



BANK OF PAPUA NEW GUINEA

MEDIA RELEASE

10th August, 2021

Quarterly Economic Bulletin December Quarter 2020

Mr. Loi M. Bakani CMG, Governor of the Bank of Papua New Guinea (Bank of PNG), today released the December 2020 Quarterly Economic Bulletin (QEB). This statement provides an overview of the economic and financial developments during the December quarter of 2020.

1. OVERVIEW OF THE DEVELOPMENTS IN THE DECEMBER QUARTER OF 2020

Economic indicators available to the Bank of Papua New Guinea (the Bank) show that domestic economic activity contracted in 2020, despite a recovery in the December quarter. The decline was due to the COVID-19 pandemic that adversely impacted the global economy, the subsequent containment measures of the State of Emergency (SOE) imposed by the Papua New Guinea (PNG) Government, and the shutdown of the Porgera Mine. The lower production and export of most mineral commodities and some non-mineral commodities as well as declines in sales by the formal private sector contributed to the contraction. In 2020, the kina depreciated against all major currencies which resulted in a decline in the Trade Weighted Index (TWI). An increase in employment indicated a recovery as containment measures were eased in the second half of 2020. With the impact of the pandemic, headline inflation remained

elevated. To support economic activity and the recovery, the Central Bank eased its monetary policy stance, reducing the Kina Facility Rate (KFR) from 5.00 percent to 3.00 percent in March 2020 where it was maintained for the remainder of the year.

Data from the Bank's Business Liaison Survey (BLS) show that the total nominal value of sales in the formal private sector increased by 8.4 percent in the December quarter of 2020, compared to an increase of 3.3 percent in the September quarter. Excluding the mineral sector, sales increased by 8.7 percent in the December quarter, compared to an increase of 11.2 percent in the previous quarter. By sector, sales increased in all sectors, except the agriculture/forestry/fishing sector, which declined. By region, sales increased in all regions, except in the Islands region which declined. In 2020, total sales declined by 19.0 percent, compared to a decline of 3.0 percent in 2019. Excluding the mineral sector, sales declined by 8.8 percent, the same as in 2019. The decline was mainly attributed to the adverse impact of the COVID-19 containment measures, which resulted in businesses significantly scaling down operations.

The Bank's Employment Index shows that the level of employment in the formal private sector increased by 1.7 percent in the December quarter of 2020, compared to a decline of 5.0 percent in the September quarter of 2020. Excluding the mineral sector, the level of employment increased by 2.0 percent. By sector, the level of employment increased in the construction, transportation, manufacturing, agriculture/forestry/fishing and retail sectors. It declined in the wholesale, financial/business and other services and mineral sectors. By region, the level of employment increased in all the regions except the Islands region. Over the year to the December quarter of 2020, the total level of employment fell by 3.3 percent, compared to a decline of 1.4 percent in 2019. Excluding the mineral sector, the level of employment increased by 1.0 percent in 2020, following a decline of 1.9 percent in 2019.

Quarterly headline inflation, as measured by the Consumer Price Index (CPI), increased by 0.9 percent in the December quarter of 2020, compared to a decline of 0.6 percent in the September quarter of 2020. There were increases in all the expenditure groups except the 'Education' group. By urban centre, prices increased in all the surveyed centres. Annual headline inflation was 5.1 percent in the December

quarter of 2020, compared to an increase of 4.9 percent in the September quarter of 2020.

In 2020, the United States (US) dollar appreciated against all major currencies. The US dollar appreciated against the pound sterling and the Australian dollar by 2.2 percent each, the euro by 2.0 percent and the Japanese yen by 1.6 percent.

In 2020, the average daily kina exchange rate depreciated against the pound sterling by 2.8 percent to £0.2163, the Australian dollar by 2.8 percent to A\$0.3910, the euro by 2.6 percent to €0.2395, the yen by 2.3 percent to ¥31.2046 and the US dollar by 0.7 percent to US\$0.2855. These currency movements resulted in the depreciation of the TWI by 3.4 percent to 27.38 in 2020.

The weighted average kina price of PNG's export commodities, excluding Liquefied Natural Gas (LNG), increased by 7.4 percent in 2020, compared to an increase of 1.2 percent in 2019. There was an increase of 6.7 percent in the weighted average price of mineral exports, reflecting higher kina prices for gold and copper. For agricultural, logs and marine product exports, the weighted average kina price increased by 9.9 percent due to higher prices for cocoa, coffee, tea, copra, copra oil, palm oil and marine products. Excluding log exports, the weighted average kina price of agricultural and marine product exports increased by 14.2 percent in 2020, compared to an increase of 1.0 percent in 2019. The higher kina export price reflected an increase in international prices for all of PNG's non-mineral export commodities, except rubber and logs.

The balance of payments recorded a surplus of K2,103.3 million in 2020, compared to a surplus of K423.3 million in 2019. A surplus in the current account more than offset a deficit in the capital and financial account.

The current account recorded a surplus of K18,176.2 million in 2020, compared to a surplus of K18,522.2 million in 2019. This was due to a trade account surplus and net transfer receipts.

The deficit in the capital and financial accounts reflected net outflows due to the build-up in offshore foreign currency accounts of mineral companies including the LNG companies. Net Government and private sector loan repayments also contributed to the outflow.

The level of gross foreign exchange reserves at the end of December 2020, was K9,437.9 (US\$2,709.4) million, equivalent to 9.0 months of total and 15.3 months of non-mineral import covers.

The Central Bank maintained an accommodative monetary policy stance during the December quarter of 2020, with the KFR unchanged at 3.00 percent. This was aimed at supporting economic recovery and business activity impacted by the COVID-19 pandemic. The Repurchase Agreement (Repo) Facility dealing margins remained at 100 basis points on both sides of the KFR.

The Bank utilised its Open Market Operation (OMO) instruments in the conduct of monetary policy to manage liquidity. Liquidity in the banking system continued to remain high, despite some diffusion. There was a net issuance of K55.8 million in Central Bank Bills (CBBs) and a net issuance of K221.1 million in Treasury bills, which more than offset a net retirement of K82.5 million in Treasury bonds. The Central Bank's intervention in the foreign exchange market also assisted in diffusing some of the kina liquidity during the quarter. The Cash Reserve Requirement (CRR) for the commercial banks remained at 7.00 percent during the quarter.

The average level of broad money supply (M3*) increased by 0.5 percent in the December quarter of 2020, compared to an increase of 2.5 percent in the September quarter of 2020. This was due to an increase in the average net foreign assets (NFA) of the banking system. Average net domestic claims outstanding, excluding net claims on the Central Government, increased by 0.1 percent in the December quarter of 2020, following a decline of 0.1 percent in the September quarter of 2020. This reflected an increase in average net claims on the other financial corporations (OFCs), which more than offset a decline in public non-financial corporations.

The average level of monetary base (reserve money) increased by 1.8 percent in the December quarter of 2020, compared to an increase of 1.9 percent in the previous quarter. This was attributed to an increase in the average level of currency in circulation.

The NFA of the Financial Corporations (FCs), comprising deposit corporations (DCs) and OFCs, increased by 26.8 percent to K10,981.5 million in the December quarter of 2020, compared to a decline of 7.3 percent in the previous quarter. This reflected increases in NFA of the Central Bank, Other Depository Corporations (ODCs) and OFCs. The increase in NFA of the Central Bank was mainly due to inflows from external loans and grants, including from the Asian Development Bank (ADB) and Export Finance Australia. The increase in NFAs of the ODCs and OFCs was due to higher holdings of foreign assets and inflows from investments abroad, respectively.

Net claims on the Central Government by FCs declined by 6.3 percent to K14,392.7 million in the December quarter of 2020, compared to an increase of 12.8 percent in the previous quarter, reflecting increased deposits at the commercial banks by the Government for payments to service providers (mainly for outstanding arrears) and for the District and Provincial Support Improvement Programs.

In the December quarter of 2020, total domestic credit extended by the FCs to the private sector, public non-financial corporations and 'Provincial and Local Level Governments' declined by 1.2 percent to K17,899.8 million, compared to an increase of 0.3 percent in the previous quarter. This reflected a decline of K262.7 million in credit to the private sector, which more than offset an increase of K45.8 million in claims by public non-financial corporations. The decline in credit to the private sector mainly reflected repayments by the mining and quarrying, wholesale, petroleum, finance, forestry, fisheries and other business sectors. The increases in the public non-financial corporations reflected advances to the state-owned enterprises.

The fiscal operations of the National Government for 2020 showed a deficit of K7,304.4 million, compared to a deficit of K4,172.0 million in the corresponding period of 2019. This represents 8.9 percent of nominal GDP. The significantly higher deficit reflected lower revenue receipts and higher expenditure.

Total revenue and grants in 2020 was K12,093.3 million, 11.6 percent lower than in 2019 and represents 106.5 percent of the Supplementary Budget amount. In comparison to 2019, both tax and non-tax revenues as well as grants decreased.

Total expenditure for 2020 was K19,397.7 million, 8.7 percent higher than in 2019 and represents 107.8 percent of the revised Budget.

As a result of these developments in revenue and expenditure, the budget deficit of K7,304.4 million was financed from both domestic and external sources totalling K3,685.0 million and K3,619.4 million, respectively.

Total public (Government) debt outstanding at the end of December quarter of 2020 was K40,168.1 million, K2,738.4 million higher than in the September quarter, reflecting a net borrowing during the quarter. This is made up of the final tranche of the Asian Development Bank (ADB) Budget Support Loan of USD150.0 million (K526.3 million); ADB State Owned Enterprises (SOE) Reform program loan of USD100.0 million (K350.9 million); COVID-19 Pandemic Response Program loan of USD250.0 million (K877.2 million); support loan from the Australian Government of USD100 million (K350.9 million) and the balance of K633.12 million from concessional sources for capital investment projects. The total Government debt stock is 49.2 percent of GDP which is within the limits imposed by the Fiscal Responsibility Act 2006 (amended 2020) of 60 percent.

Total Government deposits at depository corporations increased by K1,058.3 million to K5,025.5 million at the end of December 2020, compared to the end of September. The increase reflected the fiscal stimulus measures introduced to revive the economy, combined with increased advances from the Central Bank to the Government under the temporary advance facility following the amendment to the Central Banking Act, 2000 in October 2020 which raised the limit from K300 million to K1.5 billion.