



BANK OF PAPUA NEW GUINEA

MONTHLY ECONOMIC REVIEW

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Economic Activity

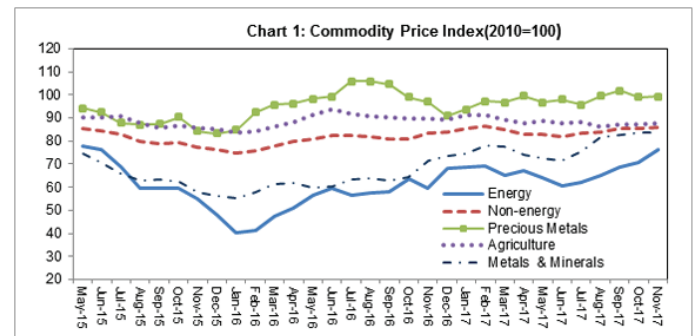
Global economic growth continued to strengthen into the third quarter of 2017 as shown by progressive outcomes of major economies, with indicators suggesting its continuity into November. The US economy remained resilient after an upward revision of its third quarter GDP data, reflecting a rise in employment; although indicators for November show a modest slowdown in its manufacturing and service sectors. In the UK, euro area and Japan, indicators for November show a pick-up in economic activity, especially in the manufacturing and construction sectors, which more than offset the slowdown in the service sectors, particularly for the UK and Japan. These developments have raised expectations for a more robust growth in advanced economies in the last quarter of 2017. Among the large emerging market economies, favourable manufacturing and service sector activity indicate continued strong growth for China and India, and a pick-up for Russia despite its slowdown in the third quarter. Meanwhile, Brazil's continued struggle to recover is weakened by a contraction in its service sector, despite expansion in its manufacturing sector.

In the domestic economy, economic indicators point towards weaker growth as reflected by lower inflation and employment outcomes for September, the persistent foreign exchange mismatches adversely affecting imports and exerting downward pressure on the exchange rate and lower government revenue. Weaker economic activity across the different economic sectors has also been impacted by negative private sector credit growth for three consecutive months since October. For 2018, expansionary fiscal policy, as contained in the recently released 2018 National Budget, is expected to provide the stimulus needed to boost growth.

Commodity Prices

Commodity price data from the World Bank published on the 04th of December 2017, show increases for the main commodity price indices in November 2017. The energy price index increased by 7.74 percent driven by price increases in crude oil of 9.13 percent to US\$59.93 per barrel at end of November, compared to US\$54.92 per barrel

in the previous month and 1.81 percent increase in the Liquefied Natural Gas (LNG) price index. The non-energy price index increased by 0.18 percent reflecting higher agriculture and metals and mineral price indices (Chart 1). The precious metals price index increased by 0.21 percent mainly attributed to price increases for gold and silver. The international prices for most of Papua New Guinea's major export commodities increased, except for tea and palm oil.



Source: World Bank

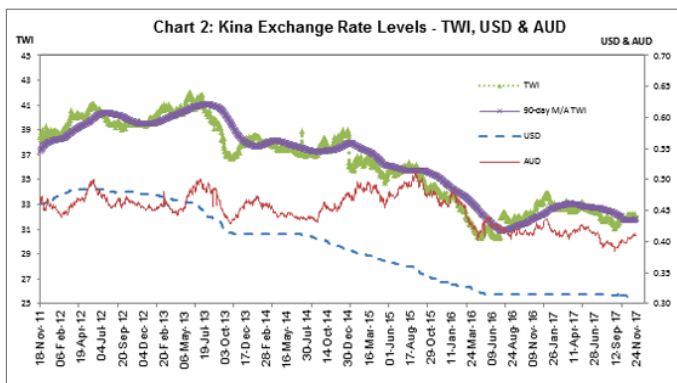
Balance of Payments

Preliminary balance of payments data for the nine months to September 2017 show an overall surplus of K327 million, compared to a surplus of K241 million in the corresponding period of 2016. This outcome was due to a surplus in the current account, which more than offset a deficit in the capital and financial account. The surplus in the current account was due to a higher trade account surplus and net transfer receipts, which more than offset higher service and income payments. The deficit in the capital and financial account was due to net outflows in portfolio and other investments, reflecting purchases of short-term money market instruments, and a build-up in offshore foreign currency account balances of mineral companies under the Project Development Agreements, respectively.

The level of gross foreign exchange reserves at the end of September 2017 was US\$1,769.5 (K5,573.2) million, sufficient for 5.6 months of total and 9.0 months of non-mineral import covers. As at 30th November 2017, the level of gross foreign exchange reserves was US\$1,691.9 (K5,345.8) million.

Exchange Rate

The average kina exchange rate depreciated against the US dollar (USD) by 9 basis points to US\$0.3116, mainly due to high import demand, while it appreciated against the Australian dollar (AUD) by 87 basis points to AU\$0.4073 over the month to 24th November 2017. The appreciation of the kina against the Australian dollar resulted from the depreciation of AUD against the USD, reflecting rising US Treasury yields, concerns over Chinese demand for raw materials, reduction in Chinese retail sales and industrial production, and disappointing Australian labour data. The Trade Weighted Index (TWI) increased by 0.28 percent to 32.1 over the same period. Despite the Central Bank's intervention of USD100.0 million in parcels over the period, the average unfilled sell orders in the foreign exchange market continue to remain above K700.0 million. This reflects the underlying high demand for USD and less foreign exchange inflows, both of which have exerted further downward pressure on the exchange rate (Chart 2).

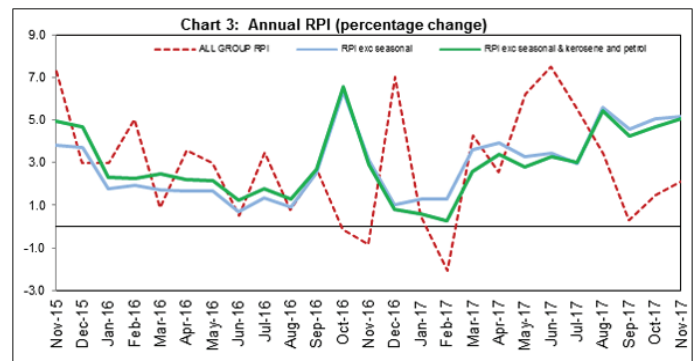


Inflation

Annual headline Consumer Price Index (CPI) increased by 5.1 percent in the September quarter of 2017, compared to an increase of 5.8 percent in the June quarter of 2017. Generally, all expenditure groups recorded increases. The 'Alcoholic Beverages, Tobacco and Betelnut' expenditure group recorded the largest increase of 13.1 percent, followed by 'Housing' with 6.6 percent, 'Household Equipment' with 5.5 percent, 'Transport' with 4.1 percent, 'Food and Non-alcoholic Beverages' with 3.8 percent, 'Health' with 3.3 percent, 'Miscellaneous' with 2.4 percent, 'Clothing and Footwear' with 2.2 percent, 'Recreation' with 1.7 percent and 'Restaurants and Hotels' with 1.6 percent. Annual trimmed mean and exclusion-based CPI measures increased by 2.6 percent and 2.4 percent, respectively, over the twelve months to September 2017 while the quarterly headline CPI increased by 1.0 percent in September 2017, compared to an increase of 1.2 percent in the June quarter of 2017.

Annual headline Retail Price Index (RPI) to October 2017 increased by 1.5 percent, compared to an increase of 0.3 percent over the twelve months to September 2017 (Chart 3).

This was mainly due to price increases of 2.3 percent and 2.0 percent in the 'Rents, council charges, fuel/power' and 'food' expenditure groups, respectively. Quarterly headline RPI decreased by 2.2 percent while the monthly headline RPI declined by 1.0 percent in October 2017.



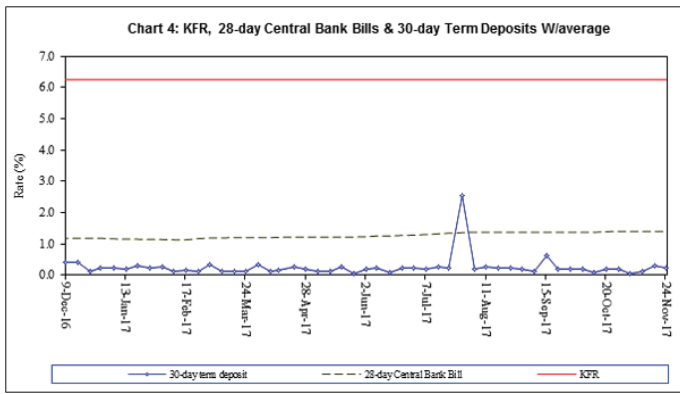
Fiscal Operations

The weekly cash-flow closing position as at week-ending 24th November 2017 was a debit balance of K99.2 million. A debit balance of K99.2 million is projected for week-ending 1st December 2017. The cash-flow continues to remain tight as the year ends and spending on 'other expenditure' in the cash flow ramps up.

The 2018 National Budget presented on the 28th of November 2017 projected a deficit of K1,987.2 with revenue totalling K12, 730.7 million, an increase of K1,751.6 million from the 2017 revised revenue level and expenditure of K14,717.9 million, an increase of K1,862.3 million from the 2017 revised expenditure level. This reflects a projected deficit to GDP ratio of 2.4 percent.

Domestic Interest Rates & Monetary Aggregates

Over the month to week-ending 24th November 2017, the Central Bank Bill (CBB) rate for the 28-day term increased to 1.40 percent from 1.39 percent, while there were no allocations at the auction for the other terms. At the Treasury bill (T-bill) auction, the 91-day rate was auctioned once during the last week of October at 2.45 percent, while the 364-day rate increased to 8.03 percent from 8.00 percent. The 182-day and 273-day rates remain unchanged at 4.73 percent and 6.76 percent, respectively. During the same period, the weighted average interest rates on wholesale deposits above K500,000 show mixed movements. The weighted average rate for the 30-day and 90-day terms increased to 0.22 percent and 2.46 percent, respectively, from 0.20 percent and 0.65 percent. The 60-day and 180-day terms decreased to 0.10 percent and 0.73 percent, respectively, from 0.19 percent and 1.39 percent (Chart 4).



Broad money supply increased by 2.4 percent over the year to October 2017, compared to an increase of 12.8 percent in the corresponding period of 2016. This was mainly due to increases in net claims on the Government and supported by credit to other financial corporations. Monetary base increased by 1.4 percent over the year to October 2017, compared to an increase of 6.0 percent in the corresponding period of 2016. This was mainly due to high commercial bank deposits at the Central Bank.

Commercial bank lending to public non-financial corporations, other financial corporations and other resident sectors decreased by K303.2 million to K12,543.3 million over the year to 24th November 2017. This mainly reflected repayments by the retail, agriculture, construction and government sectors. Over the year to 24th November 2017, the weekly average lending by banks increased by 3.7 percent to K12,536.3 million. The commercial bank deposits decreased by K405.3 million to K21,097.0 million over the same period, reflecting withdrawals mainly by the manufacturing, petroleum, communication, Government, construction, fisheries, retail, mining, agriculture and services sectors while the weekly average deposits increased by 5.9 percent to K21,522.2 million.

Monetary Policy

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

| Papua New Guinea Key Economic Indicators | | Jan-17 | Feb-17 | Mar-17 | Apr-17 | May-17 | Jun-17 | Jul-17 | Aug-17 | Sep-17 | Oct-17 | Nov-17 |
|---|---|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|
| 1. Consumer Price Index (CPI) | Headline | - | - | 6.0 | - | - | 5.8 | - | - | 5.1 | - | - |
| | Food | - | - | 3.5 | - | - | 2.7 | - | - | 3.8 | - | - |
| | Underlying | - | - | 2.1 | - | - | 2.5 | - | - | 3.4 | - | - |
| 2. Retail Price Index (RPI) (YOY % Change) | Headline | 0.5 | -2.1 | 4.3 | 2.5 | 6.2 | 7.5 | 5.6 | 8.3 | 4.3 | 1.5 | na |
| | Ex-seasonal | 1.3 | 1.3 | 3.6 | 3.9 | 3.3 | 3.4 | 3.0 | 5.6 | 4.6 | 5.1 | na |
| 3. Exchange Rates (mid-rate, eop*) | USD | 0.3150 | 0.3150 | 0.3145 | 0.3145 | 0.3145 | 0.3145 | 0.3145 | 0.3135 | 0.3125 | 0.3115 | 0.3115 |
| | AUD | 0.4166 | 0.4100 | 0.4113 | 0.4208 | 0.4220 | 0.4089 | 0.3940 | 0.3971 | 0.3987 | 0.4054 | 0.4105 |
| | GBP | 0.2517 | 0.2532 | 0.2521 | 0.2437 | 0.2454 | 0.2417 | 0.2395 | 0.2427 | 0.2331 | 0.2358 | 0.2313 |
| | JPY | 35.73 | 35.45 | 35.17 | 34.97 | 34.91 | 35.22 | 34.76 | 34.67 | 35.22 | 35.24 | 34.93 |
| | NZD | 0.4318 | 0.4380 | 0.4500 | 0.4574 | 0.4440 | 0.4293 | 0.4190 | 0.4382 | 0.4336 | 0.4535 | 0.4550 |
| 4. Balance of Payments | Current Account | | | | | | | | | | | |
| | Capital & Financial Account | | | | | | | | | | | |
| | Overall Balance | | | | | | | | | | | |
| | Foreign Exchange Reserve (eop, US\$ mill) (e) | 1,792.9 | 1,767.9 | 1,737.9 | 1,715.3 | 1,696.0 | 1,707.7 | 1,715.7 | 1,776.20 | 1,769.50 | 1,711.80 | 1,691.90 |
| 5. Liquidity (eop) | Liquid Assets Margin to Deposit Ratio (%) | 49.0 | 49.3 | 49.0 | 49.9 | 50.7 | 49.8 | 49.1 | 51.6 | 50.8 | 49.47 | 50.12 |
| | 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 |
| 6. Money and Credit (YOY % Change) | Broad Money | 9.9 | 10.8 | 13.2 | 10.0 | 12.0 | 6.6 | 5.1 | 5.5 | 5.8 | 2.4 | 2.2 |
| | Monetary Base | 24.3 | 11.2 | 19.6 | 4.6 | 8.3 | 14.3 | 9.4 | 10.3 | 13.3 | 1.4 | 7.9 |
| | Private Sector Credit | 5.7 | 2.0 | 0.6 | 0.4 | 1.5 | 1.1 | 1.1 | -0.7 | -0.5 | -5.1 | -4.5 |
| 7. Interest Rates (% pa) (monthly) | 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 |
| | Central Bank Bill (28 day) | 1.14 | 1.17 | 1.2 | 1.22 | 1.22 | 1.28 | 1.36 | 1.13 | 1.26 | 1.40 | 1.41 |
| | Commercial bank Term Deposit (30 day) | 0.21 | 0.32 | 0.35 | 0.05 | 0.05 | 0.22 | 2.55 | 0.22 | 0.2 | 0.19 | 0.2 |
| | Government Treasury Bill (364 day) | 7.8 | 7.79 | 7.82 | 7.82 | 7.88 | 7.94 | 7.86 | 7.97 | 8 | 8.00 | 8.03 |
| | 3-year Inscribed stock Rate | - | 9.08 | 9.09 | 9.41 | 9.41 | 9.41 | 9.48 | 9.54 | 9.5 | 9.48 | 9.48 |
| | 16-year Inscribed stock Rate (> 10 years) | - | 12.67 | 12.7 | 12.6 | 12.65 | 12.75 | 12.81 | 12.8 | 12.8 | 12.76 | 12.77 |
| 8. Commodity Prices (monthly average)(a)(b)(c)(d) | Oil (\$/bbl) | 53.6 | 54.4 | 50.9 | 52.2 | 49.9 | 46.2 | 47.7 | 49.9 | 53.0 | 54.9 | 59.9 |
| | LNG (\$/mmbtu) (c) | 7.5 | 7.9 | 7.7 | 8.2 | 8.5 | 8.3 | 8.3 | 8.3 | 8.1 | 7.8 | 7.8 |
| | Gold (\$/troy oz) | 1,190.3 | 1,230.1 | 1,231.4 | 1,266.4 | 1,242.8 | 1,261.6 | 1,234.7 | 1,284.2 | 1,314.7 | 1,280.4 | 1,283.7 |
| | Copper (\$/mt) | 5,712.9 | 5,937.0 | 5,833.9 | 5,693.2 | 5,590.2 | 5,683.5 | 5,959.7 | 6,495.0 | 6,573.0 | 6,795.3 | 6,813.4 |
| | Nickel (\$/tonne) | 10,018.2 | 10,545.3 | 10,281.7 | 9,664.6 | 9,175.8 | 8,902.5 | 9,441.0 | 10,886.8 | 11,191.8 | 11,285.6 | 11,864.8 |
| | Cobalt (\$/tonne) | 34,412.5 | 41,786.3 | 52,631.0 | 55,309.5 | 54,512.6 | 57,295.1 | 58,743.8 | 58,126.3 | 60,015.0 | 59,612.5 | 62,375.0 |
| | Coffee (\$/tonne) (d) | 3,655.6 | 3,663.8 | 3,502.9 | 3,477.8 | 3,333.1 | 3,177.7 | 3,329.0 | 3,403.9 | 3,301.4 | 3,152.6 | 3,180.1 |
| | Cocoa (\$/tonne) (d) | 2,211.9 | 2,035.7 | 2,057.1 | 1,988.2 | 1,983.8 | 1,999.0 | 1,983.1 | 1,993.5 | 1,998.6 | 2,096.2 | 2,132.0 |
| | Palm Oil (\$/tonne) | 835.0 | 835.0 | 807.0 | 725.0 | 740.0 | 740.6 | 725.0 | 706.8 | 753.4 | 743.6 | 750.9 |

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 thus updated in the next reporting month as per the data source.
- d) 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.
- e) The reserve figure for September 2016 was corrected.
- * end of period

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