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PAPUA NEW GUINEA

UNDP

PAPUA NEW GUINEA
ECONOMIC BRIEF

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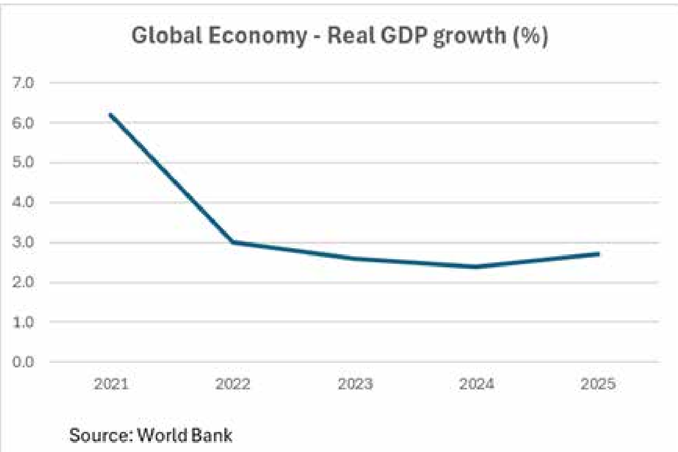
GLOBAL OVERVIEW

Global economy – 2023 performance and 2024 prospects

Global GDP growth is expected to slow from 2.7% in 2023 to 2.4% in 2024, with moderate growth to 2.7% in 2025 but still below the pre-pandemic trend growth rate of 3.0%. The slowdown is due to tight monetary policies, high inflation, restrictive credit conditions, and anemic global trade and investment. Major economies are expected to experience subdued growth while emerging markets and developing economies with solid fundamentals are expected to see improved conditions. Risks such as severe financial instability have moderated, but the overall outlook remains negative. Many developing countries, particularly vulnerable and low-income ones, have remained weak, making a full recovery from pandemic losses increasingly elusive. Despite monetary tightening and policy uncertainties, the world economy showed resilience in 2023, with large developed economies showing robust labor markets supporting consumer spending. Global trade growth weakened significantly to 0.6% in 2023 but is expected to recover to 2.4% in 2024. Price pressures remain high in many countries, and the Middle East's ongoing conflicts could disrupt energy markets and increase global inflation. Global inflation eased in 2023 but remained above the 2010-2019 average. Headline inflation fell from 8.1% in 2022 to 5.7% in 2023 and declined to 3.9% in 2024.

Chart 1: Global Economy Real Growth Rate (%) 2021-2025(proj)

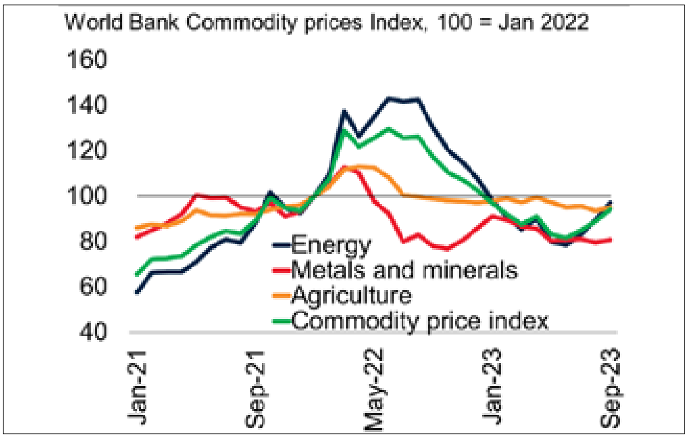


Source: UN DESA World Economic Situation and Prospects 2024; World Bank Global Economic Prospects, 2024; Asian Development Bank – Pacific Economic Monitor, December 2023; and International Monetary Fund Global Financial Stability Report

Commodity prices

The Middle East conflict has caused significant uncertainty in commodity markets, with an escalation potentially leading to surging oil prices and other commodities, intensifying food insecurity. Brent crude oil was US$84 per barrel at the end of 2023, following a 10.9 percent increase in Q3 2023 due to high demand from China and tighter global supply. The World Bank food price index declined over the first three quarters of 2023, with grain prices falling by 7.2% despite the termination of the Black Sea Grain Initiative. Liquefied natural gas prices continued to decline, while gold prices are expected to increase by 5.6% in 2024. Coffee prices were low, while logs and sugar prices rose. Due to subdued global growth, energy prices are expected to fall by 5% in 2024 and 0.7% in 2025.

Chart 2: Commodity Prices Index



Source: World Bank Commodity Markets Outlook, October 2023 and Asian Development Bank – Pacific Economic Monitor, December 2023

PACIFIC REGIONAL OVERVIEW

Pacific economies (excluding Papua New Guinea) are expected to grow 2.9% in 2024, boosted by tourism and infrastructure spending recovery. However, the GDP growth rate of Pacific Island countries with high tourism dependence remains over 10% below pre-pandemic levels. Challenges include higher fiscal deficits, elevated debt, and shrinking fiscal policy space. Cook Islands, Fiji, Samoa, and Tonga have seen a significant recovery in tourism, while the South Pacific is experiencing a recovery in visitor arrivals. Risks include capacity constraints on labor and tourism facilities, vulnerability to disasters and climate events, and inflation pressure, projected to average 4.5% in 2024 compared to 4.9% in 2023.

Chart 3: Pacific Region - GDP growth (%), by country, 2023 and 2024(proj)

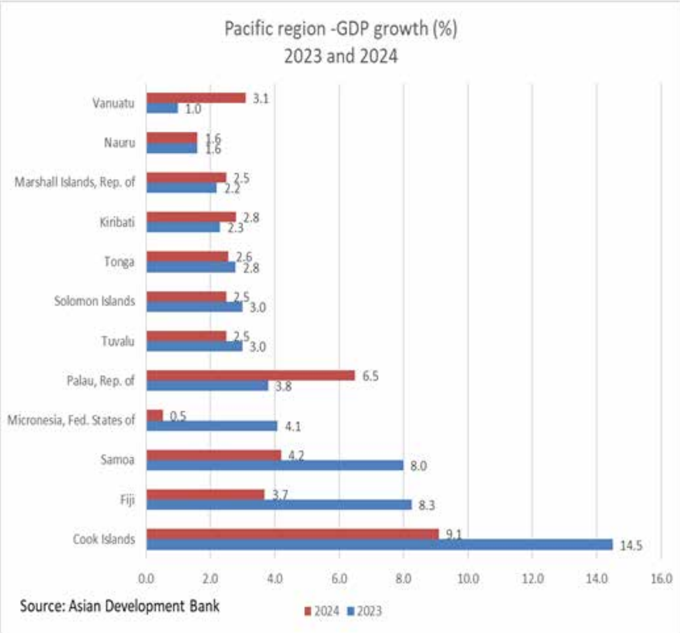


Chart 4: Pacific Region - GDP growth (%) 2019 to 2024(proj)

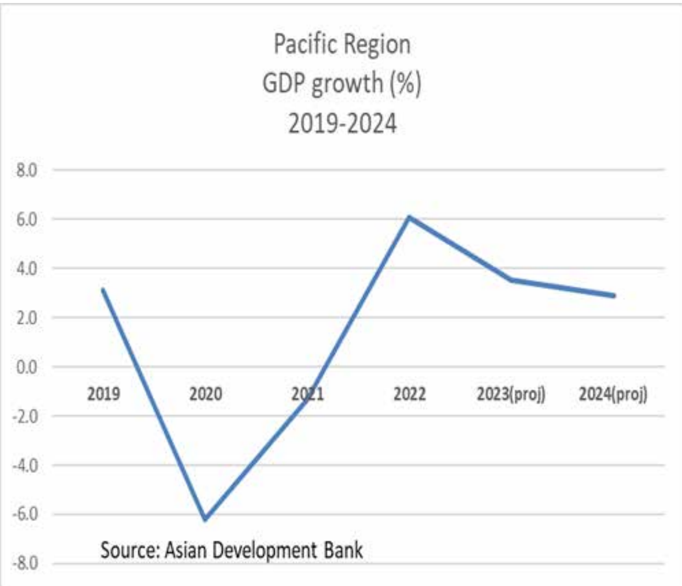


Chart 5: Pacific Region - Inflation rate (%), by country, 2023 and 2024(proj)

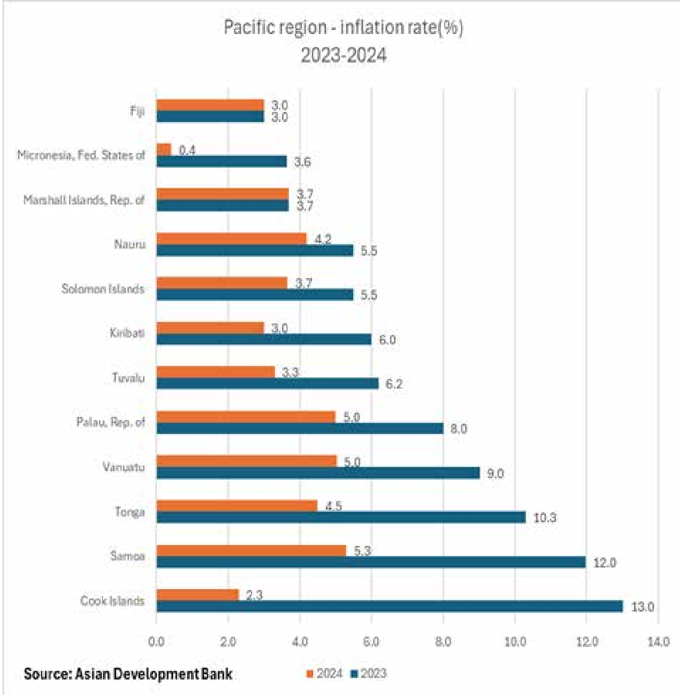
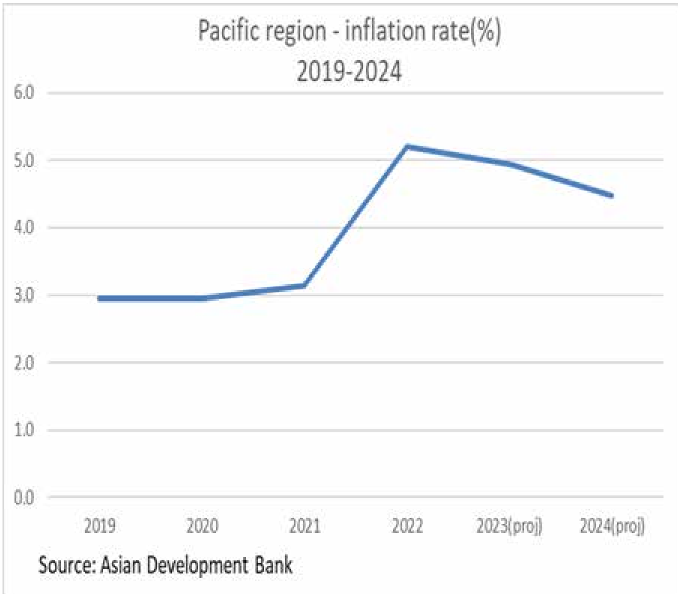


Chart 6: Pacific Region - Inflation rate (%), by country, 2019 and 2024(proj)

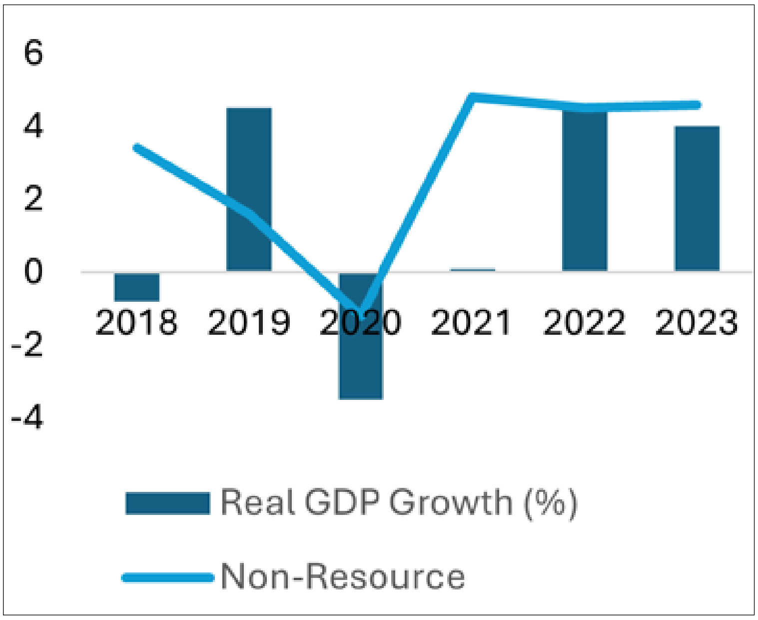


KEY DEVELOPMENTS IN 2023

Papua New Guinea's real gross domestic product is estimated to have grown by 4.0% in 2023 compared with 4.6% in 2022. This outturn was driven by a strong performance in the non-resource sector supported by an increase in public spending, strong business activity, and an 8.9% expansion in credit to the private sector. By contrast, the resource sector contracted owing to continued delays in reopening the Porgera gold mine throughout the year, among other production challenges. However, PNG outperformed the global and Asia-Pacific growth averages for the second consecutive year. In 2023, the Government released its new Medium Term Development Plan IV, designed to ensure that the economy grows sustainably and inclusively within a stable social and economic environment.

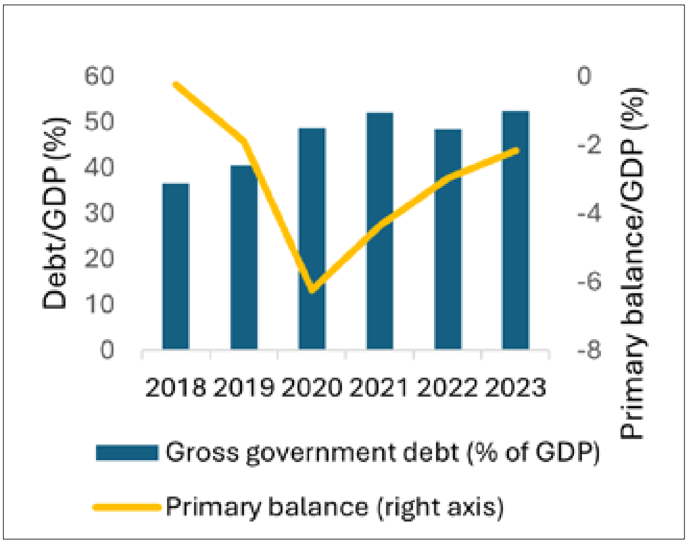
Headline inflation decreased in 2023 relative to 2022. Year-on-year inflation declined to 1.4% at the end of September 2023, comparing favourably to the 6.3% recorded for the same period in 2022. This downtick in inflation reflects a once-off reduction in tuition costs and lower inflation globally. Alcoholic beverages, tobacco, betelnut, food and non-alcoholic beverages, transport, and household equipment all recorded year-on-year declines at the end of the third quarter of 2023, whereas restaurants and hotels and clothing and footwear recorded increased inflation over the same period.

Chart 7: PNG Real Gross Domestic Product Growth



The fiscal deficit is estimated to decline slightly in 2023, driven by strong revenue performance. Total tax revenue grew by 12.6% to K19,582 million (17.3% of GDP), driven mainly by non-resource tax collections, while the total outlay for 2023 was K24,567 million (21.7% of GDP). This outturn resulted in an overall fiscal deficit of 4.4% of GDP, which compares favourably with a deficit of 5.6% in the previous year and is consistent with the authorities' fiscal consolidation efforts. The primary deficit also decreased by approximately a percentage point to just about 2.2% of GDP.

Chart 8: Fiscal and Debt Performance

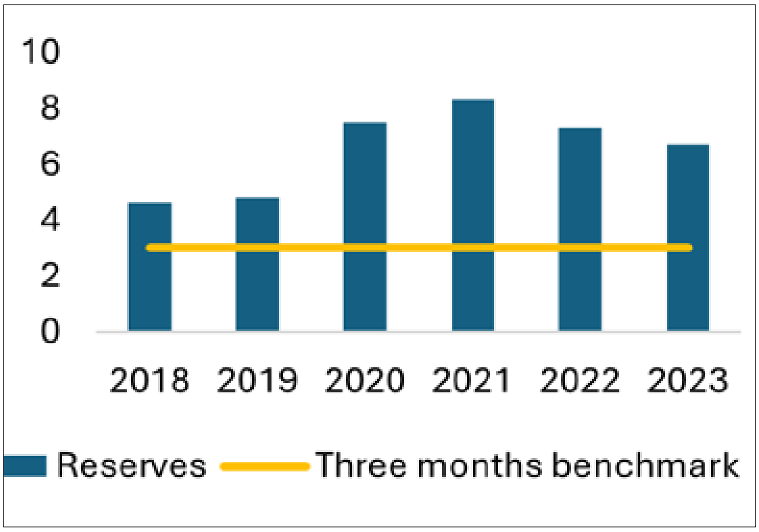


Government debt continues to rise and is estimated at 52.4% of GDP (or K59, 142.5 million). According to the International Monetary Fund, PNG's debt remains at high risk of debt distress due to high and increasing levels of debt and, more importantly, due to liquidity risks that are linked to the bullet payment due in 2028 on PNG's Eurobond and a ratcheting up of bilateral and multilateral debt service payments between 2026 and 2029. PNG's debt profile is susceptible to foreign exchange and global commodity price shocks, and because it is highly concentrated in short-term treasury bills, rollover risks make debt servicing harder to manage.

The Bank of Papua New Guinea maintains a neutral monetary policy stance. It closely monitors exchange rate-induced inflation as the Kina has moderately depreciated throughout the year due to a deliberate policy move toward greater currency flexibility. In September, the bank lowered its Kina Facility Rate by 50 basis points to 3.0% due to lower reported inflation. However, liquidity in the banking system remains high and continues to frustrate central bank efforts to influence interest rates. Because of this, the Bank of Papua New Guinea has announced measures to remove excess liquidity from the system. Generally, banks are well-capitalized and profitable, with declining rates of non-performing loans.

The move to greater flexibility has resulted in Kina's depreciation of 3.17% against the US dollar from December 31, 2022, to September 22, 2023. Although better, foreign exchange shortages persist and continue to constrain imports. The Bank of Papua New Guinea anticipates a current and capital account surplus of K19,925.8 million in 2023, primarily driven by mineral exports. The financial account recorded a deficit of K20,900.7 due to an outflow of funds to offshore foreign currency accounts for offshore investments and external loan repayments by mineral companies, including LNG project partners. Gross international reserves for 2023 are estimated at US$3.4 billion compared with US$4 billion in 2022. This amount is sufficient for 6.7 months of goods and services import cover.

Chart 9: International Reserves (in months of imports)



OUTLOOK

Notwithstanding widespread violence and looting in urban areas in January 2024 and the associated downside risks, the outlook for PNG remains positive. With the opening of the Porgera mine, the commencement of the Papua LNG project and other resource projects in 2024, sustained growth in agriculture and services, and the PNG Connect infrastructure programme continuing apace, the country is projected to grow at 4.3% in 2024 and stabilize around 3% in the coming years. If executed well, the MTDP IV, released in 2023, should produce sustainable and inclusive growth outcomes for the country.

COUNTRY UPDATE

Porgera gold mine reopened

The Porgera gold mine, which contributed about 16 percent of mining and quarrying output before its closure in 2020, reopened on December 22, 2023. The mine was closed due to the Government's refusal to renew the Barrick (Niugini) Limited operating license and disagreements over benefits for local stakeholders. The mine has also been contentious for environmental and human rights reasons. The Porgera Project Commencement Agreement was signed on December 20, 2023, involving New Porgera Ltd, landowners, and the Enga Provincial Government. The agreement delineates the equity structure of New Porgera, with clear benefits outlined for landowners and the Enga Provincial Government. They will receive benefits upon the commencement of gold production, including a 3% royalty. The state will start receiving a 30% tax upon first gold production and a 2% fiscal stability tax and will also benefit from spin-off benefits like personal income tax on mine workers. The agreement provides 7.5% for Special Mining Lease landowners, 2.5% for Lease for Mining Purposes areas, and 5% for the Enga Provincial Government. Employment at the mine ramped up to 2,000 and will increase to about 3,000 in the first six months of operation.

Source: Economist Intelligence Unit and Papua New Guinea Department of Prime Minister and National Executive Council

The reopening of the Porgera gold mine will benefit PNG's public finances and improve macroeconomic indicators, particularly gross national income and exports. Further, mining sector employment and landowners' income will increase. The Government's policy options include operationalizing the sovereign wealth fund so that the tax revenue from the mine can be invested for future generations. The additional revenues can also be spent on improving essential services such as health and education.

State Owned Enterprise debts weighing on PNG's sovereign risk profile

The Papua New Guinea (PNG) government has significant contingent liabilities of Kina8.3bn (US$2.2bn), equivalent to 7% of GDP, linked to state-owned enterprises (SOEs). These SOEs are unprofitable, generate low returns, and heavily rely on the Government for cash infusions and asset donations. The PNG government's contingent liabilities are not included in the official public debt stock, which amounted to Kina58.7bn (52.2% of GDP) in 2022. Including them would push the public debt/GDP ratio to above 60%, breaching the debt ceiling set out in the Fiscal Responsibility Act. Most contingent liabilities are from external creditors, which exposes the Government to exchange rate risk. The rise in interest rates and greater exchange-rate volatility will reduce SOEs' ability to repay foreign debt, forcing the PNG government to assist. This situation will raise PNG's debt servicing costs, although an outright sovereign default is unlikely.

Source Economist Intelligence Unit

The PNG government can seek various policy options to reduce the fiscal burden *of state-owned enterprises. These options include selling majority ownership to the private sector, exercising greater control over the SOE's borrowing, and seeking external management contracts to increase the operational efficiency of the SOEs.*

First review under the Extended Credit Facility and Extended Fund Facility (ECF/EFF) arrangements for Papua New Guinea

The IMF Executive Board completed the First Reviews under the 38-month ECF/EFF arrangements for Papua New Guinea, providing the country with immediate access to US$88 million. The review found that all end-June 2023 performance criteria were met, namely strengthening the government human resources business processes and appointments to the Independent Commission Against Corruption (ICAC). In addition, two of the August 2023 criteria were met: the modification of open market operations and the development of an action plan for exchange rate reform and monetary policy reform. The program will continue to support Papua New Guinea's reform agenda, including several other newly proposed criteria, such as cleansing the government payroll by the end of August 2024.

Source: International Monetary Fund

PNG meeting the criteria of the IMF programme will improve the country's public finances and macroeconomic prospects. The Government can use the benefits of these achievements to reduce poverty and advance human development.

PNG is exploring Free Trade Agreements(FTAs) with Australia and China

PNG is conducting feasibility studies to inform two free-trade agreements (FTAs) with China and Australia. PNG has long-standing ties with Australia, but China's influence has grown over the past decade, as elsewhere in the Pacific. The two countries are PNG's largest trade partners, followed by Japan and Singapore. China has provided a Kina1m (US$280,000) grant to PNG's Trade Office to complete a feasibility study. A trade deal with China would open several potential economic benefits for PNG. A trade deal with the Pacific's largest economy would chiefly provide geopolitical advantages for China. China is a significant and growing trade partner with which PNG maintains a large and expanding surplus. Bilateral trade is driven by PNG's shipments of liquefied natural gas (LNG), which expanded rapidly following the completion of the PNG LNG project in 2014. PNG's primary goal will be to broaden its exports to Australia, which is currently dominated by gold, and then process them. Australia's motivations are chiefly geopolitical. It seeks to cement historical ties with PNG as a bulwark against Chinese influence.

Source: Economic Intelligence Unit

FTAs can increase exports and investment and provide a higher gross national income. To ensure that the FTAs include clauses beneficial to the country, the PNG government can seek UN expertise through UNCTAD in drafting the FTAs.

RISK PROFILE

Papua New Guinea (PNG) faces numerous challenges, including high business operating risks due to poor security, tribal conflicts, and violent elections. The country's infrastructure is robust for core resource exports, but road, air travel, utilities, and digital infrastructure require improvement. The Government's effectiveness remains a significant challenge due to corruption and local interests. Civil service capacity is weak, and licensing procedures have pervasive red tape. The judicial process is fast, but there is a backlog of cases and extended contract enforcement periods. The system of communal land ownership complicates private property rights, hindering resource project development. The macroeconomic environment will improve in 2024-25 due to global energy demand, high commodity prices, and easing local regulations. The non-resource sector's growth is projected to be faster than the resource sector, suggesting spillover. The Government favors import substitution and protectionism in industries like logging and fisheries to deepen local processing capacity. Currency flow controls have led to illiquidity in foreign exchange markets, posing a significant challenge for businesses. The country's small and illiquid stock market calls for reform to widen the investor base.

Table 1: Papua New Guinea Risk Profile

Papua New Guinea risk: EIU Risk Overview				
Risk Rating	**Jan 2024**	**Jan 2024**	**Oct 2023**	**Oct 2023**
Overall assessment	C	57	C	59
Security risk	C	56	C	59
Political stability risk	C	45	C	50
Government effectiveness risk	D	66	D	66
Legal and regulatory risk	C	58	C	58
Macroeconomic risk	B	35	C	35
Foreign trade and payment risk	C	46	C	46
Financial risk	D	71	D	71
Tax policy risk	D	63	D	63
Labour market risk	C	54	C	54
Infrastructure risk	C	80	D	80
NOTE: E= most risky, 100= most risky				

Source: Economist Intelligence Unit

The policy implication of the risk review is that PNG requires structural changes in several areas. The MTDP IV and UNSDCF 2024-2028 are good starting points for enabling PNG to address these risks.

ISSUE FOCUS: PNG BUDGET 2024

This year's budget is the largest in PNG's history, with planned expenditures at K27.38 billion. Because of significant revenue growth, the fiscal deficit declined by about a billion Kina to K3.98 billion. Capital spending accounts for 39.1% of total Expenditure. It primarily focuses on PNG Connect, whereas operational expenditures such as wages and salaries and purchasing goods and services account for 44.2% of total spending.

Apart from administration, education accounts for the largest category of spending at 14.1% of total spending. These rivals' resources are allocated to the provinces. Health is 9.5% of the budget, and law and justice accounts for 7.9% of spending. All categories increased in absolute terms this year due to the overall increase in spending.

Table 2: Papua New Guinea Budget 2024

	Kina in millions	% of Expenditure
Total Revenue	23,393.8	..
Total Expenditure - Operational	27,377.6	..
Expenditure - Copensation of Employees - Goods and services	12,091.4 7,034.3 5,057.1	44.2 25.7 18.5
Provincial Transfers	1,535.6	5.6
Interest Payments (Debt services)	3,050.8	11.1
Capital investment	10,699.8	39.1
Fiscal Deficit	-3,983.8	..

Table 3: PNG Budget (by sector) 2024

Sector	Kina in millions	% of Expenditure
Administration	5,012.4	18.3
Community and Culture	214.0	0.8
Economic	1,608.3	5.9
Education	4,081.6	14.9
Health	2,588.5	9.5
Law and Justice	2,164.3	7.9
Miscellaneous	1,361.4	5.0
Provinces	4,081.8	14.9
Transport	2,013.5	7.4
Utilities	1,201.0	4.4
Interest Payment	3,050.8	11.1
Total Expenditure	**27,377.6**	**100.0**

ECONOMIC POLICY RESEARCH

Domestic resource mobilization in the Pacific

Pacific Island Countries(PICs) have faced challenges in mobilizing domestic resources, relying on transfers from development partners and income from tourism and fishing sectors. Public debt increased due to the pandemic, constricting fiscal space and limiting borrowing. To achieve the Sustainable Development Goals (SDGs), PICs must increase fiscal space by mobilizing domestic resources and optimizing expenditure efficiency. Digitalization is a promising reform that can enhance tax administration's effectiveness, transparency, and output, making it a pivotal element in domestic resource mobilization and medium-term revenue strategies. Digital tax administration offers advantages such as decreased corruption, improved tax compliance, and reduced administrative and compliance expenses, contributing to increased tax revenue collection. However, implementation of digital reform can be challenging in developing economies due to a lack of political support, ineffective coordination, and limited human and technological resources.

Source: Asian Development Bank – Pacific Economic Monitor, December 2023

DATA

The table below summarizes Papua New Guinea's critical economic and social indicators underpinning this country brief. These data are taken from several sources and are the latest available. The 2023 data are estimates and are subject to revision.

Table 4: PNG - Key economic and social indicators, 2018 to 2023

	2018	2019	2020	2021	2022	2023
Real GDP growth (%)	-0.8	4.5	-3.5	0.1	4.6	4
Average inflation (%)	4.4	3.9	4.9	4.5	5.3	2.2
Unemployment (%)		...	...	...	...	...
Primary balance (% of GDP)	-0.2	-1.9	-6.2	-4.4	-3.0	-2.2
Public sector debt (% of GDP)	36.7	40.6	48.7	52.2	48.4	52.4
Current account (% of GDP)	2.9	14.8	14.1	12.6	27.9	15.9

*Source: IMF * Assessing the unemployment rate in PNG is challenging because of the lack of data and the dominance of the informal sector. Note: e - estimate; ... - not available*

This Economic Brief, a joint RCO and UNDP product, was prepared in good faith, exercising all due care and attention. The views expressed within are not necessarily the views of the UN and may not represent their policy.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