

PRIVATE SECTOR ASSESSMENT (SUMMARY)¹

A. Private Sector Development

1. The Papua New Guinea (PNG) economy consists of a large subsistence sector, which provides a livelihood for well over 80% of the population, a capital-intensive resource sector, and a relatively small formal sector of service and small manufacturing industries. The resource sector focuses mainly upon exploiting the country's rich natural resources, notably minerals, hydrocarbons, and timber. Opportunities for downstream processing of PNG's natural resources have increased during the recent commodities boom.

2. Despite recent strong economic growth associated with the commodities boom, the performance of the economy over the past decade has been disappointing. PNG remains one of the poorest countries in the region and outside the resources sector formal business activity is limited. As has been demonstrated by many weakly performing or conflict-prone resource-rich developing countries, natural resource abundance does not necessarily lead to, and can actually undermine, broad-based development. PNG faces two fundamental economic development challenges: (i) to increase natural resource-based production and convert revenues into sustainable development outcomes; and (ii) to broaden the base of the economy and the basis for economic growth and job creation. Private sector development is therefore at the core of PNG's future economic growth prospects, yet surveys and assessments point to chronic constraints, notably poor infrastructure and utility services, a high crime rate, weak property rights, lack of competition and market access, and the inability of the financial sector to finance investment opportunities.²

3. Sustainable development will require the enclave mineral and petroleum sectors to generate ancillary investment and growth in other sectors of the economy, primarily by generating government revenues to fund the provision of essential public services. While the government's performance in delivering road, telecommunications, education, and basic health services³ has improved in recent years, other basic infrastructure service delivery remains poor, primarily due to the government's reliance on inefficient public enterprises, its weak budget execution capacity, and the limited accountability governing the use of royalty revenues paid to the provinces.⁴

4. Broadening the base of the economy requires improving the enabling environment for business and reducing transaction costs. The rural economy, which employs the vast majority of Papua New Guineans, is to a large extent remote and poorly served by infrastructure and other services. The transition from a subsistence to a market economy is severely hampered by the difficulty of getting market information and transporting goods to formal markets or to ports for export, and the lack of financial services to finance micro-entrepreneurs, including women. These factors increase the costs of doing business.

¹ This summary is based on ADB. 2008. *Foundation for the Future: A Private Sector Assessment for Papua New Guinea*. Manila. Available at <http://www.adb.org/Documents/Assessments/Private-Sector/PNG/2008/default.asp>

² These core constraints have been highlighted in ADB. 2008. *Foundation for the Future: A Private Sector Assessment for Papua New Guinea*. Manila; ADB. 2008. *The Challenger of Doing Business in Papua New Guinea: An Analytical Summary of the 2007 Business Environment Survey by the Institute of National Affairs*. Manila.

³ ADB's HIV/AIDS Prevention and Control in Rural Enclaves Project has demonstrated the positive impact of private sector delivery of health services to underserved communities. ADB. 2006. *Report and Recommendation of the President to the Board of Directors: Proposed Asian Development Fund Grant to Papua New Guinea for the HIV/AIDS Prevention and Control in Rural Development Enclaves Project*. Manila.

⁴ Department of National Planning and Monitoring. 2008. *Assessing PNG's Development: Pocketbook 2007—Medium Term Development Strategy Performance Management Framework*. Port Moresby; National Statistics Office. 2008. *2006 Demographic and Health Survey: A Summary of Preliminary Findings*. Port Moresby.

5. The ExxonMobil led liquefied natural gas project will attract significant investment and will require a substantial range of supporting services (including infrastructure investment). The government has a unique opportunity to broaden the base of economic growth through the project's linkages with micro, small, and medium-sized enterprises. To capitalize on this opportunity, the government needs to improve access to physical infrastructure and financial services and implement policy reforms to facilitate competition, open markets, and create a more secure legal environment for doing business. Recent progress in addressing these primary constraints to private sector development has been encouraging, but much remains to be done. Notable improvements have been made only in selected infrastructure sectors, largely as a result of greater public investment in roads and the introduction of competition, which has paved the way for private investment in the telecommunications, aviation, and power sectors.

6. While competition is gradually being introduced in selected infrastructure sectors, it is still being approached cautiously by the government, which places substantial emphasis on protecting state-owned enterprises (SOEs). The government's intention to develop a community service obligation (CSO) framework for SOEs is encouraging, as this should pave the way for the introduction of competition into SOE sectors by ensuring that all CSOs are provided on a fully commercial basis.⁵ Moreover, the cabinet's endorsement of the National Public–Private Partnership Policy in 2008 and the ongoing preparation of a legal and institutional framework to implement the policy should facilitate much needed private investment in infrastructure.⁶ It is anticipated that the greatest potential for public–private partnership (PPP) investments will be in the utility and transport sectors, both critical for the reduction in the cost of doing business.

B. ADB Support for Private Sector Development

7. Since the end of 2006, a significant number of ADB's private sector development activities have been supported through the Pacific Private Sector Development Initiative (PSDI).⁷ PSDI, which is cofinanced by the Australian Agency for International Development (AusAID), addresses the binding constraints of private-sector-led economic growth in the Pacific by supporting (i) increased access to finance; (ii) reform of the enabling business environment; and (iii) SOE reform and the implementation of PPPs. In addition to PSDI, ADB has supported private sector development activities in PNG during the 2006–2010 country strategy and program period through stand-alone technical assistance (TA) for Policies for Private Sector Development.⁸

8. In 2008, ADB published a new private sector assessment whose diagnosis of the key constraints to private sector development has been supported by the ADB-funded 2007 Institute of National Affairs Business Survey. Both reports developed similar conclusions and recommended policy prescriptions to improve the environment for doing business. Conversion of the policy reform recommendations into action has been disappointing, with the notable exception of the introduction of more competition into the telecommunications, power, and

⁵ A key rationale given by the government for the protection of some SOE monopolies is the role of the SOEs in delivering government-mandated noncommercial services (community service obligations). SOE monopolies are preserved so that the SOEs can generate sufficient revenues to cross-subsidize these CSOs.

⁶ In 2009, a multi-agency task force received technical assistance (TA) from ADB to prepare a draft PPP law as well as the organizational, staffing, and operating guidelines for the future PPP Centre. This work is expected to be completed in the first half of 2010 with the submission of the draft PPP law to Parliament.

⁷ ADB. 2006. *Technical Assistance for the Private Sector Development Initiative*. Manila (TA 6353-REG).

⁸ ADB. 2006. *Country Strategy and Program: Papua New Guinea, 2006–2010*. Manila; ADB. 2005. *Technical Assistance to Papua New Guinea for Policies for Private Sector Development*. Manila (TA 4722-PNG).

aviation sectors, and the development of a framework for public–private partnerships. ADB continues to engage with the government and other stakeholders to advocate other priority reforms, including placing state-owned enterprises on a fully commercial and accountable footing.

9. Since 2008, ADB has worked closely with an interdepartmental task force to develop a PPP framework. The cabinet endorsed a PPP policy in December 2008, the implementation of which, including the development of a PPP law and establishment of a PPP Centre, has been under way since early 2009 and is expected to be completed by the end of 2010. The establishment of the PPP Centre as an advisory body under the Minister for Treasury will be facilitated by a 2010 National Budget allocation, and a further budget submission will be made for 2011, which should enable core staff and technical advisors to be recruited for its start-up phase. ADB will continue to support the implementation of the PPP process in PNG so that the first PPP transactions can be effectively prepared.

10. ADB has also provided TA to the Independent Consumer and Competition Commission (ICCC) to build its capacity to execute its economic regulatory and consumer protection mandate in general, and to regulate the telecommunications sector in particular. While the TA has been essential to the ICCC's ability to foster competition in the telecommunications sector, under the new regulatory regime introduced by the National Information and Communication Technology Act adopted by parliament in 2009, ICCC will lose its *ex ante* regulatory powers over the sector. Unless the new regulatory body for the telecommunications sector proves as effective as the ICCC in promoting and regulating fair and transparent competition, this development will not have a positive impact.

11. ADB has a strong interest in furthering the efficient development of the telecommunications sector in PNG. In 2009, ADB, in collaboration with commercial banks and the International Finance Corporation (IFC), provided \$18 million in senior debt to increase Digicel PNG's term loan facility. The funds are to be used to expand Digicel's network capacity and coverage and to upgrade its billing system, among other things.

12. At the request of the Department of Treasury, the Independent Public Business Corporation, and the Department of Public Enterprises, ADB is currently providing TA for the development of a CSO framework for SOEs. This framework will allow CSOs to be identified, costed, contracted, and financed so that their delivery is on a purely commercial basis. To implement such a framework, a host of legal and governance reforms will be required to place the SOEs on a more transparent and accountable footing so that they can operate on fully commercial terms. This process should in turn facilitate the introduction of competition in those sectors in which the SOEs continue to hold dominant market positions.

13. ADB is working closely with its development partners in private sector development, in particular the IFC, which has been addressing constraints identified in its Doing Business indicators, including gender-related constraints. Current areas of focus include investment regulations, and business licensing and registration. ADB has also been coordinating closely with the IFC and the Public–Private Infrastructure Advisory Facility (PPIAF), to program TA to support the government to develop potential PPP opportunities. This coordination has resulted in joint workshops on PPP issues and, most recently, a joint ADB and IFC TA team to advise the Department of Health on PPP options for the procurement of the redevelopment of the Angau Memorial Hospital in Lae.

14. ADB is closely coordinating its private sector development work with AusAID, which is

active in the transport, health, and education, where there is scope for increased private sector participation. AusAID has provided significant grant cofinancing for ADB's private sector development activities, including for ADB's Pacific Private Sector Development Initiative.⁹ ADB will pursue further opportunities to combine or complement private sector development initiatives with AusAID, particularly in access to finance and PPP project design, assessment, and fiscal risk management.

15. ADB's support for private sector development in PNG cuts across economic sectors and directly supports two of ADB's five core areas of specialization in Strategy 2020—infrastructure and financial sector development.¹⁰ It also supports one of the key drivers of change in ADB's Pacific Strategy, 2010–2014—an improved private sector environment.¹¹ The outcome of ADB's support for private sector development will be lower costs of doing business, which will be tracked through progress in processing of the first set of PPP projects and the quantum of private sector investment in the provision of infrastructure services.

16. There are direct links between ADB's support for private sector development and the other priority sectors and themes in the country partnership strategy. Most evident are the positive links to ADB's work in the transport sector. First, the private sector needs effectively functioning transport infrastructure and services to access markets, promote trade, and carry out business, and the poor state of PNG's transport infrastructure and services has been identified as a major constraint to business. Second, ADB is promoting revised policy and institutional arrangements for road, aviation, and maritime transport, which will promote the “user pays” principle and give greater accountability to users. Third, the provision of infrastructure maintenance and upgrading and transport services is a key area of private sector activity, and one that will be actively encouraged through the transport sector program. The establishment of a PPP framework will facilitate private investment in all infrastructure sectors, including transport.

17. To support the government in its efforts to improve the reach and quality of its infrastructure services (including in rural areas), continued TA will be provided to the government to complete the implementation of its PPP program. To create further opportunities for private investment in infrastructure services, sectors dominated by SOEs will need to be further opened up to competition. The reform of SOEs, including the development of a framework for the delivery of community service obligations, will support this transition to a more open market environment for infrastructure services. In addition to the ongoing support provided through the Pacific Private Sector Development Initiative, a capacity development TA will be provided in 2011–2012 to implement the PPP program and the future CSO framework and to facilitate the transition of SOEs to a more competitive environment.

18. ADB will also pursue private sector investment opportunities in PNG through its Private Sector Operations Department during the CPS period. Such opportunities, which will be examined on their individual merits, will complement ADB's existing activities in PNG. They are likely to be concentrated in financial services, telecommunications, transport and energy. Where possible, ADB will use TA resources to fund private sector project formulation.

⁹ ADB. 2006. *Technical Assistance for the Private Sector Development Initiative*. Manila (TA 6353-REG); ADB. 2009. *Technical Assistance for the Pacific Private Sector Development Initiative, Phase II*. Manila (TA 7430-REG).

¹⁰ Strategy 2020 focuses ADB operations in five core areas and three complementary areas. The five core specializations are (i) infrastructure, (ii) environment, (iii) regional cooperation and integration, (iv) finance sector development, and (v) education. ADB. 2008. *Strategy 2020: The Long-Term Strategic Framework of the Asian Development Bank, 2008–2020*. Manila.

¹¹ ADB. 2009. *ADB's Approach to Assisting the Pacific (2010–2014)*. Manila.