



BANK OF PAPUA NEW GUINEA

MEDIA RELEASE

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Quarterly Economic Bulletin June Quarter 2022

Ms Elizabeth Genia, Acting Governor of the Bank of Papua New Guinea (Bank of PNG or the Bank), today released the June 2022 Quarterly Economic Bulletin (QEB). This statement provides an overview of the economic and financial developments during the June quarter of 2022 and some key developments since then.

1. UPDATE ON DEVELOPMENTS SINCE JUNE 2022

Global economic activity slowed down in the third quarter of 2022, reflecting tightening of policy rates by major central banks to fight inflation, accompanied by scaling back of fiscal support in major economies, including the United States (US), United Kingdom (UK) and the euro area. Growth was also lower in emerging economies driven by the slowdown in Russia and China reflecting the war and, higher COVID-19 infection rates and lock downs respectively.

In the US, real GDP declined reflecting a fall in disposable income and slowdown in activity due to monetary policy tightening by the Federal Reserve Bank to curb high inflation. The latest IMF forecast is for real GDP to grow by 1.6 percent in 2022. In the euro area, real GDP declined in the September quarter of 2022 reflecting weak growth across the economies in Europe, due to tightening of financial conditions as the

European Central Bank ended its asset purchase program and increased its policy rate by 50 basis points in June and 75 basis points in September 2022. The latest IMF forecast is for real GDP to grow by 3.1 percent in 2022. In Japan, real GDP growth has been stable, supported by higher private sector spending. Consumer prices increased, mainly due to higher prices for food and fuel. The Bank of Japan maintained its easing stance to support growth. The latest IMF forecast is for real GDP to grow by 1.7 percent in 2022. Among the emerging market economies, growth slowed down mainly reflecting the impact of Covid-19 restrictions and a sharp slowdown in the property market in China. In its October 2022 World Economic Outlook (WEO) Update, the IMF projected the world economic growth to slow down from 6.0 percent to 3.2 percent in 2022.

According to the latest international commodity price data published by the World Bank in January 2023, prices for both energy and non-energy commodities declined, while prices of precious metals increased. Energy prices declined by 17.2 percent, with the largest declines coming from Dubai Crude Oil price, followed by Brent Crude Oil and West Texas Crude Oil. Consequently, natural gas prices fell with the largest decline coming from the Europe and US natural Gas prices. Non-energy prices declined due to the slowdown in growth. For non-mineral products, prices declined for palm oil, coffee Arabica, tea and logs, while the price of coffee increased. Prices of precious metals increased by 1.7 percent, driven by gold and silver prices. As a result, prices of some of PNG's major export commodities increased, with domestic producers and exporters benefiting from higher export revenue.

Global inflation continued to increase in the third quarter of 2022 amidst interest rate increases by central banks. Higher energy and food prices and a recovery in demand saw prices continued to increase. Core inflation especially in advanced economies have increased reflecting the pass through of energy prices, supply chain cost pressures and tight labour markets. In 2022, the IMF revised up its inflation projections to be around 8.8 percent for global inflation, 7.2 percent for advanced economies and 9.9 percent for emerging and developing economies. The high inflation prompted central banks around the world to raise their official interest rates and remove fiscal and monetary stimulus. The Bank of PNG has followed suit by tightening its monetary policy to fight inflation. Acting Governor Genia noted the Government's relief

assistance packages including the temporary tax relief (GST and excise duty) on fuel products for 2022, raising the income tax threshold to K22, 000 as well as providing additional tuition fee subsidy program through its 2023 National Budget. This is expected to provide some price relief for Papua New Guineans. The Acting Governor warned that if high inflation persists, it would have severe consequences on the lower income groups and the rural population.

The annual headline inflation increased by 6.3 percent in the September quarter of 2022, compared to an increase of 5.5 percent in the previous quarter. All expenditure groups recorded increases except the 'Education', 'Clothing and Footwear' and 'Restaurants and Hotels' expenditure groups, which declined. The largest increase was in the 'Alcoholic Beverages, Tobacco and Betelnut' expenditure group with 14.0 percent, followed by 'Household Equipment' with 11.4 percent, 'Transport' with 11.3 percent, 'Food and Non-Alcoholic Beverages' with 8.0 percent, 'Health' with 5.5 percent, 'Housing' with 3.3 percent, 'Communication' with 3.0 percent, 'Recreation' with 2.9 percent and 'Miscellaneous' with 1.9 percent. These more than offset the declines in the 'Education', 'Clothing and footwear' and 'Restaurants and Hotels' expenditure groups with 13.0 percent, 1.6 percent and 1.4 percent, respectively.

The average daily kina exchange rate depreciated against almost all major currencies, except the euro. Over the year to 4th January 2023, the kina depreciated against the Australian dollar by 2.0 percent to A\$0.4176, Japanese yen by 1.3 percent to ¥37.1400 and the British pound sterling by 0.3 percent to £0.2369, while it appreciated against the euro by 0.5 percent to €0.2687. Against the US dollar (USD), the kina remained stable at US\$ 0.2840. The currency movements resulted in a decrease in the Trade Weighted Index (TWI) by 1.1 percent to 29.60 over the period. The depreciation of kina against the major currencies reflected cross-currency movements due to strengthening of the currencies against the US dollar attributed to the tightening of monetary policy stance by major central banks to ease domestic inflationary pressures.

Acting Governor Genia stated that the level of gross foreign exchange reserves as at end of June 2022 was K10,563.3 (US\$3,052.8) million, sufficient for 9.2 months of total and 16.3 months of non-mineral import cover. As of 30th December 2022, the

gross foreign exchange reserves increased to K14,298.2 (US\$4,132.2), due to inflows of foreign loans for budget support, and high mineral and petroleum taxes, mainly reflecting LNG tax revenues.

2. OVERVIEW OF THE DEVELOPMENTS IN THE JUNE QUARTER OF 2022

Economic indicators available to the Bank of Papua New Guinea point to a continued recovery in the June quarter of 2022, especially in the non-mineral sector. The increase in non-mineral employment by 3.2 percent and private sector sales by 10.8 percent in the June quarter of 2022 are indicative of the recovery. The increase in international commodity prices and production in some of the export commodities also supported the activity and resulted in a surplus in the balance of payments. While the increase in prices was mainly attributed to the Russia-Ukraine war, the consequences of war however, continued to weigh on domestic activity as crude oil and food prices remain elevated. Whilst Papua New Guinea has benefited from higher commodity prices, the high imported inflation has increased domestic prices and affected consumer demand. The annual inflation outcome was 5.5 percent in the June quarter. With inflation lower than expected, the Bank maintained an accommodative stance of monetary policy by maintaining the Kina Facility Rate at 3.0 percent. This stance is also aimed at supporting the recovery and to encourage private sector lending and investment. The kina strengthened as the US dollar appreciated against all major currencies resulting in the trade-weighted index appreciating by 3.6 percent to 28.67 during the quarter.

Data from the Bank's Business Liaison Survey show that the total nominal value of sales in the formal private sector declined by 7.0 percent in the June quarter of 2022, compared to an increase of 6.8 percent in the March quarter of 2022. Excluding the mineral sector, sales increased by 10.8 percent in the June quarter of 2022, compared to a decline of 3.2 percent in the March quarter of 2022. By sector, sales increased in all sectors except the mineral sector, which recorded a decline. By region, sales declined in the Islands and the Southern regions while it increased in the National Capital District, Morobe, Momase (excluding Morobe), and the Highlands regions. Over the year to June 2022, total sales increased by 23.6 percent, compared to an

increase of 24.8 percent over the corresponding period of 2021. Excluding the mineral sector, sales increased by 17.6 percent over the year to June 2022, compared to an increase of 29.0 percent over the corresponding period of 2021.

The Bank's Employment Index shows that the level of employment in the formal private sector increased by 2.3 percent in the June quarter of 2022, compared to an increase of 1.2 percent in the previous quarter. Excluding the mineral sector, the level of employment increased by 2.4 percent. By sector, the level of employment increased in the construction, transport, wholesale, agriculture/forestry/fishing, manufacturing, and mineral sectors, while it declined in the retail, and financial/business and other services sectors. By region, the level of employment increased in all the surveyed regions. In June 2022, the total level of employment increased by 3.7 percent, compared to a decline of 4.1 percent in the corresponding period of 2021. Excluding the mineral sector, the level of employment increased by 3.2 percent in June 2022, compared to a decline of 1.9 percent in the corresponding period of 2021.

Quarterly headline inflation, as measured by the consumer price index, increased by 2.0 percent in the June quarter of 2022, compared to an increase of 0.8 percent in the previous quarter. There were increases in the Transport, Household Equipment, Food and Non-Alcoholic Beverages, Alcoholic Beverages, Tobacco and Betelnut, Housing, Health, Miscellaneous, Restaurants and Hotel and Recreation expenditure groups, which more than offset decreases in the Education and Clothing and Footwear expenditure groups, whilst the Communication expenditure group recorded no change in the quarter. By urban centre, prices increased in all centers. Annual headline inflation was 5.5 percent in the June quarter of 2022, compared to an increase of 5.9 percent in the March quarter of 2022.

In the June quarter of 2022, the average daily kina exchange rate appreciated against all other currencies except the US dollar. It appreciated against the Japanese yen by 11.2 percent to ¥36.7729, the pound sterling by 6.4 percent to £0.2257, the euro by 5.0 percent to €0.2663, and the Australian dollar by 0.1 percent to A\$0.3969, while it depreciated against the US dollar at US\$0.2840. These currency movements resulted in the appreciation of the TWI by 3.6 percent to 28.67 in the June quarter of 2022.

The weighted average kina price of PNG's exports, excluding liquefied natural gas, increased by 18.2 percent in the June quarter of 2022, compared to the corresponding quarter of 2021. Higher international prices accounted for this increase. There was an increase of 20.5 percent in the weighted average kina price of mineral exports, reflecting higher kina prices of all mineral commodities, except gold. For agricultural, logs and marine product exports, the weighted average kina price increased by 9.8 percent, due to higher kina prices for all non-mineral commodities, except for cocoa, copra and marine. Excluding logs, the weighted average kina price of agricultural and marine product exports increased by 11.6 percent in the June quarter of 2022, compared to the corresponding quarter of 2021.

The balance of payments recorded an overall surplus of K240 million for the first six months of 2022, compared to a deficit of K813 million in the corresponding period of 2021. A surplus in the current account more than offset a deficit in the capital and financial account.

The surplus in the current account was due to a trade surplus and net transfer receipts, which more than offset net service and income payments.

The deficit in the capital and financial account was due to net outflows from direct and other investments reflecting related party transactions and build-up in offshore foreign currency account balances of mineral companies, respectively. Net outflows in Government and private sector loan repayments also contributed to the deficit.

The level of gross foreign exchange reserves at the end of June 2022 was K10,563.3 (US\$3,052.8) million, sufficient for 9.2 months of total and 16.3 months of non-mineral import cover.

The Central Bank maintained an accommodative stance of monetary policy in the June quarter of 2022, by maintaining the Kina Facility Rate at 3.0 percent, to support the economic recovery and to encourage private sector lending and investment. The dealing margins of the Repurchase Agreement (Repo) Facility was maintained at 100 basis points on both sides of the KFR and the Cash Reserve Requirement for the commercial banks was maintained at 7.00 percent during the quarter.

The average level of broad money supply increased by 4.7 percent in the June quarter of 2022, compared to an increase of 6.6 percent in the previous quarter. This was mainly driven by an increase in the average net foreign assets and net domestic claims of the banking system. The average net domestic claims, excluding net claims on Central Government, increased by 3.0 percent in the June quarter of 2022, compared to a decline of 0.7 percent in the previous quarter. This reflected increases in average net claims on other financial corporations, private sector and 'Provincial and Local Level Governments, which more than offset a decline from public non-financial corporations.

The net foreign assets of financial corporations, comprising depository corporations and other financial corporations, increased by 5.9 percent to K10,883.5 million in the June quarter of 2022, compared to a decline of 5.6 percent in the previous quarter. This was driven by an increase in the net foreign assets of the depository corporations, which more than offset the decline in other financial corporations. The increase in the net foreign assets of depository corporations was mainly from increase in foreign reserves at the Central Bank due to inflows from dividends, liquefied natural gas tax and royalty payments.

Net claims on the Central Government by financial corporations increased by 5.4 percent to K19,869.9 million in the June quarter of 2022, compared to an increase of 8.9 percent in the previous quarter. This reflected increase in net purchase of Government securities, more than offsetting the increase in Government deposits at the Central Bank.

In the June quarter of 2022, total domestic credit extended by financial corporations to the private sector, public non-financial corporations and Provincial and Local Level Governments declined by 1.1 percent to K17,970.7 million, from an increase of 2.5 percent in the previous quarter. This reflected repayment of K302.8 million by the public non-financial corporations, which more than offset an increase in lending of K92.7 million and K14.4 million to the private sector and provincial and local level governments, respectively.

The preliminary fiscal operations of the National Government over the six months to June 2022 show a deficit of K2,078.1 million, compared to a deficit of K2,690.5 million in the corresponding period of 2021. The lower deficit reflected improvement in revenue.

Total revenue and grants was K7,988.9 million over the six months to June, 45.1 percent higher than in the corresponding period of 2021 and represents 49.3 percent of the 2022 Budget amount. The outcome reflected higher tax revenue.

Total expenditure was K10,067.0 million over the six months to June 2022, 22.8 percent higher than in the corresponding period of 2021 and represents 45.4 percent of the 2022 Budget. This was due to higher recurrent expenditure and interest cost.

The developments in the revenue and expenditure in the June quarter resulted in a deficit of K2,078.1 million. The deficit was financed mainly from domestic sources totaling K2,264.0 million, which more than offset the net external loan repayment of K185.9 million. Net domestic financing comprised of K2.4 million, K1,139.6 million, K4.9 million, and K1117.1 million from BPNG, other depository corporations, other financial corporations and other resident sectors.

Total public (Government) debt outstanding was K50,568.2 million as at end of June 2022, an increase of K2,194.1 million from the March quarter, and represented 45.8 percent of gross domestic product. This comprised of K27,823.5 million in domestic debt and K22,744.7 million in external debt.