

WESTPAC PNG

Economic Bulletin –

February 2023

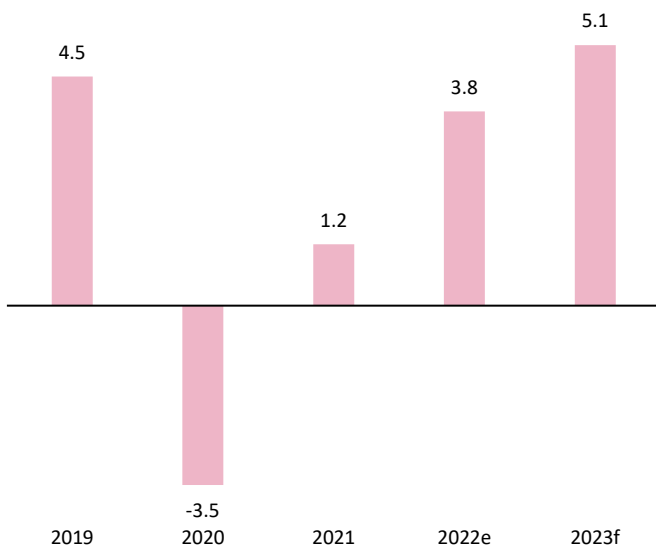
KEY HIGHLIGHTS

- Global economy remains fragile with a dampened outlook for 2023.
- Nonetheless, PNG economy continues to make strides towards recovery.
- The progressive dynamics in 2021 and 2022 have set the tone and momentum for further optimistic outcomes in 2023.
- Real GDP is projected at around 5.1% for 2023 following an estimated firm growth in 2022.
- Excess liquidity in the banking system remains high and financial sector is stable.
- The war in Ukraine is impacting PNG through higher commodity prices and higher inflation, with the former leading to a stronger balance of payments and fiscal revenues, given that PNG is a large commodity producer.
- Foreign reserves remain comfortable.
- Inflation is currently high but is expected to moderate in 2023.
- Risk to the growth outlook remain.

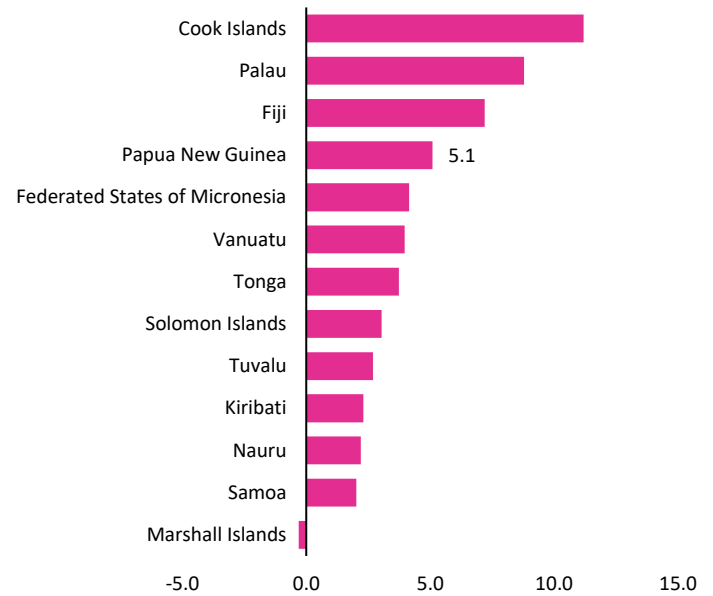


PNG Economy Summation (GDP, Inflation and Current Account)

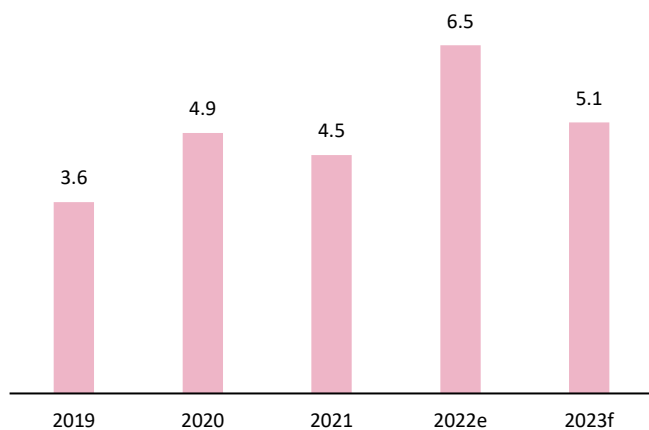
GDP Growth Rate: Papua New Guinea
(% per year)



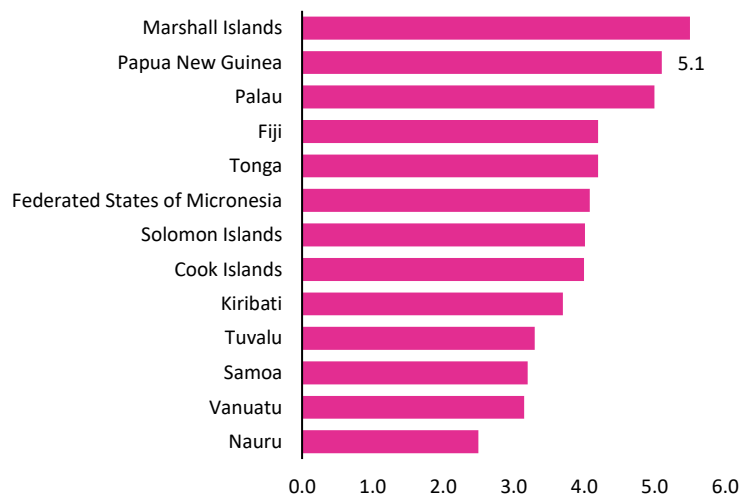
Comparative GDP forecasts (%)



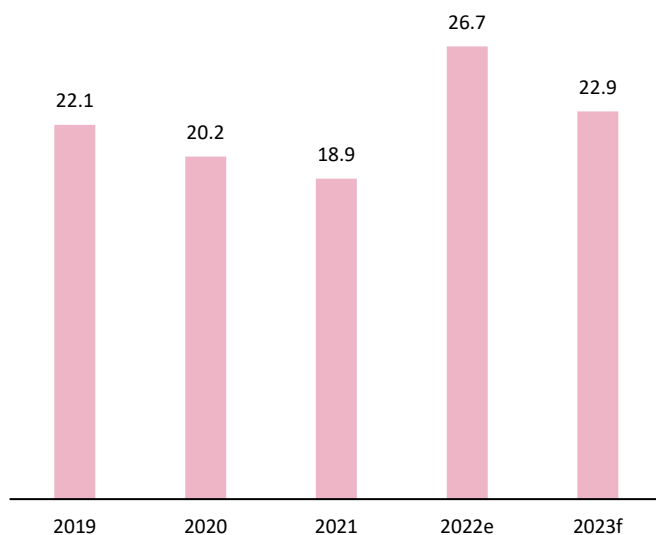
Inflation Rate: Papua New Guinea
(% per year)



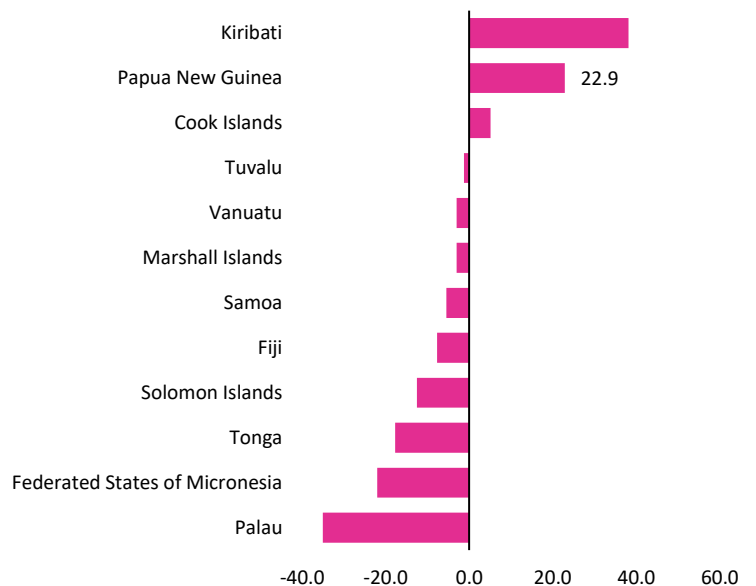
Comparative Inflation forecast (%)



Current Account Balance: Papua New Guinea
(% of GDP)



Comparative Current Account Forecast (% of GDP)



Source: IMF, ADB and Westpac Calculations

Economic Outlook in PNG remains positive for 2023

Globally, the world economy remains in a fragile state.

The global fight against inflation, Russia's war in Ukraine, and a resurgence of COVID-19 in China weighed on global economic activity in 2022, and the first two factors will continue to do so in 2023. The rise in central bank rates to fight inflation and Russia's war in Ukraine continue to weigh on economic activity. The rapid spread of COVID-19 in China dampened growth in 2022, but the recent reopening has paved the way for a faster-than-expected recovery. Taking the above into account, the International Monetary Fund (IMF) in its latest World Economic Outlook (WEO) project global growth to fall from an estimated 3.4 percent in 2022 to 2.9 percent in 2023, then rise to 3.1 percent in 2024. Global inflation is expected to fall from 8.8 percent in 2022 to 6.6 percent in 2023 and 4.3 percent in 2024, still above pre-pandemic (2017–19) levels of about 3.5 percent.

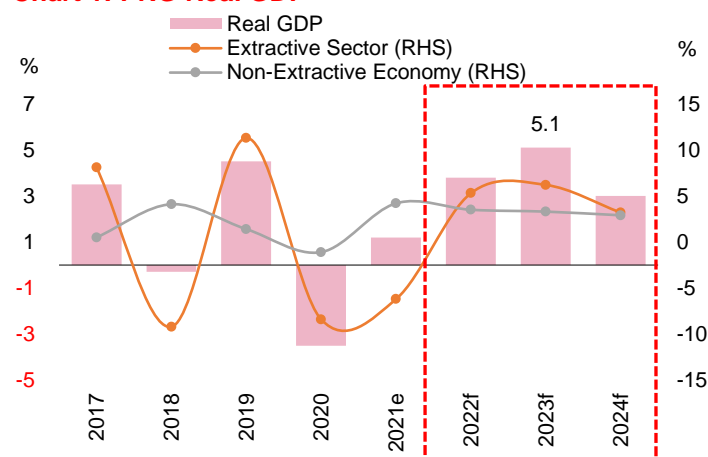
While its already looking like another challenging year for the global economy, the Papua New Guinea (PNG) economy seems to be well placed for continued recovery in 2023.

The improvement in COVID-19 situation and the successful general elections in PNG has given an uplift to economic activity in the country. Domestically, PNG economy has made good progress in business activity supported by strong performance of the non-extractive sector (agriculture), pointing towards resilience despite growing inflationary pressures. After making a rebound in 2021, the PNG economy is estimated to have grown further in 2022 with an estimated real GDP growth of around 4.0 percent, largely driven by increases in international prices, emanating from the Russia-Ukraine war, and higher production of both mineral and non-mineral commodities. The projected increase in activity in the manufacturing, wholesale, retail, transportation, and hotels and accommodation sectors following the impact of COVID-19 and higher spending by the Government will also supported growth. Additionally, supporting this outcome is the labour market which noted improvement in 2022 as total employment in the private sector increased by 2.3 percent in the first half of the year and estimated to have growth further in the second half of the year post the general elections, reopening effect and further ease in COVID environment.

Leading on from the progressive dynamics in 2021 and 2022 have set the tone and momentum for further optimistic outcomes in 2023. Despite the challenging external environment, the economic outlook in PNG remains positive, underpinned by an ongoing projected recovery in the extractive sector, higher commodity prices, and gradual recovery in economic activity. Agriculture will remain among the key contributors to the economic recovery in 2023. The other major sectors to drive growth in 2023 include manufacturing, wholesale, retail, transportation, construction, real estate and hotels & accommodation sectors. As such, the real GDP for the PNG economy is

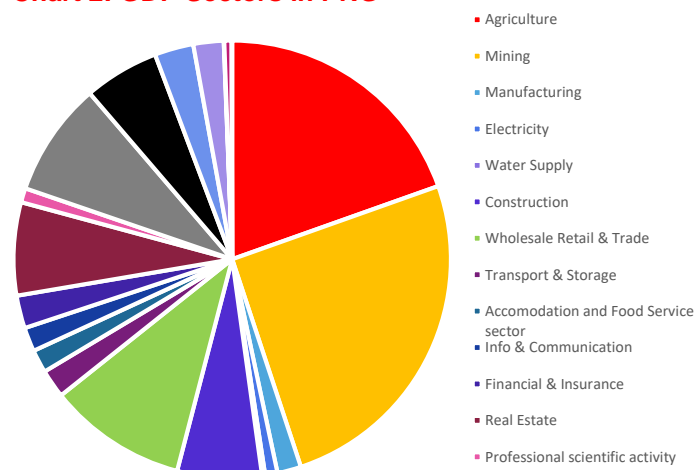
expected at around 5.1 percent for 2023¹, (IMF, October 2022, World Economic Outlook).

Chart 1: PNG Real GDP



Source: Internal Agency

Chart 2: GDP Sectors in PNG



Source: PNG National Statistics Office

Fiscal response has played a crucial role in the recovery of the PNG economy through the last two years.

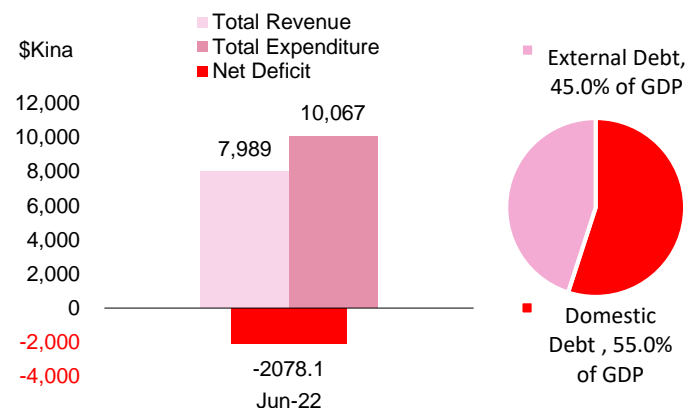
The preliminary fiscal operations of the National Government over the six months to June 2022 show a deficit of K2,078.1 million, compared to a deficit of K2,690.5 million in the corresponding period of 2021. The lower deficit reflected improvement in revenue. Total revenue and grants was K7,988.9 million over the six months to June, 45.1 percent higher than in the corresponding period of 2021 and represents 49.3 percent of the 2022 Budget amount. The outcome reflected higher tax revenue. Total expenditure was K10,067.0 million over the six months to June 2022, 22.8 percent higher than in the corresponding period of 2021 and represents 45.4 percent of the 2022 Budget. This was due to higher recurrent expenditure and interest cost. The developments in the revenue and expenditure in the June quarter resulted in a deficit of K2,078.1 million. The deficit was financed mainly from domestic sources totalling K2,264.0 million, which more than offset the net external loan repayment of K185.9 million. Net domestic financing comprised of K2.4 million, K1,139.6 million, K4.9 million,

¹ The extractive sector continued weak performance driven by disruptions to mining operations. The ongoing shutdown of the Porgera mine was a key driver of this result,

along with disruptions to production in the Lihir, OK Tedi, and Simberi mines. Porgera mine is expected to reopen in 2023 with subsequent impact on growth in 2023.

and K1117.1 million from BPNG, other depository corporations, other financial corporations and other resident sectors. Total public (Government) debt outstanding was K50,568.2 million as at end of June 2022, an increase of K2,194.1 million from the March quarter, and represented 45.8 percent of gross domestic product. This comprised of K27,823.5 million in domestic debt and K22,744.7 million in external debt.

Chart 3: Fiscal Performance June 2022



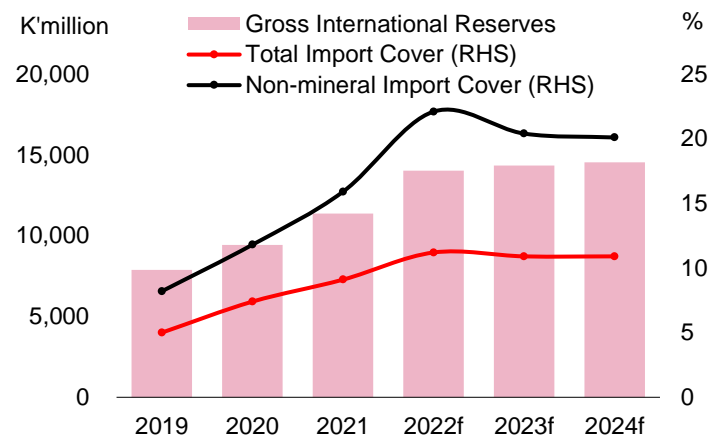
Source: Bank of Papua New Guinea

With the Government's expansionary fiscal policy and significant increase in foreign currency inflows from higher commodity prices, the growth in the money supply and monetary base are projected to increase.

This is expected to result in high deposits and liquidity in the banking system, which are already at very high levels. Excess liquidity in the financial system has also helped to lower domestic interest rates and supports funding conditions for the government. Credit growth is estimated to have increased in 2022 on the back of commercial bank lending to public non-financial corporations, other financial corporations, and other resident sectors. Going forward with pickup in demand, credit growth is anticipated to increase further in 2023.

Externally, the Russia-Ukraine war has impacted favourably on the prices of major export commodities such as crude oil, LNG and condensate, with an overall balance of payment (BOP) surplus. Latest statistics shows that the overall BOP recorded a surplus of K239.8 million in the first half of 2022, compared to a deficit of K812.8 million in the corresponding period of 2022. This outcome was due to a surplus in the current account, which more than offset a deficit in the capital and financial account. The surplus in the current account was driven mainly by higher production and international prices of all major export commodities, and easing of supply constraints, following the lifting of the COVID-19 restrictions. The level of gross foreign exchange reserves at the end of June 2022 was K10,563.3 (US\$3,052.8) million, sufficient for 9.2 months of total and 16.3 months of non-mineral import cover and is expected to remain at comfortable levels in the medium term.

Chart 4: Foreign Reserves

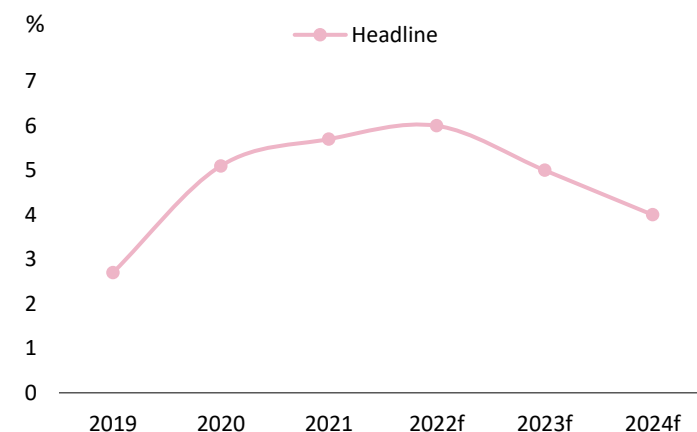


Source: Bank of PNG

Inflation remains a challenge although expected to moderate this year.

The feed-through of the high level of global inflation to domestic prices has resulted in an increase in the Consumer Price Index of 5.5 percent in the June quarter of 2022. According to Bank of PNG annual headline inflation is estimate to have remained elevated in 2022 and is expected to ease over the medium term. High inflation has increased costs for businesses and reduced households' purchasing power, thereby affecting people's livelihood. The major sectors driving inflation in PNG include, the Transport, Household Equipment, Food and Non-Alcoholic Beverages, Alcoholic Beverages, Tobacco and Betelnut, Housing, Health, Miscellaneous, Restaurants and Hotel and Recreation expenditure groups, which more than offset decreases in the Education and Clothing and Footwear expenditure groups. In response to high inflation, the Bank tightened the stance of monetary policy in July 2022, by increasing the Kina Facility Rate to 3.25 percent. To support its stance, the Bank has progressively increased the Cash Reserve Requirement to 9.0 percent in September and issued additional Central Bank bills.

Chart 5: Inflation in PNG



Source: National Statistics Office and BPNG

Overall, PNG's economy has the potential to grow faster. Whilst the economy has more than tripled in size since independence, real GDP per capita has increased by only marginally per year – a lower growth in comparison to peers. Economic growth has been and continues to be subject to significant upward and downward swings. The

inclusivity of recent growth performance has been limited by the relatively low productivity of the non-resource sector, and insufficient investment in the human capital, underpinned by weak governance. At the same time, PNG can leverage some of its comparative advantages, notably its large stock of renewable assets and relatively young population.

Having said that, both the global and domestic outlooks for growth and inflation involve considerable uncertainties stemming from various supply-side

factors. The ongoing challenges from the Russia-Ukraine war, supply-chain disruptions, high crude oil and gas, and food prices, and high inflation could adversely impact on the recovery. This calls for a renewed policy focus on economic growth, not only on the short-term factors affecting the outlook for this year, but also on the longer-term drivers of the growth and welfare of the people. These long-term drivers of growth will also be influenced by some of the significant global trends such as accelerated digitalization and increasing shift to climate change action that will govern flows of goods, services and capital.

Economic & Financial Statistics/Forecasts

Economic Statistics

PNG	2019	2020	2021	2022f	2023f	2024f
Money Supply (%)	4.4	7.0	11.8	13.7	3.0	4.0
Private Sector Credit (%)	4.0	4.3	0.4	3.0	2.5	3.0
Current Account (K millions)	18,522.2	17,255.6	21,722.8	38,528.6	32,844.4	33,958.9
Gross International Reserves (K millions)	7,880.0	9,437.9	11,368.7	14,028.2	14,345.1	14,539.1
Total Import Cover (months)	5.0	7.4	9.1	11.2	10.9	10.9
Non-mineral Import Cover (months)	8.2	11.8	15.9	22.1	20.4	20.1
Headline Inflation	2.7	5.1	5.7	6.0	5.0	4.0
Fiscal Surplus/Deficit (K Million)	-4,172.1	-7,304.4	-6,612.8	-5,984.6	-4,785.1	-3,798.7
Deficit % of GDP	-5.0	-8.9	-7.1	-5.4	-4.4	-3.3

Source: Bank of PNG, International Monetary Fund and National Statistics Office

Interest Rate Forecast

Australia	Latest	Mar-23	Jun-23	Sept-23	Dec-23	Mar-24	Jun-24	Sept-24	Dec-24
Cash	3.35	3.60	3.85	3.85	3.85	3.60	3.35	3.10	2.85
10 Year Bond	3.39	3.20	3.10	3.00	2.90	2.80	2.70	2.60	2.50
US									
Fed Funds	3.875	4.875	4.875	4.875	4.875	4.375	3.875	3.375	2.875
US 10 Year Bond	3.50	3.40	3.30	3.20	3.00	2.90	2.70	2.60	2.50
New Zealand									
Cash	4.25	5.00	5.50	5.50	5.50	5.25	4.75	4.25	3.75
10 Year Bond	4.14	4.00	3.95	3.90	3.80	3.70	3.60	3.50	3.50

Source: Westpac Economics

Global & Trading Partner Growth Forecast

	2019	2020e	2021f	2022f	2023f	2024f
World Economy	2.8	-3.1	6.2	3.4	2.9	3.1
US	2.2	-3.4	5.9	2.0	1.4	1.0
Eurozone	1.3	-6.4	5.3	3.5	0.7	1.6
Australia	2.0	-2.1	4.9	3.8	1.9	NA
New Zealand	2.9	-2.1	5.6	2.3	1.9	NA
Japan	0.3	-4.5	2.1	1.4	1.8	0.9
China	6.0	2.2	8.4	3.0	5.2	4.5
India	4.2	-6.6	8.7	6.8	6.1	6.8

Source: International Monetary Fund, World Economic Outlook



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