

Loi M Bakani: Economic overview and future developments in Papua New Guinea

Statement by Mr Loi M Bakani, Governor of the Bank of Papua New Guinea, at the 2010 Annual Meetings of the International Monetary Fund and the World Bank Group, Washington DC, 8 October 2010.

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Mr. Chairman, Colleague Governors, President of the World Bank Group, Managing Director of the International Monetary Fund, Ladies and Gentlemen, it is my pleasure to address this 2010 Annual Board of Governors Meeting. On behalf of the Government of Papua New Guinea I would like to extend our appreciation to the Bank and the Fund for the ongoing effort and initiatives to improve our living standards and global financial systems. We look forward to a fruitful round of discussions here in Washington DC.

Governors and colleagues, the prospects for global growth continue to be impacted by the aftermath of the financial crisis. I reiterate the International Monetary Fund's (IMF) outlook on the world economy with an anticipated growth of 4½ per cent in 2010. Whilst the growth is heading in the right direction we must acknowledge that growth remains sluggish by past standards. At the same time downside risks remain, due to rising concern over sovereign debt and fiscal imbalances that could trigger a repeat of the financial and economic crisis.

The downside risks underscore the need for ongoing cooperation and commitments from mutual partners to develop policies and governance mechanisms to address the challenges and secure global prosperity. At the global level, we should support policies that address structural imbalances over the medium term including supportive monetary conditions, accelerating financial sector reform, and rebalancing global demand.

Papua New Guinea, as a small open economy, was able to navigate the negative impact of the global financial crisis and grew by 5½ percent in 2009. In 2010, growth prospects remain positive as the economy enters its fourth year of economic expansion. The combination of a stable exchange rate and moderate interest rates is encouraging businesses expansion. Employment is strong, foreign exchange reserve level is high and Government debt is at a sustainable level.

The solid performance of the Papua New Guinea economy reflects increased investor and consumer confidence following a period of macroeconomic and political stability. The country has also benefited from a number of important economic and structural reforms the Government has undertaken in recent years to complement its macroeconomic policies and management.

At the same time, competition has improved the delivery of telecommunication services throughout the country. This is one of our success stories of the past few years. Services such as electronic banking and payment of some utility charges have taken advantage of the impressive take-up by the population of the mobile telephone services.

Papua New Guinea is benefiting from high commodity prices for its major exports and from inflows of capital investments related to the PNG LNG project. As a result, the country's balance of payments has shown an overall surplus of K526 million up to June 2010, and the level of gross foreign exchange reserves at the end of June 2010 was US\$2,580.5 million, sufficient for 10.9 months of total import cover.

Inflation however remains a concern due to increased domestic demand. The annual headline inflation was 6.2 percent in June 2010 and is expected to be around 7.0 percent by end of 2010. Price pressures are expected to come from domestic demand related to the PNG LNG project and Government spending. In coherence, the Central Bank continued to take a cautious approach to Monetary Policy. The country's stable macro economic

conditions coupled with the slow pace of economic recovery in the global economy has enabled the Central Bank to maintain its Kina Facility Rate at 7.0 percent for the last nine (9) months of 2010.

Our financial system remains resilient, well capitalized with adequate levels of liquidity, low level of non-performing loans and are highly profitable. In 2009, the Central Bank commenced work on the National Payments project to promote a cost effective and an efficient national and international payment system. In 2010, the Central Bank commenced work in partnership with the World Bank and UNDP to undertake a Financial Literacy Survey during 2011, which will lead to specific intervention programs aimed at extending financial services to the unbanked and underserved segment of the population. This will compliment the growth of microfinance services in making a positive contribution to providing banking services to our rural population.

On the fiscal front, the Government recorded a small deficit of K36.3 million (0.2 per cent of GDP) in 2009 compared to the fiscal deficit of K478.5 million, (2.2 per cent of GDP) in 2008. In its Mid Year Economic and Fiscal Outlook (MYEFO) Report released on 31 July 2010, the Government projects a revenue surplus of K533.3 million for 2010. This surplus is expected to be spent through a Supplementary Budget later on in the year to meet financial commitments to the development partners and landowners of the PNG LNG project.

The Government remains committed to growing and building our economy, and the private sector investment is an integral part of our economic development plans. The country will continue to pursue structural reforms to encourage investments and remove impediments to doing business and investment, thereby promoting a competitive and dynamic private sector. These are fundamental to reducing poverty, generating income and employment to improve our living standards. The Government will also continue to invest in priority infrastructure projects, improve services to districts, priority areas of education, health and justice, and ensure its debt level is sustained.

Development prospects however continue to remain a challenge for Papua New Guinea. Significant improvements are still required in the provision of education, health, justice services and transport infrastructure. There is a great need to raise the efficiency of service delivery and implementation capacity of Government institutions throughout the country. The Government acknowledges these limitations and has formulated a 20-year long term development blueprint for the country, *the Papua New Guinea Development Strategic Plan, 2010–2030* which underpins the new Medium Term Development Strategy and complements the existing *Medium-Term Fiscal Strategy* and the *Medium-Term Debt Strategy*. These initiatives provide a coherent medium term policy framework that sets out our goals and future plans, to achieve the aspirations of our people reflected in the Government's *Vision 2050*.

Looking ahead, the country still faces potential risks to its growth outlook. The risks include down-turn in the global economy that could hurt our exports, increase inflation pressure arising from domestic demand pressure related to the PNG LNG project and managing the impact of this project on the economy.

The significant foreign exchange inflows expected from the PNG LNG project will add to the already high liquidity levels in our banking system. This is one of our greatest challenges in the pursuit and maintenance of price and macroeconomic stability. Thus there is a need for adherence to the Government's Medium Term Fiscal Strategy framework to ensure that Government expenditure is kept under control and does not fuel instability.

As a way forward, the Government has decided on the establishment of a Sovereign Wealth Fund (SWF) which will manage revenues flowing from the PNG LNG project. The goal is to find a balance between macroeconomic development and stability, improvement in the welfare of the broader population and the need for effective transparency and accountability in utilizing the revenues from the PNG LNG project.

We acknowledge the involvement of the World Bank and the International Monetary Fund in Papua New Guinea. We are grateful for the continued assistance provided by the Bank, the Fund and our development partners in terms of technical assistance, funding and advice. Working together, we can ensure our efforts complement each other and are directed in the most effective way for the benefit of our people.

To end, I would like to express my country's sincere gratitude to the management and staff of the World Bank and the Fund for their continuous support in Papua New Guinea.