



# BANK OF PAPUA NEW GUINEA

## MONTHLY ECONOMIC REVIEW

Vol. 2

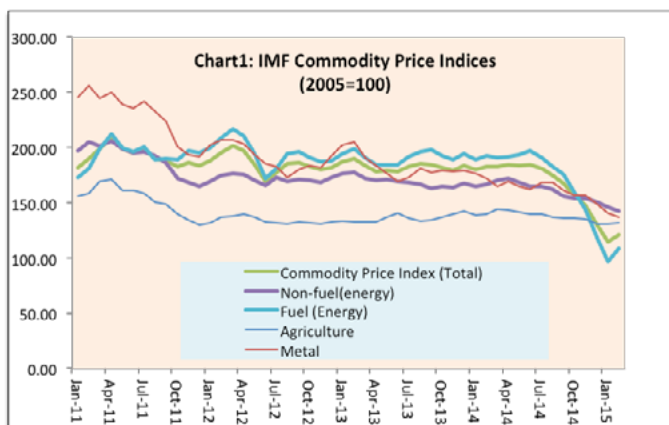
No. 2

Month Ended  
February 2015

### Economic Activity

Global economy continued to grow at a slow pace, reflecting low pace of economic activity in advanced economies, especially in Japan and the advanced economies in the Euro area. Activity in the emerging market economies also slowed down, mainly driven by Russia and China, which experienced persistent weaknesses. The growth in the US and UK combined with lower international oil prices and, the past and current monetary easing and fiscal adjustments assisted to maintain the global growth. International Monetary Fund's (IMF) World Economic Outlook (WEO) for January 2015 projected the annual growth of 3.5 percent in 2015 to be generated mainly by expected growth in the US.

The IMF's Commodity Market Monthly for March 2015, indicated a 5.5 percent rebound in commodity prices in February, the first increase in eight months, attributed to a notable improvement in international crude oil prices. Crude oil prices surged by 15.8 percent to an average of \$54.9/bbl due to a combination of factors, including an improvement in the demand for refined products and several impediments to crude supply. Non-energy prices dropped by 2.2 percent, partly due to the appreciation of the US dollar, with both agriculture and metal recording declines of 2.2 percent.



On the domestic front, the Bank of Papua New

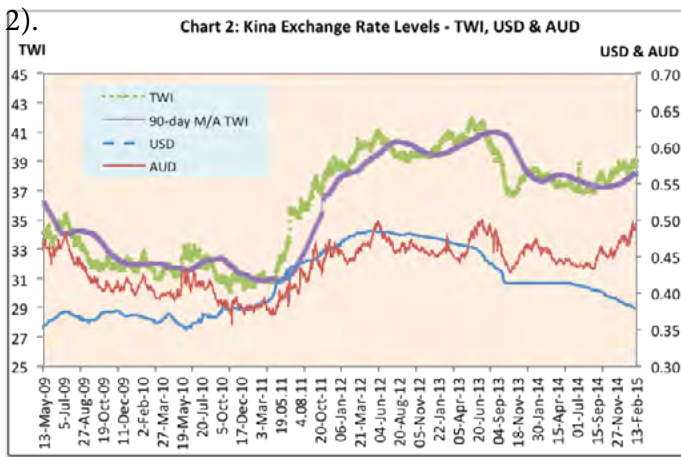
Guinea's (BPNG) estimated economic growth in 2014 to be higher than the 8.4 percent contained in the 2015 National Budget document. This is attributed to the earlier than expected commencement of production and export of LNG, and increased Government spending on priority areas; including education, health, agriculture, district and local level Governments, and major infrastructure projects including the sporting facilities for the 2015 Pacific Games. For 2015, economic growth will reflect a full year of LNG production and export. However, lower net inflows than earlier envisaged are now expected from LNG revenue, due to the lower international oil prices and its link to LNG price.

### International Reserves

As of 27<sup>th</sup> February 2015, the level of gross foreign exchange reserves decline by US\$164.6 million to US\$2,070.2 (K 5,398.1) million, from end of January, reflecting the Central Bank's intervention to supply foreign currency to the market. This level of reserve is sufficient for around 7.0 months of total import cover and 10.5 months of non-mineral import cover.

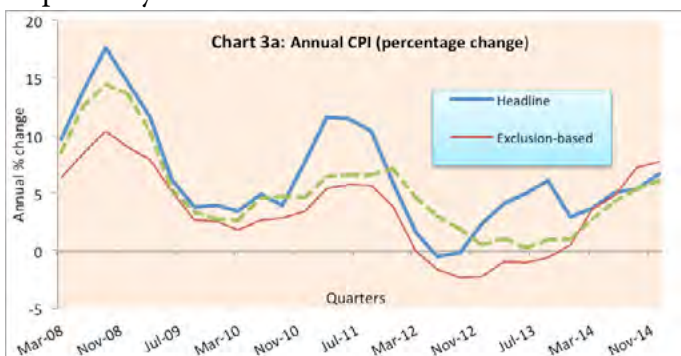
### Exchange Rate

The average kina exchange rate depreciated against the US dollar by 112 basis points to US\$0.3797 over the month to 27<sup>th</sup> February 2015, mainly reflecting high demand for foreign currency. Over the same period, the average kina exchange rate appreciated against the Australian dollar by 251 basis points to AU\$0.4870, due to cross-currency movements as the Australian dollar weakened against the US dollar. This follows the 25 basis points cut in the cash rate by the Reserve Bank of Australia on the 4<sup>th</sup> of February 2015 and the continued recovery in the US economy. The average Trade Weighted Index (TWI)<sup>1</sup> increased by 0.41 percent to 38.80 over the month to 27<sup>th</sup> February 2015, reflecting the appreciation of the kina against the Australian dollar and other major currencies outweighing the depreciation against the US\$ (Chart



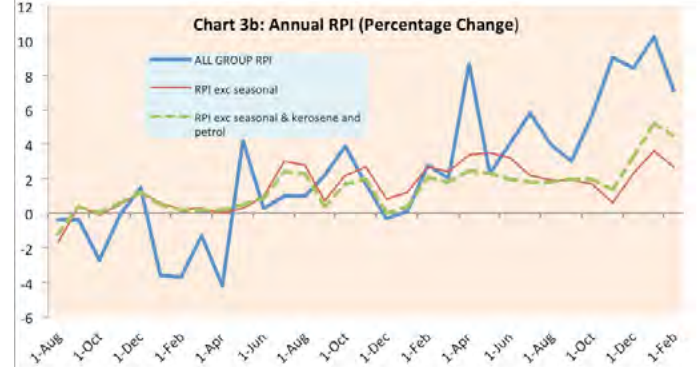
## Inflation

Annual headline Consumer Price Index (CPI) for the December quarter of 2014 was 6.6 percent, compared to an increase of 2.9 percent in the corresponding period of 2013 (Chart 3a). This increase was mainly influenced by increases in the following expenditure groups, with 24.1 percent in the 'Health', 14.9 percent in the 'Housing', 9.2 percent in the 'Household equipment', 9.0 percent in the 'Clothing and Footwear', 7.4 percent in the 'Transport', 7.2 percent in the 'Miscellaneous', 6.5 percent in the 'Recreation' and 6.2 percent in the 'Food and non-alcoholic beverages' expenditure groups. The only decline in prices was recorded in the 'Communications' expenditure group by 5.5 percent. In 2014, annual headline CPI recorded progressive increases of 3.7 percent, 5.1 percent and 5.3 percent for March, June and September quarters, respectively. Underlying measures also increased with the annual trimmed-mean and exclusion-based measures recording 4.3 percent and 5.2 percent, respectively.



The annual headline Retail Price Index (RPI)<sup>2</sup> for Port Moresby increased by 7.1 percent over the twelve months to February 2015, 3.1 percent lower than the January RPI. Annual RPI ex-seasonal and Annual RPI ex-seasonal and fuel recorded an increase of 3.2 percent and 5.5 percent, respectively reflecting increases

in the 'Drinks, Tobacco & Betelnut' by 13.4 percent and 'Food' expenditure groups by 8.8 percent (Chart 3b). These, more than offset the declines in the 'Rents, council charges fuel/power' expenditure group and 'Motor vehicle operation (petrol only)' subgroups



## Fiscal Operations

Preliminary estimates of the fiscal operations of the National Government over the twelve months to December 2014 show an overall deficit of K2,815.2 million, compared to a deficit of K2,672.4 million in the corresponding period of 2013. This represents 7.1 percent of nominal GDP, reflecting higher expenditure. The budget deficit and net external repayment of K200.2 million was financed from domestic sources totalling K3,015.5 million. Priority spending out of the 2014 Supplementary Budget has contributed to the increase in expenditure in 2014.

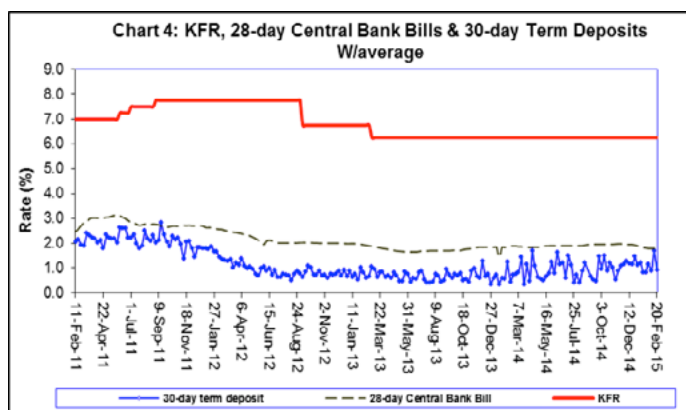
Total revenue, including foreign grants, was K10,379.2 million in 2014, 5.6 percent higher than receipts collected in the corresponding period of 2013. This represents 82.1 percent of the revised budgeted revenue for 2014. The increase in revenue is primarily due to higher non-tax receipts and foreign grants. Total expenditure in 2014 was K13,194.4 million, 5.5 percent higher than in the corresponding period of 2013 and represents 87.5 percent of the revised budget appropriation for 2014. This outcome represents higher recurrent and development expenditures.

## Domestic Interest Rates & Monetary Aggregates

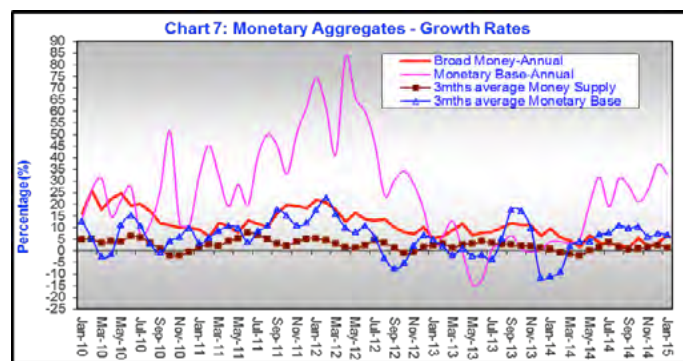
Over the month to 27<sup>th</sup> February 2015, the 28-day Central Bank Bill (CBB) rate declined marginally from 1.79 to 1.78 per cent whilst the 63 and 91 day rates remained unchanged at 2.70 and 2.84 per cent, respectively. At the Treasury bill auction, the 182-day rate was unchanged at 4.63 percent, while the 364-day rate decreased to 7.37 percent from 7.38 percent. Over the same period, the weighted average interest

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

rates on wholesale deposits above K500,000 were mixed. The 30 and 180-day rates fell to 0.92 percent and 1.44 percent from 1.16 percent and 2.45 percent respectively, while the rate for 90-day term increased to 1.68 percent from 1.63 percent. The 60-day rate remained unchanged at 1.25 percent. The KFR was maintained at 6.25 percent in February 2015, with the trading margins for the Repos remaining at 100 basis points from the KFR (Chart 4). The Cash Reserve Requirement (CRR) was kept at 10.0 percent. The Central Bank continued to use the weekly Open Market Operations (OMO) to manage liquidity during the month. The Government's issuance of new Treasury bills and Inscribed stock supported the Bank's effort in diffusing excess liquidity in the banking system.



other resident sectors increased by K41.5 million to K10,864.5 million between December 2014 and weekending 20<sup>th</sup> February 2015. This mainly reflected net advances (mainly overdrafts) to the construction, retail, petroleum, wholesale, manufacturing, and other business sectors. Over the year to 20<sup>th</sup> February 2015, average lending by commercial banks increased by 15.4 percent to K10,029.3 million. The commercial bank deposits declined by K30.0 million to K19,270.4 million between December 2014 and week-ending 20<sup>th</sup> February 2015, reflecting net withdrawals by the Government, wholesale, manufacturing, finance, mining, and other business sectors. Over the year to 20<sup>th</sup> February 2015, average deposits increased by 3.6 percent to K18,870.8 million.



Broad money supply increased by 6.5 percent in January 2015, compared to an increase of 9.7 percent in the corresponding period of 2014 (Chart 5). This was driven by increases in private sector credit and net claims on the Government, which outweighed the decline in net foreign assets. Monetary base grew significantly by 32.8 percent in January 2015, compared to an increase of 4.0 percent recorded in the corresponding period of 2014. This was due to increases in deposits of commercial banks at the Central Bank and currency in circulation. Commercial bank lending extended to public non-financial corporations, other financial corporations and

## Monetary Policy

Annual headline Inflation increased progressively each quarter in 2014, ending the year at 6.6 percent in the December quarter. This outcome is still within the Bank's projection for 2014, and is considered manageable in light of the economic growth. RPI for February 2015 recorded a lower increase, compared to the previous month. The Bank also considered the developments in exchange rates and international commodity market. It cautiously maintained the policy signalling rate, the Kina Facility Rate at 6.25 percent for the month of February 2015.

<sup>1</sup>The RPI only covers Port Moresby and so it may not be comparable to the overall CPI movements.

Papua New Guinea Key Economic Indicators							
		Sep-14	Oct-14	Nov-14	Dec-14	Jan-15	Feb-15
<b>1. Consumer Price Index (CPI)</b>	Headline	5.3	-	-	6.6	-	-
	Food	5.1	-	-	6.1	-	-
<b>2. Retail Price Index (RPI) (YOY % Change)(a)</b>	Headline	3.00	5.7	9.0	8.4	10.2	7.1
	Ex-seasonal	2.10	1.9	0.7	2.6	4.2	3.2
<b>3. Exchange Rates</b> (mid-rate, eop)	USD	0.4030	0.3965	0.3910	0.3855	0.3815	0.3785
	AUD	0.4605	0.4511	0.4600	0.4708	0.4898	0.4849
	GBP	0.2479	0.2483	0.2489	0.2477	0.2529	0.2451
	JPY	44.06	43.99	46.23	46.17	44.96	45.11
	NZD	0.5164	0.5066	0.4988	0.4921	0.5234	0.5013
<b>4. Balance of Payments</b>	Current Account						
	Capital & Financial Account						
	Overall Balance						
	Foreign Exchange Reserve (eop, US\$ mill)	2,489.3	2,577.8	2,422.6	2,347.3	2,234.8	2,070.2
<b>5. Liquidity (eop)</b>	Liquid Assets Margin to Deposit Ratio (%)	45.5	44.0	46.3	46.1	45.8	46.3
	Banks' Demand Deposits (K'bn)	14.2	14.7	14.4	15.1	14.95	14.82
<b>6. Money and Credit (YOY %)</b>	Broad Money	2.8	5.5	1.7	3.1	6.5	-
	Monetary Base	27.9	21.1	26.3	37.1	32.8	-
	Private Sector Credit	3.2	4.3	4.4	3.5	8.9	-
<b>7. Interest Rates (% pa) (monthly)</b>	Kina Facility Rate	6.25	6.25	6.25	6.25	6.25	6.25
	Central Bank Bill (28 day)	1.95	1.95	1.96	1.92	1.79	1.78
	Commercial bank Term Deposit (30 day)	1.46	1.01	1.16	1.46	1.16	0.97
	Government Treasury Bill (364 day)	7.30	7.36	7.42	7.42	7.38	7.35
	3-year Inscribed stock Rate	8.03	8.06	8.01	7.95	-	9.78
	16-year Inscribed stock Rate (> 10 years)	15.40	15.3	14.49	13.74	-	-
<b>8. Commodity Prices</b> (monthly average)	Oil (\$/bbl)	95.9	86.1	77.0	60.7	47.1	54.8
	Gold (\$/troy oz)	1240.9	1221.3	1176.3	1200.4	1255.8	1227.2
	Copper (\$/mt)	6885.5	6735.9	6700.7	6430.8	5790.5	5701.5
	Coffee (cents/kg)	215.3	226.5	213.9	202.4	190.6	180.7
	Cocoa (cents/kg)	195.7	195.0	184.6	188.6	193.5	292.1

Authorised for release by Mr Loi M. Bakani, Governor