

**Speech by
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as Guest of Honor at the National Research Institute
Graduation of Candidates for the award of
PNG NRI Diploma in Economic Policy Analysis**

Port Moresby, 29 October 2016

Why urgent action is needed on the economy



It is generally recognized by academics, business leaders and the general public that the non-mining sector economy is in recession.

The facts are that budget over-spending, printing and spending money that we have not earned combined in decline in revenue, have landed us in a situation where kina is struggling and being artificially administered, where foreign reserve shortages are severe and being rationed, where Government is not paying bills on time or in full, where health and education services are being starved of finance, and prices of basic goods are increasing.

Public debt, shown in the budget and outside the budget is over K30b, with annual repayment approaching K3b – around 30% of government revenue.

Some more examples. I refer you to a blog of 22nd August on the ANU Dev Policy Centre site by Stephen Howes and Rohan Fox, showing that the real revenue (after adjustment for inflation), in 2016 is at the same level as ten years ago, in 2006.

Paul Flanagan in his blog of 7th October argues that non-mining sector GDP has fallen by at least 10% in the last two years, possibly double that. He uses data from Treasury (the MYEFO), with domestic tax receipts for this year showing a decline of over 20%; from the PNG Business Council, which has reported 35% drop in sales of member companies in the first six months of this year; and coastal shipping data which shows a contraction of 25% over last year.

Of course it is non-mining sector GDP that affects and reflects the real health of the economy and welfare and the general living standards of Papua New Guineans. A note Flanagan sent out this week expands the earlier analysis with the conclusion that on current trends it will take until 2022 for the living standards of most Papua New Guineans to return to 2013 levels.

Has Government recognized and taken policy adjustments to rectify these problems? To me, not sufficiently, not on time, and not on the scale required.

The current economic and public finance challenges, reminds me of the state of the economy and the budget I inherited in 1999 when I became Prime Minister:

- Inflation was 22%
- The 182 day Treasury bill rate was 28%
- Foreign reserves were US\$89 million, one week of total import cover
- K1 was buying .28 US cents
- The budget deficit was running at 5%

Recognizing this situation, and the need to act decisively on all fronts, I announced 5 major objectives in my acceptance speech in Parliament.

The first objective was to restore integrity to the important institutions of state, the very institutions that are necessary for our security and for our prosperity – institutions such as the Bank of Papua New Guinea, the Departments of Treasury and Finance, the Department of Justice, the Parliament, the Courts, the Ombudsman, the Cabinet Office.

The second objective was to stabilise the kina, to earn again its respect in the international community, and to stop further rapid increase in prices.

The third objective was to restore stability to the national budget.

The fourth objective was to remove obstacles to investment and growth.

The fifth, but not least important objective, was to continue the Bougainville peace process.

What did I achieve in the 3 short years I had? The point of mentioning a few achievements is not to boast or self congratulate, but to show that meaningful reforms can happen, if the leaders have the concern for the welfare of the people and the future of the nation.

- Inflation was reduced from 21.8% to 7.9% in two years
- T Bill rates were reduced from 28% to 10.9% in two years

- Foreign reserves rose from US\$89m to US\$371m in two years
- US\$-Kina rate rose from 28 cents to 30 cents
- Over K400m in Government arrears were paid in the 2000 and 2001 budgets

Knowing that Government did not have the financial resources to support the necessary adjustments, I called on the multilateral institutions and bilateral governments to form what I called Friends of PNG. To them I outlined my diagnosis of the problems, and the policy prescriptions I would follow. The reform program was supported by all the members of the Friends of PNG.

The figures quoted show that meaningful adjustments can be undertaken and important reforms can be instituted. But these have to be led by the Prime Minister if they are to succeed.

What were the reforms, apart from achieving peace on Bougainville and improving the macro-economic indicators?

First – **financial sector reform:**

- A new Central Banking Act and the Banks and Financial Institutions Act increased the powers and independence of the Central Bank and its Governor. Sadly, those independent powers are being ignored – though the laws are still there. In other words, the laws are being broken.
- The Superannuation Act removed political involvement in supervision and decision-making regarding investments of superannuation funds. These powers were removed from the Treasurer and given to the Central Bank – and look at the results. A bankrupt NPF is now worth billions of kina and is travelling well as Nasfund, with a similar result for Nambawan Super.
- The Commission of Inquiry into NPF was absolutely necessary to find out why it was virtually bankrupt and to lay the ground for its recovery. The Commission of Inquiry was not set up to catch anybody; it was set up to provide answers to contributors, both employees and employers, and to the Government, as to what had gone wrong. In that process, surprisingly, some people were caught hiding in the cupboard.
- The merging of BSP and PNGBC saved a bankrupt PNGBC and, in fact, the entire banking industry. Government was left with 25% ownership of the new entity, which is now worth many times more than when Government owned 100% of PNGBC - not to mention the tax revenue and increase in employment that also occurred. BSP is now a regional bank with branches in many Pacific countries.

Let us hope that the Government will leave these successful institutions alone.

Second – **reform of public enterprises:**

- IPBC was established to coordinate and supervise all the state-owned commercial enterprises, many of which were operationally stranded due to lack of capital and operational funds. The owner – the state – was also stranded, virtually bankrupt and unable to resource the SOEs.
- IPBC was also required to prepare selected SOEs for:
 - sale – privatization, or
 - partial sale (mergers), or
 - lease of assets, or
 - contract management of the assets, or
 - recapitalization and streamlining of the management.
- PNGBC was the first SOE to be merged, with BSP - and see how successful it is now.
- Another successful merger was that of Orogen Minerals with Oil Search. I could see that Orogen was becoming stagnant and passive, and would not have sufficient capital to undertake any meaningful investment. The government ended up with almost 20% ownership of Oil Search – which as you know would now be hugely valuable. Unfortunately our shares were later mortgaged to support a loan from IPIC and lost. The State's reacquisition of 10% in Oil Search is one of the worst deals in PNG's economic history.
- Also unfortunately, the plans I hatched for PNG Power and Telikom were not completed, nor were they further developed by the successor government.

Third – **competition policy:**

- ICC was established and powers previously held by the Treasurer were transferred to an independent Commission. I knew that once the SOEs like Telikom or PNG Power were privatized, in full or in part, they would become powerful monopoly companies so ICC was set up to regulate their operations and protect the public.

One other area I want to touch on briefly is **constitutional and political reform**. Given the numerous changes of government that had occurred since Independence, it was clear that political instability and frequent changes of government were hampering government's ability to take a longer term view of development. So I introduced OLIPAC, and limited preferential voting. It is my view that we can enhance political stability through strengthening the political party system. Sadly, OLIPAC has been eroded. As a result we have a system where one

party buys up everyone else, and the other parties are struggling for survival because of lack of funds and MPs are free to roam. Roaming may be in the interest of the individual MPs but it is not, in my view, in the national interest.

So where do we go from here? If we know where we want to go, do we have the political will and the determination to get there?

We have really two choices:

- 1) do nothing or pretend to be doing something and only scratch the surface of the problems, or
- 2) adopt a set of comprehensive policy and institutional reforms.

We face a dilemma if we adopt the second – correct - choice.

The Government needs to spend more of the money we have to stop the recession from getting worse. But revenue levels are now back to 2006 levels in real terms and unlikely to improve given the recession. More borrowing and more printing of the Kina are not an option. Our debt is K30b, eating up K3b each year in interest payments. We must not force the Central Bank to print any more Kina, because increasing domestic credit through Government expenditure, without foreign currency backing will put pressure on foreign reserves and threaten Kina convertibility.

That is the dilemma. What do we do?

To me, the Government's priority should be to shift or reallocate the revenue we have to fund projects and activities in sectors that will generate growth and diversification of the economy, and to properly fund the maintenance of existing economic infrastructure and essential services such as health and education. We have enough money to do that. But we do not have enough money for new highways or ring roads, new government office blocks, new Universities or lavish show-off events.

The Government should stop wasting millions of kina, hosting expensive international conferences and parading Heads of Government the likes of President Mugabe. The opportunity cost of such events is unacceptably high.

Papua New Guinea's immediate future is uncertain if we continue to behave the way we have in the last four years. We have become so greedy that we are eating and consuming all that we are harvesting from our garden, and saving or storing no seeds for future gardens. See where we are now - short of foreign currencies, a struggling Kina, being manhandled and Government not paying its bills in full and on time. And yet we have the US\$21 billion, PNG LNG plant in full production exporting and earning hundreds of millions in foreign currencies and paying taxes to the Government. And yet we are struggling. What a paradox; rich in resources but poor in services. Something is not right.

You are all leaders in your own sphere, occupying positions of importance and influence in terms of policy advice. I urge you to get involved in public and responsible social media debate on economic policy issues. It will only be when Papua New Guineans speak the facts; it will only be when Papua New Guineans discuss the issues openly and frankly that we will overcome the challenges confronting us, and lay a strong foundation for growth.

Thank you all.