BANK OF PAPUA NEW GUINEA

MONTHLY ECONOMIC REVIEW

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Economic Activity

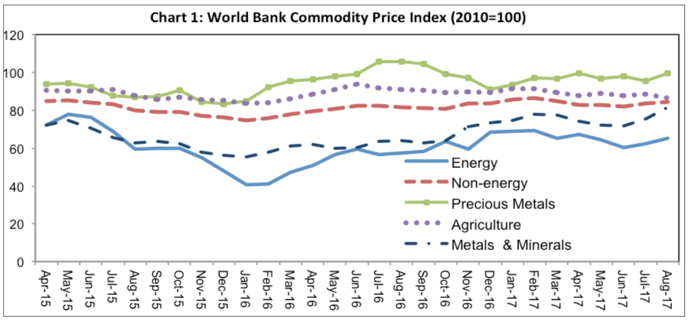
Global economic growth continued to maintain momentum, supported mainly by the advanced economies with accommodative monetary policies and less restrictive fiscal policies. The US economy remained resilient through robust consumer spending and strong business confidence and low unemployment and inflation. The Euro Area continued on a steady growth as improved manufacturing activity more than offset the softer service sector, whilst the appreciation of the euro further dampened inflationary pressures. Japan's economy improved due to the strong export sector supported by a weak yen and improved demand. Emerging market economies continued to grow, mainly driven by China and India. Growth in China improved due to high infrastructure spending and increased domestic demand, while exports declined following the appreciation of yuan. In India, the recovery in economic activity was mainly driven by the manufacturing sector following the fall in July this year due to the introduction of the new *Goods and Services Tax (GST).*

In the domestic economy, the Bank's Employment Index show that the level of employment in the formal private sector declined by 1.1 percent in the June quarter of 2017 due to low activity in the formal non-mineral sectors. However, improvement in prices and production of some of PNG's major export commodities continued to contribute to growth in the exporting industries, and inducing foreign exchange inflows into the domestic foreign exchange market.

Commodity Prices

Commodity price data available from the World Bank and published on the 06th of September 2017, show increases across most major price indices, compared to the broad based decline in the previous month. Energy price index improved by 0.03 percent following a 6.08 percent decline in the previous month. Non-energy price index increased by 1.93 percent from increases in metals and mineral, and agriculture prices of 5.13 percent and 0.81 percent, respectively. Precious metal index showed a decline of 2.29 percent. The international prices for most of PNG's major export commodities increased except for tea, coffee and natural gas.

Chart 1: World Bank Commodity Price Index (2010=100)



Source: World Bank

Balance of Payments

Preliminary balance of payments data for the six months to June 2017 show an overall surplus of K141 million, compared to a deficit of K73.3 million in the corresponding period of 2016. A surplus in the current account more than offset a deficit in the capital and financial account. The surplus in the current account was due to a higher trade surplus and net transfer receipts, which more than offset a lower net income payment. The deficit in the capital and financial account was due to outflows in portfolio and other investments, which more than offset net inflows from Government loan drawdown.

The level of gross foreign exchange reserves at the end of June 2017 was US$1,697.8 million (K5,398.4 million), sufficient for 6.2 months of total and 9.9 months of non-mineral import covers. As at 31st August 2017, the level of gross foreign exchange reserves was US$ 1,776.2 million (K5,576.2 million).

Exchange Rate

The average kina exchange rate was stable against the US dollar (USD) at US$0.3145, while it depreciated against the Australian dollar (AUD) by 114 basis points to AU$0.3970 over the month to 25th August 2017. The kina depreciated against the Australian dollar from cross currency losses, as the AUD appreciated against the USD, reflecting higher commodity exports by Australia to China. The kina has since depreciated by 10 basis points to USD0.3135 on 28th August 2017. The Trade Weighted Index (TWI) decreased by 0.14 percent to 31.81 over the same period *(Chart 2).*

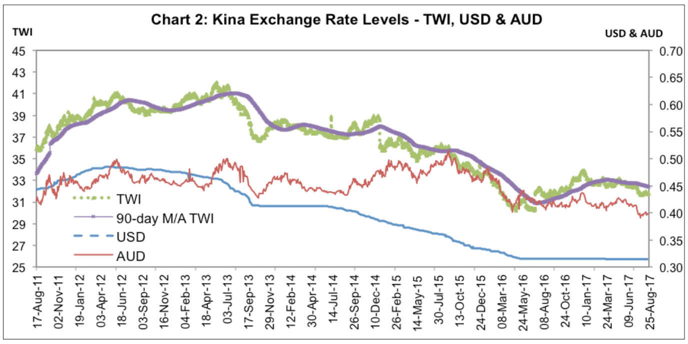


Chart 2: Kina Exchange Rate Levels - TWI, USD & AUD

Inflation

Annual headline inflation as measured by the Consumer Price Index (CPI) increased by 5.8 percent in the June quarter, compared to an increase of 6.0 percent in the March quarter of 2017. All expenditure groups recorded an increase except for "Recreation". There was no price change for the "Education" and "Communication" group. By urban centre, prices increased in all the surveyed centres. The annual underlying measures of inflation; the exclusion-based and trimmed mean increased by 2.0 percent and 2.2 percent, respectively. The quarterly exclusion-based inflation increased by 0.8 percent, while the quarterly trimmed-mean CPI increased by 0.5 percent in the June quarter of 2017. These outcomes indicate that headline inflation is trending downward, while the underlying inflation rates remained low and stable in the first half of 2017.

Annual headline Retail Price Index (RPI) over the twelve months to July 2017 increased by 5.6 percent, compared to an annual increase of 7.5 percent in June. This reflected increases in the "Food", "Drinks, Tobacco and Betelnut" and "Rents, council charges fuel/power" expenditure groups, and the "motor vehicle operation" sub-group. Annual RPI excluding seasonal items increased by 3.0 percent, compared to an increase of 3.4 percent in June, while annual RPI excluding seasonal items and fuel increased by 3.0 percent in July 2017, compared to an increase of 3.3 percent in June (Chart 3). Quarterly headline and monthly headline RPI increased by 2.3 percent and 0.3 percent, respectively, in July.

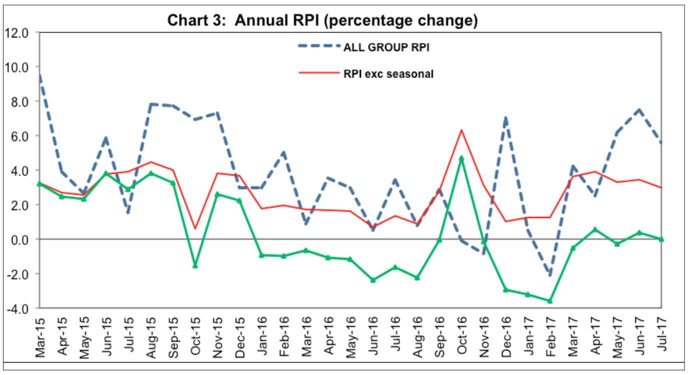


Chart 3: Annual RPI (percentage change)

Domestic Interest Rates & Monetary Aggregates

Over the month to 25th August 2017, the Central Bank Bill rates for 28-day and 63-day terms increased to 1.37 percent and 2.35 percent, respectively, from 1.36 percent and 2.33 percent. There were no allocations at the auction for the other terms. At the Treasury bill auction, the 63-day and 91-day terms were offered once in August at 2.40 percent and 2.49 percent, respectively. The 273-day and 364-day rates increased to 6.71 percent and 7.97 percent, respectively, from 6.68 percent and 7.96 percent. The 180-day rate remained at 4.74 percent. During the same period, all the weighted average interest rates on wholesale deposits above K500,000 decreased except for the 90-day. The weighted average rate for the 30-day, 60-day and 180-day terms decreased to 0.22 percent, 0.18 percent and 0.64 percent, respectively, from 2.55 percent, 0.28 percent and 1.02 percent. The 90-days term increased to 1.04 percent from 0.77 percent *(Chart 4)*.

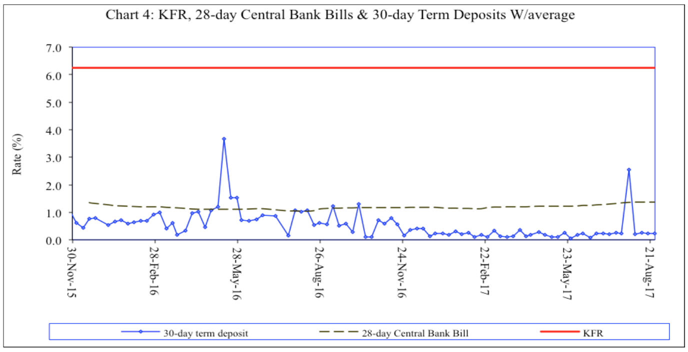


Chart 4: KFR, 28-day Central Bank Bills & 30-day Term Deposits W/average

Broad money supply increased by 5.1 percent over the year to July 2017, compared to an increase of 10.7 percent in the corresponding period of 2016. This was mainly due to increases in net claims to Government and net credit to other financial corporations, public non-financial corporations and private sector. Monetary base increased by 9.4 percent over the year to July 2017, compared to an increase of 6.2 percent in the corresponding period of 2016. This was mainly due to an increase in currency in circulation, partly due to the National Elections, as well as high commercial banks' deposits at the Central Bank.

Commercial bank lending to public non-financial corporations, other financial corporations and other resident sectors decreased by K394.2 million to K12,452.3 million over the eight months to the 25th August 2017. Over the same period , the weekly average lending by banks increased by 6.8 percent to K12,532.1 million. This reflected advances to the retail, agriculture, finance, manufacturing, petroleum, mining, construction, fisheries, transportation and services sectors, including lending to State Owned Enterprises (SOEs). The level of deposit at commercial banks decreased by K182.5 million to K21,319.7 million over the year to the 25th August 2017, reflecting withdrawals mainly by the manufacturing, petroleum, finance, retail, mining, agriculture and services sectors. Over the year to 25th August 2017, the weekly average deposits increased by 7.8 percent to K21,604.4 million.

Monetary Policy

The Bank maintained its policy signalling rate, the Kina Facility Rate (KFR), at 6.25 percent for the month of August 2017.

Papua New Guinea Key Economic Indicators													
		Sep-16	Oct-16	Nov-16	Dec-16	Jan-17	Feb-17	Mar-17	Apr-17	May-17	Jun-17	Jul-17	Aug-17
1. Consumer Price Index (CPI).	Headline	6.8	-	-	6.6	-	-	6.0	-	-	5.8	-	-
	Food	5.3	-	-	2.8	-	-	3.5	-	-	2.7	-	-
	Underlying	2.0	-	-	2.5	-	-	2.1	-	-	2.5	-	-
2. Retail Price Index (RPI) (YOY % Change)	Headline	2.9	-0.1	-0.8	7.0	0.5	-2.1	4.3	2.5	6.2	7.5	5.6	na
	Ex-seasonal	2.8	6.3	3.1	1.0	1.3	1.3	3.6	3.9	3.3	3.4	3.0	na
3. Exchange Rates (mid-rate, eop*)	USD	0.3155	0.3155	0.3150	0.3150	0.3150	0.3150	0.3145	0.3145	0.3145	0.3145	0.3145	0.3135
	AUD	0.4137	0.4145	0.4215	0.4354	0.4166	0.4100	0.4113	0.4208	0.4220	0.4089	0.3940	0.3971
	GBP	0.2435	0.2589	0.2525	0.2564	0.2517	0.2532	0.2521	0.2437	0.2454	0.2417	0.2395	0.2427
	JPY	31.89	33.0600	35.54	36.75	35.73	35.45	35.17	34.97	34.91	35.22	34.76	34.67
	NZD	0.4338	0.4413	0.4414	0.4524	0.4318	0.4380	0.4500	0.4574	0.4440	0.4293	0.4190	0.4382
4. Balance of Payments													
Current Account	PGK (millions of kina)	1,541.4	1,584.4	1,434.2	1,698.6	1,080.4	1,697.4	1,636.9	1,625.7	1,732.2	1,772.3	na	na
Capital & Financial Account	PGK (millions of kina)	-1559.5	-1527.5	-1568.2	-1832.5	-7,118.7	-1,773.5	-1,574.4	-1,823.1	-1,792.0	-1,743.3	na	na
Overall Balance	PGK (millions of kina)	-17.7	58.6	-133.9	-135.0	368.3 p	-69.1 p	69.4 p	-197.3 p	-57.8 p	27.3	na	na
Foreign Exchange Reserve (eop, US$ mill) (e)		1,726.40	1,679.80	1,705.50	1,685.40	1,792.87	1,767.90	1,737.90	1,715.30	1,696.01	1,707.73	1,715.70	1,776.20
5. Liquidity (eop)	Liquid Assets Margin to Deposit Ratio (%)	45.7	44.7	46.4	48.9	49.0	49.3	49.0	49.9	50.7	49.8	49.1	51.6
	Banks' Demand Deposits (K'bn)	14.8	14.8	14.8	14.8	14.8	14.8	14.8	14.8	14.8	14.8	14.8	14.8
6. Money and Credit	Broad Money	12.0	8.1	13.4	10.4	9.9	10.8	13.2	10.0	12.0	6.6	5.1	na
(YOY % Change)	Monetary Base	1.5	5.8	7.4	24.4	24.3	11.2	19.6	4.6	8.3	14.3	9.4	na
	Private Sector Credit	6.0	9.6	3.6	7.2	5.7	2.0	0.6	0.4	1.5	1.1	1.1	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)	1.16	1.17	1.17	1.18	1.14	1.17	1.2	1.22	1.22	1.28	1.36	1.13
	Commercial bank Term Deposit (30 day)	0.29	0.71	0.16	0.22	0.21	0.32	0.35	0.05	0.05	0.22	2.55	0.22
	Government Treasury Bill (364 day)	7.71	7.7	7.73	7.77	7.8	7.79	7.82	7.82	7.88	7.94	7.86	7.97
	3-year Inscribed stock Rate	9.05	9.1	9.1	-	-	9.08	9.09	9.41	9.41	9.41	9.48	9.54
	16-year Inscribed stock Rate (> 10 years)	-	-	-	-	-	12.67	12.7	12.6	12.65	12.75	12.81	12.8
8. Commodity Prices (monthly average)(a)(b)(c)(d)	Oil ($/bbl)	45.0	49.3	45.3	52.6	53.6	54.4	50.9	52.2	49.9	46.2	47.7	49.9
	LNG ($/mmbtu) (c)	7.0	7.2	7.1	7.1	7.5	7.9	7.7	8.2	8.5	8.3	8.3	8.3
	Gold ($/troy oz)	1,326.9	1,266.5	1,247.0	1,147.1	1,190.3	1,230.1	1,231.4	1,266.4	1,242.8	1,261.6	1,234.7	1,284.2
	Copper ($/mt)	4,716.2	4,727.0	5,359.3	5,640.4	5,712.9	5,937.0	5,833.9	5,693.2	5,590.2	5,683.5	5,959.7	6,495.0
	Nickel ($/tonne)	10,222.9	10,248.1	11,076.9	10,899.2	10,018.2	10,545.3	10,281.7	9,664.6	9,175.8	8,902.5	9,441.0	10,886.8
	Cobalt ($/tonne)	26,709.0	28,220.0	29,181.6	31,869.4	34,412.5	41,786.3	52,631.0	55,309.5	54,512.6	57,295.1	58,743.8	58,126.3
	Coffee ($/tonne) (d)	3,944.9	3,932.5	4,108.9	3,597.7	3,655.6	3,663.8	3,502.9	3,477.8	3,333.1	3,177.7	3,329.0	3,403.9
	Cocoa ($/tonne) (d)	3,168.9	3,168.9	2,648.4	2,320.8	2,211.9	2,035.7	2,057.1	1,988.2	1,983.8	1,999.0	1,983.1	1,993.5
	Palm Oil ($/tonne)	820.0	835.0	835.0	835.0	835.0	835.0	807.0	725.0	740.0	740.6	725.0	706.8

Notes:

a) Balance of Payments data are provisional (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.
b) Liquefied Natural Gas (LNG), nickel, cobalt and palm oil are also included as some of PNG's major commodities.
c) The LNG price is an estimate for the current month and subject to change in the next reporting month when update is made from the data source.
d) The unit price of measurement for cocoa and coffee have been changed from US cents per pound to US$ per tonne, which is widely used and consistent with many other commodities unit price of measurement.
*end of period

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