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Papua New Guinea: Staff Report for the 2000 Article IV Consultation And First Review Under Stand-By Arrangement; Statement by Staff Representative; Public Information Notice Following Consultation; Statement by Papua New Guinea Representative on the IMF Executive Board

As required under Article IV of its Articles of Agreement, the International Monetary Fund conducts periodic consultations with its member countries. In the context of the 2000 Article IV consultation with Papua New Guinea, the following documents have been released and are included in this package:

- the staff report for the 2000 Article IV consultation, prepared by a staff team of the IMF, was completed on **August 6, 2000**. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF;
- a staff statement released the day of the Board discussion on **October 13, 2000**, updating information on recent economic developments;
- the Public Information Notice (PIN), which summarizes the **views of the Executive Board as expressed during the October 13, 2000, Executive Board discussion** of the staff report that concluded the Article IV consultation; and
- a statement by the authorities of Papua New Guinea.

Further background documentation prepared by IMF staff for the consultation may be published separately at a later date. The policy of publication of Article IV staff reports and PINS allows for the deletion of market-sensitive information.

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PAPUA NEW GUINEA

Staff Report for the 2000 Article IV Consultation and First Review Under the Stand-By Arrangement

Prepared by the Asia and Pacific Department

(In consultation with other departments)

Approved by R. Anthony Elson and Leslie Lipschitz

October 2, 2000

- Discussions were held in Port Moresby during July 24–August 6, 2000. The staff team met with Chief Secretary Igara, Secretary for Finance and Treasury Tarata, Bank of Papua New Guinea Governor Kamit, and other senior government officials.[1]

- The 14-month Stand-By Arrangement, in the amount of SDR 85.5 million (65 percent of quota) was approved by the Executive Board on March 29, 2000.

- Performance under the program has been satisfactory. Approval of the arrangement prompted an improvement in market sentiment, with the kina appreciating through June and the net international reserves of the central bank increasing strongly.

- All quantitative performance criteria for end-June were observed. The end-June structural performance criterion on the preparation of a plan for public sector reform was not observed, but the plan has now been completed. Therefore, the staff support the authorities' request for a waiver and also for a modification of the definition of the performance criterion adjuster on the government's domestic financing.

- Papua New Guinea has accepted the obligations of Article VIII, Sections 2, 3, and 4 and maintains an exchange system free of restrictions on payments and transfers for current international transactions.

- The authorities have consented to publication by the Fund of the Letter of Intent, the Memorandum of Economic and Financial Policies, and the staff report following the conclusion of the discussion by the Executive Board.

[1]The team comprised Messrs. Kronenberg, Rosales, Oestreicher, and Khatri (all APD), Ms. Roehler (FAD), Mr. Sobolev (PDR), and Ms. Villar (staff assistant, APD). The team was assisted by Mr. Tareen (Resident Representative).

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Executive Summary

- **The government that took office in July 1999 is improving economic management and working to create the conditions for sustained private sector-led economic growth**. The government has made stabilization its main macroeconomic objective and is implementing an economic program supported by the Fund, other multilateral agencies, and bilateral donors.

- **Performance under the Stand-By Arrangement has been satisfactory, and all quantitative performance criteria for end-June 2000 were met**. However, the structural performance criterion on the completion of a plan for a comprehensive public sector reform by end-June was not observed. The plan has now been prepared and endorsed by Cabinet as a prior action for completing the first review.

- **Macroeconomic conditions have improved so far in 2000**. The overall government balance recorded a small surplus during the first half of the year, compared to a deficit in the program. Renewed confidence prompted exporters to accelerate the repatriation of export receipts, sparking an appreciation of the kina during the second quarter. To slow down this appreciation, the central bank intervened in the market during the second quarter of the year. As a result, the net international reserves at end-June stood at $230 million, some $80 million higher than programmed. The exchange rate has been broadly stable since August.

- **The quarter-on-quarter inflation rate rose to 4.4 percent in the second quarter of 2000, in part reflecting recent tax increases**. However, it is expected to decline rapidly in the second half of the year with the lagged effect of the appreciation of the kina during the second quarter of the year and continued tight monetary policy.

- **Progress is being made in implementing structural reforms**. As part of the preparations for the public sector reform, the government is conducting departmental reviews to define core functions and appropriate staffing in selected agencies. Preparations for the privatization of a large bank have been initiated. The government is also seeking an early resolution of the financial problems faced by the National Provident Fund.

- **The authorities agreed to performance criteria for end-December 2000 that are more ambitious than the original indicative targets**. Also, they reiterated their intention to aim at broad fiscal balance in 2001, excluding the clearance of pre-1999 obligations.

I. Background

1. **Economic performance in the late 1990s was adversely affected by a large terms-of-trade shock, a severe drought, a relaxation of macroeconomic policies, and widespread governance problems.** Depressed export earnings resulted in low tax revenue, which contributed to weak government finances in 1998 and 1999 (Table 1). As confidence deteriorated, private capital outflows intensified, and gross official international reserves fell sharply. Despite intervention by the central bank, the kina lost nearly one-third of its value against the U.S. dollar between end-1997 and mid-1999, pushing inflation up from the mid-single digits to the 12–20 percent range (Figure 1).

2. **At the conclusion of the last Article IV consultation in June 1999, Executive Directors expressed concern about the economic situation and outlook.** Directors recommended sustained implementation of tight monetary and fiscal policies, including the reining-in of domestic credit to government. They also strongly encouraged the authorities to improve transparency and accountability in the public sector, develop a concrete action plan for privatization, and improve the quality of macroeconomic statistics.

3. **With an economic crisis looming, parliament formed a new government in July 1999 with a mandate to undertake fundamental reforms.** The new government initiated policy discussions with the Fund and World Bank, quickly implemented a supplementary budget that included significant revenue measures, and pledged to undertake reforms to improve the governance, transparency, and efficiency of the public sector.

II. The Stand-By Arrangement: Objectives and Initial Performance

4. **A 14-month Stand-By Arrangement (SBA) in the amount of SDR 85.5 million (65 percent of quota) was approved by the Executive Board on March 29, 2000.** The program aims at macroeconomic stabilization and laying the basis for sustained growth over the medium term. It targets a reduction in inflation to 5 percent by the end of the year, and an increase in gross international reserves to $408 million (3.8 months of import cover). These targets are to be achieved through a tightening of monetary policy and a reduction in the overall government deficit. Structural policies are focused on public sector reforms; enhancing the independence and accountability of the central bank and strengthening the supervision of the financial system; and promoting private sector development through privatization and tax reform. The program is also supported by a $90 million World Bank Governance Promotion Structural Adjustment Loan (SAL) approved in June 2000, and sizable financial packages from Australia, Japan, and other donors.

5. **Macroeconomic performance and market sentiment improved following approval of the arrangement in March.** The overall government balance recorded a small surplus during the first half of the year, compared to a deficit in the program. This was the result mainly of buoyant tax revenue, reflecting strong mineral export prices and better collection efforts. Renewed confidence in the economy prompted exporters to accelerate the repatriation of export receipts in the second quarter of 2000, triggering an appreciation of the

kina and foreign exchange purchases by the central bank. Subsequently, the central bank sold foreign currency in the face of some downward exchange rate pressure as capital reflows dried up, with expectations for lower coffee exports. In all, the net international reserves increased at a faster pace than originally envisaged, from $180 million at end-1999 to $260 million at end-August 2000, and the kina appreciated from a low of $0.32 in late February to $0.42 in early June, and has since settled at around $0.37.

6. **The quarter-on-quarter inflation rate rose from 2.6 percent at end-March to 4.4 percent at end-June (21.8 percent on a year-on-year basis), due in part to recent tax increases**. Inflation is expected to decline sharply during the second half of 2000, as the lagged effect of the appreciation of the kina during the second quarter of 2000 passes through to prices.

7. **Compliance with quantitative performance criteria and benchmarks has been broadly satisfactory** (Tables 2, 3, and 4). All quantitative performance criteria for end-June were observed. Most quantitative fiscal benchmarks were also observed at end-June, but the benchmark on the clearance of pre-1999 domestic arrears was missed by a relatively small amount at end-June. However, payments are now back on schedule. The benchmark on central government recurrent expenditure also was not observed due to larger-than-anticipated interest payments stemming from higher-than-expected interest rates and an underestimation of the initial debt stock.

8. **Implementation of structural reforms has been generally on track**. Structural performance criteria on the completion of audits of the two major pension funds (for end-March) and parliamentary passage of the revised Central Bank Act and the new Bank and Financial Institutions Act (for end-April) were observed. Progress has also been made in the implementation of the new guidelines to improve the transparency, fairness, and efficiency of rural development spending. Preparation of a plan for comprehensive public administration reform (a performance criterion for end-June) took somewhat longer than originally expected, but a detailed plan and timetable have now been completed and endorsed by Cabinet (prior action for the completion of the first review).

III. Discussions

9. **The authorities remain committed to the program and are determined to maintain policies conducive to stabilization and structural reform**. Agreement was reached on a supplement to the March 2000 Memorandum of Economic and Financial Policies and on performance criteria for end-December 2000. The program targets for net international reserves (NIR) and net domestic assets (NDA) of the central bank for end-December 2000 constitute a tightening relative to the original indicative targets, reflecting the saving of the export revenue windfall that materialized during the first half of the year. The authorities agreed to targets for 2001 based on the original program objective of broad fiscal balance (excluding the clearance of pre-1999 obligations) and revised external financing projections.

Fiscal policy

10. **While the revised program for 2000 entails a modest increase in the overall fiscal deficit relative to the original target,[2] the performance criterion on net domestic financing for the year is more ambitious** (Tables 5 and 6). Tax revenue is projected to be higher than in the original program partly as a result of higher oil prices than originally envisaged, but this will be more than offset by a shortfall in nontax revenue due to lower-than-expected central bank profits in 1999; larger-than-originally expected interest payments; payment of a foreign loan guarantee to facilitate divestment of the government's equity in a cement company; and a small increase in health spending.

11. **Although the authorities are still at a relatively early stage in formulating the 2001 budget, they noted that policies will be guided by the objectives of maintaining broad underlying fiscal balance and lowering inflation.** The indicative program for 2001 envisages a reduction in the overall government deficit to ½ percent of GDP; excluding the payment of pre-1999 obligations, the overall position would be in balance.[3] Tax revenue in relation to GDP is expected to rise modestly, reflecting better administration of the recently introduced VAT and the full-year impact of tax increases that took effect in early 2000. The authorities are committed to limit the increase in the wage bill to10 percent in 2001, allowing for a moderate recovery in real wages after a large contraction in 1999–2000, and for a realignment of pay scales. They intend to maintain the temporary hiring freeze introduced in November 1999 pending progress in initiatives aimed at rationalizing the civil service in the context of a public sector reform program (Box 1). With privatization revenue expected to amount to about 2 percent of GDP and exceptional financing estimated at 1.5 percent of GDP, the indicative program would provide room for a further reduction in net domestic bank credit to government in 2001.

12. **The mission emphasized that the budget for 2001 should be framed in a manner consistent with program objectives.** Although the near-term outlook for tax revenue is satisfactory and savings from reduced interest obligations are likely to materialize, there are potential pressures for additional spending in 2001 and beyond. The possible costs of pension reform, which are as yet unquantified, are of particular concern. In this light, and in view of a projected decline in oil revenue over the medium term, the mission emphasized the need to establish clear expenditure priorities and to identify contingent measures to ensure that fiscal targets are achieved. To avoid the need for renewed cuts in real public sector wages, which could adversely affect the government's ability to attract and retain well-qualified staff, it

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[2]The National Statistical Office recently issued official GDP data for 1993–98 for the first time. Historical data and revised program projections are based on the new series, while original program ratios are expressed relative to the previous unofficial GDP estimates.

[3]Remaining pre-1999 obligations comprise mainly claims that were previously under dispute.

Box 1. Papua New Guinea: The Public Sector Reform Program

Reform of the public sector is a high priority for the current government. Commitment to such reform was made as part of both the Stand-By Arrangement and the World Bank's Structural Adjustment Loan. The Public Sector Reform Program (PSRP) has been developed by a Public Sector Reform Task Force, chaired by the Chief Secretary, in consultation with heads of departments and provincial authorities, and with assistance from the World Bank, the Asian Development Bank, and APEC. To avoid the poor outcomes of similar past programs, the plan emphasizes domestic ownership: participation of stakeholders, public and political support for the design and implementation of the program, and coordination with the international donor community.

The PSRP has nine principal objectives:

- Strengthen the policy, planning, and decision-making process as well as the relationship between the political institutions and state services (public services, constitutional, and statutory organizations).
- Streamline functions, organization structures, and resource management.
- Establish and align cost of government operations with available funding and development priorities.
- Improve efficiency and accountability.
- Establish a stable, professional, and performance-oriented public service.
- Improve reporting systems and data base linkages at both agency and government-wide levels.
- Rationalize facilities to better support sector operations.
- Improve partnership and cooperation between the public sector and churches, NGOs, and the private sector.
- Ensure probity, integrity, and respect for the law.

Thirty-six strategies with associated programs have been identified to achieve these objectives. Costing for the programs will be developed in the next few months and incorporated into the 2001 budget. Technical assistance will be forthcoming from Australia, the AsDB, and the World Bank.

Overall political responsibility and leadership for the implementation of the PRSP is being provided by the Cabinet's National Planning Committee, while the Central Agencies Coordinating Committee, chaired by the Chief Secretary, will be responsible for day-to-day implementation. To strengthen capacity for the reform process, a Public Sector Reform Management Unit has been established in the Department of the Prime Minister. To involve the community in the reform process, the Prime Minister will appoint a Public Sector Reform Advisory Group consisting of representatives of provinces, churches, trade unions, and research institutions.

Initial steps to move the PSRP ahead have already been taken. Functional expenditure reviews for the Departments of Finance and Treasury, Personnel Management, Defense, Foreign Affairs, Fisheries, and the Office of the Prime Minister will be completed by end-2000. Reviews of other core departments will be undertaken by early 2001. An audit of public sector staffing will be carried out as part of the 2001 budgetary process.

will be critical for the government to downsize the civil service as part of the public sector reform.

13. **A high level tax review commission was expected to submit its report to Cabinet before end-September (structural benchmark).** The report has been prepared and is expected to be discussed when Cabinet reconvenes in mid-October. The review is expected to suggest ways to improve corporate taxes (both the general and the special mineral resources regimes), personal income taxes, excise taxes, and log export taxes.[4] Recommendations are to be implemented as part of the 2001 budget. A separate review of the VAT has also been initiated. The authorities also intend to increase resources to support revenue collection, particularly to strengthen the administration of the VAT and increase the number of tax audits.

Monetary and exchange rate policies

14. **The authorities agreed to a revised financial program for end-December 2000 with more ambitious targets for NIR and NDA of the central bank.** These targets reflect the high level of open market sales during the first half of the year to mop up the liquidity overhang that existed at end-1999 and to sterilize external inflows, which took place in the wake of the approval of the SBA. In addition, despite the slightly higher fiscal deficit now projected for the year as a whole, the government is expected to make larger net repayments to the domestic banking system (Tables 7 and 8) due to lower-than-originally estimated external amortization obligations. On this basis, and in spite of a slight decrease in reserve money growth relative to the original program, the target for NIR at end-December 2000 has been raised by \$22 million to \$339 million (Table 9).

15. **The interest rate on treasury bills remained high—on the order of 20 percent—during the first half of 2000 reflecting both the high actual rate of inflation and the tightening of monetary policy.** Since May, the rate on bills has declined by about 6 percentage points. While the authorities noted that there were pressures to lower interest rates further, the staff argued that the central bank should resist pressures for additional reductions in interest rates until inflation is on a clearly declining trend.

16. **On operational aspects of monetary policy, the mission welcomed recent steps to strengthen competition in the treasury bill auction and noted the challenges ahead.** As the present stock of treasury bills is projected to be extinguished in the latter part of 2001, the mission noted that continued conduct of open market operations may require conversion of medium-term government debt held by the central bank into treasury bills, or issuance of central bank securities. Direct instruments of monetary policy, such as changes in the cash reserve requirement or the minimum liquid assets requirement, which were used often in

[4] The log export tax regime is being reviewed in the context of a forestry management project under the World Bank SAL.

1998 and the first half of 1999, proved disruptive to the efficient functioning of the financial system, and should continue to be avoided.

17. **The recently approved new Central Bank Act (CBA) has improved the framework for monetary policy.** The CBA redefines the objectives of the central bank and enhances its statutory independence, making price stability its principal objective. Independence has been enhanced through strict limits on lending to government, the charging of market-determined interest rates on credit to government, separation of debt management from the conduct of monetary policy, clear rules for the appointment of the central bank governor as well as procedures for his removal, and the requirement for the bank to publish semi-annual reports outlining monetary policy developments and prospects (the first one was published in July 2000).

18. **The authorities indicated that the condition of the banking system remains sound.** In particular, the share of nonperforming loans to total loans has remained broadly stable in recent months, and stood at 9 percent at end-June 2000. The authorities agreed that close surveillance over the banking system should remain a priority, noting that the recently passed Banks and Financial Institutions Act will help strengthen bank supervision. Most banks are subsidiaries of Australian banks and are also subject to consolidated supervision by Australian regulators. The largest bank (PNGBC) has been recently audited and due diligence will soon be conducted in preparation for its privatization.

19. **The authorities agreed to preserve a flexible exchange rate policy, and that intervention in the foreign exchange market should continue to be limited to the smoothing of short-term volatility and the achievement of the international reserve targets.** While the kina depreciated sharply in real effective terms from mid-1997 through February 2000, there was an appreciation during the remainder of the first half of 2000, reflecting improved confidence in the policy environment and the strengthening of the terms of trade (Figure 2).

Structural reform policies

20. **Progress is being made in implementing structural reforms.** In August, Cabinet endorsed a public sector reform program which aims at strengthening the policy and decision-making process, and improving efficiency and accountability of the public sector (see Box 1). In line with the recommendations of the World Bank, departmental reviews are being conducted in place of the public expenditure review that had been originally envisaged. These reviews seek to define core functions and appropriate staffing in selected agencies and will permit shedding redundant staff and improving service delivery. Separations have already been effected in the Defense Department, and a decision will be taken shortly on the rationalization of diplomatic missions abroad. Also, to increase transparency and accountability in financial management, the government has closed all major revenue-retaining trust accounts, with control over these proceeds transferred to the Treasury.

21. **The government is implementing new procedures to improve the transparency, efficiency, and fairness of spending for rural development.** Earlier this year with World Bank assistance, the government fundamentally redesigned the Rural Development Program (RDP), replacing a system that had been driven by political patronage with a transparent one which stresses accountability.[5] Project applications are evaluated by the Joint District and Provincial Planning and Budget Priorities Committee and the Office of Rural Development (ORD) and, once approved, are subject to ongoing review, which includes quarterly reports, on-site inspections, and financial control by an independent private managing agent. Most of the initial round of recent project proposals submitted by parliamentarians to ORD did not comply with the new guidelines and were not approved. However, ORD has since undertaken a strong drive to help familiarize parliamentarians with the objectives and requirements of the new system, and a significant number of recent project proposals have been approved. More generally, the authorities consider that governance and macroeconomic performance will be enhanced by planned political reforms aimed at strengthening democratic institutions.

22. **As regards the privatization program, the authorities are preparing to take Finance Pacific (a conglomerate that includes PNGBC) to the point of sale by end-2000** (a structural performance criterion). With support from the World Bank, the PNGBC's financial accounts are being audited, and the contract for carrying out due diligence has been awarded to a major international accounting firm. Meanwhile, in July the government divested its stake in a failed cement company (Halla Cement), albeit at a net cost equivalent to 0.2 percent of GDP. To facilitate the future sale of key utilities, the government is planning an international tender for a contract to review the regulatory framework for utilities. The authorities agreed to set a timetable for the privatization of another major public enterprise by the time of the discussions for the second review.

23. **Headway is also being made in the trade area.** Implementation of the seven-year Tariff Reform Program (TRP) launched in 1999 is continuing. As there are no significant nontariff barriers and the simple average tariff is already below 10 percent, Papua New Guinea is rated 1 on the Fund's index of trade restrictiveness. In July 2000, parliament passed a free trade zone legislation establishing the framework and mechanism for the creation and operation of free trade zones with the purpose of bringing investment and setting up processing industries with export and employment creation potential in the less developed provinces.

24. **The mission stressed the need for an early resolution of the problems of the National Provident Fund (NPF), which faces an accumulated loss of about 1½ percent of GDP.** The mission welcomed the recent change in the board of NPF and the appointment of a commission that will review past management and governance practices, but expressed reservations about plans to suspend benefit payments, which could have significant social

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[5]See Box 2 of EBS/00/53 Supplement 1, Papua New Guinea: Request for Stand-By Arrangement (March 22, 2000).

consequences. Instead, the mission urged the authorities to write down NPF member balances to reflect audited values to the extent permissible by law. It also emphasized that any government payment to attenuate the impact of the write-down (or contribute to a possible recapitalization of the NPF) should be limited, fully reflected in the budget, and preceded by a comprehensive restructuring of the pension industry. The authorities indicated that the speed of their action to bring benefits in line with the actual value of NPF assets is being constrained by a legal challenge. Also, they underlined that the NPF is a defined-contribution provident fund and that the government is under no legal obligation in respect to its losses. In addition, they noted that a new superannuation bill and a new life insurance bill are being drafted. These bills are intended to introduce supervision, establish the central bank as regulator, and outline the architecture of the industry.

IV. The Medium-Term Outlook

25. **The staff have formulated a medium-term scenario (Tables 10 and 11) predicated on full implementation of the authorities' program for the period 2000–01 supported by the SBA**. The scenario assumes continued sound fiscal and monetary policies and further efforts at structural reform that would underpin macroeconomic stability and the growth of the nonmineral sector. Assumptions about the external environment are in line with WEO projections (July 2000). It takes into account the authorities' projection that oil output will contract sharply in the years ahead as fields are depleted, with existing wells running dry by 2015. In the absence of major new investments in the gas and nickel industries, projected increases in output of gold and other minerals are not expected to offset the decline in oil production, with mineral GDP declining over the medium term.

26. **In this context, the early and substantial fiscal adjustment envisaged in the program remains essential to permit a reduction in interest obligations over the medium term**. The secular decline in oil output will erode government revenue and put pressures on the public finances. Early fiscal adjustment would permit a reduction in public sector debt relative to GDP and a lowering in interest rates that would set in a virtuous cycle, with a reduction in the interest bill in relation to GDP helping to offset a declining tax-to-GDP ratio over the medium term. In addition, continued improvements in revenue administration would need to be accompanied by firm expenditure control. Preserving a prudent fiscal policy will also facilitate continued external assistance and a domestic borrowing requirement consistent with the availability of sufficient bank credit for the private sector. In the context of rapid nonmineral real GDP growth and price stability, the demand for monetary aggregates would rise at a somewhat faster pace than GDP, the flexible exchange rate regime would ensure that external competitiveness remains adequate, and the official net international reserves would remain at a comfortable level.

27. **Prospects would improve if major investments in gas and nickel, presently being contemplated by investors, were to take place in the years ahead**. These very large investments (about $1.7 billion over the projection period (2001–05) and about $3 billion through 2011) would result in relatively large external current account deficits during the

construction phase (particularly during 2002–04), which would be covered by equity capital inflows. Output could commence around 2004, with tax revenue rising soon thereafter.

28. **There are risks to the near- and medium-term outlook**. A slackening in the determination to maintain sound policies would complicate economic conditions in the near term and could hinder private investment, including the prospects for the gas and nickel projects. Such a weakening in financial policies would magnify the effects of the secular decline in oil exports, with the deterioration in the public finances likely leading to the return of high inflation and exchange rate instability. Over the medium term, Papua New Guinea remains vulnerable to large terms-of-trade shocks.

V. Program Monitoring and Capacity to Repay the Fund

29. **There was agreement about the desirability of broadening the scope of the adjuster on the government's domestic financing**. Such modification would help ensure the saving of revenue windfalls beyond any increase in domestic interest obligations that could result from a tighter monetary policy. Instead of a partial (80 percent) adjuster for excesses in nonmineral tax revenue only, the ceiling on net domestic financing of the government would be adjusted downward by the full amount of the excess of the sum of nonmineral tax revenue and nontax revenue less domestic interest payments over the program level. The adjuster would continue to operate only in the direction of reducing the ceiling on the government's domestic financing.

30. **Apart from the changes to the adjuster, the specification of the performance criteria remains unchanged**. The performance criteria for end-September and end-December 2000 on the ceilings on new public and publicly guaranteed short-, medium-, and long-term external nonconcessional debt exclude financial leases. This is because no reporting procedures have yet been established with the authorities. The authorities asserted that they do not have financial lease contracts nor do they expect to engage in such contracts. While the staff have no reason to doubt this assertion, the staff will propose to include financial leases in the respective performance criteria for end-March 2001 and to establish appropriate reporting procedures during the second review (expected to be concluded in December 2000–January 2001). As budget preparation was at an early stage, the mission agreed to set performance criteria for end-March 2001 during the second review discussions, when the budget would be finalized.

31. **As regards the revised external financing requirement for 2000 ($180 million), prospects have improved with the recent approval of the World Bank SAL**. Japan ($50 million) and Australia ($30 million) have linked their lending operations to performance under the World Bank and Fund programs, respectively. The financing need envisaged for 2001 is expected to be filled by loans from Australia and other bilateral donors, the World Bank, the Asian Development Bank, and possibly the European Union. In light of the proposed schedule of purchases under the arrangement (Table 12), capacity to repay the Fund remains strong, with obligations to the Fund over the medium term projected not to exceed 2 percent of exports of goods and nonfactor services (Table 13).

VI. Statistical and Other Issues

32. **While data provision to the Fund is broadly adequate for surveillance and program monitoring, there is a need to improve macroeconomic statistics further.** Following a recent assessment of its observance of the Fiscal Transparency Code, the government will begin work, with FAD technical assistance, to expand the coverage of the public sector statistics to include the operations of the rest of the general government. Also, it will intensify efforts to resolve inconsistencies between monetary and fiscal statistics and take early action to improve the statistical coordination between the Department of Finance and Treasury and the Central Bank. Among other important developments in the statistics area, the National Statistical Office has published official national accounts data for 1993–98 and is compiling the ten-year census.

33. **The authorities also**:

- agreed to the publication of the fiscal Report on Observance of Standards and Codes (ROSC) module following the completion of the Article IV consultation;
- undertook to provide written acceptance of the Fourth Amendment to the Articles of Agreement and to cooperate with the safeguards initiative; and
- expressed their strong appreciation for the appointment of a resident representative in Port Moresby in late May 2000.

VII. Staff Appraisal

34. **The government that took office in July 1999 is improving economic management and is working to create the conditions for sustained private sector-led economic growth**, through rapid stabilization and structural reform. After taking corrective fiscal action in the latter part of 1999, the government maintained tight fiscal and monetary policies in the first half of 2000. Also, it is setting the stage for structural reforms aimed at raising efficiency in the provision of public services and fostering private saving and investment. This should help sustain robust economic growth in the face of falling oil output, as existing fields are depleted. Confidence in the government's program has been enhanced by the Board's approval of the SBA and support from multilateral and bilateral donors.

35. **The government's main challenge ahead is to sustain the adjustment effort and press ahead with the implementation of the structural reform agenda.** The government's observance of the quantitative performance criteria for end-June 2000 augurs well for the success of the program. Perseverance with program policies should facilitate the attainment of the authorities' objectives for 2000. At the same time, strong and timely implementation of planned structural measures remains essential to solidify confidence in the program.

36. **Containing the fiscal deficit and reducing net government debt are essential to ensure fiscal sustainability.** The fiscal adjustment envisaged under the program should help

reduce government debt relative to GDP and contribute to the targeted decline in inflation, thereby facilitating a fall in interest rates. These factors would put in train a gradual reduction of the interest bill in relation to GDP that would help offset the projected decline in tax revenue from oil activities. Thus, the staff support the authorities' efforts to achieve broad fiscal balance (excluding the clearance of pre-1999 obligations) in 2001 and over the medium term. However, the staff urge the authorities to stand ready to take additional adjustment measures, if needed, to ensure that this goal is met. It will also be important to ensure continued adherence to the schedule for the clearance of pre-1999 domestic arrears.

37. **Higher oil prices and tax measures adopted in the latter part of 1999 and early 2000 have contributed to a significant improvement in revenue performance**. Going forward, efforts to strengthen revenue administration should help sustain this improvement. The staff support plans to allocate sufficient resources to support revenue collection.

38. **In line with the recommendations of the ROSC report, the authorities are making progress toward addressing shortcomings in the expenditure process**. In particular, they are working to prevent unbudgeted commitments by certain departments and agencies which, in the recent past, led to arrears. Efforts also are being directed at establishing firmer control over the wage bill, which is essential to improve the flexibility of current expenditure. The authorities have undertaken to limit the increase in the wage bill to not more than 10 percent in 2001. Also, the temporary hiring freeze in place since November 1999 should be maintained pending progress in public sector reform initiatives aimed at rationalizing the civil service. Planned privatization will also help check the growth of government transfers to the rest of the public sector.

39. **Monetary policy has been successful in mopping up the large overhang of liquidity that existed at end-1999 and in sterilizing external inflows in the first half of 2000**. The NIR and NDA targets for end-December 2000 have been revised to preserve the overperformance achieved through end-June. The central bank should resist pressures for additional reductions in interest rates until inflation is on a clearly declining trend. The staff welcome the recent steps taken to strengthen competition in the treasury bill auction, as well as the recent passage of the revised Central Bank Act and the Banks and Financial Institutions Act, which have improved the framework for monetary policy and supervision of financial institutions.

40. **The staff support the authorities' request for a modification of the arrangement to broaden the scope of the adjuster on the government's domestic financing**. Such a modification would help ensure the saving of revenue windfalls beyond any increase in domestic interest obligations that could result from a tighter monetary policy.

41. **The staff support the authorities' flexible exchange rate policy**. Intervention in the foreign exchange market should continue to be limited to the smoothing of short-term volatility and the achievement of the international reserve targets.

42. **The authorities are making good progress in implementing structural reforms aimed at improving the governance, transparency, and efficiency of public sector operations.** The recent introduction of new procedures and management structures for the operation of the RDP is expected to improve accountability and governance, and increase efficiency in this program. Recent audits of the major pension funds have set the stage for the planned reform of the pension industry, which also has been affected by deficiencies in management and governance. In addition, the review of the tax system that is under way is expected to suggest ways to enhance the transparency of the tax code and reduce the cost of compliance.

43. **While the end-June structural performance criterion on the preparation of a comprehensive plan for public sector reform was not observed, a detailed plan has subsequently been prepared and endorsed by Cabinet.** The authorities are already conducting reviews of selected departments aimed at improving efficiency and service delivery. It would now be important to extend these reviews to remaining departments and to move ahead with the shedding of identified redundancies and the redefinition of core functions.

44. **In the area of privatization, it will be important to ensure that Finance Pacific is brought to the point of sale by end-2000.** Also, a timetable for the privatization of another major public enterprise should be set by the time of the second review, and preparations for the privatization of selected utilities should continue.

45. **The situation of the NPF remains a cause for concern.** The staff urge the authorities to ensure that NPF member balances are written down to reflect audited values to the extent permissible by law, and to ensure that any government payment to attenuate the impact of the write-down (or contribute to a possible recapitalization of the NPF) be limited, fully reflected in the budget, and preceded by a comprehensive restructuring of the pension industry.

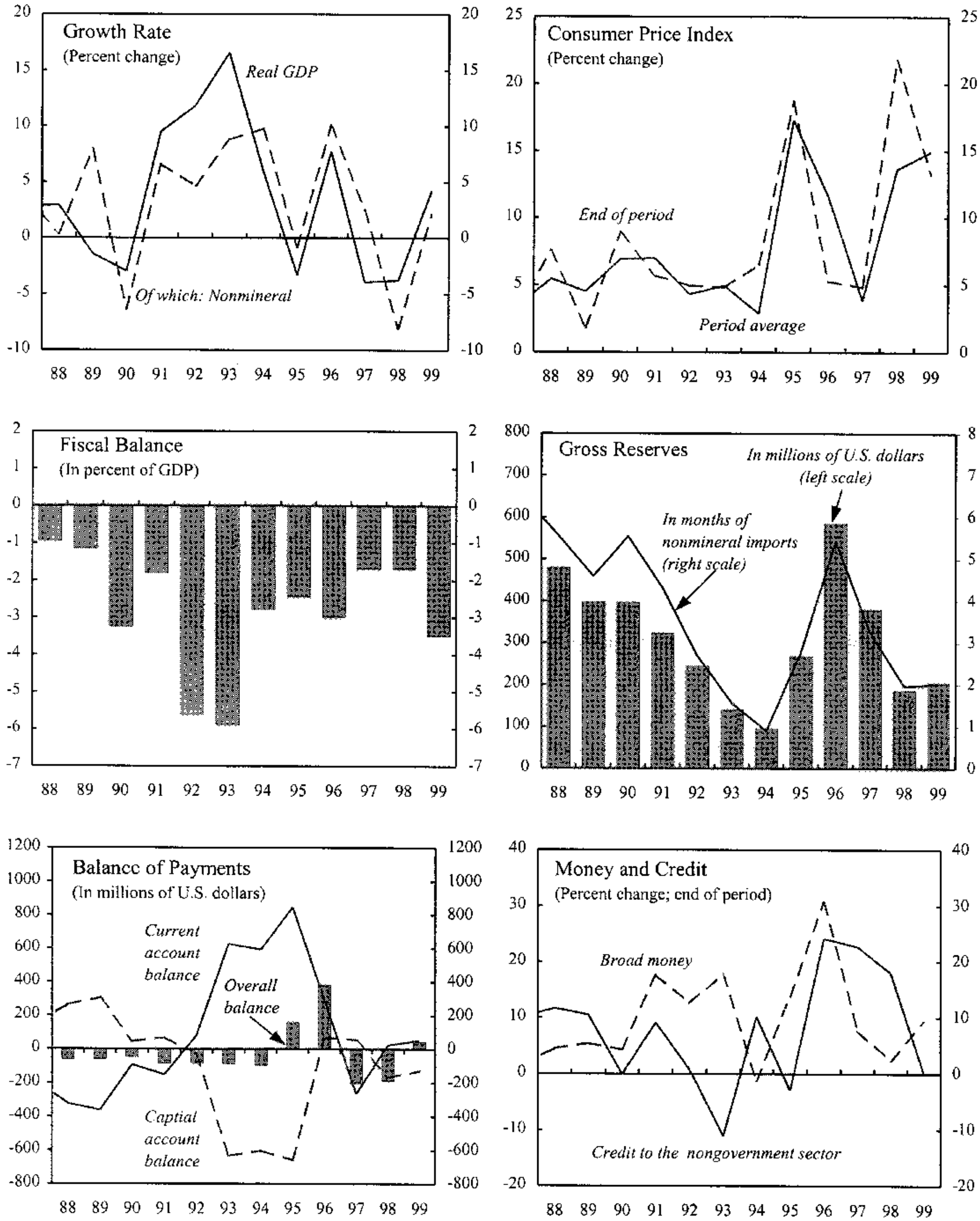
46. **While the authorities have taken important steps to improve the economic statistics, there is a need to redress remaining deficiencies.** A consistent set of national accounts for 1993–98 has been prepared and improvements have been made to the quality and timeliness of data reporting to the Fund, which are broadly adequate for program monitoring and surveillance. However, further improvements are still warranted in the price, external, and public finance statistics, and these should be promptly addressed. It is particularly urgent to compile more frequent and timely price statistics that could better guide monetary policy action. Strengthening the technical and managerial capacity of the National Statistical Office is a prerequisite for effective use of technical assistance.

47. **In sum, the early results of Papua New Guinea's program of adjustment and reform are very encouraging, reflecting the authorities' strong commitment to the program.** With perseverance in the implementation of appropriate policies, Papua New Guinea's economic and financial position will continue to strengthen. On this basis and in view of the recent endorsement by Cabinet of the plan and timetable for the public sector reform program, the staff support the completion of the first review, and the authorities'

request for a waiver to make available to Papua New Guinea the purchase subject to end-June 2000 performance criteria, and a modification of the definition of the adjuster on the performance criterion for the government's domestic financing.

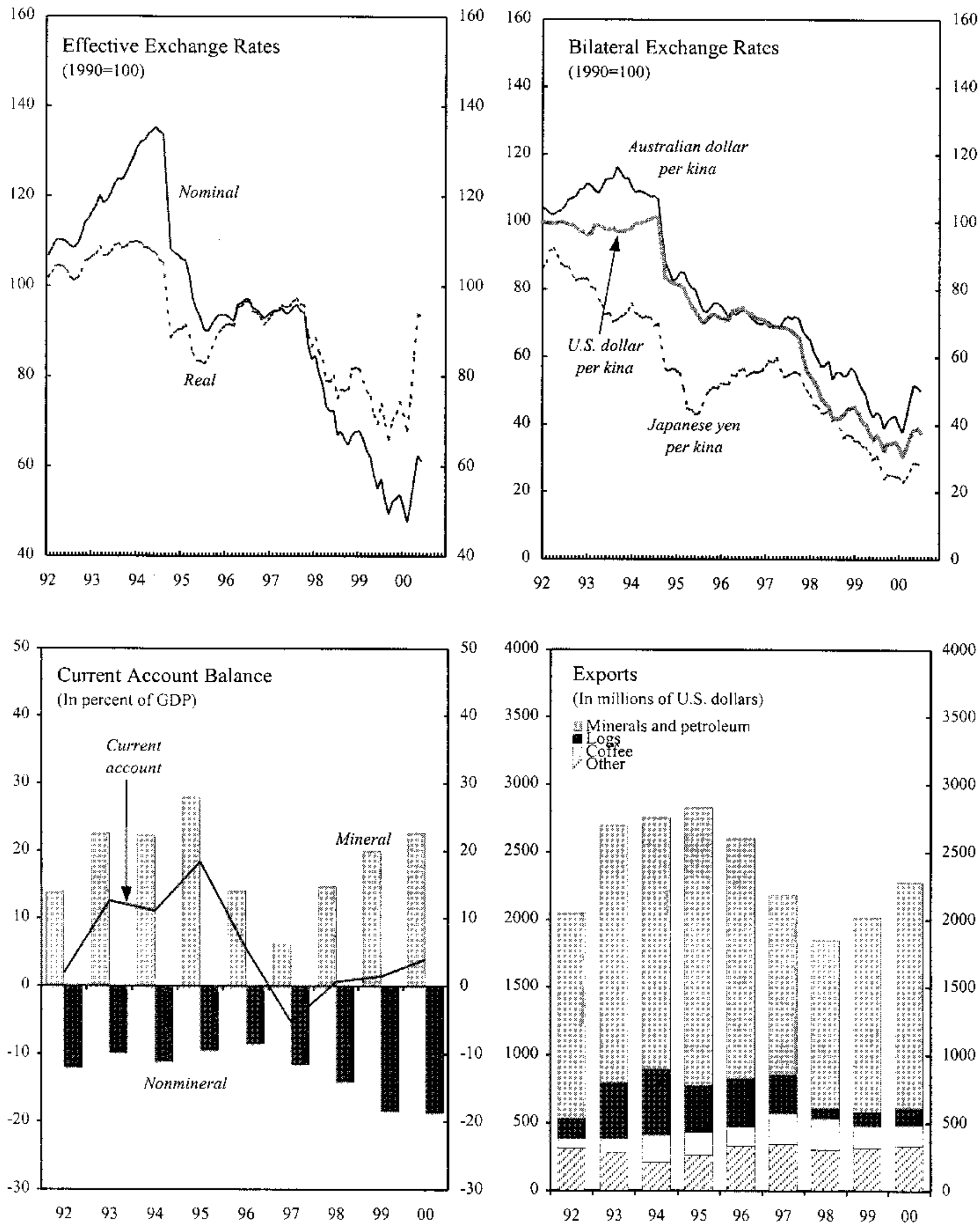
48. It is proposed that the next Article IV consultation be held on the standard 12-month cycle.

Figure 1. Papua New Guinea: Economic and Financial Indicators, 1988-99



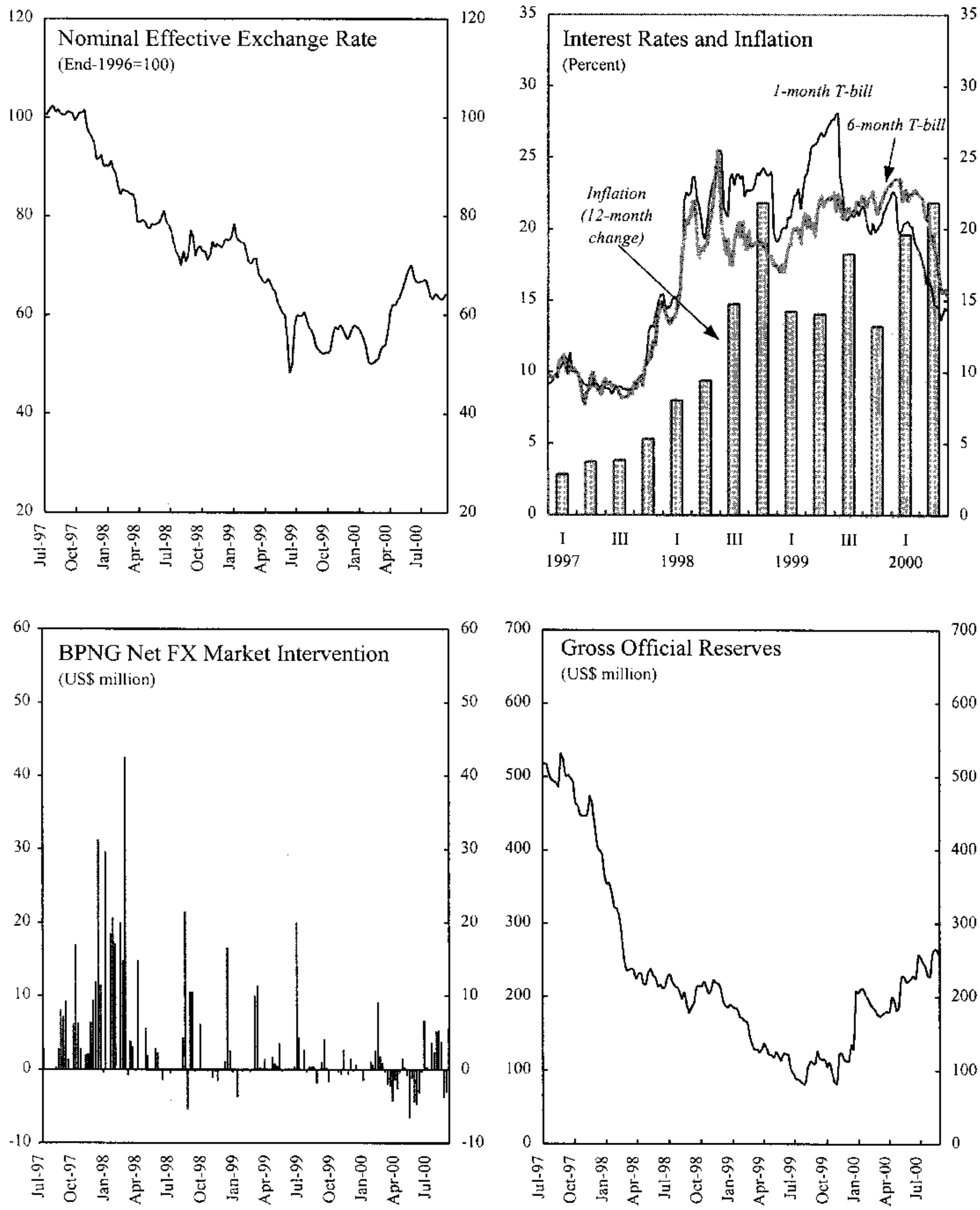
Sources: Data provided by the Papua New Guinea authorities; and Fund staff estimates.

Figure 2. Papua New Guinea: Selected External Indicators, 1992-2000



Sources: Data provided by the Papua New Guinea authorities; IMF, Information Notice System; and Fund staff estimates.

Figure 3. Papua New Guinea: Short-Term Financial Indicators, 1997-2000



Source: Data provided by the Bank of Papua New Guinea.

Table 1. Papua New Guinea: Selected Economic Indicators, 1996–2001

Nominal GDP (1999): US$3.6 billion
Population (1999): 4.7 million
GDP per capita (1999): US$776
Quota: SDR 131.6 million

	1996	1997	1998	1999	Prog. 2000	Prog. 2001
Real sector (percent change)						
Real GDP growth	7.7	-3.9	-3.8	4.2	3.4	2.7
Mineral	0.3	-26.0	16.8	12.3	1.5	-4.7
Nonmineral	10.1	2.5	-8.1	2.1	4.0	4.8
CPI (annual average)	11.6	3.9	13.6	14.9	12.0	4.3
CPI (12 months)	5.3	5.3	21.8	13.2	5.0	3.5
Terms of trade (percent change)	...	-4.2	-8.8	-1.9	8.9	-3.6
Central government budget (percent of GDP)						
Revenue and grants	26.7	31.2	29.2	27.9	29.2	29.5
Expenditure and net lending	27.0	31.0	31.6	30.3	31.3	30.0
Of which:						
Clearance of pre-1999 arrears	...	...	...	1.6	1.1	0.6
Structural adjustment expenditures 1/	...	...	...	...	1.0	...
Overall balance, cash basis (excluding grants) 2/, 3/	-5.5	-6.1	-7.7	-8.7	-7.2	-5.7
Overall balance, cash basis (including grants) 2/, 3/	-3.0	-1.7	-1.7	-3.5	-1.9	-0.5
Underlying balance 4/	-3.0	-1.7	-1.7	-1.9	0.2	0.1
Domestic financing	2.0	2.9	2.8	1.3	-1.5	-1.5
Of which: Banking system 5/	1.6	2.2	1.6	1.2	-1.5	-1.5
Foreign financing, net	0.1	-1.2	-1.2	1.9	3.2	0.1
Money and credit (year-on-year percentage change)						
Total domestic credit	5.8	22.7	17.1	4.0	-2.2	1.1
Net credit to government	19.2	22.7	15.4	11.2	-14.4	-16.8
Credit to the private sector	-7.8	36.3	29.0	10.5	9.0	11.2
Broad money	31.3	6.8	1.8	8.9	8.7	7.2
Balance of payments (US$ million)						
Exports, f.o.b.	2,603	2,186	1,849	2,019	2,278	2,176
Imports, c.i.f.	-1,791	-1,972	-1,425	-1,525	-1,710	-1,844
Current account (including grants)	289	-263	23	53	153	-30
(In percent of GDP)	5.5	-5.3	0.6	1.5	3.9	-0.8
Exceptional financing (net)	15	25	0	80	180	10
Overall balance	382	-204	-189	42	156	-10
Reserves and external debt (end-of-year, US$ million)						
Gross official reserves	586	380	187	204	408	499
(In months of nonmining imports, c.i.f.)	5.4	3.3	2.0	2.0	3.8	4.3
External amortization/gross international reserves (in percent)	69.2	84.0	195.4	240.9	73.7	54.0
Net international reserves	532	328	139	181	339	380
(In months of nonmining imports, c.i.f.)	4.9	2.8	1.5	1.8	3.1	3.3
Medium- and long-term external debt (percent of GDP)	36.3	43.3	51.8	45.3	43.2	39.5
Debt-service ratio (percent of external current receipts)	17.7	17.0	22.5	27.6	17.8	16.8
Exchange rates						
US$ per kina (end-period) 6/	0.74	0.57	0.48	0.37	0.38	...
Interest rate (182-day T-bills) 6/	9.2	14.5	23.9	20.4	14.3	...
Nominal effective rate 7/	-0.1	-10.5	-19.1	-20.6	-3.5	...
Real effective rate 7/	2.1	-6.4	-5.3	-10.0	-1.5	...

Sources: Data provided by the Papua New Guinea authorities; and Fund staff estimates and projections.

1/ One-off expenditures under a World Bank Structural Adjustment Loan (SAL) to support structural reforms.

2/ Includes expenditure on arrears and structural reform financed under the SAL.

3/ Includes residual deficit.

4/ Excludes clearance of arrears and spending on structural reform financed under the SAL.

5/ Includes a K 52 million write-down of the commodity stabilization fund in 1999.

6/ Actual end-of-period rate for 1996-99; value for 2000 refers to that recorded on September 5, 2000.

7/ Percent change from 12 months earlier, based on IMF Information Notice System. Figure for 2000 refers to percent change of March 2000 over December 1999.

Table 2. Papua New Guinea: Performance Criteria and Indicative Targets Under the Stand-By Arrangement, 2000-01

	Dec. 31, 1999	Mar. 31, 2000			Jun. 30, 2000			Sep. 30, 2000	Dec. 31, 2000		Mar. 31, 2001
		Original Program Indicative Targets			Original Program Performance Criteria			Original Program Performance Criteria	Original Program Indicative Targets	First Review Performance Criteria	First Review Indicative Targets
	Actual Stock	Unadjusted	Adjusted	Actual	Unadjusted	Adjusted	Actual				
					(In millions of kina)						
Ceiling on net domestic assets of the central bank 1/, 2/	183	251	244	89	226	201	(100)	83	(144)	(267)	(285)
Ceiling on net domestic financing of the government 2/, 3/, 4/	1534	59	45	(75)	133	34	17	101	(123)	(156)	(75)
					(In millions of U.S. dollars)						
Floor on net international reserves of the BPNG 5/, 6/, 7/	181	130	133	164	150	160	230	214	307	339	348
Ceiling on the contracting or guaranteeing of new nonconcessional external debt by the public sector with a maturity of over one year 3/, 7/, 8/	14	0	0	0	0	0	0	0	0	0	0
Ceiling on the stock of public sector and publicly guaranteed nonconcessional short-term external debt with initial maturity of up to one year 3/, 7/, 9/	0	0	0	0	0	0	0	0	0	0	0
Nonaccumulation of external payments arrears by the public sector		Continuing									

Sources: Data provided by the Papua New Guinea authorities; and Fund staff estimates and projections.

1/ Defined as reserve money less net foreign assets of the central bank. Actual figures for March and June 2000 are calculated by valuing net foreign assets at the program exchange rate of US$0.38/kina. For values of NDA calculated using historical exchange rates, refer to Tables 7 and 8.

2/ The ceiling on net domestic assets of the BPNG and net domestic financing of the government will be adjusted downward by the full extent to which the value of the following items exceeds the program targets laid out in Table 2: (i) Mineral Resource Stabilization Fund (MRSF) receipts, as recorded in the BPNG foreign exchange cash flow; (ii) exceptional external financing flows to the budget, as recorded in the BPNG foreign exchange cash flow; and (iii) total net receipts from asset sales. Upward adjustments will be made by the amounts that the values of the following items fall short of the program targets laid out in Table 2: (i) MRSF receipts, as recorded in the BPNG foreign exchange cash flow (to a maximum upward adjustment of K 20 million); (ii) exceptional external financing flows to the budget, as recorded in the BPNG foreign exchange cash flow (to a maximum upward adjustment of $70 million); and (iii) total net receipts from asset sales. With respect to the adjuster in (iii), if net receipts from asset sales are negative, the value of net receipts from asset sales shall be set at zero for the purposes of comparison with the benchmark values in Table 2.

3/ Cumulative flow since the beginning of the year.

4/ For adjustments to the ceiling on net domestic financing of the government prior to September 2000 refer to IMF Staff Report EBS/00/53. From September 2000 onward the ceiling on net domestic financing of the government will be adjusted downward by the full amount of the excess of the sum of nontax revenue (excluding grants) and non-MRSF tax revenue, less domestic interest payments over the program levels shown in Table 2.

5/ The floor on net international reserves of the BPNG will be adjusted upward by the full extent to which the value of the following items exceeds the program targets laid out in Table 2: (i) MRSF receipts, as recorded in the BPNG foreign exchange cash flow; (ii) exceptional external financing flows to the budget, as recorded in the BPNG foreign exchange cash flow; and (iii) foreign currency-denominated net receipts from asset sales. Downward adjustment will be made by the amounts that the values of the following items fall short of the program targets laid out in Table 2: (i) MRSF receipts, as recorded in the BPNG foreign exchange cash flow (to a maximum downward adjustment of $7.6 million); (ii) exceptional external financing flows to the budget, as recorded in the BPNG foreign exchange cash flow (to a maximum downward adjustment of $70 million); and (iii) foreign currency-denominated net receipts from asset sales. With respect to the adjuster in (iii), if net receipts from asset sales are negative, the value of net receipts from asset sales shall be set at zero for the purposes of comparison with the benchmark values in Table 2.

6/ Valued at the program exchange rate of US$0.38/kina.

7/ The public sector is defined to include the national and provincial governments and statutory authorities. Excluded from the limits on external borrowing are the use of Fund resources, loans from the World Bank, the Asian Development Bank, and other multilateral and official bilateral donors; loans contracted for debt rescheduling or refinancing (provided the terms of the new loans are at least as concessionary as the terms of the debt being rescheduled or refinanced); and credits that are regarded as concessionary.

8/ This performance criterion applies not only to debt as defined in point No. 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt adopted on August 24, 2000, but also to commitments contracted or guaranteed for which value has not been received. Excluded from this performance criterion are leases.

9/ The term "debt" has the meaning set forth in point No. 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt adopted on August 24, 2000. Excluded from this performance criterion are normal import-related trade credit and leases. Included in this performance criterion are off-balance sheet assets and liabilities (e.g., swaps and forwards).

Table 3. Papua New Guinea: Quantitative Benchmarks Under the Stand-By Arrangement, 2000-01

	Actual			Indicative Targets				
				Original Program			First Review	First Review
	Dec. 31 1999	Mar. 31 2000	Jun. 30 2000	Mar. 31 2000	Jun. 30 2000	Sep. 30 2000	Dec. 31 2000	Mar. 31 2001
	(In millions of kina)							
Ceiling on central government wages and salaries 1/, 2/	777	149	352	144	377	570	814	193
Ceiling on central government recurrent expenditures 1/, 3/, 4/, 5/	2,015	469	1,015	436	1,006	1,515	...	...
Ceiling on central government noninterest recurrent expenditures 1/, 3/, 4/, 6/	1,628	364	790	372	815	1,236	1,705	423
Floor on pre-1999 domestic arrears reduction 1/	149	40	64	37	77	99	109	16
Floor on non-MRSF tax revenue 1/, 7/	1,662	402	935	393	842	1,318	1,931	486
	(In millions of U.S. dollars)							
Floor on Mineral Resource Stabilization Fund receipts 1/, 8/	131	8	54	5	43	74	129	0
Memorandum items:								
Exceptional external financing (in millions of U.S. dollars) 8/, 9/	80	0	35	0	36	81	180	195
Privatization receipts, net of cost of sales (in millions of kina) 1/, 10/, 11/	26	0	0	0	0	0	0	175
Of which: Foreign currency-denominated								
In millions of kina 1/, 10/, 12/	...	...	...	0	0	0	0	117
In millions of U.S. dollars 1/, 10/, 12/	...	...	...	0	0	0	0	45
Nontax revenue 1/	166	26	56	19	92	148	169	27
Domestic interest payments 1/	261	79	159	42	123	175	317	54

Sources: Data provided by the Papua New Guinea authorities; and Fund staff estimates and projections.

1/ Cumulative flow since the beginning of the year.
2/ Defined as sum of national and provincial department expenditures on wages and salaries (including wages and salaries for teachers of provincial governments) but excluding retrenchment allowances, contributions to superannuation funds, and other PEs (leave benefits and overtime).
3/ Gross expenditure (includes estimated K 30.2 million of appropriations for services of the Department of Works to be recovered as nontax revenue from within the government).
4/ The benchmark on total recurrent expenditure in the original program was altered to noninterest recurrent expenditure at the time of the first review.
5/ Includes net lending.
6/ Excludes net lending.
7/ In 1999 excludes VAT revenue collected in trust accounts.
8/ As recorded in the foreign exchange cash flow of the Bank of Papua New Guinea.
9/ Cumulative from January 1, 2000.
10/ Net revenues from the expected privatization of the Halla Cement Company in the fourth quarter of 2000 are projected at zero because receipts will be matched by an equivalent or greater cost of sales.
11/ As reported by the Department of Finance and Treasury.
12/ As reported in the balance of payments cash flow of the Bank of Papua New Guinea.

Table 4. Papua New Guinea: Prior Actions, Structural Perfomance Criteria, and Benchmarks Under the Stand-By Arrangement, 2000-01

	Program Target Date	Status
I. Prior actions for first review		
Endorsement by Cabinet of a plan and timetable for the Public Sector Reform Program (PSRP)		Met.
II. Structural performance criteria		
Completion of financial and managerial audits of the two major pension funds: the Public Officers' Superannuation Fund (POSF) and the National Provident Fund (NPF)	By end-March 2000	Met.
Passage by parliament of the Central Bank Act	By end-April 2000	Met.
Passage by parliament of the Banks and Financial Institutions Act	By end-April 2000	Met.
Completion and submission to Cabinet of the design and timetable for the PSRP	By end-June 2000	Not observed by target date. Waiver requested based on subsequent completion (see above).
Finance Pacific brought to the point of sale	By end-December 2000	Expected to be met.
III. Structural benchmarks		
The self-assessment questionnaire on good fiscal practices will be completed and submitted to the Fund	By end-March 2000	Met.
The Privatization Commission will have identified candidates for privatization and will have formulated a detailed schedule and methodology to be employed	By end-March 2000	Met.
Actuarial reviews of the NPF and POSF will have begun	By end-April 2000	Superseded by future comprehensive industry reform.
Endorsement by Cabinet of the recommendations on the PSRP	By end-August 2000	Met, also a prior action for the first review (see above).
Endorsement by Cabinet of the recommendations of the Public Expenditure Review	By end-August 2000	Replaced by ongoing departmental reviews.
Cabinet approval of the tax system review	By end-September 2000	Not observed. Expected to be met by mid-October 2000.
Ongoing effort to close down remaining pyramid schemes	Continuing	

Table 5. Papua New Guinea: Central Government Budget, 1996-2001

(In millions of kina)

	1996	1997	1998	1999	Original Program 2000	Revised Program 2000	Revised Program 2001
Revenues and grants	1,837.5	2,201.5	2,299.8	2,583.3	2,914.4	2,984.4	3,114.3
Tax	1,526.4	1,674.4	1,595.4	1,940.7	2,124.6	2,270.7	2,394.1
Nonmineral	1,121.0	1,284.4	1,354.8	1,682.0	1,824.6	1,930.7	2,119.1
Mineral	405.4	390.0	240.6	258.7	300.0	340.0	275.0
Nontax	141.0	215.1	234.1	165.5	245.1	169.0	175.0
Of which: Mineral	18.8	60.8	65.8	37.3	21.4	21.4	20.0
Grants	170.1	312.0	470.3	477.1	544.7	544.7	545.2
Budget support grants	164.5	133.0	113.5	125.8	15.6	15.6	23.2
Project grants 1/	5.6	179.0	356.8	351.3	529.1	529.1	522.0
Expenditures and net lending	1,861.0	2,192.4	2,486.5	2,801.2	3,081.2	3,197.2	3,169.0
Recurrent	1,528.8	1,767.9	1,895.4	2,020.2	2,085.1	2,160.9	2,174.4
Salaries and wages	604.2	655.4	690.2	776.9	814.2	814.2	894.8
Goods and services, and transfers 2/	667.3	814.9	869.8	701.9	781.1	781.7	843.4
Pre-1999 arrears, court cases, etc.	...	...	...	148.8	109.0	109.0	62.3
Interest	257.3	297.6	335.4	392.7	380.8	456.0	373.9
Domestic	174.5	206.3	228.0	260.5	233.3	316.8	215.0
Foreign	82.8	91.3	107.4	132.2	147.4	139.2	158.9
Development expenditures and net lending	332.2	424.5	591.1	781.0	996.1	1,036.4	994.6
Development budget 2/	338.6	427.6	595.7	786.1	868.4	878.4	...
Project grants	...	...	...	351.3	529.1	529.1	...
Concessional loans	...	...	...	121.3	93.7	93.7	...
Domestic funds	...	...	...	313.4	245.6	255.6	...
Maintenance budget 3/	...	...	...	...	35.0	35.0	...
Structural adjustment expenditures	...	...	...	...	101.0	101.0	...
Net lending 4/	-6.4	-3.1	-4.6	-5.0	-8.3	22.0	...
Statistical discrepancy 5/	-185.4	-128.6	50.4	-107.6	0.0	19.4	0.0
Overall balance	-208.9	-119.5	-136.3	-325.6	-166.8	-193.4	-54.7
Financing	208.9	119.5	136.3	325.6	166.8	193.4	54.7
External (net)	10.1	-87.5	-94.1	178.2	289.8	327.1	12.1
Borrowing	118.5	85.6	108.1	196.5	93.7	106.9	100.0
Amortization 6/	-125.7	-206.8	-202.2	-233.2	-277.6	-246.6	-245.8
Exceptional financing 7/	17.3	33.7	0.0	214.8	473.7	466.9	157.9
Domestic (net)	138.5	207.0	216.5	121.0	-122.9	-156.1	-157.4
Banking system 8/	110.9	155.3	129.1	56.1	-122.9	-154.9	-155.4
Other	27.7	51.7	87.4	64.9	0.0	-1.2	-2.0
Privatization 9/	60.3	0.0	13.9	26.4	0.0	22.4	200.0
Memorandum items:							
Underlying balance (excluding arrears, and structural adjustment expenditures)	-208.9	-119.5	-136.3	-176.8	43.2	16.6	7.6
Overall balance, excluding grants	-379.0	-431.5	-606.6	-802.7	-711.5	-738.1	-599.9
Nominal GDP (millions of kina)	6,881.2	7,063.8	7,863.4	9,256.1	11,468.5	10,230.0	10,566.0

Sources: Data provided by the Papua New Guinea authorities; and Fund staff projections.

1/ Does not include project grants received from Australia prior to 1997.
2/ Some conditional grants to provinces (District Support Grants, Mining Agreements, and Special Support Grants), which were previously part of recurrent expenditures, are now shown in the development budget.
3/ For roads; previously included in domestically financed development budget.
4/ In 2000 includes settlement of a loan guarantee in conjunction with privatization of Halla Cement Company.
5/ The overall balance is estimated from financing data. Figure for 2000 refers to actual for first half of the year.
6/ Figure for 2000 includes effect of a roll-over of a swap involving official support from Australia into a government loan.
7/ Figure for 2001 includes K 131.6 million financing gap, expected to be filled by concessional loans.
8/ Figure for 1999 differs from monetary records due to an adjustment to reflect the drawdown of collateral deposits at the central bank in conjunction with a commodity price stabilization scheme.
9/ Figure for 2000 refers to gross proceeds from the divestment of the government's stake in Halla Cement Company.

Table 6. Papua New Guinea: Central Government Budget, 1996-2001

(In percent of GDP)

	1996	1997	1998	1999	Original Program 2000	Revised Program 2000	Revised Program 2001
Revenues and grants	26.7	31.2	29.2	27.9	25.4	29.2	29.5
Tax	22.2	23.7	20.3	21.0	18.5	22.2	22.7
Nonmineral	16.3	18.2	17.2	18.2	15.9	18.9	20.1
Mineral	5.9	5.5	3.1	2.8	2.6	3.3	2.6
Nontax	2.0	3.0	3.0	1.8	2.1	1.7	1.7
Of which: Mineral	0.3	0.9	0.8	0.4	0.2	0.2	0.2
Grants	2.5	4.4	6.0	5.2	4.7	5.3	5.2
Budget support grants	2.4	1.9	1.4	1.4	0.1	0.2	0.2
Project grants 1/	0.1	2.5	4.5	3.8	4.6	5.2	4.9
Expenditures and net lending	27.0	31.0	31.6	30.3	26.9	31.3	30.0
Recurrent	22.2	25.0	24.1	21.8	18.2	21.1	20.6
Salaries and wages	8.8	9.3	8.8	8.4	7.1	8.0	8.5
Goods and services, and transfers 2/	9.7	11.5	11.1	7.6	6.8	7.6	8.0
Pre-1999 arrears, court cases, etc.	...	...	...	1.6	1.0	1.1	0.6
Interest	3.7	4.2	4.3	4.2	3.3	4.5	3.5
Domestic	2.5	2.9	2.9	2.8	2.0	3.1	2.0
Foreign	1.2	1.3	1.4	1.4	1.3	1.4	1.5
Development expenditures and net lending	4.8	6.0	7.5	8.4	8.7	10.1	9.4
Development budget 2/	4.9	6.1	7.6	8.5	7.6	8.6	...
Project grants	...	...	...	3.8	4.6	5.2	...
Concessional loans	...	...	...	1.3	0.8	0.9	...
Domestic funds	...	...	...	3.4	2.1	2.5	...
Maintenance budget 3/	...	...	...	...	0.3	0.3	...
Structural adjustment expenditures	...	...	...	...	0.9	1.0	...
Net lending 4/	-0.1	0.0	-0.1	-0.1	-0.1	0.2	...
Statistical discrepancy 5/	-2.7	-1.8	0.6	-1.2	0.0	0.2	0.0
Overall balance	-3.0	-1.7	-1.7	-3.5	-1.5	-1.9	-0.5
Financing	3.0	1.7	1.7	3.5	1.5	1.9	0.5
External (net)	0.1	-1.2	-1.2	1.9	2.5	3.2	0.1
Borrowing	1.7	1.2	1.4	2.1	0.8	1.0	0.9
Amortization 6/	-1.8	-2.9	-2.6	-2.5	-2.4	-2.4	-2.3
Exceptional financing 7/	0.3	0.5	0.0	2.3	4.1	4.6	1.5
Domestic (net)	2.0	2.9	2.8	1.3	-1.1	-1.5	-1.5
Banking system 8/	1.6	2.2	1.6	0.6	-1.1	-1.5	-1.5
Other	0.4	0.7	1.1	0.7	0.0	0.0	0.0
Privatization 9/	0.9	0.0	0.2	0.3	0.0	0.2	1.9
Memorandum items:							
Underlying balance (excluding arrears, and structural adjustment expenditures)	-3.0	-1.7	-1.7	-1.9	0.4	0.2	0.1
Overall balance, excluding grants	-5.5	-6.1	-7.7	-8.7	-6.2	-7.2	-5.7
Nominal GDP (millions of kina)	6,881.2	7,063.8	7,863.4	9,256.1	11,468.5	10,230.0	10,566.0

Sources: Data provided by the Papua New Guinea authorities; and Fund staff projections.

1/ Does not include project grants received from Australia prior to 1997.
2/ Some conditional grants to provinces (District Support Grants, Mining Agreements, and Special Support Grants), which were previously part of recurrent expenditures, are now shown in the development budget.
3/ For roads; previously included in domestically financed development budget.
4/ In 2000 includes settlement of a loan guarantee in conjunction with privatization of Halla Cement Company.
5/ The overall balance is estimated from financing data. Figure for 2000 refers to actual for first half of the year.
6/ Figure for 2000 includes effect of a roll-over of a swap involving official support from Australia into a government loan.
7/ Figure for 2001 includes K 131.6 million financing gap, expected to be filled by concessional loans.
8/ Figure for 1999 differs from monetary records due to an adjustment to reflect the drawdown of collateral deposits at the central bank in conjunction with a commodity price stabilization scheme.
9/ Figure for 2000 refers to gross proceeds from the divestment of the government's stake in Halla Cement Company.

Table 7. Papua New Guinea: Monetary Survey, 1997-2001

	Actual 1/					Original Program					Revised Program					
	1997	1998	1999	2000		2000				2001	2000		2001			
	Dec.	Dec.	Dec.	Mar.	Jun.	Mar.	Jun.	Sep.	Dec.	Dec.	Sep.	Dec.	Mar.	Jun.	Sep.	Dec.
	(In millions of kina)															
Net foreign assets 2/	767	463	676	588	732	515	569	737	981	1,121	854	1,062	1,083	1,090	1,122	1,168
Bank of Papua New Guinea	575	291	489	432	563	342	396	564	808	948	686	893	915	921	954	999
Assets	666	391	551	461	624	433	471	691	998	1,271	803	1,073	1,162	1,236	1,267	1,312
Liabilities	91	100	62	29	61	91	75	127	190	323	117	180	247	315	314	313
Commercial banks	192	171	187	156	168	173	173	173	173	173	168	168	168	168	168	168
Net domestic assets	1,831	2,183	2,204	2,189	2,129	2,286	2,369	2,317	2,155	2,180	2,136	2,069	2,065	2,093	2,084	2,098
Domestic credit	2,320	2,716	2,825	2,669	2,828	2,792	2,859	2,827	2,657	2,669	2,850	2,763	2,754	2,791	2,774	2,793
Net credit to consolidated central government 3/	840	969	1,077	876	986	1,136	1,210	1,178	954	743	995	922	848	864	788	767
Bank of Papua New Guinea	-97	368	498	266	212	576	562	398	182	89	182	60	41	40	14	-20
Claims on government	881	1,285	599	398	338	678	664	500	284	191	307	185	166	165	139	105
Government deposits	978	917	102	133	125	102	102	102	102	102	125	125	125	125	125	125
Commercial banks	937	601	580	611	774	560	648	779	772	654	813	863	806	824	773	787
Credit to other sectors 4/	1,480	1,747	1,747	1,793	1,842	1,656	1,649	1,650	1,703	1,926	1,855	1,840	1,907	1,927	1,987	2,026
Of which: Claims on private sector	1,064	1,372	1,517	1,563	1,596	1,413	1,422	1,437	1,503	1,711	1,624	1,653	1,719	1,739	1,799	1,838
Other items (net)	-489	-533	-620	-480	-699	-506	-490	-511	-502	-489	-714	-693	-689	-698	-690	-695
Broad money	2,598	2,646	2,880	2,778	2,861	2,801	2,939	3,054	3,136	3,302	2,990	3,131	3,149	3,182	3,206	3,266
Narrow money	919	1,021	1,234	1,138	1,115	1,149	1,206	1,253	1,287	1,500	1,171	1,226	1,233	1,246	1,256	1,279
Quasi money	1,679	1,624	1,646	1,640	1,746	1,652	1,733	1,801	1,849	1,801	1,819	1,905	1,915	1,936	1,950	1,987
	(Percentage change) 4/															
Net foreign assets 4/	-9.3	-39.7	46.0	59.8	99.8	39.9	55.4	75.4	47.3	14.3	103.2	57.1	84.1	48.9	31.4	10.0
Bank of Papua New Guinea	-19.7	-49.4	67.8	88.1	296.7	48.9	178.8	145.1	65.3	17.3	198.2	82.8	111.9	63.5	39.1	11.9
Commercial banks	48.1	-10.5	9.0	12.9	-25.0	24.9	-22.8	-8.9	-2.4	0.0	-11.6	-10.0	7.4	0.0	0.0	0.0
Net domestic assets	15.4	19.2	1.0	-6.2	-11.7	-2.0	-1.8	-4.3	-2.7	1.2	-11.8	-6.1	-5.7	-1.7	-2.4	1.4
Domestic credit	22.7	17.1	4.0	-7.9	-2.9	-3.7	-1.8	-5.6	-1.5	0.4	-4.8	-2.2	3.2	-1.3	-2.7	1.1
Net credit to consolidated central government 3/	22.7	15.4	11.2	-30.8	-13.2	-10.2	6.5	-5.5	-11.4	-22.1	-20.2	-14.4	-3.3	-12.4	-20.8	-16.8
Net credit to other sectors 4/	22.7	18.0	0.0	9.8	3.7	1.4	-7.1	-5.7	5.2	13.1	6.1	5.3	6.3	4.6	7.1	10.1
Of which: Claims on private sector	36.3	29.0	10.5	16.6	8.0	5.3	-3.8	-1.8	9.2	13.8	11.1	9.0	10.0	9.0	10.7	11.2
Broad money	6.8	1.8	8.9	2.8	3.0	3.7	5.8	7.5	8.8	5.3	5.2	8.7	13.4	11.2	7.2	4.3
Memorandum items:																
Net international reserves (millions of U.S. dollars)	328	139	181	165	230	130	150	214	307	360	261	339	348	350	362	380
Gross reserves (millions of U.S. dollars)	380	187	204	176	254	165	179	263	379	483	305	408	442	470	482	499
Change in net credit to government (beginning of year)	155	129	108	-201	-91	59	133	101	-123		-82	-155	-75	-59	-135	-155
Exchange rate (US$/kina)	0.571	0.477	0.371	0.382	0.408	0.380	0.380	0.380	0.380	0.380	0.380	0.380	0.380	0.380	0.380	0.380
Velocity of broad money	2.7	3.0	3.2	3.4	3.4	3.8	3.7	3.7	3.7	3.7	3.3	3.3	3.3	3.3	3.3	3.2

Sources: Data provided by the Papua New Guinea authorities; and Fund staff estimates and projections.

1/ Actual values are based on historical exchange rates. For values of NIR and NDA calculated at the program exchange rate refer to Table 2.
2/ Projections for 2000-01 based on the program exchange rate of US$0.38/kina.
3/ Includes net credit to the central government and the commodity stabilization funds.
4/ Includes credit to the private sector, provincial governments, and nonfinancial public enterprises.
5/ Change on corresponding quarter of previous year.

Table 8. Papua New Guinea: Balance Sheet of the Central Bank, 1997-2001

(In millions of kina, unless otherwise indicated)

	Actual 1/					Original Program					Revised Program					
	1997	1998	1999	2000		2000				2001	2000		2001			
	Dec.	Dec.	Dec.	Mar.	Jun.	Mar.	Jun.	Sep.	Dec.	Dec.	Sep.	Dec.	Mar.	Jun.	Sep.	Dec.
Net foreign assets	575	291	489	432	563	342	396	564	808	948	686	893	915	921	954	999
Assets	666	391	551	461	624	433	471	691	998	1271	803	1073	1162	1236	1267	1312
Liabilities	91	100	62	29	61	91	75	127	190	323	117	180	247	315	314	313
Net domestic assets	-254	97	184	89	-62	251	226	83	-144	-249	-122	-267	-285	-287	-312	-346
Domestic credit	120	490	555	323	269	633	619	455	240	146	239	117	99	97	71	38
Net credit to government	-97	368	498	266	212	576	562	398	182	89	182	60	41	40	14	-20
Of which : Claims on government	881	1285	599	398	338	678	664	500	284	191	307	185	166	165	139	105
Credit to other sectors	217	122	57	57	57	57	57	57	57	57	57	57	57	57	57	57
Other items, net	-374	-393	-370	-234	-332	-382	-393	-373	-384	-395	-361	-384	-384	-384	-384	-384
Reserve money	322	388	673	521	501	593	622	646	664	699	564	626	630	634	641	653
Currency in circulation	276	324	421	344	343	371	389	404	415	437	372	414	299	302	304	433
Notes	246	293	387	309	308	337	354	367	377	397	333	372	268	271	273	388
Coins	30	32	34	35	35	34	36	37	38	40	38	43	31	31	31	44
Deposits of commercial banks	26	60	247	173	149	222	233	242	248	257	184	203	322	323	328	212
ESA deposits	26	60	110	37	9	91	96	99	102	106	38	52	169	169	173	54
CRR deposits	0	0	137	136	139	131	137	142	146	151	145	152	152	154	155	158
Other deposits	20	4	5	5	9	4	4	4	4	4	9	9	9	9	9	9
Memorandum items:																
Broad money	2,598	2,646	2,880	2,778	2,861	2,801	2,939	3,054	3,136	3,302	2,990	3,131	3,149	3,182	3,206	3,266
Currency outside banks	225	277	342	266	263	275	288	300	308	324	284	297	299	302	304	310
Deposits	2,373	2,369	2,538	2,511	2,598	2,526	2,650	2,754	2,828	2,978	2,706	2,833	2,850	2,880	2,901	2,955
(As a percent of broad money)	91	90	88	90	91	90	90	90	90	90	91	91	91	91	91	91
Currency/deposits (ratio)	9.5	11.7	13.5	10.6	10.1	10.9	10.9	10.9	10.9	10.9	10.5	10.5	10.5	10.5	10.5	10.5
Broad money multiplier (ratio)	8.1	6.8	4.3	5.3	5.7	4.7	4.7	4.7	4.7	4.7	5.3	5.0	5.0	5.0	5.0	5.0
Net international reserves (millions of U.S. dollars)	328	139	181	165	230	130	150	214	307	360	261	339	348	350	362	380
Gross reserves (millions of U.S. dollars)	380	187	204	176	254	165	179	263	379	483	305	408	442	470	482	499

Sources: Data provided by the Papua New Guinea authorities; and Fund staff estimates and projections.

1/ Actual values are based on historical exchange rates. For values of NIR and NDA calculated at the program exchange rate refer to Table 2.

Table 9. Papua New Guinea: Balance of Payments, 1996-2001

(In millions of U. S. dollars)

	1996	1997	1998	1999	Program 2000	Program 2001
Current account balance	289	-263	23	53	153	-30
Mineral	736	311	564	718	881	664
Nonmineral	-447	-574	-540	-665	-728	-695
Trade balance	813	213	424	494	568	332
Exports (f.o.b.)	2,603	2,186	1,849	2,019	2,278	2,176
Mineral	1,777	1,328	1,239	1,438	1,669	1,488
Nonmineral	827	857	610	581	609	688
Imports (c.i.f.)	-1,791	-1,972	-1,425	-1,525	-1,710	-1,844
Mineral	-496	-573	-287	-308	-406	-465
Nonmineral	-1,294	-1,399	-1,138	-1,218	-1,304	-1,378
Services balance	-690	-673	-629	-615	-590	-559
Mineral (net)	-544	-444	-389	-413	-382	-358
Nonmineral (net)	-146	-229	-240	-202	-208	-201
Unrequited transfers (net)	166	197	228	174	176	196
Official	219	229	215	181	185	207
Private	-53	-32	13	-8	-9	-11
Capital account balance	68	53	-167	-123	-178	11
Medium- and long-term loan disbursements	-196	189	-185	-391	-190	-153
Official (net)	-5	-76	-46	-10	-65	-67
Private capital flows (net)	-191	266	-139	-381	-124	-87
Foreign direct investment (net)	226	23	121	307	108	137
Commercial banks	-12	-10	15	-2	0	0
Other (net)	49	-149	-118	-37	-96	27
Exceptional financing 1/	15	25	0	80	180	10
Errors and omissions	10	-19	-45	32	0	0
Overall balance	382	-204	-189	42	156	-10
Change in net international reserves (-increase)	-382	204	189	-42	-156	-40
Gross official reserves	-318	206	194	-18	-204	-91
IMF (net)	3	0	-4	-23	44	49
Purchases	3	0	0	0	63	50
Repurchases	0	0	-4	-23	-20	-1
Other foreign liabilities	-67	-1	-1	-2	4	2
Financing gap	0	0	0	0	0	50
Memorandum items:						
Current account (in percent of GDP)	5.5	-5.3	0.6	1.5	3.9	-0.8
Mineral	14.1	6.3	14.7	19.8	22.7	16.5
Nonmineral	-8.6	-11.6	-14.1	-18.3	-18.7	-17.3
Net international reserves						
(In millions of U.S. dollars)	532	328	139	181	339	380
Gross official reserves (end-year)						
(In millions of U.S. dollars)	586	380	187	204	408	499
(In months of nonmineral imports)	5.4	3.3	2.0	2.0	3.8	4.3
Debt-service ratio (in percent of goods and nonfactor services exports)	17.7	17.0	22.5	27.6	17.8	16.8
Debt-to-GDP ratio (in percent)	36.3	43.3	51.8	45.3	43.2	39.5

Sources: Data provided by the Papua New Guinea authorities; and Fund staff estimates.

1/ The total in 1999 includes: $29 million loan from AsDB; and $80 million from the Reserve Bank of Australia under a swap agreement. After the IMF approval of SBA, the swap was converted to a longer-term loan.

Table 10. Papua New Guinea: Medium-Term Balance of Payments Outlook, 1998-2005

(In millions of U. S. dollars)

	1998	1999	Program 2000	Program 2001	Projection 2002	2003	2004	2005
Current account balance	23	53	153	-30	-93	-92	-82	-71
Mineral	564	718	881	664	594	577	557	525
Nonmineral	-540	-665	-728	-695	-688	-669	-639	-596
Trade balance	424	494	568	332	252	238	239	240
Exports (f.o.b.)	1,849	2,019	2,278	2,176	2,186	2,252	2,326	2,395
Mineral	1,239	1,438	1,669	1,488	1,435	1,436	1,441	1,437
Nonmineral	610	581	609	688	751	817	885	958
Imports (c.i.f.)	-1,425	-1,525	-1,710	-1,844	-1,934	-2,015	-2,087	-2,155
Mineral	-287	-308	-406	-465	-500	-524	-549	-573
Nonmineral	-1,138	-1,218	-1,304	-1,378	-1,434	-1,491	-1,538	-1,582
Services balance	-629	-615	-590	-559	-529	-513	-505	-503
Mineral (net)	-389	-413	-382	-358	-341	-334	-334	-339
Nonmineral (net)	-240	-202	-208	-201	-187	-179	-171	-164
Unrequited transfers (net)	228	174	176	196	183	184	185	191
Official	215	181	185	207	193	193	194	194
Private	13	-8	-9	-11	-10	-10	-9	-3
Capital account balance	-167	-123	-178	11	136	121	148	136
Medium- and long-term loan disbursements	-185	-391	-190	-153	-112	-122	-117	-112
Official (net)	-46	-10	-65	-67	-45	-55	-51	-43
Private capital flows (net)	-139	-381	-124	-87	-67	-67	-66	-69
Foreign direct investment (net)	121	307	108	137	254	258	290	297
Commercial banks	15	-2	0	0	0	0	0	0
Other (net)	-118	-37	-96	27	-5	-15	-26	-48
Exceptional financing	0	80	180	10	0	0	0	0
Errors and omissions	-45	32	0	0	0	0	0	0
Overall balance	-189	42	156	-10	43	29	66	65
Change in net international reserves (- increase)	189	-42	-156	-40	-43	-29	-66	-65
Gross official reserves	194	-18	-204	-91	-39	-21	-18	-16
IMF (net)	-4	-23	44	49	0	-8	-48	-48
Purchases	0	0	63	50	0	0	0	0
Repurchases	-4	-23	-20	-1	0	-8	-48	-48
Other foreign liabilities	-1	-2	4	2	-4	0	0	0
Financing gap 1/	0	0	0	50	0	0	0	0
Memorandum items:								
Current account (in percent of GDP)	0.6	1.5	3.9	-0.8	-2.2	-2.0	-1.7	-1.4
Mineral	14.7	19.8	22.7	16.5	13.9	12.7	11.6	10.4
Nonmineral	-14.1	-18.3	-18.7	-17.3	-16.1	-14.7	-13.3	-11.8
Net international reserves								
(In millions of U.S. dollars)	139	181	339	380	422	451	516	580
Gross official reserves (end-year)								
(In millions of U.S. dollars)	187	204	408	499	538	559	577	593
(In months of nonmineral imports)	2.0	2.0	3.8	4.3	4.5	4.5	4.5	4.5
Debt-service ratio (in percent of goods and nonfactor services exports)	22.5	27.6	17.8	16.8	14.1	14.0	15.0	14.4
Debt-to-GDP ratio (in percent)	51.8	45.3	43.2	39.5	34.5	29.6	24.5	20.1

Sources: Data provided by the Papua New Guinea authorities; and Fund staff estimates and projections.

1/ The financing gaps shown are expected to be filled by exceptional donor financing.

Table 11. Papua New Guinea: Medium-Term Scenario, 1996-2005

					Revised Program		Projection			
	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
Growth and prices (change in percent)										
Real GDP	7.7	-3.9	-3.8	4.2	3.4	2.7	3.6	3.9	3.7	3.1
CPI (end of period)	5.3	5.3	21.8	13.2	5.0	3.5	3.0	3.0	3.0	3.0
CPI (annual average)	11.6	3.9	13.6	14.9	12.0	4.3	3.3	3.0	3.0	3.0
Central government operations (percent of GDP)										
Total revenue and grants	26.7	31.2	29.2	27.9	29.2	29.5	28.1	27.5	26.9	26.3
Of which : Grants	2.5	4.4	6.0	5.2	5.3	5.2	4.5	4.3	4.0	3.8
Total expenditure	27.0	31.0	31.6	30.3	31.3	30.0	28.0	27.6	26.8	26.4
Overall balance (including discrepancy)	-3.0	-1.7	-1.7	-3.5	-1.9	-0.5	0.1	-0.1	0.1	-0.1
Domestic financing	2.0	2.9	2.8	1.3	-1.5	-1.5	-0.5	0.0	-0.4	0.1
Of which : Banking system	1.6	2.2	1.6	0.6	-1.5	-1.5	-0.5	0.0	-0.4	0.1
Foreign financing, net	0.1	-1.2	-1.2	1.9	3.2	0.1	-0.9	-1.1	-0.9	-0.7
Privatization	0.9	0.0	0.2	0.3	0.2	1.9	1.3	1.2	1.2	0.7
Debt (percent of GDP)	36.3	43.3	51.8	45.6	43.1	39.4	34.1	29.3	24.2	19.8
Debt-service ratio (in percent of exports of goods and NFS)	17.7	17.0	22.5	27.9	17.8	16.9	14.1	14.0	15.0	14.4
Money and credit (annual percent change)										
Net foreign assets	...	-9.3	-39.7	46.0	57.1	10.0	10.8	5.8	14.9	10.6
Net domestic assets	...	15.4	19.2	1.0	-6.1	1.4	5.6	8.5	5.6	8.2
Credit to private sector	...	36.3	29.0	10.5	9.0	10.6	9.5	9.1	8.7	8.1
Broad money	...	6.8	1.8	8.9	8.7	4.3	7.5	7.5	9.0	9.1
Balance of payments (US$ million, unless otherwise indicated)										
Current account	289	-263	23	53	153	-30	-93	-92	-82	-71
Mineral	736	311	564	718	881	664	594	577	557	525
Nonmineral	-447	-574	-540	-665	-728	-695	-688	-669	-639	-596
Exports, f.o.b	2,603	2,186	1,849	2,019	2,278	2,176	2,186	2,252	2,326	2,395
Mineral	1,777	1,328	1,239	1,438	1,669	1,488	1,435	1,436	1,441	1,437
Nonmineral	827	857	610	581	609	688	751	817	885	958
Imports, c.i.f.	-1,791	-1,972	-1,425	-1,525	-1,710	-1,844	-1,934	-2,015	-2,087	-2,155
Mineral	-496	-573	-287	-308	-406	-465	-500	-524	-549	-573
Nonmineral	-1,294	-1,399	-1,138	-1,218	-1,304	-1,378	-1,434	-1,491	-1,538	-1,582
Unrequited transfers (net)	166	197	228	174	176	196	183	184	185	191
Official	219	229	215	181	185	207	193	193	194	194
Private	-53	-32	13	-8	-9	-11	-10	-10	-9	-3
Capital account balance	68	53	-167	-123	-178	11	136	121	148	136
Of which : Medium- and long-term loan disbursements	-196	189	-185	-391	-190	-153	-112	-122	-117	-112
Foreign direct investment (net)	226	23	121	307	108	137	254	258	290	297
Other (net)	49	-149	-118	-37	-96	27	-5	-15	-26	-48
Exceptional financing	15	25	0	80	180	10	0	0	0	0
Errors and omissions	10	-19	-45	32	0	0	0	0	0	0
Overall balance	382	-204	-189	42	156	-10	43	29	66	65
Change in net international reserves (- increase)	-382	204	189	-42	-156	-40	-43	-29	-66	-65
Gross official reserves	-318	206	194	-18	-204	-91	-39	-21	-18	-16
IMF (net)	3	0	-4	-23	44	49	0	-8	-48	-48
Purchases	3	0	0	0	63	50	0	0	0	0
Repurchases	0	0	-4	-23	-20	-1	0	-8	-48	-48
Other foreign liabilities	-67	-1	-1	-2	4	2	-4	0	0	0
Financing gap 1/	0	0	0	0	0	50	0	0	0	0
Net international reserves										
(In millions of U.S. dollars)	532	328	139	181	339	380	422	451	516	580
Gross official reserves (end-year)										
(In millions of U.S. dollars)	586	380	187	204	408	499	538	559	577	593
(In months of nonmineral imports)	5.4	3.3	2.0	2.0	3.8	4.3	4.5	4.5	4.5	4.5
Exchange rate (US$/kina, end of period)	0.743	0.571	0.477	0.371	...	...	...	...	...	...
Interest rate (182-day T-bills)	9.2	14.5	23.9	20.4	...	...	...	...	...	...
Nominal GDP (millions of kina)	6,881	7,064	7,863	9,256	10,230	10,566	11,356	12,137	12,945	13,732

Sources: Data provided by the Papua New Guinea authorities; and Fund staff estimates and projections.

1/ The financing gaps shown are expected to be filled by exceptional donor financing.

Table 12. Papua New Guinea: Proposed Schedule of Purchases Under the Stand-By Arrangement

Amount	Availability Date	Conditions Necessary for a Purchase
SDR 10.00 million	March 30, 2000	Board approval of the arrangement.
SDR 18.885 million	August 15, 2000	Observance of end-June PC, and ***completion of the First Review***.
SDR 18.885 million	November 15, 2000	Observance of end-September PC, and ***completion of the Second Review***.
SDR 18.885 million	February 15, 2001	Observance of end-December PC, and ***completion of the Third Review***.
SDR 18.885 million	May 15, 2001	Observance of end-March PC, and ***completion of the Fourth Review***.
Memorandum item:		
Total access	SDR 85.54 million (65 percent of quota; 55.7 annualized access)	

Table 13. Papua New Guinea: Indicators of Capacity to Repay the Fund

	1999	2000	2001	2002	2003	2004	2005
Outstanding UFR	21.4	64.6	113.0	113.7	106.2	58.8	10.8
Obligations to the IMF	24.9	21.4	6.6	6.1	14.3	53.1	53.4
Repurchases and repayments	22.8	19.5	1.3	0.0	8.2	48.0	48.3
Charges and interest	2.1	1.9	5.3	6.1	6.2	5.1	5.1
Outstanding UFR in percent of:							
GDP	0.6	1.7	2.8	2.7	2.3	1.2	0.2
Exports of goods and nonfactor services	0.9	2.5	4.5	4.6	4.1	2.2	0.4
External debt	1.3	3.8	7.1	7.7	7.9	5.0	1.1
Net official international reserves	11.8	19.0	29.8	26.9	23.6	11.4	1.9
Quota	11.9	37.0	64.9	64.9	60.3	33.2	6.1
Obligations to the IMF in percent of:							
GDP	0.7	0.5	0.2	0.1	0.3	1.1	1.1
Exports of goods and nonfactor services	1.1	0.8	0.3	0.2	0.6	2.0	2.0
Total debt service	4.0	4.7	1.6	1.7	4.0	13.4	13.6
Net official international reserves	13.7	6.3	1.7	1.4	3.2	10.3	9.2
Memorandum items:							
Total debt service (in percent of exports of goods and nonfactor services)	27.6	17.8	16.8	14.1	14.0	15.0	14.4

Sources: Data provided by the Papua New Guinea authorities; and Fund staff estimates.

PAPUA NEW GUINEA: FUND RELATIONS
(As of August 31, 2000)

I. **Membership Status**: Joined October 9, 1975; Article VIII

II.	**General Resources Account**:	**SDR Million**	**Percent Quota**
	Quota	131.60	100.0
	Fund holdings of currency	145.36	110.5
	Reserve position in Fund	0.11	0.0

III.	**SDR Department**:	**SDR Million**	**Percent Allocation**
	Net cumulative allocation	9.30	100.0
	Holdings	9.61	103.4

IV.	**Outstanding Purchases and Loans**:	**SDR Million**	**Percent Quota**
	Stand-By Arrangement	13.86	10.5

V. **Financial Arrangements**:

Type	**Approval Date**	**Expiration Date**	**Amount Approved (SDR Million)**	**Amount Drawn (SDR Million)**
Stand-by	3/29/00	5/28/01	85.54	10.00
Stand-by	7/14/95	12/15/97	71.48	35.34
Stand-by	7/31/91	9/30/92	26.36	0.00
Stand-by	4/25/90	6/24/91	26.36	0.00

VI. **Projected Obligations to Fund** (SDR million; based on existing use of resources and present holdings of SDRs):

	Overdue	**Forthcoming**				
	8/31/00	**2000**	**2001**	**2002**	**2003**	**2004**
Principal	0.0	2.9	1.0	0.0	2.5	5.0
Charges/interest	0.0	0.2	0.6	0.6	0.5	0.3
Total	0.0	3.1	1.6	0.6	3.0	5.3

VII. **Exchange Rate Arrangement**:

The kina was pegged to a basket of currencies of Papua New Guinea's major trading partners from December 1976 through October 1994. Kina trading was suspended on October 4, 1994, and the currency was floated as of October 10, 1994. Since August 14, 1995, the value of the kina has been determined through a screen-based foreign exchange market; this replaced the auction system initially introduced when the kina was floated. Exchange restrictions against Iraq were imposed in August 1990 and continue to be maintained in accordance with UN Security Council Resolution 661.

VIII. Article IV Consultation and the Stand-By Arrangement:

Papua New Guinea is on the standard 12-month consultation cycle. The last Article IV consultation discussions were held during January 14–25, 1999, and the consultation was concluded on June 8, 1999 (SM/99/86 and SM/99/119).

A 14-month Stand-By Arrangement was approved by the Executive Board on March 29, 2000.

IX. Technical Assistance:

FAD: A mission visited Port Moresby in September/October 1995 to provide advice on the introduction of a broad-based consumption tax. A joint FAD/PFTAC mission in March 2000 assisted the authorities in filling out the self-assessment questionnaire on good fiscal practices.

LEG: A mission visited Port Moresby in November 1996 to provide advice on the legal framework for the National Value-Added Tax (NVAT).

MAE: A mission visited Port Moresby in September 1995 to provide assistance in developing monetary instruments and primary and secondary markets. Missions in November 1997, June 1998, and January 1999 provided advice on banking supervision. Ongoing technical assistance is being provided for the current financial sector restructuring. In November 1999, an MAE mission reviewed technical assistance requirements.

PFTAC: A mission in May 1996 provided advice on fiscal reporting of provincial governments. In July 1996, a mission visited Port Moresby to provide assistance in upgrading bank supervision. A mission in January 1997 provided advice on implementation of the NVAT. A mission in March 1998 (in conjunction with the Asian Development Bank and AusAID) discussed financial management. A mission in November 30–December 11, 1998 provided assistance in the areas of national accounts and balance of payments statistics. A mission on March 13–24 reviewed statistical operations in the context of the GDDS. A mission in July 24–28, 2000 identified priorities for improvement of the National Statistical Office.

STA: Four missions visited Port Moresby over the period August 1995 to April 1996 to provide advice on the compilation of national accounts.

X. Resident Representative:

A new post was opened in Papua New Guinea in 2000 and is currently filled by Mr. M. Tareen.

Papua New Guinea: Relations with the World Bank Group
(As of June 30, 2000)

To date the World Bank has provided 30 IBRD loans and 13 IDA development credits amounting to $622 million and $115 million, respectively, for a total of 43 projects. This includes a second Structural Adjustment Loan which was approved in 1995, the second tranche of which was released in January 1997. A $90 million Structural Adjustment Loan was approved in June 2000, of which $35 million has been disbursed.

The Bank's assistance strategy comprises four elements: (a) to help government with analytical support to develop a coherent set of macroeconomic and structural reforms; (b) to provide a judicious combination of balance of payments support, project, and technical assistance to assist the reforms and build institutional capacity to sustain them; (c) to coordinate donor assistance to Papua New Guinea through Consultative Group Meetings, as well as through bilateral arrangements with Australia, Japan, the Asian Development Bank, and other donors; and (d) to work closely with NGOs and other civic organizations to improve service delivery, effective resource management, and broad-based ownership of reforms in the context of Fund/World Bank programs.

Thus far, there has been only one IFC investment in Papua New Guinea: a $0.3 million investment in a small-scale fishing operation. IFC continues to look for private sector initiatives and, through the South Pacific Facility, is assisting in the development of project proposals and in the mobilization of funding. Papua New Guinea signed the MIGA Convention in 1990. As of December 31, 1999, MIGA had issued two guarantees, for a total amount of $75 million, in the mining sector.

Papua New Guinea: IBRD/IDA Lending Operations

(In millions of U.S. dollars)

Fiscal year ending June 30	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000 1/
Loan approvals	67	51	27	42	11	0	50	0	5	0	132
Loan disbursements	39	60	49	12	23	23	39	42	21	11	40
Balance undisbursed (end of period)	160	151	127	154	130	106	117	70	54	43	135

Source: Data provided by the World Bank.

1/ As of June 30, 2000.

Papua New Guinea: Relations with the Asian Development Bank[1]
(As of August 31, 2000)

Through August 31, the Asian Development (AsDB) had approved 50 loans totaling $729 million for 41 projects. Of this total, 22 loans ($373 million) had been extended from ordinary capital resources and 28 loans ($356 million) from special funds resources. In addition, $32.2 million had been provided for 107 technical assistance projects.

With the overarching objective of alleviating poverty, the AsDB strategy for Papua New Guinea focuses on improved governance, private sector development, and improved social indicators. Poor governance and ineffective public sector management being the main development problems, AsDB is focusing on strengthening public sector financial management and enhancing public sector management. For private sector development, in addition to improving the supportive performance of the central agencies, AsDB will help improve sector policy and institutional frameworks (especially in agriculture and fisheries), enhance factor productivity (skills development and financial services), and improve market access by selected infrastructure investments (transport) especially in rural areas. In the social sectors, AsDB will continue to take a leading role in policy development in health and rural water supply and to assist infrastructure investments and service delivery, especially in rural areas.

In 2000, current plans now call for loans totaling about $45 million for three projects, including support for microfinance and employment, maritime navigation aids, and provincial towns' water supply and sanitation. In addition, preparations for assistance for public sector reforms are under way; it is expected that approvals will be forthcoming early in 2001. Current plans envisage annual lending of about $60 million during 2001–03 (with support for public sector reform boosting the total in 2001). The current 2000 program for grant-financed technical assistance comprises nine projects totaling about $3.4 million.

Table 1. Papua New Guinea: Loan Approvals and Disbursements, 1993–99

(In millions of U.S. dollars)

	1993	1994	1995	1996	1997	1998	1999
Loan approvals	25.6	0.5	0.0	0.0	60.0	14.1	109.0
Loan disbursements	28.3	29.9	17.6	11.9	24.3	24.0	35.1

Source: Data provided by the AsDB.

[1]Prepared by Asian Development Bank staff.

Papua New Guinea: Social and Demographic Indicators 1/

Area	452,860 square kilometers
Population	4.6 million
Rate of growth	2.2 percent per annum
Density	10.2 persons per square kilometer
Population characteristics	
Life expectancy at birth	58 years
Infant mortality	59 per thousand
Fertility rate	4.2 births per woman
School enrollment ratios 2/	
Primary	
Total	80 percent
Female	74 percent
Secondary	
Total	14 percent
Female	11 percent
Health	
Population per physician 3/	14,271
Population per hospital bed 4/	260
Access to safe water 5/	
Total population	33 percent
Urban population	94 percent
Rural population	20 percent

Source: World Bank, World Development Indicators, 1999.

1/ Figures are for 1998 unless otherwise stated.
2/ Figures are for 1995.
3/ Figure is for 1990.
4/ Figure is for 1998.
5/ Figure is for 1991.

PAPUA NEW GUINEA: STATISTICAL ISSUES

Monetary data are normally of reasonably good quality and, with some exceptions, available on a timely basis, but national accounts, price statistics, government finance, and balance of payments data are seriously deficient. The compilation of the balance of payments and national accounts statistics has recently been reviewed by the Pacific Financial Technical Assistance Centre (PFTAC), which found a number of problems in both areas. Existing legislation limits data collection authority to the National Statistical Office (NSO) except for data collected by the Bank of Papua New Guinea (BPNG) through records of the commercial banks. However, NSO lacks both the capacity and willingness to exercise its function. Currently, the NSO is concentrating on conducting the 2000 Census, for which it has recently received technical assistance from the United Nations Population Fund. The only surveys conducted on a regular basis are the consumer price and migration surveys, published quarterly.

National accounts: In mid-2000, the NSO released a set of national income accounts: *National Income, Expenditure and Product, 1993-98*. These are compiled on a consistent basis with their previous published series (using the 1968 United Nations System of National Accounts). The NSO estimates of GDP and its components are compiled on the basis of a "production approach," but in addition an expenditure and income breakdown are also provided for the first time. In the expenditure breakdown, private consumption is the residual category.

The authorities acknowledge deficiencies with the official national economic statistics, but note that the NSO has access to all the information used by the Department of Finance and Treasury and BPNG in their forecasts, plus other sources and more detail. Thus the authorities were confident that the NSO GDP series was more reliable than their own estimates, which were used for macroeconomic analysis.

Prices: The only price data produced is a quarterly consumer price index (CPI); the main deficiencies include outdated weights which are based on consumption studies from the mid-1970s and the weakness of data collection.

Government finance: While central government tax revenue statistics are generally accurate and timely, nontax revenue and public expenditure data are deficient. In particular, development budget expenditures and the utilization of grants and project loans are only recorded with large lags, and few records on the use of accrual trust accounts are available. The weaknesses in fiscal statistics lead to large discrepancies between observed domestic financing from monetary and debt data and the domestic financing requirement derived from fiscal data. Recently, however, the government has taken significant steps to improve government statistics. The timeliness of data after the end of the fiscal year and of current data throughout the year has much improved. Trust accounts are to be internally audited and if possible reconciled. With the recent decision to pay market interest rates to all holders of government securities including the central bank, interest payment records should become fairly accurate. No data are available on deferred pension liabilities to civil servants, and on provincial and local level government budgets, off-budget outlays and corresponding liabilities, and potentially large implicit transfers between the government and public enterprises.

The latest published data in the *GFS Yearbook* are for 1994, and in *International Financial Statistics* for December quarter 1997, but data for the years 1994 to 1999 have been provided in July by the NSO.

External sector: Aggregate data on the balance of payments are published by the BPNG on a quarterly basis. Balance of payments data are based on the exchange record system which is not tightly monitored despite BPNG reporting requirements. The financial account data are of poor quality because of major deficiencies in data collection, especially in the areas of private external debt. In many cases, donors and lenders disburse funds directly to contractors for the purchase of goods and services, effectively bypassing the exchange record system. Therefore, a substantial proportion of current account and capital flows are not recorded. The authorities are attempting to address the problem with the coverage of the merchandise trade statistics by moving to customs-based data. However, it is expected to be some time before the customs-based system will be fully operational.

Papua New Guinea: Core Statistical Indicators
(as of September 14, 2000)

	Exchange Rate	Interna-tional Reserves	Central Bank Balance Sheet	Reserve/ Base Money	Broad Money	Interest Rates	Consumer Price Index	Exports/ Imports	Current Account Balance	Overall Govern-ment Balance	GDP/GNP	External Debt/Debt Service
Date of latest observation	09/06/00	08/31/00	07/31/00	07/31/00	07/31/00	09/06/00	2000 Q2	2000 Q1	2000 Q1	08/30/00	1999	2000 Q1
Date received	09/14/00	09/14/00	08/28/00	8/28/00	08/28/00	09/14/00	09/07/00	07/28/00	07/28/00	09/14/00	07/31/00	07/28/00
Frequency of data 1/	D	W	M	M	M	W	Q	Q	Q	M	A	Q
Frequency of reporting1/	D	W	M	M	M	W	Q	Q	Q	M	A	Q
Source of data 2/	A	A	A	A	A	A	A	A	A	A	A	A
Mode of reporting 3/	C	C	C	C	C	C	C	M	M	O	V	M
Confidentiality 4/	C	D	D	D	D	C	D	C	C	C	C	C
Frequency of publication 1/	W	W	Q	Q	Q	Q	Q	Q	Q	M	A	Q

1/ D-daily; W-weekly; M-monthly; Q-quarterly; A-annually.
2/ A-direct reporting by Bank of Papua New Guinea and/or Department for Treasury and Planning.
3/ C-fax; M-mail; O-Internet; V-obtained during mission and/or Annual Meetings.
4/ C-for unrestricted use; D-embargoed for a specified period and thereafter for unrestricted use.

Papua New Guinea: Review of Fund-Provided Technical Assistance

This annex presents an assessment of Fund-provided technical assistance to Papua New Guinea.

Fiscal Affairs Department

Past experience. In 1993, a mission advised on reforming the tax system for mining and petroleum products. In 1995, a mission provided advice on the introduction of a VAT, reviewed other aspects of the tax system, and recommended reforms in the area of capital gains taxation, tax incentives and exemptions, and import and excise duties. In March 2000, a joint FAD-Pacific Financial Technical Assistance Centre (PFTAC) mission provided technical assistance for a self-assessment of fiscal transparency and prepared a fiscal Report on Observance of Standards and Codes (ROSC) module.

Assessment. The implementation record for the technical assistance provided in the 1990s is mixed. A tax reform commission was established in September 1999, which wanted to use some of the 1993 recommendations on mining taxation. However, no recommendations have as yet been published. Three years following the second technical assistance mission, a VAT was introduced and is expected to yield about 3 percent of GDP in 2000.

Future needs. Papua New Guinea receives most of its fiscal technical assistance from Australia, the World Bank, and the Asian Development Bank. Fund involvement is limited, but the authorities have requested technical assistance to support data reconciliation between fiscal and monetary data and to follow up on the ROSC.

Recent FAD technical assistance reports:

- *Papua New Guinea: Natural Resource Taxation*, by E. M. Sunley and others, January 1993.

- *Papua New Guinea: Introduction of a National Value-Added Tax*, by T. Muzondo, R. Fulford, and P. Serra, January 1996.

Monetary and Exchange Affairs Department

Past experience. MAE involvement in Papua New Guinea has been quite extensive:

- Missions by an MAE-sponsored expert on seven occasions,[1] over the course of three fiscal years, provided advice on the structure, procedures, and staffing for the bank

[1]November 1997, May–June 1998, January, October–November, and December 1999, and January–February and March 2000.

supervision function of the Bank of Papua New Guinea (BPNG); and on the reform of a major state-owned bank.

- The same expert provided major inputs for the revision of the Central Bank Act, and the rewriting of the law governing banking services (the Banks and Financial Institutions Act). His contributions included a framework paper which provided the point of departure for the legal drafting of the banking law, and detailed comments and recommendations to the legal draftsmen on drafts of both pieces of legislation at each stage of their preparation. Comments on the draft legislation were also provided by MAE staff at headquarters.

- In November 1999, an MAE staff expert assessed the technical assistance needs of the BPNG in the areas of monetary policy formulation and implementation, bank supervision and regulation, and financial legislation and financial sector reform.

Assessment. Utilization of technical assistance from MAE has generally been quite good.

- Following each banking supervision mission, an aide memoire with specific recommendations was left with the Governor of the Bank. However, to date, implementation of these recommendations was slow, because of difficulties experienced in recruiting staff with the required skills.

- The revised Central Bank Act, which establishes institutional autonomy and accountability, and the Banks and Financial Institutions Act were passed by parliament in April 2000.

- Following the overview mission in November 1999, much of the technical assistance needs identified in the mission's report were met by the Reserve Bank of Australia.

Future needs. The report of the November 1999 mission envisaged:

- Continuing MAE assistance in the areas of legislation and bank supervision through expert visits. One expert visit took place in May–June 2000, two more are planned for October 2000.

- Providing assistance with the legislative framework for nonbank financial institutions. This would take place once work on the regulations associated with the central bank and banking legislation is complete. MAE technical assistance will be coordinated with assistance from the World Bank, which has assumed oversight of financial sector reform (including privatization of state-owned financial institutions), and with the advisors from the Reserve Bank of Australia.

- Continued assistance with reform of the state-owned bank and its preparations for privatization (scheduled as a performance criterion under the Stand-By Arrangement for end-2000).

- Providing assistance in the formulation of legislation governing the regulation of the superannuation and insurance industries.

Recent MAE reports:

- *Papua New Guinea: Staff Visit—Technical Assistance for the Financial Sector,* by D. Worrell, February 2000.

Legal Department

Past experience. LEG has not provided any technical assistance to Papua New Guinea over the past 2–3 years.

Future needs. Papua New Guinea may benefit from a LEG diagnostic mission that would identify weaknesses in the legal framework that could be addressed by technical assistance from the Fund and other agencies.

Statistics Department

Past experience. A series of four STA missions provided technical assistance to the National Statistical Office (NSO) over the period August 1995 to April 1996. The main area of concern was national accounts compilation (including the censuses and surveys that are the main sources for the national accounts); and some assistance in the formulation of the consumer price index.

Assessment. Utilization of technical assistance from STA has been poor. As a result of the lack of implementation of the missions' recommendations, no further assistance was provided by the Real Sector Division of STA after 1996. However, advisors from the PFTAC have made subsequent visits to NSO since then to undertake overviews and assessments.

Future needs.

- Priority should be given to improving the quality and timeliness of the consumer price index; and to the development of a monthly rather than quarterly series.

- The deterioration in the NSO performance and low effectiveness of technical assistance across the range of statistics during the 1990s appear to indicate severe institutional weaknesses. Consequently, if the preconditions for the success of future technical assistance are to be established, a clear need exists to strengthen the technical and managerial capacity of the NSO. However, care must be taken in the design of this assistance to avoid the problems of overly ambitious objectives that have characterized some previous assistance projects.

- STA believes that the statistical needs of Papua New Guinea would best be met through a coordinated approach that would design assistance in a way that avoids duplication among donors (Australia, New Zealand, the Asian Development Bank, and the United Nations are potential sources of assistance). PFTAC is taking the initiative with the NSO to develop a framework for institution-building, as well as a range of statistical tasks including improvement of timeliness, quarterly indicators, greater use of administrative data, core inflation measures, and household expenditure surveys; and setting up a council for consultation with data users and suppliers. The Fund may play a role in this through a series of short-term missions. However, in view of the institutional nature of the problems, long-term assistance is likely to be more effective.

Recent STA technical assistance reports:

- *Papua New Guinea: National Accounts Statistics* (08/09/96).

Statement by the IMF Staff Representative on Papua New Guinea
October 13, 2000

The staff supports the authorities' request for a waiver of applicability of end-September 2000 quantitative performance criteria. Data to assess observance of end-September performance criteria are not yet available. However, staff believes that the program is on track, and data for end-August and partial data for September indicate that all quantitative performance criteria are likely to have been observed.

The Fiscal Transparency Module for the Report on the Observance of Standards and Codes was issued to the Board on October 11. As noted already by Mr. Taylor, the authorities of PNG are broadly in agreement with the recommendations of the report, which focused mainly on improving fiscal management by enhancing budget preparation, execution and reporting, and strengthening watchdog agencies.

Even before the preparation of the ROSC, the government in power since August 1999 initiated important steps to strengthen expenditure control, clear arrears, and improve information management. The budget preparation process for the 2001 budget is being conducted in a transparent and consultative manner. The scope of the government sector will be reduced in the course of the privatization process. The broad public sector reform program will improve fiscal management in many ways: reporting systems are to be strengthened, the accountability and the professionalism of the civil service enhanced, and the policy planning and decision-making process improved. Measures to strengthen watchdog agencies are an important component of the World Bank SAL program. An FAD TA mission scheduled for December will assist with the reconciliation of monetary and fiscal data, and assess options to enhance the coverage of fiscal statistics.

INTERNATIONAL MONETARY FUND
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EXTERNAL RELATIONS DEPARTMENT

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International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Papua New Guinea and the First Review Under the Stand-By Arrangement

On October 13, 2000, the Executive Board concluded the Article IV Consultation and the First Review under the Stand-By Arrangement with Papua New Guinea (See News Brief 00/94, October 13, 2000).[1]

Background

In the late 1990s Papua New Guinea was adversely affected by a large terms-of-trade shock, a severe drought, a relaxation of macroeconomic policies, and widespread governance problems. Depressed export earnings resulted in low tax revenue, which contributed to weak government finances in 1998 and 1999. As confidence deteriorated, private capital outflows intensified, and gross official international reserves fell sharply. Despite intervention by the central bank, the kina lost nearly one-third of its value against the U.S. dollar between end-1997 and mid-1999, pushing inflation up from under 5 percent to around 20 percent.

At the conclusion of the last Article IV consultation in June 1999, Executive Directors expressed concern about the economic situation and outlook. Directors recommended sustained implementation of tight monetary and fiscal policies, including the reining-in of domestic credit to government. They also strongly encouraged the authorities to improve transparency and accountability in the public sector, develop a concrete action plan for privatization, and improve the quality of macroeconomic statistics.

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. In this PIN, the main features of the Board's discussion are described.

With an economic crisis looming, parliament formed a new government in July 1999 with a mandate to undertake fundamental reforms. The new government initiated policy discussions with the IMF and World Bank, quickly implemented a supplementary budget that included significant revenue measures, and pledged to undertake reforms to improve the governance, transparency, and efficiency of the public sector.

In March 2000 the Executive Board approved a 14-month Stand-By Arrangement in the amount of SDR 85.5 million (65 percent of quota). The program aims at macroeconomic stabilization and laying the basis for sustained growth over the medium term. It targets a reduction in inflation to 5 percent by the end of the year, and an increase in gross international reserves to $408 million (3.8 months of import cover). This is to be achieved through a tightening of monetary policy and a reduction in the overall government deficit. Structural policies are focused on public sector reforms; enhancing the independence and accountability of the central bank and strengthening the supervision of the financial system; and promoting private sector development through privatization and tax reform. The program is also supported by a $90 million World Bank Governance Promotion Structural Adjustment Loan approved in June 2000, and sizable financial packages from Australia, Japan, and other donors. Performance under the Stand-By Arrangement has been satisfactory, and all quantitative performance criteria for end-June 2000 were met.

Macroeconomic performance and market sentiment improved following approval of the arrangement in March. The overall government balance recorded a small surplus during the first half of the year. This was the result mainly of buoyant tax revenue, reflecting strong mineral export prices and better collection efforts. Renewed confidence in the economy prompted exporters to accelerate the repatriation of export receipts in the second quarter of 2000, triggering an appreciation of the kina and foreign exchange purchases by the central bank. Subsequently, the central bank sold foreign currency in the face of some downward exchange rate pressure resulting from expectations for lower coffee exports. In all, net international reserves increased from $180 million at end-1999 to $260 million at end-August 2000, and the kina appreciated from a low of $0.32 in late February to $0.42 in early June, and has since settled at around $0.37. The quarter-on-quarter inflation rate rose from 2.6 percent at end-March to 4.4 percent at end-June, due in part to recent tax increases.

Executive Board Assessment

Executive Directors agreed with the thrust of the staff appraisal. They commended the authorities' achievement in launching a comprehensive and ambitious program of macroeconomic stabilization and structural reform. Directors emphasized that continued determined implementation of the program will be needed to create the conditions for economic diversification and sustained private-sector-led growth, which would help to increase the economy's resilience to external shocks and, more generally, to ensure that the authorities' efforts bring a lasting break from the disappointing performance of earlier years. Directors expressed confidence that the authorities would move decisively in facing up to these challenges.

Directors welcomed the improved fiscal performance during 2000, which has resulted in an overall surplus in the first half of the year. Higher oil prices and tax measures have raised revenues, and expenditure control has improved. Looking forward, Directors supported the authorities' policy of consolidation in order to contain the government debt, and ensure fiscal sustainability. They noted that petroleum output, and thus revenues from that sector, are expected to decline, and that the public sector needs to be prepared to play a key role over time in promoting rural development and in poverty reduction. Directors considered that the required consolidation would have to rely heavily on further efforts to raise and diversify budget revenue over the medium term, including through improved administration.

Directors welcomed the authorities' plan for the 2001 budget, now under preparation, to be in broad overall balance. They emphasized the importance of limiting the increase in the wage bill—including through continuation of the temporary hiring freeze—and of proceeding as rapidly as possible in implementing public sector reforms aimed at rationalizing the civil service. They also emphasized the importance of further improving expenditure controls to prevent unbudgeted commitments by certain agencies, which in the past has led to arrears, and of preparing contingency measures to ensure the attainment of budget targets.

Directors noted that the authorities had succeeded in mopping up the large overhang of liquidity that had accumulated in late 1999. They also noted, however, that inflation in the first half of 2000 was still relatively high. This partly reflected temporary influences, which would likely abate, notably the depreciation of the kina and recent excise tax increases. Directors considered that achieving the targeted reduction in inflation by end-2000 would require the maintenance of a tight monetary policy. In this connection, they noted that the recent decline in nominal interest rates was partly a sign of improved confidence, and welcomed the authorities' intention to avoid any further reduction in interest rates until inflation was on a clearly declining trend. In this context, they also considered that particularly close attention to price developments and their measurement would be warranted.

Directors considered Papua New Guinea's flexible exchange rate policy appropriate for a commodity export-based economy susceptible to price and output shocks. They welcomed the passage of the revised Central Bank Act and the Banks and Financial Institutions Act, which has improved the framework for monetary policy and for supervision of financial institutions.

Directors commended the authorities' for the progress in implementing structural reforms to improve the governance, transparency, and efficiency of the public sector, as indicated by the recent assessment of Papua New Guinea's observance of the code on fiscal transparency (ROSC). The introduction earlier this year of new procedures and institutional structures for rural development spending was seen as a signal of the authorities' determination to tackle difficult issues. Directors welcomed the preparations underway to bring the conglomerate, Finance Pacific, to the point of sale by end-2000 and urged the authorities to proceed with their privatization program without delay, but on the basis of a careful consideration of the options. Directors welcomed the openness of Papua New Guinea's trade regime, but noted the need for some caution regarding the establishment of free trade zones.

Directors noted that audits conducted earlier this year had revealed serious financial and monetary problems at the National Provident Fund, which needed to be urgently and comprehensively addressed with careful attention to the social and all other aspects of the issues. While recognizing the important steps that the authorities had already taken, Directors stressed the importance of implementing the recently designed Public Sector Reform Program as rapidly as possible to meet the overall goal of improving the efficiency of the public sector.

Directors appreciated the authorities' efforts to improve the quality of economic and financial statistics, but considered that improvements are still needed, including in the compilation of more timely price statistics that could provide a better guide for monthly policy action, and in reconciling monetary and fiscal data. Directors indicated that strengthening the technical and managerial capacity of the National Statistical Office should be given high priority, and noted the potential role of technical assistance in improving statistics.

It is expected that the next Article IV consultation with Papua New Guinea will be held on the standard 12-month cycle.

Public Information Notices (PINs) are issued, (i) at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies; and (ii) following policy discussions in the Executive Board at the decision of the Board. As part of a pilot project, the staff report for the 2000 Article IV consultation with Papua New Guinea is also available.

Papua New Guinea: Selected Economic and Financial Indicators

	1996	1997	1998	1999	2000	2001
Real sector (percent change)						
Real GDP growth	7.7	-3.9	-3.8	4.2	3.4	2.7
Mineral	0.3	-26.0	16.8	12.3	1.5	-4.7
Nonmineral	10.1	2.5	-8.1	2.1	4.0	4.8
CPI (annual average)	11.6	3.9	13.6	14.9	12.0	4.3
CPI (12 months)	5.3	5.3	21.8	13.2	5.0	3.5
Terms of trade (percent change)	...	-4.2	-8.8	-1.9	8.9	-3.6
Central government budget (percent of GDP)						
Revenue and grants	26.7	31.2	29.2	27.9	29.2	29.5
Expenditure and net lending	27.0	31.0	31.6	30.3	31.3	30.0
Overall balance, cash basis (including grants) 1/, 2/	-3.0	-1.7	-1.7	-3.5	-1.9	-0.5
Domestic financing	2.0	2.9	2.8	1.3	-1.5	-1.5
Foreign financing, net	0.1	-1.2	-1.2	1.9	3.2	0.1
Money and credit (year-on-year percentage change)						
Domestic credit	5.8	22.7	17.1	4.0	-2.2	1.1
Net credit to government	19.2	22.7	15.4	11.2	-14.4	-16.8
Credit to the private sector	-7.8	36.3	29.0	10.5	9.0	11.2
Broad money	31.3	6.8	1.8	8.9	8.7	7.2
Balance of payments (US$ million)						
Exports, f.o.b.	2,603	2,186	1,849	2,019	2,278	2,176
Imports, c.i.f.	-1,791	-1,972	-1,425	-1,525	-1,710	-1,844
Current account (including grants)	289	-263	23	53	153	-30
(In percent of GDP)	5.5	-5.3	0.6	1.5	3.9	-0.8
Overall balance	382	-204	-189	42	156	-10
Reserves and external debt (end-of-year, US$ million)						
Gross official reserves	586	380	187	204	408	499
(In months of nonmining imports, c.i.f.)	5.4	3.3	2.0	2.0	3.8	4.3
External amortization/gross international reserves (in percent)	69.2	84.0	195.4	240.9	73.7	54.0
Net international reserves	532	328	139	181	339	380
(In months of nonmining imports, c.i.f.)	4.9	2.8	1.5	1.8	3.1	3.3
Medium- and long-term external debt (percent of GDP)	36.3	43.3	51.8	45.3	43.2	39.5
Debt-service ratio (percent of external current receipts)	17.7	17.0	22.5	27.6	17.8	16.8
Exchange rates						
US$ per kina (end-period) 3/	0.74	0.57	0.48	0.37	0.38	...
Interest rate (182-day T-bills) 3/	9.2	14.5	23.9	20.4	14.3	...
Nominal effective rate 4/	-0.1	-10.5	-19.1	-20.6	-3.5	...
Real effective rate 4/	2.1	-6.4	-5.3	-10.0	-1.5	...

Sources: Data provided by the Papua New Guinea authorities; and IMF staff estimates and projections.

1/ Includes expenditure on arrears and structural reform financed under the SAL.
2/ Includes residual deficit.
3/ Actual end-of-period rate for 1996-99; value for 2000 refers to that recorded on September 5, 2000.
4/ Percent change from 12 months earlier, based on IMF Information Notice System. Figure for 2000 refers to percent change of March 2000 over December 1999.

Statement by Greg Taylor, Executive Director
for Papua New Guinea
October 13, 2000

I agree entirely with staff that "the early results of Papua New Guinea's program of adjustment and reform are very encouraging, reflecting the authorities' strong commitment to the program."

2. When the Board approved Papua New Guinea's (PNG) Stand-by Arrangement in March this year, the Board and others were justifiably cautious. But the evidence speaks for itself. Yes, approval of the SBA itself went a long way toward rebuilding confidence. But, more importantly, the Government has now built up an impressive record of reform that has helped restore economic stability, improved the policy environment and further buttressed confidence.

3. At this point, there are only a few issues that I would like to emphasize.

Performance under the Program

4. The authorities have met all of the end-June quantitative performance criteria, with over performance in some instances. For example, the authorities had by end-June surpassed the original program performance criterion for end-September net international reserves - and the authorities have locked-in these advances by adjusting the relevant end-December performance criteria (Table 2 of the staff report).

5. In the case of the one structural performance criterion and the structural benchmark where there has been slippage, the delays have been brief, minor and, in significant degree, reflect the authorities' strong determination to follow due process, build consensus and establish ownership. In the case of the structural performance criterion on the public service reform plan, my authorities missed the end-June deadline, but have now completed the plan (see also below). I therefore ask that the Board agrees to my request for a waiver in this regard.

6. There is every reason to believe that compliance with the program will continue - the authorities have strong ownership of the comprehensive macroeconomic stabilization and structural reform program. As a clear demonstration of that commitment, the authorities have agreed to publish the staff report and associated documentation.

Macroeconomic Outlook

7. The improvement in PNG's economic performance and management is continuing - GDP growth continues to be quite solid. Fiscal discipline is being maintained. The authorities' reasonable expectation is that the inflation performance over the second half of 2000 will improve materially - a fully firm monetary posture will be maintained to that end.

Monetary and Financial Sector

8. The new *Central Bank Act* greatly expands the powers and independence of the Bank of PNG. Since the passage of the Act in March, BPNG has confronted circumstances requiring an early demonstration of independent judgement in the takeover of the administration of PNG Banking Corporation, pending its privatization.

9. The magnitude of the accumulated losses of the National Provident Fund is extremely unfortunate. But the fact that this information has been made available is a demonstration of the Government's willingness to identify and address this problem in a transparent and accountable way. Furthermore, new Superannuation and Life Insurance legislation is in preparation, which will strengthen the supervision and operations of these institutions.

Fiscal and Public Sector Reforms

10. The Government's public sector reform plan is the cornerstone of its reform efforts, *inter alia* strengthening accountability and transparency across the whole sector. As the process evolved, circumstances dictated that a slightly different approach be taken from the one foreseen in the program. Rather than a simple review of public expenditure, the authorities have developed a plan for a "whole of government" reform agenda. This meant that the end-June structural performance criterion could only be met with some delay. At the same time, however, there has been extensive consultation with the wide range of interested parties, enabling broad ownership of the reform plan. Reviews have already been completed for two major departments and implementation is expected before the end of the year, subject to finalization of World Bank funding. The review process is at an advanced stage in respect of one agency and three further key departments. In a closely related exercise, service delivery in the government sector is being comprehensively reformed with support from the Asian Development Bank.

11. During our last meeting on PNG, we pointed to the development of the new framework for the Rural Development Program. Staff notes that "most of the initial round of recent project proposals ..... did not comply with the new guidelines and were not approved". This provides reassurance of the Government's commitment to improve the quality of, and accountability for, these expenditures. The authorities have recently opened a liaison office in Parliament to assist Members to comply with the new guidelines.

12. Although the end-September structural benchmark being missed, substantial progress has been made on the comprehensive taxation review. The final report has been completed and is due to be considered by Cabinet in coming days. Following Cabinet consideration, a final submission will be prepared to incorporate recommendations for inclusion in the 2001 budget.

13. It is also noteworthy that the authorities have agreed to publish the fiscal ROSC completed earlier this year with the assistance of FAD and PFTAC. More important is the authorities' commitment to implementing the recommendations in the ROSC in the context of the 2001 Budget, for which ongoing technical assistance from the Fund will be essential.

Other

14. Since this review is taking place in October, I have to ask the Board to waive the applicability of the quantitative performance criteria for end-September, for which the necessary data are not yet available. The end-September quantitative performance criteria, of course, continue to apply for the second review of the SBA.