

## Loi M Bakani: Recent review of Papua New Guinea's economy

Speech by Mr Loi M Bakani, Governor of the Bank of Papua New Guinea, to the International Education Agency (IEA) College of TAFE Port Moresby Graduation, Port Moresby, 19 February 2016.

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Acknowledgement – Executives of the International Education Agency, Board of Directors, staff, invited guests, parents and guardians and students, and graduands of the 15th Graduation ceremony.

Let me first of all thank the IEA for the invitation to be the key note speaker at today's important occasion marking another stage in the graduands' educational life.

You graduands will be entering the workforce or pursuing further education at an exciting time in our young country's history that is experiencing rapid changes. You only have to look around Port Moresby and the rest of the country to see the transformation change that is taking place.

Papua New Guinea as a nation has grown and transformed into a modern, sophisticated economy. This year, 2016, marks the fourteenth year of continuous economic growth as measured by growth in real gross domestic product (GDP), the longest streak of growth since independence in 1975. The construction of the US\$19 billion PNG LNG project has transformed the PNG economy, with spin-off benefits into other sectors and place PNG on the world map as a suitable investment destination that can host world-class multi-billion dollar projects.

As a small, open and developing economy, our economic fortunes are intertwined with developments happening elsewhere around the globe. With the subdued global economic growth, volatility in international financial markets and geo-political uncertainties, international prices for our major export commodities remain low. The slowdown in China has also affected global growth.

Let me briefly outline the current state of the economy, as reflected in the main economic indicators.

**Economic activity** – growth in real GDP is expected to slow down in 2016 reflecting lower international commodity prices, including oil, and the adverse effects of the El Niño weather phenomenon. This resulted in lower export receipts and government revenues.

**Employment** – According to the Bank's Private Sector Employment Index, over the year to September 2015, the total level of employment declined by 2.6 percent, while excluding the mineral sector, it declined by 2.8 percent. The decline reflected the slowdown in economic activity.

**Balance of Payments (BOP)** – Preliminary balance of payments data for the eleven months to November 2015 show a deficit of K380 million, compared to a deficit of K7587 million in the same period last year. This outcome was due to a deficit in the capital and financial accounts, which more than offset a surplus in the current account.

**International reserves** – The level of gross foreign exchange reserves at the end of November 2015 was US\$1,910 (K5,600) million, sufficient for 10.8 months of total and 18.7 months of non-mineral import covers. As at 17th February 2015, the level of gross foreign exchange reserves was US\$1,816 (K5,439) million.

**Exchange Rate** – As a small open economy, the exchange rate of our currency, the kina, is determined by our international trade transactions and international economic and financial developments. We are a price taker for our export products and the kina continued to

depreciate against the US dollar (USD) reflecting the shortage of foreign currency in the market.

**Fiscal Operations** – Preliminary estimates of the fiscal operations of the National Government over the ten months to October 2015 showed an overall deficit of K2,142.5 million, compared to a deficit of K1,834.2 million in the corresponding period of 2014. This reflected higher expenditure which more than offset an increase in revenue. The budget deficit of K2,142.5 million was financed from net external borrowing of K215.6 million from concessional sources and from domestic sources totalling K1,926.9 million.

**Inflation** remained within manageable levels. Annual headline inflation for September 2015 was 5.8 percent.

**Monetary aggregates** – The level of broad money supply increased by 7.7 percent over the year to December 2015, compared an increase of 3.4 percent in the corresponding period of 2014 due to increases in credit to the public non-financial corporations and private sector combined with higher net claims on the Government, which exceeded decline in net foreign assets. Monetary base declined by 2.2 percent in December 2015, compared to an increase of 37.1 percent in the corresponding period of 2015. This was due to decreases in deposits of commercial banks at the Central Bank, more than offsetting the increase in currency in circulation.

The Government's large budgets (expansionary fiscal policy) in recent years are aimed at supporting economic activity after the end of the construction phase of the PNG LNG project. Whilst lower revenue has impacted on the Government's expenditure plans, it has maintained expenditure on key priority areas of education, health, law and order, and infrastructure.

The Government's focus on free education and primary health care are commendable as it strive to address the poor social indicators in the country. Redirecting the focus of Government resources to agriculture, tourism and small to medium enterprises (SMEs) will broaden the economic base of the country, reduce reliance on imported food and create employment opportunities for the majority of the population. Serious investment in these sectors will assist in reducing the economy's dependence on the mineral sector and increasing its resilience to adverse shocks, such as falling mineral prices or unexpected adverse weather conditions.

Let me turn to the area of financial system development. The Central Bank undertook two major financial sector reforms. The first was in 2000 as part of the structural reforms undertaken by the PNG Government to address serious shortcomings in the financial system. This was followed by reforms towards the end of 2000 to broaden the financial sector, increase competition and improve accessibility to financial services, and to create a sound and stable financial system.

The reforms in 2000 involved the following:

Banking sector – strengthening governance of banks with prudent management standards and guidelines Superannuation funds – introduce voluntary superannuation and increase wider participation by the workforce (reduce employees to 10 from 15)

Life Insurance – introduced good governance and management practice standards and guidelines Savings and loan societies – enhance market-oriented institutions and improved management (reduced from 100 to 21)

Major legislations enacted were:

- a. Central Banking Act 2000 making the Central Bank Independent;
- b. Banks and Financial Act 2000, Superannuation Act, Life and Insurance Act
- c. Life Insurance Act 2000

d. Superannuation (General Provisions) Act 2000

There were other financial sector reforms:

- *Exchange Control Liberalisation* for ease of doing business with exchange contracts broaden to allow residents to remit more abroad (1992), restrictions on (kina) lending to non-resident companies from domestic banks liberalised in 2004, current account transactions liberalised in 2005 and capital account transactions in 2007. There are now only a few controls in place.
- *Financial Inclusion* towards the end of 2000s, there were further reforms striving towards financial inclusion and interconnectivity. These included:
  - Establishment of Centre of Excellence for Financial Inclusion (CEFI) to promote growth of microfinance
  - Reach out to the large non-bank population
  - Introduced financial literacy programmes to develop inclusive financial system
- *Improve National Payments System* to enhance efficiency of payment system
  - Introduction of New Payments System, Kina Automated Transfer Systems (KATS) – improve efficiency and safety of transactions (real time settlement for high value payments, cheque truncation, direct credits)
  - Reduce incidence of fraudulent transactions
- *Anti-Money Laundering & Countering Financing of Terrorism* to reduce criminal use of financial system
  - Establishment of a unit (FASU) at the central bank to monitor, investigate and report proceeds of crime to Police
  - *Passage* through Parliament to enact relevant Acts
  - Criminal code amendment (money laundering and terrorism financing)
  - UN Financial sanctions
  - AML/counter terrorist financing
  - Proceeds of Crime Act

These reforms have ensured we have a sound and prudently managed financial system with a world-class payment system. I encourage you all to utilise the financial products and services offered by our financial system with institutions authorised by the Central Bank when you enter the workforce.

In line with the Government's Vision 2050 objective of wealth creation, the Bank is driving the Financial Inclusion program under the National Strategy for Financial Inclusion & Financial Literacy 2014–2015. A key priority of the Strategy is to reach one million unbanked low-income Papua New Guineans and micro and small enterprises, with a diverse range of financial services. 50 percent of whom are to be women. The program has been rolled out with the support of the licensed financial institutions to promote the savings culture among the population. These have been facilitated through establishment of the micro finance companies and micro banks.

To enhance financial literacy of the population, the Central Bank carried out the financial education through the financial literacy program. These include visits to selected provinces to conduct the programs, schools programmes for financial products tailored to students, hosting of conferences and workshops through the CEFI. There are plans for collaborative work with the Department of Education by including it in the core curricular for primary and secondary schools.

You graduands will be entering the workforce as the country experiences a lot of development. Your training at IEA Port Moresby equips you for a working life. Equally important though is the need for you to be financially literate in managing the earnings of your labour. You must know how to budget your earnings, how to save and also how to invest. For what is the point of going to work everyday, earn an allowance or salary but struggle to get by in life with all the pressures that come with it.

You have acquired a technical skill here that has prepared you well for a working career in a competitive job market. PNG is posed to experience continuous economic growth and no doubt you will all play your part in our country's development. But also make the effort to invest in your financial education to enjoy the fruits of your labour. You deserve that – for you as well as for your family.

In concluding, I wish you all every success in your career opportunities and best wishes for a rewarding career and a safe financial future.

Thank you for the invitation to speak and God bless you all.