

## **New Economic Scenario, Hazards and Requirements**

PNG is facing substantially changing economic conditions and opportunities, providing new challenges and difficulties. The driving forces are largely external, but how government, private sector and the whole community respond will determine the impact, and whether the country's population ends up winners or losers.

PNG is a major net beneficiary of the higher commodity prices for minerals and oil of recent years, driven by increased raw material demand particularly from China and India. This has pushed up PNG's growth rate (encouraged also by other stimuli, including more stable economic management, certain reforms, partial competition and increased investment in telecommunications). Over recent months various agricultural prices have also risen, some substantially, also shored up by increased Chinese/Indian demand, e.g. for rubber with growing car ownership, and demand for bio-fuels (produced from oil palm, sugar and other crops) supposedly providing cleaner/greener energy, substitutes for the greenhouse-gas producing fuels, notably oil and coal.

PNG's growth rate has risen from low, even negative real rates earlier this decade, to an estimated 6.2 % in 2007 and forecast at 6.7% in 2008. With PNG's high population growth rate (at perhaps 2.7%) these nevertheless remain minimum growth levels required if economic development opportunities are to be extended through the economy and community. This higher growth rate and increased revenue, largely from mineral taxes were, however, considered unsustainable, unless more substantive structural reform is achieved, as the country's economy remains so dependent upon fickle commodity prices and a few major projects, like Ok Tedi and Kutubu oil, largely nearing the end of their commercial lives.

The looming (perhaps prevailing) recession in the US may impose restraint on commodity prices, although some of PNG export products are bolstered, with gold deemed a safe refuge during US dollar weakness, and oil by uncertainty over future supply. Current improved prospects for an LNG project in PNG (and possible associated on-shore processing) have improved the outlook for sustained economic growth and revenue, whilst the growing agricultural prices, including demand for bio-fuels (and from carbon trading) provide further opportunities for rural areas, if substantial preconditions are met.

With net winners and losers amongst countries from higher commodity prices, there are also potential winners and losers within PNG. For years PNG has missed economic opportunities, often owing to inconsistent policies, government mishandling and corruption, whilst other countries have been more nimble. It is critical that government now works with the private sector and civil society bodies to face the challenges, ensure sound opportunities are grasped, whilst avoiding or minimising negative social and environment repercussions.

The risks include: failure to prepare adequately and benefit from this major prospective (LNG) project, and other prospective natural resource projects, and/or puts too many eggs in one basket, allowing them to distort the whole economy unduly, undermining prospects for diversification (notably agriculture and tourism), pushing up real exchange rates, wages and expectations, undermining competitiveness, and driving wider inflationary effects. LNG will change PNG's

economic opportunities, but, as with other mineral projects, opportunities will largely be in enclaves, including main cities, whilst PNG requires a diversified economy providing economic opportunities for the majority, unable to participate directly in enclave ventures.

Surging recent agricultural prices provide the potential for small and largeholder producers to make a good return from investment in intensifying or expanding and diversifying agricultural crops, if prices are sustained and exchange rates don't appreciate unduly. Whilst PNG has a large portion of its population in rural areas, many are not in a position to benefit from improved prices, whilst there are significant segments of the population adversely affected by higher food prices.

PNG is poorly prepared to take advantage of opportunities. Infrastructure, education and health services are poor and run down, particularly in rural areas, and excessive impediments to investment and business, including changing policies, inefficient and corrupt public administration, excessive red tape, and inefficient monopolies running utilities and services.

Transport infrastructure was poorly developed before Independence, but allowed to wither subsequently, particularly over the past 20 years, and since the introduction of catastrophic Organic Law on Provincial and LLG. Likewise the education system was inadequately developed before Independence, with inadequate coverage, including trainees for professional and management positions for the new State. Inadequate subsequent resources for education and training have resulted in low entry, retention and standards and inadequate technical and practical life skills training. The virtual disappearance of rural sea and air services, (partly owing to high fuel costs and discontinuation of government charters) combined with unavailability of extensive rural health services has resulted in thousands of unnecessary deaths, and remoter areas virtually abandoned by the State.

One positive recent advance for rural people has come from the (limited) competition in mobile phones, allowing better rural access and empowerment including to participate in economic opportunities (but Govt continues to deny opportunities for its citizens by preventing investment and full ICT competition, including affordable internet for schools and rural information centres and mobile phone banking).

Now, whilst increased revenue allows funding for restoring and upgrading rural infrastructure and services, lack of administrative capacity, cronyism in public sector appointments and an unsuitable system for district planning and fund management (with MPs unduly controlling funds), bureaucratic corruption, inadequate funding for official watchdogs and lack of community information and oversight, results in extensive abuse. The Treasury is providing improved Budget information and reporting, but there's been inadequate management and control of the "development budget" and "windfall" allocations (which are heavily under-spent in the priority service areas). More emphasis is required on core government functions, requiring adequate but better targeted recurrent funding. Unduly conservative budget forecasts fuel excessive windfall allocations, where capacity is especially weak, rules fluid, oversight inadequate, whilst greater upfront debt reduction would be a better investment for the future (until reforms and capacity are in place).

PNG has long seen winners and losers from development. The winners (like some resource owners and urban political-bureaucratic elite) have been hoarding the benefits, whilst growing numbers are becoming marginalised, largely by living in remoter locations or from vulnerable backgrounds. Leaders should be taxed in relation to entitled earnings, rather than simply reported income. Higher agricultural prices provide opportunities for producers (the majority), but squeeze consumers on fixed or marginal incomes. Those without land or access to markets miss out (older men often hoard land, not releasing it to younger unmarried men and women).

Whilst PNG's wantok system is one of the most vibrant customary social support systems operating worldwide, enabling transfers between those with greater access to resources and those without, it is increasingly under stress, with families struggling with increasing numbers of relatives or distant wantoks. Thousands should be commended for their service to relatives and the wider community. But there are growing numbers of orphans and other vulnerable children. Higher fuel prices and lack of earning capacity in remoter areas, and collapse of govt systems has left hundreds of thousands in PNG without access, un-serviced by planes or boats let alone roads, without access to health or other support. PNG has a growing underclass and people in poverty or at high risk, contrasted with the growing affluence in some urban areas. Specific measures to these growing disparities, which run counter to the objectives of PNG's enlightened National Constitution, must be provided.

Government, private sector and the community have big tasks ahead:

1. to get the economy moving and providing wider opportunities requires:
  - Restoring and maintaining rural (and urban) infrastructure, which includes ensuring all-weather roads and other transport requirements, but also providing adequate and hygienic market facilities (notably for fresh produce etc)
  - Tackling law and order problems (largely through generating formal and informal employment, implementing Police Review Recommendations, improved management, training and oversight and strengthening community police, mediation and justice capacity)
  - Removing unnecessary red tape and other impediments to business, including the informal sector (particularly addressing corruption now widely pervading public sector functions, including land administration, police, migration, and extensive other parts of the bureaucracy, including central agencies and utilities/SOEs etc)
  - Ensuring immediate open competition in information and communications (including mobile telephony and airlines) to encourage investment, extending reliable and affordable services, whilst providing fair and impartial supervision of competition and the application of suitable standards
  - Government withdrawing from competitive and commercially viable business activities (including ICT), but selling these businesses transparently and competitively, whilst developing Public-Private Partnerships over utilities, or other needed but non-fully commercial enterprises.
  - Maintaining fiscal restraint, reduce debt, but provide adequate funds for core recurrent expenditure (away from poorly planned/managed/overseen special funds, or "slush funds")

- Maintaining sound monetary management, restraining inflationary pressures and avoiding currency appreciation, which would jeopardise opportunities for diversification and wider income earning/employment
  - Even with LNG proceeding, the focus must be encouraging diverse and sustainable economic activity (beyond the life of temporary mineral resource projects)
  - Provision of an overall Human Resources Development study/plan, identifying skills needed and short-longer term education and training requirements to meet the country's future economic and social needs. A whole-of-education approach is required, meeting universal primary education needs but balancing this better than in the past with the need to meet professional and technical requirements, including major restoration and upgrading of tertiary capacity, to provide the required calibre of teachers for schools and technical skills for potential growth industries and the public sector.
2. Capacity building for government to perform its core functions, requiring:
- immediate short term and longer term measures, including major strengthening of training capacity, restoring regional training colleges and collaboration with the private sector, interim use of outside managers/mentors/trainers, where necessary, in various public sector bodies (including education and training institutions, finance and public administration, law and justice bodies, internal revenue, public watchdogs, etc)
  - Public sector reform, including independent oversight in selection (and suitable conditions for) professional district administration, rationalisation of institutions and focus on core functions (infrastructure, core services, health and environmental regulatory conditions, some R &D, information dissemination and culture), public accountability, streamlining of appointment and dismissal procedures, capacity to retain performing older professionals, whilst developing private sector secondment/exchanges, and ensuring steady new quality intake to provide needed continuity.
  - priority to preventing and tackling corruption – not necessarily establishing new institutions, but providing adequate resources and reinforcing existing ones (for investigations and prosecution), ensuring their independence and impartial oversight of public sector bodies at all levels (including by legislators, through an effective PAC, working with a strong Auditor-General's office), and encouraging inter-agency anti-corruption coordination, and adequate penalties are in place in the legislation and applied through effective investigation and prosecution capacity
  - addressing the current inadequacy of provincial/district administration (following the 1995 OLPLLG), by consulting, agreeing and applying a publicly supported system or systems (one size may not fit all). This system must be administratively simple, effective and accountable; perhaps shifting elected political participation largely to the District level, with planning and administrative coordination at the provincial level.
  - upgrading effective provision of other core Government functions, including practical research (agricultural, marine, health etc), information dissemination to empower households, including small farmers and businesses, to improve their lives and welfare, and take advantage of economic and human development/health and welfare opportunities.

3. Addressing the needs of the disadvantaged and vulnerable: a major focus is required to empower and address the needs of those (particularly vulnerable children) increasingly marginalised by the current development process, or from prevailing diseases (including HIV/AIDS) leaving orphans and other vulnerable youth.
  - this should reinforce and reduce pressure upon, rather than undermine, the wantok system to care of people, helping the more vulnerable gain a step on to ladder to access opportunities and services, especially health and education
  - it will require adequate funding from the State, probably initially with significant international technical and financial assistance
  - provide improved opportunities, facilities and training for (male and female) informal sector participants, including opportunities to graduate to the formal sector through simpler procedures and skills support
  - train and employ more welfare staff, and be prepared to allocate more substantial funding for welfare support, to counter social marginalisation and empower people to participate in PNG's growing economy and society
  - restore a system of government air and boat charters (including rural transport subsidies), as a component of a programme to restore services back to remoter rural communities.