reflections

- Cash flow problem due to (i) limited domestic appetite for further lending to the government and (ii) significant reduction in tax collections
- Expenditure cut in health and education not a solution
- Government needs to stimulate economy and examine the scope for tax increases to boost revenue, and reprioritize expenditures through cuts in the constituency spending

# Exchange Rate

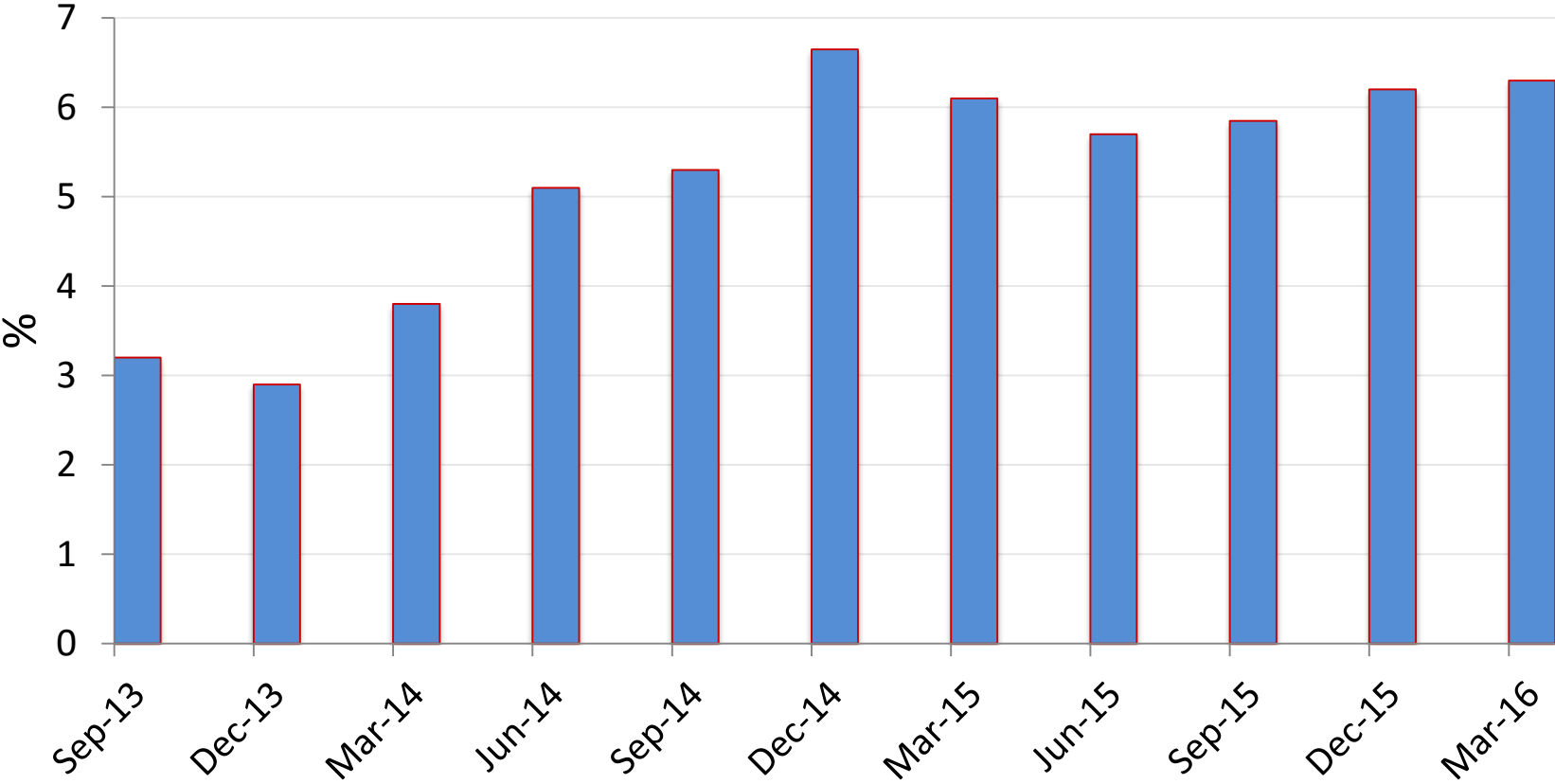


# Recent modest nominal depreciation



Source: BPNG

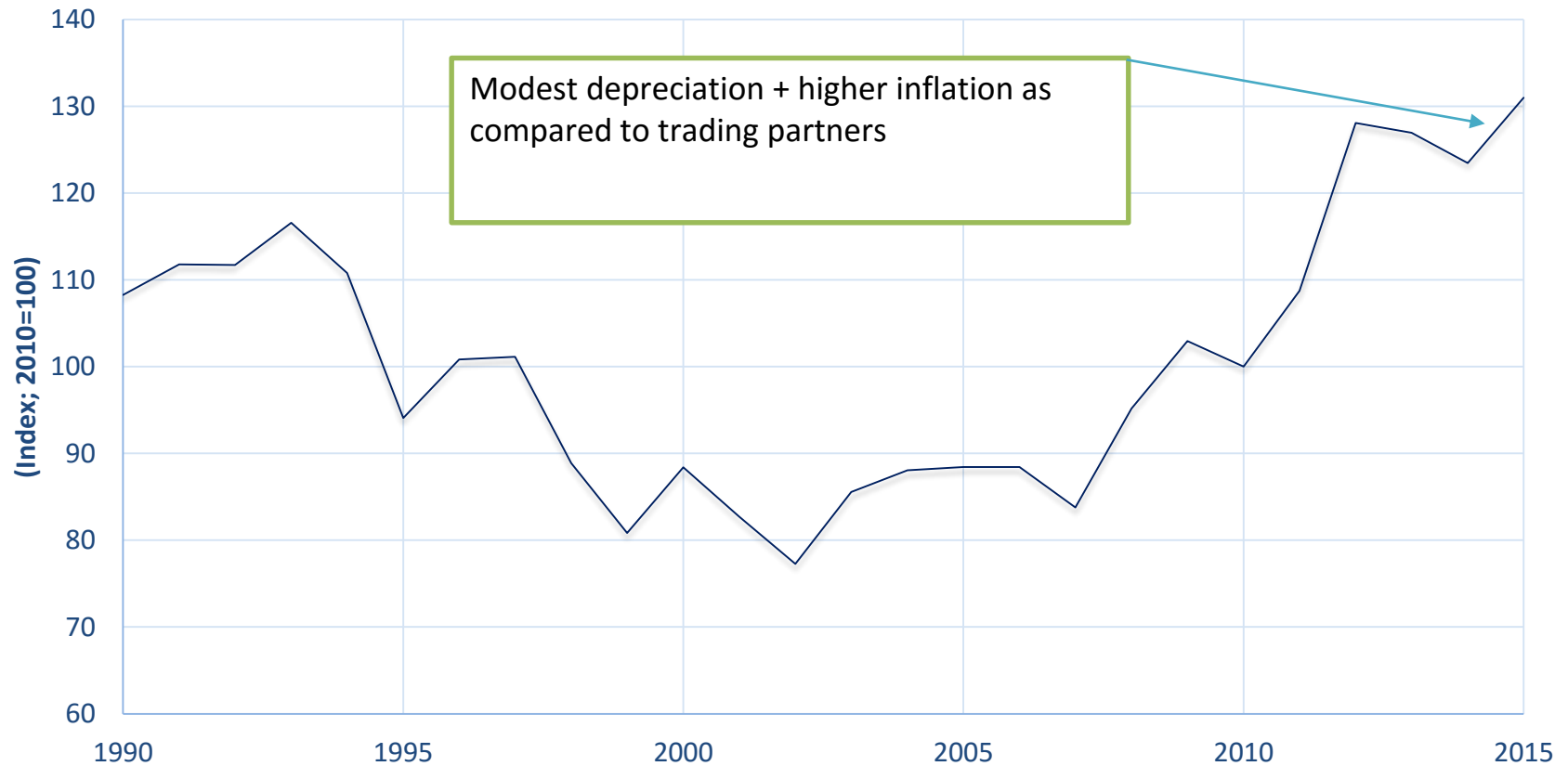
# Inflation remains at about 6%



Source: BPNG

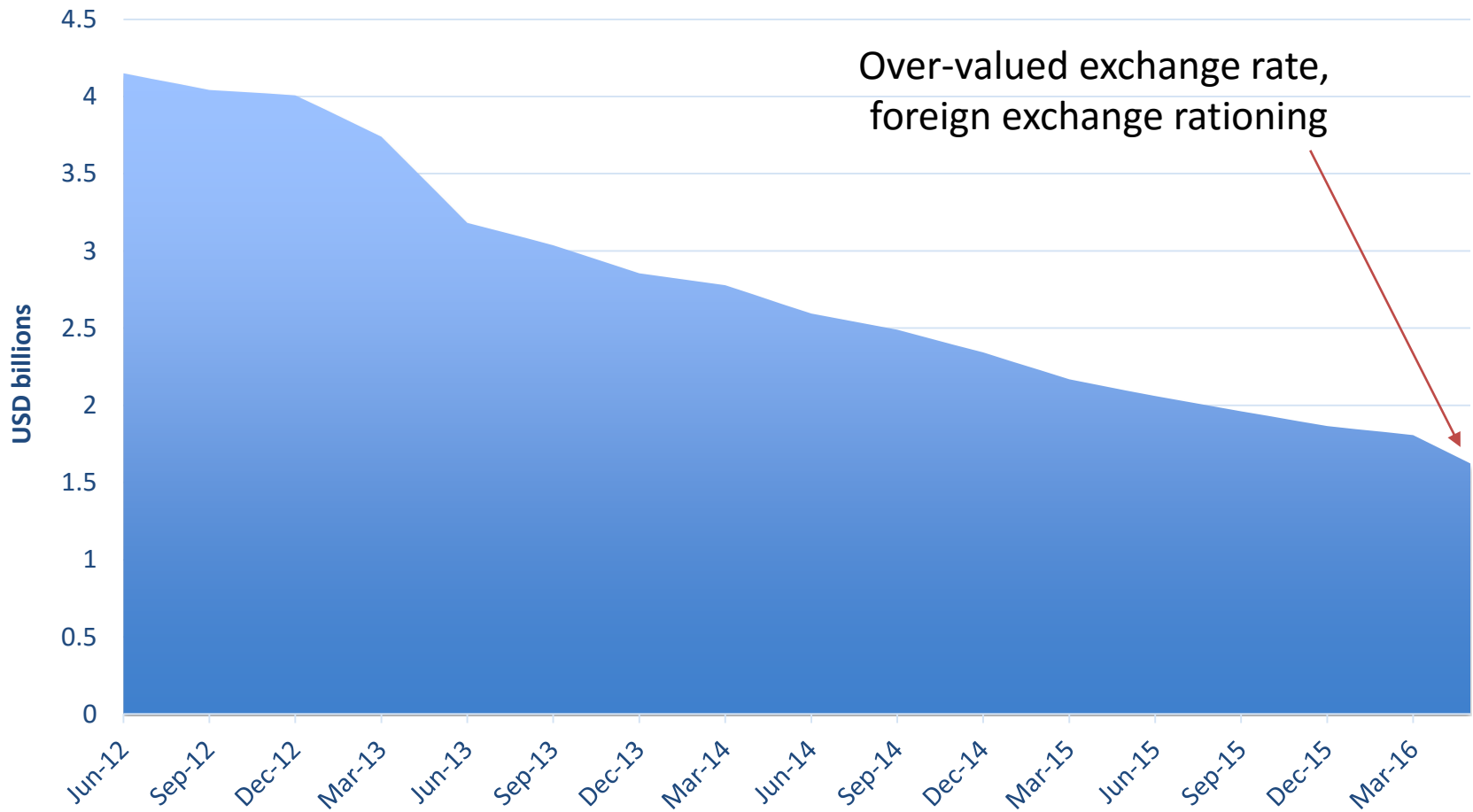
# Real exchange rate at a record high

## Real Effective Exchange Rate



Source: World Bank (2016)

# Foreign exchange reserves are falling



# Foreign exchange rationing

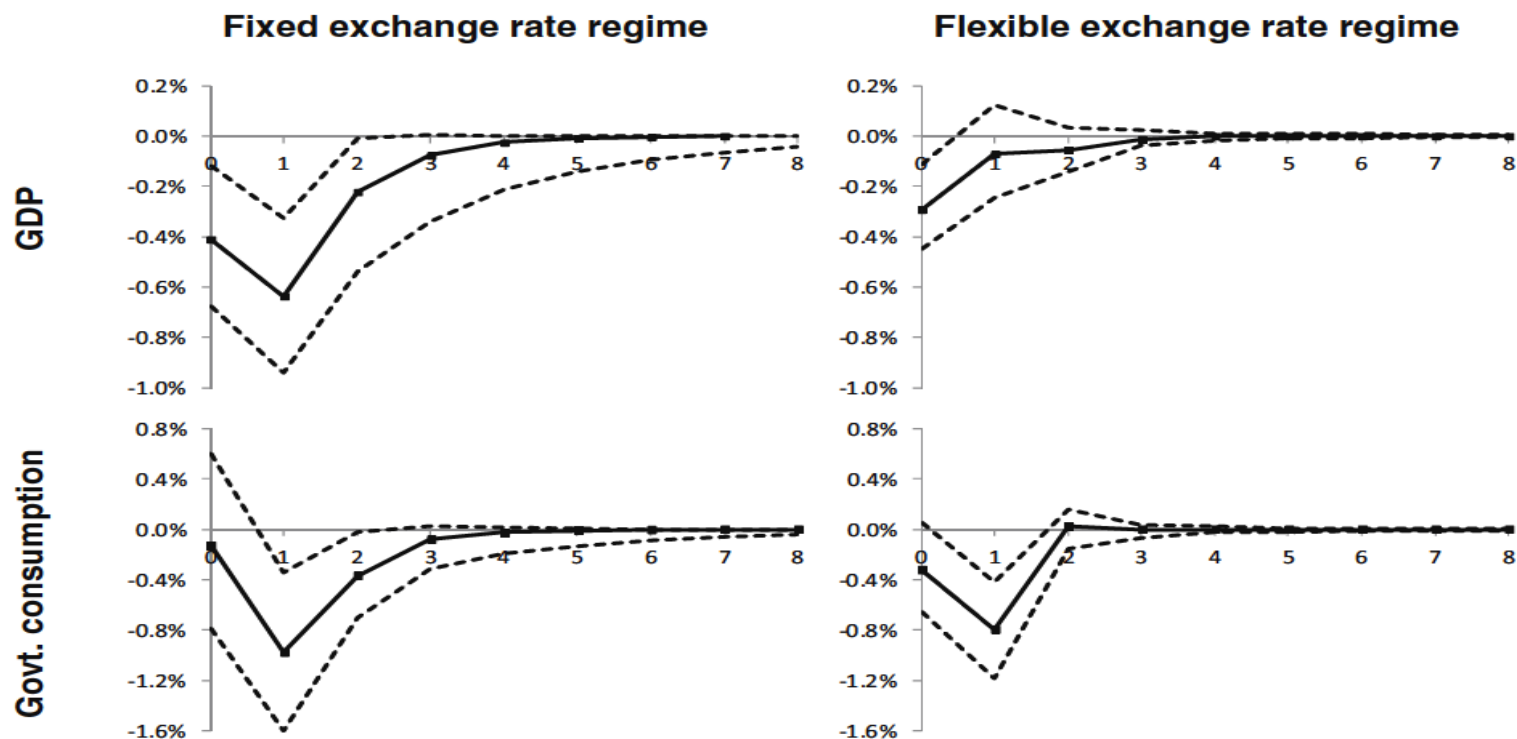
- Overvalued currency leads to excess market demand
- To cater, BPNG needs to provide foreign currency to the market but not enough reserves available. Result: forex rationing
- Wait list is as high as 1 billion USD
- Imports are compressed
- Business deferring investment in lack of forex

# Kina depreciation modest by international comparisons

Country	%Δ exchange rate 1 June 2014 – 1 June 2016	Natural resource rents as % of GDP
Mozambique	-45.8	13.6
Brazil	-37.3	5
Zambia	-34.8	16.1
South Africa	-32.5	7.6
Mexico	-30.5	6.3
Norway	-28.3	9.1
Madagascar	-26.6	10.9
Uganda	-24	11.3
<b>PNG (interbank rate)</b>	<b>-23.5</b>	<b>29.6</b>
Australia	-22	7.1
Ghana	-21.9	21.1
Chile	-20.5	16.2
Peru	-18	8.7
Indonesia	-14.5	6.3
Mongolia	-9.2	22.1
<b>PNG (market rate)</b>	<b>-8.7</b>	<b>29.6</b>
Solomon Islands	-8.7	41

# Lessons from cross-country research

Oil exporters with more flexible exchange rate regimes have a smaller GDP and government spending shock when oil prices fall



Source: [Koh \(2015\)](#) "Oil prices shocks and macroeconomic adjustments in oil-exporting countries" *International Economics and Economic Policy*

# Lesson from international experience

- Several oil-exporting economies have moved to more flexible exchange rates in response to commodity price falls
- Examples include Azerbaijan, Colombia, Kazakhstan, Malaysia, Nigeria and Venezuela.
- PNG has done the opposite.
- Needs to stimulate growth through more flexible exchange rate



# Structural policy

# New policy initiatives

- Ban on vegetable agricultural imports
  - Introduced last year, then lifted again, now reintroduced.
  - Also further discussions of rice import quotas
- SME policy
  - Goals of policy to increase employment, income per capita, SME contribution to GDP, local ownership
  - Foreign ownership of businesses in several areas (e.g. trade stores, tourism) to be restricted.
- Land policy
  - Ban of foreign ownership and leasing of land
  - Existing foreign leases have to be given up within 30 years

# Commentary on the new policies

- All protectionist in nature, limiting trade and investment.
- Limiting trade will increase domestic output, but push up higher prices.
- Limiting foreign investment will reduce output.
- Unclear if policies will be implemented, but the announcement effect may further scare off foreign investment, already deterred by foreign exchange rationing.

# Conclusion

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- In the face of economic slowdown and severe government expenditure cuts, the government needs to stimulate the economy, but lacks borrowing capacity.
- The real exchange rate is at a record high. Rather than introducing protectionist measures, would be better to allow further currency depreciation.
- This would have an immediate impact, and would not scare off foreign investors.

**Thank you!**