

## SECTOR ASSESSMENT (SUMMARY): PUBLIC SECTOR MANAGEMENT<sup>1</sup>

### Sector Road Map

#### 1. Sector Performance, Problems, and Opportunities

1. **Summary.** Papua New Guinea's (PNG) economic situation is volatile, with a narrow economic base highly reliant on global commodity prices for its natural resources exports. Absent of vibrant private sector activity, and an extensive subsistence economy, large natural resource investment projects and public spending drive growth. Public service delivery is inadequate, both due to insufficient financing and weak government capacity for policy development and implementation. The latter also delays responsiveness to pressing macroeconomic challenges, including a conducive monetary policy and structural reforms to promote private sector development. In this context, the government needs to implement critical reforms that lead to better allocation and use of public resources for growth and development. The Health Services Sector Development Program supports public sector management (PSM) (and health) reform prioritization, sequencing, and implementation; addresses development financing needs; and incentivizes reform implementation.

2. **Policy and institutional performance.** According to the Asian Development Bank's country performance assessment (CPA), PNG's policy and institutional performance gradually improved until 2012–2013 and has since been deteriorating across all four CPA components (economic management, structural policies, policies for social inclusion, and public sector management and institutions). The equal-weighted average score of the CPA for PNG decreased from 3.4 to 2.9 (on a scale from 0 to 6) from 2012–2016.<sup>2</sup> A steep fall in scores in 2016 coincides with the prolonged downturn in global commodity prices and the resulting deteriorating economic and fiscal situation in PNG, exemplifying the impact of external shocks on weak public institutions and the inability of policy-makers and the public administration to respond to such shocks swiftly.

3. **Macroeconomic management.** PNG continues to face headwinds from weaker global prices for its export commodities. This follows more than a decade of strong, uninterrupted growth—averaging 6.8% per annum—supported by high global commodity prices and large private investments in the mineral sector. In 2014 total exports increased by 47.2% on the back of LNG exports but, with the downturn in global commodity prices, export growth reduced to 1.6% in 2015 and contracted by 6.4% in 2016. Similarly, non-resource exports, particularly agriculture, sharply slowed down as outputs were adversely affected by drought. Increasing exchange rate flexibility. Limited exchange rate flexibility led to an overvaluation of the Kina, which, together with associated foreign exchange restrictions and rationing by the Bank of PNG, is contributing to weakness in business activity and growth. Over the longer term, sustained overvaluation of the currency will inhibit development of the non-resource sector (footnote 1).

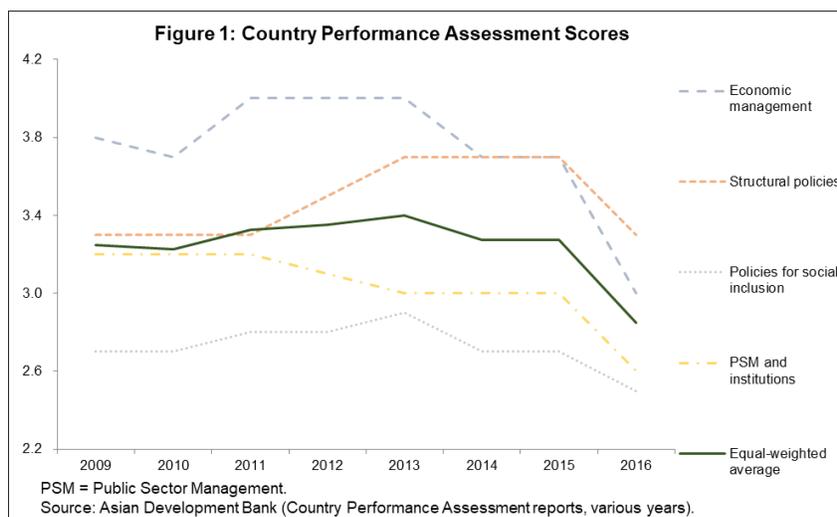
4. **Fiscal management.** After a period of fiscal consolidation and public debt reduction from 2008 to 2012, an expansionary fiscal policy stance from 2012–2014 coinciding with a falling domestic-revenue-to-gross domestic product (GDP) ratio driven by weakening global commodity prices led to rise in fiscal deficit from 0.2% of GDP in 2011 to an unsustainable 9.6% of GDP in

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<sup>1</sup> This summary is based on International Monetary Fund (IMF). 2017. *Papua New Guinea 2017 Article IV Consultation Staff Report*. IMF Country Report No. 17/411. Washington, DC; IMF. 2015. *Papua New Guinea: Public Expenditure and Financial Accountability Assessment*. Washington, DC; and various other documents referenced in footnotes throughout the document.

<sup>2</sup> The equal-weighted average referred to here does not include country portfolio performance and does not follow the composite country performance rating calculation formula.

2013 and 8.3% in 2014 before drastic cuts in expenditure led to gradually reducing deficits in subsequent years.<sup>3</sup> Tax revenue fell from 18.6% of GDP in 2013 to 12.5% in 2016, and resource revenue from 7.4% of GDP in 2011 to 0.6% in 2016, both together severely undermining sustainable financing of public goods and services (footnote 1). Gross government debt rose from 24.9% of GDP to an expected 35.4% in 2017, with a changing maturity profile to shorter tenor, which raises interest and rollover risks (footnote 1).

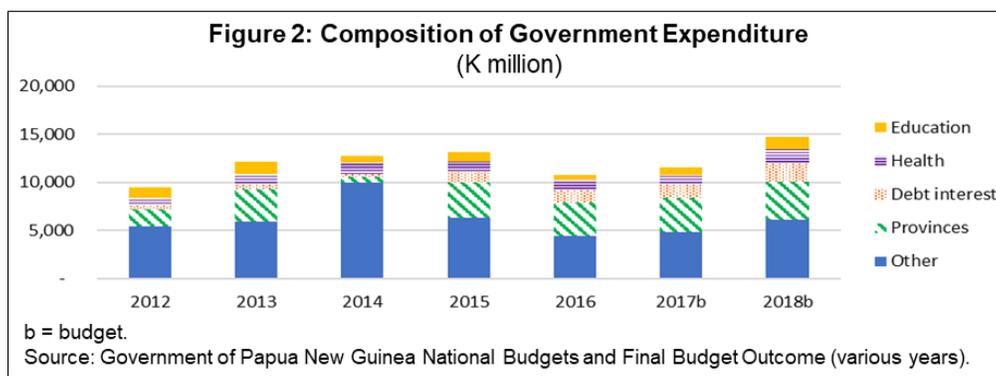


5. **Expenditure prioritization.** The government has been prioritizing allocations for key enablers identified in its development plans, including health and education, and has devolved an increasing share of the budget to subnational government levels. While all sectors were affected from overall spending cuts, allocations for essential health services were largely protected and saw an increase in the 2018 budget. However, original budget allocations are rarely fully funded, and funds flows significantly delayed throughout the fiscal year, partially due to large lumpy tax payments towards the end of the fiscal year. Furthermore, shortcomings in budget classification and formats do not allow an accurate functional overview, e.g., provincial allocations include subnational sector funding, including for health (Figure 2). Resulting from a combination of increasing government debt and interest rates, a concerning development are growing debt servicing costs that increasingly crowd out priority sector spending.

6. **Public financial management.** A public expenditure and financial accountability (PEFA) assessment in 2015 indicated positive performance on credibility of fiscal strategy and budget, and policy-based planning and budgeting while PNG performed weak in the quality, availability, comprehensiveness, and timeliness of fiscal accounts; management of public assets and associated fiscal risks; accountability; and comprehensiveness and transparency (footnote 1).<sup>4</sup> Limited coverage of an up-to-date integrated financial management system (IFMS), currently operational in 43 national government entities and five statutory authorities, hinders the adequate management, accounting and reporting of public funds, blurring transparency and accountability. Public procurement is constrained by an incomplete legal framework including the lack of an independent complaints mechanism, and weak systems and capacity, leading to a lack of procurement planning and frequent interference with procurement processes. Streamlining the government payroll and continued strengthening of subnational public financial management (PFM) systems will further be critical to increase expenditure control and effectiveness.

<sup>3</sup> Country Economic Indicators (accessible from the list of linked documents in Appendix 2).

<sup>4</sup> Sector Development Program Impact Assessment (accessible from the list of linked documents in Appendix 2).



## 2. Government's Sector Strategy

7. **Public sector reform strategies.** The country's cascading strategic planning framework, with the PNG Vision 2050, PNG's Development Strategic Plan (2010–2030), and Medium Term Development Plan 2 (2016–2017), outlines PNG's high-level commitment to effective leadership, good governance, performance management and accountability aiming to provide service delivery and ultimately quality of life improvements.<sup>5</sup> The new O'Neill led government reiterated its commitment to stable law and order, responsive and transparent fiscal policies, capacity building through strengthened leadership and discipline, and the delivery of essential services for its term covering 2017–2022.<sup>6</sup> The implementation of these high-level plans and commitments is done through a number of strategies and reform plans, including:

- (i) The Treasury 100 Day, 25 Point Plan that aims to ensure sound macroeconomic and fiscal management to restore confidence and generate investment.<sup>7</sup> The plan outlines an ambitious reform program covering fiscal policy and debt management, tax reform and administration strengthening, procurement reform, and broad structural reforms.
- (ii) National Budget for FY2018, which outlines a medium-term fiscal strategy, 2017–2021 and a domestic revenue mobilization strategy to gradually reduce the fiscal deficit and bring public finances on a more sustainable path.<sup>8</sup>
- (iii) PEFA Road Map, 2015–2018, which aims to close gaps identified in an external PEFA assessment of 2015.<sup>9</sup> One of the priorities is the roll out of the IFMS.
- (iv) PFM Sub-national Strategy and an IFMS Sub-National Roll Out Plan aiming to strengthen PFM to enhance service delivery in provinces and districts.<sup>10</sup>

8. **Implementation of sector strategies.** As indicated by the CPA, government agencies' capacity to implement reform measures is severely constraint by weak management and technical expertise, a small skills pool, limited financial resources, and an infant performance management system. The track record of progress against implementation strategies and set targets has

<sup>5</sup> Independent State of Papua New Guinea. 2009. *Papua New Guinea Vision 2050*. Port Moresby; Government of Papua New Guinea (GoPNG), Department of National Planning and Monitoring. 2010. *Papua New Guinea Development Strategic Plan, 2010–2030*. Port Moresby; and Independent State of Papua New Guinea. 2015. *Papua New Guinea Medium Term Development Plan 2, 2016-2017*. Port Moresby.

<sup>6</sup> Government of Papua New Guinea. 2017. [Alotau Accord II](#).

<sup>7</sup> Department of Treasury. 2017. *The Treasury 100 Day, 25 Point Plan*. Port Moresby.

<sup>8</sup> Independent State of Papua New Guinea. 2017. *2018 National Budget, Volume 1: Economic and Development Policies*. Port Moresby.

<sup>9</sup> Government of Papua New Guinea. 2015. *Public Expenditure and Financial Accountability Road Map, 2015–2018*. Port Moresby; Footnote 1.

<sup>10</sup> Department of Finance. 2017. *Public Financial Management Sub-National Strategy*. Port Moresby; and Department of Finance. 2017. *Integrated Financial Management System Sub-National Roll Out Plan*. Port Moresby.

therefore been mixed and there is a risk that reform implementation stalls due to dwindling political reform commitment, the complex political economy, limited internal capacities, and/or lacking external assistance. Sector strategies and reforms therefore need to be strategic, highly prioritized and sequenced while implementation support is required via technical assistance (TA).

### 3. ADB Sector Experience and Assistance Program

9. **Strategic direction.** ADB's country partnership strategy (CPS) and country operations business plan, 2018–2020 for PNG are aligned with the government's planning frameworks, including the Papua New Guinea Development Strategic Plan, 2010–2030.<sup>11</sup> PSM is one of the five sector priorities highlighted in the CPA, with a specific focus on increasing PSM accountability and transparency so that the government can more effectively and efficiently translate growing public revenues into delivering services and providing infrastructure.

10. **Past and ongoing engagement.** ADB has been actively engaged in PSM through three complementary avenues: (i) ongoing economic and policy reform dialogue, including as part of ADB's economic monitoring and the annual CPA exercise; (ii) TA in fiscal management, PFM, and private sector development; and (iii) the design and implementation of policy reforms linked to the policy-based loan component of the Health Services Sector Development Program (HSSDP). Particularly relevant for the HSSDP is ADB's ongoing TA support in fiscal management and strategic budgeting, which builds upon two previous TA phases that strengthened the oversight and accountability of statutory authorities, improved project evaluation and prioritization, supported procurement reform efforts, and enhanced subnational service delivery monitoring, among others.<sup>12</sup> The HSSDP also introduced a technical working group comprising the Departments of Treasury, Finance, National Planning and Monitoring, and Health to lead policy reform design, implementation progress tracking, and inter-agency coordination. The HSSDP will address several priorities of the PEFA Road Map, 2015–2018 (footnote 9), which are directly relevant for PFM and service delivery in health.<sup>13</sup>

11. **Development partner collaboration.** Partnerships continue to be an important element of ADB's engagement in PNG. Regular consultations between the main partners in the PSM space—the International Monetary Fund, the World Bank, the Australian government and its PNG Governance Facility, and the European Union—and with government aim to ensure that support is aligned to government priorities, duplications are avoided and that the government's TA needs are comprehensively addressed.<sup>14</sup> Consultations take place as part of ADB's CPS development, intervention design, and through ongoing economic and policy reform dialogue. The International Monetary Fund leads the engagement in macroeconomic, monetary and financial sector policy, including through annual Article IV consultations. World Bank assistance focusses on revenue reform and sector engagement including in health. The Australian government provides extensive support across reform areas, complemented by European Union support in PFM.

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<sup>11</sup> ADB. 2015. *Country Partnership Strategy: Papua New Guinea, 2016–2020*. Manila; ADB. 2017. *Country Operations Business Plan: Papua New Guinea, 2018–2020*. Manila; Footnote 5.

<sup>12</sup> ADB. 2009. *Technical Assistance to Papua New Guinea for Supporting PFM*. Manila; ADB. 2012. *Technical Assistance to Papua New Guinea for Supporting PFM (Phase 2)*. Manila; and ADB. 2016. *Technical Assistance to Papua New Guinea for Supporting PFM (Phase 3)*. Manila.

<sup>13</sup> See (i) Sector Assessment (Summary): Health for details on health sector PFM challenges and (ii) Links between Public Financial Management Reform Priorities and the Sector Development Program (accessible from the list of linked documents in Appendix 2).

<sup>14</sup> The HSSDP technical working group (para. 10) could evolve into a broader government–development partner policy reform coordination mechanism in the future.

## Problem Tree for Public Sector Management

