



Country Partnership Strategy

August 2010

Papua New Guinea 2011–2015

Asian Development Bank

CURRENCY EQUIVALENTS

(as of 6 August 2010)

Currency Unit	–	kina (K)
K1.00	=	\$0.3700
\$1.00	=	K2.70

ABBREVIATIONS

ADB	–	Asian Development Bank
ADF	–	Asian Development Fund
AusAID	–	Australian Agency for International Development
CPS	–	country partnership strategy
CSO	–	community service obligation
CSP	–	country strategy and program
DSP	–	Development Strategic Plan
IMF	–	International Monetary Fund
LNG	–	liquefied natural gas
MFF	–	multitranches financing facility
MTDS	–	Medium-Term Development Strategy
OCR	–	ordinary capital resources
PEFA	–	public expenditure and financial accountability
PFM	–	public financial management
PNG	–	Papua New Guinea
PPP	–	public–private partnership
PSD	–	private sector development
RCI	–	regional cooperation and integration
SOE	–	state-owned enterprise
TA	–	technical assistance

NOTE

In this report, "\$" refers to US dollars unless otherwise stated.

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I. DEVELOPMENT TRENDS AND ISSUES

A. Country Background

1. **Social developments.** Since 2003, Papua New Guinea (PNG) has experienced sustained economic growth, driven primarily by a commodity price boom. However, given that few of the poor depend directly on the mineral sector and its links with the rest of the economy are weak, the direct contribution of extractive industry growth to poverty reduction is limited. Urban poverty is defined as lack of livelihood and income generation opportunities and rural poverty as not having access to basic services. However, income poverty analysis in PNG is constrained by weak and outdated data.¹ There is evidence that many Papua New Guineans are resilient to income shocks because they are able to respond by producing more domestic food staples and turning to traditional coping mechanisms, grounded in strong ethnic group links. However, groups that are particularly vulnerable to food security issues include landless populations living in settlements around provincial towns. In these communities traditional social systems are becoming stretched because of greater mobility and urban drift.² About 87% of the population lives in rural areas. Despite a rich resource base and high levels of external assistance, PNG social indicators lie below those of other countries with similar income per capita levels. The country is not expected to meet any of the Millennium Development Goals by 2015. Child and maternal mortality and the HIV/AIDS prevalence rate remain worryingly high, school enrollment rates are low, and measures to tackle pervasive gender inequality are inadequate.³

2. **Role of government.** The government plays a critical role in setting the conditions for livelihood opportunities because the formal private sector remains small. Most people are subsistence farmers engaged in some cash crop production and scattered over a vast and geographically challenging terrain. Since independence in 1975, the government has had insufficient funds to maintain national infrastructure assets. These have deteriorated because of natural conditions⁴ and an increase in use and they need to be rebuilt and rehabilitated. Windfall revenues earned during the early 1990s were not well managed. The government learned from that experience, and as a result windfall revenues earned from the recent commodity boom were better managed, although fiscal discipline weakened in 2009. Nevertheless, the government has not had the fiscal capacity to finance the significant reconstruction and rehabilitation backlog. The ExxonMobil-led PNG liquefied natural gas (LNG) project and potential other LNG projects will be the largest resource projects in the country's history, and will significantly boost revenues and partially fill this financing gap. The development cost of the LNG project is \$15 billion and its output value will total approximately \$150 billion over its 30-year life, including approximately \$30 billion revenue for the government and landowners. The project is expected to increase the gross domestic product by 15%–20% over its lifetime.

3. **Government systems.** The government has struggled to deliver basic social and economic services because of poor public sector management,⁵ capacity issues, institutional

¹ The most recent and comprehensive projection and analysis of the existing data is provided by a World Bank poverty assessment completed in 2004. It uses data from the most recent household income expenditure survey, which was carried out in 1996. A new survey is being carried out and is scheduled to be completed by September 2010. The 2006 demographic and health survey helps to address some of the data constraints.

² D. Mellor. 2010. *Social Impact of Commodity Price Volatility in Papua New Guinea*. Manila.

³ Country and Portfolio Indicators (Appendix 2).

⁴ Extreme weather events, especially heavy rain and floods, frequently damage economic and social infrastructure and this risk is likely to increase.

⁵ Government of PNG. 2010. *PNG Development Strategic Plan 2010–2030*. Port Moresby. p. 122.

weaknesses, and geographic challenges. The Asian Development Bank (ADB) recognizes these as characteristics of fragile situations and elements of its approach to engaging with weakly performing countries will apply.⁶ With regard to reforming existing government systems, PNG's development partners will need to have realistic expectations about what can be achieved within a particular timeframe. They also need to act strategically and to respond to changing circumstances by shifting the focus of their technical assistance (TA). Reforms and TA interventions should be carefully sequenced and take into account institutional capacity constraints at national and subnational levels.

B. Economic Assessment and Outlook

4. **Economy.** There are few direct economic links between PNG and nearby countries in Asia and the Pacific, notably Indonesia.⁷ PNG relies on commodity exports: minerals constitute 77% of total exports, agriculture products 17%, and forestry products 5%. Despite the effects of the global financial crisis, the PNG economy grew by 4.5% in 2009. Successful reforms have created a sound fiscal policy framework that left PNG well positioned at the onset of the crisis and helped to sustain growth.⁸ However, recently policy implementation has weakened and spending in 2009 from accumulated windfall revenues was above the limit set in the medium-term fiscal strategy. Fiscal policy was unnecessarily and unselectively expansionary, given the solid levels of private sector activity. Lack of coordination between monetary and fiscal policy undermined the effectiveness of monetary policy. The LNG project construction phase will further stimulate growth and add to inflationary pressures because of a shortage of skilled labor and capacity constraints, especially in the construction and real estate sectors. Domestic demand pressures combined with the recovery in international commodity prices will fuel a pickup in the inflation rate, which could reach 10% in 2010–2011.

5. **Reforms.** After good initial progress, the public financial management (PFM) reform agenda has stalled. Resources from trust fund accounts⁹ are being channeled outside the national budget framework and hence are not subject to standard budgetary controls. The government is now focused on managing resource volatility and wealth creation from the prospective LNG projects. ADB's 2008 private sector assessment¹⁰ highlighted law and order problems, weak property rights, poor infrastructure, lack of credit access, weak competition, and the dominant role of the state in the economy as the reasons for the high transaction costs that have discouraged investment outside the minerals sector. State-owned enterprises (SOEs) continue to dominate many sectors of the economy and their performance affects economic growth outside the minerals sector. There has been some progress on reform, with more competition in telecommunications, aviation, and power. However, massive investment is needed, particularly within those SOEs that will see considerable increases in demand from the LNG project. The government is committed to implementing its public–private partnership (PPP) policy in order to encourage significant private investment in infrastructure.

⁶ ADB. 2007. *Achieving Development Effectiveness in Weakly Performing Countries*. Manila.

⁷ ADB. 2009. *Report and Recommendation of the President to the Board of Directors: Proposed Loan and Technical Assistance to Papua New Guinea for the Pilot Border Trade and Investment Development Project*. Manila.

⁸ Fiscal discipline was underpinned by the Fiscal Responsibility Act, 2006, the medium-term fiscal strategy, 2008–2012, and the medium-term debt strategy, 2005–2009.

⁹ The objective of these trust fund accounts, accumulated during the commodity boom, is to avoid unsustainable and inflationary pressures by smoothing out recurrent and development expenditures over the commodity cycle.

¹⁰ ADB. 2008. *Foundation for the Future: A private sector assessment for PNG*. Manila.

B. Highlights of Previous ADB Country Strategy

6. **Previous strategy.** The country strategy and program (CSP), 2006–2010 has been the basis of ADB's engagement in PNG over the past 5 years.¹¹ The CSP objective was to help PNG deliver its Medium-Term Development Strategy (MTDS), 2005–2010, in particular its focus on the core function of delivering basic services.¹² The CSP emphasized ADB support for (i) PFM, (ii) transport, (iii) private sector development, and (iv) health and combating HIV/AIDS.

7. **Strategy validity.** The CSP final review¹³ found that the underlying rationale for the CSP remained valid throughout the implementation of the MTDS, 2005–2010. Good governance was a core development challenge. The review regarded strengthening PFM as a key governance intervention that could drive broader public sector reform and improve MTDS implementation. ADB's support for transport reflected the sector's pivotal role in achieving economic growth and improving social service delivery. The CSP's support for private sector development was an appropriate way to help the government address its economic growth objectives and to increase the participation of Papua New Guineans in the economy. The CSP responded to pressures in the health sector by contributing new ideas and models for effective health service delivery and HIV prevention.

8. **Portfolio performance.** Preliminary performance indicators for the transport sector will not be fully met, particularly for road infrastructure. The performance targets for PFM consisted of nine public expenditure and financial accountability (PEFA) indicators. The 2008 PEFA assessment showed that performance against five of these indicators had remained unchanged since 2006 and against the other four it had deteriorated. ADB's support for private sector development has partly followed the CSP and partly been opportunistic, seizing opportunities when commitment and buy-in existed. The reform of SOEs has been slow. There has been good progress in microfinance, and ADB helped the government prepare a national PPP strategy, which was endorsed by the cabinet in December 2008. There has been good progress in addressing HIV prevention and control, including piloting and demonstrating a private sector participation model for delivering basic health services in rural areas.

9. **Alignment.** In terms of aid effectiveness, the portfolio was well aligned with the government's main planning tools, the MTDS, and its sector policies. Most expenditure funded by ADB through the development budget was undertaken using government procurement and financial systems, subject to ADB "no objection." However, using government systems and processes has slowed the implementation of transport projects.

10. **Main lessons.** The CSP final review identified the following lessons: (i) longer development partnerships and more realistic project implementation schedules are needed, and the design phase of projects should allow for comprehensive consultation with all relevant stakeholders, especially in the Highlands Region where local community structures are often complex; (ii) programming should be underpinned by an analysis of the political economy that considers both technical and political dimensions of development efforts; (iii) reform efforts should focus on areas with effective reform leaders; (iv) capacity constraints in government systems mean that ADB should further explore the efficacy of service delivery models that draw on private sector strengths; (v) a stronger and more consistent link between large-scale projects and capacity development TA is desirable, both to support the success of the project and to

¹¹ ADB. 2006. *Country Strategy and Program: Papua New Guinea, 2006–2010*. Manila.

¹² Government of Papua New Guinea. 2004. *The Medium-Term Development Strategy, 2005–2010*. Port Moresby.

¹³ Country Strategy and Program Final Review (Appendix 2).

increase government willingness to pursue capacity development efforts; (vi) the capacity of line agencies to collect data (including gender-disaggregated data) needs strengthening; and (vii) strategies and contract packaging should be designed to attract large and competent international contractors to the PNG infrastructure market. These lessons influenced the design of the ADB-supported Highlands Region Road Improvement Investment Program and the Civil Aviation Development Investment Program, both multitranche financing facilities (MFFs).¹⁴

II. THE COUNTRY STRATEGY

A. Government National Strategy

11. **Vision.** Papua New Guinea Vision 2050 is the national development framework.¹⁵ Development and sector strategies at all levels of government are to be aligned with Vision 2050. Vision 2050 aims to transform an economy dominated by the mining and energy sectors into one that can generate more inclusive economic growth.

12. **Development plan.** The government has approved the PNG Development Strategic Plan (DSP), 2010–2030,¹⁶ which confirms national development priorities and provides a strategic framework for development planning. The DSP will provide overarching guidance for all development agendas and sector strategies. All sector strategies and lower-level government plans will be aligned with the DSP. The government is also developing other policies, such as the national PPP policy and the PNG Commitment on Aid Effectiveness,¹⁷ which will enhance the implementation of the DSP.

13. **Strategy intersection.** The DSP intersects with ADB's Strategy 2020¹⁸ in the core areas of infrastructure, climate change,¹⁹ and education. DSP priorities also include health and agriculture, which are classified as other areas of operations under Strategy 2020 that ADB can support if its presence is needed. The DSP also emphasizes the importance of private sector development, good governance, and gender and development.

14. **Government request.** Ministers and senior officials are strongly committed to strengthening PNG's development partnership with ADB. The government has asked ADB to align its assistance with DSP priorities, and to broaden its infrastructure support beyond the transport sector. In addition to the priorities of the previous CSP, the government identified civil aviation, telecommunications, water supply and sanitation, cross-border trade, and power as core priorities. The government favors a programmatic approach to its partnership with ADB, featuring long-term predictable financing effectively coordinated with support from other development partners, with the government taking the lead and using national systems so far as possible. The government has indicated a preference for MFFs for this purpose. A programmatic approach is also preferred for TA.

15. **Fiscal and debt strategies.** Under the Fiscal Responsibility Act, 2006, PNG's fiscal policy is set within a sustainable medium-term framework and is based on principles of sound fiscal management. It is consistent with key development strategies, including the medium-term debt strategy, 2010–2014 and the medium-term fiscal strategy, 2008–2012. Under the debt

¹⁴ Details of ongoing ADB projects are in Table 9 of Country and Portfolio Indicators (Appendix 2).

¹⁵ Government of Papua New Guinea. 2009. *Papua New Guinea Vision 2050*. Port Moresby.

¹⁶ Government of PNG. 2010. *PNG Development Strategic Plan 2010–2030*. Port Moresby.

¹⁷ PNG Commitment on Aid Effectiveness. 2008. <http://www.pngecbp.com/PNGCommitmenttoAidEffectiveness.pdf>

¹⁸ ADB. 2008. *Strategy 2020: The Long-Term Strategic Framework of the Asian Development Bank, 2008–2020*. Manila.

¹⁹ Climate-compatible development for Papua New Guinea, March 2010

strategy, all new external debt should be on concessional terms, which is defined as having a grant element of 35% or more. The government is exploring the option of channeling flows from the LNG project into three trust funds: (i) a stabilization fund to manage revenue streams with the aim of minimizing potential “resource curse” impacts, (ii) an infrastructure fund to focus on optimizing the use of dividends to leverage and mobilize financing of infrastructure, and (iii) a future fund to be set aside for future generations.

B. ADB Country Strategy

16. **Strategic direction.** The prospect of large income and revenue flows from the LNG project and other major projects is fueling expectations of an economic and social transformation. The proposed country partnership strategy (CPS), 2011–2015 aims to help PNG plan and implement a successful transition through the conversion of its resource wealth into inclusive economic growth.

17. **Sovereign wealth management.** The potential adverse macroeconomic implications of large resource projects will need to be managed skillfully. Over 2011–2015, ADB will help the government prepare for the expected mineral revenue. It will conduct knowledge work to help the government make the transition to the new economic and fiscal environment offered by the LNG project, particularly on sovereign wealth management. PNG will also need to ensure that revenue from LNG and other mining and petroleum projects are efficiently and equitably utilized and aligned with development priorities. Lifting the standard of governance, particularly with regard to the management of revenue from petroleum and mining projects, is essential to ensuring that the government can convert financial wealth into broad-based delivery of basic services. ADB will therefore continue to support the government to strengthen PFM.

18. **Inclusive growth.** ADB interventions will support more inclusive growth by creating livelihood opportunities and improving access to basic services, especially in rural areas where 87% of the population lives. ADB's support will focus on infrastructure, which is vital for better service provision and market access in rural areas. The government faces a large fiscal gap before LNG project revenues build up toward 2020, and it is seeking assistance from ADB to finance the rehabilitation of critical infrastructure. To ensure these investments are sustainable, ADB will help establish reliable financing mechanisms for asset maintenance. It will also support rural populations by providing them with greater access to finance and primary health services. ADB support for private sector development, through SOE reform, will lower business transaction costs, thereby helping to expand small and medium-sized enterprises and to create jobs in the formal economy. ADB will mainstream gender in all general intervention projects.

19. **Infrastructure.** Economic growth in 2008 and 2009 has revealed that poor infrastructure often acts as a bottleneck limiting further growth. The national transport network is often cited as the major constraint on economic growth and improved service provision, especially in rural areas. Investment in power generation, transmission, and distribution has been inadequate and only 12% of Papua New Guineans have access to electricity. The electricity supply to urban areas is unreliable. Greater investment and more efficient infrastructure are needed if PNG is to derive the full benefits from growth opportunities. The government is committed to improving the state of national infrastructure, and the LNG and other petroleum and mining projects will provide the fiscal capacity to service additional borrowing for long-term transport assets. The government recently elevated power sector development to a national priority in the DSP and, following ADB's support for the national power sector development plan, has requested ADB support for the plan's implementation, including power infrastructure financing. This CPS responds to the government's request for ADB to scale-up its support for infrastructure

development and management. A strong portfolio and forward pipeline has been developed in road transport, maritime transport, civil aviation, and power. Limited and unreliable infrastructure maintenance funding pose a significant risk to the sustainability of infrastructure projects, which ADB is addressing through alternative mechanisms for maintenance and the financing of operating costs (para. 40).

20. **Private sector development.** Public enterprises and utilities remain a drag on economic growth and their reform will remain a key activity. The performance of these entities affects PNG's ability to deliver its DSP objectives of economic growth and rural service delivery. There has been some progress on reform but more needs to be done, particularly with those SOEs that will see considerable increases in demand from the LNG projects. ADB will continue to support the government's efforts to implement the PPP policy, with a view to facilitating significant private investment in infrastructure. ADB is also working with the government to develop a national community service obligation (CSO) framework for SOEs that would pave the way for the introduction of competition into the SOE sectors by ensuring that CSOs are provided on a fully commercial basis (footnote 16, p. 38).

21. **Private sector operations.** ADB approved its first private sector loan in PNG in 2009 and remains open to further private sector operations, including loans, equity investments, and credit enhancement products, with a focus on infrastructure and financial services. ADB will help facilitate private investment in power developments, especially for major grid development. These sector-specific initiatives will complement cross-sectoral efforts to improve the enabling environment for the private sector. ADB will also help develop financial solutions through innovative contractual and financial structures to encourage private company participation, enhance management expertise, and improve corporate governance.

22. **Good governance.** Better governance will ensure more effective and efficient utilization of public finances for service delivery and infrastructure provision and will be critical in the context of the anticipated windfall revenues from the LNG and other major projects. ADB is ready to support the government in its efforts to implement the Extractive Industries Transparency Initiative²⁰ and to adopt the Santiago Principles²¹ around the proposed sovereign trust funds. ADB will also continue to support the government-wide framework for enhancing fiscal management led by the departments of finance and treasury, and efforts to raise governance standards for infrastructure projects, statutory authorities, SOEs (including Kroton No. 2, which will hold the state's interest in the LNG project), and executing agencies. In partnership with other development partners, ADB will continue to pursue opportunities to help the government strengthen PFM with appropriate budget and accountability structures, and transparent processes. These efforts will be designed to help sustain the performance of the public sector and also to alleviate the constraint on the performance of ADB's portfolio arising from the use of government systems and processes.

23. **Knowledge solutions.** Given its key role in infrastructure development, ADB will work closely with the government in planning the proposed infrastructure fund and making it operational. It will also explore other financial mechanisms to ensure the sustainability of infrastructure. Desired development outcomes will need to be carefully prioritized and sequenced if they are to be achieved. The government has moved toward using results-based

²⁰ Extractive Industries Transparency Initiative. <http://eiti.org/>

²¹ The generally accepted principles and practices for sovereign wealth funds, informally known as the "Santiago Principles," are a set of voluntary principles agreed to by the international working group of sovereign wealth funds in September 2008. The 24 principles offer guidelines covering governance, accountability, transparency, and conduct of investments for sovereign wealth funds.

management approaches. Successful monitoring and evaluation of results-based frameworks will require adequate and reliable data that can inform development planning decision making. ADB will support development planning in key line agencies, including the transport, works, and health departments, by utilizing available planning resources such as the geographic information system handbook recently developed by the University of PNG. ADB will also support the government's efforts to analyze key socioeconomic survey data and to integrate the findings into strategic and project planning.

24. **Environment.** Extreme weather conditions and other natural hazards frequently damage infrastructure and the risk of the climate-related events is likely to increase. ADB will seek to climate- and hazard-proof infrastructure projects, in particular in transport and power. In the power sector, clean energy solutions will be given priority and market mechanisms such as the Clean Development Mechanism will be explored, which may bring in additional carbon revenue.

25. **Finance sector development.** The level of savings and lending in rural areas is low, partly as a result of inefficient local financial outreach. This limits opportunities to participate in the cash economy. Since 2001, ADB has been supporting a successful microfinance project that led to the establishment of the Nationwide Microbank. The government has asked for this support to be continued and expanded. It has also asked for additional mainstream "access to finance" support, which ADB will provide, including secured transactions reform to allow for the use of moveable assets as collateral. ADB will also look to adapt innovative solutions such as mobile banking through assistance to the central bank for legal and regulatory work.

26. **Health.** For several years, ADB has successfully piloted and demonstrated innovative partnerships with the private sector to prevent and control HIV in remote rural communities. These arrangements are very significant in the face of declining health services in PNG and weak health sector indicators (including high maternal and infant mortality). ADB's support is appreciated by the government and other development partners. In response to a government request, ADB will expand its support to providing primary health services to rural populations.

27. **Education.** ADB is currently not providing direct support for education. Despite massive support from other partners, primarily the Australian Agency for International Development (AusAID), access to primary and secondary education has not significantly improved. There is no strong argument for ADB to provide education support, especially as structural issues remain unresolved. Direct support for education will continue to be provided by other partners (mainly AusAID) while ADB will focus on developing human resource capacities directly linked to infrastructure projects in specific sectors. ADB will continue to keep the education sector under active review.

28. **Gender equity.** Women continue to face severe inequalities in access to essential social services. The prevalence of gender-based violence restricts women's security and their opportunities to participate in economic and political systems. ADB is committed to the gender mainstreaming of projects that promote women's empowerment, particularly in rural areas. Its infrastructure, finance, power, and health projects will include sector-specific gender analysis and incorporate gender-specific target indicators within the results frameworks.

29. **Regional cooperation and integration.** The DSP employs a growth corridor approach, including a corridor between PNG and Indonesia. This approach is consistent with Strategy 2020. The government recognizes ADB's unique experience in regional cooperation and integration and has asked for this support to continue. The ongoing Pilot Border Trade and Investment Project will be monitored and assessed for possible expansion.

30. **Partnerships.** Cooperation with development partners through government-led processes will continue to be a key feature of ADB's work. ADB will actively seek to enhance partnerships with other development partners and to explore cofinancing opportunities. ADB is also increasingly seeking out opportunities to partner with non-state actors, as demonstrated by the successful partnership with the private sector in the delivery of rural health services. ADB will continue to participate in International Monetary Fund (IMF) Article IV missions and to conduct debt sustainability analysis jointly with the IMF and the World Bank. ADB will further enhance its collaboration with AusAID and the Japan International Cooperation Agency in the transport and power sectors. In PFM, ADB is coordinating closely with AusAID, the European Union, and the World Bank through a government-wide framework for enhancing fiscal management and public expenditure and financial accountability assessments. ADB will continue to promote harmonization by participating in the sector-wide approach in the health sector. AusAID provides significant grant cofinancing for ADB's private sector development interventions, an area in which ADB is taking the lead in assisting the government. ADB will expand its partnership approach to providing primary health and financial services to rural populations, working primarily with the private sector and civil society.

III. STRATEGY IMPLEMENTATION

A. Indicative Resource Parameters

31. **Lending and technical assistance.** PNG is a group B country and is eligible for a blend of ordinary capital resources (OCR) and Asian Development Fund (ADF) borrowing. OCR public sector lending is expected to average about \$60 million per annum from 2011 to 2015, mostly for projects. However, levels of OCR lending will not be spread evenly over the period, because of the small number of relatively large OCR-funded projects in PNG, for instance in the power sector. PNG's ADF X biennial allocation for 2011–2012 is \$126 million and this will primarily be used for interventions that have a high impact on poverty and for capacity development. ADB will seek to leverage its lending resources by mobilizing joint and parallel cofinancing. ADB TA will help the government prepare projects and support project implementation and sector reform in line with CPS priorities. Commitments will average about \$4 million per year, for four to five operations. ADB will actively seek TA cofinancing.

32. **Cost sharing.** ADB's cost-sharing limit is 85% for both ADF and OCR loans. The TA cost-sharing limit is 99%. These apply across all sectors, although lower percentages of ADB financing are expected for income-earning projects in transport and infrastructure so as to encourage local ownership.

B. Program Overview

33. **Infrastructure.** Transport infrastructure support will account for over 80% of ADB's PNG program. The two ongoing road and civil aviation MFFs will continue beyond the CPS period. Since most externally-funded road rehabilitation projects do not include bridges, a stand-alone national bridges development investment program may be considered. The ADB-supported Lae Port Development Project will continue until 2014 and may overlap with or be followed by other port investments. Many more small jetties will still be needed in addition to those being constructed or rehabilitated by the ongoing Community Water Transport Project, and ADB will consider financial support for such efforts. The government may also request a second phase of the successful Rehabilitation of Navigation Aids Systems Project. In power, ADB is preparing the Towns Electrification Project, and will consider investments in grid development, including

large hydropower facilities. The government has recognized that the single national power tariff is a disincentive to the corporatized PNG Power Limited to invest in grid extensions that are not financially viable. It proposes to address this by establishing a CSO policy with ADB TA to support financially unviable power infrastructure, and also by establishing an Electricity Trust Fund under the proposed Electricity Industry Policy to support such investments. ADB will provide project financial management support for all investments; PPP opportunities will be explored and supported. At the national level, ADB support for improving PFM and PPP institutional arrangements and capacity will help the government fund infrastructure investments.

34. **Environment.** ADB support for the power sector will focus on renewable and clean energy. TA and financing support will help climate and hazard proofing and adaptation of climate-sensitive projects, including for ADB-funded transport and power infrastructure, which are at moderate or high risk from the impacts of climate change and other natural hazards. These include changes in rainfall and temperature extremes, sea level rise, and storm surges as well as seismic, volcanic, landslide, storm, and flooding risk. Regional TA will help strengthen the country's capacity to build resilience in key sectors and to manage its natural resources.

35. **Regional cooperation and integration.** ADB will provide significant regional cooperation and integration TA and will build on experience gained from the ongoing Pilot Border Trade and Investment Project.

36. **Financial sector development.** ADB will use its Pacific Private Sector Development Initiative²² to help the government prepare a new Microfinance Expansion Project. The project will provide wholesale microfinance services through existing intermediaries (such as grassroots cooperatives, specialized nongovernment organizations, and other microfinance institutions) to expand its geographical reach to the rural poor. The project will improve capacity within these intermediaries and their clients, broaden its reach to provide financing to both micro- and small businesses, and help the government reform the legal and regulatory environment for microfinance. ADB will also use the Private Sector Development Initiative to support a broader access to finance agenda including the implementation of secured transactions reform.

37. **Health.** ADB is helping the government prepare a long-term plan for rural primary health services, including innovative partnership models and arrangements for community health posts. This work will inform the follow-up project to the successful HIV/AIDS Prevention and Control in Rural Development Enclaves Project. ADB will consider supporting PPP in the health sector.

IV. RESULTS MANAGEMENT

A. Monitoring

38. **Results framework.** ADB will monitor the implementation of the CPS using the results framework (Appendix 1), which will be updated annually during country portfolio review missions and country programming missions and reported in related documentation. The sector outcome data will be compiled by sector specialists in collaboration with the sector agencies. ADB will

²² The Pacific Private Sector Development Initiative was established by ADB in 2006 with co-financing by AusAID to support efforts by ADB's Pacific Developing Member Countries to encourage private sector-led, sustainable economic growth.

monitor the continued alignment of the CPS with the government's DSP. The updated results framework will be used to confirm and modify the CPS and the country program.

39. **Sector capacity.** ADB is providing support to the key executing agencies to develop their results management capacity through training and conduct of workshops.

B. Risks

40. **Sustainability risk.** Limited and unreliable infrastructure maintenance funding poses the greatest risk to infrastructure sustainability and there is a large maintenance backlog. The limited funds available for infrastructure maintenance are programmed according to multi-year projects, but annual allocations are inconsistent and disbursements are often delayed, leading to interruptions in implementation. Landslides and floods are common and they often damage critical network links, forcing the government to reallocate funds from routine maintenance to emergency works. ADB has helped the government address sustainability risk through the creation of dedicated revenue streams, trust funds, and the promotion of cost-recovery mechanisms.²³ ADB is also supporting government efforts to establish a CSO framework that would improve the viability of infrastructure service providers and improve SOEs' ability to produce surpluses that can be used for maintenance. The approved MFFs for land and air transport provide private sector civil works contractors with an assurance of sustained funding through long-term performance-based maintenance contracts. Emphasis will also be placed on ensuring that potential PPP projects undergo a rigorous, objective, and transparent assessment process, as prescribed in the national PPP policy, with a central role played by the Department of Treasury in managing long-term fiscal risks.

41. **Efficiency and effectiveness risks.** The limited capacity of private civil works companies is a threat to both efficiency and effectiveness. The few construction contractors large enough to execute large road projects are overcommitted and seldom deliver projects on time. The lack of competition among civil works contractors raises costs and limits the recourse after poor performance. ADB will confer with the government on prioritization, coordination, and phasing of both government and externally-funded projects. High levels of public expenditure combined with the LNG project's enormous demands for construction and civil works will strain the already limited capacity of the industry. Inflationary impacts are expected to peak between 2010 and 2012. ADB will work with the government to ensure efficiency and effectiveness by carefully sequencing ADB-funded projects. ADB is also working with the National Roads Authority and other agencies to promote the entry of large foreign contractors capable of undertaking large road maintenance contracts, expand the capacity of civil works companies, and introduce competition.

²³ Institution Building in Infrastructure Sector (Appendix 2).

COUNTRY PARTNERSHIP STRATEGY RESULTS FRAMEWORK

Country Development Goals (Papua New Guinea Development Strategic Plan 2010–2030)			
1. Quality education for all; building a highly skilled workforce; creating opportunities for PNG entrepreneurs 2. Prosperity for rural areas with more transport, utilities, education, health and business opportunities 3. Two million jobs created; economy growth averaging 8.4% a year; good governance facilitates participation by PNG investors 4. Resource revenues retained by PNG for nation building while protecting the environment 5. Law and order restored; customary landowners given access to markets; society developed in a PNG way			
Sectors Selected for ADB Support			
Government Sector Objectives	Sector Outcomes that ADB Contributes to and Indicators^a	ADB Areas of Intervention	ADB Indicative Resource Allocation in the Next Pipeline and Thematic Priorities
1. Transport (Strategy 2020 Core Area 1: Infrastructure)			
Triple length of national roads to 25,000 km 100% of national roads in good condition	More efficient, safer movement of people and goods on roads in the Highlands Region 100,000 people benefiting from a 25% reduction in their travel time from their communities to nearest market from 2011 levels	Land transport policies and reforms Road maintenance and upgrading	\$550 million, 34.6% of total CPS envelope, of which: ENV – 0% RCI – 0% GEN + EGM – 50% PSD – 30%
All international airports meet international certification standards 10 airports upgraded to allow them to be used by jets with higher seating capacity	More efficient movement of people and goods through the 21 National Airports Corporation airports in a safe manner 116,000 passengers per year (2011 baseline: 100,000)	Airports, air navigation and security Development of civil aviation capacity	\$480 million, 30.2% of total CPS envelope, of which: ENV – 0% RCI – 0% GEN + EGM – 0% PSD – 30%
Triple the number of water transport routes serviced and the number of vessels, and upgrade ports Reduce international port turnaround time to 1 day	More efficient, safer, movement of people and goods through Lae and other ports and by water transport among remote communities 4.0 million revenue tons of break bulk throughput in Lae (2011 baseline: 2.8 million revenue tons)	Ports and terminal facilities Small landings, shipping Community water transport	\$284 million, 17.8% of total CPS envelope, of which: ENV – 0% RCI – 0% GEN + EGM – 50% PSD – 30%
2. Power (Strategy 2020 Core Area 1: Infrastructure)			
All households have access to a reliable and affordable energy supply, and sufficient power is generated and distributed to meet future energy requirements and demands	Improved conditions for commercial activity through consumption of reliable, sustainable, and more affordable power supply in urban areas 10% reduction in household expenditure on energy services from 2011 levels	Construction of power generation to supply demand in provincial towns and the main grids Provision of power and lighting services to unserved households	\$204 million, 12.8% of total CPS envelope, of which: ENV – 33% RCI – 0% GEN + EGM – 50% PSD – 30%

3. Public Sector Management (2020 Core Area 1: Infrastructure)			
High standards of public sector management at all levels and in all institutions of government More transparency in SOEs' service delivery	More effective and efficient utilization of public finances for service delivery and infrastructure provision; and lower cost of doing business ADB country performance assessment indicators 8a increase to 4.0 (2011 baseline: 3.0)	Stronger oversight of statutory authorities, improved project evaluation and prioritization	\$2 million, 0.1% of total CPS envelope, of which: ENV – 0% RCI – 0% GEN + EGM – 0% PSD – 50%
4. Trade (2020 Core Area 3: Regional Cooperation and Integration)			
Flourishing trade with the rest of the world Border economic corridor to integrate development and broad-based growth	Increased flow of goods and services across the border 10% increase in the total amount of agriculture commercially produced and 34 % increase in the amount of subsistence agriculture production, both from 2011 levels.	Development of border infrastructure for customs, immigration, and quarantine	\$25 million, 1.7% of total CPS envelope, of which: ENV – 0% RCI – 100% GEN + EGM – 0% PSD – 30%
5. Finance (2020 Core Area 4: Financial Sector Development)			
Stronger financial and banking services Small and medium-sized enterprises developed and promoted	Financial institutions sustainably and safely provide financial services to a substantially increased number of clients across PNG 100,000 increase in households with active deposit accounts from 2011 levels	Expansion of microfinance services to rural areas Collateral or secured transaction reforms	\$24 million, 1.5% of total CPS envelope, of which: ENV – 0% RCI – 0% GEN + EGM – 20% PSD – 50%
6. Health (Other Areas of Operations)			
Efficient health system which delivers an internationally acceptable standard of health service Healthy population, free from sexually transmissible infections and HIV/AIDS threats	Greater and more equitable utilization of quality primary health services in rural catchment areas Percentage of pregnant women receiving antenatal care at least once increased from 61% to 66% Percentage of children immunized against DPT3 increased to from 61% to 70%	Rehabilitation of rural health facilities and provision of minimum standards for quality primary health care services in rural catchment areas	\$20 million, 1.3% of total CPS envelope, of which: ENV – 0% RCI – 0% GEN + EGM – 50% PSD – 30%

ADB = Asian Development Bank, CPS = country partnership strategy, EGM = effective gender mainstreaming, ENV = environmental sustainability, GEN = gender equity, PNG = Papua New Guinea, PSD = private sector development, RCI = regional cooperation and integration.

Source: PNG Development Strategic Plan, 2010–2030; Sector Assessments (Appendix 2).

^a By 2015.

LIST OF LINKED DOCUMENTS

<http://www.adb.org/Documents/CPS/?id=PNG-2011>

1. Economic Analysis (Summary): Asian Development Outlook 2010 (Papua New Guinea)
2. Poverty Analysis (Summary)
3. Gender Analysis (Summary)
4. Environment Assessment (Summary)
5. Private Sector Assessment (Summary)
6. Sector Assessment (Summary): Transport
7. Sector Assessment (Summary): Power
8. Sector Assessment (Summary): Public Sector Management
9. Sector Assessment (Summary): Finance
10. Sector Assessment (Summary): Health
11. Sector Assessment (Summary): Trade
12. Risk Assessment and Risk Management Plan (Summary)
13. Country and Portfolio Indicators
14. Country Performance Assessment Ratings
15. Country Cost-Sharing Arrangements and Eligible Expenditure Financing Parameters
16. Country Partnership Strategy Formulation
17. Country Strategy and Program Final Review
18. Country Operations Business Plan

Supplementary Documents

19. Transport Sector Assessment
20. Institution Building in Infrastructure Sector
21. Civil Works Capacity Constraints
22. Fragile Situation Assessment
23. Sector-Level Risk Assessment and Risk Management Plan