from remarks made by World Bank Country Manager for PNG Laura Bailey on the occasion of the 31 March CIMC Workshop on "Impact of LNG on the Agriculture Sector"

I have been asked to make a few remarks on the international perspective on avoiding the resource curse and managing mineral wealth. My esteemed colleagues from the Central Bank and Treasury have already given you some of the key points that are relevant here, so I won't repeat those key messages. Instead, I'll focus on why international experience tells us we need to pay attention to this mysterious 'resource curse' and why I think that's especially important for agriculture.

First let me offer you four numbers: I won't explain them now, but I will come back to them – I promise:

- 400%
- *minus* 60%
- 85%
- 2

What's this resource curse? Well, it refers generally to the sad reality that many more countries who have found and exploited minerals have ended up worse off, rather than better off, in terms of human and economic development indicators. To add insult to injury, on top of not getting sustainable improvements in lives and livelihoods, they have often suffered from corruption and poor governance which seems to feed on minerals-led growth. History and experience around the world tell us it's not impossible to generate sustainable equitable inclusive development using money from oil gas and minerals – it's just really hard.

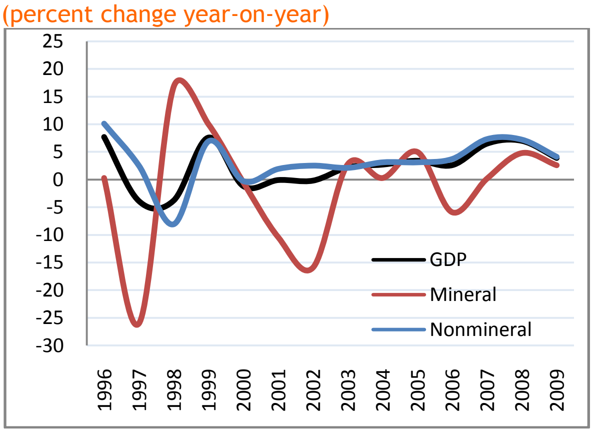
So why is this especially relevant to the agriculture sector? First, just to remind everyone: the World Bank Group cares very much about the agriculture sector, which is we have two major projects in the sector covering three of the four largest export crops: coffee, cocoa, and oil palm.

OK, so what's the connection between the resource curse and agriculture? Well, it's this strange thing called "Dutch disease" – and I won't go into too much detail because the Governor and the Deputy Secretary have done that already. [*That term refers to the rapid increase in wealth due to a positive shock either from large inflows of foreign capital most usually from either a resource discovery or a surge in the price of a commodity export. If the inflow of foreign exchange is converted into domestic currency and boosts spending in the non-tradable (services) sector, the real exchange rate appreciates ("spending effect"). At the same time, productive resources will shift to the non-tradable sector and the booming mineral sector, shrinking the non-mineral sector ("resource movement effect").*]

While there may have been evidence of Dutch disease in Papua New Guinea in the late 1990s, it is hard to find such evidence in recent years. In 1998-2000, mineral export prices rose, the real exchange rate appreciated and growth in the non-mineral sector lagged that of the mineral sector. In 2004-08, however, when mineral export prices were accelerating and the real exchange rate was strengthening, growth in the non-mineral sector led that of the mineral sector, as we see in the figures below.

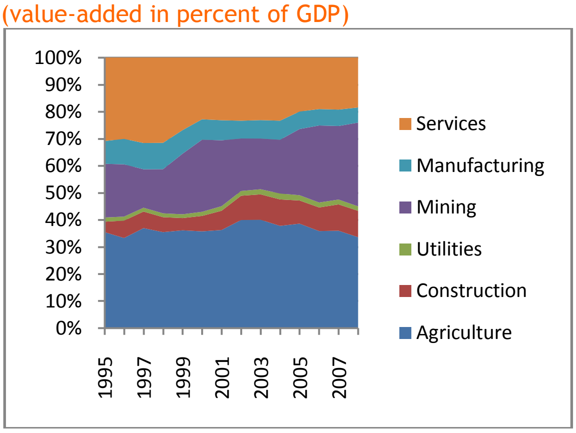
The evidence on mineral versus non-mineral sector growth is mixed ...

(percent change year-on-year)



... although the mineral sector continues to dominate manufacturing and services

(value-added in percent of GDP)



Source: PNG authorities and Fund/Bank staff calculations. *Source:* PNG authorities and Fund/Bank staff calculations.

Does this mean, as some have suggested, that PNG "structural immunity" that protects it from Dutch disease? Certainly not: it was all about Government making sensible choices, and an economy that was growing in a more balanced way than before. Acyclical macroeconomic policies on minerals revenues during that period combined with robust contemporaneous growth in the non-mineral sector, and that balanced out the potential damage that booming commodity prices could have inflicted on the non-minerals sector through the exchange rate.

So can't we just continue with prudent acyclical macro policies and rely upon the choices made by the Central Bank and GoPNG to save us? Won't the non-minerals sector just automatically keep growing even more, thus protecting us from Dutch disease and avoiding any harm to the agriculture sector? Well, the short answer is no, for two reasons:

- the magnitude of the increase in minerals revenues from the oil and gas sector is of such a scale that the challenges grow significantly, no matter how prudent the macro policies,
- AND the growth in non-minerals sectors was led by manufacturing and services, not by agriculture. In fact, agriculture's share of the economy has been stagnant for almost 20 years, even though with current population growth rates the 85% of the population who live in rural areas and depend on agriculture and rural ag-related service jobs is actually a much larger number of people.

We just haven't seen the kind of diversification that we need in the agriculture sector, in terms of getting better quality premiums for commodity exports, exploiting niche markets, and capturing more value-added by doing more transformation of commodities into processed products.

Fine, so can't we just sequester a share of the minerals revenue and use it to finance Government to subsidize or direct the agriculture sector? No, because all of the things that we want to see happen – quality premiums, niche products, capturing value-added through agribusiness investment – all of those have to be responsive to and led by consumer demand and market forces. Countries that have pursued a role for the state as **enabler** and supported communities and businesses in grabbing the opportunities that consumer demand provides have received large economic gains.

OK, so now let me come back to those four numbers

- 400% is the increase in per capita income that is aspired to in the 20-year Development Strategic Plan of government
- 16 billion is the size of the PNGLNG project in terms of total value of production over it's life
- 85% is the share of Papua New Guineans who live in rural areas and are involved in the agriculture-led economy

- 2 is the number of countries worldwide who have managed **similarly dramatic growth** in minerals revenue over a **similarly short time period** <u>without</u> corruption problems and <u>with</u> tangible sustainable and inclusive development results for their people

Let me leave you with three key points:

1. Choices that the Government makes in managing minerals revenues – the structure and governance and rules around the SWFs – matters HUGELY in preventing damage to the non minerals sectors of the economy and the population who depends on them.
2. Choices that Government makes about how to invest in enabling agricultural businesses through access to finance and better infrastructure, and investing in skills, matters HUGELY in helping the agriculture sector to. You might choose to target certain structural challenges, like remoteness, with specific interventions like freight subsidies as Warren Dutton has suggested – **but before that** we should emphasize meeting the policy and behavioral challenge of investing in rehabilitating and maintaining infrastructure that is directly relevant to rural communities, and removing barriers to access to finance, skills and technology, and market information that could help the ag sector grow.
3. For both revenue management and expenditure management, communicating transparently with PNG's citizens and with the world on how revenues are received and used is critical to avoid the resource curse – and so it is critical that Government consider joining the Extractive Industries Transparency Initiative, or EITI.