## CONTENTS

1. General Overview 2

2. International Developments 5

3. Domestic Economic Development 8
   - Domestic Economic Activity
   - Employment
   - Consumer Price Index

4. Export Commodities Review 13
   - Mineral Exports
   - Agriculture, Logs and Fisheries Exports

5. Balance of Payments 17

6. Monetary Developments 19
   - Interest rates and Liquidity
   - Money Supply
   - Lending

7. Public Finance 21

   Special Article
   - September 2009 Monetary Policy Statement 23

Glossary of Terms and Acronyms 36

Reference ‘For the Record’ 39

Reference 40

Statistical Section 41

List of Tables S1

---

The contents of this publication may be reproduced provided the source is acknowledged.

PORT MORESBY
28th December 2009
1. GENERAL OVERVIEW

Economic indicators available to the Bank of Papua New Guinea (the Bank) show that low economic growth in the domestic economy, induced by the global recession, continued into the third quarter of 2009. Albeit an increase in business sales in the June quarter 2009 compared to the March quarter, lower employment growth in the private sector, lower credit growth, and continued deterioration of the current account in the September quarter are indicative of the low growth. The deficit in the current account was, however, more than offset by a surplus in the capital and financial accounts, yielding an overall balance of payments surplus. Annual headline inflation subsided to 5.3 percent in the September quarter of 2009 from 13.5 percent in the corresponding period of 2008, attributed to reduced international fuel and food prices, low imported inflation and prices of domestic seasonal produces. With the economic recovery in Australia and the consequent appreciation of the Australian dollar against the US dollar, the kina depreciated against Australian dollar and other major trading partner currencies, while it appreciated against the US dollar. As a result, the Trade Weighted Exchange Rate Index (TWI) depreciated by 1.7 percent in the September quarter. Although the rate of inflation had come down, potential inflationary pressures can come from a weaker kina and excessive Government spending, especially a fast draw down of Government trust funds. The Bank therefore maintained its tight monetary policy stance by keeping the policy signaling rate, the monthly Kina Facility Rate (KFR), unchanged at 8.0 percent throughout the September quarter 2009.

Data from the Bank’s Business Liaison Survey (BLS) show that the total nominal value of sales in the private sector increased by 9.1 percent in the June quarter of 2009, compared to a decline of 12.0 percent in the March quarter. Excluding the mineral sector, sales increased by 4.9 percent in the June quarter, compared to a decline of 14.3 percent in the previous quarter. By sector, all sectors recorded increases, except the manufacturing. All regions recorded increases, except the Islands. Over the twelve months to June 2009, total sales declined by 20.9 percent.

The Bank’s Employment Index shows that the level of employment in the formal private sector increased by 0.6 percent in the September quarter of 2009, compared to an increase of 1.1 percent in the June quarter. Excluding the mineral sector, employment increased by 0.6 percent in the September quarter of 2009, compared to an increase of 1.2 percent in the previous quarter. By industry, employment increased in the manufacturing, mineral, wholesale, and retail sectors, which more than offset declines in agriculture/forestry/fisheries, building and construction, transportation, financial/business and other service sectors. By region, NCD, Southern, and Momase recorded increases. Over the twelve months to September 2009, total employment increased by 3.8 percent while excluding the mineral sector it increased by 4.0 percent.

Quarterly headline inflation, as measured by the Consumer Price Index (CPI), was 1.8 percent in the September quarter of 2009, compared to 0.4 percent in the June quarter. There were increases in the ‘Drinks, Tobacco and Betelnut’, ‘Food’, ‘Clothing and Footwear’, ‘Household equipment and operations’, ‘Transport and Communication’, and ‘Miscellaneous’ expenditure groups. Annual headline inflation was 5.3 percent in the September quarter of 2009, compared to 6.7 percent in the previous quarter. The lower inflation outcome was mainly attributed to lower international fuel and food prices, imported inflation and prices of domestic seasonal produce. By region, all urban areas recorded both quarterly and annual price increases in the September quarter.

In the September quarter of 2009, the daily average kina exchange rate depreciated against all major trading currencies except the US dollar compared to the June quarter. While the kina appreciated against the US dollar by 4.0 percent to US$ 0.3680, it depreciated against the Australian dollar by 5.1 percent to A$ 0.4428, pound sterling by 2.0 percent to 0.2242 sterling, the euro by 0.8 percent to 0.2576 euro and the Japanese yen by 0.02 percent to 34.4473 yen. These movements resulted in the daily average TWI depreciating by 1.7 percent during the September quarter of 2009 compared to the June quarter.

Lower international prices for most mineral and agricultural exports resulted in a 17.4 percent decline in the weighted average kina price of exports in the September quarter of 2009, compared to the corresponding quarter of 2008. There was a 18.8 percent decline in the weighted average price of mineral exports, with lower kina prices of copper and crude oil. The weighted average price of agricultural, logs and marine product...
exports declined by 11.1 percent and was accounted for by lower kina prices of coffee, palm oil, copra, copra oil, tea, rubber and marine product exports.

There was an overall surplus in the balance of payments for the nine months to September 2009 of K833 million, compared to a surplus of K560 million in the corresponding period of 2008. This outcome was due to a surplus in the capital and financial accounts, which more than offset a deficit in the current account.

The current account recorded a deficit of K905 million in the nine months to September 2009, compared to a surplus of K2,068 million in the corresponding period of 2008. This outcome was attributed to a lower trade surplus, higher net service payments and lower net transfer receipts.

The capital and financial account recorded a net inflow of K1,783 million in the nine months to September 2009, compared to a net outflow of K1,674 million in the corresponding period of 2008.

The capital account recorded a lower net inflow of K58 million in the nine months to September 2009, compared to K63 million in the corresponding period of 2008. The decline reflected lower capital inflows by donor agencies for project financing.

The financial account recorded a net inflow of K1,725 million in the nine months to September 2009, compared to a net outflow of K1,674 million in the corresponding period of 2008. This outcome reflected a higher net inflow from direct investments due to equity investments in a mineral company, liquidation of investments in financial derivative instruments and drawdown of foreign currency account balances by mineral companies.

The level of gross foreign exchange reserves at the end of September 2009 was K6,155.0 (US$2,349) million, sufficient for 9.8 months of total and 13.5 months of non-mineral import cover.

The Bank of Papua New Guinea maintained its tight monetary policy stance during the September quarter of 2009 as stated in the September Monetary Policy Statement (MPS). The Kina Facility Rate (KFR) was kept unchanged at 8.00 percent with the dealing margin for the Repurchase Agreements (Repos) maintained at 100 basis points on both sides of the KFR. Domestic interest rates for short-term securities and deposits showed declining trends across most maturities during the September quarter.

The Bank continued to utilise Open Market Operation (OMO) instruments in the conduct of monetary policy over the September quarter of 2009. The commercial banks also used the interbank market to meet their daily liquidity needs. The Cash Reserve Requirement (CRR) and the Minimum Liquid Assets Ratio (MLAR) of commercial banks were maintained at 3.0 percent and 25.0 percent, respectively, over the September quarter 2009.

The average level of broad money supply (M3*) increased by 7.0 percent in the September quarter of 2009, compared to an increase of 4.1 percent in the June quarter. This outcome was mainly due to a substantial increase by 209.6 percent in average net claims on the Central Government following higher issuance of Treasury bills, 4.4 percent increase in average net private sector credit and an increase of 1.0 percent in average net foreign assets of depository corporations. Net domestic claims outstanding, excluding advances to the Central Government and outstanding loans under the Government’s Agricultural export commodity price support schemes increased by 4.1 percent in the September quarter of 2009, compared to an increase of 2.9 percent in the June quarter of 2009.

During the September quarter of 2009, total domestic credit extended by depository corporations to the private sector, public non-financial corporations, Provincial and Local Governments, and other financial corporations, increased by K192.9 million to K6,284.9 million, compared to an increase of K220.5 million in the June quarter of 2009. This was mainly due to an increase of K196.8 million in private sector credit. The annualised growth in domestic credit, excluding Central Government and advances under the price support schemes was 29.7 to September 2009.

Preliminary estimates of the fiscal operations of the National Government over the nine months to September 2009 showed an overall surplus of K541.3 million, compared to a surplus of K885.8 million in the corresponding period of 2008. This represents 2.6 percent of nominal GDP.

Total revenue, including foreign grants, during the nine months to September 2009 was K4,063.8 million, 11.6 percent lower than the receipts collected in the corre-
sponding period of 2008. This represents 55.9 percent of the budgeted revenue. The decline reflected low tax receipts during the period, which more than offset increases in non-tax revenue and foreign grants.

Total expenditure over the nine months to September 2009 was K3,522.5 million, 5.1 percent lower than in the corresponding period of 2008, and represents 52.8 percent of the budgeted expenditure for 2009. This was due to lower development expenditure, which more than offset an increase in recurrent expenditure.

The surplus was used to make net external loan repayments of K125.8 million and net negative financing to domestic sources of K415.5 million. The net overseas loan repayments comprised of K85.7 million, K9.8 million and K30.2 million to concessionary, commercial and extraordinary sources, respectively. The net negative financing to domestic sources comprised of K1,019.3 million in cheque floats that were settled, which more than offset a net draw down of K603.8 million from Government deposits at the Central Bank.
2. INTERNATIONAL DEVELOPMENTS

While world economic activity declined on the whole in the nine months to September 2009, there were some signs that the recession may have reached its trough and some indications of economic recovery have emerged. Significant pick-up in economic growth in China and India, and the recovery in Australia, France and Germany are positive indications. Also, there were some gains made in the manufacturing and industrial sectors in the USA, Japan and the Euro area for the first time since early 2008. The aggressive measures taken by central banks in easing monetary policy, through interest rate cuts, and large fiscal stimulus packages of Governments have helped slow down the impact of the financial crisis and the recession, and assisted economies to recover. However, the recovery is expected to be slow as financial systems remain impaired, support from public policies are gradually removed while households are slowly recovering and rebuilding savings. The October 2009 World Economic Outlook (WEO) Update of the International Monetary Fund (IMF) revised upwards its global growth projection for 2009 made in the July Update from a negative growth of 1.4 percent to negative 1.1 percent. Global growth is projected to improve significantly in 2010 to 3.1 percent, mainly driven by the emerging and developing economies. It is anticipated that growth in the advanced economies will decline by 3.4 percent in 2009, while the emerging and developing economies are expected to grow by 1.7 percent. The growth in the emerging and developing economies is mainly driven by China and India. Unemployment will remain relatively high in 2009 and 2010, while inflation is expected to decline and remain low.

In September 2009, leaders of the G20 countries met in Pittsburgh, Pennsylvania, USA and discussed the withdrawal of emergency support for the global economy. The leaders from Britain, France and Germany expressed concerns that whilst indicators point to some stability in key economies, the crisis is not over yet and the labour markets will suffer the consequences of low capacity utilisation over the months to come. The leaders called for work to start on “exit strategies” to be implemented in a coordinated manner so that the unprecedented level of financial support from public policies will gradually be withdrawn.

Also in September 2009, the World Bank-IMF held its Annual Meeting. At the meeting, the World Bank President Robert Zoellick called on world leaders to reshape the multilateral system and forge a “responsible globalization”—one that would encourage balanced global growth and financial stability, embrace global efforts to counter climate change, and advance opportunities for the poorest. The crisis has given an opportunity to reshape our policies and underscored the growing importance of the large emerging economies, such as China and India. The global trading system, he added, is failing to keep up with the demands of the global economy. He also raised the concern that the Doha Round is fast falling behind the new challenges and urged every member country to get the Doha Round of talks started and completed on important trade related issues. The World Bank President further noted that to be effective and strengthen their legitimacy, the international institutions must also evolve to accord proper representations and voting rights to reflect the weights and new responsibilities of emerging powers, while assuring a voice for the poor.

In the September quarter, oil prices increased to around US$70 per barrel. Brent crude oil prices stood at US$70.3 per barrel on 2nd September, which was 78 percent higher than at the beginning of 2009. Market expects higher prices in the medium term, with future contracts for December 2011 trading at around US$77 per barrel. While expectation of future increase in demand had a positive effect on spot oil prices, current oil stocks remained high while oil demand continued to decline – albeit at a slower pace. The prices of some non-energy commodities also increased over the past months. In aggregate terms, the price index for non-energy commodities (denominated in US dollars) was approximately 20.0 percent higher towards the end of August than at the beginning of the year. Metal prices rose, led by gold, supported by higher demand in China and OECD countries in the second half of the year. By contrast, the prices of food commodities declined in aggregate terms given more favourable supply prospects, particularly for wheat and maize. Sugar prices were an exception, posting strong increases against the backdrop of concerns about the crops in Brazil and India.

In the United States, real GDP declined by 2.3 percent over the year to the September quarter of 2009, compared to a growth of 0.8 percent over the corresponding period in 2008. However, for the first time since the September quarter of 2008, US experienced a positive quarterly growth of 0.7 percent or 2.8 percent.
annualised. The increase was primarily due to positive contributions from personal consumption expenditure, exports, private inventory investments, federal government spending, and residential fixed investments. The latest IMF forecast is for real GDP to contract by 2.7 percent in 2009.

Industrial production decreased by 6.1 percent over the year to September 2009, compared to a decrease of 4.9 percent over the year to June 2008. The Institute of Supply Management’s Purchasing Managers Index was 48.9, 52.9 and 52.6 in July, August and September 2009, respectively. An index below 50 indicates contraction while an index above 50 indicates expansion in the manufacturing industry. Retail sales decreased by 3.2 percent over the year to September 2009, compared to a decrease of 3.3 percent over the corresponding period in 2008, reflecting low consumer demand and high unemployment. The annual unemployment rate was 9.8 percent in September 2009, compared to 6.1 percent in September 2008.

Consumer prices fell by 1.3 percent over the year to September 2009, compared to an increase of 4.9 percent over the same period in 2008, due to the global recession resulting in lower food and energy prices. Broad money supply increased by 6.7 percent over the year to September 2009, compared to 6.2 percent over the corresponding period in 2008. The Federal Reserve (Fed) maintained the target range for the federal funds rate at 0 to 0.25 percent. The Fed anticipates that economic conditions are likely to warrant exceptionally low levels of the federal funds rate for an extended period.

The trade deficit was US$550.7 billion over the year to September 2009, compared to a deficit of US$851.1 billion over the year to September 2008. The huge fall was attributed to the global recession that resulted in lower import demand.

In Japan, real GDP contracted by 4.5 percent over the year to September 2009, compared to a 0.1 percent decline over the corresponding period in 2008. This was associated with weak corporate profits and private consumption as a result of increasing unemployment and falling income. However, on a quarterly basis, the economy grew by 1.2 percent in the September quarter, aided by a 3.3 percent rise in domestic demand and a rebound in public investments, exports and manufacturing. The October 2009 IMF forecast is for real GDP to contract by 5.4 percent in 2009.

Industrial production decreased by 18.4 percent over the twelve months to September 2009, compared to an increase of 0.2 percent over the year to September 2008. Retail sales increased by 1.5 percent over the year to September 2009, compared to a 1.8 percent decline over the corresponding period in 2008. The unemployment rate was 5.3 percent in September 2009, compared to 4.0 percent in September 2008.

Consumer prices decreased by 2.2 percent over the year to September 2009, compared to an increase of 2.1 percent over the year to September 2008. The decline in the CPI was mainly due to lower prices of petroleum products and the substantial slowdown in the economy reflecting the global recession. Broad money supply grew by 3.0 percent over the year to September 2009, compared to an increase of 2.2 percent over the same period in 2008. The Bank of Japan has maintained the uncollateralized overnight call rate at around 0.1 percent during the September quarter of 2009.

The current account surplus was US$120.8 billion over the year to September 2009, compared to US$185.9 billion over the year to September 2008. The lower surplus was due to declines in exports as a result of the global recession.

In the Euro area, the recession appeared to have ended with real GDP growing by 0.4 percent in the September quarter 2009, with Germany and France showing positive growth, while the Spanish and Greek economies still contracting. However, on an annual basis, it contracted by 4.1 percent over the year to September 2009, compared to a growth of 0.7 percent over the year to September 2008. The October 2009 IMF forecast is for real GDP to contract by 4.2 percent in 2009.

Industrial production fell by 14.0 percent over the year to September 2009, compared to a fall of 2.4 percent over the corresponding period in 2008. This was due to a drop in production of durable capital goods, consumer goods, and intermediate goods. Retail sales declined by 3.6 percent over the year to September 2009, compared to a decrease of 1.6 percent over the year to September 2008. The unemployment rate was 9.7 percent in September 2009, compared to 7.5 percent in September 2008.

Consumer prices in the Euro area decreased by 0.3 percent over the year to September 2009, compared to
an increase of 3.6 percent over the year to September 2008. The decline reflected significantly lower energy and food prices and lower consumer demand. Broad money supply increased by 1.8 percent over the year to September 2009, compared to an increase of 8.6 percent over the corresponding period in 2008. The European Central Bank (ECB) continued to pursue an accommodative monetary policy stance. Since October 2008, the Euro Refinancing Rate has been gradually lowered from 4.25 percent to 1.0 percent in May 2009 and maintained at that rate throughout the September quarter.

The current account of the Euro zone was in deficit of US$116.4 billion in September 2009, compared to a deficit of US$51.4 billion over the corresponding period in 2008.

In Germany, real GDP contracted by 4.8 percent over the year to September 2009, compared to a growth of 0.8 percent in the corresponding period in 2008. The economy did, however, grow again by 0.3 percent on a quarter-on-quarter basis, which was due to increases in private and public consumption, construction, and net trade, where a drop in imports outpaced a decline in exports. The October 2009 IMF forecast is for real GDP to contract by 5.3 percent in 2009.

Industrial production decreased by 12.8 percent over the year to September 2009, compared to a decline of 2.3 percent over the corresponding period in 2008. Retail sales declined by 4.0 percent over the year to September 2009, compared to an increase of 1.2 percent over the corresponding period in 2008. The unemployment rate in Germany was 8.2 percent in September 2009, compared to 7.6 percent in September 2008. Consumer prices declined by 0.3 percent over the year to September 2009, compared to an increase of 2.9 percent over the year to September 2008.

The current account surplus was US$144.2 billion over the year to September 2009, compared to US$266.8 billion over the corresponding period in 2008. The lower surplus was due to the global economic downturn.

In the UK, real GDP contracted by 5.2 percent over the year to September 2009, compared to a growth of 0.3 percent over the same period in 2008, reflecting the severity of the financial crisis and global recession. The decline was in all sectors, with business services and finance contributing significantly to the decline in output. The October 2009 IMF forecast is for real GDP to contract by 4.4 percent in 2009.

Industrial production declined by 10.3 percent over the year to September 2009, compared to a decrease of 2.2 percent over the same period in 2008. Retail sales increased by 1.2 percent over the year to September 2009, compared to an increase of 1.8 percent over the corresponding period in 2008. Sales of clothing and footwear picked up and homewares and furniture sales also rose above last September's very weak levels, helped by some improvement in consumer confidence and the housing market. The unemployment rate was 7.8 percent in September 2009, compared to 5.4 percent in September 2008.

Consumer prices increased by 1.1 percent over the year to September 2009, compared to an increase of 5.2 percent over the year to September 2008. Broad money supply increased by 11.3 percent over the year to September 2009, compared to an increase of 12.2 percent over the corresponding period in 2008. The Bank of England continued to maintain its official Bank Rate at 0.5 percent in the September quarter of 2009.

The trade deficit was US$128.2 billion over the year to September 2009, compared to US$185.5 billion deficit over the year to September 2008. The improvement was mainly due to lower import demand reflecting the low global demand.

In Australia, real GDP grew by 0.9 percent over the year to September 2009, compared to an increase of 1.9 percent over the year to September 2008. Economic recovery has been stronger than expected. In contrast to other developed economies, the Australian economy is estimated to have expanded, albeit modestly, over the first half of the year and recent data suggest that this expansion has continued into the third quarter. Confidence has improved and spending has been supported by stimulatory settings for both monetary and fiscal policies. The Australian economy has also benefited from the strong bounce-back in Asia, particularly in China and India, with export volumes remaining broadly unchanged during a period in which global trade fell markedly. According to the IMF, Australia will record a modest growth of 0.7 percent in 2009. This means Australia will be the only advanced economy to record a positive growth in 2009, in contrast to a collective contraction of 3.4 percent for advanced economies in 2009.
Industrial production declined by 3.8 percent over the year to June quarter 2009, compared to an increase of 2.8 percent over the same period in 2008. Retail sales increased by 3.4 percent over the year to September 2009, compared to an increase of 1.0 percent over the year to September 2008. The unemployment rate was 5.7 percent in September 2009, compared to 4.3 percent in September 2008.

Consumer prices rose by 1.3 percent over the year to September 2009, compared to an increase of 5.0 percent over the year to September 2008. Broad money supply increased by 9.1 percent over the year to September 2009, compared to an increase of 14.7 percent over the year to September 2008. To stimulate economic activity, the Reserve Bank of Australia lowered its Cash Rate from 3.25 to 3.00 percent in April and maintained it to September 2009.

There was a trade surplus of US$0.8 billion over the year to September 2009, compared to a deficit of US$14.0 billion over the same period in 2008.

In the September quarter of 2009, the daily average kina exchange rate depreciated against the Australian dollar by 5.1 percent to A$0.4428, pound sterling by 2.0 percent to 0.2242 sterling, euro by 0.8 percent to 0.2576 euro, and Japanese yen by 0.02 percent to 34.4473 yen. Against the US dollar, it appreciated by 4.0 percent to US$0.3680. These movements resulted in the daily average TWI depreciating by 1.7 percent during the September quarter of 2009.

3. DOMESTIC ECONOMIC DEVELOPMENT

DOMESTIC ECONOMIC ACTIVITY

Data from the Bank’s Business Liaison Survey (BLS) show that the total nominal value of sales in the private sector increased by 9.1 percent in the June quarter, compared to a decline of 12.0 percent in the March quarter of 2009. Excluding the mineral sector, sales increased by 4.9 percent in the June quarter, compared to a decline of 14.3 percent in the previous quarter. By sector, all sectors recorded increases, except manufacturing. By region, all regions recorded increases, except Islands. Over the twelve months to June 2009, total sales declined by 20.9 percent.
In the transportation sector, sales increased by 24.3 percent in the June quarter, compared to a decline of 1.8 percent in the March quarter of 2009. The rise was mainly attributed to higher cargo haulage by sea transportation, and passenger travel by both air and sea. Over the twelve months to June 2009, sales increased by 36.5 percent.

In the agriculture/forestry/fisheries sector, sales grew by 16.7 percent in the June quarter, compared to a decline of 27.1 percent in the March quarter of 2009 with increases in all the three sub-sectors. The increase in the agriculture sub-sector was due to high palm oil and coffee exports from improved production and a rebound in international prices. In the forestry sub-sector, the increase was due to growth in exports due to a rebound in international prices and improved harvest of logs, as global demand rebounded, especially in China. The increase in the fisheries sub-sector was mainly due to increased exports of tuna and favorable international prices of marine products. Over the twelve months to June 2009, the total nominal value of sales declined by 35.9 percent.

In the retail sector, sales increased by 14.3 percent in the June quarter, compared to a decline of 11.7 percent in the March quarter of 2009. The increase was mainly associated with higher demand, especially for heavy duty machinery and vehicles by mining and construction projects. Over the twelve months to June 2009, sales increased by 8.7 percent.

In the mineral sector, sales rose by 15.0 percent in the June quarter of 2009, compared to a decline of 7.7 percent in the preceding quarter. The increase was due to higher exports of crude oil, copper and gold, reflecting higher international prices. Over the twelve months to June 2009, sales declined by 44.2 percent.

In the financial/business and other services sector, sales increased by 4.9 percent in the June quarter, compared to an increase of 2.5 percent in the March quarter of 2009. The increase was mainly due to higher guest turnovers at hotels and increased demand for catering and security services and for real estate. Over the twelve months to June 2009, sales increased by 20.1 percent.

In the building and construction sector, sales increased by 4.7 percent in the June quarter, compared to an increase of 10.3 percent in the previous quarter. The continuation of building projects in Morobe and NCD and road maintenance work in the Highlands and Southern regions contributed to this growth. Over the twelve months to June 2009, sales increased by 9.0 percent.

In the wholesale sector, sales increased by 2.1 percent in the June quarter, compared to a decline of 23.4 percent in the March quarter of 2009. The increase in sales was due to opening of new company branches and increased demand from mining and building projects. Over the twelve months to June 2009, sales declined by 26.2 percent.

In the manufacturing sector, sales declined by 6.9 percent in the June quarter of 2009, compared to a fall of 16.3 percent in the previous quarter. The decline was mainly due to lower throughput for oil-based products by a major oil refinery and food processing associated with lower demand for consumables. Over the twelve months to June 2009, sales declined by 18.4 percent.

In the Southern region, sales increased significantly by 24.7 percent in the June quarter, compared to a fall of 21.7 percent in the March quarter of 2009. The increase was mainly driven by growth in the mineral sector and agriculture and forestry sub-sectors. The increase in the mineral sector reflected higher exports and copper prices, while the increase in the agriculture sub-sector was due to higher production and price of palm oil. The increase in the forestry sub-sector mainly reflected higher prices of forestry products. Over the twelve months to June 2009, sales declined by 81.1 percent.

In the Highlands region, sales increased by 22.0 percent in the June quarter, compared to a decline of 6.6 percent in the March quarter of 2009. The increase was mainly in the mineral and wholesale sectors and the agriculture sub-sector. The increase in the mineral sector was driven by higher prices, while the increase in the wholesale sector reflected higher demand. The increase in the agriculture sub-sector was due to higher coffee exports and prices. Over the twelve months to June 2009, sales declined by 1.1 percent.

In the Momase region, sales increased by 22.4 percent in the June quarter, compared to a fall of 30.6 percent in the previous quarter. The increase came from the agriculture/forestry/fisheries, manufacturing, building and construction, retail and wholesale sectors. In the agriculture/forestry/fisheries sector, the increase was mainly in the forestry and fisheries sub-sectors. The increase in the forestry sub-sector was due to higher
international prices and production of logs, while the increase in fisheries was due to increased exports of tuna and favorable international prices of marine products. The increase in the building and construction was due to private sector sponsored buildings and road projects. In the retail and wholesale sectors, the rise was due to higher demand for consumables generated by mining projects. Over the twelve months to June 2009, sales declined by 4.9 percent.

In Morobe, sales grew by 6.0 percent in the June quarter, compared to a decline of 7.7 percent in the previous quarter. The growth was mainly driven by the wholesale and building and construction sectors. In the wholesale sectors, the increase was due to higher demand from mining and construction projects reflecting increased activity. In the building and construction sector, the increase reflects ongoing private sector building projects and road maintenance. Over the twelve months to June 2009, sales declined by 1.3 percent.

In NCD, sales rose by 4.7 percent in the June quarter, compared to a decline of 16.9 percent in the preceding quarter. The increase was in the transportation, wholesale, and retail sectors. The growth in the retail and wholesale were due to higher demand, especially for heavy duty machinery and expansion of business activity while the increase in the transportation sector, was due to higher cargo haulage by sea transportation and passenger travel by both air and sea. Over the twelve months to June 2009, sales declined by 12.2 percent.

In the Islands region, sales fell by 7.9 percent in the June quarter, compared to an increase of 8.2 percent in the previous quarter. The decline was mainly in the mineral and wholesale sectors. The decrease in the mineral sector was due to lower export of gold from an existing mine, while the fall in the wholesale sector was due to lower sales by a major cocoa exporter, and lower prices of agricultural commodities. Over the twelve months to June 2009, sales increased by 33.0 percent.

EMPLOYMENT

The Bank’s Employment Index shows that the level of employment in the formal private sector increased by 0.6 percent in the September quarter of 2009, compared to an increase of 1.2 percent in the previous quarter. Over the twelve months to September 2009, employment increased by 3.8 percent, compared to an increase of 3.8 percent over the year to June. Excluding the mineral sector, employment increased by 4.0 percent over the year to September 2009, compared to an increase of 3.9 percent over the year to June 2009.

By industry, employment increased in the manufacturing, mineral, wholesale, and retail sectors, which was more than offset by decreases in agriculture/forestry/fisheries, building and construction, transportation, financial/business and other services sectors. By region, NCD, Southern, and Momase recorded increases.

In the agriculture/forestry/fisheries sector, employment decreased by 1.7 percent in the September quarter of 2009, compared to an increase of 4.4 percent in the June quarter. The decrease was mainly due to seasonal fluctuations and the retirement of employees. Over the year to September 2009, employment in the agriculture/forestry/fisheries sector increased by 4.0 percent.

In the building and construction sector, employment declined by 1.2 percent in the September quarter of 2009, compared to an increase of 4.0 percent in the June quarter. The decrease was mainly due to downsizing of operations and completion of projects in the Morobe province. Over the year to September 2009, employment in the building and construction sector increased by 1.3 percent.

In the financial/business and other services sector, employment increased by 2.3 percent in the September quarter of 2009, compared to an increase of 3.9 percent in the June quarter. The increase in the financial/business sub-sector was mainly due to expansion by a commercial bank and a finance company. The increase in the hotel sub-sector was due to an increase in new hotel rooms and the merger of several companies. The increase in the other services sub-sector was due to new recruitment and additional contracts by two security companies and the recruitment of casuals for a telecommunication contract. Over the year to September 2009, employment in the financial/business and other services sector grew by 11.3 percent.

In the mineral sector, employment increased marginally
by 0.2 percent in the September quarter of 2009 compared to an increase of 0.2 percent in the June quarter. One company laid off seasonal workers as it completed a drilling program, which was offset by several others that reported marginal increases. Over the year to September 2009, employment in the mineral sector increased by 3.7 percent.

In the manufacturing sector, employment increased by 4.0 percent in the September quarter of 2009, compared to a decrease of 0.4 percent in the June quarter. The increase was mainly due to massive hiring by one company to keep up with increased volume of work and another company recruiting to replace employees who had left. Over the year to September 2009, employment in the manufacturing sector increased by 3.8 percent.

In the wholesale and retail sectors, employment increased by 1.7 percent in the September quarter of 2009, compared to a decline of 1.6 percent in the June quarter. In the wholesale sector, the level of employment increased by 1.0 percent, compared to an increase of 1.7 percent in the June quarter, due to an increase in activity to meet higher demand. In the retail sector, the level of employment increased by 2.0 percent in the September quarter of 2009, compared to a decline of 3.2 percent in the previous quarter. The increase was due to the opening of new shops and business expansion. Over the year to September 2009, the level of employment in the wholesale sector increased by 3.1 percent, while the retail sector recorded an increase of 2.0 percent.

In the transportation sector, the level of employment decreased by 1.5 percent in the September quarter of 2009, compared to a decrease of 15.0 percent in the June quarter. This was mainly due to the completion of projects in Lae, Lihir, and the Southern Highlands. Over the year to September 2009, the level of employment in the transportation sector declined by 8.4 percent.

By region, the level of employment increased in the Momase, Southern, and NCD regions, while there were declines in Highlands, Morobe, and Islands. In the Momase region (excluding Morobe), the level of employment increased by 11.9 percent in the September quarter of 2009, compared to an increase of 8.7 percent in the June quarter. The increase was in the manufacturing, agriculture/forestry/fisheries and building and construction sectors. The increase in the manufacturing sector reflected recruitment for increased business activity while the growth in the agriculture/forestry/fisheries sector was due to expansion of palm oil operations. The increase in the building and construction sector was due to a new project in Madang, new hotel construction, and the construction of a new market. Over the year to September 2009, the level of employment increased by 12.9 percent.

In the Southern region, the level of employment increased by 2.1 percent in the September quarter of 2009, compared to a decline of 2.3 percent in the June quarter. The increase was focused in the agriculture/forestry/fisheries sector, where recruitment increased due to the peak crop period and the partial resumption of logging operations. Over the year to September 2009, employment increased by 6.7 percent.

In NCD, employment increased by 1.8 percent in the September quarter of 2009, compared to an increase of 0.9 percent in the June quarter. The growth was in the building and construction, retail, transportation, and financial/business and other services sectors. In the building and construction sector, the increase was due to new building and road projects, while in the retail sector, the growth was due to business expansion and the opening of new shops. In the transportation sector, the growth in employment was associated with the opening of new offices and a customer loyalty program. In the financial/business and other services sector, the increase was mainly due to the recruitment of additional employees by security companies and the employment of casuals for a contract with a telecommunications company. Over the year to September 2009, employment increased by 8.8 percent.

In Morobe, the level of employment decreased slightly by 0.7 percent, compared to an increase of 0.5 percent in the June quarter. The decrease was mainly in the manufacturing and building and construction sectors, where several major projects and contracts were completed. Over the year to September 2009, employment increased by 7.3 percent.

In the Islands region, employment decreased by 2.3 percent in the September quarter of 2009, compared to a decrease of 3.5 percent in the June quarter. The decline was in the agriculture/forestry/fisheries, manufacturing, and building and construction sectors. In the agriculture/forestry/fisheries sector seasonal workers were laid off and many employees retired.
The decrease in the manufacturing sector was largely due to terminations and resignations as a company shut down as well as a company downsizing its operation due to lower global demand. The decrease in building and construction was due to the completion of a project and reduced activity. Over the year to September 2009, employment decreased by 0.4 percent.

In the Highlands region, the level of employment decreased by 5.5 percent in the September quarter of 2009, compared to an increase of 12.2 percent in the previous quarter. The decrease was concentrated in the agriculture sub-sector where employment declined due to the end of the coffee season. Over the year to September 2009, the level of employment declined by 11.4 percent.

**CONSUMER PRICE INDEX**

Quarterly headline inflation, as measured by the Consumer Price Index (CPI), was 1.8 percent in the September quarter of 2009, compared to 0.4 percent in the June quarter. There were increases in the 'Drinks, Tobacco and Betelnut', 'Food', 'Clothing and Footwear', 'Household equipment and operations', 'Transport and Communication', and 'Miscellaneous' expenditure groups. Annual headline inflation was 5.3 percent in the September quarter of 2009, compared to 6.7 percent in the previous quarter. The lower inflation outcome was mainly attributed to low imported inflation and prices of seasonal produce. By region, all urban areas recorded both quarterly and annual price increases in the September quarter.

The CPI for the 'Food' expenditure group increased by 1.5 percent in the September quarter of 2009, compared to an increase of 0.3 percent in the June quarter. The increase was in all sub-groups with the largest from fruits and vegetables. This expenditure group contributed 0.6 percentage points to the overall movement in the CPI.

In the 'Drinks, Tobacco and Betelnut' expenditure group, prices increased by 3.2 percent in the September quarter of 2009, compared to an increase of 0.7 percent in the previous quarter. The increase was in all sub-groups, the largest being the betelnut. The expenditure group contributed 0.6 percentage points to the overall movement in the CPI.

In the 'Clothing and Footwear' expenditure group, the CPI increased by 1.7 percent in the September quarter of 2009, compared to a decrease of 1.5 percent in the previous quarter. The increase was in the men and boys clothing, and other clothing and footwear, while prices for woman and girls clothing declined. The group contributed 0.1 percentage points to the overall movement in the CPI.

The CPI for the 'Rents, Council charges, Fuel and power' expenditure group increased by 2.7 percent in the September quarter of 2009, compared to an increase of 1.9 percent in the June quarter. The increase was in the fuel and power sub-group, while the council charges recorded a decline. The group contributed 0.2 percentage points to the overall movement in the CPI.

The CPI for the 'Household equipment and operations' expenditure group increased by 2.5 percent in the September quarter of 2009, compared to a decrease of 0.1 percent in the previous quarter. The increase was in all sub-groups, the largest from semi-durable goods. This expenditure group contributed 0.1 percentage points to the overall movement in the CPI.

In the 'Transport and Communication' expenditure group, prices increased by 1.1 percent in the September quarter of 2009, compared to an increase of 0.8 percent in the June quarter. The increase was in the motor vehicle purchase and operations sub-group. This expenditure group contributed 0.1 percentage points to the overall movement in the CPI.

In the 'Miscellaneous' expenditure group, prices remained unchanged in the September quarter of 2009, from the level in the previous quarter. This expenditure group's contribution to the overall
movement in the CPI was negligible.

By urban areas, quarterly headline inflation increased in all the surveyed centers in the September quarter of 2009. Lae recorded the highest increase of 2.9 percent followed by Port Moresby and Madang with 1.6 percent each, then Rabaul and Goroka with 1.5 percent and 1.2 percent, respectively.

In Lae, prices increased by 2.9 percent in the September quarter of 2009, compared to an increase of 0.4 percent in the June quarter. The increase was in all expenditure groups, except the ‘Household equipment and operation’, which recorded no price change, and the ‘Miscellaneous’ expenditure group which had a decline. Large increases of 5.0 percent and 4.7 percent were recorded in the ‘Clothing and Footwear’ and ‘Drinks, Tobacco and Betelnut’ expenditure groups, respectively. The ‘Rents, Council charges, Fuel and power’, ‘Food’ and ‘Transport and Communication’ expenditure groups recorded increases of 2.9 percent, 2.4 percent and 0.7 percent, respectively.

In Port Moresby, prices increased by 1.6 percent in the September quarter of 2009, compared to an increase of 0.2 percent in the June quarter. The largest increases were recorded in the ‘Household equipment and operations’ ‘Rents, Council charges, Fuel and power’, and ‘Drinks, Tobacco and Betelnut’ expenditure groups of 4.3 percent, 3.0 percent and 2.8 percent, respectively. The ‘Food’, ‘Transport and Communication’, and ‘Miscellaneous’ expenditure groups recorded small increases, while the ‘Clothing and Footwear’ expenditure group recorded a decline.

In Goroka, prices increased by 1.2 percent in the September quarter of 2009, compared to an increase of 0.7 percent in the previous quarter. All expenditure groups recorded price increases. The ‘Clothing and Footwear’, ‘Household equipment & operation’, and ‘Rents, Council charges, Fuel and power’ expenditure groups recorded increases of 3.6 percent, 3.5 percent and 2.3 percent, respectively. The ‘Drinks, Tobacco and Betelnut’ and ‘Food’ expenditure groups recorded increases of 0.9 percent and 0.8 percent, respectively.

In Madang, prices increased by 1.6 percent in the September quarter of 2009, compared to an increase of 1.2 percent in the June quarter. The increases were in all the expenditure groups except the ‘Miscellaneous’ group. The ‘Drinks, Tobacco and Betelnut’ expenditure group recorded the highest increase of 2.9 percent. The ‘Rents, Council charges, Fuel and power’ and ‘Food’ expenditure groups recorded an increase of 1.8 percent and 1.3 percent, respectively.

The CPI for Rabaul increased by 1.5 percent in the September quarter of 2009, compared to an increase of 0.7 percent in the previous quarter. There were increases in all expenditure groups except the ‘Miscellaneous’ group. The highest increases were in the ‘Rents, Council charges, Fuel and power’ of 2.7 percent and ‘Drinks, Tobacco and Betelnut’ expenditure groups of 2.6 percent.

The quarterly exclusion-based and trimmed-mean inflation were 0.9 percent and 1.4 percent, respectively, in the September quarter of 2009, compared to 0.7 percent each in the previous quarter. The annual exclusion-based inflation was 5.2 percent in the September quarter of 2009, compared to 7.5 percent in the June quarter. Annual trimmed-mean inflation was 3.8 percent in the September quarter of 2009, compared to 5.0 percent in the previous quarter.

4. EXPORT COMMODITIES REVIEW

The total value of merchandise exports in the September quarter of 2009 was K3,057 million, 24.7 percent lower than in the corresponding quarter of 2008. There were declines in the export values of copper, crude oil, coffee, cocoa, palm oil, copra, copra oil, tea, rubber, marine, refined petroleum products and other non-mineral exports, which more than offset increases in the values of gold, and forestry exports. Mineral export receipts, excluding crude oil were K1,871.7 million and
accounted for 61.2 percent of total merchandise exports in the September quarter of 2009, compared to K2,117.7 million or 52.2 percent in the corresponding quarter of 2008. Crude oil exports totaled K473.0 million and accounted for 15.5 percent of total merchandise exports in the September quarter of 2009, compared to K883.9 million or 21.8 percent of total merchandise exports in the corresponding quarter of 2008.

The value of agricultural, marine products and other non-mineral exports, excluding forestry and refined petroleum product exports was K515.8 million and accounted for 16.9 percent of total merchandise exports in the September quarter of 2009, compared to K726.2 million or 17.9 percent of total merchandise exports in the corresponding quarter of 2008. Forestry product exports were K102.9 million and accounted for 3.4 percent of total merchandise exports in the September quarter of 2009, compared to K100.8 million or 2.5 percent in the corresponding quarter of 2008. Refined petroleum product exports were K93.6 million and accounted for 3.1 percent of total merchandise exports in the September quarter of 2009, compared to K32.4 million or 5.7 percent in the corresponding quarter of 2008.

The weighted average price of Papua New Guinea’s exports was 17.4 percent lower in the September quarter of 2009, compared to the corresponding quarter of 2008. There was an 18.8 percent decline in the weighted average price of mineral exports, with lower kina prices of copper and crude oil. The weighted average price of agricultural, logs and marine product exports declined by 11.1 percent and was accounted for by lower kina prices of coffee, palm oil, copra, copra oil, tea, rubber and marine product exports. Excluding logs, the weighted average price of agricultural and marine product exports declined by 15.7 percent in the September quarter of 2009, compared to the corresponding period of 2008.

Mineral Exports

Total mineral export receipts were K2,344.7 million in the September quarter of 2009, a decline of 21.9 percent from the corresponding quarter of 2008. The decline was due to lower prices of copper and crude oil exports combined with lower volumes of gold and crude oil, which more than offset the increase in price of gold and volume of copper.

Gold export volumes in the September quarter of 2009 was 14.4 tonnes, a decline of 8.9 percent from the corresponding quarter of 2008. This outcome was due to the extraction of low ore grades from the Ok Tedi mine and lower production from Lihir mine due to a routine plant shutdown for maintenance work, which more than offset the increase in production from the Porgera mine. The average free on board (f.o.b.) price received for Papua New Guinea’s gold exports was K82.2 million per tonne during the September quarter of 2009, 14.5 percent higher than in the corresponding period of 2008. The increase is mainly attributed to higher international prices during the quarter. The average gold price at the London Metal Exchange was US$961 per fine ounce in the September quarter of 2009, an increase of 10.1 percent from the corresponding quarter of 2008. The increase was due to higher demand from investors for gold-based investments as a safe haven after increased volatility of prices in the equity markets, and as a currency hedge given the uncertainty surrounding the US dollar. The increase in export price more than offset the decline in export volume and resulted in a 4.4 percent increase in export receipts to K1,184.1 million in the September quarter of 2009, from the corresponding quarter of 2008.

Copper export volumes in the September quarter of 2009 was 46.2 thousand tonnes, an increase of 0.9 percent from the corresponding quarter of 2008. This outcome was due to a combined result of higher shipment and marginal increase in production from the Ok Tedi mine. The average f.o.b. price of Papua New Guinea’s copper exports was K14,535 per tonne in the September quarter of 2009, a decline of 31.0 percent from the corresponding quarter of 2008. This outcome was mainly attributed to the decline in international prices as a result of lower demand, compared to the corresponding period of 2008. The decline in export price more than offset the increase in volume resulting in a 30.4 percent decline in export receipts to K671.5 million in the September quarter of 2009, from the corresponding quarter of 2008.

Crude oil export volumes in the September quarter of 2009 was 2,389.9 thousand barrels, a decline of 2.6 percent from the corresponding quarter of 2008. The decline reflected lower extraction rates and production from the Moran, South East Mananda, Gobe Main and South East Gobe oil fields. The average export price of crude oil was K198 per barrel in the September quarter of 2009, a decline of 45.0 percent from the corresponding quarter of 2008, due to lower interna-
tional prices. This outcome was due to lower demand for crude oil based final products and high level of stocks in the September quarter of 2009, compared to the corresponding quarter in 2008. The combined decline in export price and volume resulted in export receipts of K473.0 million in the September quarter of 2009, a decline of 46.5 percent from the corresponding quarter of 2008.

Export receipts of refined petroleum products from the Napa Napa Oil Refinery in the September quarter of 2009 was K93.6 million, a decline of 59.7 percent from the corresponding period of 2008. The decline was mainly due to significantly lower international prices of refined petroleum products.

Agriculture, Logs and Fisheries Exports

With the exception of cocoa, export prices of most agricultural export commodities declined in the September quarter of 2009, compared to the corresponding quarter of 2008. Coffee prices declined by 3.2 percent, palm oil by 26.3 percent, copra by 38.2 percent, copra oil by 46.8 percent, tea by 1.8 percent and rubber by 43.7 percent. The average export price of logs was K216 per cubic metre in the September quarter of 2009, an increase of 21.3 percent from the corresponding quarter of 2008. The net effect of these price movements was a 11.1 percent decline in the weighted average price of agricultural, logs and marine export products. Excluding logs, the weighted average price of agricultural and marine export products declined by 15.7 percent in the September quarter of 2009, compared to the corresponding period of 2008.

The volume of coffee exported in the September quarter of 2009 was 20,200 tonnes, a decline of 6.0 percent from the corresponding quarter of 2008. The outcome was due to lower production combined with maintaining high stock levels by exporters in anticipation of a price increase. The average export price of coffee was K7,688 per tonne in the September quarter of 2009, a decline of 3.2 percent from the corresponding quarter of 2008. This outcome was due to lower international prices resulting from higher production and shipment from Uganda, India and Vietnam caused by favourable weather conditions, combined with lower demand associated with global economic downturn. The combined declines in export price and volume resulted in export receipts of K155.3 million in the September quarter of 2009, a decline of 9.0 percent from the corresponding period of 2008.

The volume of cocoa exported in the September quarter of 2009 was 15,500 tonnes, a decline of 7.7 percent from the corresponding quarter of 2008. The decline was attributed to lower production as a result of the cocoa pod borer disease which affected production from East New Britain Province, one of the major cocoa producing provinces. The average export price of cocoa was K7,213 per tonne in the September quarter of 2009, an increase of 3.0 percent from the corresponding period of 2008. This outcome was due to higher international prices resulting from lower production and shipment from the Ivory Coast, Brazil, Indonesia and Nigeria due to aging plantations and unfavourable weather conditions. The decline in export volume more than offset the increase in price and resulted in a decline in export receipts by 5.0 percent to K111.8 million in the September quarter of 2009, compared to the corresponding period of 2008.

The volume of copra exported in the September quarter of 2009 was 5,200 tonnes, a decline of 45.3 percent from the corresponding quarter of 2008. The decline was attributed to rising cost of production of copra due to higher fuel and freight costs which forced most producers to cultivate alternate cash crops. The average export price for copra was K904 per tonne in the September quarter of 2009, a decline of 38.2 percent from the corresponding quarter of 2008. The outcome was mainly due to higher production and exports by Philippines, the world’s major producer. The combined declines in export price and volume resulted in export receipts of K4.7 million in the September quarter of 2009, a decline of 66.2 percent from the corresponding period of 2008.

The volume of copra oil exported in the September quarter of 2009 was 11,400 tonnes, a decline of 19.1 percent from the corresponding period of 2008. The decline was mainly due to lower volumes of copra purchased by the two domestic copra oil mills for processing and exporting due to lower production resulting from rising costs of inputs used for production. The average export price of copra oil was K1,904 per tonne in the September quarter of 2009, a decline of 46.8 percent from the corresponding period of 2008. The outcome was due to lower international prices resulting from higher production of copra by Philippines, the world’s major producer. The combined declines in export price and volume resulted in export receipts of K21.7 million in the September quarter of 2009, a decline of 57.0 percent from the corresponding period of 2008.
The volume of palm oil exported in the September quarter of 2009 was 84,100 tonnes, a decline of 2.8 percent from the corresponding period of 2008. The outcome was due to the marginal decline of export volume from Poliamba and Milne Bay Estate which more than offset the increase in export volumes from other exporters. The average export price of palm oil was K1,730 per tonne in the September quarter of 2009, a decline of 26.3 percent from the corresponding quarter of 2008. The decline reflected lower international prices as a result of higher production from Malaysia and Indonesia caused by favourable weather conditions. The combined decline in export price and volume resulted in export receipts of K145.5 million in the September quarter of 2009, which is 28.3 percent lower than the corresponding period of 2008.

The volume of tea exported in the September quarter of 2009 was 1,400 tonnes, a decline of 6.7 percent from corresponding quarter of 2008. The decline was due to lower production caused by unfavourable dry weather conditions. The average export price of tea was K3,143 per tonne in the September quarter of 2009, a decline of 1.8 percent from the corresponding period of 2008. The combined decline in export price and volume resulted in an 8.3 percent decline in export receipts to K4.4 million in the September quarter of 2009, from the corresponding period of 2008.

The volume of rubber exported in the September quarter of 2009 was 1,700 tonnes, an increase of 30.8 percent from the corresponding quarter in 2008. The increase was due to favourable weather conditions. The average export price was K3,765 per tonne in the September quarter of 2009, a decline of 43.7 percent from the corresponding period of 2008. The outcome was associated with lower international prices as a result of increased supply of rubber combined with lower global demand in the world market. The decline in price more than offset the increase in volume and resulted in export receipts of K6.4 million in the September quarter of 2009, 26.4 percent lower than in the corresponding period of 2008.

The volume of logs exported in the September quarter of 2009 was 450,000 cubic metres, a decline of 2.4 percent from the corresponding period of 2008. The outcome was mainly attributed to lower production and shipment from major logging projects due to unfavourable wet weather conditions. The average export price of logs was K216 per cubic metre in the September quarter of 2009, an increase of 21.3 percent from the
corresponding period of 2008. This outcome was due
to higher international prices reflecting higher demand
from Asia, especially China. The increase in export
price more than offset a decline in volume and resulted
in export receipts of K97.1 million in the September
quarter of 2009, an increase of 18.1 percent from the
corresponding period of 2008.

The value of marine products exported was K30.0
million in the September quarter of 2009, a significant
decline of 70.3 percent from the corresponding period
of 2008. The outcome was due to declines in export
price and volume.

5. BALANCE OF PAYMENTS

The overall surplus in the balance of payments for the
nine months to September 2009 was K833 million,
compared to a surplus of K560 million in the corre-
sponding period of 2008. This was due to a significant
surplus in the capital and financial accounts, which
more than offset a deficit in the current account.

The deficit in the current account was attributed to a
lower trade surplus, higher net service payments and
lower net transfer receipts. The surplus in the capital
and financial accounts was due to a higher net inflow
of direct investments mainly from share placements by
a resident mineral company to raise capital for on-
going and operating capital related expenditures and
investments in financial derivatives through hedge
arrangements. The net inflow from other investments
reflects a draw down of: net foreign assets of the
banking system; and foreign currency account bal-
ances of resident mineral companies.

During the nine months to September 2009, the kina
appreciated against the currencies of Papua New
Guinea’s major trading partners with the exception of
the Japanese yen, compared to the corresponding
period of 2008.

The trade account recorded a surplus of K2,876 million
in the nine months to September 2009, a decline of
49.5 percent from the corresponding period of 2008.
The lower surplus was due to a decline in the value of
merchandise exports, despite a decline in the value of
merchandise imports. The value of merchandise ex-
ports in the nine months to September 2009 was
K8,538 million, a decline of 30.3 percent from the
corresponding period of 2008. The decline was attrib-
uted to lower values of copper, crude oil, coffee, cocoa,
palm oil, copra, copra oil, tea, rubber, marine products,
other non-mineral and refined petroleum product ex-
ports.

The value of merchandise imports was K5,662 million
in the nine months to September 2009, a decline of
13.6 percent from the corresponding period of 2008.
There was a decline in imports by all sectors. General
imports declined by 10.2 percent to K4,113 million in
the nine months to September 2009, compared to the
corresponding period of 2008. Mining sector imports
dropped by 24.4 percent to K1,041 million in the nine
months to September 2009, compared to the corre-
sponding period of 2008. The decline reflected lower
capital expenditure undertaken by Ok Tedi and Porgera
mines, which more than offset an increase in imports
by Lihir gold mine. Petroleum sector imports declined
by 15.2 percent to K508 million in the nine months to
September 2009, compared to the corresponding pe-
riod of 2008.

The deficit in the services account was K3,122 million
in the nine months to September 2009, an increase of
12.0 percent from the corresponding period of 2008.
The outcome was due to higher payments for educa-
tion, computer and information, other business, con-
struction and refining and smelting services, combined
with lower service receipts by resident companies.

The deficit in the income account was K917 million in
the nine months to September 2009, a decline of 22.5
percent from the corresponding period of 2008. This
outcome was due to lower payments of dividend and
interest on foreign loans, combined with lower income
receipts.

The surplus in the transfers account was K258 million
in the nine months to September 2009, a decline of
23.9 percent from the corresponding period of 2008.
This outcome was due to lower payments for family
maintenance, gifts and grants and tax, combined with
lower transfer receipts for gifts, grants and tax.

As a result of these developments in the trade, serv-
cices, income and transfers accounts, the current
account recorded a deficit of K905 million in the nine
months to September 2009, compared to a surplus of
K2,068 million in the corresponding period of 2008.

The capital account recorded a lower net inflow of K58
million in the nine months to September 2009, compared to the corresponding period of 2008. The decline reflected lower capital inflows by donor agencies for project financing.

The financial account recorded a net inflow of K1,725 million in the nine months to September 2009, compared to a net outflow of K1,674 million in the corresponding period of 2008. This outcome reflected a higher net inflow from direct investments, due to equity investments into a mineral company, drawdown from investments in financial derivative instruments and foreign currency account balances of mineral companies. There was also a net inflow of other investments, reflecting drawdown of: net foreign assets of the banking system; and foreign currency account balances of resident mineral companies.

In the September quarter of 2009, the balance of payments recorded an overall surplus of K169 million, compared to a deficit of K88 million in the corresponding quarter of 2008.

The value of merchandise exports was K3,057 million in the September quarter of 2009, a decline of 24.7 percent from the corresponding quarter of 2008. The decline was due to lower export values of copper, crude oil, coffee, cocoa, palm oil, copra, copra oil, tea, rubber, other non-mineral and refined petroleum products exports.

The value of merchandise imports was K1,861 million in the September quarter of 2009, a decline of 13.5 percent from the corresponding quarter of 2008. This outcome was due to lower general and petroleum imports which more than offset an increase in mining imports. General imports declined by 13.5 percent to K1,310 million in the September quarter of 2009, compared to the corresponding quarter of 2008. Imports by the petroleum sector declined by 40.5 percent to K140 million in the September quarter of 2009, compared to the corresponding quarter of 2008. Imports by the petroleum sector declined by 40.5 percent to K140 million in the September quarter of 2009, compared to the corresponding quarter of 2008. Mining sector imports increased by 1.6 percent to K411 million in the September quarter of 2009, compared to the corresponding quarter of 2008. The increase was due to higher capital expenditure undertaken by the Porgera and Lihir gold mines, which more than offset a decline from the Ok Tedi gold mine.

The deficit in the services account was K1,301 million in the September quarter of 2009, an increase of 47.0 percent from the corresponding quarter of 2008.
higher deficit was due to increases in service payments for transportation, insurance, other financial, computer and information, construction and refining and smelting services. These more than offset higher service receipts by resident companies.

The deficit in the income account was K396 million in the September quarter of 2009, a significant decline of 155.5 percent from the corresponding quarter of 2008. This outcome was due to a decline in interest and dividend payments by resident companies.

The deficit in the transfers account was K9 million in the September quarter of 2009, compared to a surplus of K14 million in the corresponding quarter of 2008. The outcome was mainly due to lower gifts and grants receipts.

As a result of these developments in the trade, services, income and transfers accounts, the current account recorded a deficit of K510 million in the September quarter of 2009, compared to a surplus of K883 million in the corresponding quarter of 2008.

The capital account recorded a lower net inflow of K10 million during the September quarter of 2009, compared to the corresponding period of 2008. This reflected lower capital transfers by donor agencies for project financing.

The financial account recorded a net inflow of K702 million in the September quarter of 2009, compared to a net outflow of K1,039 million in the corresponding period of 2008. This outcome was due to net inflows for direct investments reflecting equity investments in a mineral company, drawdown from investments in portfolio and financial derivative instruments and drawdown from foreign currency account balances of resident mineral companies. These more than offset net outflows reflecting net loan repayments by the Government and a build-up in the net foreign assets of commercial banks.

The level of gross foreign exchange reserves at the end of September 2009 was K6,155.0 (US$2,349) million, sufficient for 9.8 months of total and 13.5 months of non-mineral import cover.

6. MONETARY DEVELOPMENTS

INTEREST RATES AND LIQUIDITY

The Bank of Papua New Guinea maintained a tight monetary policy stance during the September quarter of 2009 as stated in the September 2009 Monetary Policy Statement (MPS). The Kina Facility Rate (KFR) was kept unchanged at 8.00 percent and the dealing margin for the Repurchase Agreements (Repos) was also maintained at 100 basis points on both sides of the KFR.

Interest rates for short-term securities showed declining trends across most maturities during the September quarter of 2009. At the CBB auction, the 28-day rate declined to 6.35 percent from 6.47 percent, 63-day to 6.02 percent from 6.80 percent and 91-day rates to 6.62 percent from 6.85 percent, respectively. Despite the Central Bank’s action to diffuse excess liquidity and align domestic interest rates with the KFR, excess demand for CBBS exerted downward pressure on the CBB rates. At the Treasury bill auction, the 182-day Treasury bill rate declined to 6.65 percent from 7.50 percent, while the 365-day rate increased to 7.98 percent from 7.96 percent. There was no auction for the 91-day maturity. The weighted average deposit rates quoted by commercial banks on wholesale deposits (K500,000 and above) declined. The 30-day rate decreased to 5.70 percent from 6.26 percent, 60-day rate to 5.67 percent from 5.94 percent, 90-day rate to 6.21 percent from 6.38 percent and 180-day rate declined to 6.09 percent from 6.10 percent. The weighted average interest rate on total deposits paid by commercial banks increased to 2.6 percent from 2.5 percent, while the weighted average interest rate on total loans increased to 10.5 percent from 10.1 percent. The commercial banks’ Indicator Lending Rates (ILR) spread remained at 10.95 – 11.95 percent during the period.

The Bank continued to utilise Open Market Operation (OMO) instruments in the conduct of monetary policy over the September quarter of 2009. The issuance of CBBS during the quarter helped to diffuse excess liquidity. The commercial banks used the interbank market to meet their daily liquidity needs. The CRR and the MLAR of commercial banks were maintained at 3.0 percent and 25.0 percent, respectively, over the September quarter 2009.
MONEY SUPPLY

The average level of broad money supply (M3*) increased by 7.0 percent in the September quarter of 2009, compared to an increase of 4.1 percent in the June quarter. This outcome was mainly due to a significant increase of 209.6 percent in average net claims on the Central Government following higher issuance of Treasury bills and withdrawal of Government deposits, 4.4 percent increase in average net private sector credit and an increase of 1.0 percent in average net foreign assets of depository corporations. Net domestic claims outstanding, excluding advances to the Central Government and outstanding loans under the Government’s Agricultural export commodity price support schemes increased by 4.1 percent in the September quarter of 2009, compared to an increase of 2.9 percent in the June quarter of 2009. The average level of monetary base increased by 5.1 percent in the September quarter of 2009, compared to a decline of 18.0 percent in the June quarter of 2009. The increase reflected higher deposits of commercial banks at the Central Bank and currency in circulation.

The average level of narrow money supply (M1*) increased by 8.5 percent in the September quarter of 2009, compared to a decline of 2.6 percent in the June quarter of 2009. This was due to an increase in both transferable deposits and currency in circulation. The average level of quasi money increased by 5.4 percent in the September quarter of 2009, compared to an increase of 11.6 percent in the June quarter of 2009, mainly due to an increase in term deposits.

The average level of deposits of the ODCs increased by 4.1 percent to K12,598.7 million in the September quarter of 2009 from K12,101.9 million in the June quarter of 2009, due to an increase in transferable and other deposits, which more than offset a decline in average Central Government deposits.

LENDING

During the September quarter of 2009, total domestic credit extended by depository corporations to the private sector, public non-financial corporations, Provincial and Local Governments, and other financial corporations, increased by K192.9 million to K6,264.9 million, compared to an increase of K220.5 million in the June quarter of 2009. This was mainly due to an increase of K196.8 million in private sector credit.
Credit to the private sector comprised lending to the agriculture, forestry and fisheries, manufacturing, transport and communication, building and construction, other business services sectors and housing advances to the household sector. There were no repayments under the price support schemes. The annualised growth in domestic credit, excluding Central Government and advances under the price support schemes was 29.7 percent in the third quarter of 2009.

7. PUBLIC FINANCE

Preliminary estimates of the fiscal operations of the National Government over the nine months to September 2009 show an overall surplus of K541.3 million, compared to a surplus of K885.8 million in the corresponding period of 2008. This represents 2.6 percent of nominal GDP.

Total revenue, including foreign grants, during the nine months to September 2009 was K4,063.8 million, 11.6 percent lower than the receipts collected in the corresponding period of 2008. This represents 55.9 percent of the budgeted revenue. The decline reflected low tax receipts during the period, which more than offset increases in non-tax revenue and foreign grants.

Total tax revenue amounted to K3,396.1 million, 21.7 percent lower than the receipts collected during the same period in 2008, and represents 73.6 percent of the budgeted tax receipts for 2009. Direct tax receipts totalled K2,253.0 million, 32.4 percent lower than the receipts collected during the corresponding period in 2008, and represents 74.0 percent of the budgeted amount. This outcome reflected declines in company and other direct tax receipts, which more than offset an increase in personal income tax. The decline in company tax receipts reflected lower mining and petroleum taxes associated with lower international commodity prices due to the economic recession. The decrease in other direct tax receipts was attributed to lower collections in dividend withholding tax and stamp duty receipts. The increase in personal income tax was due to higher remuneration and employment resulting from increased domestic economic activities.

Indirect tax receipts was K1,143.1 million, 13.8 percent higher than in the corresponding period in 2008, and represents 72.8 percent of the budgeted receipts for 2009. The increase was attributed mainly to higher
Goods and Services Tax (GST) collection, and import duties and excise duties to an extent, which more than offset declines in export tax and other indirect tax receipts. The increase in GST receipts reflected increased domestic economic activity resulting in higher collections in the main contributing provinces. The decline in export tax reflected lower log export volumes due to the appreciation of the kina exchange rate, while the decline in other indirect tax receipts reflected lower payment of arrears for mining levy.

Total non-tax revenue amounted to K559.5 million, K413.1 million higher than the amount collected in the corresponding period of 2008. The increase was mainly due to transfer from the gas commercialisation trust account and an increase in other internal revenue collected by National Departments, which more than offset a decline in the dividend payments by statutory bodies. Foreign grants amounted to K108.2 million compared to K93.2 million in the corresponding period of 2008, while Infrastructure tax credits were not reported during the period.

Total expenditure over the nine months to September 2009 was K3,522.5 million, 5.1 percent lower than in the corresponding period of 2008, and represents 52.8 percent of the budgeted expenditure for 2009. This was due to lower development expenditure, which more than offset an increase in recurrent expenditure.

Recurrent expenditure over the nine months of 2009 was K2,928.8 million, 2.5 percent higher than in the corresponding period of 2008, and represents 75.0 percent of the budgeted appropriation for 2009. The increase came from higher Provincial Government spending, interest payments, and grants to Statutory Bodies. National Departmental expenditure totalled K1,694.4 million, 6.6 percent lower than the amount spent during the same period in 2008, and represents 71.7 percent of the budgeted appropriation. The decrease reflected lower payments for departmental goods and services, which more than offset an increase in disbursement of personnel emoluments. Provincial Government expenditure was K759.6 million, 23.5 percent higher than the expenditure level during the same period in 2008, and represents 84.7 percent of the budgeted amount. There were increases in the disbursement of personal emoluments, payments for goods and services in the provinces and an increased allocation to the Bougainville Autonomous Government. Interest payments totalled K254.9 million, 11.4 percent higher than in the corresponding period of 2008, and represents 64.9 percent of budgeted expenditure. The increase reflected higher interest payments on Inscribed stocks and Treasury bills due to increase in issuance.

Total development expenditure for the first nine months of 2009 was K593.7 million, 10.2 percent lower than in the corresponding period of 2008, and represents 22.9 percent of the budgeted expenditure for 2009. The lower development outlay on projects reflected capacity constraints in the implementation of the 2009 Development Budget.

As a result of these developments in revenue and expenditure, the Government recorded an overall budget surplus of K541.3 million over the nine months to September 2009. The surplus was used to make net external loan repayments of K125.8 million and net negative financing to domestic sources of K415.5 million. The net overseas loan repayments comprised of K85.7 million, K9.8 million and K30.2 million respectively to concessionary, commercial and extraordinary loan sources. The net negative financing to domestic sources comprised of K1,019.3 million in cheque floats that were settled, which more than offset a net draw down of K603.8 million from Government deposits, mainly trust account funds, at the Central Bank. The net draw down comprised of K1,292.0 million in withdrawal from Government deposits at the Central Bank, K645.5 million in Government deposits at commercial banks’ and K42.7 million repayment of Treasury bills to other financial corporations.
Executive Summary

Inflation intensified in 2008 mainly due to a larger than expected fiscal deficit and high international oil and food prices, with inflation reaching 13.5 percent in the September quarter of 2008. The large fiscal deficit in 2008, and high inflation outcomes in the second half of 2008 and early 2009 attest to the correlation between excessive Government expenditure and inflation as alluded to in the March 2009 Monetary Policy Statement (MPS). In spite of the understanding between the Bank and the Government to have the trust account funds moved to the Central Bank, most of these accounts continue to remain with commercial banks. As a result, the Bank did all it could to absorb excess liquidity and contain inflation by issuing a substantial amount of Central Bank Bills (CBBs) over the nine months to September 2009, in line with the tight monetary policy stance.

The Government has already revised its 2009 budget to a higher deficit of 1.2 percent of GDP. This is a matter of serious concern to the Bank as it can be a repeat of 2008 and the late 1990s where excessive Government spending translates to high domestic demand and high inflation.

Looking forward into the medium term, continuing high Government expenditure in addition to an expected increase in domestic demand associated with the Liquefied Natural Gas (LNG) project can further exacerbate inflationary pressures. The Central Bank on its own does not have enough instruments to deal with inflationary pressures generated by fiscal operations. Therefore, it is absolutely necessary that there must be close coordination between monetary and fiscal management to achieve and maintain price stability.

Inflation has come down over the first six months of 2009 to 6.7 percent in the June quarter, as a result of the lag pass-through of declines in international food and fuel prices, appreciation of the kina exchange rate in the second half of 2008, and lower prices of domestic seasonal produce. However, due to ongoing inflationary pressures, the Central Bank maintained its tight stance of monetary policy over the period, keeping the Kina Facility Rate (KFR) unchanged at 8.00 percent.

As a result of the tight stance of monetary policy, private sector credit slowed down to 19.5 percent, limiting the growth in money supply to 10.2 percent in August 2009. However, persistently high liquidity remained in the banking system for most of 2009, mainly as a result of Government expenditure. Consistent with the tight stance of monetary policy, the Central Bank utilized the available instruments to diffuse liquidity. This was done through the issuance of a substantial amount of CBBs over the nine months to September 2009. It is therefore important that the Government’s management of fiscal policy, including efforts to transfer some of the trust account funds to the Central Bank, complements the Bank’s effort at managing monetary policy.

The global recession that began in 2008 adversely impacted on PNG’s export sector, resulting in the current account recording a deficit and the kina slightly depreciating in the nine months to September 2009. As a result, domestic economic activity and inflation slowed down.

Given the above developments, the Bank projects for 2009:

- Headline inflation to be around 6.5 percent;
- Private sector credit to grow by 15.0 percent; and
- Real Gross Domestic Product (GDP) growth to be around 5.0 percent.

With these projections and potential inflationary pressures, the Bank will maintain its current tight stance of monetary policy over the next six months.

Over the medium term, inflation is projected to be around 5.0 percent in 2010 and 6.0 percent in 2011. The major upside risks to the Bank’s inflation forecasts are: a significant depreciation of the kina exchange rate; high imported inflation; excessive Government expenditure; a rapid draw down of trust account funds; and additional domestic
demand pressures associated with the LNG project.

The Bank will assess these developments and their potential effects on price stability and make adjustments to the monetary policy stance as appropriate.
1.0 Monetary Policy Discussions

1.1 Monetary Policy Assessment and Issues

The large fiscal deficit of K478.5 million in 2008 contributed to the high domestic demand, resulting in high inflation outcomes in the second half of 2008 and early 2009. This outcome re-affirmed the correlation between excessive Government expenditure and inflation, which the Bank alluded to in the March 2009 MPS. Despite the consensus between the Bank and the Government to have the trust account funds with the commercial banks transferred to the Central Bank, most of the accounts continue to remain with commercial banks. Therefore the Bank did all it could to contain inflation by issuing a substantial amount of CBBs over the nine months to September 2009, to absorb excess liquidity in line with its tight monetary policy stance. The tight stance of policy led to lower growth in money supply, mainly resulting from a slowdown in private sector credit growth. This, combined with the pass-through of lower international food and fuel prices, and appreciation in the kina exchange rate contributed to the lower rate of inflation in the first half of 2009.

Inflation has progressively declined over successive quarters, from a high of 13.5 percent in the September quarter of 2008 to 6.7 percent in the June quarter of 2009. Whilst the lower rate of inflation is a favorable development, the Bank is mindful of the upside risks in 2009 and the medium term that could come from: a weaker kina exchange rate; imported inflation; and domestic demand pressures associated with increased Government spending, especially a fast drawdown of trust account funds and the LNG project. Therefore, the Bank has maintained the tight stance of monetary policy leaving the KFR at 8.00 percent since December 2008.

Annual growth in broad money supply (M3*) and the monetary base were 10.2 percent and negative 14.3 percent, respectively, over the year to August 2009. The low growth in broad money supply, which was mainly attributed to the slow down in private sector credit to 19.5 percent in August 2009, and the negative growth in the monetary base reflected the tight stance of monetary policy. To diffuse excess liquidity from the banking system and counter inflationary pressures, the Bank issued net new CBBs totaling K1,520.9 million over the nine months to 2009. Every effort by the Government to transfer some trust accounts from commercial banks to the Central Bank and maintain expenditure within budget would support the Bank’s management of monetary policy.

The Government has already revised its 2009 budget to a higher deficit of 1.2 percent of GDP. This is a matter of concern to the Bank as it can be a repeat of 2008 and the late 1990s, where excessive Government spending translates to high domestic demand and high inflation.

Looking forward into the medium term, continuing high Government expenditure in light of the LNG associated demands can further exacerbate inflationary pressures. Close coordination between monetary and fiscal management is therefore required to achieve and maintain price stability.

Global economic activity remained depressed in the first half of 2009, however there have been signs of recovery in recent months, following appropriate monetary policy actions and large fiscal stimulus measures in the major economies. In line with the decline in global demand, inflation in the major economies has been low. The global recession has adversely affected PNG’s export sector, with the current account recording a deficit in the first half of 2009 and lowering growth prospects for the year.

In 2009, broad money supply is expected to grow by 7.4 percent, reflecting a moderation in growth of credit to the private sector, while monetary base is expected to grow by 4.1 percent, indicative of the tight monetary policy stance. Whilst this could counter inflation in the short term, the Bank is mindful of the impact of a further slowdown in credit growth and global recession on economic growth.

Preliminary estimates of the Government’s fiscal operations indicate a surplus of K387.7 million for the first six months of 2009. This was mainly due to the use of K423.0 million from the Gas Commercialization Trust Account held at the Central Bank and treated as revenue in 2009. Government expenditure and revenue were within budget but were below 50 percent of the budgeted amount in the first half of the year. Recurrent expenditure represented 47.7 percent and development expenditure represented 12.7 percent of the budgeted amounts. The poor performance of the development budget in the first half of the year is of concern, drawing attention to the on going capacity issues of implementing agencies. This has implications on the Government’s Medium Term Development Strategy.
The Government has revised upwards its forecast of the budget deficit to 1.2 percent of GDP for 2009, due to lower than forecasted revenue. The deficit will be financed domestically, which has the potential to crowd out private sector credit and exert upward inflationary pressures.

For the medium term, the Bank’s projections of key macroeconomic indicators have not taken into account the impact of the proposed LNG project, particularly on GDP and balance of payments (BOP), given the unavailability of relevant data and pending final project decision.

The Bank will closely monitor the above developments in the next six months and their potential impact on inflation and price stability, and make appropriate changes to the stance of monetary policy.

1.2 Monetary Policy Stance

Inflation has moderated in the first half of 2009. However, in view of the potential inflationary pressures, the Bank will maintain its current tight stance of monetary policy in the next six months.

In line with the stance, the Bank has issued a substantial amount of CBBs to absorb persistent excess liquidity in the banking system for most of 2009, which was mainly a result of Government expenditure. To achieve low inflation outcomes for 2009 and the medium term, a closer co-ordination is required between fiscal and monetary policies. In that regard, it is necessary that fiscal policy is prudently managed in line with the budget framework and the Government’s medium term policies.

The Bank projects broad money supply to grow by 7.4 percent and the monetary base by 4.1 percent in 2009. Private sector credit is expected to slow further to 15.0 percent in 2009, as the increase in cost of borrowing will slow aggregate demand. This is considered sufficient to support economic activity.

The Bank projects that headline inflation to be around 6.5 percent in 2009. Upside risks to this projection could arise from:

- A larger than expected depreciation of the kina exchange rate;
- Increase in imports for early works and construction and related activities with the LNG project;
- Excessive Government expenditure and a rapid draw down of trust account funds; and
- Other unforeseen external and domestic shocks.

The Bank will assess these developments and, if necessary, make appropriate adjustments to the stance of monetary policy in the coming six months.

1.3 Conduct of Monetary Policy

Monetary policy will be conducted within the reserve money framework. The Monetary Policy Statement (MPS) provides the overall monetary policy stance, while the monthly KFR remains the instrument for signalling this stance or any changes through an announcement by the Governor. Following the announcement, Open Market Operations (OMOs) will be conducted to support the Bank’s monetary policy stance. The OMOs involve Repurchase Agreement (Repo) transactions with commercial banks and the auction of CBBs to licensed ODCs and Treasury bills to the general public.

The Bank is committed to adopting appropriate monetary policy management strategies that will help to achieve price stability.

2.0 Developments and Expectations

2.1 International Developments

The global economic recession, which started in 2008, continued into the first half of 2009. The most severe part of the recession appears to have passed as the impact of stimulus measures taken by many economies around the world have begun to result in modest gains in some key financial and economic indicators. The positive indications include: the significant pick-up in economic growth in India and China; recovery in Australia following one quarter of negative growth; and some gains made in the manufacturing and industrial sectors in the USA, Japan and the Euro area for the first time since early 2008. The economic conditions, however, remain weak and fragile, and a recovery in global growth is not expected until 2010. According to the International Monetary Fund’s (IMF) July update of its World Economic Outlook (WEO), global economic growth is expected to contract by 1.4 percent in 2009 before expanding by 2.5 percent in 2010.
Economic conditions among advanced economies continue to remain weak although the rate of deterioration is diminishing. US economic growth during the second quarter of 2009 contracted by 1.0 percent compared to a contraction of 6.4 percent during the first quarter, mainly reflecting an increase in government spending. In Japan, GDP in the second quarter increased by 3.7 percent after an 11.7 percent decrease in the previous quarter due to a recovery in exports and consumer spending. GDP in the Eurozone fell by only 0.1 percent during the June quarter after contracting by 2.5 percent in the previous quarter, reflecting growth in Germany and France. In the UK, GDP declined by 0.8 percent during the second quarter after contracting by 1.9 percent in the first quarter. The outcome mainly reflected an improvement in business investment and an increase in government expenditure. However, economic activity among the advanced countries continues to be weighted down by deteriorating labor market conditions as unemployment rates continue to surge.

Emerging and developing economies are expected to grow by 1.5 percent in 2009, led by China. GDP in China picked up momentum during the second quarter at an annual rate of 7.9 percent after expanding at its slowest pace in a decade during the first quarter of 6.1 percent. The rebound was mainly attributed to large fiscal stimulus provided by the government to encourage investment and increase bank lending. Other countries in Asia have also benefited from China’s economic growth along with their own fiscal stimulus measures. Less sophisticated financial systems in these emerging and developing economies have also helped them overcome the financial market stress that many advanced economies are still in.

Global inflationary pressures have declined in line with weakening global demand. Headline inflation in advanced economies declined further into negative territory in July as weakening demand contributed to lower commodity prices. Headline inflation in July for the US, Eurozone and Japan declined by 2.1 percent, 0.7 percent and 2.2 percent, respectively. Whilst commodity prices are generally lower compared to a year ago, improving economic conditions in emerging market economies have exerted some upward momentum on commodity prices in recent months. These gains are likely to be minimal given the subdued economic conditions in the advanced economies. Inflation is expected to remain low with the IMF projecting inflation in advanced economies at 0.1 percent in 2009 and 0.9 percent in 2010, compared to 3.4 percent in 2008. In comparison, inflation in emerging and developing countries is projected to be at 5.3 percent in 2009 and 4.6 percent in 2010, lower than 9.3 percent recorded in 2008.

The price of crude oil has increased by about 55
percent since the start of 2009 to currently trading around US$70 per barrel. The increase mainly reflects increasing demand from emerging and developing economies and optimism about global growth. The prices of precious metals such as gold and silver have also increased since the start of 2009. The increase in the price of gold and silver has mainly been attributed to the weakening US dollar. Gold is currently trading around US$950 per ounce and is about 7.0 percent higher from the end of 2008, while silver is trading around the US$16 per ounce.

Major Central Banks maintained an accommodative monetary policy stance in the first half of 2009. They have also continued to inject liquidity to their respective financial systems in various forms, including the buy back of illiquid financial instruments, to foster a gradual improvement in financial conditions. These efforts are expected to continue throughout the remainder of 2009 and into 2010. Since the start of 2009, the US Federal Reserve and the Bank of Japan have maintained their benchmark rates at 0.25 and 0.10 percent, respectively. The European Central Bank and the Bank of England have reduced their official rates by 150 basis points each to 1.00 and 0.50 percent respectively, while the Reserve Bank of Australia has cut its overnight cash rate by 125 basis points to 3.0 percent.

Financial markets have remained volatile in the first half of 2009 with market sentiment driven mainly by economic fundamentals and changes in investor risk appetite. Equity markets have strengthened quite significantly from their lows in March 2009 on the back of better than expected earnings reports and optimism for global recovery. Global bond yields have also increased since the start of 2009, mainly on the back of increased issuance of government securities as part of the stimulus measures. The US dollar has weakened against other major currencies since the beginning of 2009 as investors reverse safe haven trades that have supported the US dollar since the peak of the financial market crisis. These trends in financial markets are expected to continue throughout the remainder of 2009.

2.2 Domestic Economic Conditions

The Bank’s Employment Index over the year to the June quarter of 2009 indicates that the total level of employment in the formal private sector increased by 3.8 percent. The increase was in the building and construction, agriculture/forestry/fisheries, wholesale, mineral and financial/business and other services sectors, which more than offset the decline in the transportation, manufacturing and retail sectors. Excluding the mineral sector, the employment level increased by 3.9 percent over the year to the June quarter. All regions recorded increases, except the Islands and Southern regions.

![Chart 2: Annual Real GDP Growth (percent)](source: Department of Treasury)
The Bank revised downwards its GDP growth projection for 2009 in light of the global recession and falling demand. The Bank’s projection is slightly higher than the Government’s revised projection of 4.8 percent. Decline in sales and lower employment growth in the first half of 2009 support the moderation in growth. All sectors are expected to grow in 2009, except the commerce and petroleum sectors, with notable growth from the building and construction, mining and quarrying sectors, and the communication sub-sector. The increase in the construction sector and its spill-over effects to the other sectors is attributed to the Ramu Nickel/Cobalt and Hidden Valley mines, some early works and initial construction and related activities on the LNG project and major transport infrastructure and building projects undertaken by the Government and private sector. The growth in the mining and quarrying sector will come from increased production of gold at existing mines and commencement of production at the Hidden Valley mine, while the increase in the communication sub-sector reflects the expansion of mobile phone networks by the two mobile phone companies.

For the medium term, the economy is expected to continue to grow at a lower pace. Growth in the building and construction sector is associated with the remaining construction of the Ramu Nickel/Cobalt mine and ongoing construction of Government and private sector funded projects. The increase in the mineral sector reflects the commencement of production by the Ramu Nickel/Cobalt mine, as well as increased production of gold at Lihir and Hidden Valley. Whilst the LNG project was not included in these projections, its full construction and related activities will further support growth.

2.3 Balance of Payments

Preliminary balance of payments data for the six months to June 2009 showed an overall surplus of K663.6 million, compared to a surplus of K648.3 million in the corresponding period of 2008. This outcome was due to a surplus in the capital and financial account, which more than offset a deficit in the current account. The surplus in the capital and financial account was mainly due to a higher net inflow from direct investments reflecting share placements by a resident mineral company to raise capital for on-going capital and operation expenditures. In addition, the surplus reflected investments in financial derivative instruments through hedge arrangements. These more than offset net outflows from investment short-term money market instruments and other investments, combined with lower net loan repayments by the government. The net outflow from other investments was due to a build-up in the net foreign assets of the banking system and foreign currency account balances of resident mineral companies. The deficit in the current account was mainly attributed to a lower trade account balance and lower net transfer receipts. The lower trade account balance resulted from a significant decline in export

---

**Chart 3: Current Account**

source: Bank of PNG
receipts due to lower international prices of most commodities.

The level of gross foreign exchange reserves at the end of June 2009 was US$2,263.7 (K5,985.2) million, sufficient for 9.9 months of total and 13.8 months of non-mineral import covers. As at 31st August 2009, the level of gross foreign exchange reserves was US$2,287.0 (K6,197.9) million.

The IMF’s September 2009 price forecasts indicate that international prices of most of PNG’s non-mineral exports will be lower in 2009, compared to 2008. According to the mineral companies, prices of most mineral exports are also expected to be lower in 2009, except for gold. The lower prices reflect the downturn in global economic activity. In the medium term, international commodity prices are expected to improve as the world economy recovers from the recession.

The volumes of most of PNG’s major non-mineral commodities are projected to decline in 2009 compared to 2008, with the exception of palm oil. The declines are mainly due to lower production as a supply response to lower international prices. In the medium term, non-mineral export volumes are projected to increase as producers anticipate international prices to improve. Mineral commodity export volumes are projected to decline in 2009 compared to 2008, with the exception of gold. The decline in copper exports reflects maintenance work on one of Ok Tedi’s processing plants, lower ore grades and delays in shipment. The increase in gold production is due to the upgrading of the processing plant at Lihir. As a result, the overall balance of payments is projected to be in surplus by K539 million in 2009, compared to a deficit of K598 million in 2008. At the end of 2009 the gross foreign exchange reserves are projected to be around US$2,287.6 (K6,305.4) million, sufficient for 7.8 months of total and 12.4 months of non mineral import cover. Gross reserves are projected to increase over the medium term (see Appendix - Table 2).

2.4 Fiscal Operations of the National Government

Preliminary estimates of the fiscal operations of the National Government over the six months to June 2009 showed an overall surplus of K387.7 million, compared to a surplus of K304.3 million in the corresponding period of 2008. This represents 1.8 percent of nominal GDP and reflects higher non-tax revenue, which more than offset an increase in recurrent expenditure. The budget surplus was used to make net repayments of overseas loans totalling K86.3 million and net negative financing of K301.4 million to domestic sources. The net settlement of cheque floats totalling K362.2 million to other resident sectors more than offset net drawdown of Government deposits of K60.8 million mainly from the Central Bank.

Total revenue, including foreign grants, represented 38.7 percent of the 2009 Budget while total expenditure represented 32.9 percent over the six months to June 2009. The increase in non-tax revenue was mainly due to a reappropriation of K423.0 million from the Gas Commercialisation Trust Account to one-off expenditures. The increase in recurrent expenditure was attributed to higher domestic interest payments and grants.
to statutory bodies. Development expenditure declined by 16.4 percent during the same period and represented 12.7 percent of the budget. This was due to ongoing capacity constraints of implementing agencies combined with non-reporting of projects funded by international aid donors. The Government deposits in depository corporations between end of 2008 and July 2009 increased by K442.8 million to K3,782.2 million, mainly reflecting net deposits at ODCs.

Total debt to nominal GDP ratio increased to 30.0 percent from 27.0 percent between the end of December 2008 and June 2009 reflecting the net issuance of domestic securities. Total domestic debt increased by 26.1 percent to K3,884.8 million, due to higher interest payments and issuance of Inscribed stocks and Treasury bills. Foreign debt decreased by 8.4 percent to K2,778.3 million, reflecting Government repayment of external loans.

In July, the Government revised its forecast for the 2009 budget deficit to be K249.6 million or 1.2 percent of GDP from a K10.3 million deficit in the original budget. This outcome is due to lower mineral taxes, dividend payments from statutory bodies and lower foreign grants.

2.5 Exchange Rate

The kina weakened against the US and Australian dollars by 2.5 percent and 11.0 percent on average to US$0.3610 and AU$0.4852, respectively, during the nine months to September 2009. During the six months to June the Trade Weighted Index (TWI) depreciated by 3.0 percent, whilst the Real Effective Exchange Rate (REER) depreciated by 11.1 percent (see Chart 4). Between June 2009 and September 2009 the kina depreciated against the US dollar by 2.5 percent to average US$0.3682, while it depreciated against the Australian dollar by 8.9 percent to average AU$0.4431. The depreciation of the kina against the US and Australian dollars were due to an increase in import demand.

2.6 Inflation

Annual headline inflation was lower at 6.7 percent in the June quarter of 2009, compared to 10.2 percent in the March quarter. The moderation in inflation mainly reflected lower imported prices, lag effects of the exchange rate appreciation in the second half of 2008 and lower prices of seasonal produce. This was also attributed to a decline in domestic fuel prices reflecting lower international oil prices and appreciation of the kina. All urban areas recorded increases over the year.
to June 2009. Central Bank implementation of its tight monetary policy stance through its OMO assisted in bringing inflation down.

The underlying inflation measures also subsided reflecting some easing in inflationary pressures. Annual exclusion-based inflation was 7.5 percent in the June quarter of 2009, following an increase of 10.7 percent in the previous quarter, while annual trimmed mean inflation recorded 5.0 percent in the June quarter, compared to 7.9 percent in the previous quarter (see chart 5).

The Bank has revised its annual headline inflation for 2009 to be around 6.5 percent, while trimmed-mean inflation and exclusion based measure are projected to be around 4.0 percent and 7.5 percent, respectively. The downward revisions in the headline and trimmed-mean measures from the projections made in the March 2009 Monetary Policy Statement (MPS) are based on the following factors:

• Lower international food and fuel prices in 2009 relative to 2008;
• Lower imported inflation from PNG’s major trading partners;
• Stability in the exchange rates for the rest of 2009; and
• Slowdown in domestic demand as shown by lending, sales and employment data.

For the medium term, headline inflation is projected to be around 5.0 percent in 2010 and 6.0 percent in 2011. The main assumptions used for these projections are that all of PNG’s major trading partners’ currencies are expected to depreciate slightly against the US dollar. Inflation in PNG’s major trading partners is also expected to increase gradually over the medium term. Domestic demand is also expected to generate inflationary pressures.

The upside risks to these projections would be the depreciation of the kina, increasing inflation in the major international economies, and domestic demand pressures associated with the LNG project.

2.7 Monetary and Financial Market Developments

Despite the moderation in inflation in the March and June quarters of 2009, expectations of strong domestic demand, a weaker kina exchange rate and a rapid draw down of Government trust account balances prompted the Bank of Papua New Guinea to maintain a tight monetary policy since March 2009. The KFR was maintained at 8.00 percent over the six months to September 2009 (See Chart 6). The trading margin for the Repo was maintained at 100 basis points on both sides of the KFR in the first half of 2009.

The Bank issued net new CBBs totalling over K1,520.9 million to diffuse excess liquidity in the banking system over the nine months to September 2009. As a
Total liquidity of the banking system increased by 25.6 percent to K6,178.2 million over the twelve months to August 2009, mainly due to increase in net Government expenditure. Lending extended by ODCs to the private sector increased by 19.5 percent over the twelve months to August 2009. The growth in private sector credit was broad based across all sectors, mainly to the mining, petroleum, retail/wholesale and construction sectors. This was due to the continued strong domestic demand in the first half of 2009 and increased business activities partly associated with expectation of benefits from LNG projects. Net claims on the Government declined by K1,619.1 million over the twelve months to July 2009, mainly due to an increase in Trust Account deposits in ODCs.

The level of broad money supply (M3*) increased by 10.2 percent over the twelve months to August 2009 as a result of growth in private sector credit, which more than offset the decline in net credit to Government. The monetary base declined by 14.3 percent during the same period, mainly reflecting the decline in the Exchange Settlement Accounts of the commercial banks’ held at the Central Bank (see Appendix-Table 1).
### Appendix

#### Table 1: Monetary and Credit Aggregates (annual % changes)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Broad Money Supply</td>
<td>30.7</td>
<td>39.0</td>
<td>27.3</td>
<td>11.2</td>
<td>10.2</td>
<td>11.5</td>
<td>7.4</td>
<td>6.0</td>
<td>9.9</td>
</tr>
<tr>
<td>Monetary Base</td>
<td>3.0</td>
<td>21.7</td>
<td>61.8</td>
<td>-12.0</td>
<td>-14.3</td>
<td>-9.7</td>
<td>4.1</td>
<td>3.4</td>
<td>7.2</td>
</tr>
<tr>
<td>Claims on the Private Sector</td>
<td>25.2</td>
<td>36.8</td>
<td>30.8</td>
<td>39.4</td>
<td>19.5</td>
<td>11.3</td>
<td>15.0</td>
<td>13.9</td>
<td>9.6</td>
</tr>
<tr>
<td>Net Claims on Gov't</td>
<td>-24.7</td>
<td>-11.6</td>
<td>-83.5</td>
<td>-174.3</td>
<td>-134.3</td>
<td>-473.4</td>
<td>122.1</td>
<td>-277.4</td>
<td>138.5</td>
</tr>
<tr>
<td>Net Foreign Assets</td>
<td>33.5</td>
<td>58.2</td>
<td>51.7</td>
<td>-9.4</td>
<td>-8.2</td>
<td>-1.1</td>
<td>13.4</td>
<td>-5.9</td>
<td>4.4</td>
</tr>
</tbody>
</table>

Source: Bank of PNG

#### Table 2: Summary of Other Macroeconomic Indicators

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>CONSUMER PRICE INDEX</strong> (annual % changes)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Headline</td>
<td>4.6</td>
<td>1.3</td>
<td>3.2</td>
<td>11.2</td>
<td>6.7</td>
<td>7.0</td>
<td>6.5</td>
<td>5.0</td>
<td>6.0</td>
</tr>
<tr>
<td>Trimmed-mean</td>
<td>3.3</td>
<td>0.4</td>
<td>6.0</td>
<td>11.7</td>
<td>5.0</td>
<td>7.0</td>
<td>4.0</td>
<td>4.5</td>
<td>6.0</td>
</tr>
<tr>
<td>Exclusion-based</td>
<td>-1.4</td>
<td>2.9</td>
<td>6.0</td>
<td>11.0</td>
<td>7.5</td>
<td>3.0</td>
<td>7.5</td>
<td>5.0</td>
<td>6.0</td>
</tr>
<tr>
<td><strong>BALANCE OF PAYMENTS</strong> (kina millions)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Current account</td>
<td>2,009</td>
<td>1,354</td>
<td>550</td>
<td>2,145</td>
<td>-361</td>
<td>-1,418</td>
<td>-1,269</td>
<td>1,102</td>
<td>278</td>
</tr>
<tr>
<td>Financial account</td>
<td>-1,714</td>
<td>618</td>
<td>1,001</td>
<td>-2,796</td>
<td>976</td>
<td>1,116</td>
<td>1,808</td>
<td>861</td>
<td>-2</td>
</tr>
<tr>
<td>Overall balance</td>
<td>296</td>
<td>1,958</td>
<td>1,592</td>
<td>-986</td>
<td>664</td>
<td>-265</td>
<td>538</td>
<td>-242</td>
<td>276</td>
</tr>
<tr>
<td>Gross Int. Reserves</td>
<td>2,368</td>
<td>4,326</td>
<td>5,919</td>
<td>5,322</td>
<td>5,985</td>
<td>5,558</td>
<td>6,305</td>
<td>6,084</td>
<td>6,340</td>
</tr>
<tr>
<td><strong>IMPORT COVER</strong> (months)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>6.0</td>
<td>8.5</td>
<td>9.1</td>
<td>7.9</td>
<td>9.3</td>
<td>7.0</td>
<td>7.8</td>
<td>7.2</td>
<td>7.3</td>
</tr>
<tr>
<td>Non-mineral</td>
<td>8.2</td>
<td>11.5</td>
<td>13.0</td>
<td>11.4</td>
<td>13.8</td>
<td>12.6</td>
<td>12.4</td>
<td>11.1</td>
<td>10.8</td>
</tr>
<tr>
<td><strong>EXPORT PRICE</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Crude oil (US$/barrel)*</td>
<td>55</td>
<td>67.3</td>
<td>73</td>
<td>106.7</td>
<td>46.4</td>
<td>79.2</td>
<td>52.1</td>
<td>53.3</td>
<td>61.6</td>
</tr>
<tr>
<td>Gold (US$/ounce)</td>
<td>403</td>
<td>554.7</td>
<td>671</td>
<td>850.9</td>
<td>914.5</td>
<td>805.6</td>
<td>865.7</td>
<td>772.6</td>
<td>768.5</td>
</tr>
<tr>
<td>Copper (US$/pound)</td>
<td>161.6</td>
<td>296.6</td>
<td>320</td>
<td>327.8</td>
<td>167.6</td>
<td>250.0</td>
<td>168.0</td>
<td>160.0</td>
<td>175.0</td>
</tr>
<tr>
<td><strong>FISCAL OPERATIONS OF THE GOVERNMENT</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Surplus/Deficit (K'm)</td>
<td>7.6</td>
<td>535.8</td>
<td>476.2</td>
<td>-478.5</td>
<td>387.7</td>
<td>-10.3</td>
<td>-249.6</td>
<td>24.8</td>
<td>31.8</td>
</tr>
<tr>
<td>% of GDP</td>
<td>0.1</td>
<td>3.1</td>
<td>2.5</td>
<td>2.2</td>
<td>1.8</td>
<td>0.0</td>
<td>1.2</td>
<td>0.1</td>
<td>0.1</td>
</tr>
<tr>
<td><strong>REAL GROSS DOMESTIC PRODUCT</strong> (annual % growth)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total GDP</td>
<td>3.3</td>
<td>3.7</td>
<td>6.5</td>
<td>7.2</td>
<td>6.2</td>
<td>7.6</td>
<td>6.2</td>
<td>5.2</td>
<td>3.7</td>
</tr>
<tr>
<td>Non-mineral GDP</td>
<td>3.1</td>
<td>4.1</td>
<td>7.3</td>
<td>7.9</td>
<td>5.6</td>
<td>7.1</td>
<td>5.6</td>
<td>4.1</td>
<td>3.9</td>
</tr>
</tbody>
</table>

* Prices take into account company hedging and differ from market prices.

** Fiscal operations for 2009 actuals to June 2009; 2009 projection is from Department of Treasury’s Mid Year Economic and Fiscal Outlook (MYEFO), while 2011 as per the original 2009 National Budget.

*** GDP figures are from the Department of Treasury.

Source: Bank of PNG, NSO and Department of Treasury
MONTHLY KINA FACILITY RATE ANNOUNCEMENTS

The Central Bank introduced the Kina Facility Rate (KFR) in February 2001 as the official rate to indicate its stance of monetary policy. The KFR is a monthly rate and any changes to it should translate to changes in market interest rates. Changes to the KFR is based on assessment of economic fundamentals consistent with the overall objective of monetary policy of price stability in the economy. From January 2007, the KFR announcements by the Bank were;

<table>
<thead>
<tr>
<th>Year</th>
<th>Month</th>
<th>Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007</td>
<td>02 January</td>
<td>Maintained at 6.00 %</td>
</tr>
<tr>
<td></td>
<td>05 February</td>
<td>Maintained at 6.00 %</td>
</tr>
<tr>
<td></td>
<td>05 March</td>
<td>Maintained at 6.00 %</td>
</tr>
<tr>
<td></td>
<td>02 April</td>
<td>Maintained at 6.00 %</td>
</tr>
<tr>
<td></td>
<td>07 May</td>
<td>Maintained at 6.00 %</td>
</tr>
<tr>
<td></td>
<td>04 June</td>
<td>Maintained at 6.00 %</td>
</tr>
<tr>
<td></td>
<td>02 July</td>
<td>Maintained at 6.00 %</td>
</tr>
<tr>
<td></td>
<td>06 August</td>
<td>Maintained at 6.00 %</td>
</tr>
<tr>
<td></td>
<td>03 September</td>
<td>Maintained at 6.00 %</td>
</tr>
<tr>
<td></td>
<td>01 October</td>
<td>Maintained at 6.00 %</td>
</tr>
<tr>
<td></td>
<td>05 November</td>
<td>Maintained at 6.00 %</td>
</tr>
<tr>
<td></td>
<td>03 December</td>
<td>Maintained at 6.00 %</td>
</tr>
<tr>
<td>2008</td>
<td>07 January</td>
<td>Maintained at 6.00 %</td>
</tr>
<tr>
<td></td>
<td>04 February</td>
<td>Maintained at 6.00 %</td>
</tr>
<tr>
<td></td>
<td>03 March</td>
<td>Maintained at 6.00 %</td>
</tr>
<tr>
<td></td>
<td>07 April</td>
<td>Maintained at 6.00 %</td>
</tr>
<tr>
<td></td>
<td>05 May</td>
<td>Maintained at 6.00 %</td>
</tr>
<tr>
<td></td>
<td>02 June</td>
<td>Maintained at 6.00 %</td>
</tr>
<tr>
<td></td>
<td>10 June</td>
<td>Raised to 6.25 %</td>
</tr>
<tr>
<td></td>
<td>07 July</td>
<td>Maintained at 6.25 %</td>
</tr>
<tr>
<td></td>
<td>04 August</td>
<td>Raised to 6.50 %</td>
</tr>
<tr>
<td></td>
<td>01 September</td>
<td>Raised to 7.00 %</td>
</tr>
<tr>
<td></td>
<td>06 October</td>
<td>Maintained at 7.00 %</td>
</tr>
<tr>
<td></td>
<td>03 November</td>
<td>Maintained at 7.00 %</td>
</tr>
<tr>
<td></td>
<td>01 December</td>
<td>Raised to 8.00 %</td>
</tr>
<tr>
<td>2009</td>
<td>05 January</td>
<td>Maintained at 8.00 %</td>
</tr>
<tr>
<td></td>
<td>02 February</td>
<td>Maintained at 8.00 %</td>
</tr>
<tr>
<td></td>
<td>02 March</td>
<td>Maintained at 8.00 %</td>
</tr>
<tr>
<td></td>
<td>06 April</td>
<td>Maintained at 8.00 %</td>
</tr>
<tr>
<td></td>
<td>04 May</td>
<td>Maintained at 8.00 %</td>
</tr>
<tr>
<td></td>
<td>01 June</td>
<td>Maintained at 8.00 %</td>
</tr>
<tr>
<td></td>
<td>06 July</td>
<td>Maintained at 8.00 %</td>
</tr>
<tr>
<td></td>
<td>03 August</td>
<td>Maintained at 8.00 %</td>
</tr>
<tr>
<td></td>
<td>07 September</td>
<td>Maintained at 8.00 %</td>
</tr>
</tbody>
</table>

For details of the KFR, see Table 6.3 (S34) of the QEB.
KFR announcements prior to January 2007 are reported in various bulletins starting with the March 2001 QEB.
### GLOSSARY OF TERMS AND ACRONYMS

<table>
<thead>
<tr>
<th>Term</th>
<th>Definition</th>
</tr>
</thead>
<tbody>
<tr>
<td>Balance of Payments</td>
<td>A statistical statement that systematically summarizes a country’s economic transactions with the rest of the world, over a specific time period. It comprises the Current and Capital and Financial Accounts.</td>
</tr>
<tr>
<td>Broad Money Supply (M3*)</td>
<td>Total volume of money comprising narrow money (M1*) and quasi money in the economy at a point in time. See ‘narrow’ and ‘quasi’ money.</td>
</tr>
<tr>
<td>Cash Reserve Requirement (CRR)</td>
<td>A requirement imposed on commercial banks to hold cash as a percentage of total deposits and other prescribed liabilities at all times.</td>
</tr>
<tr>
<td>Capital Account</td>
<td>Records all transactions that involves the receipts or transfers of capital and acquisitions/disposal of non-produced, non-financial assets such as purchase of production facilities, i.e. plants and machinery, etc.</td>
</tr>
<tr>
<td>Central Bank Bill (CBB) ¹</td>
<td>A monetary policy instrument of the Bank of PNG used to manage liquidity in the banking system by either injecting or defusing it in order to achieve a desired level of interest rate.</td>
</tr>
<tr>
<td>Current Transfers Account</td>
<td>Records all foreign transactions that are not transfers of capital and cannot be repaid. These includes donations, gifts and grants, superannuation funds and licensing fees.</td>
</tr>
<tr>
<td>Exchange Settlement Account (ESA)</td>
<td>Accounts of the commercial banks with the Bank of PNG for settlement transactions with each other.</td>
</tr>
<tr>
<td>Exclusion-based CPI measure</td>
<td>An underlying inflation measure which involves zero weighting of volatile sub-groups or items such as fruit &amp; vegetables, betelnut and prices that are largely determined by non-market (seasonal) forces, as well as alcoholic drinks, cigarettes &amp; tobacco, etc. See ‘Underlying CPI’.</td>
</tr>
<tr>
<td>Financial Account</td>
<td>Records all transactions associated with changes of ownership of foreign financial assets such as holdings of monetary gold, special drawing rights (SDR), claims on non-residents and foreign liabilities.</td>
</tr>
<tr>
<td>Headline Consumer Price Index (CPI)</td>
<td>A measure of inflation as calculated and published quarterly by the National Statistical Office (NSO), which measures the total price movements in goods and services in the basket.</td>
</tr>
</tbody>
</table>

¹ See ‘For the Record’ on page 34 in the 2004 September QEB.
<table>
<thead>
<tr>
<th><strong>Income Account</strong></th>
<th>Records transactions such as compensation of employees, which cover wages, salaries, and other benefits in cash and kind, dividends and interest earned on investments between PNG and the other countries.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Inscribed Stock (bond)</strong></td>
<td>A Government debt instrument sold to the public for a maturity term of one year or longer for Budget financing.</td>
</tr>
<tr>
<td><strong>Kina Facility Rate (KFR)</strong></td>
<td>Official benchmark rate used by the Bank of PNG to signal its monetary policy stance. The KFR is announced monthly by the Governor and published in the newspapers and on the Bank’s website.</td>
</tr>
<tr>
<td><strong>Liquid Assets</strong></td>
<td>Assets of the commercial banks, which are in near liquid form, comprising cash, ESA balances, CBBs, Treasury bills and Inscribed stocks less than 3 years to maturity.</td>
</tr>
<tr>
<td><strong>Minimum Liquid Asset Ratio (MLAR)</strong></td>
<td>A prudential requirement imposed by the Bank of PNG on commercial banks to hold liquid assets as a percentage of total deposits and other prescribed liabilities at all times.</td>
</tr>
<tr>
<td><strong>Monetary Base (or Reserve Money)</strong></td>
<td>Comprised of currency held by the public and liquid assets of the commercial banks, including deposits held with the Bank of PNG under the Repurchase Agreement Facility (RAF) or Repos.</td>
</tr>
<tr>
<td><strong>Narrow Money</strong></td>
<td>A component of total money supply that is considered liquid or can be converted easily to cash on demand, and comprises of currency in circulation (held outside the banking system) and demand deposits.</td>
</tr>
<tr>
<td><strong>Open Market Operations (OMO)</strong></td>
<td>Operations of liquidity management conducted by the Bank of PNG with commercial banks and other financial intermediaries involving Government securities, CBB, Repos and foreign exchange trading to influence short-term interest rates.</td>
</tr>
<tr>
<td><strong>Over the year CPI</strong></td>
<td>Percentage change in the CPI of a quarter compared to the corresponding quarter of the previous year (Also called ‘annual’ CPI).</td>
</tr>
<tr>
<td><strong>Portfolio Investment</strong></td>
<td>Investments, mainly in equity and debt securities such as bonds and notes, money market debt instruments and financial derivatives, as well as long-term debt, equity and securities.</td>
</tr>
<tr>
<td><strong>Quasi Money</strong></td>
<td>A component of total money supply that is not easily convertible to cash on demand and comprises of savings and term deposits.</td>
</tr>
<tr>
<td>Term</td>
<td>Description</td>
</tr>
<tr>
<td>-------------------------------------------</td>
<td>-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------</td>
</tr>
<tr>
<td>Repurchase Agreement Facility (RAF)</td>
<td>A money market instrument used by Bank of PNG to lend to or borrow from the commercial banks, for liquidity management, and is unwound on maturity. The terms range from overnight to 14 days and can be collateralised, for instance, using Treasury bills.</td>
</tr>
<tr>
<td>Tap Facility</td>
<td>A facility conducted by the Bank of PNG for sale of Treasury bills and Inscribed stocks to the public.</td>
</tr>
<tr>
<td>Temporary Advance Facility</td>
<td>A statutory mechanism stipulated under Section 54 of the Central Banking Act 2000, that provides the National Government with access to short-term financing to meet mismatches in revenue.</td>
</tr>
<tr>
<td>Trade Account</td>
<td>Records all economic transactions associated with merchandise exports and imports of physical goods.</td>
</tr>
<tr>
<td>Trade Weighted Index</td>
<td>The Trade Weighted Index (TWI) measures the value of the kina against a basket of currencies of PNG’s major trading partners.</td>
</tr>
<tr>
<td>Treasury Bill</td>
<td>Government security or debt instrument sold at a discount value, but redeemed at face value on maturity for purposes of Budget financing. In PNG, Treasury bills are issued for 28, 61, 91, 182 and 364 day maturities.</td>
</tr>
<tr>
<td>Trimmed-mean CPI measure</td>
<td>A fixed proportion of prices at each end of the distribution of price changes are zero weighted and the mean of the remaining price changes recomputed. See also ‘Underlying CPI’.</td>
</tr>
<tr>
<td>Underlying CPI (exclusion-based and trimmed-mean CPI measures)</td>
<td>A measure of inflation that excludes short-term volatile movements in prices, such as seasonal factors, Government policy decisions and price controlled items.</td>
</tr>
</tbody>
</table>

\(^2\) See ‘For the Record’ p.24 in the 2005 September QEB.
**REFERENCE “FOR THE RECORD”**

Some issues of the Quarterly Economic Bulletin (QEB) have 'For the Record’ as additional information relating to changes introduced to various statistical tables. The following 'For the Record' have appeared in the QEB since March 2000.

<table>
<thead>
<tr>
<th>Issue</th>
<th>For the Record</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mar 2000</td>
<td>Removal of QEB Table 3.8</td>
</tr>
<tr>
<td>Jun 2000</td>
<td>Inflation - Consumer Price Index (CPI)</td>
</tr>
<tr>
<td></td>
<td>Changes to Table 7.2: Other Domestic Interest Rates</td>
</tr>
<tr>
<td>Mar 2001</td>
<td>Introduction of Monthly Kina Facility Rate</td>
</tr>
<tr>
<td>Jun 2001</td>
<td>Changes to Table 10.2: Prices and Wages</td>
</tr>
<tr>
<td>Dec 2001</td>
<td>Measures of Inflation</td>
</tr>
<tr>
<td></td>
<td>Changes to Table 7.1: Commercial Banks Interest Rates</td>
</tr>
<tr>
<td></td>
<td>Changes to Table 7.2: Other Domestic Interest Rates</td>
</tr>
<tr>
<td></td>
<td>Changes to Table 10.2 Prices and Wages</td>
</tr>
<tr>
<td>Jun 2002</td>
<td>Exclusion of QEB Tables 4.2: Rural Development Bank of PNG and Table 10.1: Indicators of Economic Activity</td>
</tr>
<tr>
<td>Mar 2003</td>
<td>Changes to Balance of Payments Tables</td>
</tr>
<tr>
<td></td>
<td>Bank of PNG Employment Index: Changes to Table 10.4 and Table 10.5</td>
</tr>
<tr>
<td></td>
<td>Regional and Industrial Classifications and Abbreviations</td>
</tr>
<tr>
<td>Jun 2003</td>
<td>Changes to Open Market Operations Instruments</td>
</tr>
<tr>
<td></td>
<td>Directions of Merchandise Trade</td>
</tr>
<tr>
<td>Sep 2003</td>
<td>Changes to the Treasury Bills Auction Allocation Process</td>
</tr>
<tr>
<td>Dec 2003</td>
<td>Further Change to the Treasury Bills Auction Allocation Process</td>
</tr>
<tr>
<td></td>
<td>Bank of PNG Employment Survey</td>
</tr>
<tr>
<td>Sep 2004</td>
<td>Introduction of Central Bank Bill (CBB)</td>
</tr>
<tr>
<td>Mar 2005</td>
<td>Changes to Table 9.5 to include Exports from Napanapa Oil Refinery</td>
</tr>
<tr>
<td></td>
<td>Changes to Tables 1.2 and 1.3 'Other Items (Net)'</td>
</tr>
<tr>
<td>June 2005</td>
<td>Changes to Tables 8.2 and 8.5 'External Public Debt'</td>
</tr>
<tr>
<td>Sep 2005</td>
<td>Trade Weighted Exchange Rate Index</td>
</tr>
<tr>
<td></td>
<td>Employment Index - Changes to Tables 10.4 and 10.5</td>
</tr>
<tr>
<td></td>
<td>Central Bank Bill (CBB) Auction - Changes to Tables 3.8 and 7.2</td>
</tr>
<tr>
<td>Mar 2006</td>
<td>Updated Weights for the Trade Weighted Index (TWI)</td>
</tr>
<tr>
<td>June 2006</td>
<td>Expansion of Monetary and Financial Data Coverage</td>
</tr>
<tr>
<td></td>
<td>Upgrade of PNG's Private Debt and Equity Recording System</td>
</tr>
<tr>
<td>Dec 2006</td>
<td>Changes to Table 8.1 - Capital Transfers</td>
</tr>
<tr>
<td>Jun 2007</td>
<td>Revisions to the March Quarter 2007 and December Quarter 2006 Consumer Price Index</td>
</tr>
<tr>
<td>Jun 2007</td>
<td>Debt Ratios</td>
</tr>
<tr>
<td>Sep 2007</td>
<td>Revisions to the Consumer Price Indices in June Quarter 2007 back to September Quarter 2005.</td>
</tr>
<tr>
<td>Mar 2008</td>
<td>Updated Weights for the Trade Weighted Index (TWI)</td>
</tr>
<tr>
<td>Mar 2009</td>
<td>Changed Monetary Policy Statement release month from January to March</td>
</tr>
<tr>
<td>Mar 2009</td>
<td>Updated Weights for the Trade Weighted Index (TWI)</td>
</tr>
</tbody>
</table>
Each issue of the Quarterly Economic Bulletin contains a review of economic conditions for the past quarter and a comprehensive set of updated statistical tables. Articles of special interest to current economic policy are also prepared by Bank staff for inclusion in the Bulletin. The following articles have appeared in the Quarterly Economic Bulletin since March 1998.

<table>
<thead>
<tr>
<th>Issue</th>
<th>Title</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mar 1998</td>
<td>Papua New Guinea’s Total External Exposure</td>
</tr>
<tr>
<td>Dec 1998</td>
<td>The 1999 National Budget</td>
</tr>
<tr>
<td>Dec 1998</td>
<td>Monetary Policy for 1999</td>
</tr>
<tr>
<td>Mar 1999</td>
<td>Papua New Guinea’s Total External Exposure</td>
</tr>
<tr>
<td>Sep 1999</td>
<td>The 1999 Supplementary Budget</td>
</tr>
<tr>
<td>Dec 1999</td>
<td>The 2000 National Budget</td>
</tr>
<tr>
<td>Dec 2000</td>
<td>The 2001 National Budget</td>
</tr>
<tr>
<td>Dec 2001</td>
<td>The 2002 National Budget</td>
</tr>
<tr>
<td>Jun 2002</td>
<td>Semi-annual Monetary Policy Statement, July 2002</td>
</tr>
<tr>
<td>Sep 2002</td>
<td>The 2002 Supplementary Budget</td>
</tr>
<tr>
<td>Dec 2002</td>
<td>The 2003 National Budget</td>
</tr>
<tr>
<td>Mar 2003</td>
<td>Special article: Export Price Index, Volume Index and Weights Calculations Methodology</td>
</tr>
<tr>
<td>Dec 2003</td>
<td>The 2004 National Budget</td>
</tr>
<tr>
<td>Dec 2003</td>
<td>Semi-annual Monetary Policy Statement, January 2004</td>
</tr>
<tr>
<td>Sep 2004</td>
<td>Semi-annual Monetary Policy Statement, July 2004</td>
</tr>
<tr>
<td>Dec 2004</td>
<td>Semi-annual Monetary Policy Statement, January 2005</td>
</tr>
<tr>
<td>Dec 2004</td>
<td>The 2005 National Budget</td>
</tr>
<tr>
<td>Jun 2005</td>
<td>Papua New Guinea’s Total External Exposure</td>
</tr>
<tr>
<td>Jun 2005</td>
<td>Semi-annual Monetary Policy Statement, July 2005</td>
</tr>
<tr>
<td>Dec 2005</td>
<td>The 2006 National Budget</td>
</tr>
<tr>
<td>Dec 2005</td>
<td>Semi-annual Monetary Policy Statement, January 2006</td>
</tr>
<tr>
<td>Jun 2006</td>
<td>Papua New Guinea’s Total External Exposure</td>
</tr>
<tr>
<td>Dec 2006</td>
<td>The 2007 National Budget</td>
</tr>
<tr>
<td>Jun 2007</td>
<td>Papua New Guinea’s Total External Exposure</td>
</tr>
<tr>
<td>Jun 2007</td>
<td>Supplement to the July 2007 Monetary Policy Statement</td>
</tr>
<tr>
<td>Dec 2007</td>
<td>The 2008 National Budget</td>
</tr>
<tr>
<td>Jun 2008</td>
<td>Papua New Guinea’s Total External Exposure</td>
</tr>
<tr>
<td>Dec 2008</td>
<td>The 2009 National Budget Document</td>
</tr>
<tr>
<td>Dec 2008</td>
<td>Monetary Policy Statement, January 2009 Update</td>
</tr>
<tr>
<td>Mar 2009</td>
<td>Monetary Policy Statement, March 2009</td>
</tr>
<tr>
<td>Jun 2009</td>
<td>Papua New Guinea’s Total External Exposure</td>
</tr>
<tr>
<td>Sep 2009</td>
<td>Monetary Policy Statement, September 2009</td>
</tr>
</tbody>
</table>
STATISTICAL SECTION

Sources

Statistics for the commercial banks have been derived from returns submitted to the Bank. Statistics on Savings and Loan Societies and Papua New Guinea Government securities are derived from sources within the Bank.

Government financial statistics are supplied by the Department of Finance and Treasury.

Information on prices of Papua New Guinea exports are gathered from marketing boards or export producers; world indicator prices are reproduced from the Public Ledger published in London. Tea prices are from the Tea Market Report, London. The general indices of commodity prices are constructed from data published in The Economist, London.

Most other statistics are published initially by the National Statistical Office.

Symbols used

<table>
<thead>
<tr>
<th>Symbol</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>n.a</td>
<td>not available</td>
</tr>
<tr>
<td>..</td>
<td>figure less than half the digit shown</td>
</tr>
<tr>
<td>-</td>
<td>nil</td>
</tr>
<tr>
<td>e</td>
<td>estimate</td>
</tr>
<tr>
<td>f</td>
<td>forecast</td>
</tr>
<tr>
<td>p</td>
<td>provisional</td>
</tr>
<tr>
<td>r</td>
<td>revised</td>
</tr>
<tr>
<td>n.i.e</td>
<td>not included elsewhere</td>
</tr>
</tbody>
</table>
## LIST OF TABLES

1.0 **MONETARY AND CREDIT AGGREGATES**

1.1 Monetary and Credit Aggregates: Movements S3
1.2 Depository Corporations Survey S4
1.3 Volume of Money: Determinants S5
1.4 Volume of Money: Components S6

2.0 **BANK OF PAPUA NEW GUINEA**

2.1 Central Bank Survey S7
2.2 Liabilities S8
2.3 Assets S9

3.0 **OTHER DEPOSITORY CORPORATIONS (ODCs)**

3.1 Other Depository Corporations Survey S10
3.2 Liabilities S11
3.3 Assets S12
3.4 Liquid Asset Holdings S13
3.5 Deposits Classified by Sector S14

**COMMERCIAL BANKS**

3.6 Liabilities S15
3.7 Assets S16
3.8 Deposits Classified by Depositor S17
3.9 Deposits Classified by Industry S18
3.10 Advances Outstanding Classified by Borrower S19
3.11 Selected Deposits and Advances Classified by Interest Rate S20
3.12 Movements in Lending Commitments S21
3.13 Liquid Assets S22

**FINANCE COMPANIES**

3.14 Liabilities S23
3.15 Assets S24

**MERCHANT BANKS**

3.16 Liabilities S25
3.17 Assets S26

**SAVINGS AND LOANS SOCIETIES**

3.18 Liabilities S27
3.19 Assets S28

**MICROFINANCE COMPANIES**

3.20 Liabilities S29
3.21 Assets S29

4.0 **OTHER FINANCIAL CORPORATIONS**

**NATIONAL DEVELOPMENT BANK**

4.1 Liabilities S30
4.2 Assets S30
5.0 COMMODITY INDUSTRY BOARDS AND STABILISATION FUNDS

5.1 Deposits S31
5.2 Investments S31

6.0 INTEREST RATES AND SECURITY YIELDS

6.1 Commercial Bank Interest Rates S32
6.2 ODCs Average Interest Rates (excl. commercial banks) S33
6.3 Other Domestic Interest Rates S34
6.4 Overseas Interest Rates S35

7.0 GOVERNMENT OPERATIONS

7.1 Fiscal Operations of the Government S36
7.2 Mineral Resource Stabilisation Fund: Analysis of Movements S37
7.3 Public Debt Outstanding: Classified by Source S37
7.4 Domestic Debt Outstanding: Classified by Holder S38
7.5 Overseas Public Debt Outstanding: Analysis of Movements S38

8.0 BALANCE OF PAYMENTS AND INTERNATIONAL RESERVES

8.1 Balance of Payments S39
8.2 Net Foreign Assets of Depository Corporations S40
8.3 Exchange Rate S41
8.4 Exports: Classified by Commodity Group S42
8.5 Agricultural Exports: Classified by Commodity S42
8.6 Agricultural Exports: Quantities Exported of Commodities S43
8.7 Non-agricultural Exports: Quantities Exported of Major Commodities S43
8.8 Export Prices: Non-mineral Commodities S44
8.9 International Commodity Prices: Major Exports S45
8.10 International Commodity Prices: Economists Price Indices S46
8.11 Export Price Indices S47
8.12 Export Volume Indices S48
8.13 Direction of Trade: Origins of Imports S49
8.14 Direction of Trade: Destinations of Exports S49

9.0 ECONOMIC ACTIVITY AND PRICES

9.1 Prices and Wages S50
9.2 Consumer Price Index: Classified by Expenditure S51
9.3 Consumer Price Index: Classified by Urban Area S51
9.4 Employment: Classified by Region S52
9.5 Employment: Classified by Industry S53
9.6 Expenditure on Gross Domestic Product: Current Prices S54
9.7 Expenditure on Gross Domestic Product: Constant Prices S54
9.8 Income Components of Gross Domestic Product: Current Prices S54