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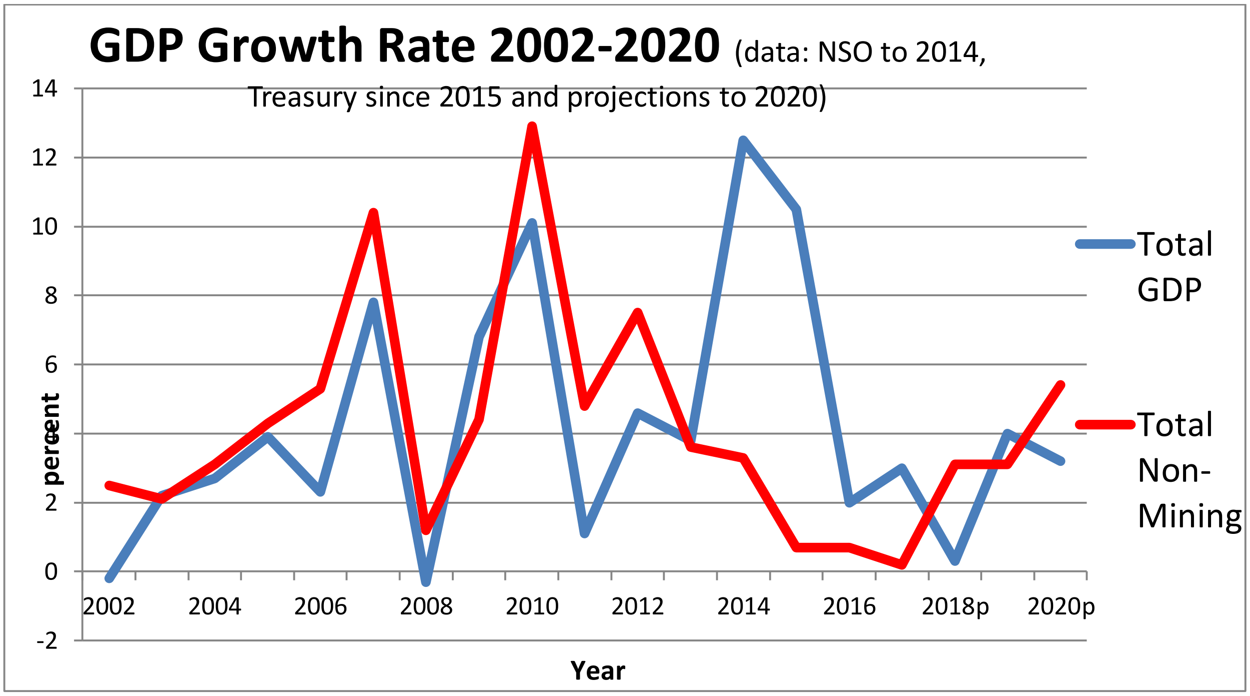
The International and Domestic Economy, including Fiscal Conditions

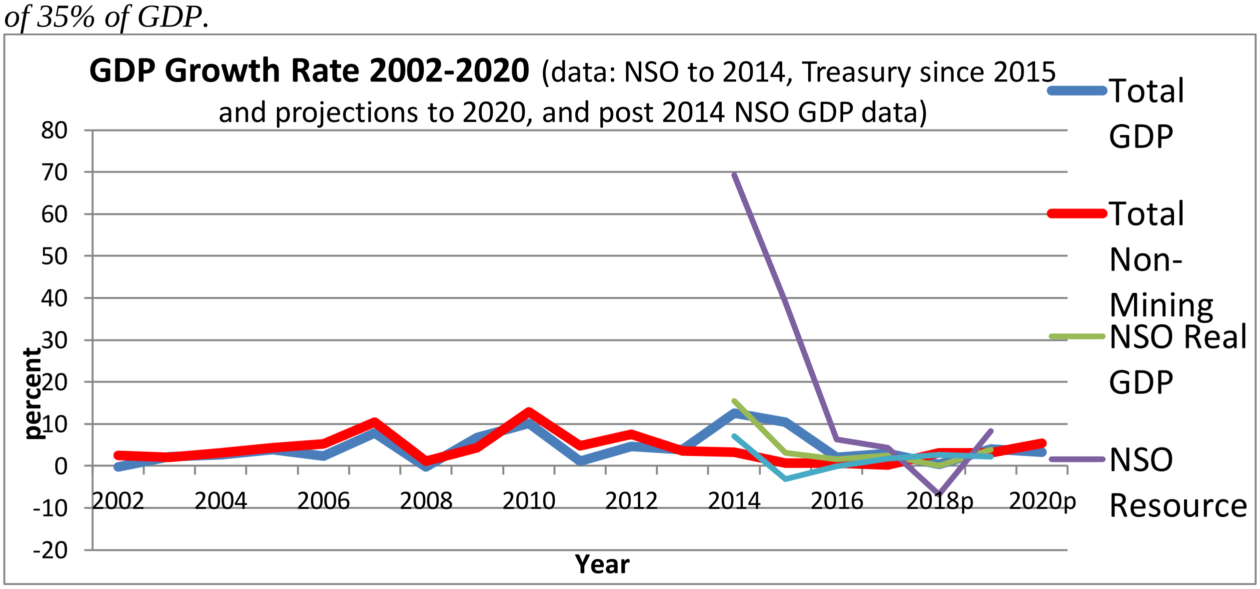
The global economy experienced sustained growth during most of 2018, led by the US but also with continued Chinese progress, despite growing uncertainty over China's level of debt and the stability of its property market and increasing market nervousness at the year end. Most commodities saw some recovery during the early part of 2018, although as the year progressed increased threats of trade war between the US and China, but also between US and its traditional allies and trading partners and divergent fiscal and monetary policy in the US, sent stocks and some commodity markets tumbling or into uncertain fluctuations, while gold prices soared to USD 1,271/oz as a safe haven.. China's increasingly forthright stance over some regional issues, and tough stance with respects to domestic issues and some minority groups, added to concerns that it was no longer business as usual. China's effort to have its growth stimulated by overseas investment and lending is logical, considering the level of apparent over-capitalisation at home, but anxiety over increasing economic dominance and indebtedness from easy loans have invariably generated tensions amongst regional neighbours in S/SE Asia and the Pacific. Some of these tensions came to the fore during the APEC Leaders' Summit hosted by PNG in November, with some unseemly interventions over the wording of texts, and some competitive inducements, perhaps providing opportunities but also risks for Pacific islands nations over infrastructure and other services.

Several commodity prices declined during the second half of 2018, but energy prices were driven by mixed signals, of continued, if slow global economic growth, strong production, including from unconventional sources in North America, steady supply growth from gas/LNG from different supply sources, and the steady fall in the price of renewable energy, but also possible supply disruption in the Middle East. Global economic growth is expected to tail off in 2019 or at least progress at a low positive rate, without immediate prospective stimuli apparent (such as the reduced US personal tax rates in 2018) and more downside risk prospects, associated with further trade conflict, potential banking and other market uncertainty in China, but also parts of Europe, S America and the Middle East (including if Brexit is allowed to proceed).

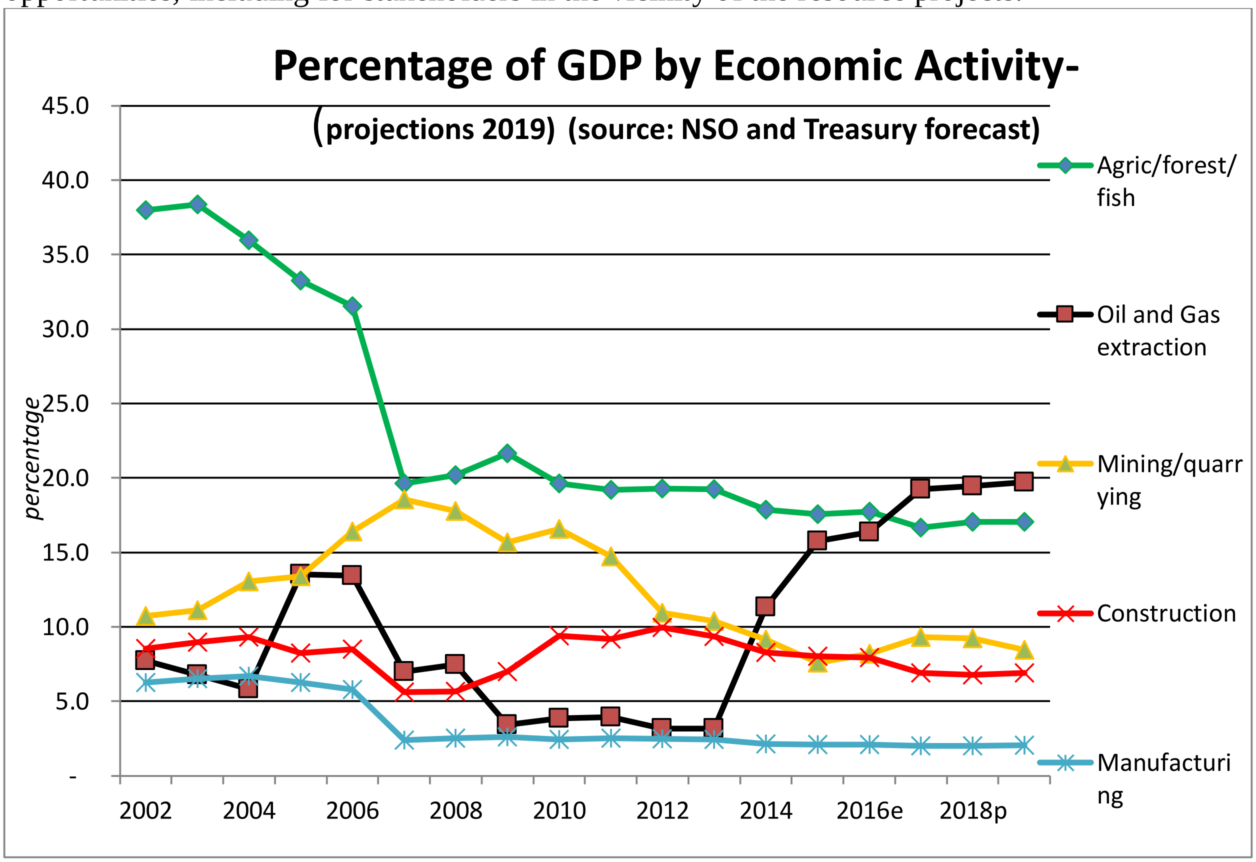
After several years of very low economic activity since the stimulus associated with the commencement of LNG production in 2014, growth is estimated to have fallen to 0% in real terms in 2018, in the face of still relatively low commodity prices (apart from gold), various constraints to economic activity (including the lack of foreign exchange), and the major earthquake in February which disrupted four of the major resource projects to different extents, as well as causing severe humanitarian catastrophe to the affected communities in SHP, Hela and Western Province, particularly. The Treasury's assessment indicated some recovery in growth in the non-mining sector in 2018 and is forecasting a modest recovery of total growth in 2019, prior to stronger economic activity in 2020 stimulated partly by prospective major new resource project developments early next decade (including Papua LNG, and later P'nyang, and potentially Wafi-Golpu copper/gold mine in Morobe province).

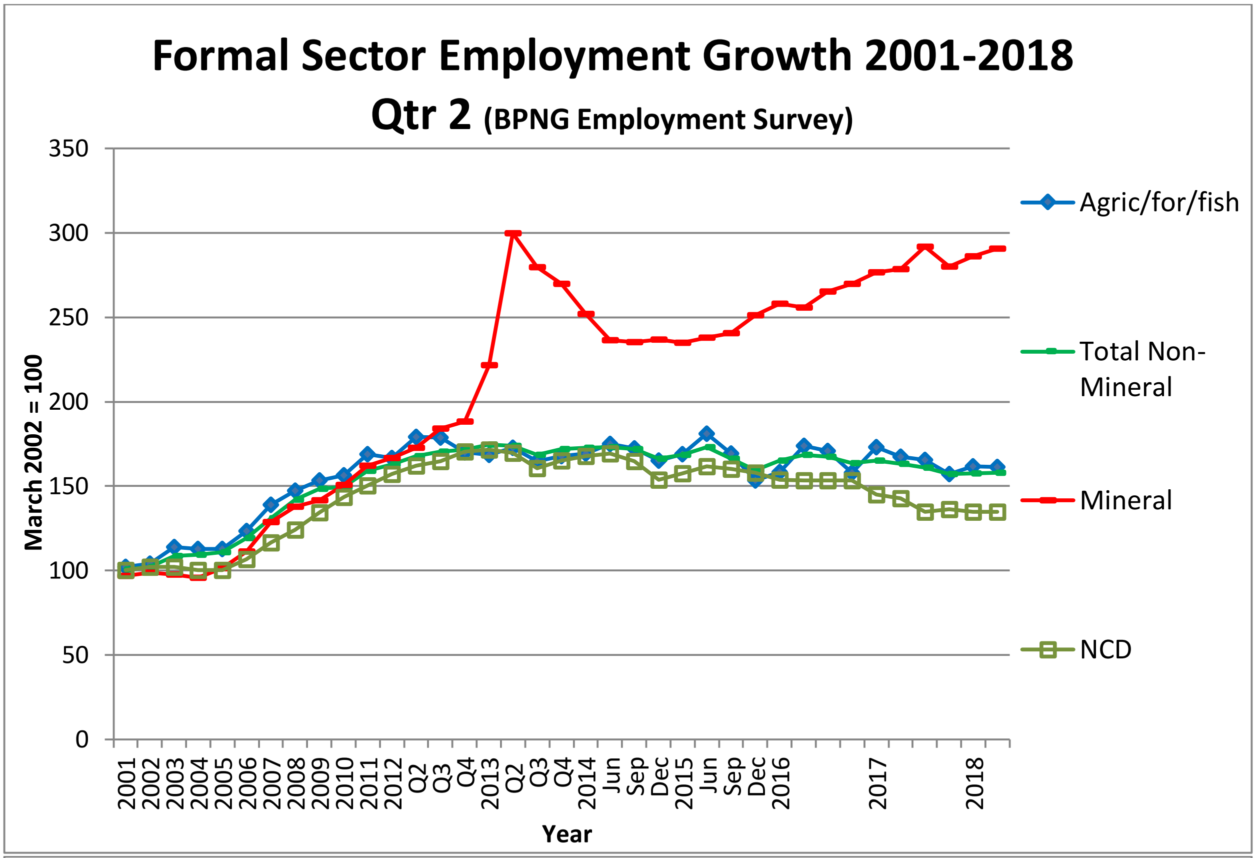


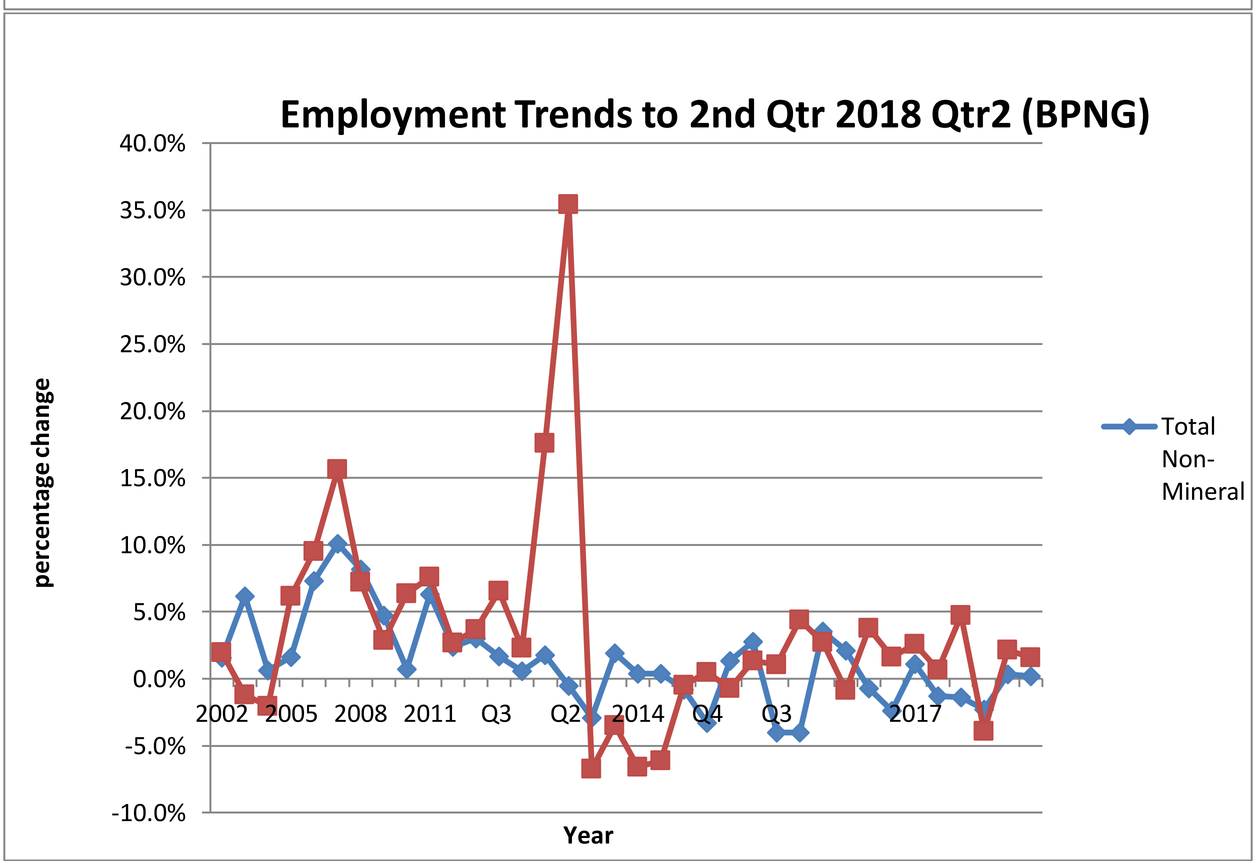
Note: NSO revised their official GDP figures during the year, following a major review, resulting in significantly contrasted outcomes and growth figures from the prior sequence. Treasury has avoided using the new NSO figures on the grounds that they distort trends; it should also be noted that, if used (as they have been by the IMF), the debt to GDP figures fall outside the legally allowable limits set by the Fiscal Responsibility Act, even with its temporary approved variation of 35% of GDP.

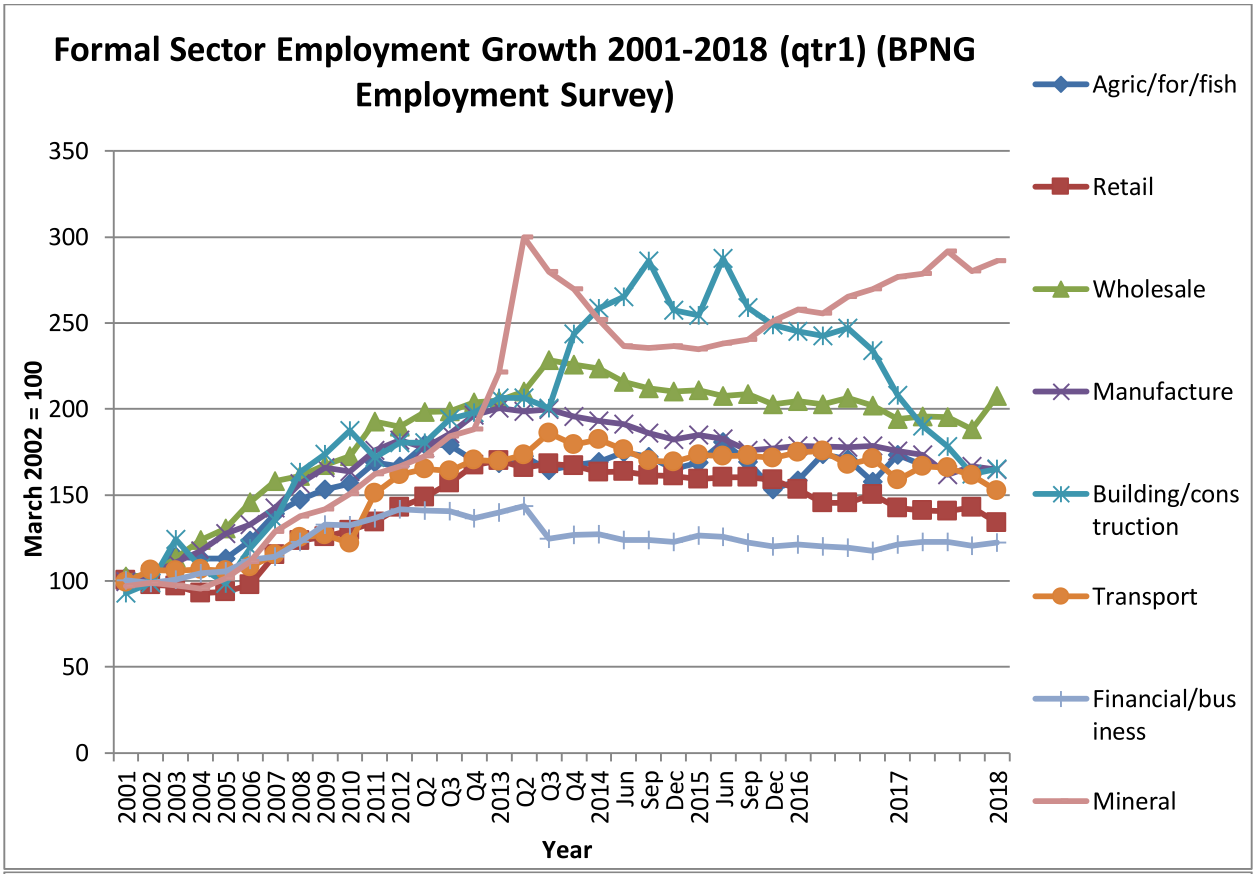


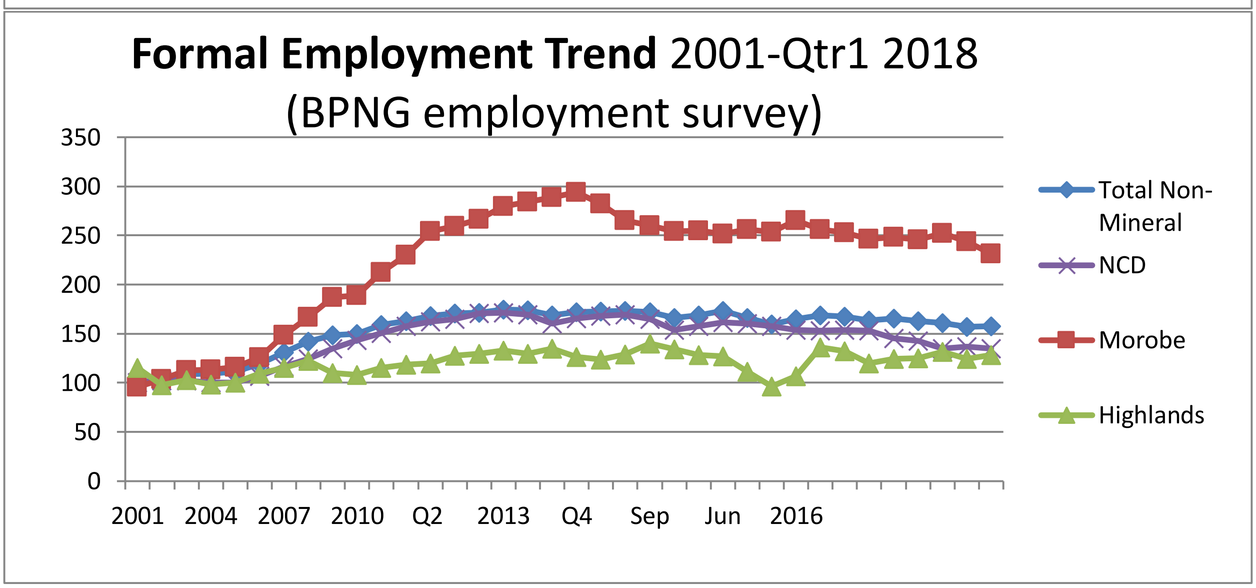
Oil and Gas (notably LNG production) have continued as the largest single component of PNG's National Output, with sustained production and stronger prices through 2018. It has also been the major export earner, and, during 2018, provided some increase in its previous modest contribution to revenue. On the other hand, in terms of employment generation, oil and gas remains a very minor contributor, at least beyond the relatively brief project construction phase. This paradox of development in PNG, entailing a major and potentially growing extractive sector, including mining, increasingly dominating GDP and exports, but generating limited immediate revenue or foreign exchange reserves in recent years and modest employment and multiplier impact has increasingly been a focus for policy makers, partly thanks to the exposure of reconciled figures through the EITI process. Apart from economic commentators, including the INA, the issue has gained greater government attention, in the face of tight fiscal conditions and the context of negotiating the next generation of resource projects, but also with some oil and mining executives, recognising increasingly that access to PNG's resources in future will require different conditions or social legitimacy than hitherto, but particularly entailing greater focus on what matters most to the fast growing population of PNG, notably practical job creation and income earning opportunities, including for stakeholders in the vicinity of the resource projects.




Formal Sector Employment Growth 2001-2018
Qtr 2 (BPNG Employment Survey)
March 2002 = 100
350
300
250
200
150
100
50
0
2001
2002
2003
2004
2005
2006
2007
2008
2009
2010
2011
2012
Q2
Q3
Q4
2013
Q2
Q3
Q4
2014
Jun
Sep
Dec
2015
Jun
Sep
Dec
2016
2017
2018
Year
Agric/for/fish
Total Non-Mineral
Mineral
NCD


Employment Trends to 2nd Qtr 2018 Qtr2 (BPNG)
percentage change
40.0%
35.0%
30.0%
25.0%
20.0%
15.0%
10.0%
5.0%
0.0%
-5.0%
-10.0%
2002
2005
2008
2011
Q3
Q2
2014
Q4
Q3
2017
Year
Total Non-Mineral

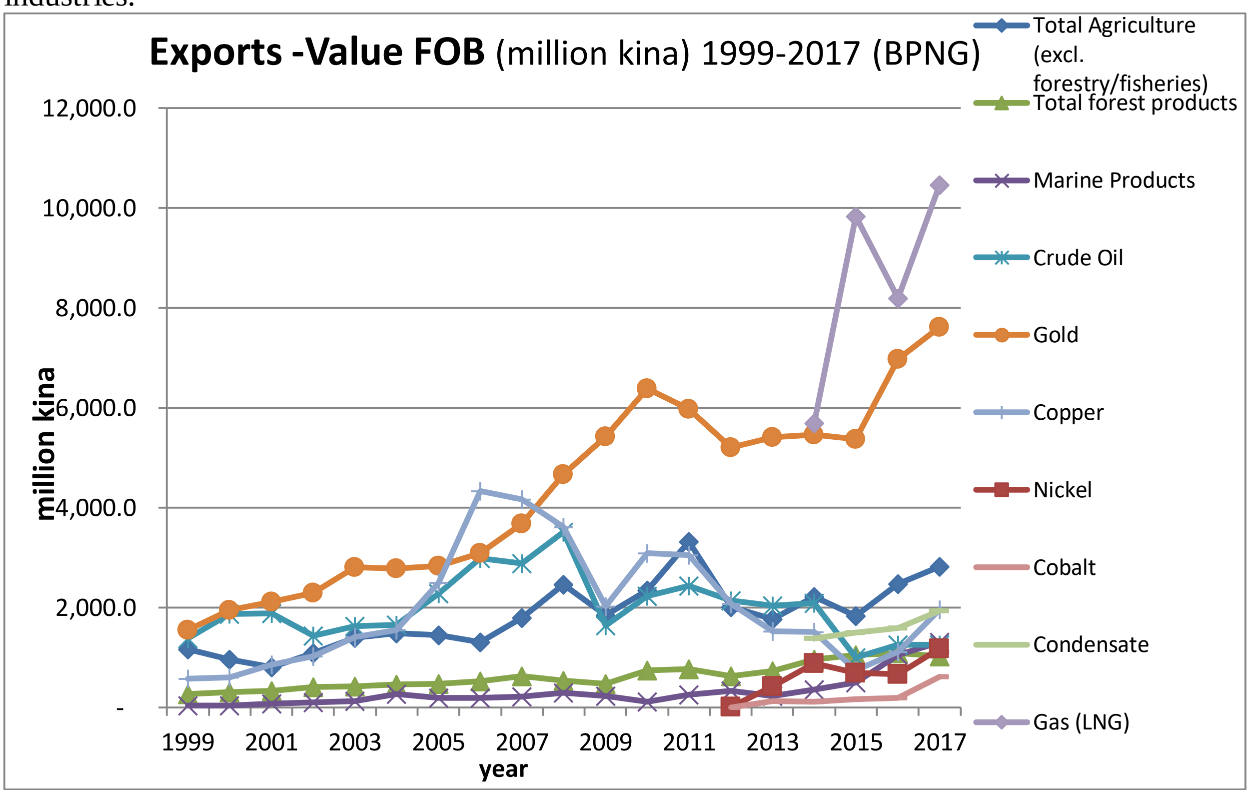


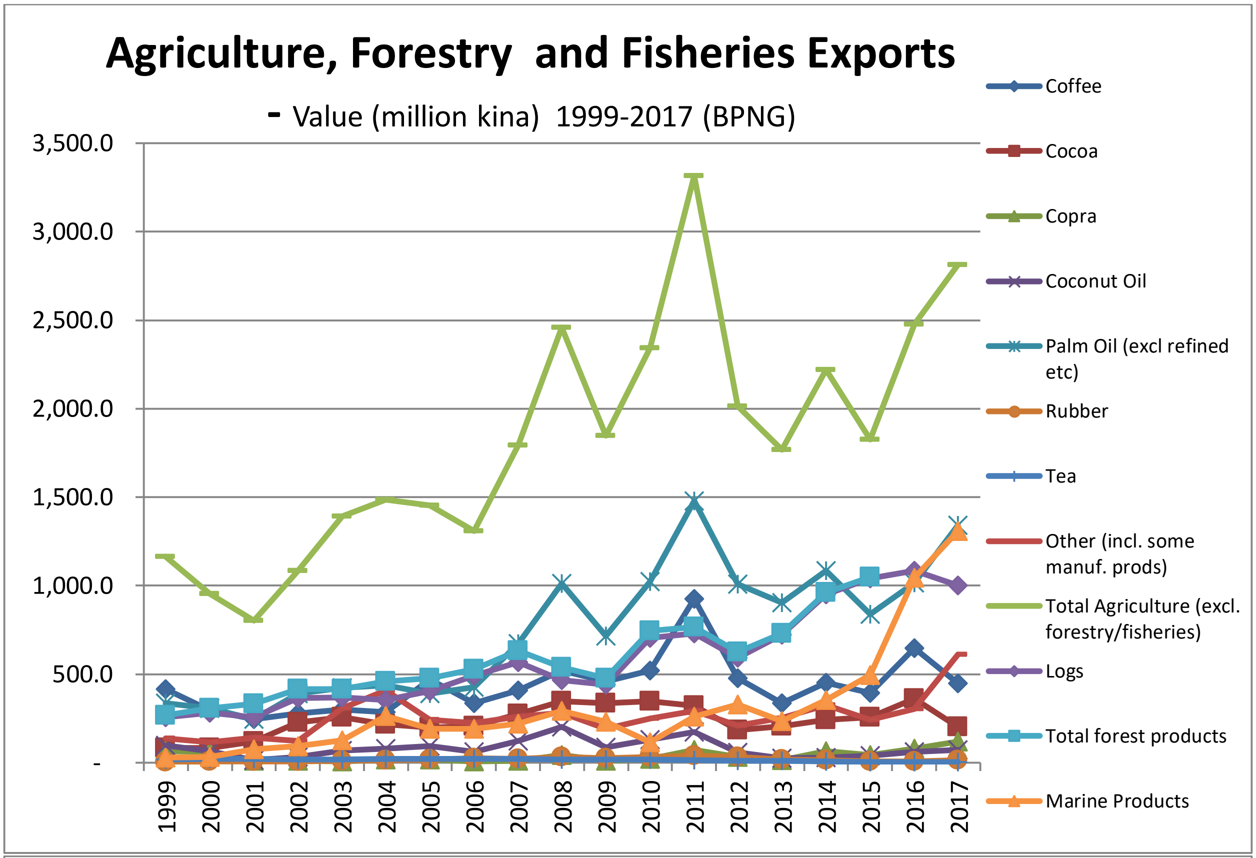


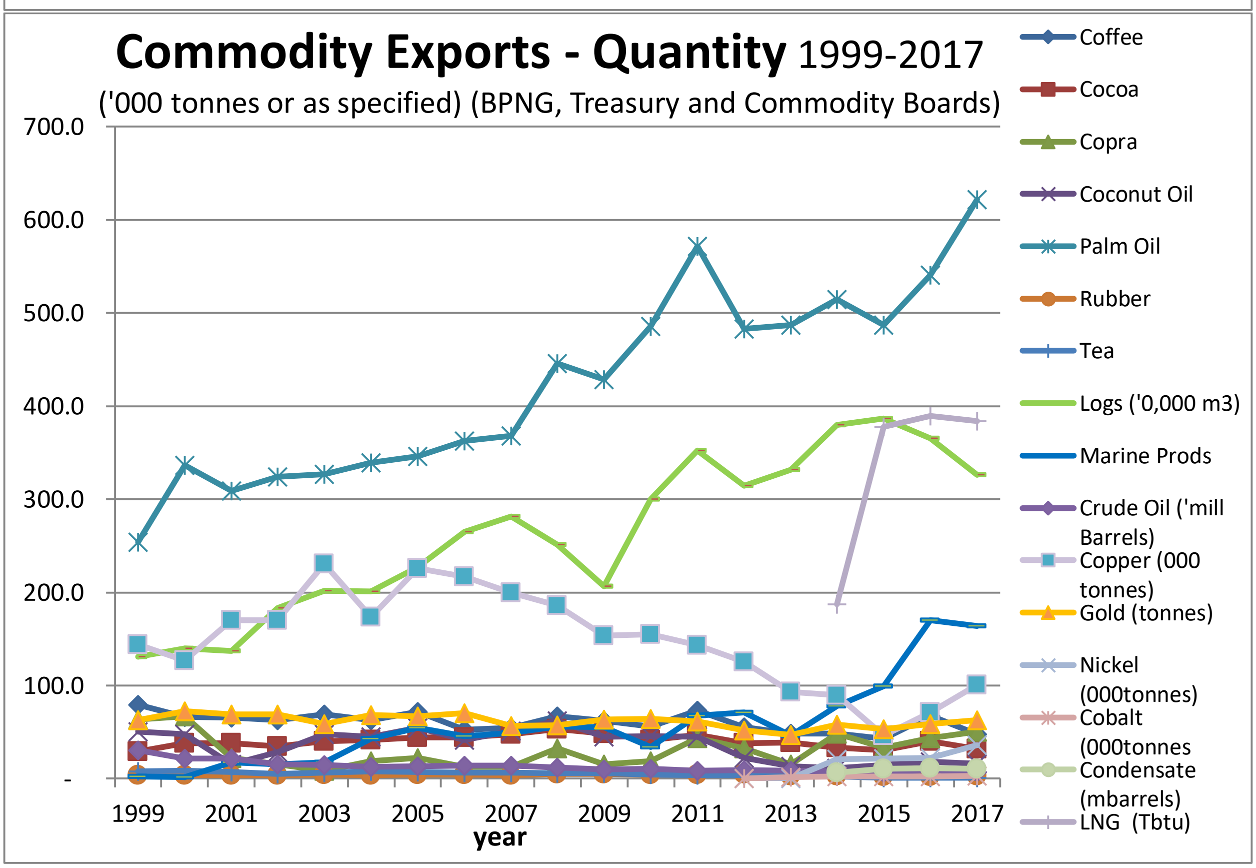
Formal sector employment only provides work for about 1/6 of the employable population, outside education, the balance needing to gain their livelihood in the informal economy. According to the Bank of PNG's long term employment survey non-mining employment have been in decline or at least steady since mid-2012, although the mining/gas-related employment is recorded as rising again since 2015, although only comprising a relatively small portion of the total workforce. Even with the major public sector investment in infrastructure and services in NCD, the Capital's employment rates have also been shown in decline since 2012.

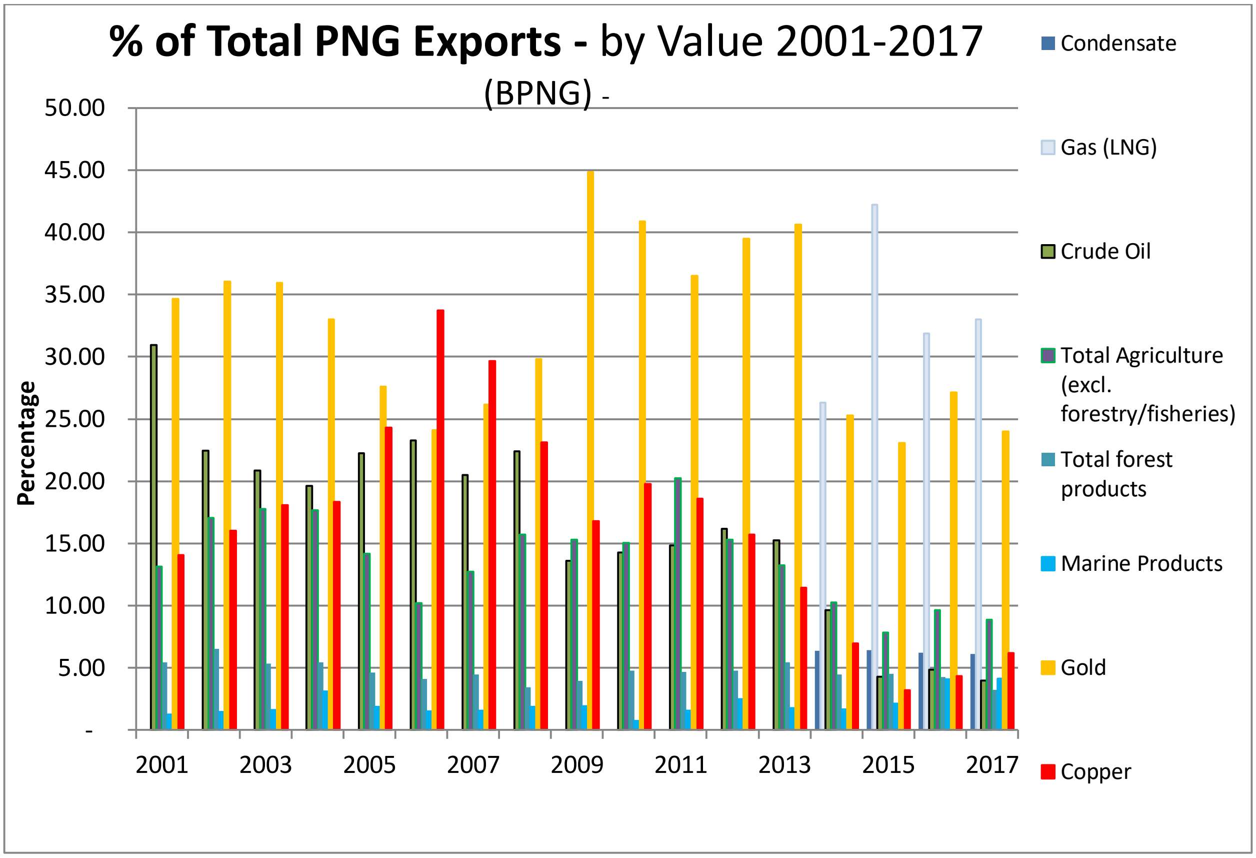
Total exports have more than doubled in value in kina terms over the past 6 years, from K13.3 billion (of which K10.6 bill was from the mineral sector) in 2013 to K21.6 bill (K18.1 bill from minerals, in the first partial year of LNG production, to K25.7 bill in 2016 (K21.1 bill from minerals), K31.7 bill in 2017 (and K26.6 bill from minerals) and around K33-34 billion in 2018. This partly reflects the commencement of LNG production in 2014, despite the major fall in petroleum/gas prices in late 2014, and then the partial recovery of petroleum/gas prices in 2016-18, and the partial recovery of copper prices, continued strength of gold, strong rise in cobalt prices, but also the initial recovery of some agricultural prices which largely slid back in 2017/18). It also reflects the weakening kina to US dollar, which at least helped safeguard producer prices and earnings in kina to agricultural exporters and producers (as well as for tourism operators).

It should be noted, however, that despite the increased overall export earnings, production and export quantities of most of PNG's exports products, apart from LNG, oil palm, logs, marine products and vanilla, have been steady or in some cases in decline since the early 2000s, including the products that provide jobs and incomes direct to ordinary Papua New Guinea producers and households (notably in agriculture). Establishing, or restoring, suitable conditions for viable and low risk business and investment and productivity in these industries, including through provision of reliable public goods and services and suitable and consistent exchange rates, should be priorities in the next years, rather than the State trying to pick winners or directly invest in selected industries.



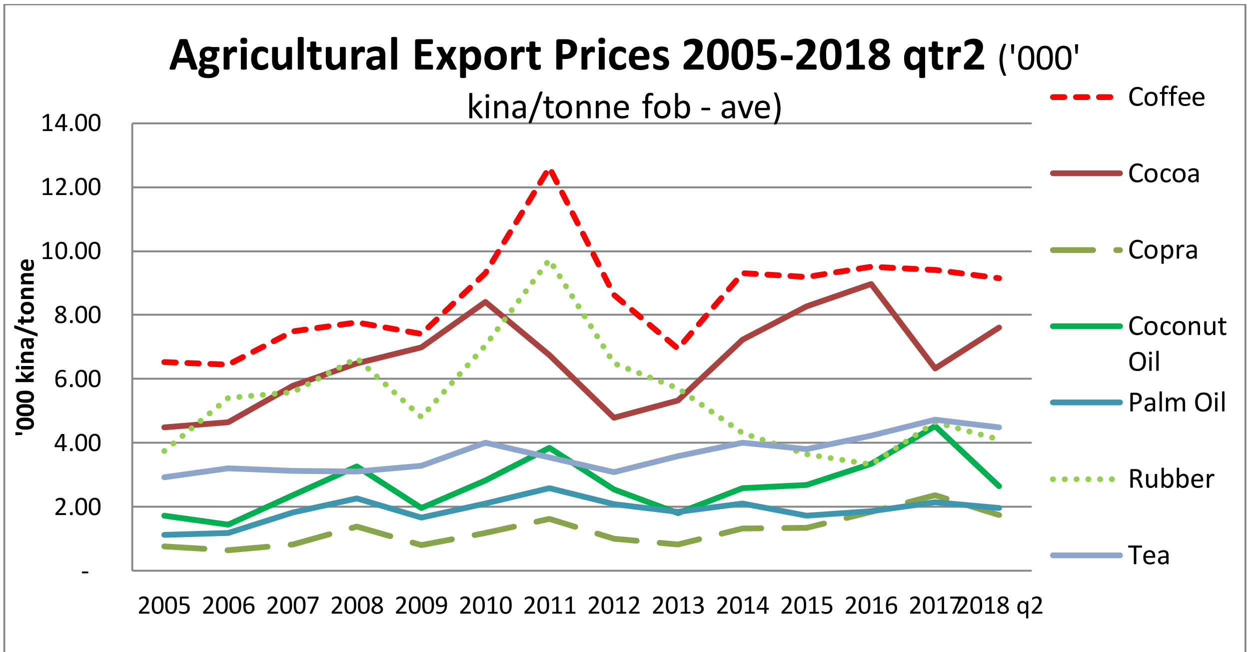

Agriculture, Forestry and Fisheries Exports
- Value (million kina) 1999-2017 (BPNG)
3,500.0
3,000.0
2,500.0
2,000.0
1,500.0
1,000.0
500.0
-
1999
2000
2001
2002
2003
2004
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
2015
2016
2017
Coffee
Cocoa
Copra
Coconut Oil
Palm Oil (excl refined etc)
Rubber
Tea
Other (incl. some manuf. prods)
Total Agriculture (excl. forestry/fisheries)
Logs
Total forest products
Marine Products

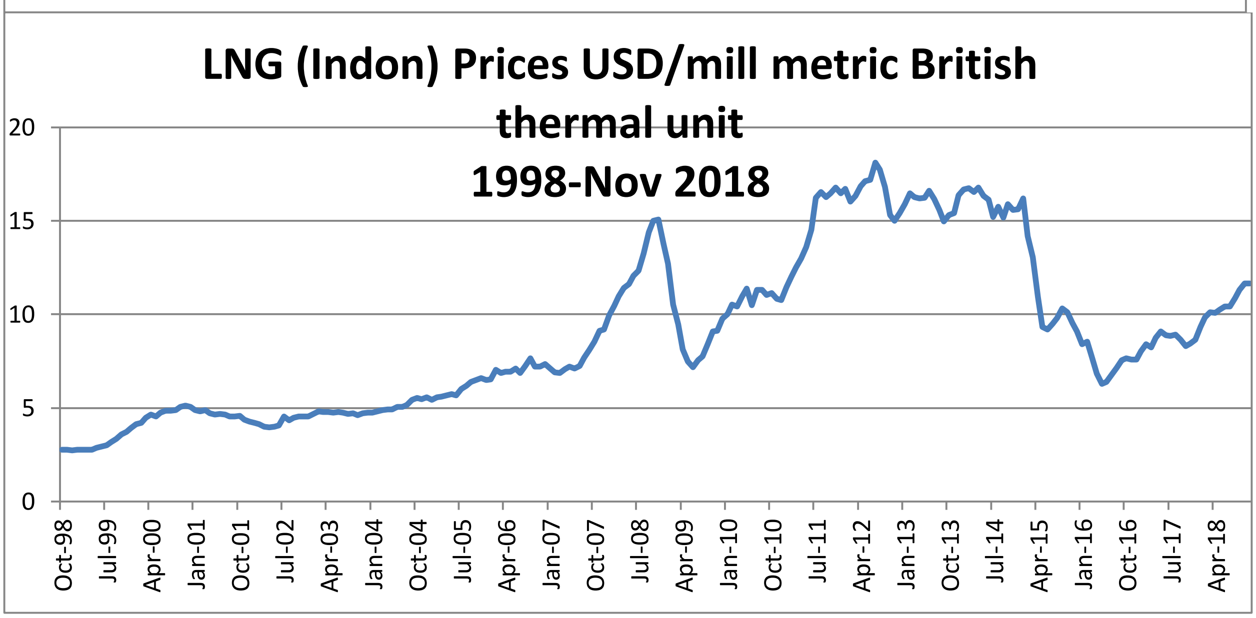

Commodity Exports - Quantity 1999-2017
('000 tonnes or as specified) (BPNG, Treasury and Commodity Boards)
700.0
600.0
500.0
400.0
300.0
200.0
100.0
-
1999
2001
2003
2005
2007
2009
2011
2013
2015
2017
year
Coffee
Cocoa
Copra
Coconut Oil
Palm Oil
Rubber
Tea
Logs ('0,000 m3)
Marine Prods
Crude Oil ('mill Barrels)
Copper (000 tonnes)
Gold (tonnes)
Nickel (000tonnes)
Cobalt (000tonnes
Condensate (mbarrels)
LNG (Tbtu)

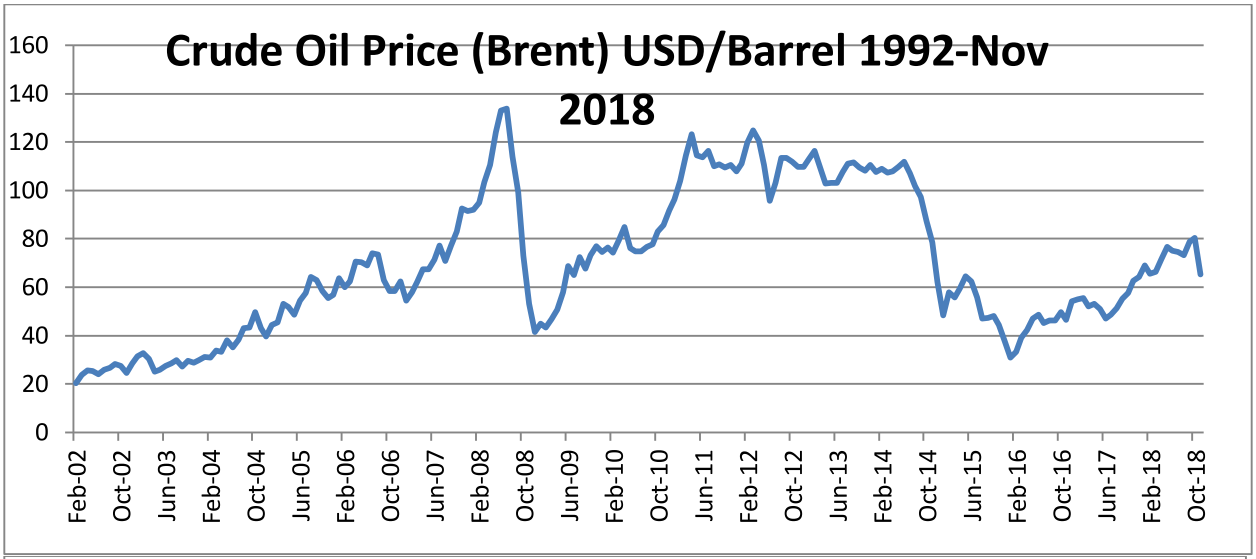


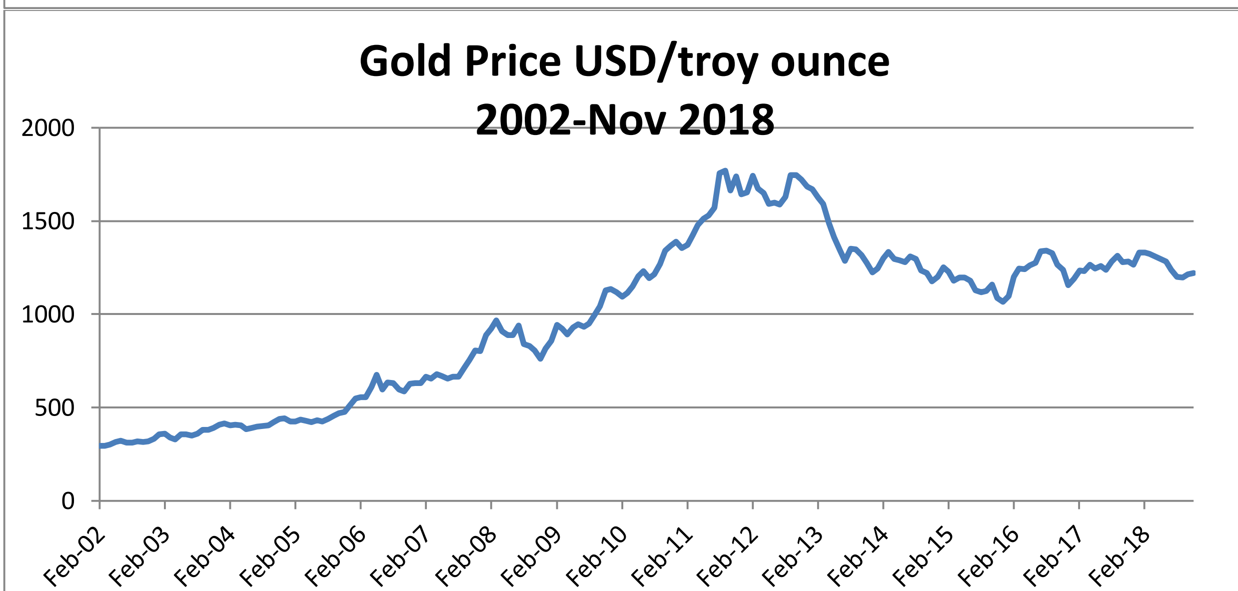
This graph shows the shifting dominance to LNG as the major export earner, although gold, which has been PNG's main export earner most years since the 1980s, remains close behind, particularly with its sustained strong price, despite no major new mines commencing since the mid-1990s.

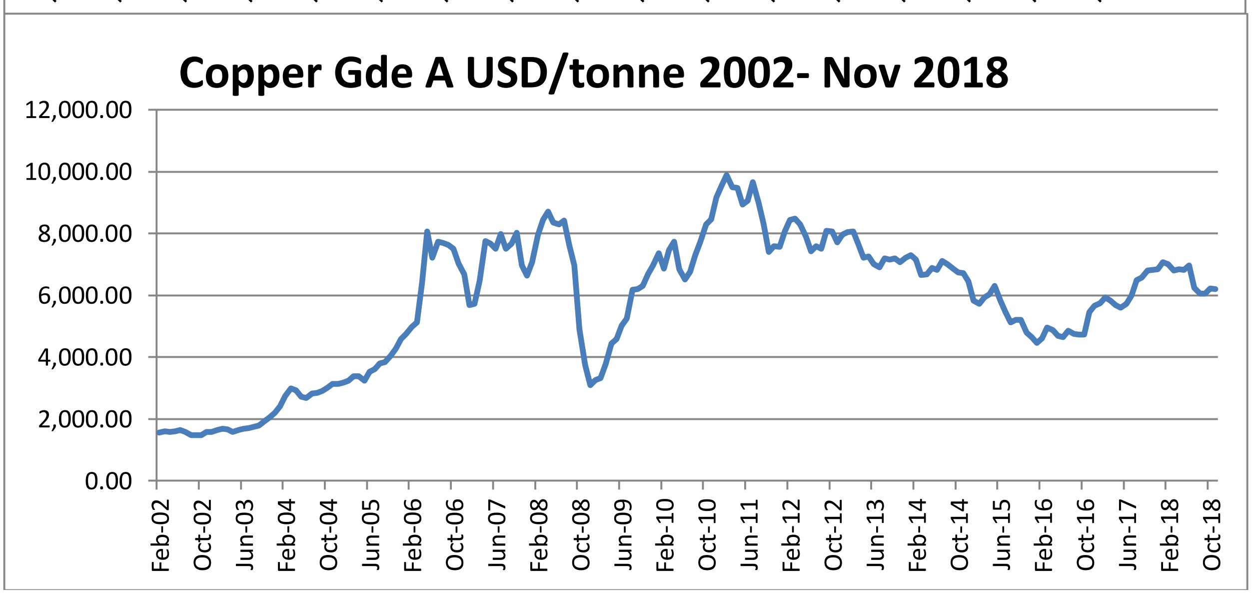
The failure to convert this high export earning and the strong balance of trade surplus, into greater revenue to the State, at least until 2018 when it has been partially recovering, or even the provision of foreign exchange, desperately needed by the rest of the economy, highlights the weakness or obsolescence of aspects of PNG extractive resource conditions and agreements, particularly some of the more recent agreement, which failed to provide early revenue or foreign exchange flows, but also entailed costly State equity investments, diverting major expenditure away from priority State functions of providing basic public goods, needed by both the private sector and households.

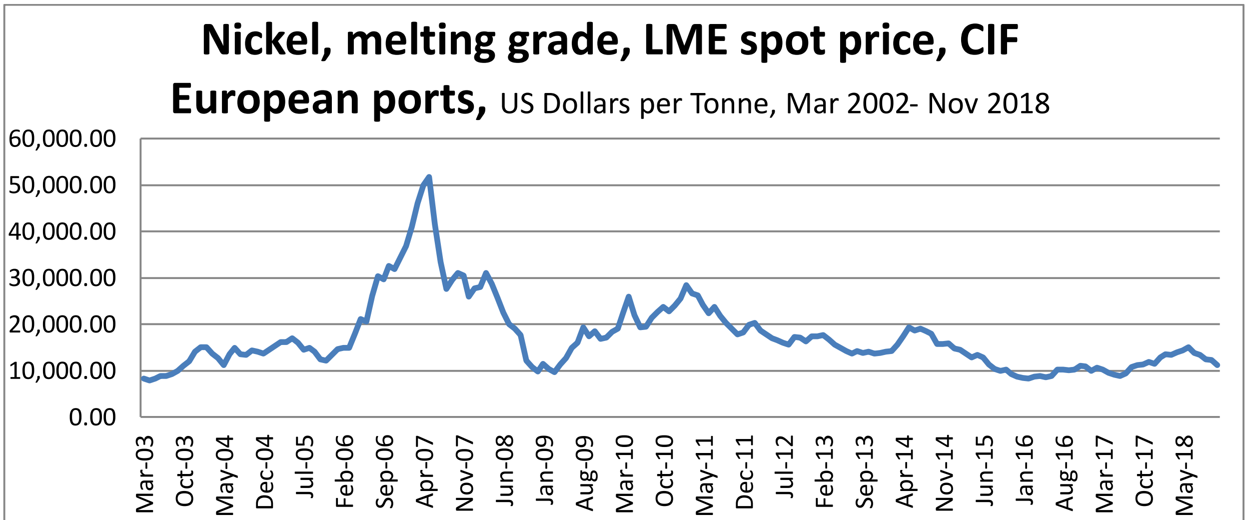

Agricultural Export Prices 2005-2018 qtr2 ('000' kina/tonne fob - ave)
'000 kina/tonne
14.00
12.00
10.00
8.00
6.00
4.00
2.00
-
2005 2006 2007 2008 2009 2010 2011 2012 2013 2014 2015 2016 2017 2018 q2
Coffee
Cocoa
Copra
Coconut Oil
Palm Oil
Rubber
Tea

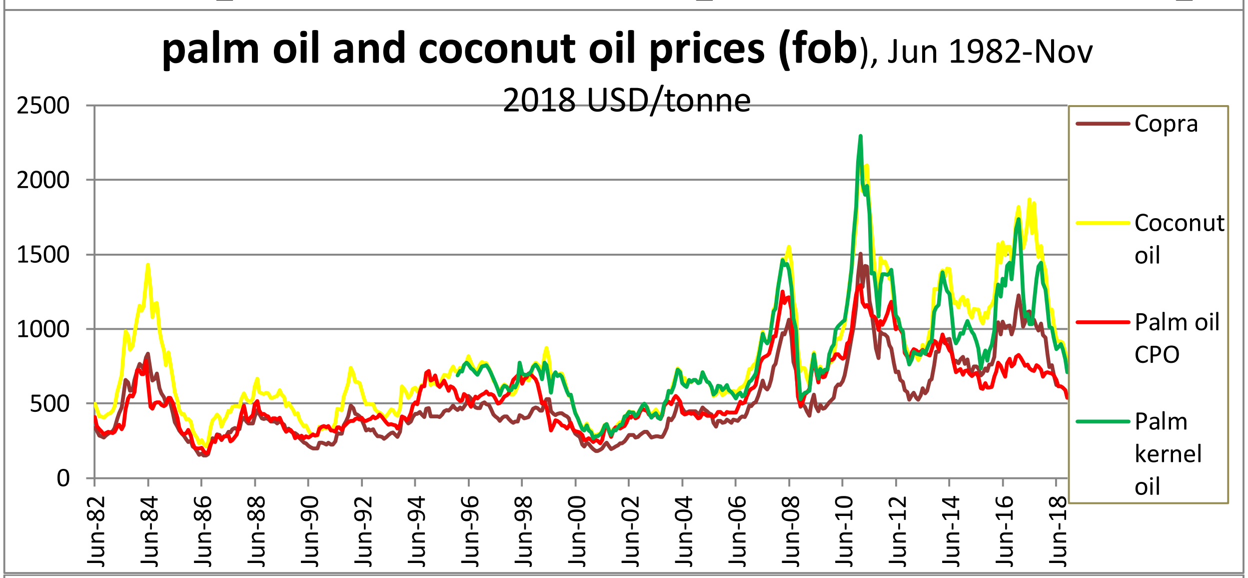

LNG (Indon) Prices USD/mill metric British thermal unit
1998-Nov 2018
20
15
10
5
0
Oct-98 Jul-99 Apr-00 Jan-01 Oct-01 Jul-02 Apr-03 Jan-04 Oct-04 Jul-05 Apr-06 Jan-07 Oct-07 Jul-08 Apr-09 Jan-10 Oct-10 Jul-11 Apr-12 Jan-13 Oct-13 Jul-14 Apr-15 Jan-16 Oct-16 Jul-17 Apr-18

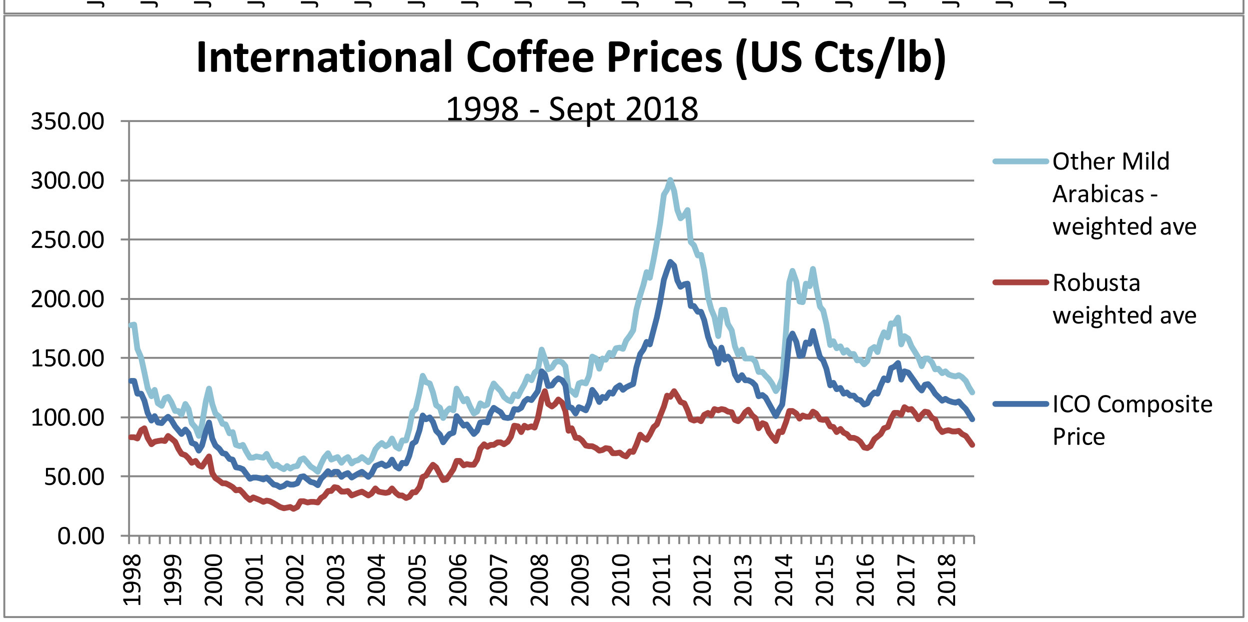

Crude Oil Price (Brent) USD/Barrel 1992-Nov 2018
160
140
120
100
80
60
40
20
0
Feb-02
Oct-02
Jun-03
Feb-04
Oct-04
Jun-05
Feb-06
Oct-06
Jun-07
Feb-08
Oct-08
Jun-09
Feb-10
Oct-10
Jun-11
Feb-12
Oct-12
Jun-13
Feb-14
Oct-14
Jun-15
Feb-16
Oct-16
Jun-17
Feb-18
Oct-18

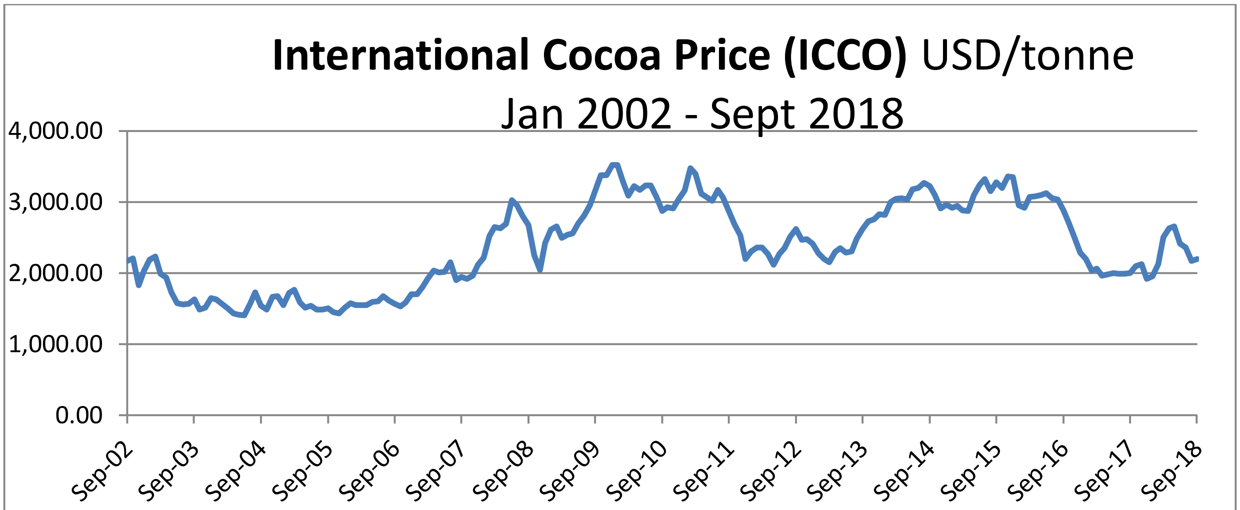

Gold Price USD/troy ounce 2002-Nov 2018
2000
1500
1000
500
0
Feb-02
Feb-03
Feb-04
Feb-05
Feb-06
Feb-07
Feb-08
Feb-09
Feb-10
Feb-11
Feb-12
Feb-13
Feb-14
Feb-15
Feb-16
Feb-17
Feb-18

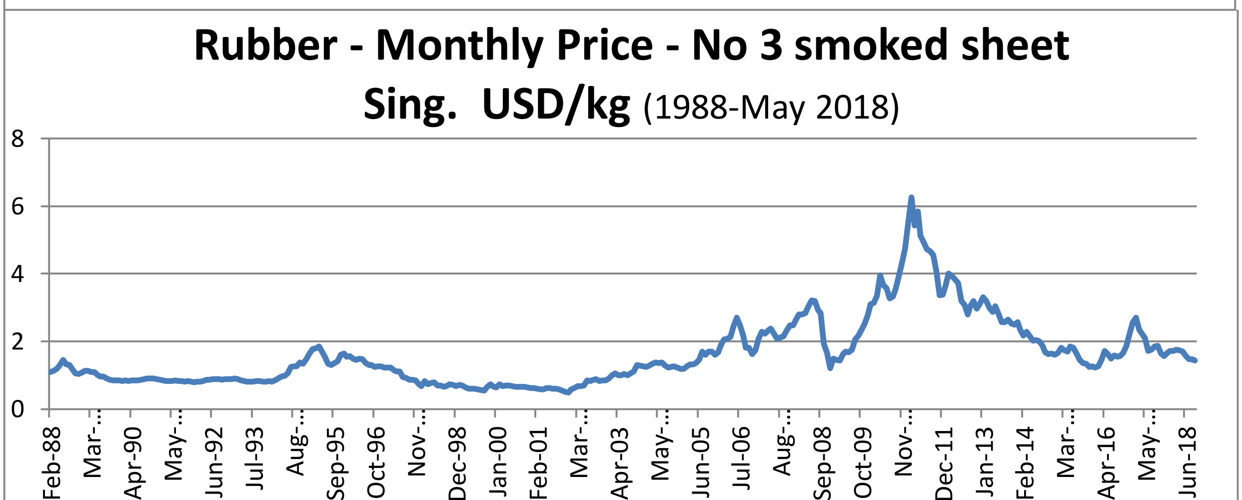

Copper Gde A USD/tonne 2002- Nov 2018
12,000.00
10,000.00
8,000.00
6,000.00
4,000.00
2,000.00
0.00
Feb-02
Oct-02
Jun-03
Feb-04
Oct-04
Jun-05
Feb-06
Oct-06
Jun-07
Feb-08
Oct-08
Jun-09
Feb-10
Oct-10
Jun-11
Feb-12
Oct-12
Jun-13
Feb-14
Oct-14
Jun-15
Feb-16
Oct-16
Jun-17
Feb-18
Oct-18

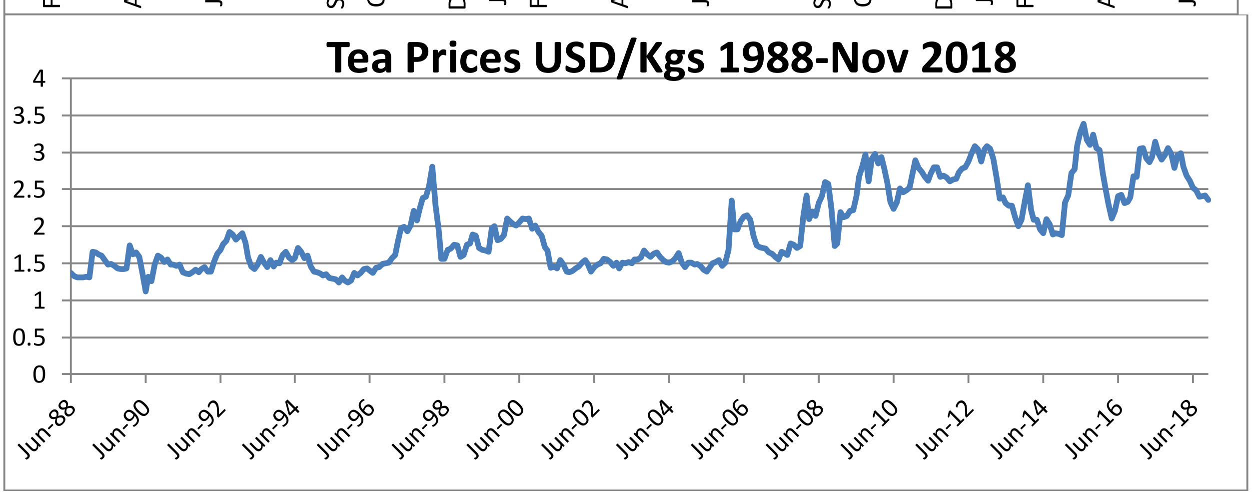

Nickel, melting grade, LME spot price, CIF European ports, US Dollars per Tonne, Mar 2002- Nov 2018
60,000.00
50,000.00
40,000.00
30,000.00
20,000.00
10,000.00
0.00
Mar-03
Oct-03
May-04
Dec-04
Jul-05
Feb-06
Sep-06
Apr-07
Nov-07
Jun-08
Jan-09
Aug-09
Mar-10
Oct-10
May-11
Dec-11
Jul-12
Feb-13
Sep-13
Apr-14
Nov-14
Jun-15
Jan-16
Aug-16
Mar-17
Oct-17
May-18

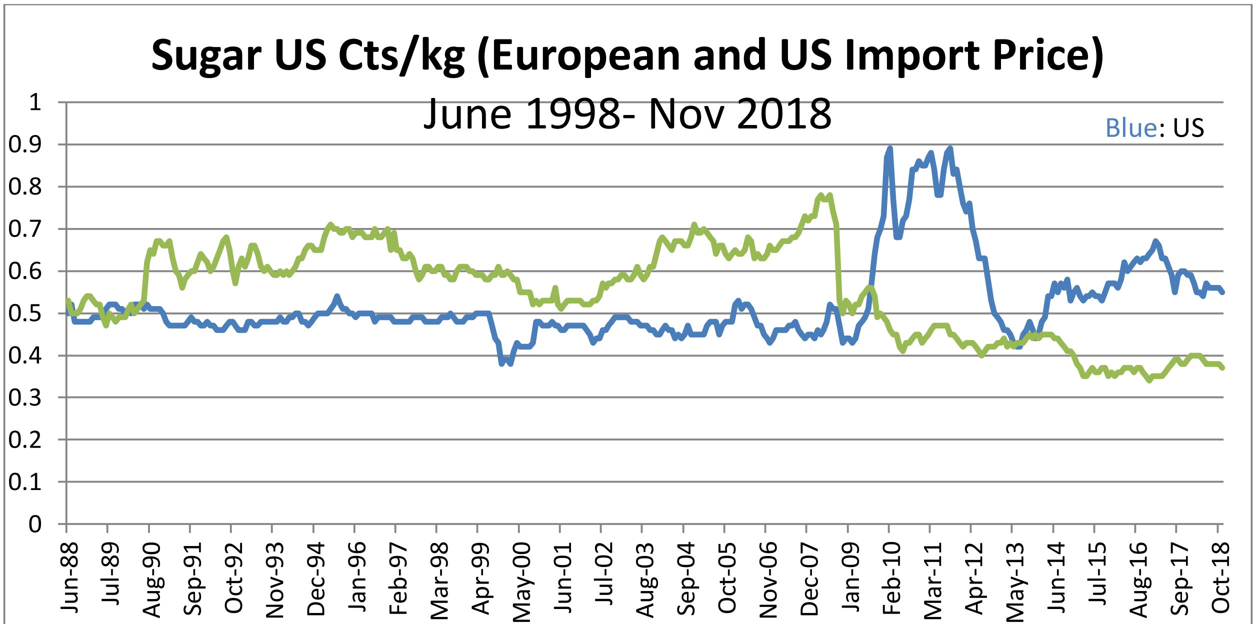

palm oil and coconut oil prices (fob), Jun 1982-Nov 2018 USD/tonne
2500
2000
1500
1000
500
0
Jun-82
Jun-84
Jun-86
Jun-88
Jun-90
Jun-92
Jun-94
Jun-96
Jun-98
Jun-00
Jun-02
Jun-04
Jun-06
Jun-08
Jun-10
Jun-12
Jun-14
Jun-16
Jun-18
Copra
Coconut oil
Palm oil CPO
Palm kernel oil

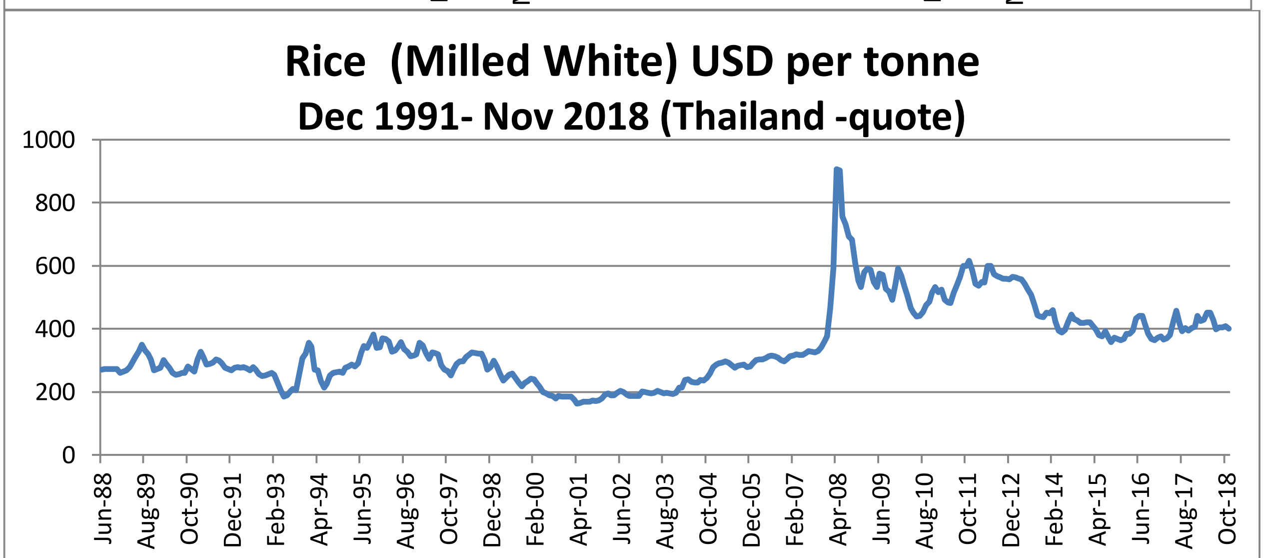

International Coffee Prices (US Cts/lb)
1998 - Sept 2018
350.00
300.00
250.00
200.00
150.00
100.00
50.00
0.00
1998
1999
2000
2001
2002
2003
2004
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
2015
2016
2017
2018
Other Mild Arabicas - weighted ave
Robusta weighted ave
ICO Composite Price

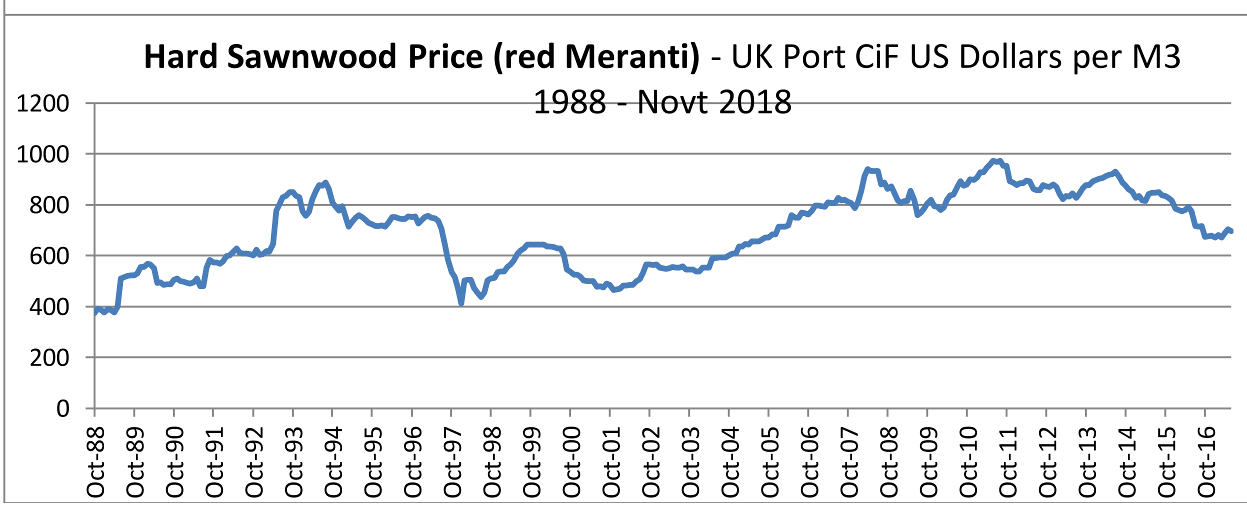

International Cocoa Price (ICCO) USD/tonne
Jan 2002 - Sept 2018
4,000.00
3,000.00
2,000.00
1,000.00
0.00
Sep-02
Sep-03
Sep-04
Sep-05
Sep-06
Sep-07
Sep-08
Sep-09
Sep-10
Sep-11
Sep-12
Sep-13
Sep-14
Sep-15
Sep-16
Sep-17
Sep-18


Rubber - Monthly Price - No 3 smoked sheet
Sing. USD/kg (1988-May 2018)
8
6
4
2
0
Feb-88
Mar-…
Apr-90
May-…
Jun-92
Jul-93
Aug-…
Sep-95
Oct-96
Nov-…
Dec-98
Jan-00
Feb-01
Mar-…
Apr-03
May-…
Jun-05
Jul-06
Aug-…
Sep-08
Oct-09
Nov-…
Dec-11
Jan-13
Feb-14
Mar-…
Apr-16
May-…
Jun-18


Tea Prices USD/Kgs 1988-Nov 2018
4
3.5
3
2.5
2
1.5
1
0.5
0
Jun-88
Jun-90
Jun-92
Jun-94
Jun-96
Jun-98
Jun-00
Jun-02
Jun-04
Jun-06
Jun-08
Jun-10
Jun-12
Jun-14
Jun-16
Jun-18

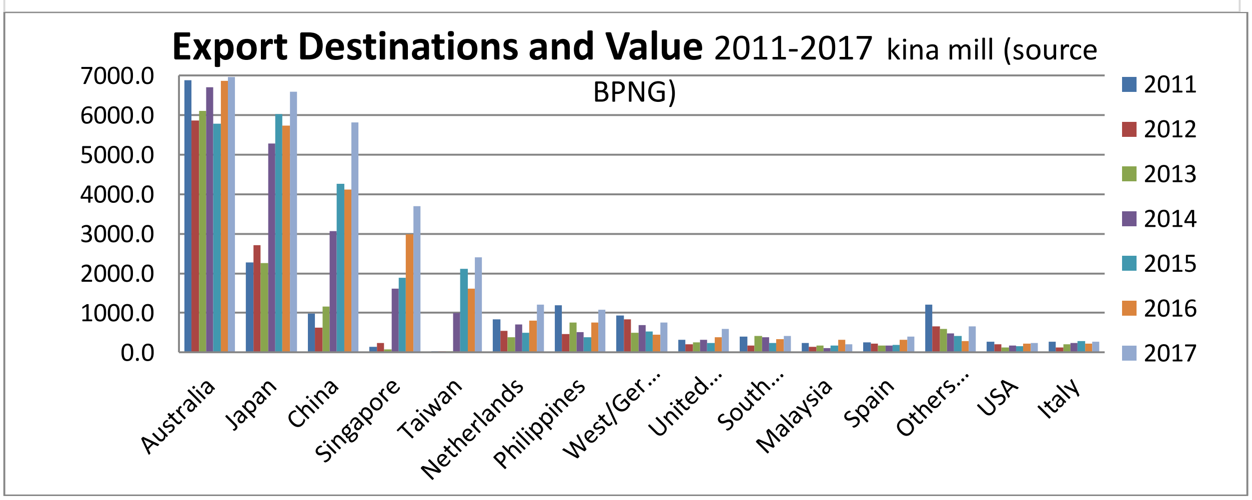

Sugar US Cts/kg (European and US Import Price)
June 1998- Nov 2018
Blue: US
1
0.9
0.8
0.7
0.6
0.5
0.4
0.3
0.2
0.1
0
Jun-88
Jul-89
Aug-90
Sep-91
Oct-92
Nov-93
Dec-94
Jan-96
Feb-97
Mar-98
Apr-99
May-00
Jun-01
Jul-02
Aug-03
Sep-04
Oct-05
Nov-06
Dec-07
Jan-09
Feb-10
Mar-11
Apr-12
May-13
Jun-14
Jul-15
Aug-16
Sep-17
Oct-18

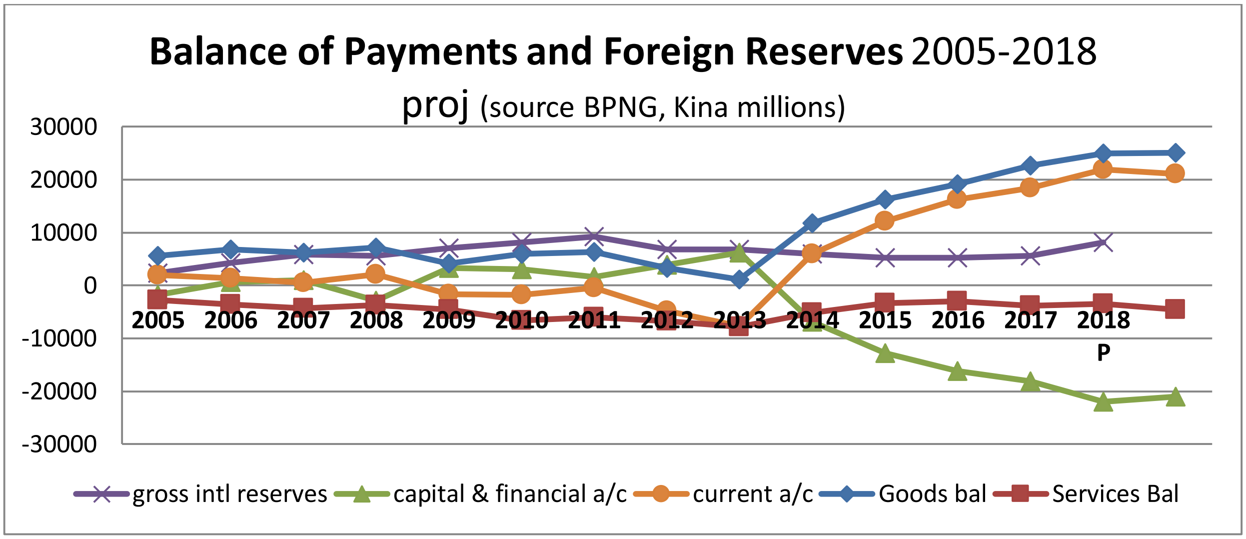

Rice (Milled White) USD per tonne
Dec 1991- Nov 2018 (Thailand -quote)
1000
800
600
400
200
0
Jun-88
Aug-89
Oct-90
Dec-91
Feb-93
Apr-94
Jun-95
Aug-96
Oct-97
Dec-98
Feb-00
Apr-01
Jun-02
Aug-03
Oct-04
Dec-05
Feb-07
Apr-08
Jun-09
Aug-10
Oct-11
Dec-12
Feb-14
Apr-15
Jun-16
Aug-17
Oct-18


Hard Sawnwood Price (red Meranti) - UK Port CiF US Dollars per M3
1988 - Novt 2018
1200
1000
800
600
400
200
0
Oct-88
Oct-89
Oct-90
Oct-91
Oct-92
Oct-93
Oct-94
Oct-95
Oct-96
Oct-97
Oct-98
Oct-99
Oct-00
Oct-01
Oct-02
Oct-03
Oct-04
Oct-05
Oct-06
Oct-07
Oct-08
Oct-09
Oct-10
Oct-11
Oct-12
Oct-13
Oct-14
Oct-15
Oct-16

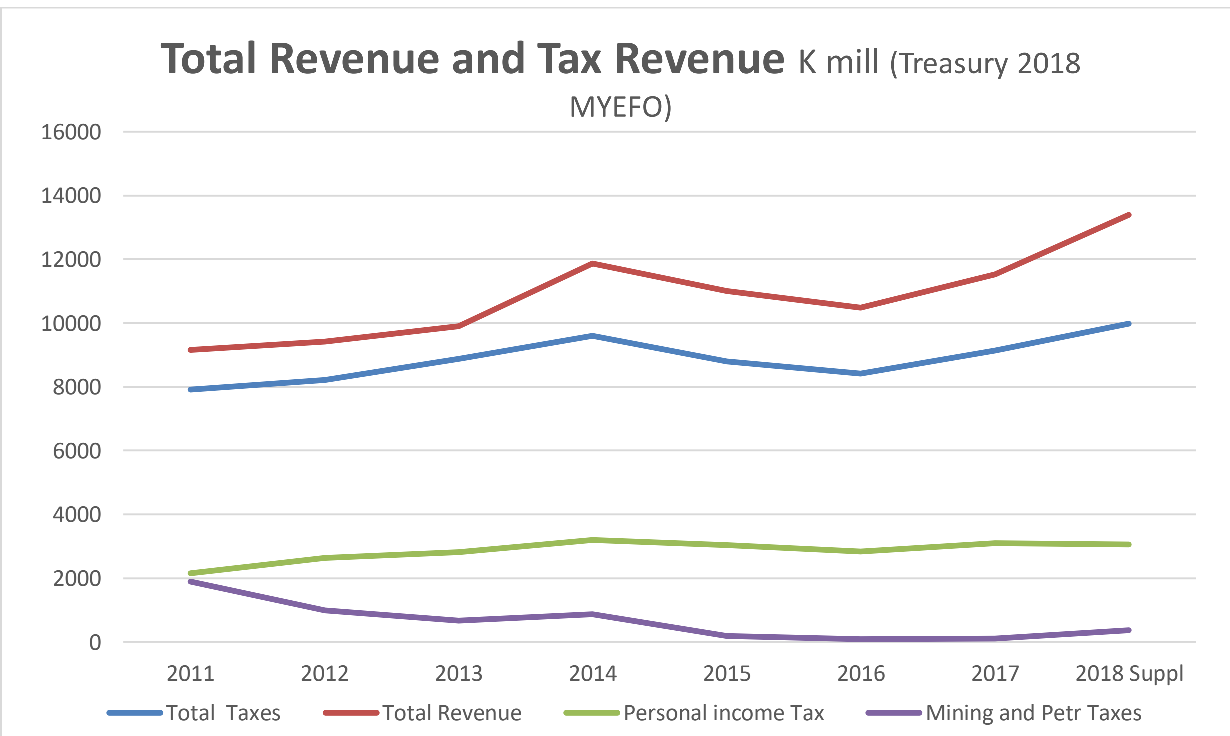
As highlighted here, extractive resource prices have largely shown firm partial recoveries, with gold strengthening further at the end of the year in the face of market instability, although nickel prices remain low, in contrast to cobalt's substantial, if volatile rise during the year. Prices for many of the major agricultural export (and import substitution) crops are low again, after some earlier recoveries during 2014-17. Kina prices have been safeguarded by the weakening kina, but producer incentives would be badly undermined if agricultural prices fail to strengthen and the kina were to strengthen significantly again, associated with extractive industry developments and revenue flows. The need for activating an effective and transparently managed sovereign wealth fund in a timely manner remains important, partly to stabilise foreign exchange flows, revenue and expenditure, both with respect to major new investments and existing projects, as outstanding project debt is diminished.

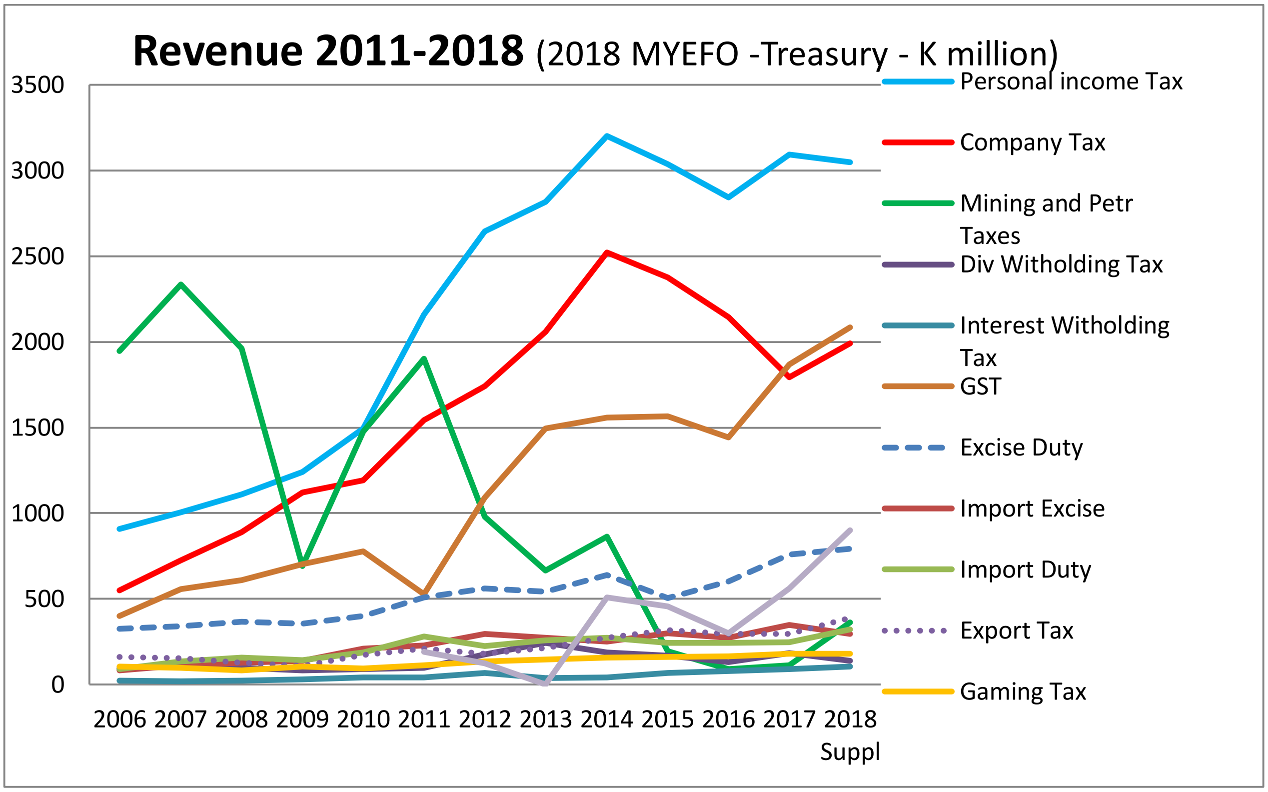
The commencement of the LNG trade has greatly altered the pattern of PNG's trade flow, with Japan, followed by China now coming close to Australia as export destinations by value. Many of the mineral exports to Australia are re-exported, as are some of the exports to China (timber etc) after further processing. East Asian demand for reliable and cleaner energy (notably LNG) is strong and growing, and PNG is competitive in terms of cost and delivery time and reliability, but it must still compete in an increasingly cut throat market and have supply available in an agreed timely manner to meet market demand. The trade imbalance, both for goods and services, is forecast to diminish from 2021, if major new resource projects (particularly Papua LNG) progress, requiring major, though temporary import flow, of equipment and skills.





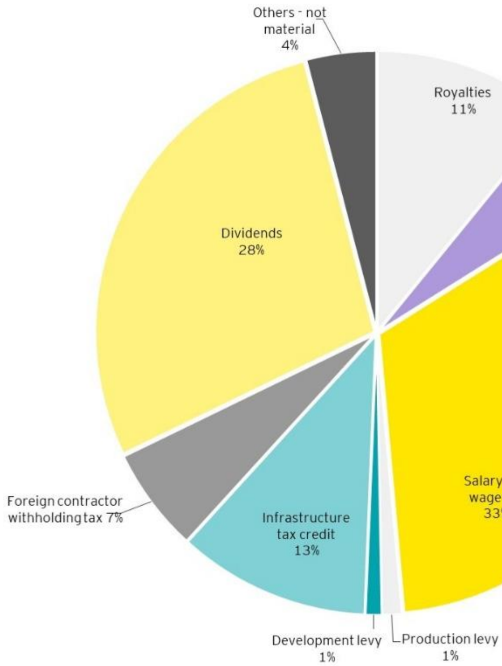
The steady decline of foreign exchange reserves, and accessible foreign exchange for the private sector to conduct ongoing business transactions and new investment, was supposedly slowing during 2017 and early 2018, although severe rationing was still ongoing, with a major backlog of debt to pay to suppliers, apart from payment of dividends and other transfers. In the 4th quarter of 2018 reserves were firmly boosted, however, by the successful international issue by the Government of the USD 500 million 10 year Sovereign Bonds, albeit at a relatively high interest rate of K8.375%, plus Budget support financing from the ADB and World Bank. This should provide some interim relief, but it's noted that Government department/agencies seemed to be in an intensive expenditure mode in December 2018, risking undermining the Treasury's efforts at expenditure restraint and drawing heavily on the newly-gained and borrowed foreign exchange.



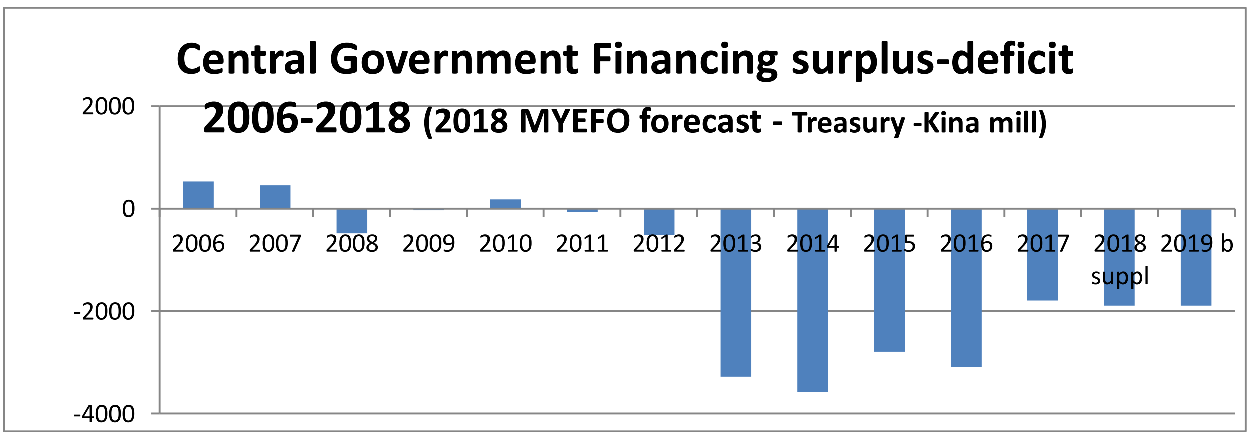


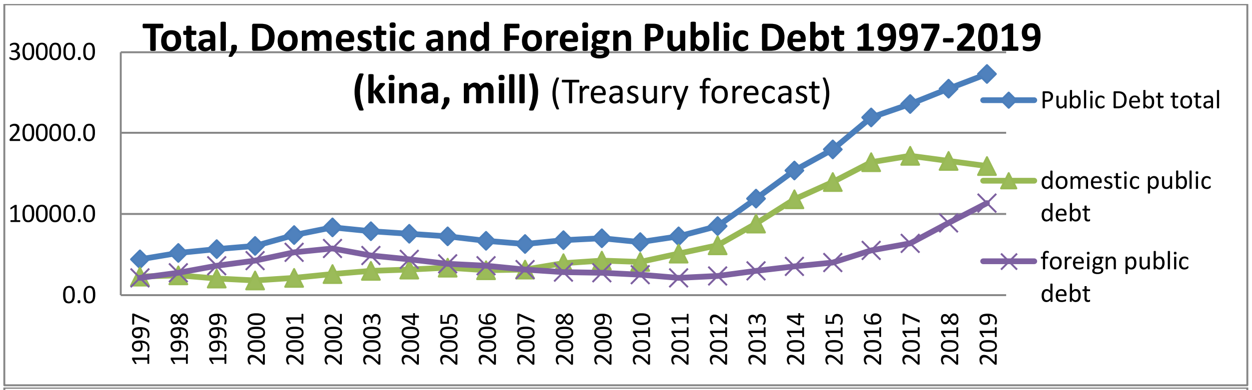
Revenue in 2017 and 2018 continue to be dominated by personal income tax, although the downturn in the workforce in recent years has constrained this source. GST has just overtaken Company tax as the second major revenue source, with business profits widely constrained by lack of foreign exchange and other business constraints, including greater competition from unregulated (and largely non-tax-paying operations). There was a valuable, if at this stage modest, recovery of tax revenue from the resource sector, although still only a fraction of the taxes paid by this sector prior to 2011, when output and exports were far lower. Dividend revenue from the extractive industries have been rising firmly since 2017, albeit requiring major prior public investment and in some cases heavy borrowing. Accountability over the proceeds and its prompt transfer to the State (as opposed to operating parallel, quasi-public expenditure) is critical, and partly being facilitated by the EITI process, chaired by the Treasurer, but including private and civil society participation including INA & CIMC.

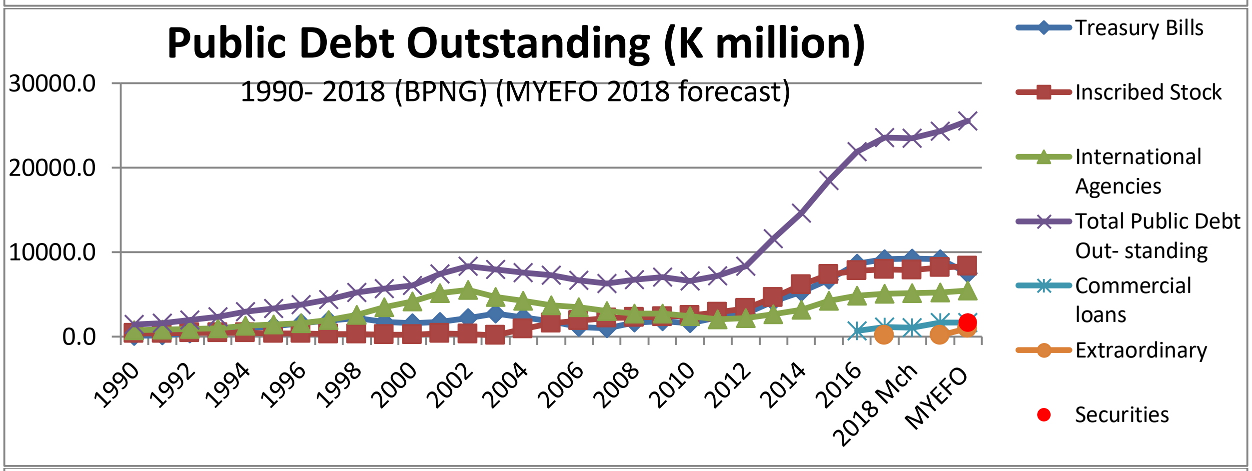
Revenue from Extractive Industries.

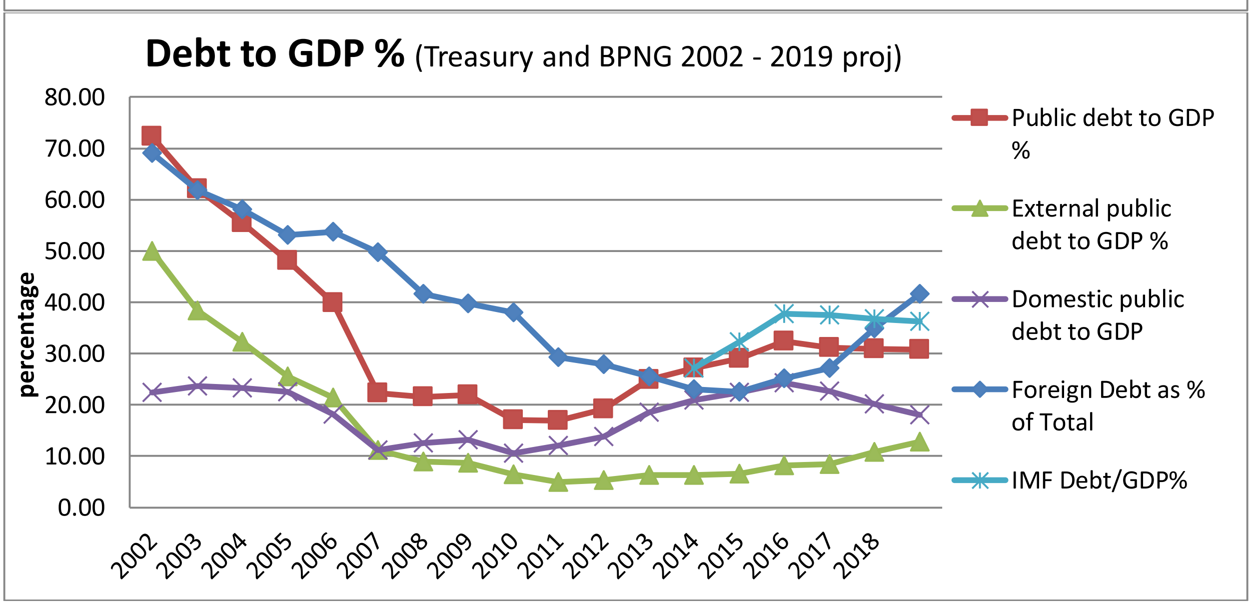


Source of Revenue from Extractive Industries; from draft 2017 EITI Report (prepared by E & Y); this highlights the surprisingly large portion of revenue from the extractive industries derived from employee personal tax (33%, as opposed to 23% in 2015) i.e. paid by the employees, as against from corporate income tax (5% plus tax credit of 13% in 2017; 8%, plus tax credit of 9% in 2015), with dividends having leapt @ 28% in 2017, albeit that in 2015 'equity distributions from the companies to the SOEs were recorded by E & Y as 42% of revenue, although not at the time reflected in the Treasury's revenue data anywhere near that level, (partly reflecting debt servicing obligations, but far from fully explained).





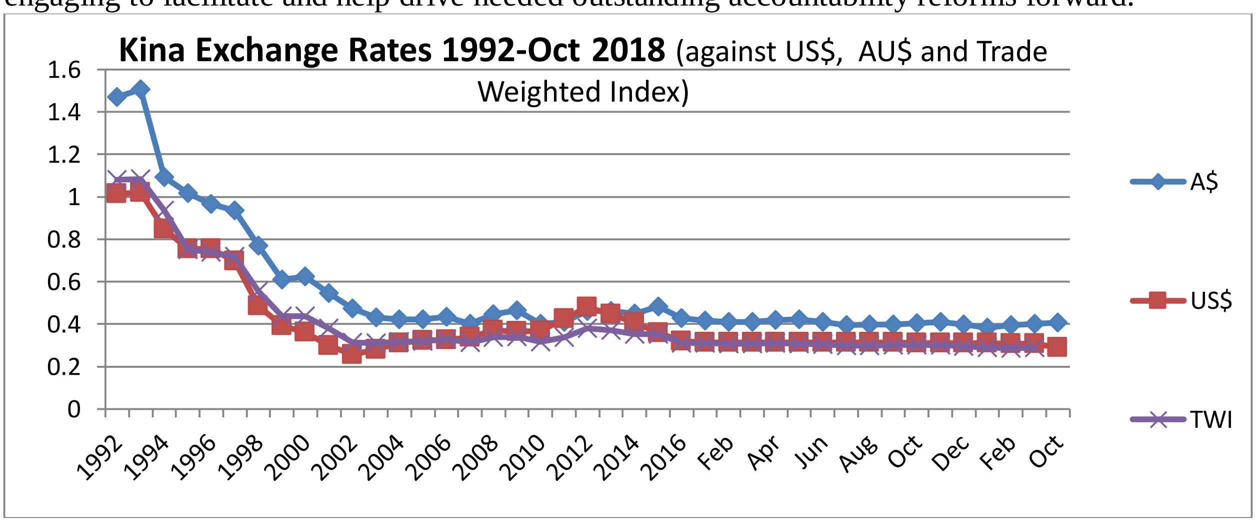




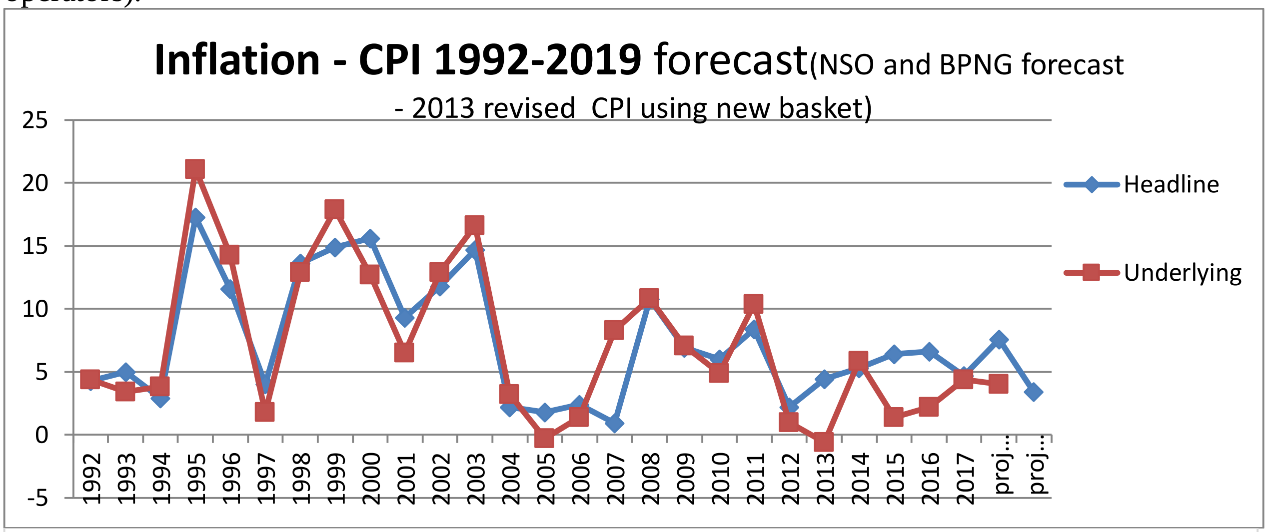
The Government has continued financing the Budget from borrowings since 2012. Deficit financing is a well-worn path, particularly seeking to sustain essential public goods and services and stimulate the economy during downturns in the economic cycle, notably consistent with Keynesian models for stimulating demand and employment and hence facilitating earlier recovery. In this regard, it is really important to ensure the expenditure is well targeted and utilised accountably, particularly on activities which really do facilitate economic activity, including core infrastructure, job creation, as well as investment in human capital. That was clearly partly the aim, but unfortunately the financial accountability mechanisms in PNG have long been weak and links between planning and output tenuous, while far too much was diverted to relatively unproductive status projects, which did generate some short term economic activity, but little beyond, whilst leaving extensive ongoing infrastructure maintenance obligations.

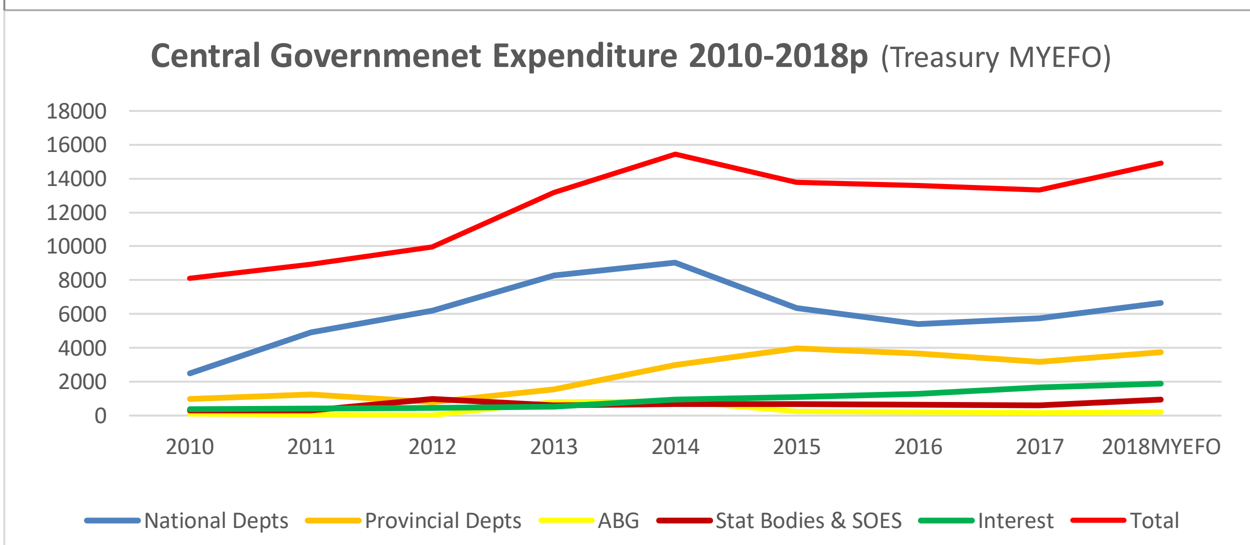
Although debt to GDP may fall within the revised authorised ceiling of 35% of GDP (it lies above this level if the revised official NSO GDP figures are used, as they are by the IMF, and would certainly do so, if other liabilities are included), these figures are largely artificial, as it's the actual financing capacity of the State, rather than GDP that's critical. PNG's GDP has grown substantially since 2010, but its revenue have trailed far behind for various reasons, with a very low tax revenue efficiency rate in relation to overall economic activity, including because of low formal sector employment rates, but also low contributions by many formal (and unregulated) corporate entities, including in the extractive sector, at least during initial production years. The capacity to manage a growing overall debt level, which is now also imposing major debt servicing costs on the annual budget (at around K2 billion for 2018 and rising) depends on that capacity not only to grow the economy but also to ensure a sound and steady revenue flow, without imposing an undue burden on business and households, which in turn would act as a disincentive on business and investment. This also requires that the State can manage its revenue effectively, including in delivering the infrastructure and other public goods needed for a dynamic economy.

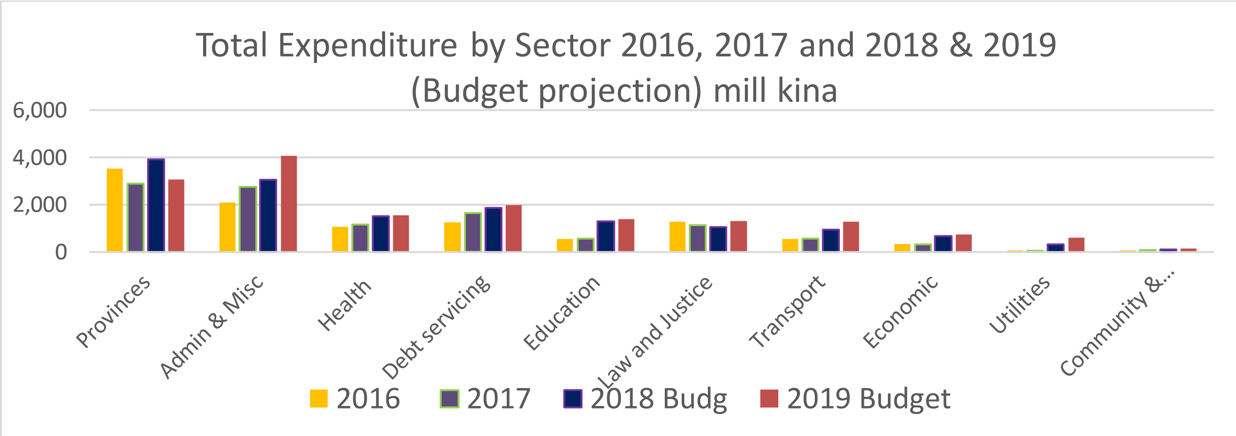
In 2018 the Government did introduce various policy and planning initiatives, combined with new governance and tighter financial management systems (from the new Medium Term Development Plan 3, to the new Public Procurement requirements, further roll-out of the IFMS and the approval of the Open Government Partnership National Action Plan 2018-22). Some sound initiatives were introduced in 2017 and the 2018 Budgets to improve oversight of public funds managed by SOEs and NSAs, albeit with aspects of the measures also potentially undermining the operational capacity of Regulatory Authorities, unless applied more constructively. However, at the end of the day, these governance initiatives are only as good as the actions actually taken, which need to followed closely, with Non-State Actors and commentators, including INA and CIMC, actively engaging to facilitate and help drive needed outstanding accountability reforms forward.

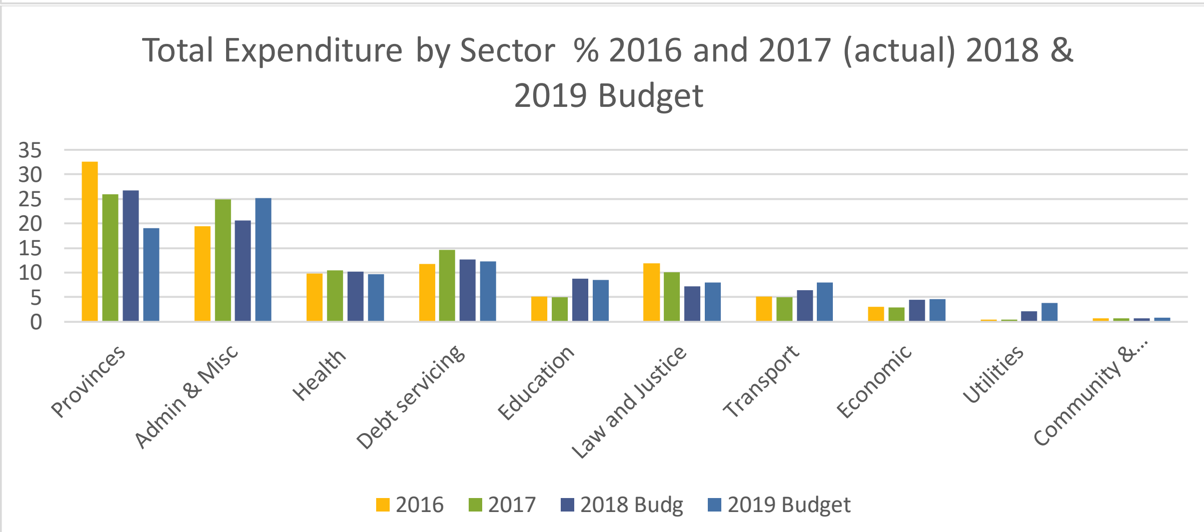


The exchange rate against the USD has weakened to about a quarter of what it was in the early 1990s, albeit only declining relatively slowly and steady during 2016-2018, largely as a result of the restraint on foreign exchange access and other interventions by the Bank of PNG. Many economists favour a move to a freer market adjustment, leaving the kina likely to fall significantly further initially before finding its own level, and thereafter restoring confidence and potential investment and reinvestment. The Central Bank is cool towards this approach on the grounds of discouraging inflation and driving up living costs, and that the market (local production) is barely stimulated in PNG by lower exchange rates, and why let the currency fall, when the situation may be reversed shortly with major new investments and when revenue flows finally make their way back, as PNG LNG debt is progressively paid off. It must be recognised, however, that the weaker exchange rate in 2018 has helped offset the fall in agricultural commodity prices in kina terms, providing some needed relief to producers (and other exporters/import substituters and tourism operators).





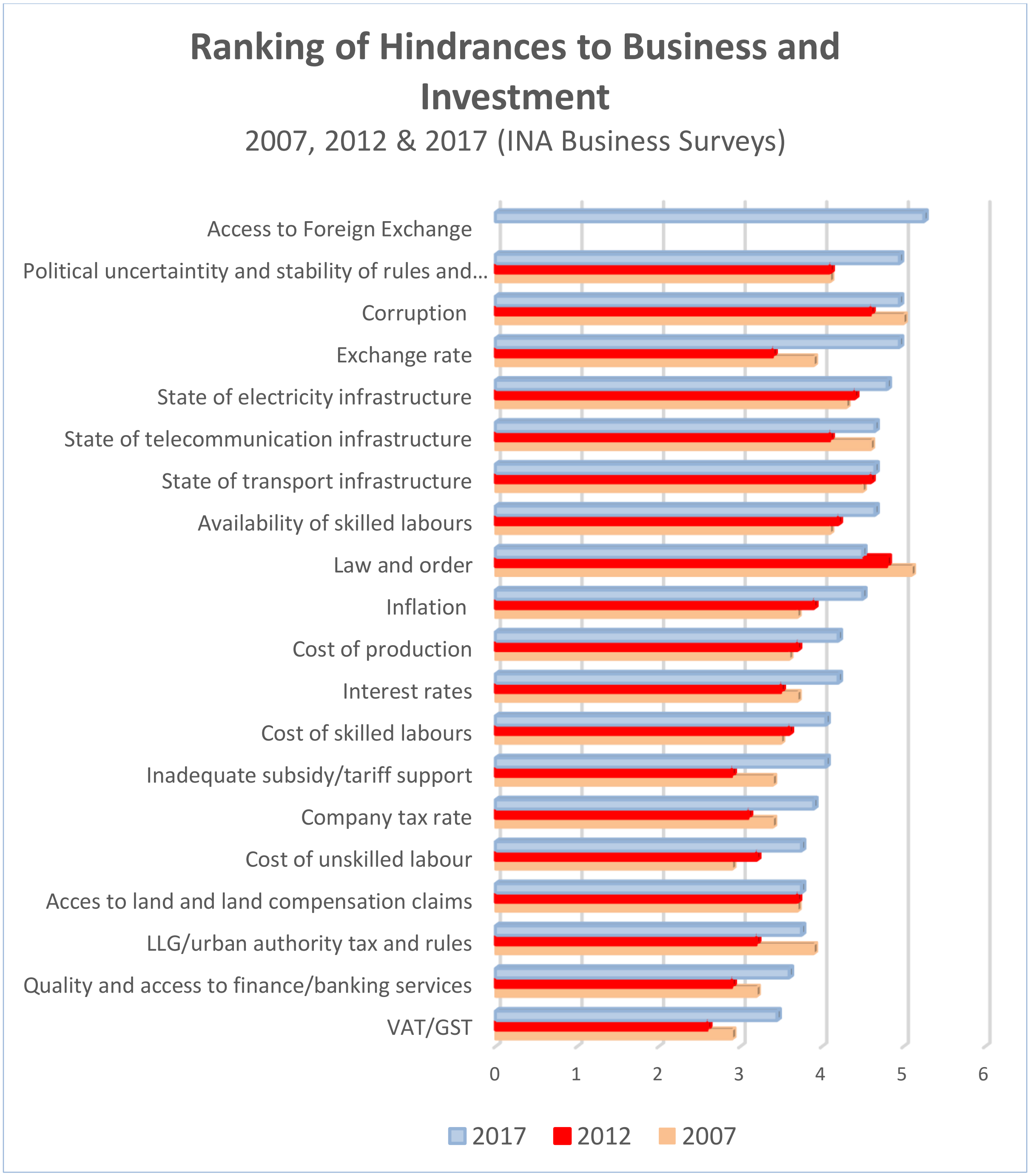




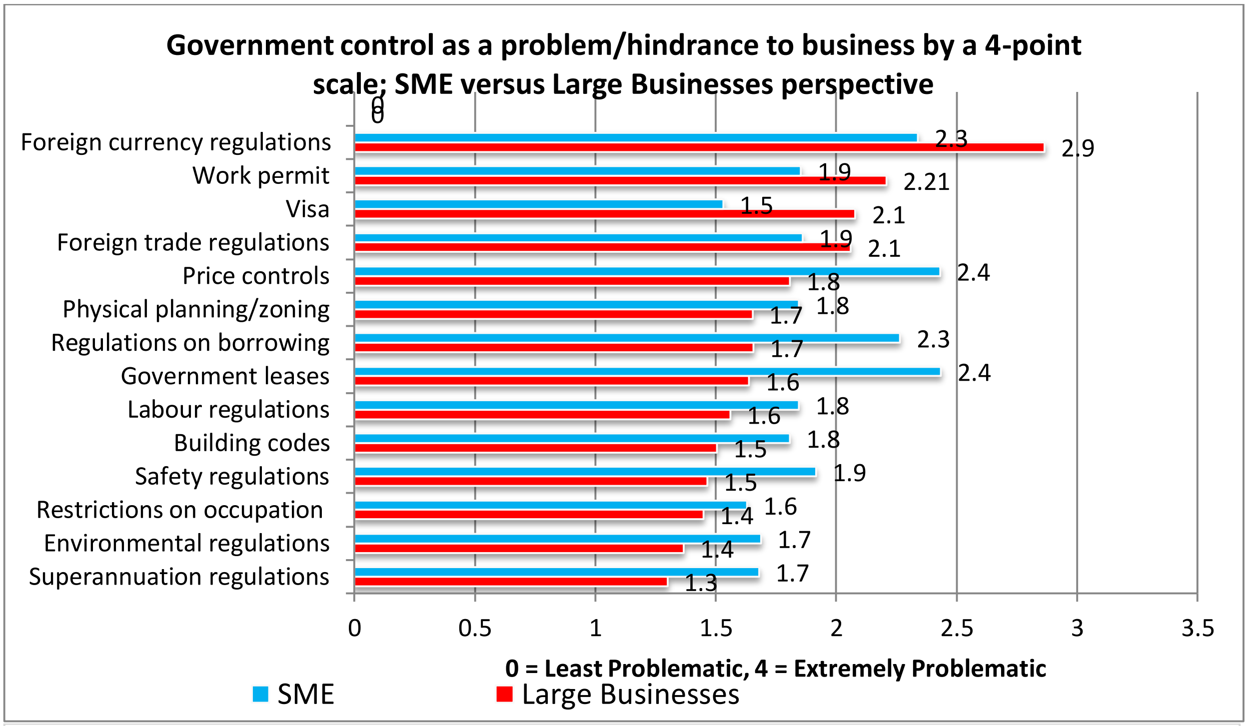
Administration, including DSIP (reallocated for recording and disbursement from the centre), debt servicing, certain major Departments and the provinces are taking the lion's share of expenditure, with an overdue boost for transport and law and justice in the 2019 Budget, but less funding for health and education, both in desperate need for more funding, including better expenditure planning and tracking, but also coordination with infrastructure restoration and development. District expenditure remains the weakest link; critically important, but with the weakest planning, implementation and oversight capacity, and a DSIP/DDA system heavily controlled by the MP, if he's able to access the funds, the output over the years has been poor and unsustainable, with little value for money, in most districts. Strengthening districts demographic and other critical planning data, management and accountability systems, including community awareness and engagement is critical to ensuring greater utility and improved services at district levels. With a heavy focus over the years of public expenditure in NCD, much core infrastructure and services are concentrated in the capital, including 45% of doctors, leaving most of the country and whole districts devoid of even basic facilities. Clearly, providing equal services across the country is inconceivable, but balancing the provision, and raising accountability mechanisms at local levels would enable a more balanced economic and social growth, utilising resources where the people live, rather than driving high levels of urban migration, in the absence of formal sector skills and employment opportunities.

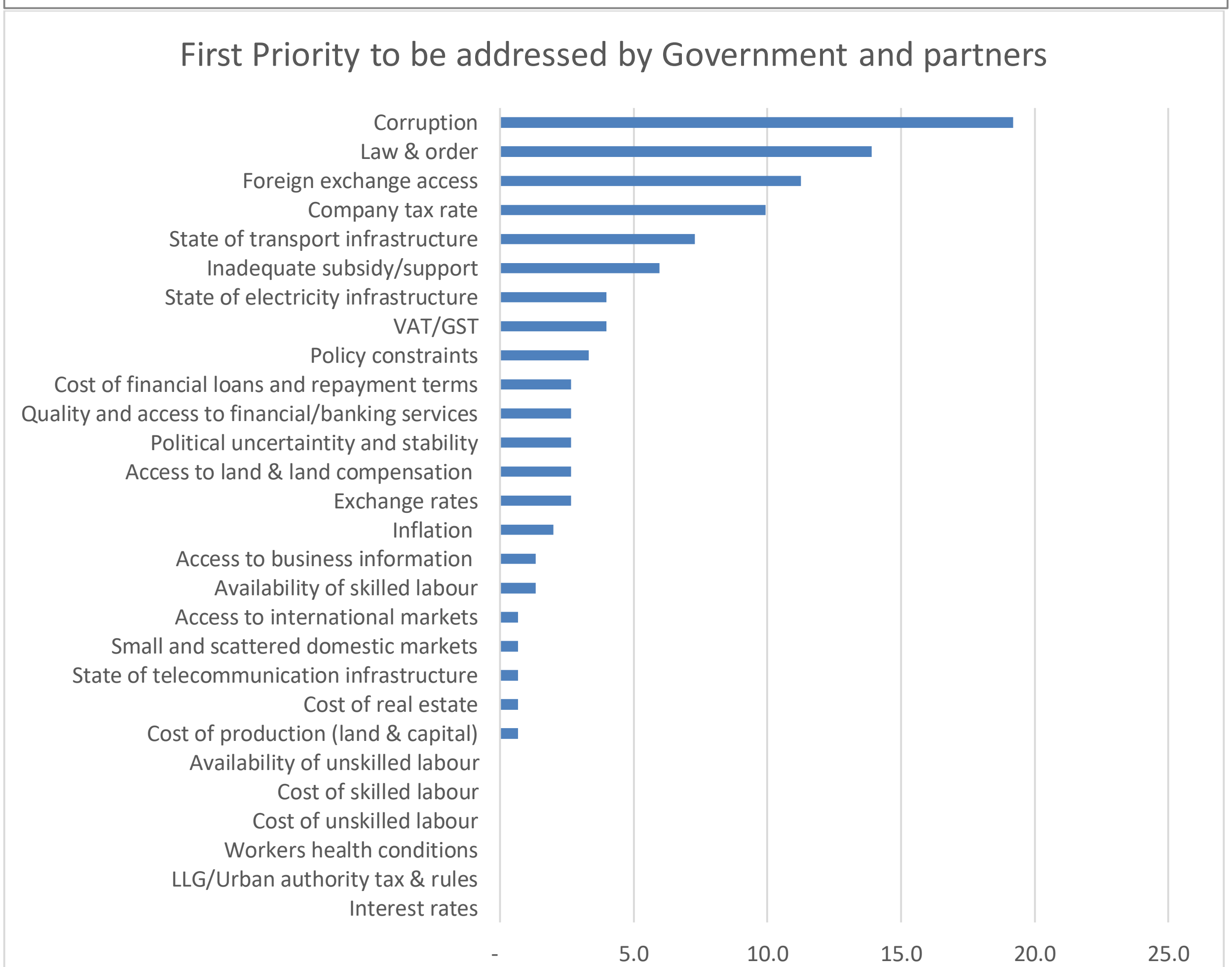
2019 will see the Government driving forward, or reluctantly progressing a variety of decentralisation initiatives, some of which conflict with each other and have limited apparent rationale, other than political expediency. So there is the Bougainville referendum and all the ensuring economic and fiscal (as well social/environmental) challenges for Bougainville if they choose independence, including how they secure revenue, whether or not to proceed with large scale mining and by whom, and its potential threat to the non-mining economy, which drives employment and broad-based income earning opportunities. There are associated regional security concerns associated with a new weak economic state falling into powerful hands.

New autonomous governments may be rolled out, on the basis of strong administrative capacity, as with part of ENBP, but on less explicable grounds for New Ireland and Enga provinces, at least in terms of governance, although more understandable on simple political grounds. The roll out of DDAs and where the future of LLGs lie will be critical to most ordinary people's lives. Current administrative systems are overlapping and undermining effective governance and service delivery. It may not be possible to design or redesign the most appropriate systems, but at least it is critical to ensure that whatever system is applied, is given the best opportunity to be effective and accountable. INA and CIMC are both engaged in various initiatives to improve information and accountability mechanisms at district levels; (largely comprising ideas, but some actions in the field, notably with budget tracking over several years, albeit with very limited current funding)



Ranking of Hindrances to Business and Investment
2007, 2012 & 2017 (INA Business Surveys)
Access to Foreign Exchange
Political uncertaintinty and stability of rules and...
Corruption
Exchange rate
State of electricity infrastructure
State of telecommunication infrastructure
State of transport infrastructure
Availability of skilled labours
Law and order
Inflation
Cost of production
Interest rates
Cost of skilled labours
Inadequate subsidy/tariff support
Company tax rate
Cost of unskilled labour
Acces to land and land compensation claims
LLG/urban authority tax and rules
Quality and access to finance/banking services
VAT/GST
0
1
2
3
4
5
6
2017
2012
2007


Government control as a problem/hindrance to business by a 4-point scale; SME versus Large Businesses perspective
Foreign currency regulations
Work permit
Visa
Foreign trade regulations
Price controls
Physical planning/zoning
Regulations on borrowing
Government leases
Labour regulations
Building codes
Safety regulations
Restrictions on occupation
Environmental regulations
Superannuation regulations
2.3
2.9
1.9
2.21
1.5
2.1
1.9
2.1
2.4
1.8
1.7
1.8
2.3
1.7
2.4
1.6
1.8
1.6
1.8
1.5
1.9
1.5
1.6
1.4
1.7
1.4
1.7
1.3
0
0.5
1
1.5
2
2.5
3
3.5
0 = Least Problematic, 4 = Extremely Problematic
SME
Large Businesses


First Priority to be addressed by Government and partners
Corruption
Law & order
Foreign exchange access
Company tax rate
State of transport infrastructure
Inadequate subsidy/support
State of electricity infrastructure
VAT/GST
Policy constraints
Cost of financial loans and repayment terms
Quality and access to financial/banking services
Political uncertaintity and stability
Access to land & land compensation
Exchange rates
Inflation
Access to business information
Availability of skilled labour
Access to international markets
Small and scattered domestic markets
State of telecommunication infrastructure
Cost of real estate
Cost of production (land & capital)
Availability of unskilled labour
Cost of skilled labour
Cost of unskilled labour
Workers health conditions
LLG/Urban authority tax & rules
Interest rates
-
5.0
10.0
15.0
20.0
25.0

The 2017 INA Business Survey, which was released in 2018, provided clear indications of constraints to business and investment in PNG, and priorities to be addressed. Access to foreign exchange, which had been a relatively low concern in previous INA surveys, had come to the fore in recent years, particularly by larger businesses. Interestingly, the foreign exchange constraint was still considered a temporary glitch, which should be addressed relatively promptly; therefore, in terms of priorities for action it was only ranked third, with the main focus by businesses remaining, as from previous INA surveys, on addressing governance, corruption and law and order issues, which pose such an ongoing problem, which severely restrain business and employment opportunities in PNG, yet which seem so intractable, apparently in the face of lack of determined and coordinated action, yet, as, seen in some other countries, can be addressed with the right focus and measures. The other major concerns were the inadequate state of basic power, communications and transport infrastructure, and inadequate availability of skilled workers. As priorities for action lowering the corporate tax rate was a priority.

All these factors, from lack of foreign exchange, to poor public goods and high costs of power and internet, law and order problems, relatively high tax rate and inadequate available local skills, all add to the cost and uncertainty of doing business in PNG, undermining potential viability and hence discouraging needed diverse investment. PNG cannot compete with East Asia for many products, but by progressively improving public goods, increasing competition, where practical, lowering costs and risks to businesses (and households) then the opportunities for new and more diversified businesses in goods and services grow.