

Wilson Kamit: Current economic and financial conditions in Papua New Guinea

Speech by Mr Wilson Kamit, Governor of the Bank of Papua New Guinea, to the Western Highlands Provincial Community, on the occasion of the Bank Board meeting, Mt Hagen, 15 June 2005.

* * *

1. Introduction

Representatives of the Western Highlands Provincial Administration, leaders of the business and civic sectors of the Western Highlands community, distinguished guests, ladies and gentlemen.

On behalf of the Board and officers of the Bank of Papua New Guinea, I wish to express our great pleasure for us to be here and to have the opportunity to meet with you. Many of you are no strangers to the Central Bank through the Business Liaison Surveys you assist in.

The members of the Board comprise the Governor as Chairman, the two Deputy Governors, Mr. Benny Popoitai, the Deputy Governor for Management and Operations, and Mr. Loi Bakani, the Deputy Governor for Policy and Regulations. The members of the Board (ex-officio) who are appointed in accordance with Section 27 of the CBA (2000), which specifies representation by various industry and community organisations are:

Mr. John Mahuk, President of the PNG Trade Union Congress

Mr. Michael Mayberry, President of the PNG Chamber of Commerce

Mr. Kostas Constantinou – Managing Director of the Lamana Hotel

Ms. Betty Palaso – Deputy Commissioner, IRC

There are three vacancies, the President of the PNG Institute of Accountants, the Chairman of the Securities Commission and another appointee of the Minister. The vacancy in the PNG Institute of Accountants was due to the death of the son of the Western Highlands Province, the Late Mr Patrick Kolta.

The Bank of Papua New Guinea has only its head office in Port Moresby. We do not have branches in the other centers. As such, the only time we have the opportunity to visit provincial centres is through our business liaison trips, visits to provincial-based savings and loan societies, through special awareness/training such as on Exchange Control Liberalisation, through special invitations to talk or make presentations at conferences, and through Board meetings such as today. In the last seven years, we have had the opportunity to address conferences/meetings in Mount Hagen, Kavieng, Kokopo, Goroka and Lae without the Board, and with the full Board in Lae, Alotau, Kavieng, Wewak, Goroka, and Kimbe. Today is another such meeting outside of Port Moresby.

We have covered all the regions of Papua New Guinea – Highlands, Islands, Southern and Momase in our visitation. The last time we had a Board meeting were in Mt. Hagen was in the 1980s. As the Central Bank is a national institution that belongs to all the people of PNG, we will continue to go out to them in this manner. These visits are important as they provide an opportunity for the Board members and senior Bank officials to meet with community leaders and our business liaison and other business contacts, make educational presentations to provincial high schools and present school materials, mainly books. These are opportunities by which the Central Bank also gets to spend some money in the outside centres. I also hope the Board members and officials will spend some money in the fresh food and craft markets so that I can confidentially reflect on our contribution to the tourism industry in Mount Hagen.

Over these years in which the Board has met in Port Moresby and around the country, we have seen the economy turned around from a depressed state some three years ago. The economy has recovered and there is renewed confidence in the market. However, much of the fundamentals still have to be continuously nurtured, including that of transportation and other physical infrastructure. We therefore have to remain vigilant and work towards ensuring these gains are sustained.

2. Current economic conditions

The Central Bank, in its March 2005 Quarterly Economic Bulletin, released on 31st May 2005, noted improvements in the main economic indicators, and I shall not spend too much time on these developments. The Board has been brief on this. In brief:

- **Domestic Economic Conditions:** Economic activity continued to improve in 2004, led by the export sector with higher production and prices of most mineral and non-mineral commodities, and increased employment.
- **Inflation:** The annual inflation rate continues to trend downwards in the March quarter of 2005, to negative 1.2 percent. Over the year to March 2005, inflation was 0.1 percent, compared to 2.9 percent in March 2004. This reflected the positive impact of the stability in the exchange rate and fiscal restraint by the Government. In 2005, we expect inflation to remain low, if current stability in macroeconomic conditions, particularly exchange rate prevails.
- **Exchange Rate:** The positive developments in the foreign exchange market since the second half of 2003 with stable inflows from both the mineral and agricultural sectors has resulted in the appreciation of the kina. The exchange rate appreciated from US\$0.3200 at the end of December 2004 to US\$0.3210 and from A\$0.4106 to A\$0.4197.
- **Balance of Payments (BOP):** The improved inflows of export receipts reflect higher prices and volumes by the non-mineral sector, which is an encouraging sign that growers and exporters are responding positively to the improvements in commodity prices. The Central Bank's gross foreign exchange reserves are currently at high levels of US\$600 million or about K1.8 billion, equal to pay for over four months of total imports.
- **Fiscal Operations:** Preliminary estimates to March 2005 show a surplus of K113.2 million, compared to K13.8 million in the same period in 2004, reflecting higher revenue and tight controls on expenditure. The Government has continued to use the surplus to retire treasury bills and re-structure its domestic debt.
- **Domestic Interest Rates:** Consistent with the easing stance of monetary policy since the second half of 2003, interest rates continued to trend downwards. The Treasury bill rates are currently around 3 – 4 percent, while the commercial banks' indicator lending rates (ILRs) trended downwards to reach a range of between 9.95 and 11.00 percent. With the annual inflation rate at 0.1 percent, the real returns on Treasury bills are still positive.
- **Lending:** Lending by the commercial banks has picked up in recent weeks, which is an encouraging sign. We hope this will continue given the low interest rate environment. The Central Bank has encouraged the commercial banks to pass on the benefits of the low interest rates to their customers. In addition, the Bank partially liberalised exchange controls on 1st June 2005 to further encourage investment and business activity in the country.

3. The Central Bank

The reforms to the financial system, which commenced in 2000 have involved changes to the various Acts, which the Bank of PNG supervises and administers. Besides the commercial banks, finance companies, and savings and loan societies, we now oversee the life insurance companies, superannuation funds, and the micro finance institutions. Our supervision is to ensure that these institutions comply with the legislation requirements, world's best practices and operational work ethics. One of the on-going issues we continue to stress and assess is good governance and the 'fit and proper' test for the board and management of institutions we supervise.

The partial liberalisation of exchange controls early this month is another major financial reform taken by the Bank. It opens up the economy, removes one of the administrative impediments to doing business in Papua New Guinea and assists in the Government's Export-led Growth Strategy. All controls on current and capital account transactions have been liberalised, except for three. That is for approvals involving private capital account contracts between residents and non-residents, approvals to open and operate foreign currency accounts outside Papua New Guinea and the licensing of authorised dealers and gold exporters. Where tax clearance is required, this will now be the responsibility of the authorised dealers and the IRC.

Staff from the Bank have undertaken public awareness campaigns around the major centers of the country prior to the liberalisation. We would like to work together with everyone concerned to ensuring the reform is implemented successfully. Subsequent announcements on the liberalisation of the remaining controls will be made.

Coverage, in terms of accessibility of banking services to most of our population is still lacking. Whilst this is an area outside of the Bank's direct influence, it is pleasing to note that the Government, through its District Treasury Rollout Program is attempting to address this issue at the moment with the provision of such services via the postal service network and District Treasury offices and Bank South Pacific. The three large banks (ANZ, BSP and Westpac) are also expanding their points of representation.

The Central Bank also encourages the establishment of savings and loan societies to provide complementary financial services to those provided by the banks, finance companies and the existing Savings and Loan societies. This is one important mechanism of ensuring financial services reach our people in the outside centers and rural communities. As at the end of December 2004, there were twenty-one (21) active savings and loan societies. There are now three types of saving and loan societies: employer-based societies such as Teachers and Elcom; provincial-based societies like the East New Britain Savings and Loan society; and superannuation-based societies, such as NASFUND. Provincial-based societies are designed in a way that membership is open to those living in the province as well as those who are from the province but are living or working outside the province. The workers outside the province who contribute to such societies find it beneficial when they go home for holidays and need to access financial resources. The Central Bank provides advice, ensures sound management practices, and systems support.

The Bank has also embarked on addressing the issue of banking and financial service coverage in Papua New Guinea, by engaging as the Executive Agency of the PNG Micro-Finance & Employment Project in 2000. This project is co-sponsored by the Asian Development Bank, AusAID, the Government of PNG and the Central Bank. The contribution and assistance from commercial banks in this project is through the Institute of Banking and Business from where the Micro-finance Competency Centre operates. The Institute is jointly owned essentially by the banks and Bank of PNG. A pilot micro-bank which was launched in Wau, Morobe province, in 2004 has shown strong signs of growth by expanding its operations into the city of Lae after one year of commencement. This venture is technically owned by the PNG Institute of Banking and Business.

Just recently, we issued a licence to the Papua New Guinea Micro Finance Company Limited, which is owned by Papua New Guinea Sustainable Development Program Limited, the Bank South Pacific Limited and the International Finance Company (IFC), the investment arm of the World Bank. This is a vote of confidence as it is the first time that the IFC is directly involved in our country as an investor or lender.

All these initiatives are not in direct competition with the existing financial institutions, but are seen as complementary to the financial system.

We have also used our legislation to deal with financial institutions not complying with the regulations, some of whom have been placed under Statutory management with the aim that they will trade themselves out of their difficulties. May I also warn against the fast-money schemes or pyramid schemes. The Central Bank continues to work with the law enforcing agencies to get rid of these illegal schemes, which have created financial problems for many of our people. The Police Force has been helpful in this matter and I acknowledge and thank them for their assistance. We have also taken out advertisements listing the licensed financial institutions and warning the public on the illegal schemes, however the Central Bank can only do so much – we need the public's support – your support and the support from the media – to help us stop and prosecute the operators of these schemes.

4. Acknowledgements

May I take this opportunity to thank the business houses and community in Mt. Hagen and the Western Highlands province for your support in participating in the business and employment surveys conducted by the Bank – the support and co-operation that goes back some thirty years.

Your continued support in providing us with up-to-date information enhances the accuracy and quality of our reports and forecasting for the formulation of monetary policy. The input together with that from

other sources is compiled into the Quarterly Economic Bulletin and other Bank publications that are sought from within PNG and abroad. I can assure you that our QEB is read in cities like Washington D.C., Canberra, Tokyo, and Manila, to name a few.

The surveys assist the Central Bank keep abreast of developments in the real economy. The result of the surveys enables us at the Central Bank to design monetary policy, and importantly, provides another source of information for the Government to compile its estimate of Gross Domestic Product (GDP).

Whilst we can obtain information from headquarters, there is always input from actually visiting the regional centres and getting 'first hand' information. At present, a total of 496 companies are included in the survey sample covering six regions and eight industries. Of these, 24 companies that have headquarters in Mt. Hagen participate in our survey, while others are covered by their head offices in Port Moresby or Lae. I look forward to your continued cooperation in providing the required information in the surveys.

The Western Highlands province is an important contributor to the country's balance of payments performance, mainly through coffee. The Board members, Bank officials and I had the opportunity to visit one of the successful tea factories in this province, and are very encouraged by their products. It is important that producers and exporters continue to make use of any 'window of opportunity', with better commodity prices and stable economic conditions. This will ensure sustainability of the current improved macroeconomic environment.

I wish to take this opportunity to also thank bank officers in Mount Hagen, especially those working at the Currency Distribution Centre (CDC) in the BSP, the Police and escort personnel in our CDC operations.

On behalf of the Board of the Central Bank, the two Deputy Governors, and the management and staff of the Central Bank, I would like to once again thank the Western Highlands Provincial Government, the Chamber of Commerce, staff of the Highlander Hotel, and all those who have made our stay here in Mount Hagen a very pleasant one.

Thank you and God bless.