



Australian
National
University



The University of
Papua New Guinea

2018 PNG UPDATE: PNG IN THE YEAR OF APEC

Professor Stephen Howes and Professor LN Pillai (eds.)

Front Cover:
The UPNG New Lecture Theatre
(Photo: Shannon Young)

Back Cover:
The Hon Charles Abel MP
The Hon Ian Ling-Stuckey MP
Mr Nelson Atip Nema, Mr Rohan Fox, and Professor Stephen Howes
Dame Meg Taylor
(Photos: Shannon Young)

PNG's economy

Mr Ian Ling-Stuckey, Shadow Minister for Treasury and Finance



Welcome,

Acting Vice-Chancellor Malaibe, Professors Lekshmi Pillai and Stephen Howes, distinguished guests, students of PNG and other colleagues.

It's quite an honour to be here today.

Being at this UPNG/ANU Update gives me some hope. As the Shadow Treasurer, I stand in front of you, our country's future leaders, to present an alternative point of view to the Treasurer's earlier presentation. For this is the essence of something vital for the future of our society – the ability to discuss ideas, express different points of view, back up arguments with facts, reasoning and evidence, to allow for constructive criticism. This is a defining feature of a democracy. In our world, my fear is that there is a retreat from these ideas of free, open and respectful discussion. So I congratulate the organisers of this conference, for encouraging discussion and *debate*.

In this presentation, I want to cover a fair bit of ground, so I'll need to move through the following issues quickly. I will give a short introduction about myself, a historic context, some comments on APEC, then an examination of three crises facing PNG today and solutions.

Business perspective and local politician

Some quick background about myself. I'm not an economist. So if you ask some hard, technical questions, I'll have to ask Professor Howes to answer them - I guess a privilege

of being a politician! Rather, the perspective that I bring to the role of Shadow Treasurer, is the pragmatic view of a business person. I'm quite proud that my family has been operating successful businesses in Papua New Guinea for over 80 years-since 1937. Running a business means that you must have a strong vision for what you can offer, it means being realistic and pragmatic in translating your vision to practical implementation, it means being honest if there are problems, and then doing sensible things to fix them. I will bring some of these business perspectives into my presentation.

In addition to being a business person, I am also a politician, currently representing my people from the Kavieng Electorate. I understand the importance of roads, schools and aidposts, even water tanks, to provide reliable drinking water throughout the year. This is my third five-year term in Parliament. I have been a Minister for Mining, Public Services, Commerce and Industry as well as the former governor of New Ireland Province. So I hope I have a perspective from the National through the provincial and district levels, down to the actual village level of our people. And I will reflect on my view of how things are going now relative to previous decades.

Development experience since Independence

Let me put my presentation in a historic context of our development experience since Independence. This helps us better understand our current challenges and the urgency for changing from current policies.

I remember well the joyous days when Independence came to our country. There was a mixture of both joy as well as fear of the unknown as Independence came while I was still in high school.

As I reflect on our development experience, one can understand the disappointment of our people. In terms of both social and economic development, we have not done anywhere near as well as we'd hoped.

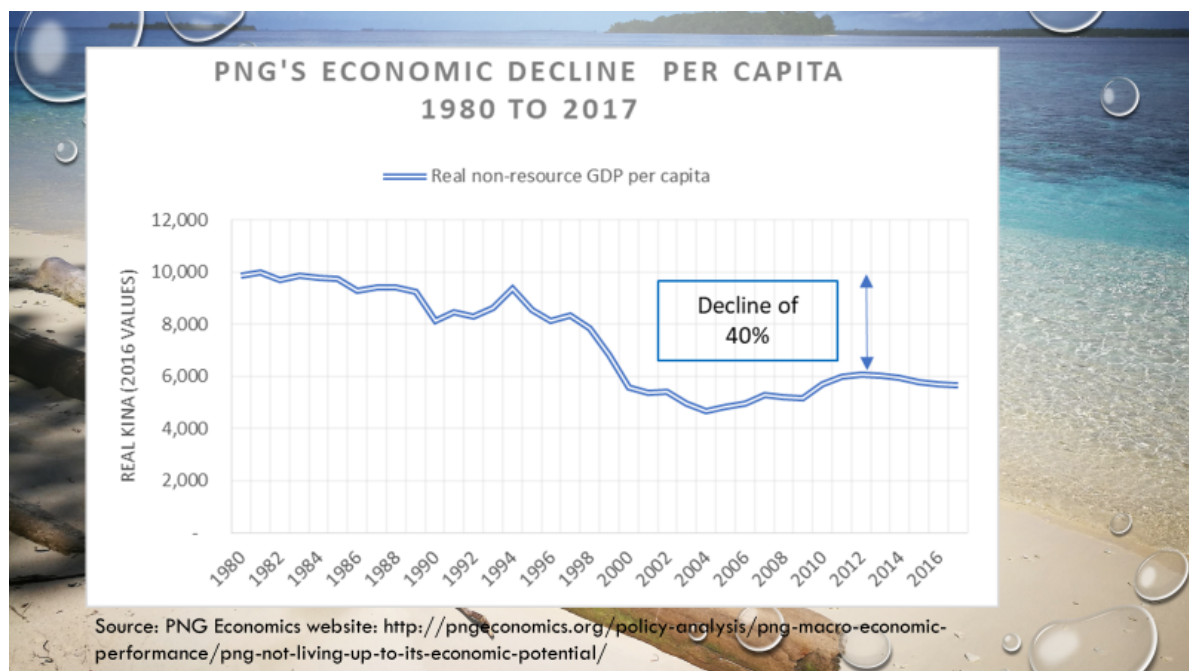


This slide covers some ten social indicators. On most criteria, we are either at or towards the bottom of most social indicators – poverty, stunting, malnutrition, infant and maternal mortality, diseases and basic services.

As a national politician in this country, I look back on this record and collectively, regret to admit, we've let our people down. The first step for changing this poor performance is to acknowledge it. We cannot pretend that things are good and rosy when they are not.

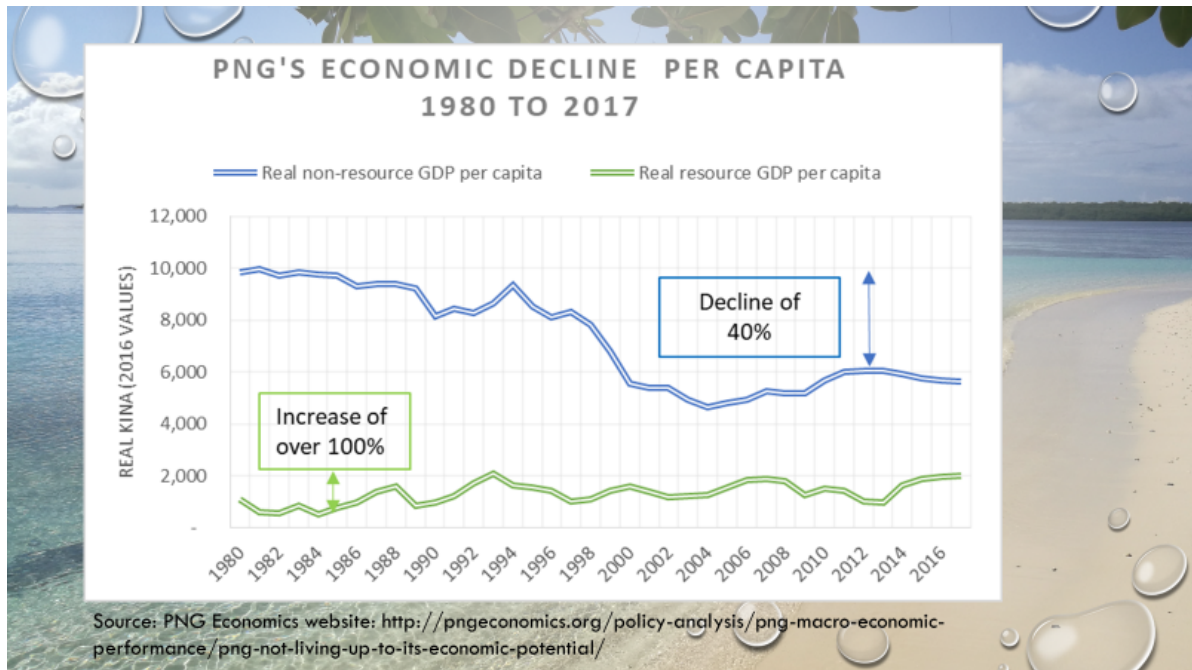
The next slide covers broad economic performance since 1980. This performance is based on measuring real non-resource GDP per capita. The non-resource sector is the focus, as this is where almost all of our economic welfare comes from, for almost all of our people.

The slide shows the terrible drop in average economic welfare in our country. It reinforces and partially helps explain our poor performance on social indicators. The bottom line is that economic welfare has gone backwards by 40% or over a third since Independence. On average, every person alive in PNG is more than one-third worse off than at 1980.



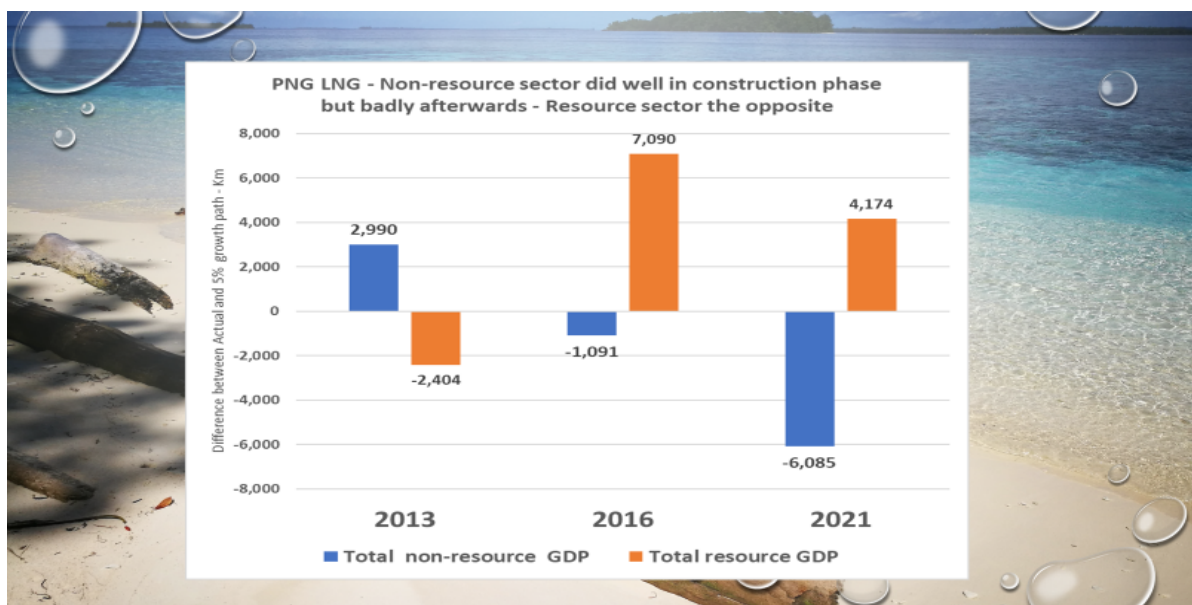
This is a very disappointing economic performance.

You will see from the graph that there was a period of turn-around during the 2000s. Being just a bit political, I note that this period was under a National Alliance government, building on the reforms of former Prime Minister Morauta. However, this upward trend has now been lost. We are going backwards again in per capita terms. Unfortunately, the people of PNG have not been told how badly things have been going in recent years. There has been a regular pattern of either not providing information or of putting a very rosy set of coloured glasses over possible numbers.



In contrast, the resource sector has done well – it has increased by over 100% per capita. But PNG is a highly dualistic economy – so what is good for the resource sector may not translate to what is good for the rest of the economy on which our people's livelihoods depends.

The most recent experience of the PNG LNG project highlights a possible adverse policy cycle loop between big resource projects and the rest of the economy. While still assessing the full details of the recent Jubilee Australia report, on the PNG LNG project, there does seem to be some logic here. While the non-resource economy did well during the construction phase, growth is now at very disappointing levels. Even official government figures project growth rates of some 2.5% per annum – this is pitiful, and less than population growth.



So how is this possible? Such a project should help the economy along. And of course there are hundreds of examples of benefits from the PNG LNG project – whether it be more local jobs than initially expected, or the help that Oil Search provides to the Tari hospital, or the contracts that are provided to local contractors (especially landowner companies).

Resource curse again

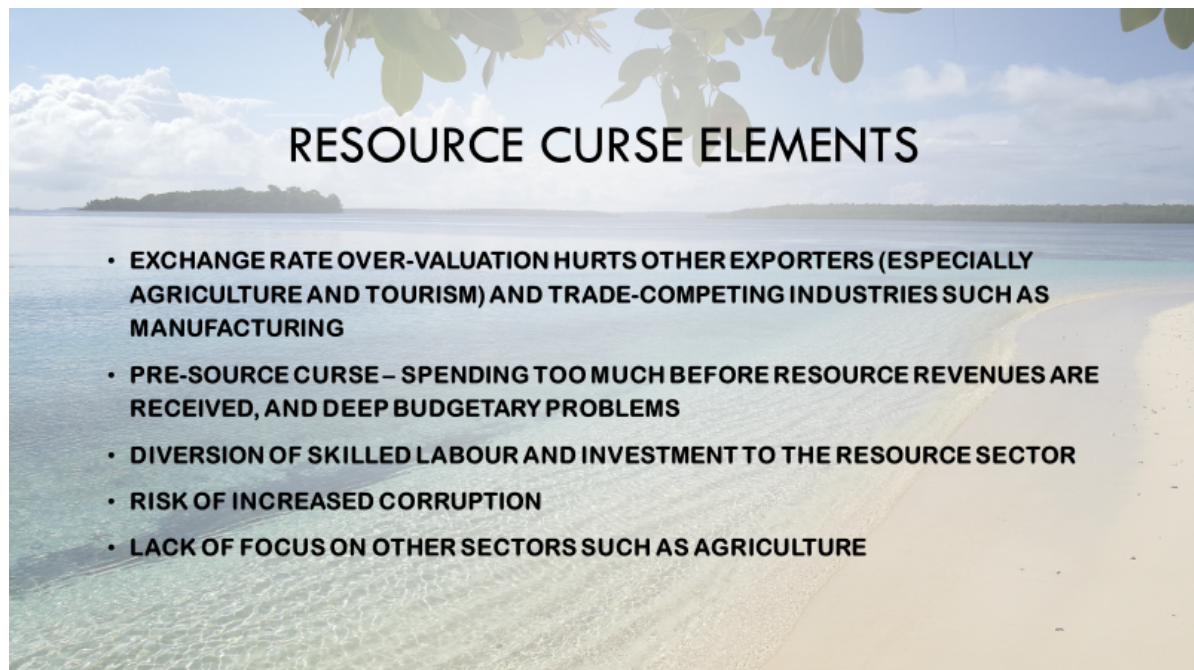
But the big picture perspective is that the non-resource economy is now performing worse than it was before the PNG LNG project. Why is this so?

The likely explanation is that PNG has fallen into what is known as the resource curse, yet again.

So despite what should be the great gains of natural resource wealth, the experience in PNG and many other countries, is that such wealth makes for poor economic outcomes.

Some of these resource curse distortions flow from the exchange rate – it becomes over-valued and hurts other traded sectors such as agriculture and manufacturing.

Some of the distortions result from what the International Monetary Fund (IMF) calls the “pre-source curse” – poor budget policy of rapidly increasing expenditure on false revenue assumptions – encouraged by some resource companies in their promises. PNG has had its worst experience since Independence, of irresponsible budget policy with budgeted expenditure increasing by an extraordinary 50% over the 2013 and 2014 budgets and a subsequent huge build-up in debt.



But there are also more subtle impacts of the resource curse. Skilled resources are attracted to the resource sector. The concentration of large profits increases the risk of

corruption. My concern, reflecting on my experiences starting from 1997, is that these corruption pressures are becoming worse.

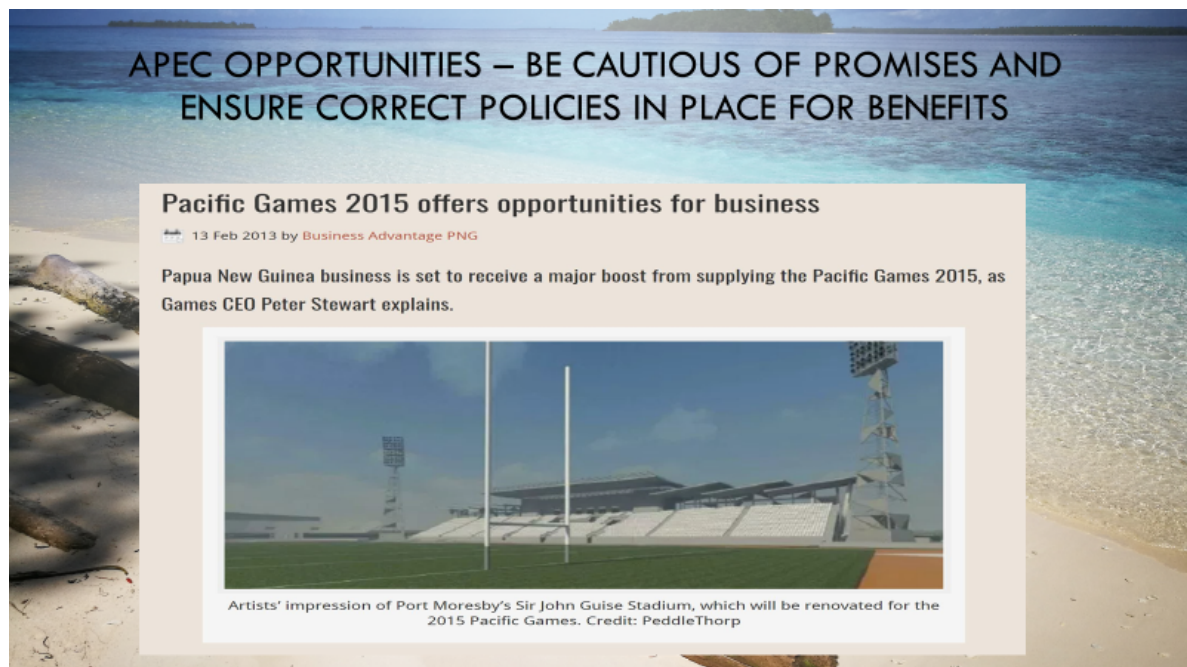
Too much focus is given to the resource sector. The political priority becomes securing the next resource project. For example, the Prime Minister recently announced the PNG negotiating team for the new Papua LNG project which includes the heads of Treasury, Prime Minister and NEC, along with relevant heads of resource agencies. Where is there a similar committee that meets regularly, to consider how to improve the agriculture sector – the key for the livelihoods of most of our people.

Good government means staying always focused on those areas that are most important for our people – and ultimately, that must come back to supporting our agriculture sector.

APEC opportunities

As the theme of this conference is around APEC, some quick comments. The Alternative Government believes that we must try and get the best out of the opportunities of APEC. There are real possibilities for showcasing our country. We are very willing to work with the government, to get the most out of this very expensive meeting.

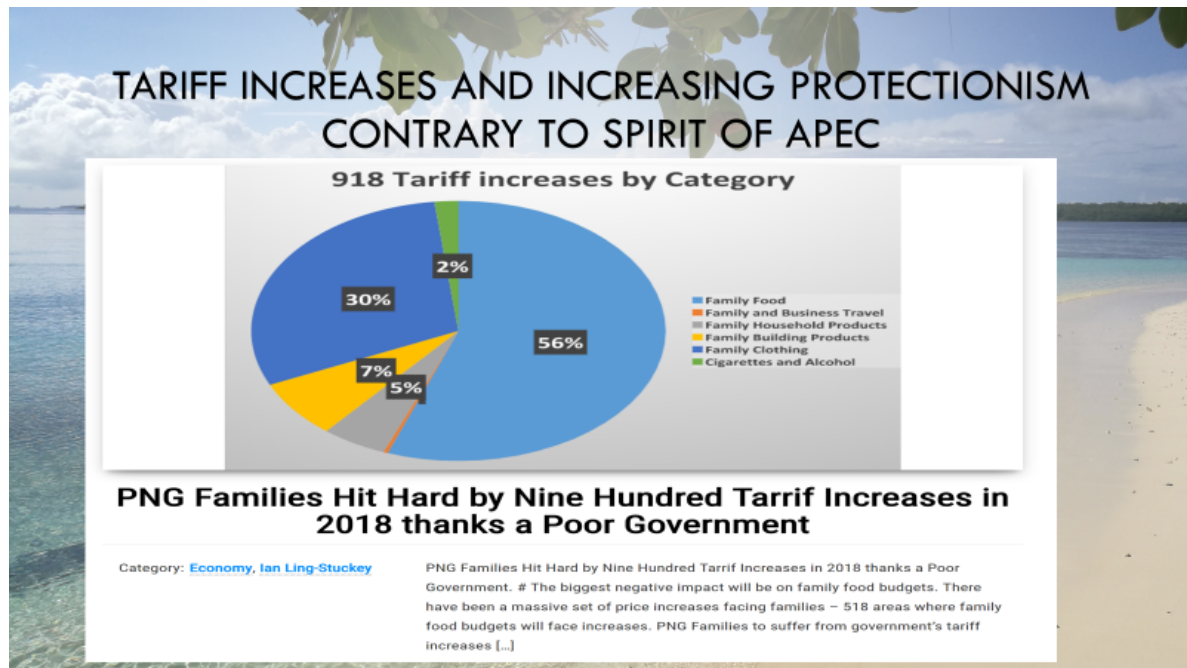
And this is an issue– APEC will be an expensive meeting, both in terms of actual expense to PNG and other donors, but also in terms of being a major distraction to other policy priorities.



One warning is “Beware of false promises”. This slide shows some false promises around the South Pacific games. Now I’m a supporter of such games – and I’m proud that I was able to win three gold medals for our country, in the 1983 and 1987 South Pacific games. But the costs of the most recent games were over the top – and we are

still waiting for some of the buildings to be completed. We must be realistic in our expectations.

There is also the hypocrisy of our hosting a meeting, which has its focus on building trade and investment links between countries, while PNG introduced over 900 tariff increases. We are becoming less open to trade in both a policy sense, as well as in reality, because of the foreign exchange shortages.



The real issue for PNG and APEC is “What else could we have done instead?” APEC may be a positive for the country, but the real cost of APEC means a lack of focus on other areas, to advance our people’s well-being.

I have no doubt that visiting APEC delegations will be enormously impressed with PNG and what it has to offer. But we need the policies in place to translate this opportunity into reality. Unfortunately, PNG does not have the right policies in place to encourage investment.

Jobs and growth

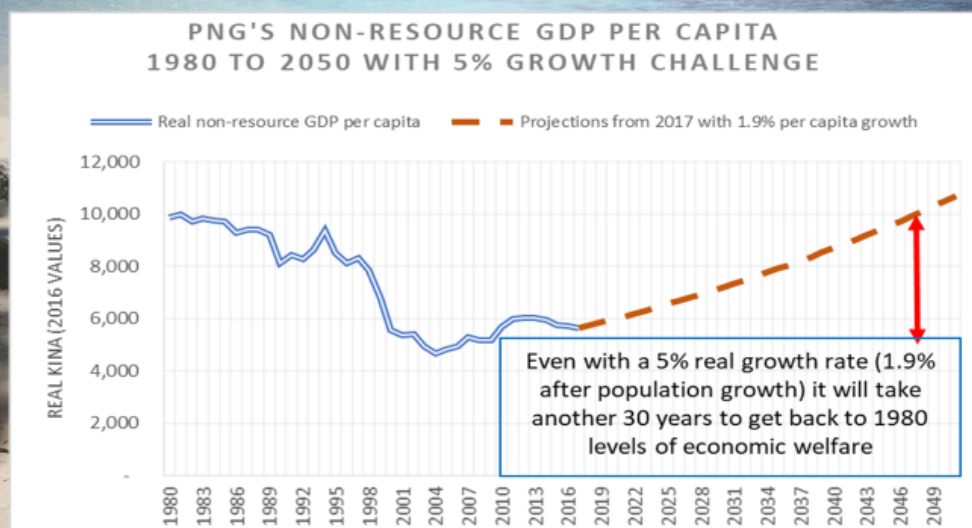
So what policies are needed to encourage investment and tap into the opportunities of APEC?

JOBS AND INCOMES ACTIONS

- **DIFFERENT PHILOSOPHY OF ECONOMIC DEVELOPMENT BASED AROUND ECONOMIC EMPOWERMENT FOR ITS PEOPLE RATHER THAN BIG GOVERNMENT. FOR EXAMPLE, THE ALTERNATE GOVERNMENT WOULD:**
 - REDIRECT FUNDS GOING TO THE PROPOSED EQUITY INVESTMENTS IN BIG AGRICULTURAL ENTERPRISES OWNED BY THE GOVERNMENT'S BESTIES AND INSTEAD PUT THIS MONEY INTO IMPROVING AGRICULTURAL EXTENSION SERVICES FOR SMALL-HOLDER CASH CROPPING FARMERS;
 - PUT ROAD INFRASTRUCTURE FUNDING INTO RURAL AREAS RATHER THAN PORT MORESBY;
 - GET INCENTIVES RIGHT FOR BUSINESS RATHER THAN IMPOSING LARGE TARIFFS THAT HURT THE COST OF LIVING;
 - DEAL WITH THE FOREIGN EXCHANGE SHORTAGES WHICH ARE KILLING BUSINESS GROWTH.
- **5% INCOME GROWTH TARGET (REAL NON-RESOURCE GDP PER ANNUM) WITHIN 3 YEARS – UP FROM 2%. NA DID THIS IN THE 2000S IN RECOVERING FROM 90S CRISIS AND CAN DO IT AGAIN.**
- **SME AND INFORMAL SECTOR FOCUS THROUGH BETTER BUSINESS ENVIRONMENT – BETTER ACCESS TO CREDIT, BETTER REGULATION, EASIER TO SET UP A BUSINESS, EASIER TO TRUST CONTRACTS, - MEASURED BY IMPROVING PNG'S RANKINGS ON EASE OF DOING BUSINESS FROM 119TH TO 100TH OF 190 COUNTRIES WITHIN 5 YEARS.**

Fundamentally, we need policies that can lift PNG's growth in non-resource GDP to at least 5% per annum. This is the minimum required to start getting jobs growth going again, and to boost government revenues to help meet our urgent development needs. Even a 5% real non-resource GDP target is only a small level above our population growth rate of 3.1% - a level that is too high and should be reduced to more sustainable levels.

A LONG ROAD BACK TO IMPROVEMENTS



This will be a long trek. So as indicated by the dashed red line, it will take about another 30 years just to get back to the level we had in 1980 – to recover from having gone backwards by a third. Possibly we should set our sights even higher, but as a pragmatic

business person, given our recent history, we should start to walk before we try and run.

So how are we doing? We have heard one view this morning that there are economic challenges driven primarily by the fall in commodity prices. The argument was that things are now being done to fix things, and despite low growth projections of only 2 to 3% for the next few years, there is a possible boom ahead following the APEC meeting and new resource projects.

My message is a much more cautious one. Things in PNG have not been going well. We don't know how bad things are because key pieces of information are being suppressed, or we have simply stopped measuring certain inconvenient facts. Talk of a super-cycle from new projects raises the risk again, of yet another boom/bust cycle and falling further into the resource curse.

The next slide highlights some of the current problems. Three years out from the fall in commodity prices, we are still struggling. At some time, and this should have been two years ago, the government should have stopped blaming the fall in commodity prices or the drought. Remedies have taken too long and our people continue to suffer.



2015 AND 2017 - WORRYING RECENT DEVELOPMENTS

- PNG'S NATIONAL STATISTICS OFFICE TOOK NEARLY 10% OFF THE ESTIMATED SIZE OF THE PNG ECONOMY FOR 2015, REDUCING IT FROM K62.3 BILLION (PNG 2018 BUDGET FIGURE) DOWN TO K57.1 BILLION.
- NOMINAL GDP GROWTH WAS SLASHED FROM 9.8% TO ONLY 0.7%, AND AFTER ALLOWING FOR PNG LNG EXPORTS INCREASING BY K4.2 BILLION, THIS MEANS THE NON-RESOURCE SECTOR MUST BE IN A SEVERE RECESSION – PROBABLY GOING BACKWARDS BY WELL OVER 5% AFTER ALLOWING FOR INFLATION. BUT THE GOVERNMENT IS HIDING THESE FIGURES AND REFUSING TO RELEASE THE FULL SET OF TABLES.
- FOR 2018, THE CENTRAL BANK GOVERNOR IN HIS MONETARY POLICY STATEMENT SAID GDP GROWTH SHOULD BE HIGHER THAN THE PNG TREASURY ESTIMATE AT 3%, BUT MOODY'S INTERNATIONAL RATING AGENCY EXPECTED THE FIGURE WOULD BE ONLY 0.5% IN 2018, AND THE ASIAN DEVELOPMENT BANK RELEASED A GROWTH ESTIMATE OF ONLY 1.8% IN THE LATEST ASIAN DEVELOPMENT OUTLOOK PUBLICATION.
- THE S&P CREDIT RATING AGENCY DOWNGRADE IS A REAL KNOCK TO THE PNG ECONOMY. IT IS ONLY THE SECOND TIME THAT PNG'S CREDIT RATING HAS BEEN DOWNGRADED BY S&P – THE FIRST TIME WAS IN AUGUST 2001 AS PNG STRUGGLED WITH THE LATE 1990S CRISIS.
- THE GOVERNMENT IS NOT DOING ENOUGH ABOUT THE FOREIGN EXCHANGE CRISIS. BPNG GOVERNOR CLAIMING THEIR WILL BE A BALANCE OF PAYMENTS SURPLUS OF K1.5 BILLION IN 2018. BUT THIS WAS BEFORE THE EARTHQUAKE, AND LOSS OF 2 MONTHS OF PNG LNG EXPORTS OF K2 BILLION, THE MOST LIKELY OUTCOME IS NOW A LOSS OF K500 MILLION IN FOREIGN EXCHANGE RESERVES.
- TREASURER ABEL IS CLAIMING THE IMF HAS ENDORSED ITS MEDIUM-TERM FISCAL STRATEGIES, BUT THE 2018 BUDGET OVER-SPENT THE IMF'S UNDERSTANDINGS BY K2 BILLION, AND THEN INVENTED FAKE REVENUE OF AT LEAST K1.5 BILLION ABOVE ITS OPTIMISTIC SCENARIO.
- THE TREASURER SAYS THEY KEPT TO THE 2.5% DEFICIT FIGURE IN 2017, BUT THIS IS A FICTION AND REFLECTS AN INCREASING TENDENCY TO FIDDLE THE BOOKS. IN PARLIAMENT, WE HAVE HAD TWO GOVERNMENT MINISTERS ADMIT THAT THERE ARE MASSIVE UNPAID BILLS – OVER K700 MILLION IN PUBLIC WORKS ALONE – AND THIS LEADS TO MIS-REPRESENTING THE TRUE STATE OF PNG'S PUBLIC FINANCES.
- AND AS A TRUE SIGN OF HOW THE PRIVATE SECTOR IS STILL STRUGGLING AND HAS LOST CONFIDENCE IN THE WORD GAMES OF THIS GOVERNMENT, PRIVATE SECTOR CREDIT-LOANS FOR BUSINESS INVESTMENT AND HOUSING, DECREASED BY 3.4% IN 2017 EVEN BEFORE ALLOWING FOR INFLATION.

How are we viewed externally? In March and April, so after the 100 Day Plan, after the 2018 Budget, and after the early release of the 2017 Final Budget Outcome, two international credit ratings that survey our economy have either downgraded PNG's credit rating or put us on negative watch. This has never happened before. People looking from the outside are looking through budget numbers and saying things are not going well, and they don't trust the current government's so-called fixes.

HISTORIC CREDIT RATINGS DOWNGRADE – OUTSIDERS ARE LOOKING THROUGH FAKE FIGURES

Papua New Guinea - Credit Rating

Standard & Poor's credit rating for Papua New Guinea stands at B with stable outlook. Moody's credit rating for Papua New Guinea was last set at B2 with negative outlook. In general, a credit rating is used by sovereign wealth funds, pension funds and other investors to gauge the credit worthiness of Papua New Guinea thus having a big impact on the country's borrowing costs. This page includes the government debt credit rating for Papua New Guinea as reported by major credit rating agencies.

Agency	Rating	Outlook	Date
S&P	B	stable	Apr 16 2018
Moody's	B2	negative	Mar 23 2018
Moody's	B2	stable	Apr 25 2016
TE	35	stable	Apr 16 2016
Moody's	B1	negative watch	Feb 25 2016
S&P	B+	negative	Oct 08 2015

Our required actions to get growth going again, and to make the best of the opportunities of APEC, can be found in recent surveys about what makes it hard to do business in PNG.

According to our Institute for National Affairs, the latest business survey indicates the greatest current barrier to doing business in PNG is foreign exchange shortages. Having to go begging to your bank for even basic payments to overseas customers, makes it really hard to grow your business - or just keep afloat! Additionally, any business person who currently invests in this country cannot take any profits back out. People will simply not invest in PNG, at the level we want, if people can't get their money back out. An APEC meeting does not deal with this fundamental barrier to investment.

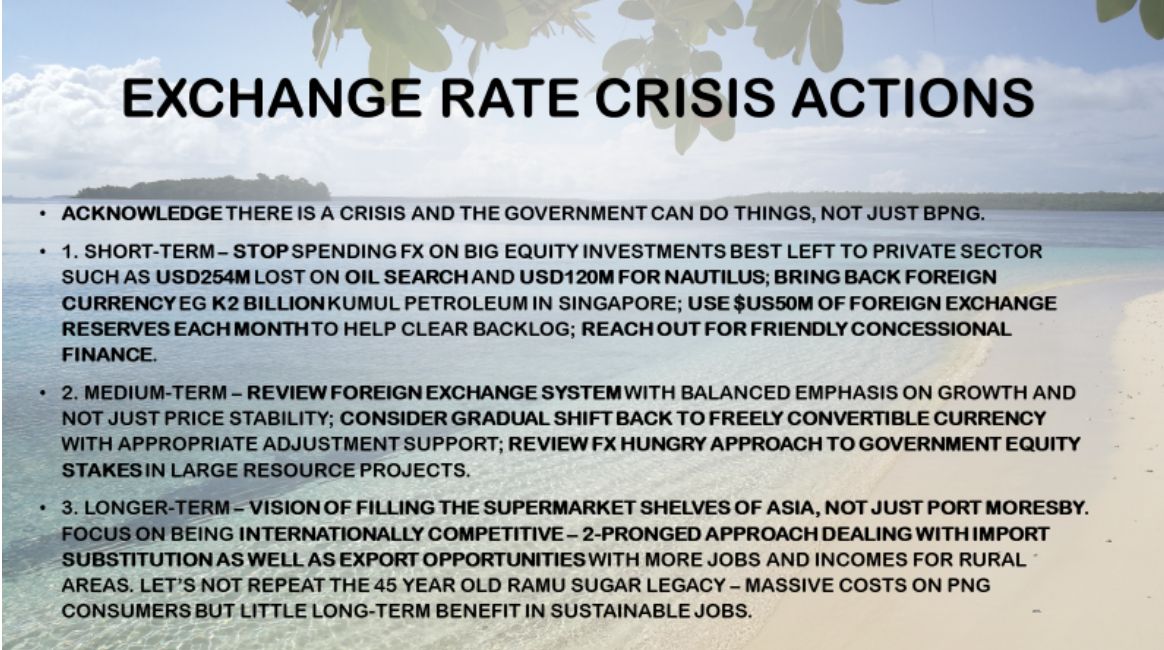
Decisions on investment also must be realistic about other barriers to doing business in PNG. There is a need to sit down with the business community and identify the highest priority five things that can be done to start improving business conditions. Sometimes these changes will be simply about making better regulations. Some actions will require longer-term planning, such as building our police force up to the average per capita size of other countries, and undertaking a major infrastructure program.

A sad fact is that in 2017 lending to the private sector actually fell by 3.4% - so a decline of around 8% after allowing for inflation of 4.7%. Turning this around can include specific actions. However, fundamentally this is about trust. We need to re-build trust – trust that the government procurement system will not be manipulated to serve the interests of besties; trust that if one has a business contract, that payments will be made; trust that power and water will be available at reasonable prices; trust that foreign exchange is freely convertible; trust that taxes won't suddenly be increased to unreasonable levels. People have lost trust in this government.

Exchange rate crisis

This conference will certainly cover the ongoing foreign exchange crisis in later presentations. Suffice to say that, 70% of PNG business CEOs regard it as the greatest barrier to doing business in PNG. This is the crisis that was most avoidable. Why on earth did Bank of Papua New Guinea (BPNG) move away from a fully convertible currency in June 2014? While easily avoidable then, nearly four years later, it is now much harder to fix.

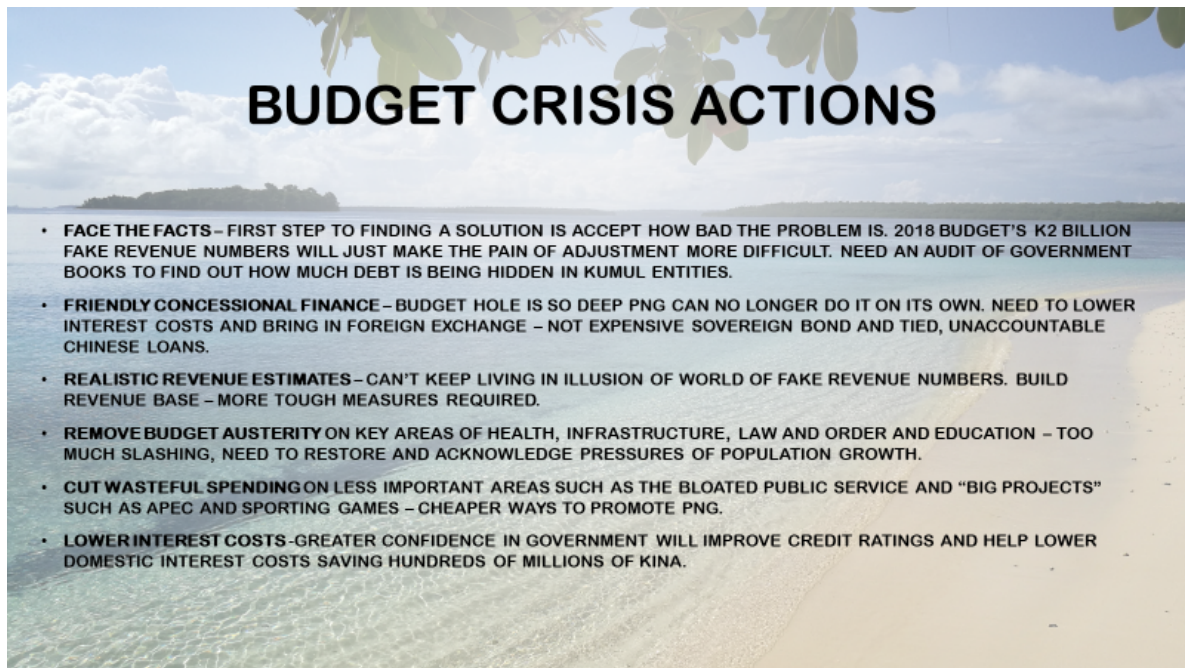
Once again, the Alternative Government has a set of policies to correct the problem – some short-term, some longer-term. These are set out in this slide. For example, there is scope to immediately release \$US50 million per month of foreign exchange reserves as we transition back to a more fair value exchange rate over 12 months. We need to review our Central Bank Act, as clearly it has not served us well enough over the last six years, as reflected by foreign exchange shortages, lack of growth in private sector credit, and declining central bank independence, reflected by its printing of money to fund the deficit through the “slack arrangement”. We need to re-shape our economy so that it is more growth orientated and more open and truly willing to engage in international trade, in line with APEC goals. Our vision is PNG filling the supermarket shelves of Asia with PNG produce, not just the shelves of Port Moresby.



EXCHANGE RATE CRISIS ACTIONS

- **ACKNOWLEDGE THERE IS A CRISIS AND THE GOVERNMENT CAN DO THINGS, NOT JUST BPNG.**
- **1. SHORT-TERM – STOP SPENDING FX ON BIG EQUITY INVESTMENTS BEST LEFT TO PRIVATE SECTOR SUCH AS USD254M LOST ON OIL SEARCH AND USD120M FOR NAUTILUS; BRING BACK FOREIGN CURRENCY E.G. K2 BILLION KUMUL PETROLEUM IN SINGAPORE; USE \$US50M OF FOREIGN EXCHANGE RESERVES EACH MONTH TO HELP CLEAR BACKLOG; REACH OUT FOR FRIENDLY CONCESSIONAL FINANCE.**
- **2. MEDIUM-TERM – REVIEW FOREIGN EXCHANGE SYSTEM WITH BALANCED EMPHASIS ON GROWTH AND NOT JUST PRICE STABILITY; CONSIDER GRADUAL SHIFT BACK TO FREELY CONVERTIBLE CURRENCY WITH APPROPRIATE ADJUSTMENT SUPPORT; REVIEW FX HUNGRY APPROACH TO GOVERNMENT EQUITY STAKES IN LARGE RESOURCE PROJECTS.**
- **3. LONGER-TERM – VISION OF FILLING THE SUPERMARKET SHELVES OF ASIA, NOT JUST PORT MORESBY. FOCUS ON BEING INTERNATIONALLY COMPETITIVE – 2-PRONGED APPROACH DEALING WITH IMPORT SUBSTITUTION AS WELL AS EXPORT OPPORTUNITIES WITH MORE JOBS AND INCOMES FOR RURAL AREAS. LET'S NOT REPEAT THE 45 YEAR OLD RAMU SUGAR LEGACY – MASSIVE COSTS ON PNG CONSUMERS BUT LITTLE LONG-TERM BENEFIT IN SUSTAINABLE JOBS.**

Budget crisis



Almost every day when we wake up there is a further sign of this country's budget and cash crisis – teachers not being paid, shortages of medicines, contractors not being paid, departments being locked out due to non-payment of rent, Tuition Fee Free (TFF) payments running months and months late. PNG is facing a massive cash crisis – one that has been going on for years - and one that has been going on for too long!

The underlying cause is, of course, poor budget policy. PNG has had its largest set of budget deficits in its history, over the last six years. This has inevitably increased debt massively (from K8.0 bill in 2012 to K24.0 bill in 2017). It has also increased interest costs from under K400m per annum in 2012, to over K1,600 million in 2017. And that is only the debt we know about! We know that more debt is hidden in State Owned Enterprises, and there are other unfunded liabilities such as superannuation for our public servants.

Unfortunately, the solution here is made more complicated because the budget numbers have become increasingly untrustworthy. As some of you may know, the Alternative Government considers the 2018 budget to be built on unrealistic revenue projections – this is why we claim it is a fake budget. The detailed reasons for this are set out in my 2018 budget reply speech. The more recent Final Budget Outcome statement is also of great concern. Politically, it is simply too convenient to meet a detailed number such as 2.5% budget deficit within 0.1%. Inap Nau! I know that that the Treasurer would simply claim good management, but I know that there are big games that can be played in a cash based budget, by simply delaying paying for expenditures, delaying tax refunds and deciding not to pay for some important things such as superannuation and education.

MASSIVE BUDGET CUTS IN KEY SECTORS SINCE 2015



We also need to be spending funds effectively, accountably and on the right things. This slide shows extraordinary cuts in health, education, infrastructure spending and law & justice since 2015, which are undermining key investments in our country's future. Although the 2018 budget claimed it will restore some health funding, it will most likely lack the revenue to do so.

Instead, we have seen massive increases in pay for public servants, and a massive increase in interest costs. These are not priority areas – they ultimately represent serious economic mismanagement.

There has also been a major increase in district support programs. I am a supporter of such programs – I believe that these funds can be spent well and more in line with local needs, especially given the demonstrated failure at the national level. However, there must be good management of these funds and much better accountability for how the funds are used. I personally think it's time for a review of the District Support Improvement Program (DSIP), and fast!

Alternative Government policies

I do not want to be too political today. I do, however, encourage students to read the detailed policies the Alternative Government is proposing, to deal with our jobs and growth crisis, our foreign exchange crisis and our budget crisis. More detail is provided in my budget response speech. More detail on government policies is also provided on the Alternative Government website.



Conclusion

There is no magic wand. Our problems are deep – and they have been building up and distorting incentives for the last six years. Taking an even longer perspective, PNG started on a development path that has, for too long, put too much hope on the resource sector or some grand project, such as an APEC meeting.

We need a better development path, one that puts the emphasis back on inclusive development and our people. We need to escape from the resource curse. Fundamentally, this means we must do much more for our agriculture sector, including our subsistence agriculture sector. This will require better policies than the current economic mismanagement.

It will also require more local leaders and honest leaders, who are genuinely interested in the wider well-being of our people. It will require more economists and other professions that can be trained, and then learn to speak out. Such people are in this room. You are our future. May you study hard, and bring a passion for making a better PNG!

When you're visiting Kavieng next, on your break, send me a text and perhaps, join us for a swim at beautiful Lemus Island.

It was nice coming back here today. Thank you.



Australian
National
University



The University of
Papua New Guinea