



Bank of Papua New Guinea

Speech by

Mr. David Toua, Chairman, Bank of PNG Board

at the

Launch of the Credit Guarantee Corporation

Tuesday 29th March 2022, APEC Haus

Acknowledgements:

- Hon. James Marape, Primes Minister,
- Interim Board Members of CGC
- Board Members and Management of the Bank of PNG,
- SME Accelerator Program Manager, Mr. Dominic Sikakau
- Representatives from Development Partners,
- Representatives from Financial Institutions,
- Invited Guests
- Ladies and Gentlemen

1.0 Introduction

Good morning. It gives me a sense of pleasure to say that, today's launching of this Credit Guarantee Corporation (CGC) is an historic and defining moment in the short history of our nation's development in light of the governments development objectives to create wealth and employment under the Vision 2050 and other medium to long term development and strategic plans. The launching of the Credit Guarantee Corporation is similar to sowing a seed of development that if successful will result in incubation of a solid foundation for micro-small and medium enterprises (MSMEs) growth in Papua New Guinea, in accessing financial institutions for loans to expand

businesses. In the absence of such an institution (CGC), MSMEs would be denied access to financial institutions' for loans to expand its capital base due to reasons such as lack of collateral, poor credit history, and unregistered mortgage which is typical features of an MSME in the country.

2.0 Genesis of Credit Guarantee Schemes

Governments all over the world have recognised a fundamental failure is allocative efficiency in resource allocation by depository corporations, in their distinguished role of financial intermediation. Financial intermediation is the process where depository corporations, such as commercial banks, mobilise surplus savings of households and lend them to businesses who need it to expand businesses and create employment. This allocative inefficiency of the financial intermediation process of the depository corporations, alone, have led to lower opportunities for employment and has become a bottleneck in development aspirations of many governments, and has become a major channel that promote financial exclusion, thereby giving rise to an ever-increasing unbanked population. This is the reason why many countries such as the G20 nations have strongly supported the renewed call for financial inclusion programs to address higher poverty levels of people at the bottom of the pyramid.

Credit guarantee schemes are now common and are established by governments to mitigate third party credit risk on financial institutions to encourage lending to private sector, especially the MSMEs, which are limited in accessing funds to expand their businesses. Studies have shown that, MSMEs lack of accessibility to bank credit is attributed to:

- unstructured nature of business due to lack of capital, capacity and financial education,
- Improper corporate structures due to their lack of knowledge of proper enterprise structures for risk mitigation and controls,
- inadequate collaterals acceptable to the banks due to lower liquidity, surplus savings and lack of deep asset base,
- low productivity due to low literacy levels, and
- poor market accessibility due to their remote locations.

For these attributes, governments have focused on capacity building, development of proper structures, improve financial education and develop supply chain modules to address issues relating to market accessibility.

3.0 MSME Landscape in Papua New Guinea

MSME's natural incubation, growth and survival is extremely challenging in PNG, given the rugged geographical terrains, tropical jungles and sparsely distributed isolated island communities that are characterised by poor physical infrastructure, such as roads, bridges, electricity, water supply, health service and financial services. The MSMEs ability to thrive in this type of environment is not only daunting but disheartening given 80-90 percent of the work force is financially illiterate and their knowledge of accessing finance is limited. The urban focused minimum wages make unit cost of overheads unsustainable for MSMEs making the industry's viability doubtful.

Compounding the challenges for MSME sector, the Covid 19 pandemic has significantly devastated the struggling industry. In a study conducted by the Bank, with a grant from the Alliance for Financial Inclusion (AFI) in 2020 on the impact of Covid 19 on the MSME sector, revealed that a significant proportion of the industry was devastated following mandatory shut down periods and with scaling down of operations. This led to significant decline in production for the sector and led to further deterioration in incomes and increase in poverty levels of those at the bottom of the pyramid.

4.0 Role of the Central Bank

The Central Bank's mandate consistent with the Central Banking Act is to develop financial policies that will bring about stability in the prices of general goods and services, a predictable interest rate structure, and a stable exchange rate that adjusts to the swings in commodity price cycles that restores its natural equilibrium.

During the Covid pandemic, the Central Bank reacted by easing monetary policy to ensure commercial banks and second tier financial institutions, had the liquidity

necessary to fund transactions demand for money and for business that might need additional capital to sustain their business. These measures included reduction of the Kina Facility Rate, the cash reserve requirement and opening the discount window for second tier financial institutions for liquidity requirements. The other supporting policy measures included the commercial banks deferred principal and interest payments on loans for three months and the members of superannuation funds who were unemployed for three months could drawdown some of their member contributions.

Since 2013, the Central Bank, in association with the financial institutions and our development partners, have undertaken massive financial inclusion drives in the country. We hope to continue that trend with access to finance for our MSMEs.

5.0 Conclusion

In conclusion, the establishment of the CGC is necessary to correct inefficiencies evident in resource allocation in the financial intermediary process of the financial institutions. In this regard, the establishment of the Credit Guarantee Corporation (CGC) brings renewed hope into the MSME sector that has been struggling from the combined lack of basic infrastructure and skill sets that are necessary elements for their growth. With the CGC establishment, it will definitely create a new path to help the government achieve its employment creation and growth objectives while improving financial inclusion that can become an effective channel for efficiency in the financial intermediary and monetary transmission mechanism.

With that, thank you and God Bless Papua New Guinea.