



BANK OF PAPUA NEW GUINEA

MONTHLY ECONOMIC REVIEW

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Volume: 3

No. 12

Month Ended: December 2016

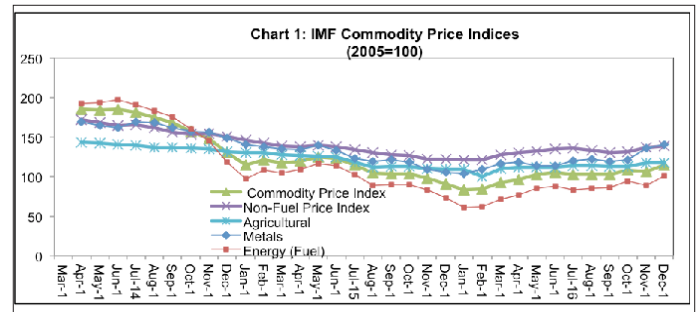
Economic Activity

Global economic growth remained low in 2016, with varying performances across regions. In December, good performance was noted in some of the major economies. In the US, a steady recovery continued on the back of favourable labour market conditions, while the federal funds rate target range was raised by 0.25 percent to 0.50 to 0.75 percent from 0.25 to 0.50 percent in anticipation of inflationary pressures. Activity in the UK remained strong, mainly driven by the services sector, as well as the export sector resulting from the depreciation of the pound sterling. In the Euro area, growth remained resilient, reflecting the expansion in the manufacturing sector. In Japan, the manufacturing sector expanded amidst the falling yen and rising import prices. China's slowdown continued as the service sector contracted, which more than offset the expansion in the manufacturing sector.

In the domestic economy, there were some good foreign exchange inflows from the mining and agriculture sectors in the last quarter of 2016 with improved prices for some of the commodities and increased production. This assisted in meeting some of the outstanding import orders in the domestic foreign exchange market. Consumption demand was strong as consumers spent for the Christmas and new year festive season.

Commodity Prices

Preliminary data from the International Monetary Fund (IMF) available on the 10th of January 2017 show that the commodity price index increased by 7.5 percent in December 2016. Energy prices recorded a marked increase of 13.0 percent, mainly reflecting sharp increase of 16.30 percent in crude oil prices to US\$51.1 per barrel in December. This was attributed mainly to the agreement by the Organisation of Petroleum Exporting Countries (OPEC) members to cut production. Metals and non-fuel price indices increased by 3.81 percent and 1.39 percent, respectively, while prices for agricultural commodities marginally declined by 0.16 percent (Chart 1). Improvements in commodity prices for some of PNG's key exports were noted for crude oil, palm oil and copra, while for others there were declines. LNG prices remained unchanged for three consecutive months.



Source: IMF

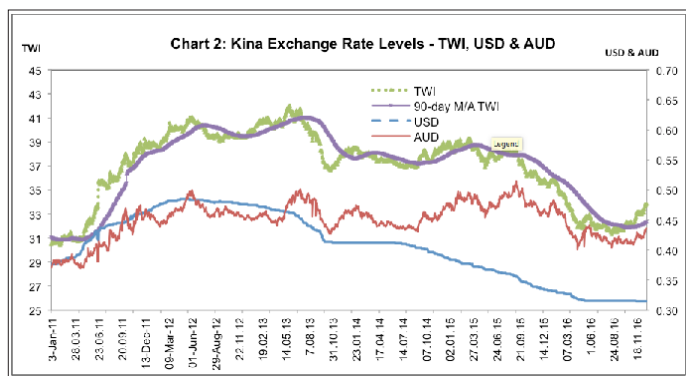
Balance of Payments

Preliminary balance of payments data for the ten months to October 2016 show an overall surplus of K298.8 million, compared to a deficit of K166.2 million in the corresponding period of 2015. A surplus in the current account more than offset a deficit in the capital and financial account. The surplus in the current account was mainly due to a higher trade surplus and lower net transfer payments. The deficit in the capital and financial account came from net outflows in portfolio and other investments, reflecting investments in short term money market instruments and a build-up in net foreign assets of commercial banks, and offshore foreign currency account balances of resident mineral companies. These more than offset inflows from net Government loan drawdowns. The level of gross foreign exchange reserves at the end of October 2016 was K5,526.1 (US\$1,705.0) million, sufficient for 13.0 months of total and 21.2 months of non-mineral import covers. As at 30th December 2016, the level of gross foreign exchange reserves was US\$1,685.4 (K 5,266.9) million.

Exchange Rate

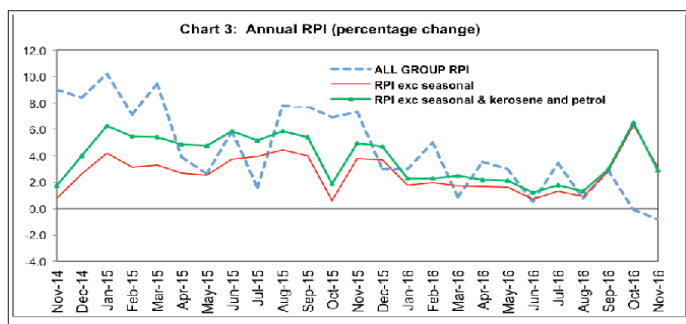
The average kina exchange rate depreciated against the US dollar (USD) by 4 basis points to US\$0.3150, while it appreciated against the Australian dollar (AUD) by 98 basis points to AU\$0.4255 from AU\$0.4157 over the month to 23rd December 2016. The depreciation against the USD was mainly due to high import demand. The appreciation against the Australian dollar was a result of the depreciation of the AUD against the USD. The AUD weakened against the USD due to interest rate differentials in favour of the US. Between the end of 2015 and 23rd December 2016,

the average Trade Weighted Index (TWI) decreased by 4.3 percent to 33.87, reflecting the depreciation of the kina against most major trading partner currencies, including the USD and AUD. (Chart 2)



Inflation

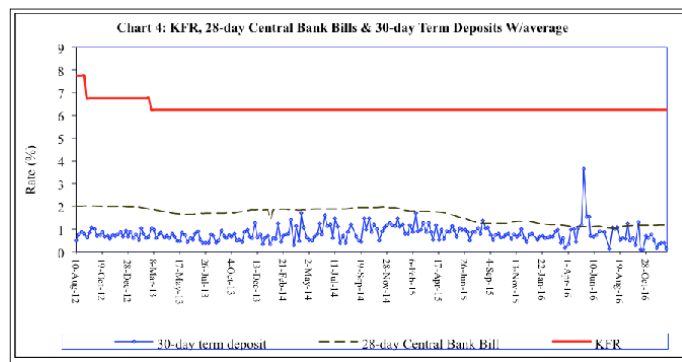
Annual headline Retail Price Index (RPI) to November 2016, decreased by 0.8 percent compared to a decline of 0.1 percent in October 2016. The decrease was attributed to declines in the 'Food' and 'Drinks, tobacco and Bitternut' expenditure groups of 1.8 percent and 0.1 percent, respectively. The decline in the 'food' expenditure group was accounted for by a 17.4 percent fall in the Fruit and vegetable prices. The decline in the 'Drinks, tobacco and Betelnut' expenditure group reflected declines in bitternut, soft drinks and cigarettes and tobacco prices by 10.2 percent, 4.5 percent and 2.8 percent, respectively. Annual RPI ex-seasonal and RPI ex-seasonal & fuel increased by 3.1 percent and 2.9 percent, respectively. Quarterly headline RPI increased by 3.4 percent, while monthly headline RPI for November 2016 increased by 1.2 percent (Chart 3).



Domestic Interest Rates & Monetary Aggregates

Over the month to week-ending 16th December 2016, the Central Bank Bill (CBB) rate for 28 days term remained at 1.18 percent, while there were no auctions for the other terms. At the Treasury bill market, the 63-day rate was unchanged at 2.40 percent, while the 91-day declined from 2.63 percent to 2.61 percent. The 182-day rate remained at 4.72 percent, while the 364 day rate increased from 7.73 percent to 7.74 percent. During the same period, the weighted average interest rates on wholesale deposits above K500, 000 increased for all maturities, except for the 180-day term. The weighted average rates for the 30days, 60 days, and 90 days increased to 0.41 percent, 0.61 percent,

and 1.95 percent from 0.16 percent, 0.57 percent, and 1.71 percent, respectively. The increase in rates reflect the uneven distribution of liquidity among banks, with banks low on liquidity offering high rates to attract deposits. (Chart 4).



Broad money supply increased by 13.4 percent over the year to November 2016, compared to an increase of 5.2 percent in the corresponding period of 2015. This was driven by increases in net claims on the Government and credit to private sectors, as well as increase in claims on public non-financial corporation sector (SOEs). Monetary base grew by 3.6 percent over the year to November 2016, compared to a decline of 0.9 percent in the corresponding period of 2015. This was mainly due to increases in currency in circulation and deposits of the commercial banks at the Central Bank.

Commercial bank lending extended to public non-financial corporations, other financial corporations and other resident sectors increased by K1,207.2 million to K12,862.1 million between December 2015 and week-ending 16th December 2016. Over the year to 16th December 2016, the weekly average lending by banks increased by 10.9 percent to K12,211.3 million. This mainly reflected advances to the finance, mining, petroleum, retail, construction, retail, SOEs, transport, manufacturing and fisheries sectors. Deposits at commercial bank deposits increased by K608.9 million to K20,965.0 million between December 2015 and week-ending 16th December 2016, reflecting placements by the mining, petroleum, Government, communication, finance, agriculture and services sectors. Over the year to 16th December 2016, the weekly average deposits declined by 4.4 percent to K20,405.6 million.

Soundness of the Financial System

As at the end of September 2016, total assets of the financial system stood at K47.0 billion. Commercial banks accounted for 70.6% of this total, other depository corporations accounted for 5.3 percent while other financial corporations (including superannuation funds) accounted for 24.1 percent. Total deposits were K27.0 billion. Commercial banks accounted for 94.8 percent while licensed financial institutions, microfinance institutions and savings & loan societies accounted for 2.4 percent, 0.7 percent, and 2.1 percent, respectively. Total loans were K17.3 billion. The ratio of non-performing loans to total loans was 3.2

percent, whilst the ratio of non-performing loans to total assets was 1.6 percent. Total Capital Adequacy ratio was 33.5 percent while the adequacy ratio for Tier 1 Capital was at 26.4 percent, well above the regulatory requirements of 12.0 and 8.0 percent, respectively. Return on Assets was at 1.7 percent while Return on Equity was at 21.3 percent.

Monetary Policy

The Bank's policy signalling rate, the Kina Facility Rate (KFR) was maintained at 6.25 percent for the month of December 2016.

Papua New Guinea Key Economic Indicators													
		Jan-16	Feb-16	Mar-16	Apr-16	May-16	Jun-16	Jul-16	Aug-16	Sep-16	Oct-16	Nov-16	Dec-16
1. Consumer Price Index (CPI)	Headline	-	-	6.5	-	-	6.8	-	-	6.8	-	-	-
	Food	-	-	5.9	-	-	6.4	-	-	5.3	-	-	-
	Underlying	-	-	3.1	-	-	2.9	-	-	2.0	-	-	-
2. Retail Price Index (RPI) (YOY % Change)	Headline	3.0	5.0	0.8	3.4	3.0	0.5	3.4	0.8	2.9	-0.1	-0.8	na
	Ex-seasonal	1.8	2.0	1.6	1.5	1.6	0.7	1.3	0.9	2.8	6.3	3.1	na
3. Exchange Rates (mid-rate, eop*)	USD	0.3295	0.3280	0.3225	0.3175	0.3160	0.3160	0.3155	0.3155	0.3155	0.3155	0.3150	0.3150
	AUD	0.4624	0.4598	0.4224	0.4150	0.4363	0.4259	0.4198	0.4199	0.4137	0.4145	0.4215	0.4354
	GBP	0.2289	0.2364	0.2251	0.2169	0.2154	0.2363	0.2395	0.2410	0.2435	0.2589	0.2525	0.2564
	JPY	39.78	37.01	36.2400	34.1000	35.1500	32.4200	32.6800	32.5400	31.89	33.0600	35.54	36.75
	NZD	0.5048	0.4981	0.4686	0.4554	0.4698	0.4467	0.4454	0.4357	0.4338	0.4413	0.4414	0.4524
4. Balance of Payments													
Current Account	PGK (millions of kina)	1219.0	1040.4	1039.5	1030.4	1,088.7	1,717.0	1,373.8	1,479.5	1,186.1	551.5 p	na	na
	Capital & Financial Account	PGK (millions of kina)	-783.6	-799.2	-1382.1	-1069.5	-1,507.7	-1,704.7	-1,387.7	-1,137.7	-1,204.0	-493.4 p	na
Overall Balance	PGK (millions of kina)	435.0	246.4	-315.4	-35.6	-418.4	14.6	-13.4 p	345.0	-18.1	58.6 p	na	na
Foreign Exchange Reserve (eop, US\$ mill) (e)		1,847.60	1,807.30	1,806.90	1,773.50	1,622.40	1,626.60	1,620.80	1,743.60	1,726.40	1,679.80	1,705.50	1,685.40
5. Liquidity (eop)	Liquid Assets Margin to Deposit Ratio (%)	44.32	44.4	45.14	45.02	45.99	45.74	44.0	45.6	45.7	44.7	46.4	na
	Banks' Demand Deposits (K'bn)	15.1	14.98	14.52	14.86	14.4	14.4	14.6	14.8	14.8	14.8	14.8	na
6. Money and Credit (YOY % Change)	Broad Money	1.4	4.8	5.6	6.0	3.9	7.9	11.0	6.5	12.0	8.1	13.4	na
	Monetary Base	-4.5	0.6	7.2	7.8	8.3	2.5	6.2	10.4	1.5	5.8	7.4	na
	Private Sector Credit	-2.2	0.8	-0.2	2.1	1.8	3.2	8.7	3.2	6.0	9.6	3.6	na
7. Interest Rates (% pa) (monthly weighted average)	Kina Facility Rate	6.25	6.25	6.25	6.25	6.25	6.25	6.25	6.25	6.25	6.25	6.25	6.25
	Central Bank Bill (28 day)	1.22	1.2	1.16	1.11	1.11	1.13	1.05	1.12	1.16	1.17	1.17	na
	Commercial bank Term Deposit (30 day)	0.59	0.69	0.6	0.45	1.53	0.96	1.08	0.61	0.29	0.71	0.16	na
	Government Treasury Bill (364 day)	7.65	7.72	7.71	7.7	7.67	7.67	7.69	7.69	7.71	7.7	7.73	na
	3-year inscribed stock Rate	-	-	-	9	9	9	-	9	9.05	9.1	9.1	na
	16-year inscribed stock Rate (> 10 years)	-	-	-	-	-	-	-	-	-	-	-	-
8. Commodity Prices (monthly average)(a)(b)(c)(d)	Oil (\$/bbl)	29.8	31.0	37.3	40.8	45.9	47.7	44.1	44.9	45.0	49.3	45.3	52.6
	LNG (\$/mmbtu) (c)	7.9	8.0	7.2	6.4	5.9	6.0	6.3	6.7	7.0	7.2	7.2	7.2
	Gold (\$/troy oz)	1,097.4	1,198.2	1,245.0	1,243.7	1,263.1	1,273.8	1,337.2	1,343.8	1,326.9	1,266.5	1,247.0	1,147.1
	Copper (\$/mt)	4,462.3	4,589.5	4,942.3	4,849.1	4,716.5	4,635.7	4,859.0	4,773.1	4,716.2	4,727.0	5,359.3	5,640.4
	Nickel (\$/tonne)	8,479.9	8,300.9	8,678.2	8,873.4	8,727.7	8,881.8	10,284.8	10,413.6	10,222.9	10,248.1	11,076.9	10,899.2
	Cobalt (\$/tonne)	23,208.5	22,312.6	23,094.4	22,961.8	23,443.1	23,788.6	25,139.0	26,297.8	26,709.0	28,220.0	29,181.6	31,869.4
	Coffee (\$/tonne) (d)	3,227.1	3,303.0	3,443.2	3,426.9	3,443.4	3,606.5	3,781.4	3,764.4	3,944.9	3,932.5	4,108.9	3,597.7
	Cocoa (\$/tonne) (d)	2,977.7	2,892.5	3,052.4	3,086.1	3,115.2	3,130.8	3,168.9	3,168.9	3,168.9	3,168.9	2,648.4	2,320.8
	Palm Oil (\$/tonne)	580.0	654.5	714.0	750.8	746.3	736.0	721.7	780.8	820.0	835.0	835.0	835.0

Notes:

- Balance of Payments data are provincial (p) for the current and the two recent months hence updated in the next reporting quarter of the year. Small (r) means data has been revised.
 - Liquefied Natural Gas (LNG), nickel, cobalt and palm oil are also included as some of PNG's major commodities.
 - The LNG price is an estimate for the current month and subject to change thus updated in the next reporting month as per the data source.
 - The unit price of measurement for cocoa and coffee have changed from US cents per pound to US\$ per tonne, which is widely reported internationally and to be consistent with many other commodities unit price of measurement.
- *end of period

Authorised for release by Mr Loi M. Bakani, CMG, Governor