PAPUA NEW GUINEA

Growth slowed in 2023 on lower resource output, while foreign exchange restrictions and frequent power supply disruptions stifled other economic activity. The resumption of full production at the Porgera gold mine should accelerate growth in 2024 and 2025, but civil unrest in January this year and a poor business environment cloud the outlook. Energy reforms such as tariff adjustments are urgently needed to improve economic prospects.

Economic Performance

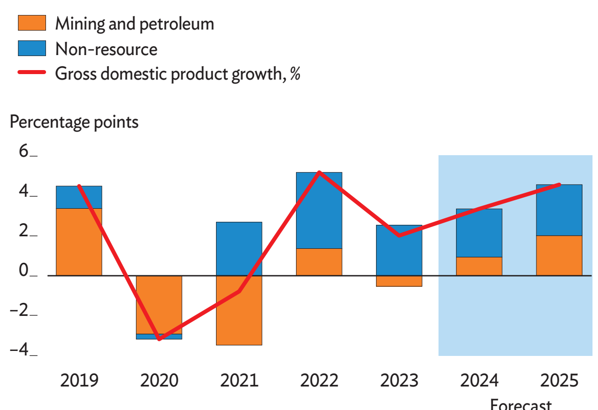
Growth slowed to an estimated 2.0% in 2023 as resource output weakened (Figure 2.34.1). Production of gold and liquefied natural gas (LNG) fell below 2022 levels, resulting in a 2.0% contraction in the resource sector. A combination of maintenance and bad weather affected gold production, while scheduled maintenance lowered output at the LNG plant.

The non-resource sector expanded moderately by an estimated 3.4%. Easing global supply chain disruptions supported growth in manufacturing along with information and communications. Increased government spending provided stimulus to education, health, and public administration. However, after a spike in 2022, the fall in global commodity prices—including those for the country's key agricultural exports—weakened economic activity. Low palm oil production also slowed growth in agriculture.

Several business impediments, including a lack of foreign exchange, stifled non-resource economic activity. Despite the central bank's increased interventions in 2023 to provide foreign exchange to the market, businesses continued to struggle with timely access, hindering restocking and investment. The protracted and unresolved dispute between Puma Energy, the country's near-monopoly fuel supplier, and the central bank over forex and regulatory issues affected transport. Other setbacks to business operations last year included disruptions to power and water supply, frequent cancellations and delays in domestic flights due to technical issues with Air Niugini's aging fleet, and glitches in banking transactions. Sales in various sectors were reported to have dropped substantially during the year.

Figure 2.34.1 Supply-Side Contributions to Growth

Growth slowed in 2023 as resource output contracted.



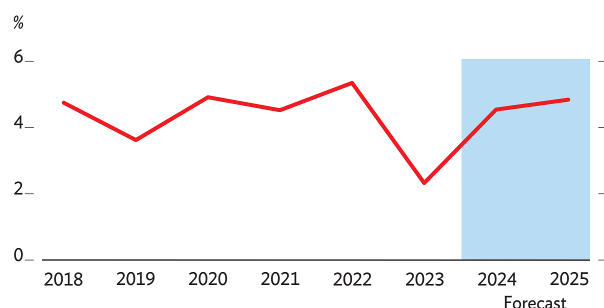
Source: Asian Development Bank estimates using data from Papua New Guinea National Statistical Office.

Headline inflation slowed, but prices of essential consumer items continued to surge. The consumer price index (CPI) rose by 2.3% in 2023, down from 5.3% in 2022 (Figure 2.34.2). This was mostly driven by a one-off decrease of 22.9% in education costs as the government implemented its Tuition Fee Free

This chapter was written by Marcel Schroder and Magdelyn Kuari of the Papua New Guinea Resident Mission, ADB, Port Moresby.

Figure 2.34.2 Inflation

A one-off drop in education costs brought down inflation, but prices rose for many consumer goods and services.



Sources: Papua New Guinea National Statistical Office; Asian Development Bank estimates.

Education Policy. Inflation decelerated for several CPI components, including housing, communications, recreation, and alcoholic beverages, tobacco, and betelnut. However, costs for many essential consumer goods and services soared. Prices for food and non-alcoholic beverages rose by 7.0%, household equipment by 9.0%, and clothing and footwear by 7.0%.

A supplementary budget in November 2023 estimated the fiscal deficit at 4.4% of GDP. The government's fiscal consolidation plan continued to reduce the fiscal deficit from 5.3% of GDP in 2022. Although total expenditure increased through the operational budget, it was offset by additional revenue from taxes on salaries and wages. Public debt rose to the equivalent of 52.6% of GDP. An IMF program approved in March 2023 supports further fiscal consolidation to promote both external and overall debt sustainability. The IMF's first review report in December found that the government was meeting all end-June 2023 criteria and implementing its structural benchmarks.

Economic Prospects

Growth is projected to accelerate to 3.3% in 2024 and 4.6% in 2025 on strong mining output (Table 2.34.1). Following the conclusion of the Porgera Project Commencement Agreement, the Porgera gold mine resumed operation on 22 December 2023, ending almost 4 years of closure. The mine produced its first gold in February and full production is expected

Table 2.34.1 Selected Economic Indicators, %

Strong mining performance will drive growth in 2024 and 2025.

	2022	2023	2024	2025
GDP growth	5.2	2.0	3.3	4.6
Inflation	5.3	2.3	4.5	4.8

GDP = gross domestic product.
Source: Asian Development Bank estimates.

to resume in the third quarter. Along with increased output from Ok Tedi and Lihir in 2025—the other two major mines—the sector is expected to grow by 10.0% in 2024 and 23.4% in 2025. In the petroleum and gas sector, production at newly drilled wells will likely support growth in 2024, before flattening afterward.

Porgera's reopening should generate growth spillovers to the rest of the economy. The mine's reopening should create additional operation-related spending on goods and services, employment, and provide foreign exchange inflows. A boost in cocoa and copra oil production, while somewhat offset by slight decreases in coffee and copra output, is expected to support growth in agriculture, forestry, and fisheries. Continued government spending should boost growth in construction. Several favorable developments should help transport's prospects. Air Niugini, the national airline, has temporarily leased a Boeing 737, reducing flight delays and cancellations. The airline will purchase six new aircraft and lease five more to replace its ageing fleet. The first plane is scheduled to join Air Niugini's fleet in 2025. Further stimulus will be provided by a new airport terminal in Lae and a roundtrip flight connection between Port Moresby and Guangzhou in the People's Republic of China that began in late December 2023.

Forex restrictions, the foremost business constraint, could ease under the IMF program this year. The central bank has allowed the Kina to depreciate gradually, bringing it closer to a market rate. To promote a steady transition to greater exchange rate flexibility under the IMF program, a limit on unmet import-related forex orders has been established. Set initially at $150 million in January 2024, the ceiling will be reduced each quarter, reaching $75 million in December.

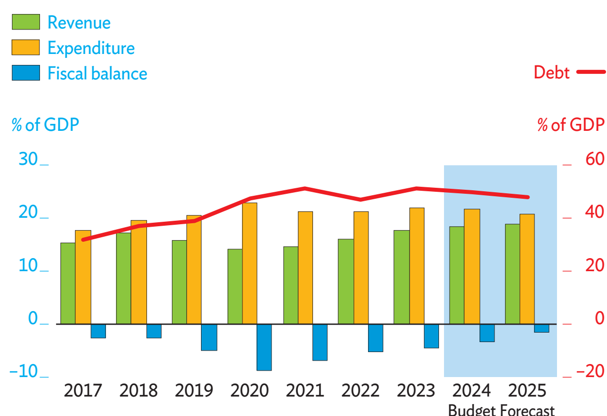
Civil unrest in January and ongoing challenges such as power supply disruptions cloud the outlook. Strikes by law enforcers over a pay cut resulted in looting and damaging retail shops throughout the capital Port Moresby. The unrest spread to other provinces but was swiftly contained. In total, 53 businesses were affected with an estimated damage of about K1.2 billion (1.2% of GDP) and 2,000 jobs lost. These losses, combined with shaken investor and consumer confidence, will decrease spending. Persisting forex restrictions will cause delays and higher costs for businesses in rebuilding lost capacity, replenishing stocks, and expanding operations. Disruptions to power and water supply in the main urban centers will also affect business operations in key sectors. Especially in Lae, the country's manufacturing and logistics hub, businesses face frequent blackouts and power fluctuations, forcing them to rely on generators to maintain operations, escalating operational costs and affecting competitiveness. In February and March, Puma Energy again limited fuel supplies over forex issues, affecting mobility across the country.

Headline inflation is expected to rise because of base effects, exchange rate depreciation, and civil unrest. Education subsidies will continue, but their disinflationary effect will dissipate throughout the year. While slowing global inflation lowers imported inflation, it is counterbalanced by further exchange rate depreciation as the central bank moves to a market-determined exchange rate. Domestic inflation could rise because of supply issues caused by the civil unrest. To assist businesses affected by the looting and the wider economy generally, the central bank lowered the Kina Facility Rate, its main monetary policy instrument, from 2.5% to 2.0% in February, where it will likely remain. Overall, inflation is projected to accelerate to 4.5% in 2024 and 4.8% in 2025. However, El Niño could disrupt agriculture and lead to higher commodity prices.

The government's fiscal consolidation aims to balance the budget by 2027. The consolidation strategy involves domestic revenue mobilization while restraining and rationalizing spending. The government plans to further reduce the fiscal deficit to 3.3% of GDP in 2024 and 2.0% of GDP in 2025 (Figure 2.34.3). As a result, public debt is projected to decrease to 51.1% of GDP in 2024 and 49.2% of GDP in 2025. Under the IMF program, the country must limit the present value of new external borrowing to $1,072 million in 2024 and keep the fiscal deficit at or below K4,810 million (3.9% of GDP).

Figure 2.34.3 Fiscal Balance and Debt

Under the national budget, the fiscal deficit will be reduced to 2.0% of GDP in 2025.



GDP = gross domestic product.
Source: Papua New Guinea Department of Treasury.

Revenue growth is projected to outweigh expenditure growth, subject to risk. Revenue excluding development partner grants is projected to increase in 2024 by K2.8 billion (2.6% of GDP) mainly from taxes on profits, salaries, and wages, and non-tax revenue. Expenditure will grow less, by K1.86 billion (1.8% of GDP). The capital budget allocation is projected to increase by 9.0%, the operations budget by 8.0%, and the payroll bill by 1.3%. These projections are, however, at risk because they do not consider the damage from the social unrest and potential government assistance to affected businesses. Executing the budget will continue to depend on support from bilateral and multilateral development partners.

Risks to the outlook are predominantly on the downside. A key threat is any delay to resumption of full production at Porgera. Other downside risks include worsening law and order conditions and forex access, and an escalation in a dispute on fuel supply that could severely affect mobility. Disaster and weather-related events such as El Niño are threats to agricultural output. A major upside risk, subject to increasing uncertainty, is the start of Papua LNG, a multibillion-dollar gas project. After progressing to the front-end

engineering and design phase in March 2023, several related factors have delayed a final investment decision. These include regulatory approvals, environmental issues, gas marketing, and securing financing.

Policy Challenge—Reforming the Energy Sector

Unreliable power supply limits economic growth in the main urban areas. The electricity supply is generally poor and blackouts are frequent because of inadequate generation capacity and aging networks. Self-generation and backup generation (entirely diesel-based) are common for business and residential areas and have increased over recent years due to repeated blackouts. Operation and maintenance costs of power generation are high, but efficiencies low. The power utility, PNG Power Limited (PPL), has deprioritized maintenance on its network and generation assets because of the utility's deteriorating financial condition. This is driven by low tariffs, last adjusted in 2013, which barely recover PPL costs, and high technical and commercial losses. Aging network infrastructure leads to high losses, while electricity theft, illegal connections, and a low bill collection rate leave PPL with revenues well below expenses.

PNG lacks a national government-led plan for energy sector development. PPL instead conducts internal generation and grid planning that is neither backed nor aligned with the national regulator or the government's national budget financing plan. Since 2013, private sector participation has been allowed in power generation. As a result, independent power producers (IPPs) have made ad hoc investments that are not coordinated with grid development. Although the government set a target in 2010 to achieve 70% electrification by 2030, less than 20% of the population can currently access electricity.

The transition from diesel generation to cheaper and cleaner renewable energy resources is limited. Although PNG has abundant renewable energy resources—hydropower, solar, wind, biomass, and geothermal energy—these have not been fully explored or utilized. Hydropower has been the backbone of the country's power supply, but its role has diminished over the years, with limited new capacity added. Despite excellent solar potential and high returns on investments for many locations in the country and good alignment with peak power demand during the day, photovoltaics have not been deployed at a utility scale. Legal barriers and restrictions on behind-the-meter renewable energy installations block the development of private firms' solar photovoltaic. Hence, rooftop photovoltaic panels have been limited to small off-grid applications.

Reforms in three key areas are needed to improve power generation and promote growth. The first is to restore the financial sustainability of the power sector by adjusting tariffs and improving the utility's operations. The regulator needs to establish a process and methodology for independent annual tariff adjustments, while considering the effects on poor and vulnerable households. PPL also needs to develop a comprehensive revenue strategy to reduce commercial losses and public sector payment arrears, and to connect more commercial customers. Second, there is a need to create a national transition plan to a low-carbon power sector, including guidelines to prioritize and fund power sector infrastructure. The government further needs to issue national regulations related to planning, implementation, and monitoring. This includes removing legal barriers and restrictions to renewable energy installations. And third, reforms are needed to enable efficient private sector involvement in the power sector. This requires issuing regulations on the process of competitive bidding for IPP investment. Open, transparent, and competitive tenders with bankable power purchase agreements will attract private sector investment, while promoting technical efficiency and cost-competitiveness.