



BANK OF PAPUA NEW GUINEA

MONTHLY ECONOMIC REVIEW

Vol. 1

No. 1

Month Ended
January 2014

Economic Activity

Global economic growth continued to be sluggish, with the emerging economies accounting for a large part of the growth. There was a modest acceleration of activity in a few advanced economies while the Euro zone is struggling to come out of recession. The latest outlook in October 2013 by the International Monetary Fund (IMF) is for a global growth of 2.9 percent for the year, down from the 3.1 percent projected earlier in July.

Domestically, the PNG economy continued to grow at a moderate pace, lower than the strong growth of 2012. While lower international commodity prices and the winding down of the construction phase of the Liquefied Natural Gas (LNG) project are contributing to the easing in economic growth, growth in the non-mineral private sector activity, supported by increased growth in credit extended by commercial banks, and increased Government expenditure have contributed to sustaining the growth. Indications are that real GDP growth for 2013 is lower than in 2012 but moderate at around 5.0 percent, which is still strong when compared to other developing economies. And with annual inflation low at 3.5 percent and within the Bank's forecast for the year, this is a commendable achievement.

The level of employment in the private sector declined in the third quarter by 3.1 percent but on an annual basis, it increased by 1.6 percent over the year to September 2013, and was broad based across most sectors.

Investment and consumption demand remained positive as private sector credit was strong, imports increased and tax collection increased.

Balance of Payments

Preliminary balance of payments data for the eleven months to November 2013 show an overall deficit of K1,414 million, compared to a deficit of

K769 million in the corresponding period of 2012. A higher deficit in the current account more than offset a surplus in capital and financial accounts. The deficit in the current account was due to a lower trade surplus and higher net service payments, which more than offset lower net income and net transfer receipts. The surplus in the capital and financial account was due to net inflows from foreign direct investment and other investments more than offsetting net outflows from portfolio investments. The level of gross foreign exchange reserves at the end of November 2013 was US\$2,943.7 (K7,088.2) million, sufficient for 7.9 months of total and 12.3 months of non-mineral import covers. As at 31st January 2014, the level of gross foreign exchange reserves was US\$2,811.3 (K6,725.6) million.

Exchange Rate

The kina has steadied against the US dollar at US\$0.4130 since November 2013. This follows the measures the Central Bank took, in consultation with the commercial banks, to support the kina besides the Central Bank intervention in the foreign exchange market to ease the pace of depreciation during the period. The measures included allowing only forward orders of 3 months or less to be brought to the inter-bank foreign exchange market, starting in October, and subsequently, only spot orders as of December 2013. Over the month to 31st January 2014, the kina appreciated against the Australian dollar by 65 basis points on average to AU\$0.4667, due to cross currency movements as the Australian dollar depreciated against the US dollar on the back of positive growth outlook for the US economy. The average TWI¹ increased by 0.8 percent to 38.41 over the month to 31st January 2013, reflecting the kina's appreciation against the Australian dollar and other major currencies.

Inflation

The annual headline Retail Price Index (RPI)² to December 2013 declined by 0.3 percent, compared to an increase of 1.7 percent in November 2013. This was due to a decline in prices of the 'Drink, tobacco and

¹ The Trade Weighted Index (TWI) measures the value of the kina against a basket of currencies of PNG's major trading partners.

² The RPI survey covers the major supermarkets in Port Moresby only and is compiled monthly.

betelnut' and 'Food' expenditure groups. The RPI ex-seasonal increased by 0.9 percent and RPI ex seasonal kerosene and petrol fell by 0.4 percent, compared to a decline of 1.5 percent in November 2013. This is the latest on inflation following the National Statistical Office release for the September quarter, which reported annual headline inflation at 3.5 percent and quarterly headline inflation at 1.2 percent.

The pass-through effect of the depreciation of the kina to domestic prices has been minimal and largely being offset by other factors, including low imported inflation, alternative cheaper sources of imports and competition among firms that resulted in low inflation outcomes.

The persistent depreciation in the kina may lead to an increase in inflation at some point in time in the future. For the moment all measures of inflation are within the Bank's end year forecast of 5.5 percent.

Fiscal Operations

Preliminary estimates of the fiscal operations of the National Government for 2013 show an overall deficit of K2,495 million, compared to a deficit of K1,380 million in 2012. This represents 4.2 percent of nominal GDP. Expenditure increased by more than the increase in revenue. Total expenditure was 8.5 percent higher and total revenue was 2.0 percent lower than in 2012. The budget deficit was financed from net external borrowing of K299.5 million and domestic sources totalling K2,195.3 million. The National Government's cash flow for week-ending 31st January 2014 show a credit position of K401.1 million mainly due to higher tax revenue.

Domestic Interest Rates & Monetary Aggregates

Over the month ending 31st January 2014, movements in Central Bank Bill (CBB) rates were mixed. The 28-day rate declined from 1.84 percent to 1.83 percent, while the 63-day rate increased from 2.10 percent to 2.11 percent and the 91-day rate from 2.17 percent to 2.18 percent. The 182-day rates remain unchanged at 2.51 percent. Treasury bill rates, on the other hand, increased. The 182-day rate increased from 2.52 percent to 2.77 percent and the 364-day rate from 3.76 percent to 4.44 percent. There were mixed results for wholesale deposit rates.

Credit conditions remain conducive for consumption and investment activity. Broad money supply

(M3*) grew by 6.5 percent on an annual basis in December 2013, largely underpinned by an increase in net claims on the Central Government, drawdown of Government deposits and an increase in private sector credit. Over the year to 27th December 2013, average lending by commercial banks increased by 18.5 percent to K8,660.6 million. Total liquidity of the banking system, comprising cash, balance of Exchange Settlement Accounts, Central Bank Bills, Treasury bills and Inscribed stocks of less than 3 years to maturity, was K8.3 billion as at the end of December 2013, compared to K7.8 billion a month earlier.

Monetary Policy

Being mindful of potential inflationary pressures, the Bank is taking a cautious approach by maintaining its neutral stance of monetary policy. The policy signalling rate, the Kina Facility Rate (KFR), is kept at 6.25 percent for the month of January 2014. This stance is also to support economic growth as the construction phase of the LNG project winds down.

Financial System Stability

The financial system in PNG is very sound. As at the end of September 2013, total assets of the system stood at K21.9 billion, of which the amount for the banking sector is 77.0 percent, superannuation system 21.8 percent, and life insurance 1.2 percent. Total loans were K11.3 billion. Non-performing loans as a proportion of total loans was 1.9 percent and as a share of total assets was 0.8 percent. The capital adequacy ratio (CAR) for the banking system was 28.1 percent, well above the minimum requirement of 12 percent. The return on assets (ROA) was 2.6 percent and return on equity (ROE) was 21.8 percent.

Payments System (KATS)

The National Payments System Act (NPSA) 2013 was passed by the National Parliament on 19th July 2013, followed by the launching of the first stage of the project on 14th October 2013 called the Kina Automated Transfer System (KATS). The KATS brings the domestic payment system in line with the international payments system, providing Real Time Gross Settlement (RTGS). This is expected to improve the payment system by reducing costs of transactions, improving efficiency and making payments safer.

Papua New Guinea Key Economic Indicators					
		Sep-13	Oct-13	Nov-13	Dec-13
1. Consumer (YOY % Change)	Headline	3.5	-	-	n.a
	Food	0.7	-	-	n.a
2. Retail Price Index (YOY % Change)	Headline	2.2	3.9	1.7	-0.3
	Ex-seasonal	0.8	2.5	3.1	0.9
3. Exchange Rates (mid rate, eop)	USD	0.4160	0.4130	0.4130	0.4130
	AUD	0.4468	0.4352	0.4538	0.4622
	GBP	0.2574	0.2579	0.2525	0.2506
	JPY	40.70	40.60	42.23	43.38
	NZD	0.5029	0.5006	0.5091	0.5024
4. Foreign Exchange Reserve (eop US\$ mill)		3,037	3,064	2,944	2,855
5. Liquidity (eop)	Liquid Assets Margin to Deposit Ratio (%)	45.4	42.5	41.9	44.6
	Banks Demand Deposits (K'bn)	10.3	10.2	10.6	10.7
6. Money and Credit (YOY % change)	Broad Money	11.9	11.0	11.0	6.5
	Monetary Base	6.6	0.9	-0.4	-0.5
	Private Sector Credit	17.6	17.7	16.1	17.5
7. Interest Rates (% pa) (monthly weighted average)	Kina Facility Rate	6.25	6.25	6.25	6.25
	Central Bank Bill Rate (28 day)	1.72	1.77	1.85	1.84
	Commercial bank Term Deposit (30 day)	0.75	0.55	0.61	0.35
	Government Treasury bill (364 day)	3.13	3.18	3.60	3.72
	3-year Inscribed stock Rate	-	0.04	0.05	-
16-year Inscribed stock Rate	-	0.11	0.11	-	
8. Commodity Prices	Oil (\$/bbl)	108.8	105.4	102.6	105.5
	Gold (\$/troy oz)	1348.6	1309.5	1280.8	1223.7
	Copper (\$/mt)	7159.3	7181.6	7096.3	7193.6
	Coffee (cents/kg)	132.3	130.4	123.1	127.0
	Cocoa (cents/kg)	261.6	273.0	276.0	279.1

Authorised for release by Mr. Loi M. Bakani, Governor