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PAPUA NEW GUINEA

December 2023

FIRST REVIEWS UNDER EXTENDED ARRANGEMENT UNDER THE EXTENDED FUND FACILITY AND AN ARRANGEMENT UNDER THE EXTENDED CREDIT FACILITY, AND REQUEST FOR MODIFICATION OF QUANTITATIVE PERFORMANCE CRITERIA—PRESS RELEASE; STAFF REPORT; STAFF STATEMENT, AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR PAPUA NEW GUINEA

In the context of the First Reviews under extended arrangement under the Extended fund Facility and an arrangement under the Extended credit Facility, and Request for modification of quantitative performance criteria, the following documents have been released and are included in this package:

- A **Press Release** including a statement by the Chair of the Executive Board.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on November 22, 2023, following discussions that ended on September 21, 2023, with the officials of Papua New Guinea on economic developments and policies underpinning the IMF arrangements under the Extended Fund Facility and the Extended Credit Facility. Based on information available at the time of these discussions, the staff report was completed on November 6, 2023.
- A **Debt Sustainability Analysis** prepared by the staffs of the IMF and the World Bank.
- A **Staff Statement** updating information on recent developments.
- A **Statement by the Executive Director** for Papua New Guinea.

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PRESS RELEASE

PR23/409

IMF Executive Board Completes the First Reviews Under the Extended Credit Facility and Extended Fund Facility Arrangements for Papua New Guinea

FOR IMMEDIATE RELEASE

- The IMF Executive Board completed the First Reviews under the 38-month ECF/EFF arrangements for Papua New Guinea, providing the country with immediate access to about US$88 million.
- Program performance has been strong, with all end-June 2023 performance criteria met and all structural benchmarks implemented.
- The program will continue to support Papua New Guinea's reform agenda, help protect the vulnerable and foster inclusive growth, with a focus maintained on strengthening debt sustainability, alleviating FX shortages, and enhancing governance and operationalizing the anti-corruption framework.

Washington, DC: On November 22, 2023, the Executive Board of the International Monetary Fund (IMF) completed the First Reviews of Papua New Guinea's Fund-supported program. The 38-month ECF/EFF arrangements, approved on March 22, 2023, support the authorities' reforms to address long-standing structural impediments to inclusive growth. This review completion allows for the immediate disbursement of SDR 65.81 million (about US$88 million) toward budget support, bringing total disbursements under the program so far to SDR 131.62 million (about US$176 million).

Papua New Guinea's economic outlook remains favorable. Growth is expected to soften to 3.0 percent this year, due to the normalization of LNG production, but is projected to rebound to 5.0 percent in 2024, spurred by the expected reopening of Porgera gold mine and by sustained growth in the agriculture and service sectors. Inflation—after significantly declining in the past year due to fiscal measures and lower imported inflation, is projected to rise, reaching 3.5 percent by end-2023 and 5.0 percent by end-2024.

The medium-term outlook is positive but subject to both large upside and downside risks. PNG is vulnerable to both domestic and external shocks, which is exacerbated by the buildup in public debt, ongoing FX shortages and capacity constraints that impact the government's ability to formulate and implement economic stabilization and development policies. On the upside however, the start of the construction of major resource projects, which are not yet in the baseline scenario, could yield additional economic growth in the short to medium run, as well as gains in exports and fiscal revenues once they enter into operation.

Program performance has been strong, with the authorities displaying a continued commitment to reforms. All end-June 2023 quantitative performance criteria were met, and all structural benchmarks were implemented.

At the conclusion of the Executive Board's discussion, Mr. Bo Li, Deputy Managing Director, and Acting Chair, made the following statement:

The strong program performance recorded in the first six months of the ECF/EFF arrangements attests to the authorities' sustained commitment to reforms, successfully overcoming technical and institutional capacity constraints. The government's fiscal consolidation strategy, which aims at a balanced budget by 2027, is on track, and the deficit is expected to return to pre-pandemic levels this year. To address foreign exchange shortages, the central bank has sharply reduced excess liquidity by modernizing its monetary policy operations, and the exchange rate has undergone a gradual depreciation, bringing it closer to a market-clearing rate. The governance and anti-corruption frameworks have been enhanced, including the appointment of Commissioner and Deputy Commissioners of the Independent Commission Against Corruption.

The authorities are well placed to build on these achievements and continue their reform efforts to achieve resilient, inclusive and sustainable growth. Debt vulnerabilities will be addressed by sustaining fiscal consolidation while creating space to tackle development needs, adapt to climate change and preserve social spending. Consolidation will need to rely both on domestic revenue mobilization, guided by the new Medium-term Revenue Strategy and supported by critical amendments to the legal framework, and on expenditure rationalization and efficiency gains, enabled by improvements in public financial management and payroll management. The central bank should continue implementing its sequenced roadmap of reforms, devised with IMF support, to facilitate a gradual and orderly return to greater exchange rate flexibility, alleviate foreign exchange shortages and further strengthen liquidity management. The authorities are encouraged to provide sufficient resources for the Independent Commission Against Corruption to become fully operational and should keep on fostering greater transparency and accountability.

The ECF/EFF arrangements will continue to support this homegrown reform agenda, helping to address balance of payment needs and rebuild buffers while avoiding disruptive adjustment, and catalyzing support from other international partners. Timely technical assistance and advice from the IMF will accompany reform implementation.

Table 1. Papua New Guinea: Selected Economic and Financial Indicators, 2019-2028

Nominal GDP (2021):	US$26.3 billion 1/
Population (2021):	11.8 million
GDP per capita (2021):	US$2,233
Quota:	SDR 263.2 million

	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028
			Est.	Est.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
	(Percentage change)									
Real sector										
Real GDP growth	4.5	-3.2	0.1	4.3	3.0	5.0	3.1	3.1	3.0	3.1
Resource 2/	11.3	-9.2	-11.0	3.7	-1.4	6.3	0.1	0.1	0.1	0.2
Non-resource	1.6	-0.4	4.8	4.6	4.6	4.6	4.1	4.1	4.0	4.0
Mining and quarrying (percent of GDP)	10.8	10.2	8.5	8.0	8.4	9.6	9.7	9.6	9.4	8.8
Oil and gas extraction (percent of GDP)	17.6	14.1	15.9	22.6	16.8	16.0	14.4	12.2	10.4	9.7
CPI (annual average)	3.9	4.9	4.5	5.3	2.2	4.0	4.8	4.8	4.6	4.5
CPI (end-period)	2.7	5.1	5.7	3.4	3.5	5.0	4.8	4.8	4.6	4.5
	(In percent of GDP)									
Central government operations										
Revenue and grants	16.3	14.7	15.0	16.7	18.2	18.0	18.5	18.8	19.4	19.6
Of which: Resource revenue	1.5	0.9	1.1	3.9	3.6	3.1	3.3	3.1	3.2	3.2
Expenditure and net lending	20.7	23.5	21.8	22.0	22.6	22.0	21.0	20.2	19.3	19.3
Net lending(+)/borrowing(-)	-4.4	-8.9	-6.8	-5.3	-4.4	-3.9	-2.5	-1.4	0.1	0.3
Non-resource net lending(+)/borrowing(-)	-5.9	-9.8	-7.9	-9.2	-8.0	-7.0	-5.8	-4.6	-3.1	-2.9
	(Percentage change)									
Money and credit										
Domestic credit	5.2	2.3	15.9	-0.6	10.4	12.3	7.2	4.5	4.8	16.9
Credit to the private sector	4.1	4.2	2.5	6.9	8.9	8.8	8.9	8.8	8.6	8.6
Broad money	4.4	7.0	13.4	14.7	0.6	5.5	3.2	7.8	7.7	8.8
	(In billions of U.S. dollars)									
Balance of payments										
Exports, f.o.b.	10.9	9.1	11.3	14.4	13.2	13.8	14.3	14.7	15.1	15.6
Imports, c.i.f.	-4.1	-3.7	-5.1	-4.2	-4.1	-4.2	-4.3	-4.5	-4.7	-4.9
Current account (including grants)	3.7	3.4	3.5	7.2	5.6	5.3	5.5	4.9	4.1	3.6
(In percent of GDP)	14.8	14.1	13.2	22.8	18.6	16.3	16.7	14.8	11.9	10.2
Gross official international reserves	2.3	2.7	3.2	4.0	3.4	3.1	3.1	3.5	3.6	2.8
(In months of goods and services imports)	5.2	4.5	6.3	8.0	6.7	6.0	5.8	6.3	6.3	4.7
	(In percent of GDP)									
Government debt										
Government gross debt	40.6	48.7	52.2	48.4	52.4	52.2	52.7	52.1	49.2	46.5
External debt-to-GDP ratio (in percent) 3/	17.1	21.8	24.8	23.6	26.4	29.7	32.4	33.6	32.5	29.2
External debt-service ratio (percent of exports)	1.2	5.4	4.1	2.1	2.7	3.4	4.5	5.4	5.6	8.9
Exchange rates										
US$/kina (end-period)	0.2935	0.2850	0.2850	0.2840	...	...	...	...	...	...
NEER (2005=100, fourth quarter)	97.0	90.7	91.2	100.3	97.0	...	...	...	...	...
REER (2005=100, fourth quarter)	125.5	122.6	125.1	135.5	125.5	...	...	...	...	...
Terms of trade (2010=100, end-period)	59.4	57.4	49.4	68.2	62.3	62.1	62.7	63.2	63.4	63.6
Nominal GDP (in billions of kina)	83.8	82.5	92.3	111.0	112.2	122.9	130.4	137.0	144.3	153.5
Non-resource nominal GDP (in billions of kina)	60.1	62.5	69.8	77.1	84.0	91.4	99.0	107.1	115.8	125.2

Sources: Department of Treasury; Bank of Papua New Guinea; and IMF staff estimates and projections.

1/ Based on period average exchange rate.

2/ Resource sector includes production of mineral, petroleum, and gas and directly-related activities such as mining and quarrying, but excludes indirectly-related activities such as transportation and construction.

3/ Public external debt includes external debt of the central government, the central bank, and statutory authorities.

PAPUA NEW GUINEA

November 6, 2023

FIRST REVIEWS UNDER EXTENDED ARRANGEMENT UNDER THE EXTENDED FUND FACILITY AND AN ARRANGEMENT UNDER THE EXTENDED CREDIT FACILITY, AND REQUEST FOR MODIFICATION OF QUANTITATIVE PERFORMANCE CRITERIA

EXECUTIVE SUMMARY

Background. On March 22, 2023, the IMF Executive Board approved 38-month Extended Credit Facility (ECF) and Extended Fund Facility (EFF) arrangements with Papua New Guinea to help address a protracted balance of payments need manifested in foreign exchange shortages and to support the authorities' reforms to address long-standing structural impediments to inclusive growth. While ambitious, the program is focused on macro-critical conditionality, supported by capacity development (CD), and informed by a Country Engagement Strategy, in line with the IMF's Strategy for Fragile and Conflict-Affected States (FCS).

Program performance. Program performance has been strong, with the authorities displaying a continued commitment to reforms. All end-June 2023 quantitative performance criteria (QPCs) were met. Fiscal consolidation is on track. Foreign exchange reserves were well above the program floor, despite a large FX intervention in May 2023. New external debt remains well below the ceiling. In addition, the structural reform agenda has progressed well. All structural benchmarks (SBs) were met in timely fashion, except for one, which was implemented with a slight delay. The Medium-term Revenue Strategy (MTRS) and the monetary and FX reform roadmap (the 'Roadmap'), two key SBs, benefitted from IMF CD and will guide future reforms under the program.

Modification of quantitative performance criteria. In light of stronger-than-expected performance and to further build external and fiscal buffers, the end-December 2023 targets for the budget deficit and the present value of external debt ceilings are proposed to be reduced, and the floor on net international reserves increased. The definitions of two QPCs (net international reserve floor and gross credit to government ceiling) are proposed to be modified, in line with safeguards assessment recommendations, and the scope of the deficit ceiling QPC clarified to capture budgetary transfers to trust accounts without adding net movements in trust account balances.

Policy discussions. Policy discussions focused on i) the preparation of the supplementary budget for 2023 and the budget for 2024, including the composition of the consolidation effort and the specific measures to support it, consistent with the authorities' medium-term fiscal strategy; ii) the implementation of the Roadmap, in particular the start of the gradual return to kina convertibility and the modernization of monetary and FX policy operations; and iii) the first concrete steps for the operationalization of the governance and anti-corruption framework.

Staff Views. Given the strong program performance and the authorities' sustained commitment to reforms, staff supports the request for completion of the first review under the EFF and ECF arrangements. The Letter of Intent and Memorandum of Economic and Financial Policies demonstrate program ownership and appropriate policies to reach the goals of the authorities' program.

Approved By
Sanjaya Panth (APD) and Jarkko Turunen (SPR)

A staff team consisting of Tahsin Saadi Sedik (head), Fabien Gonguet, Yirbehogre Modeste Some (all APD), Asad Qureshi (MCM), Miguel Ricaurte (SPR) and Kaleb Tamiru Gulilat (FAD) visited Port Moresby during September 7-21, 2023. The mission met with Treasurer Ian Stuckey-Ling, BPNG Acting Governor Elizabeth Genia, Chair of the BPNG Board David Toua, Treasury Secretary Andrew Oaeke, Internal Revenue Commissioner General Sam Koim, senior government officials, development partners, and representatives of the private sector. Ms. Karl (OED) participated in meetings with the government. The mission was assisted by Sohrab Rafiq, Resident Representative and Sylvester Kilian, local economist. Nadine Dubost, Loa Anisi and Saraf Nawar provided administrative and research support for the preparation of the staff report.

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CONTEXT

1. **The ECF and EFF arrangements, approved by the Board in March 2023, aim to support the Papua New Guinea (PNG) authorities' reforms to address a protracted balance of payments need and long-standing structural impediments to inclusive growth.** While ambitious, the program is focused on macrocritical conditionality, supported by capacity development (CD), and informed by the Country Engagement Strategy (CES, Annex IV), in line with the IMF's Strategy for Fragile and Conflict-Affected States (FCS).

2. **The program is off to a strong start, with the authorities displaying a continued commitment to reforms.** End-June 2023 budget execution data points to strides in the government's fiscal consolidation strategy, which the 2024 budget, under preparation, is expected to continue supporting. The Bank of PNG (BPNG) has announced monetary policy operations reforms in its March and September 2023 Monetary Policy Statements, allowed a gradual depreciation of the exchange rate, and intervened actively to alleviate FX shortages. The Independent Commission Against Corruption (ICAC) Commissioner and Deputy Commissioners have been formally sworn in.

3. **From a political standpoint, the current grace period continues to offer a window of opportunity for reforms, despite challenges.** The government, elected in July 2022 with a wide majority, cannot face motions of no confidence in parliament until February 2024, which currently provides an environment of political stability conducive to reforms. The government has repeatedly communicated the objectives of the program to Parliament and the private sector, emphasizing that the IMF program is supporting homegrown reforms.

RECENT DEVELOPMENTS, OUTLOOK AND RISKS

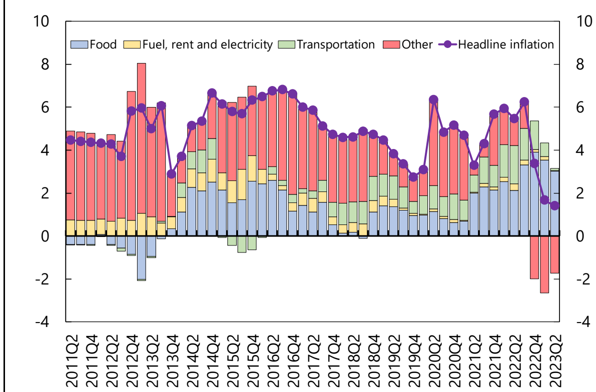
4. **Growth in 2022 was driven by the non-resource sector as the economy fully reopened.** In 2022, growth is estimated at 4.3 percent, supported by the removal of COVID-related restrictions allowing the non-resource sector to rebound. The resource sector, however, was affected by delays in reopening of the Porgera gold mine and planned maintenance shutdown of LNG production.

5. **Headline inflation has fallen faster than expected, but core inflation remains sticky.** Year-on-year headline inflation declined to 1.4 percent in 2023Q2, mainly reflecting a one-off reduction in tuition costs, and lower imported inflation. Core inflation is stickier, at 4.5 percent as of 2023Q2, slightly lower than the historical average.

6. **At 5.3 percent of GDP, the 2022 fiscal deficit was slightly lower than expected, driven by strong resource revenue performance**. The fiscal balance improved by 1.5 percentage point relative to 2021, consistent with the authorities' medium-term budget repair strategy. Revenue collection exceeded projections, driven by mining and petroleum taxes (owing to higher commodity prices).

Contribution to Headline Inflation

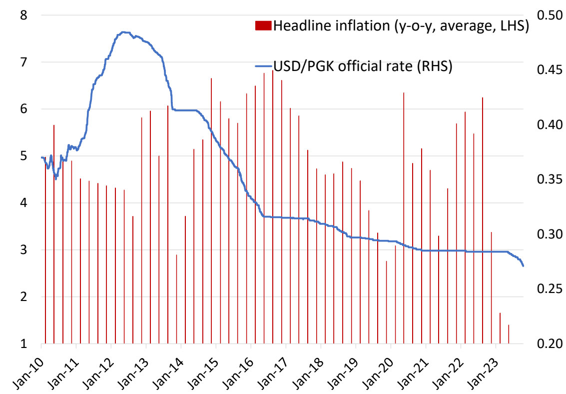
(In percentage points)



Source: IMF staff based on official data.

Inflation and Exchange Rate

(In percentage points (lhs) and US dollar per kina (rhs))



Source: IMF staff based on official data.

7. PNG's public and publicly guaranteed debt remains at high risk of debt distress (Debt Sustainability Analysis (DSA)). The elevated debt, compounded with the liquidity risk associated with the bullet payment due in 2028 on PNG's existing Eurobond and higher official bilateral and multilateral debt service payments between 2026 and 2029, leads to breaches of the debt service-to-revenue ratio threshold. External debt is also susceptible to export-related shocks in a global environment of high uncertainty; and the profile of domestic debt, highly concentrated in short-term Treasury bills, raises rollover risks and calls for a proactive debt management strategy by the authorities to deal with lumpy debt servicing.

8. The current and capital account balances improved in 2022, but FX shortages persist. The current account balance was boosted by a wider trade surplus, driven by high commodity prices and weaker imports, while the capital account balance also widened, leading to further accumulation of FX reserves. The exchange rate has been gradually depreciating since May 2023 (about 5 percent against the US dollar as of end-October 2023). In line with the EBA-lite REER model presented at program approval,[1] PNG's external position in 2022 was substantially weaker than the level implied by medium-term fundamentals and desirable policies, with the REER overvalued by 13.4 percent. Alternative models using higher frequency data point to a milder overvaluation of the REER of 7 percent as of end 2022 (Annex VI), which has continued to moderate in the first half of 2023 due to lower inflation in PNG. Despite this, FX shortages remain persistent, hampering imports and economic activity.[2]

9. Banks are reported to be well-capitalized, profitable, and with ample liquidity. As of mid-2023, capital adequacy ratios remain well above prudential standards, and bank profits, while

[1] See Annex II of the Staff Report for the Requests for an Arrangement Under the ECF and an Extended Arrangement Under the EFF (IMF Country Report No. 23/126).

[2] See Annex VII of the Staff Report for the 2022 Article IV Consultations (IMF Country Report No. 2022/305) for more details on the reasons for FX shortages.

moderating in the first half of 2023, remain comfortable. Private sector credit has picked up in the first half of 2023 and nonperforming loans have decreased since 2021.

10. In light of declining inflation, the BPNG lowered its monetary policy rate. The Kina Facility Rate (KFR) was lowered from 3.5 percent to 3.0 percent in September 2023, signaling a more accommodative stance. However, the BPNG's successful efforts in absorbing excess liquidity constitute a *de facto* tightening.

11. The outlook remains positive. Growth in 2023 is expected to soften to 3.0 percent, due to the normalization of LNG production, before rebounding to 5.0 percent in 2024, spurred by the expected reopening of Porgera gold mine and by sustained growth in the agriculture and service sectors. Inflation is projected to rise in the latter half of 2023 and into 2024, as the base effect of fiscal measures fades and the exchange rate passthrough from kina depreciation progresses, reaching 3.5 percent by end-2023 (year-on-year) and 5.0 percent by end-2024. Over the medium term, growth is projected to stabilize at around 3.1 percent, supported by the non-resource sector, and inflation is expected to converge to 4.5 percent.

12. Risks to the outlook are tilted to the downside but there are also significant upside risks to growth, exports, and fiscal revenues (Annex I). Downside risks include a weaker external demand for PNG's exports, a drop in commodity prices, and natural disasters, including from El Niño. Reform implementation could be hampered by political developments, particularly once the grace period expires. The ongoing dispute between the BPNG and the main fuel importer about access to FX could lead to economy-wide fuel supply issues in the absence of resolution. On the upside, risks include higher commodity prices, and the start of major resource projects, which are not yet in the baseline scenario. The construction phase of Papua LNG could yield an average 0.6 percentage point of additional annual growth over 2024-29 (see Annex III for a detailed alternative scenario).

PROGRAM PERFORMANCE

13. Program performance has been strong, with all end-June 2023 quantitative performance criteria (QPCs) met (Text Table 1 and Table 10). The fiscal overperformance was supported by non-resource tax collection, while priority spending was well above the indicative floor. Net international reserves (NIR) have remained above the QPC floor despite a large FX intervention in May 2023. PNG has not accumulated new external arrears, and new external debt remains well within the present value QPC. There was no new multiple currency practice (MCP) nor modification of existing MCPs, and no intensification of exchange restrictions since program approval.[3]

[3] For details on MCPs and exchange restrictions maintained by PNG, see Annex II of the Staff Report for the Requests for an Arrangement Under the ECF and an Extended Arrangement Under the EFF (IMF Country Report No. 23/126).

Text Table 1. Papua New Guinea: QPCs and ITs, First Half of 2023
(In millions kina, unless mentioned otherwise)

	2022	2023					
	December	March			June		
		Indicative target			Test date		
	Est.	Approved	**Outcome**	Status	Approved	**Outcome**	Status
A. Quantitative performance criteria[1]							
Fiscal deficit of the government (ceiling, cumulative from the beginning of the year)	5,985	1,646	**449**	met	3,092	**2,858**	met
Stock of net international reserves of the BPNG (floor, US$ millions)	3,226	2,845	**2,996**	met	2,463	**2,831**	met
BPNG's gross credit to government (ceiling)	2,051	2,400	**1,913**	met	2,400	**2,032**	met
B. Continuous quantitative performance criteria (ceilings)[2]							
New external payment arrears of the government (ceiling, US$ millions)	0.0	0.0	**0**	met	0.0	**0**	met
Present value of new external debt contracted or guaranteed by the government[3] (ceiling, US$ millions)		1,405	**0**	met	1,405	**60**	met
C. Indicative Targets							
Non-resource tax revenue of the government (floor, cumulative from the beginning of the year)	10,831	2,512	**2,787**	met	5,023	**5,900**	met
Social and other priority spending (floor, cumulative from the beginning of the year)[4]	3,678	500	**998**	met	1,500	**2,069**	met
BPNG provision of foreign exchange to authorized FX dealers (floor, cumulative from the beginning of the year, US$ millions)	878	300	**300**	met	600	**773**	met

Sources: Papua New Guinea authorities and Fund staff estimates.
[1] Quantitative performance criteria listed under A. and indicative targets listed under C. are assessed as at the end of each reference month above.
[2] Quantitative performance criteria listed under B. are effective continuously from program approval.
[3] Annual for 2023.
[4] Comprises government spending on health, education and law and order (both capital and operating expenses).

14. The structural reform agenda is progressing well (Table 11). All structural benchmarks (SBs) were met in timely fashion, except for the adoption of the new Medium-term Revenue Strategy (MTRS), which was implemented with slight delay. The MTRS and the monetary and FX reform roadmap (the 'Roadmap'), are key strategic documents which were prepared by the authorities with IMF TA support and will serve as references for the setting of future SBs.

POLICY DISCUSSIONS

A. Sustaining the Fiscal Consolidation Momentum

15. The authorities' deficit target for 2023 is slightly smaller than at program approval, sustaining a significant fiscal adjustment of 0.9 percentage point of GDP relative to 2022. In line with the supplementary budget for 2023, the deficit target stands at 4.4 percent of GDP (Text Table 2 and MEFP ¶11), smaller by K50 million relative to program approval (QPC).[4] Revenue is

[4] The deficit target has been revised from K4.985 bn in the initial budget to K4.935 bn in the supplementary budget. Because of a downward revision of the 2023 nominal GDP from K114.8 bn at program approval to K112.2 bn, the deficit-to-GDP ratio is however slightly more negative (4.4 percent of GDP, against 4.3 at program approval).

expected to be K0.8 billion higher than in the initial budget, as the observed overperformance in tax revenue collection in the first half of the year (K1.4 billion), driven largely by higher corporate income tax revenues in both the non-resource and resource sectors, was partly offset by lower dividend payments from the resource sector (-K0.7 billion). The end-December 2023 IT on non-resource tax revenue is proposed to be revised from K12.5 billion to K12.7 billion, driven by the overperformance in tax collection. On top of the slight deficit reduction, this additional revenue will be used to cover additional interest expenditure from higher global interest rates (+K0.3 billion), and additional goods and services expenditure (+K0.5 billion) to face additional rental and utility costs and enable faster clearance of domestic arrears. In case of further revenue overperformance by the end of the year,[5] the authorities are committed to either further accelerate arrears' clearance, reduce the deficit or increase priority spending (MEFP ¶13).

16. Fiscal consolidation is expected to continue in 2024, in line with the authorities' medium-term budget repair strategy. A more moderate fiscal adjustment is expected in the 2024 budget, to be tabled to parliament in late November, with a deficit reduction of 0.5 pp of GDP (MEFP ¶12). Total revenue is projected to fall by 0.1 pp of GDP; the sharp expected decrease of resource tax revenue due to lower commodity prices (-1.0 pp of GDP) will be offset by (i) the adoption of new tax policy measures (+0.4 pp of GDP), including revisions to personal income tax rules on fringe and dependent benefits, the rollout of the goods and services tax (GST) to the extractive and finance sectors, and the reform of taxes on tobacco and alcohol; and (ii) a new dividend policy regarding state entities in the extractive sector (+0.6 pp of GDP). Expenditure will decrease by 0.6 pp of GDP relative to 2023, in keeping with the strategy to rationalize current spending while preserving priority sectors (MEFP ¶17). Capital spending will also contribute about half of this effort (-0.3 pp of GDP), to avoid crowding out private sector investment. As a contingency, the authorities have identified expenditure items that could be deferred or cancelled in case of revenue shortfalls (MEFP ¶13).

17. Authorities intend to stay the course on fiscal consolidation. The authorities' medium-term fiscal framework envisions a fiscal consolidation path that entails a balanced budget by 2027 and surpluses thereafter, largely underpinned by sustained domestic revenue mobilization efforts,

Text Table 2. Papua New Guinea: Fiscal Adjustment Plan, 2020-2026

(In percent of GDP)

	2020	2021	2022	2023		2024	2025	2026
				Prog. Approval	First Rev. Latest		Proj.	
Revenue and Grants	**14.7**	**15.0**	**16.7**	**17.1**	**18.2**	**18.0**	**18.5**	**18.8**
Resource revenue 1/	0.9	1.1	3.9	3.5	3.6	3.1	3.3	3.1
Non-resource revenue	13.7	13.9	12.8	13.5	14.6	14.9	15.2	15.6
Non-resource tax revenue (% non-resource GDP)	15.4	13.6	16.1	15.2	15.8	16.7	17.0	17.2
Expenditure	**23.5**	**21.8**	**22.0**	**21.4**	**22.6**	**22.0**	**21.0**	**20.2**
Expense	19.3	17.9	18.0	17.4	18.5	18.2	17.4	16.8
Net acquisition of non-financial assets	4.3	4.0	4.0	4.0	4.1	3.8	3.6	3.4
Overall deficit	**8.9**	**6.8**	**5.3**	**4.3**	**4.4**	**3.9**	**2.5**	**1.4**
Primary deficit	6.2	4.4	3.0	2.2	1.9	1.5	0.2	-0.9
Fiscal adjustment		**-2.1**	**-1.5**	**-0.9**	**-0.9**	**-0.5**	**-1.4**	**-1.1**
Revenue		*-0.4*	*-1.7*	*-0.3*	*-1.5*	*0.1*	*-0.4*	*-0.3*
Expenditure		*-1.7*	*0.2*	*-0.6*	*0.6*	*-0.6*	*-1.0*	*-0.8*

Sources: Department of Treasury; and IMF staff estimates and projections.

1/ Does not include projected revenues from new mining projects where the investment decision has not yet been reached.

[5] The legality of the Additional Company Tax introduced in the 2022 Budget is being challenged, with payments received in 2022 held in escrow accounts and not included in reported revenue. Should the courts uphold the ACT, revenues would be higher.

continued expenditure rationalization (MEFP ¶15 and ¶16) and prudent external and domestic borrowing mix. Fully executed, the envisaged fiscal consolidation strategy would help strengthen debt sustainability by lowering public debt to 46.5 percent of GDP in 2028 from an estimated 52.4 percent in 2023.

18. Strengthening revenue collection remains key to a successful fiscal consolidation strategy (MEFP ¶14). This relies on the implementation of the MTRS and a rewrite of the Income Tax Act (ITA) to simplify and modernize the tax system (ongoing SB for end-December 2023), with the support of FAD TA. The scope of the MTRS is broad to encompass all main revenue collecting agencies and cover all main taxes collected from the resource and non-resource economy. To enhance revenue administration, the authorities will continue the modernization of the IRC's tax administration system and ensure the implementation of the 2017 Tax Administration Act (TAA), which means to make revenue collection procedures more uniform across taxes but is not yet operational. The Internal Revenue Commission (IRC) has adopted a new functional structure in late July 2023. The adoption by IRC of an initial set of key performance indicators, with Fund support, to enhance revenue administration is proposed as a ***new SB by end-May 2024***. To reinforce IRC's accountability, the creation of an oversight board, which requires to amend the 2014 IRC Act, is also proposed as a ***new SB by end-October 2024***.

19. To create space for social and capital spending, ongoing efforts to improve expenditure efficiency need to be sustained.

- *Payroll management (MEFP ¶17)*. To enhance payroll management, the authorities have completed HR Business Process workshops on staffing and remuneration guidelines with the main government departments (SB for end-June 2023). Based on the findings of the staffing and establishment review for teachers, completed in 2023, and the recent payroll diagnostic review, planned reforms include changes in HR policies to unify practices across departments and enhancements in payroll management systems. While the authorities work on upgrading AscenderPay (payroll IT system) to the latest version, cleansing of payroll records in the system is proposed as a ***new SB by end-August 2024***.

- *Expenditure management and controls (MEFP ¶18 and ¶19)*. To accelerate arrears clearance (remaining stock of unverified claims amounting to K1.96 billion), the authorities plan to increase their budget allocation in the 2024 budget, and in case of future revenue over-performance going forward. While the authorities are committed to prevent new arrears from arising, FAD TA has been requested to assist in strengthening expenditure controls throughout the expenditure chain and enabling more automated, timely and effective monitoring of budget execution. In addition, to better manage trust accounts, authorities plan to gradually reduce their cash balances, with Fund advice, while committing to close all remaining COVID-related trust accounts by end 2023.

- *Cash management (MEFP ¶20)*. To modernize cash management practices, the authorities intend, with FAD TA support, to centralize government funds from commercial banks into the central bank, paving the way for a Treasury Single Account (TSA).

20. The authorities are committed to continued prudent external borrowing policy to preserve debt sustainability (MEFP ¶21). Prioritization of concessional loans and grants, alongside semi-concessional financing for critical projects, is essential to ensure debt enters a downward trajectory. To inform borrowing decisions, a limit on the PV of new external borrowing is proposed for 2024 (QPC), allowing for some loans previously expected but unlikely to be contracted in 2023 to occur next year. The PV limit for 2023 is proposed to be revised down accordingly.

B. Making the Exchange Rate More Flexible and Enhancing Monetary Policy Effectiveness

21. To address FX shortages, the authorities are committed to a gradual transition to exchange rate flexibility and a clearer monetary policy framework (MEFP ¶23). The authorities agree that the most appropriate framework for the gradual return to kina convertibility by the end of the program is to implement a crawl-like exchange rate arrangement, which will act as the nominal anchor for monetary policy (Annex II). Setting the key parameters for the arrangement is proposed as a ***new SB for end-November 2023***, for implementation in early December 2023. The new arrangement should allow to help address the overvaluation of the kina. While tackling the overvaluation rapidly, for instance through upfront devaluation, would help resolve FX shortages sooner and reduce the burden of FX interventions on reserves, the authorities see high political and social costs associated with that strategy, hence their stated preference for a gradual approach to depreciation. The authorities are determined to fully resolve the misalignment of the exchange rate during the program. That said, the kina has been gradually depreciating since May 2023, at a pace which is expected to help reduce part of the estimated overvaluation (7 percent, see Annex V) by the time of the shift to the crawl-like arrangement.

22. The authorities' Roadmap proposes a sequencing of measures consistent with the transition. Prepared with the support of MCM TA, the Roadmap includes measures to enhance the formulation of monetary policy, gradually remove FX rationing, support more effective liquidity management, and enhance communication (MEFP ¶22). It also includes government cash management reforms and needed improvements to inflation data compilation and forecasting. The BPNG will share regular progress reports on the implementation of the Roadmap with the Board of the BPNG, the Treasury and the IMF.

23. The long-standing vacancies in BPNG's senior management and Board create a governance gap, with implications for oversight and for progress in modernization efforts. To reinforce BPNG's governance and to ensure adequate steering of the implementation of the Roadmap, it is critical for the authorities to swiftly appoint BPNG's permanent Governor and Deputy Governors and to fill out vacancies at the BPNG Board (proposed ***new SB by end-November 2023***), which have prevented reaching a quorum in a number of recent instances (MEFP ¶26).

24. The BPNG aims to take cautious first steps towards reducing FX rationing (MEFP ¶24). Despite BPNG's record FX intervention to the market in May 2023 (US$273 million), the backlog of FX orders has been building up again due to a persistent mismatch between FX demand and supply.

In addition, there is large pent-up FX demand from dividends waiting to be repatriated. In line with the Roadmap and IMF TA and advice, FX rationing measures should be gradually eased as the exchange rate approaches its equilibrium to limit the cost on reserves. In the early days of the new arrangement, the size of FX interventions by the BPNG should hence be guided by the quantity of unmet import-related orders. For that reason, it is proposed that as of January 2024, the indicative floor on BPNG's provision of FX to the market be replaced by a new indicative ceiling on the stock of unmet import-related orders in the orderbook, with the aim to ensure that these orders do not linger on the orderbook. To safeguard FX reserves, the NIR floor (QPC) is proposed to be adjusted upwards relative to program approval, given higher FX inflows than expected from resource tax revenue (MEFP ¶37) and due to SDR allocations no longer being subtracted in the calculation. In addition, the following short-term actions aimed at levelling the playing field in the FX market are proposed as ***two new SBs for end-December 2023***: (i) the publication on BPNG's website of all regulations and directives regarding the FX market; and (ii) the elimination by BPNG of its requiring a tax clearance certificate prior to including FX orders related to intercompany loans obtained for import payments in the orderbook. Staff recommends eliminating existing exchange restrictions and MCPs in gradual fashion, consistent with the Roadmap and in line with Fund advice.

25. The BPNG intends to build on the fixed-rate full-allotment (FRFA) tender to further enhance liquidity management (MEFP ¶25). While commercial banks are still adjusting their liquidity management and forecasting under the new framework, the first few weekly FRFA auctions have already helped successfully mop up about K2 billion of excess liquidity. The BPNG has opted for a fixed rate of 2 percent for the issuance of the 7-day central bank bills (CBBs), thus below the KFR (3 percent). Issuance at the KFR will be needed going forward, as per MCM's recommendations, to help improve monetary transmission, avoid conflicting signals on the policy stance and enable other liquidity management reforms in the Roadmap. The alignment of the fixed rate for the issuance of the 7-day CBBs with the KFR is hence proposed as a ***new SB for end-December 2023***. The authorities also plan to implement an interest rate corridor bounded by overnight standing facilities by the end of the year, and to modify the reserve maintenance period and introduce reserve averaging in early 2024.

26. The authorities have started working on draft amendments to the CBA to tackle remaining vulnerabilities in the BPNG's mandate and governance (MEFP ¶27). Amendments will at least include the removal of the requirement for BPNG to provide advances to the government on demand, a ranking of the mandates of the BPNG with price stability as the BPNG's primary objective, and a clarification of the role of the BPNG Board in monetary policy formulation. These amendments are expected to be shared with the IMF for consultation in the fall before they are presented to Parliament (ongoing SB for end-December 2023). Additional amendments on improvements in financial regulation and supervision, based on the Independent Advisory Group (IAG)'s Phase II review of the CBA, will also be introduced, though it is important they do not contribute to unwinding gains in strengthening AML/CFT frameworks (MEFP ¶28). The financial independence of the BPNG has been reinforced in recent months, as the government moved to stop establishing the level of BPNG's dividend *ex ante*; staff also recommends the strengthening of related profit distribution provisions in the CBA. In addition to the planned amendment on the provision of advances, the QPC on BPNG's gross credit to government is maintained to prevent monetary financing.

C. Turning Good Governance Commitments into Action

27. The authorities are continuing their efforts to strengthen governance and anti-corruption frameworks.

- *Anti-corruption framework (MEFP ¶30)*. The Commissioner and two Deputy Commissioners of the Independent Commission Against Corruption (ICAC), who are all internationals with decades of experience in the field, have been competitively selected and effectively sworn in. Based on best international practice, this new management team has been working on drafts for the key implementing regulations to the ICAC law, especially regarding its preventive, investigative and prosecutorial mandates and its information sharing modalities (ongoing SB by end-December 2023). Ensuring sufficient budget allocations in 2024 and beyond will be needed for ICAC to effectively carry out its mandate.

- *AML/CFT (MEFP ¶29)*. The BPNG's Financial Analysis and Supervision Unit (FASU) increased staff capacity, provided trainings to stakeholders and strengthened supervisory activities for the Asia-Pacific Group on Money Laundering (APG)'s mutual evaluation against the FATF standards, for which an onsite visit took place in October 2023; the final report is expected to be adopted in July 2024. The AML/CFT Strategic Plan 2023-27 was adopted in September 2023 with a focus on enhancing the effectiveness of AML/CFT frameworks.

- *Governance of state-owned enterprises (SOE) (MEFP ¶33)*. The ADB has provided continuous support to Kumul Consolidated Holdings (KCH) to improve the financial and corporate governance of SOEs in its portfolio; this includes the availability of more timely and comprehensive financial information on individual SOEs. Reform priorities now include revisions to SOEs' procurement and dividend policies to harmonize practices across the SOE portfolio.

28. Some progress has been achieved in enhancing fiscal and financial transparency, but further effort is needed (MEFP ¶27, 29, 31, 32). The BPNG improved the computation and reporting of external sector statistics (ESS) (see Annex V) and financial soundness indicators (FSI) on its website, with the support of the IMF. More comprehensive GFS tables have been published alongside budget documents. The setup of an inter-agency working group to improve the consistency of ESS with other sectoral statistics is proposed as a ***new SB for end-June 2024***. The publication of information on COVID-related procurements, including on beneficial ownership, is on track to resume by the end of the year (ongoing SB for end-December 2023). However, the BPNG published its FY21 audited financial statements with delay; and the FY22 statement is not yet finalized.

PROGRAM MODALITIES

29. Program monitoring and conditionality. Program performance will continue to be monitored through semi-annual program reviews based on QPCs and ITs (Table 10), and SBs (Table 11). Target modifications are proposed for the deficit ceiling (QPC, ¶15), the NIR floor (QPC, ¶24), the ceiling on the PV of external debt (continuous QPC, ¶20) and the non-resource tax revenue floor (IT, ¶15). Modifications of the definitions of the NIR floor (TMU ¶11-14) and the gross credit to government ceiling (TMU ¶16) are proposed, in line with safeguards assessment recommendations. A revised scope of the deficit ceiling QPC is proposed to capture budgetary transfers to trust accounts without adding net movements in trust account balances, concomitantly with the authorities' commitment to better manage trust accounts (¶19). The definition of the ceiling on new domestic arrears is specified (as proposed in TMU ¶28). Nine new SBs are proposed, adding to the four already ongoing.

30. Burden sharing and financing assurances. The program is fully financed, with firm commitments for the upcoming 12 months and good prospects of adequate financing for the remainder of the arrangement. Assistance from the Fund is expected to play a catalytic financing role with other multilateral and bilateral partners. Fund burden sharing is expected to average 36.1 percent across the program.

31. Capacity to repay the Fund. PNG's capacity to repay the Fund remains adequate (Table 8) but is subject to elevated risks. Based on an ECF/EFF disbursement of 260 percent of quota, principal obligations to the Fund would peak in 2032 at around 121.7 million SDRs (46.2 percent of IMF quota). This represents 2.0 percent of government revenue and 0.9 percent of exports of goods and services. Outstanding IMF credit peaks at 34.8 percent of gross international reserves in 2028. Downside risks include weaker external demand for PNG's exports, volatility in commodity prices and natural disasters (Annex I). Risks to capacity to repay are partially mitigated by a commitment to fiscal sustainability and macroeconomic stability in the medium-term. In addition, macroeconomic projections are built on conservative assumptions regarding prospects of the new resource projects, which are not part of the baseline projections.

32. Safeguards assessment. An update safeguards assessment mission is complete. Recommendations included the urgent need to eliminate the governance gaps at the BPNG (¶23) and the need to address the remaining vulnerabilities in the legal framework (¶26). These are covered under the program through structural benchmarks. Other priority recommendations include strengthening the financial reporting timeliness, aligning the internal audit practice to international standards, and finalizing the framework for the treatment of the 2021 SDR allocations that were used for budget support.

33. Program risks and mitigating measures. Risks to the program arise from the authorities' limited implementation capacity in a volatile economic and political environment. To address these risks, conditionality is streamlined, focused, macro-critical, and informed by PNG's CES (Annex IV). Bimonthly program monitoring meetings, with both the Treasury and the BPNG, have taken place to ensure focus on program targets and commitments. The Resident Representative office, set up in November 2022, has also facilitated regular interactions with the authorities.

34. Capacity development (CD). Ongoing and planned IMF CD activities are closely integrated to the program (see CES in Annex IV). In the past year, IMF CD has hence supported the preparation of the Roadmap (MCM), the preparation of a new MTRS and the revision of the ITA (FAD), and FSI compilation (STA). This has been complemented by support on revenue administration (PFTAC), macro-fiscal forecasting (ICD/PFTAC), and BOP data (CDOT/STA). A Financial Sector Stability Review is scheduled for January 2024. Public financial management TA (FAD) on expenditure controls and cash management was requested for early 2024. Fund TA is complemented by (and coordinated with) other partners, including anti-corruption framework (UN and EU), governance of SOEs (ADB), and national accounts and AML/CFT (Australia).

35. Data gaps. Data reporting has been strengthened to support program monitoring. A Program Monitoring Committee has been set up to support information-sharing with staff. Shortcomings in National Accounts compilation, particularly the production of CPI statistics, need to be addressed.

STAFF APPRAISAL

36. The economic outlook is positive, notwithstanding downside risks. Non-resource growth is expected to continue its post-pandemic rebound, while resource growth should pick up in 2024 with the reopening of Porgera gold mine. Inflation has been declining due to the combined effects of fiscal measures and of lower imported inflation; but it is expected to rise and reach 3.5 percent at end-2023 and 5.0 percent at end-2024. Downside risks are significant, with exports, fiscal revenues and FX reserves vulnerable to commodity price shocks. However, the start of new large resource projects, such as Papua LNG, represents a major upside scenario for economic growth in the near to medium run.

37. The authorities have demonstrated continued commitment to reforms. The program performance has been strong, with the authorities meeting all QPCs and SBs, although one SB was implemented with a slight delay. This includes the adoption of important strategic documents – the MTRS and the monetary and FX reform roadmap – which will guide authorities' reform efforts for the remainder of the program and beyond.

38. Fiscal consolidation efforts should continue in order to durably reduce the deficit and address debt sustainability risks. In the past three years, the authorities have made significant headway in their deficit reduction strategy. The 2023 deficit-to-GDP ratio is on track to get back to its pre-pandemic level at 4.4 percent of GDP, that is about half of the 2020 ratio. Given the high uncertainty on resource revenue going forward, fiscal consolidation efforts in 2024 and beyond should rely both on domestic revenue mobilization, especially for non-resource tax revenue, in line with the new MTRS, and on expenditure rationalization and efficiency gains. The authorities' cautious approach to fiscal management, relying on conservative assumptions and clear contingency plans, will also be key in ensuring a successful consolidation.

39. As inflation is expected to bounce back in the coming months, the BPNG should stand ready to tighten its monetary policy stance. The concurrent easing of the policy rate and reduction of excess liquidity – a *de facto* tightening – have made communication of the monetary policy stance challenging. Going forward, further tightening may be needed to avoid inflation increasing beyond its historical average. The kina has been depreciating against the US dollar, allowing to reduce part of the overvaluation. The historically low headline inflation, strong US dollar and comfortable FX reserves place the authorities in a comfortable position to bring the exchange rate to the equilibrium.

40. BPNG's commitment to monetary and FX reforms has been encouraging since the start of the program, but it is now critical for the government to fill out the pending vacancies in its senior management and board. The BPNG has shifted to a fixed rate full allotment auction for its monetary policy operations, sharply reducing excess liquidity. Increasing the fixed rate to the KFR is appropriate, and aligning the two rates is critical to enhance monetary policy effectiveness and avoid inconsistency in signaling the monetary stance. To support these major shifts in monetary and FX operations, staff urges the government to fill out vacant Board positions and to appoint a BPNG Governor and Deputy Governors.

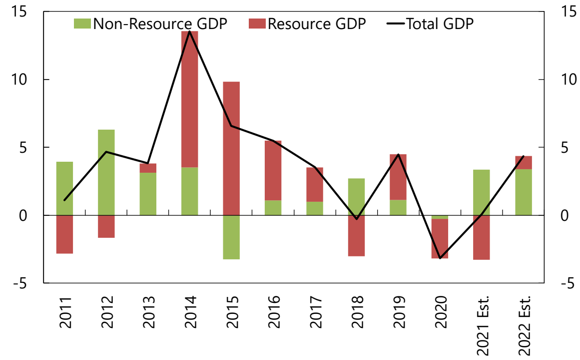
41. Building on recent achievements will be essential to effectively enhance the anti-corruption, governance and AML/CFT frameworks. The ICAC is actively gearing up to become fully operational in 2024. This however hinges on sufficient budget resources being allocated to it. Staff is also supportive of the authorities' efforts towards greater transparency, including regarding COVID-19 related procurements, which should benefit from ongoing and planned improvements in IT systems. The authorities should continue to improve their AML/CFT effectiveness through timely implementation of the AML/CFT Strategic Plan 2023-27.

42. Given the strong program performance to date and the authorities' sustained commitment to reforms, staff supports the completion of the first review under the EFF and ECF arrangements. The Letter of Intent (Appendix I) and Memorandum of Economic and Financial Policies (Attachment I) demonstrate program ownership and appropriate policies to reach the goals of the authorities' program.

Figure 1. Papua New Guinea: Real and External Sector Developments

Real GDP recovered since the pandemic, led by the non-resource sector.

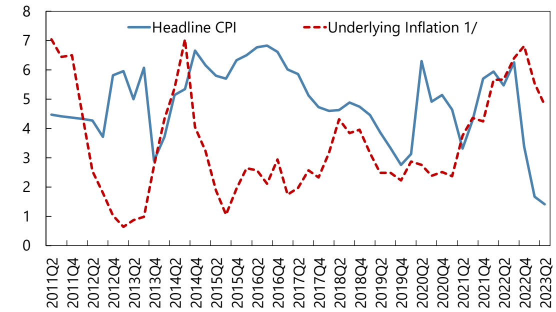
Real GDP Growth
(Contributions to percent change)



Source: IMF Staff Estimates

Headline inflation declined, but underlying inflation remains sticky.

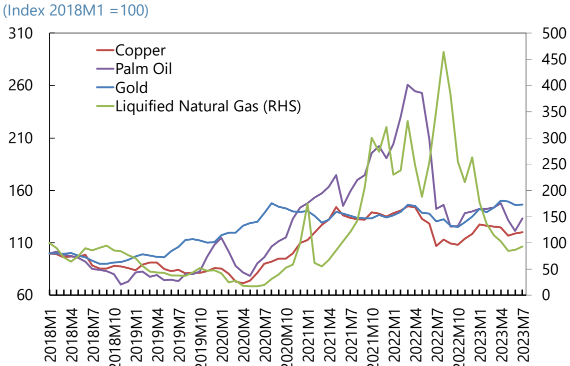
CPI Inflation
(In year-on-year percent change)



Sources: BPNG and IMF staff estimates
1/ Trimmed mean estimates published by BPNG.

Commodity prices have moderated since 2022 but remain higher than before the pandemic...

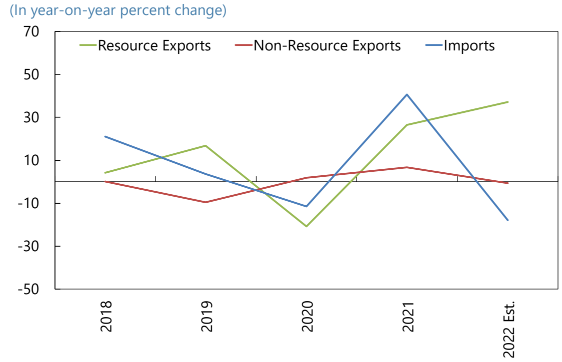
Commodity Prices
(Index 2018M1 =100)



Source: IMF Primary Commodity Price System

... supporting resource exports, while imports moderated.

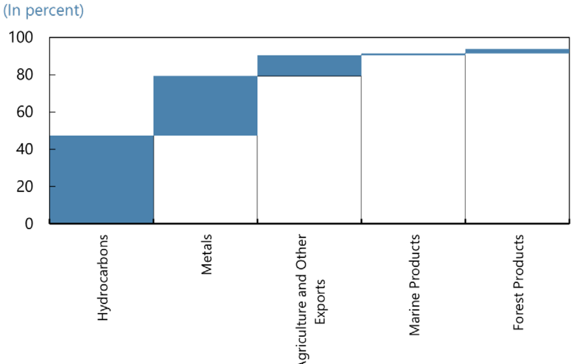
Exports and Imports
(In year-on-year percent change)



Source: IMF Staff Estimates

Strong global demand for PNG's export goods ...

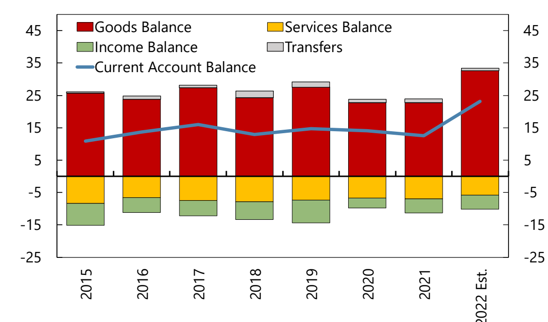
Export Product Share, 2022
(In percent)



Source: BPNG

... support the trade balance and current account.

Current Account
(In percent of GDP)

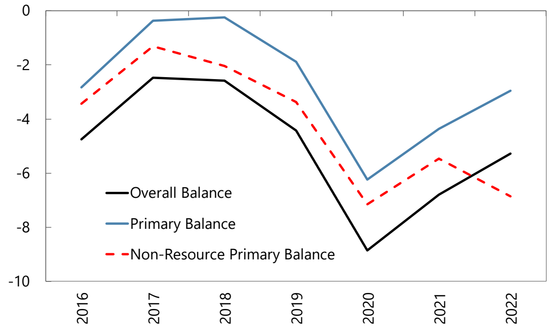


Source: BPNG, IMF Staff Calculations.

Figure 2. Papua New Guinea: Fiscal Developments

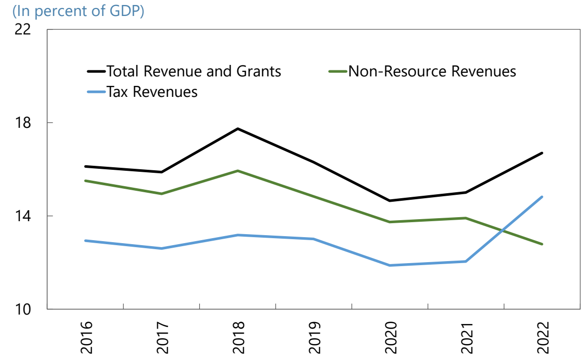
Fiscal consolidation continued in 2022…

Fiscal Balance
(In percent of GDP)



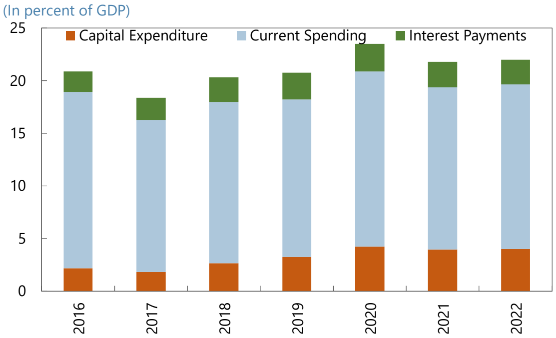
…driven by an improvement in resource revenues.

Central Government Revenue
(In percent of GDP)



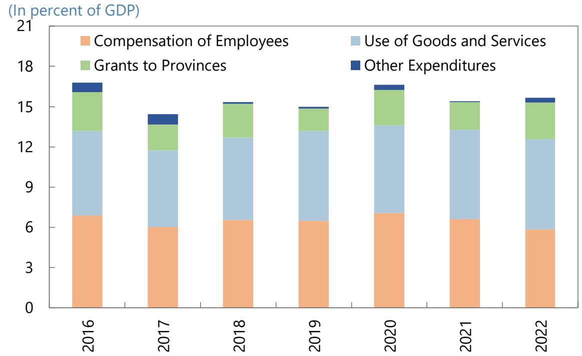
Current spending continues to take up the bulk of government spending…

Central Government Expenditure
(In percent of GDP)



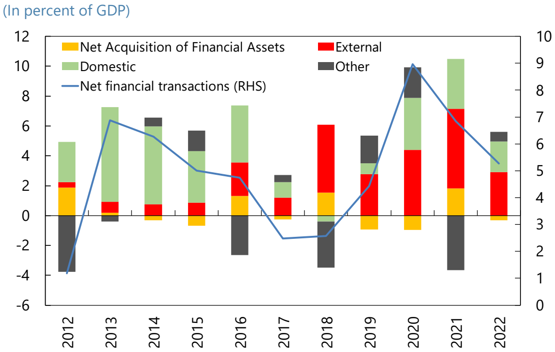
…driven by employee compensation and use of goods and services.

Recurrent Government Expenditure
(In percent of GDP)



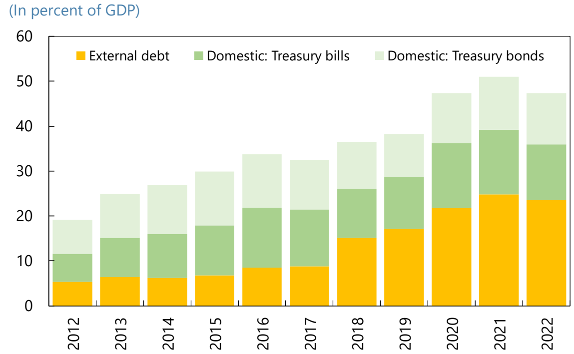
External financing sources are still dominant.

Financing
(In percent of GDP)



Despite a small decrease in 2022, public debt is more elevated than pre-pandemic.

Public Debt
(In percent of GDP)



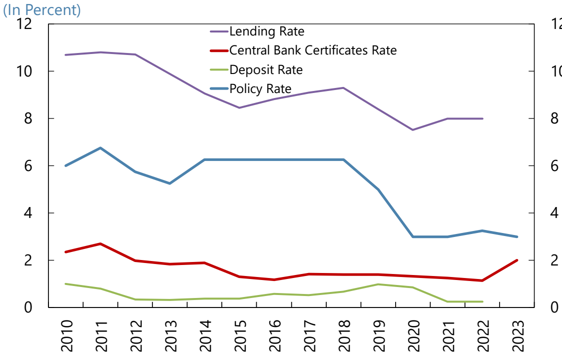
Sources: Country authorities; and IMF staff estimates and projections.

Figure 3. Papua New Guinea: Monetary and Financial Sector Developments

The central bank lifted the policy rate slightly in 2022 before reducing it back in 2023 in a context of lower inflation…

Interest Rates

(In Percent)

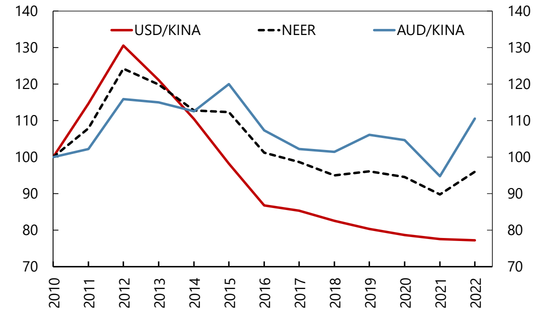


Note: Updated as of Sept 2023 (except deposit and lending rates, as of Dec 2022)
Sources: IFS and BPNG.

…while the kina had essentially stabilized against the US$ in recent years.

Exchange Rate

(Index; 2010=100)

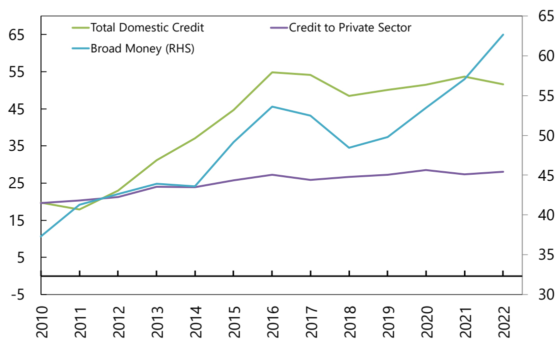


Note: Period averages.
Sources: IFS and IMF staff estimates.

Credit to the private sector has been broadly unchanged over the past six years…

Money and Credit

(In Percent of Non-Resource GDP)

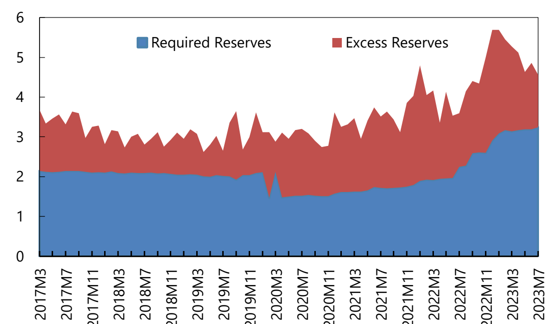


Sources: BPNG

…with significant excess liquidity in the banking system prior to the new liquidity instrument, introduced in August 2023.

Liquidity

(Billions of Kina)

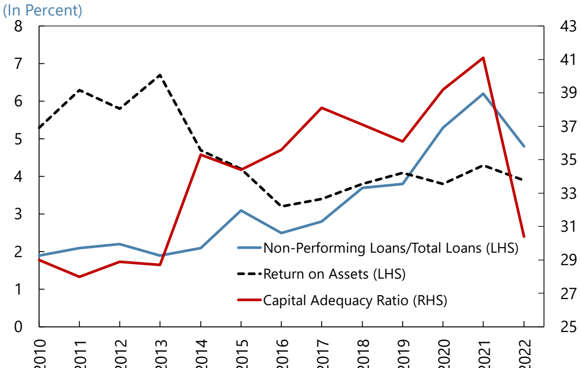


Source: BPNG.

NPLs are higher than before the pandemic, but banks remain profitable and well-capitalized.

Financial Stability

(In Percent)

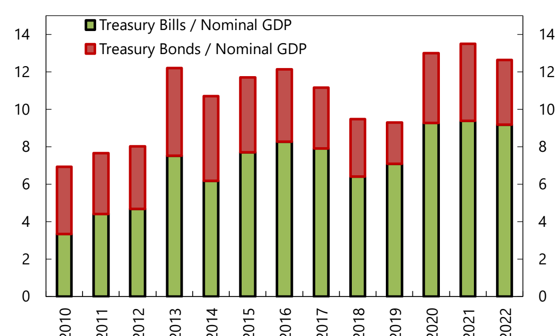


Sources: BPNG and IMF staff estimates.

Commercial banks holdings of government paper were broadly unchanged.

Holding of Government Securities by Commercial Banks

(In Percent of GDP)



Sources: BPNG and IMF staff estimates.

Table 1. Papua New Guinea: Selected Economic and Financial Indicators, 2019-2028

Nominal GDP (2021): US$26.3 billion 1/
Population (2021): 11.8 million
GDP per capita (2021): US$2,233
Quota: SDR 263.2 million

	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028
			Est.	Est.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
					(Percentage change)					
Real sector										
Real GDP growth	4.5	-3.2	0.1	4.3	3.0	5.0	3.1	3.1	3.0	3.1
Resource 2/	11.3	-9.2	-11.0	3.7	-1.4	6.3	0.1	0.1	0.1	0.2
Non-resource	1.6	-0.4	4.8	4.6	4.6	4.6	4.1	4.1	4.0	4.0
Mining and quarrying (percent of GDP)	10.8	10.2	8.5	8.0	8.4	9.6	9.7	9.6	9.4	8.8
Oil and gas extraction (percent of GDP)	17.6	14.1	15.9	22.6	16.8	16.0	14.4	12.2	10.4	9.7
CPI (annual average)	3.9	4.9	4.5	5.3	2.2	4.0	4.8	4.8	4.6	4.5
CPI (end-period)	2.7	5.1	5.7	3.4	3.5	5.0	4.8	4.8	4.6	4.5
					(In percent of GDP)					
Central government operations										
Revenue and grants	16.3	14.7	15.0	16.7	18.2	18.0	18.5	18.8	19.4	19.6
Of which: Resource revenue	1.5	0.9	1.1	3.9	3.6	3.1	3.3	3.1	3.2	3.2
Expenditure and net lending	20.7	23.5	21.8	22.0	22.6	22.0	21.0	20.2	19.3	19.3
Net lending(+)/borrowing(-)	-4.4	-8.9	-6.8	-5.3	-4.4	-3.9	-2.5	-1.4	0.1	0.3
Non-resource net lending(+)/borrowing(-)	-5.9	-9.8	-7.9	-9.2	-8.0	-7.0	-5.8	-4.6	-3.1	-2.9
					(Percentage change)					
Money and credit										
Domestic credit	5.2	2.3	15.9	-0.6	10.4	12.3	7.2	4.5	4.8	16.9
Credit to the private sector	4.1	4.2	2.5	6.9	8.9	8.8	8.9	8.8	8.6	8.6
Broad money	4.4	7.0	13.4	14.7	0.6	5.5	3.2	7.8	7.7	8.8
					(In billions of U.S. dollars)					
Balance of payments										
Exports, f.o.b.	10.9	9.1	11.3	14.4	13.2	13.8	14.3	14.7	15.1	15.6
Imports, c.i.f.	-4.1	-3.7	-5.1	-4.2	-4.1	-4.2	-4.3	-4.5	-4.7	-4.9
Current account (including grants)	3.7	3.4	3.5	7.2	5.6	5.3	5.5	4.9	4.1	3.6
(In percent of GDP)	14.8	14.1	13.2	22.8	18.6	16.3	16.7	14.8	11.9	10.2
Gross official international reserves	2.3	2.7	3.2	4.0	3.4	3.1	3.1	3.5	3.6	2.8
(In months of goods and services imports)	5.2	4.5	6.3	8.0	6.7	6.0	5.8	6.3	6.3	4.7
					(In percent of GDP)					
Government debt										
Government gross debt	40.6	48.7	52.2	48.4	52.4	52.2	52.7	52.1	49.2	46.5
External debt-to-GDP ratio (in percent) 3/	17.1	21.8	24.8	23.6	26.4	29.7	32.4	33.6	32.5	29.2
External debt-service ratio (percent of exports)	1.2	5.4	4.1	2.1	2.7	3.4	4.5	5.4	5.6	8.9
Memo Items										
US$/kina (end-period)	0.2935	0.2850	0.2850	0.2840	…	…	…	…	…	…
NEER (2005=100, fourth quarter)	97.0	90.7	91.2	100.3	…	…	…	…	…	…
REER (2005=100, fourth quarter)	125.5	122.6	125.1	135.5	…	…	…	…	…	…
Terms of trade (2010=100, end-period)	59.4	57.4	49.4	68.2	62.3	62.1	62.7	63.2	63.4	63.6
Nominal GDP (in billions of kina)	83.8	82.5	92.3	111.0	112.2	122.9	130.4	137.0	144.3	153.5
Non-resource nominal GDP (in billions of kina)	60.1	62.5	69.8	77.1	84.0	91.4	99.0	107.1	115.8	125.2

Sources: Department of Treasury; Bank of Papua New Guinea; and IMF staff estimates and projections.
1/ Based on period average exchange rate.
2/ Resource sector includes production of mineral, petroleum, and gas and directly-related activities such as mining and quarrying, but excludes indirectly-related activities such as transportation and construction.
3/ Public external debt includes external debt of the central government, the central bank, and statutory authorities.

Table 2a. Papua New Guinea: Summary Operations of the Central Government, 2020-2028
(In millions of Kina)

	2020	2021	2022	2023		2024	2025	2026	2027	2028
				Prog. Approval	First Rev. Latest			Proj.		
Revenue and Grants	**12,093**	**13,860**	**18,538**	**19,582**	**20,403**	**22,168**	**24,066**	**25,708**	**28,026**	**30,119**
Taxes	9,802	11,129	16,454	14,900	16,321	17,850	19,866	21,328	23,165	24,934
Taxes on income, profits, and capital gains	5,669	6,356	11,253	8,935	10,699	11,721	13,154	13,983	15,200	16,586
of which: Personal income tax	3,517	3,468	3,652	3,518	3,917	4,621	5,195	5,638	6,123	6,723
of which: Company tax	1,554	1,690	2,757	2,395	3,008	3,696	4,113	4,546	5,202	5,744
Taxes on payroll and workforce	0	1	1	0	1	1	1	1	1	2
Taxes on goods and services	3,373	3,994	4,294	5,015	4,684	5,149	5,668	6,236	6,788	7,090
of which: GST	2,079	2,457	2,475	3,322	3,021	3,236	3,587	3,960	4,370	4,648
Taxes on international trade and transactions	760	779	906	949	937	979	1,043	1,108	1,176	1,257
Grants	1,425	2,088	1,472	2,025	2,025	2,075	1,825	1,875	2,075	2,116
Other Revenue	866	643	613	2,657	2,056	2,243	2,375	2,505	2,786	3,069
Resource revenue 1/	752	1,016	4,336	4,024	4,008	3,800	4,296	4,290	4,552	4,984
Mining and Petroleum Taxes	183	635	4,036	2,342	3,026	2,600	2,996	2,890	2,902	3,084
Mining and Petroleum and Gas Dividends	569	381	300	1,683	982	1,200	1,300	1,400	1,650	1,900
Non-resource revenue	11,341	12,845	14,202	15,558	16,395	18,368	19,770	21,418	23,474	25,135
Non-resource tax revenue	9,619	10,494	12,418	12,558	13,296	15,250	16,871	18,438	20,263	21,850
Expenditure	**19,398**	**20,131**	**24,390**	**24,567**	**25,338**	**26,979**	**27,369**	**27,684**	**27,894**	**29,658**
Expense	15,887	16,480	19,940	19,957	20,728	22,333	22,691	22,998	23,071	23,861
Compensation of employees	5,832	6,094	6,490	6,834	6,834	7,562	7,706	7,868	7,894	8,396
of which: Clearance of retirement arrears				300	300	200	100			
Use of goods and services	5,388	6,161	7,467	6,930	7,428	7,999	8,255	8,305	8,221	9,031
of which: Clearance of arrears				300	400	500	500	500	300	
Interest	2,160	2,249	2,573	2,496	2,769	3,022	3,051	3,246	3,457	2,712
Grants 2/	2,190	1,915	3,018	3,514	3,514	3,510	3,374	3,208	3,059	3,253
Social benefits 3/	218	0	0	114	114	165	225	287	352	374
Other expenses	99	61	393	69	69	76	80	84	89	94
Net acquisition of non-financial assets	3,511	3,650	4,450	4,610	4,610	4,645	4,679	4,685	4,823	5,798
Gross operating balance	-3,794	-2,620	-1,402	-375	-325	-165	1,375	2,710	4,955	6,259
Net lending (+)/borrowing (-)	**-7,305**	**-6,270**	**-5,852**	**-4,985**	**-4,935**	**-4,810**	**-3,303**	**-1,975**	**132**	**461**
Primary balance	-5,145	-4,021	-3,279	-2,489	-2,166	-1,788	-252	1,271	3,589	3,173
Non-resource net lending (+)/borrowing (-)	-8,056	-7,286	-10,188	-9,009	-8,943	-8,610	-7,599	-6,266	-4,420	-4,523
Non-resource primary balance	-5,896	-5,037	-7,615	-6,513	-6,174	-5,588	-4,547	-3,020	-963	-1,811
Net financial transactions 4/	**7,399**	**6,324**	**5,852**	**4,985**	**4,935**	**4,810**	**3,303**	**1,975**	**-132**	**-461**
Net acquisition of financial assets	-803	1,685	-356	0	0	0	0	0	0	0
Net incurrence of financial liabilities	6,596	8,009	5,496	4,985	4,935	4,810	3,303	1,975	-132	-461
Net domestic	2,882	3,096	2,277	1,492	1,442	874	-818	-319	95	5,103
Treasury bills	1,711	1,395	493	746	721	420	-384	-147	43	2,296
Treasury bonds	1,266	1,601	1,750	746	721	455	-434	-172	52	2,807
Other accounts payable	0	0	0	0	0	0	0	0	0	0
Net external	3,619	4,913	3,220	3,493	3,493	3,936	4,121	2,295	-228	-5,564
Debt securities	0	0	0	0	0	0	0	0	0	-2,176
IMF SDR allocation		1,244	0							
Loans	3,619	4,913	3,220	3,493	3,493	3,936	4,121	2,295	-228	-3,388
of which: net Fund financing	1,276	0	0	657	657	967	1,154	382	-302	-311
Rapid Credit Facility	*1,276*	*0*	*0*	*0*	*0*	*0*	*-141*	*-293*	*-302*	*-311*
Proposed ECF/EFF program				*657*	*657*	*967*	*1,294*	*675*		
Extended Fund Facility				*438*	*438*	*645*	*863*	*450*		
Extended Credit Facility				*219*	*219*	*322*	*432*	*225*		
Gross government debt	**40,168**	**48,173**	**53,680**	**57,333**	**58,787**	**64,168**	**68,700**	**71,352**	**71,059**	**71,399**
Domestic debt	22,216	25,258	27,534	27,800	29,122	27,630	26,458	25,279	24,139	26,509
Treasury bills	11,902	13,297	13,789	14,265	14,510	14,930	14,545	14,398	14,441	16,738
Treasury bonds	9,233	10,833	12,583	12,177	13,451	11,538	10,751	9,719	8,536	8,610
Loans	1,081	1,128	1,162	1,357	1,162	1,162	1,162	1,162	1,162	1,162
External debt	17,953	22,916	26,146	29,533	29,665	36,538	42,242	46,072	46,920	44,890
Debt securities	1,701	1,750	1,761	1,701	1,761	1,761	1,833	1,898	1,942	-176
Loans	16,252	21,166	24,385	27,832	27,904	34,777	40,409	44,175	44,978	45,066
Memorandum items:										
Contingent liabilities 5/	2,431	2,431	2,431	2,431	2,431	2,381	2,331	2,281	2,231	2,181
Future unfunded superannuation liabilities	2,431	2,431	2,431	2,431	2,431	2,381	2,331	2,281	2,231	2,181
SOE borrowing	0	0	0	0	0	0	0	0	0	0
Contingent liabilities, percentage of GDP	2.9	2.6	2.2	2.1	2.2	1.9	1.8	1.7	1.5	1.4

Sources: Department of Treasury; and IMF staff estimates and projections.

1/ Does not include projected revenues from new mining projects where the investment decision has not yet been reached.

2/ Grants include spending on wages and salaries, goods and services, and capital expenditure executed by provincial and local governments.

3/ Refers to direct social assistance. For the program, the indicative target on social spending is more expansive, covering current and capital spending in the identified sectors (see Technical Memorandum of Understanding accompanying the program request).

4/ Discrepancies between the overall balance and financing may arise because of data coverage gaps in revenue and expenditure for extrabudgetary units, and payment arrears and cash withdrawals from trust accounts which are not fully accounted for due to data weaknesses.

5/ Contingent liabilities include future unfunded superannuation liabilities with Nambawan Super and SOE borrowing.

Table 2b. Papua New Guinea: Summary Operations of the Central Government, 2020-2028
(In percent of GDP)

	2020	2021	2022	2023		2024	2025	2026	2027	2028
				Prog. Approval	First Rev. Latest			Proj.		
Revenue and Grants	**14.7**	**15.0**	**16.7**	**17.1**	**18.2**	**18.0**	**18.5**	**18.8**	**19.4**	**19.6**
Taxes	11.9	12.1	14.8	13.0	14.5	14.5	15.2	15.6	16.0	16.2
Taxes on income, profits, and capital gains	6.9	6.9	10.1	7.8	9.5	9.5	10.1	10.2	10.5	10.8
of which: Personal income tax	4.3	3.8	3.3	3.1	3.5	3.8	4.0	4.1	4.2	4.4
of which: Company tax	1.9	1.8	2.5	2.1	2.7	3.0	3.2	3.3	3.6	3.7
Taxes on payroll and workforce	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Taxes on goods and services	4.1	4.3	3.9	4.4	4.2	4.2	4.3	4.6	4.7	4.6
of which: GST	2.5	2.7	2.2	2.9	2.7	2.6	2.8	2.9	3.0	3.0
Taxes on international trade and transactions	0.9	0.8	0.8	0.8	0.8	0.8	0.8	0.8	0.8	0.8
Grants	1.7	2.3	1.3	1.8	1.8	1.7	1.4	1.4	1.4	1.4
Other Revenue	1.0	0.7	0.6	2.3	1.8	1.8	1.8	1.8	1.9	2.0
Resource revenue 1/	0.9	1.1	3.9	3.5	3.6	3.1	3.3	3.1	3.2	3.2
Mining and Petroleum Taxes	0.2	0.7	3.6	2.0	2.7	2.1	2.3	2.1	2.0	2.0
Mining and Petroleum and Gas Dividends	0.7	0.4	0.3	1.5	0.9	1.0	1.0	1.0	1.1	1.2
Non-resource revenue	13.7	13.9	12.8	13.5	14.6	14.9	15.2	15.6	16.3	16.4
Non-resource tax revenue	11.7	11.4	11.2	10.9	11.8	12.4	12.9	13.5	14.0	14.2
(in percent of non-resource GDP)	*15.4*	*13.6*	*16.1*	*15.2*	*15.8*	*16.7*	*17.0*	*17.2*	*17.5*	*17.4*
Expenditure	**23.5**	**21.8**	**22.0**	**21.4**	**22.6**	**22.0**	**21.0**	**20.2**	**19.3**	**19.3**
Expense	19.3	17.9	18.0	17.4	18.5	18.2	17.4	16.8	16.0	15.5
Compensation of employees	7.1	6.6	5.8	6.0	6.1	6.2	5.9	5.7	5.5	5.5
of which: Clearance of retirement arrears				0.3	0.3	0.2	0.1			
Use of goods and services	6.5	6.7	6.7	6.0	6.6	6.5	6.3	6.1	5.7	5.9
of which: Clearance of arrears				0.3	0.4	0.4	0.4	0.4	0.2	
Interest	2.6	2.4	2.3	2.2	2.5	2.5	2.3	2.4	2.4	1.8
Grants 2/	2.7	2.1	2.7	3.1	3.1	2.9	2.6	2.3	2.1	2.1
Social benefits 3/	0.3	0.0	0.0	0.1	0.1	0.1	0.2	0.2	0.2	0.2
Other expenses	0.1	0.1	0.4	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Net acquisition of non-financial assets	4.3	4.0	4.0	4.0	4.1	3.8	3.6	3.4	3.3	3.8
Gross operating balance	-4.6	-2.8	-1.3	-0.3	-0.3	-0.1	1.1	2.0	3.4	4.1
Net lending (+)/borrowing (-)	**-8.9**	**-6.8**	**-5.3**	**-4.3**	**-4.4**	**-3.9**	**-2.5**	**-1.4**	**0.1**	**0.3**
Primary balance	-6.2	-4.4	-3.0	-2.2	-1.9	-1.5	-0.2	0.9	2.5	2.1
Non-resource net lending (+)/borrowing (-)	-9.8	-7.9	-9.2	-7.8	-8.0	-7.0	-5.8	-4.6	-3.1	-2.9
Non-resource primary balance	-7.1	-5.5	-6.9	-5.7	-5.5	-4.5	-3.5	-2.2	-0.7	-1.2
Net financial transactions 4/	**9.0**	**6.8**	**5.3**	**4.3**	**4.4**	**3.9**	**2.5**	**1.4**	**-0.1**	**-0.3**
Net acquisition of financial assets	-1.0	1.8	-0.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net incurrence of financial liabilities	8.0	8.7	5.0	4.3	4.4	3.9	2.5	1.4	-0.1	-0.3
Domestic	3.5	3.4	2.1	1.3	1.3	0.7	-0.6	-0.2	0.1	3.3
Treasury bills	2.1	1.5	0.4	0.6	0.6	0.3	-0.3	-0.1	0.0	1.5
Treasury bonds	1.5	1.7	1.6	0.6	0.6	0.4	-0.3	-0.1	0.0	1.8
Loans	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
External	4.4	5.3	2.9	3.0	3.1	3.2	3.2	1.7	-0.2	-3.6
Debt securities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	-1.4
IMF SDR allocation		1.3	0.0							
Loans	4.4	5.3	2.9	3.0	3.1	3.2	3.2	1.7	-0.2	-2.2
of which net Fund financing	1.5	0.0	0.0	0.6	0.6	0.8	0.9	0.3	-0.2	-0.2
Rapid Credit Facility	*1.5*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	*-0.1*	*-0.2*	*-0.2*	*-0.2*
Proposed ECF/EFF program	*0.0*	*0.0*	*0.0*	*0.6*	*0.6*	*0.8*	*1.0*	*0.5*		
Extended Fund Facility	*0.0*	*0.0*	*0.0*	*0.4*	*0.4*	*0.5*	*0.7*	*0.3*		
Extended Credit Facility	*0.0*	*0.0*	*0.0*	*0.2*	*0.2*	*0.3*	*0.3*	*0.2*		
Gross government debt	**48.7**	**52.2**	**48.4**	**49.9**	**52.4**	**52.2**	**52.7**	**52.1**	**49.2**	**46.5**
Domestic debt	26.9	27.4	24.8	24.2	25.9	22.5	20.3	18.4	16.7	17.3
Treasury bills	14.4	14.4	12.4	12.4	12.9	12.2	11.2	10.5	10.0	10.9
Treasury bonds	11.2	11.7	11.3	10.6	12.0	9.4	8.2	7.1	5.9	5.6
External debt	21.8	24.8	23.6	25.7	26.4	29.7	32.4	33.6	32.5	29.2
Debt securities	2.1	1.9	1.6	1.5	1.6	1.4	1.4	1.4	1.3	-0.1
Loans	19.7	22.9	22.0	24.2	24.9	28.3	31.0	32.2	31.2	29.4
Memorandum items:										
Contingent liabilities 5/	2.9	2.6	2.2	2.1	2.2	1.9	1.8	1.7	1.5	1.4
Future unfunded superannuation liabilities	2.9	2.6	2.2	2.1	2.2	1.9	1.8	1.7	1.5	1.4
SOE borrowing	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0

Sources: Department of Treasury; and IMF staff estimates and projections.

1/ Does not include projected revenues from new mining projects where the investment decision has not yet been reached.

2/ Grants include spending on wages and salaries, goods and services, and capital expenditure executed by provincial and local governments.

3/ Refers to direct social assistance. For the program, the indicative target on social spending is more expansive, covering current and capital spending in the identified sectors (see Technical Memorandum of Understanding accompanying the program request).

4/ Discrepancies between the overall balance and financing may arise because of data coverage gaps in revenue and expenditure for extrabudgetary units, and payment arrears and cash withdrawals from trust accounts which are not fully accounted for due to data weaknesses.

5/ Contingent liabilities include future unfunded superannuation liabilities with Nambawan Super and SOE borrowing.

Table 3. Papua New Guinea: Balance of Payments, 2019-2028

(In millions of U.S. dollars)

	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028
				Est.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
Current account balance	**3,655**	**3,353**	**3,466**	**7,175**	**5,614**	**5,275**	**5,497**	**4,919**	**4,067**	**3,611**
Trade balance	6,821	5,418	6,132	10,153	9,053	9,652	9,971	10,219	10,437	10,690
Exports (f.o.b.)	10,947	9,073	11,269	14,369	13,172	13,806	14,315	14,729	15,128	15,605
Resource	9,141	7,232	9,154	12,264	11,376	11,861	12,260	12,578	12,869	13,213
Nonresource	1,806	1,840	2,115	2,105	1,796	1,945	2,055	2,152	2,258	2,392
Imports (f.o.b.)	-4,126	-3,655	-5,137	-4,216	-4,119	-4,153	-4,344	-4,510	-4,690	-4,914
Resource	-1,070	-1,115	-1,120	-1,135	-1,081	-1,060	-1,109	-1,152	-1,198	-1,255
Nonresource	-3,057	-2,539	-4,016	-3,081	-3,037	-3,093	-3,235	-3,358	-3,493	-3,659
Services	-1,815	-1,592	-1,844	-1,829	-1,732	-1,721	-1,721	-1,721	-1,721	-1,721
Income	-1,737	-744	-1,125	-1,388	-2,001	-2,950	-3,046	-3,873	-4,942	-5,652
Current Transfers	387	271	302	239	294	293	293	293	293	293
Official	435	331	460	396	392	390	390	390	390	390
Private	-48	-60	-158	-158	-98	-97	-97	-97	-97	-97
Capital and financial account balance (+ = inflow)	**-2,757**	**-1,726**	**-5,356**	**-10,488**	**-6,674**	**-6,131**	**-6,191**	**-4,831**	**-3,813**	**-4,300**
Capital account balance	6	6	6	8	8	8	8	8	8	8
Financial account balance	-2,764	-1,732	-5,362	-10,496	-6,682	-6,139	-6,199	-4,839	-3,821	-4,308
Direct investment	-876	-879	-1,702	-1,787	-487	-765	-768	-770	-769	-766
Portfolio investment	20	-73	31	-206	-23	-78	-79	-79	-79	-579
Other investment	-1,908	-780	-3,691	-8,503	-6,172	-5,296	-5,352	-3,991	-2,973	-2,964
Loans (Net)	103	475	-410	530	713	816	1,013	535	-77	-802
Official[1]	617	955	204	719	924	1,022	1,039	557	-54	-778
Private	-515	-481	-614	-189	-211	-206	-26	-23	-23	-24
Commercial banks	-93	16	-229	-814	862	602	403	-199	-199	752
Other private capital flows[2]	-1,918	-1,270	-3,052	-8,219	-7,748	-6,714	-6,768	-4,326	-2,698	-2,913
Net errors and omissions	-801	-2014	2107	4149	0	0	0	0	0	0
Overall balance	**97**	**-387**	**217**	**836**	**-1,060**	**-857**	**-694**	**88**	**255**	**-690**
Financing	**-97**	**387**	**-217**	**-836**	**1,060**	**857**	**694**	**-88**	**-255**	**690**
Change in net reserve assets (+=fall in reserves)	-97	9	-217	-836	884	602	403	-199	-199	752
Use of IMF credit	0	378	0	0	176	255	292	111	-56	-62
Purchases	0	378	0	0	176	255	327	164	0	0
Repurchases	0	0	0	0	0	0	-36	-53	-56	-62
Memorandum items:	-2,135	9	-217	-836	884	602	403	-199	-199	752
Current account (in percent of GDP)	14.8	14.1	13.2	22.8	18.6	16.3	16.7	14.8	11.9	10.2
Net international reserves (end-year, millions of U.S. dollars)	2,135	2,126	2,343	3,179	2,295	1,692	1,290	1,489	1,687	935
Net international reserves as per TMU definition (prog. monitoring)	..	..	..	..	2,650	2,050	1,800	2,000	2,200	1,450
Gross international reserves (end-year, millions of U.S. dollars)	2,309	2,686	3,240	4,032	3,382	3,122	3,116	3,467	3,592	2,759
In months of nonmineral sector imports	10.9	5.8	8.2	10.5	8.7	7.8	7.6	8.2	8.3	6.1
In months of imports of goods and services	5.2	4.5	6.3	8.0	6.7	6.0	5.8	6.3	6.3	4.7
Public external debt service-to-exports ratio[3] (in percent)	1.2	5.4	4.1	2.1	2.7	3.4	4.5	5.4	5.6	8.9
Public external debt-GDP ratio[3] (in percent)	17.1	21.8	24.8	23.6	26.4	29.7	32.4	33.6	32.5	29.2
Nominal GDP	24,751	23,848	26,312	31,533	30,104	32,268	32,869	33,273	34,044	35,269
Resource exports (in percent of GDP)	37	30	35	39	38	37	37	38	38	37

Sources: Bank of Papua New Guinea; and IMF staff estimates and projections.

1/ Excludes IMF.

2/ Includes money-transfer via offshore accounts.

3/ Public external debt includes external debt of the central government, the central bank, and statutory authorities.

Table 4. Papua New Guinea: Monetary Developments, 2019-2024

	2019	2020	2021	2022	2023	2024
				Est.	Proj.	Proj.
Bank of Papua New Guinea			**(In millions of kina; end of period)**			
Net foreign assets	7,255	7,417	8,221	11,116	8,558	6,580
Foreign assets	7,867	9,424	11,369	14,197	12,616	12,142
Foreign liabilities	612	2,007	3,148	3,081	4,057	5,562
Net domestic assets	-1,340	-1,370	-1,519	-2,437	-1,640	708
Domestic credit	1,315	-918	1,009	-592	851	1,904
Net credit to government	1,251	-1,003	934	-743	799	1,852
Claims on the government	2,312	1,615	3,581	3,383	3,799	3,852
Of which: Advances and holdings of inscribed stock and securities	2,312	1,615	2,319	2,051	2,400	2,400
Loans: IMF SDR Allocation			1,260	1,330	1,399	1,452
Central government deposits	1,061	2,619	2,648	4,126	3,000	2,000
Credit to other sectors	64	86	75	151	51	51
Other items, net	-2,655	-453	-2,528	-1,845	-2,490	-1,195
Of which: Central bank securities	-1,778	-1,498	-3,040	-2,655	-5,245	-5,516
Of which: IMF credit		1,330	1,293	1,233	2,290	3,856
Reserve money	5,915	6,046	6,702	8,679	6,918	7,289
Currency in circulation	2,300	2,434	2,666	2,970	3,003	3,287
Deposits of other depository corporations	3,615	3,612	4,036	5,709	3,915	4,001
Required reserves	2,090	1,575	1,794	2,910	2,941	3,123
Excess reserves	1,525	2,037	2,242	2,800	974	878
Other deposits	0	0	0	0	0	0
Depository Corporations Survey			**(In millions of kina; end of period)**			
Net foreign assets	7,666	7,831	8,678	12,038	9,490	7,601
Net domestic assets	14,652	16,049	18,409	19,023	21,767	25,362
Domestic credit	22,477	22,990	26,636	26,481	29,225	32,821
Net credit to central government	7,150	7,451	11,262	10,472	11,933	14,140
Claims on other sectors	15,327	15,539	15,374	16,009	17,292	18,681
Claims on the private sector	12,238	12,754	13,076	13,973	15,216	16,563
Other items, net	-7,825	-6,941	-8,227	-7,458	-7,458	-7,458
Broad money	22,318	23,880	27,087	31,060	31,257	32,963
Narrow money	17,125	18,916	22,107	26,032	26,429	28,329
Currency outside other depository corporations	1,656	1,890	2,152	2,363	2,268	2,177
Demand deposits	15,469	17,026	19,955	23,669	24,161	26,152
Quasi-money	5,193	4,964	4,980	5,029	4,828	4,635
Securities other than shares	0	0	0	0	0	0
			(Annual percentage change)			
Net foreign assets	9.2	2.1	10.8	38.7	-21.2	-19.9
Net domestic assets	2.1	9.5	14.7	3.3	14.4	16.5
Net domestic credit	5.2	2.3	15.9	-0.6	10.4	12.3
Of which: Private sector	4.1	4.2	2.5	6.9	8.9	8.8
Broad money	4.4	7.0	13.4	14.7	0.6	5.5
Memorandum items:						
Reserve money (percentage change)	12.4	2.2	10.8	29.5	-20.3	5.4
Gross international reserves (in millions of U.S. dollars)	2,309	2,686	3,240	4,032	3,382	3,122
Nominal nonresource GDP/Broad money	2.7	2.6	2.6	2.5	2.7	2.8

Sources: Bank of Papua New Guinea; and IMF staff estimates and projections.

Table 5. Papua New Guinea: Financial Soundness Indicators, 2017-2023 1/
(In percent)

	2017	2018	2019	2020	2021	2022	2023 end-June
Capital Adequacy							
Capital to risk-weighted assets 1/	38.1	37.1	36.1	39.2	41.1	30.4	36.4
Tier 1 capital to risk-weighted assets	30.8	29.6	28.2	31.9	32.5	21.9	31.1
Asset Quality							
Nonperforming loans to total loans	2.8	3.7	3.8	5.3	6.2	4.8	5.4
Provisions to nonperforming loans	49.4	47.0	55.8	44.2	47.3	39.6	46.0
Earnings and Profitability							
Return on assets	3.4	3.8	4.1	3.8	4.4	3.9	1.8
Return on equity	12.1	12.7	14.4	13.1	15.2	20.1	4.5
Liquidity							
Liquid assets to total assets	16.9	15.9	17.7	18.3	18.9	22.5	20.5
Loan-to-deposit ratio	65.8	71.4	71.3	65.8	59.8	55.6	59.1
Other							
Tier 1 Capital to total assets	14.2	14.5	14.0	14.9	13.5	8.5	13.5
Risk-weighted assets to total assets	46.6	49.3	50.8	48.5	43.8	38.9	43.6

Sources: Bank of Papua New Guinea; and IMF staff calculations.
1/ Capital base includes Tier 1 and Tier 2 capital.

Table 6. Papua New Guinea: Schedule of Disbursements and Purchases under the ECF-EFF Arrangements[1]

Availability date	Amount (SDR Million)			Percent of Quota			Conditions for disbursement/purchases
	Total	ECF	EFF	Total	ECF	EFF	
22 March 2023	65.81	21.94	43.87	25.0	8.3	16.7	Executive Board approval of the ECF/EFF arrangements.
18 September 2023	65.81	21.94	43.87	25.0	8.3	16.7	Observance of end-June 2023 performance criteria, and completion of the first review under the arrangements.
18 March 2024	94.75	31.58	63.17	36.0	12.0	24.0	Observance of end-December 2023 performance criteria, and completion of the second review under the arrangements.
18 September 2024	94.75	31.58	63.17	36.0	12.0	24.0	Observance of end-June 2024 performance criteria, and completion of the third review under the arrangements.
18 March 2025	121.07	40.36	80.71	46.0	15.3	30.7	Observance of end-December 2024 performance criteria, and completion of the fourth review under the arrangements.
18 September 2025	121.07	40.36	80.71	46.0	15.3	30.7	Observance of end-June 2025 performance criteria, and completion of the fifth review under the arrangements.
18 March 2026	121.06	40.35	80.71	46.0	15.3	30.7	Observance of end-December 2025 performance criteria, and completion of the sixth review under the arrangements.
Total	**684.32**	**228.11**	**456.21**	**260.0**	**86.7**	**173.3**	

Source: IMF Staff Estimates

1/Papua New Guinea's quota is 263.2 million SDR.

Table 7. Papua New Guinea: External Financing Requirements and Sources, 2019-2028
(In millions of U.S. dollars)

	2019	2020	2021	2022 Est.	2023 Proj.	2024 Proj.	2025 Proj.	2026 Proj.	2027 Proj.	2028 Proj.
Total financing requirements	**-2640**	**-979**	**-5014**	**-10245**	**-6233**	**-5563**	**-5425**	**-4101**	**-3214**	**-3150**
Current account deficit	-3655	-3353	-3466	-7175	-5614	-5275	-5497	-4919	-4067	-3611
Public sector loan amortization	117	369	342	242	260	308	443	562	599	1156
Interest and amortization on existing IMF loans	0	0	0	1	6	6	31	57	56	55
Reserve accumulation (-=fall in reserves)	97	-9	217	836	-884	-602	-403	199	199	-752
Errors and omissions	801	2014	-2107	-4149	0	0	0	0	0	0
Financing sources	**-2660**	**-2435**	**-6016**	**-11046**	**-6895**	**-6422**	**-6068**	**-4489**	**-3214**	**-3150**
Capital account balance	6	6	6	8	8	8	8	8	8	8
Net foreign direct investments	-876	-879	-1702	-1787	-487	-765	-768	-770	-769	-766
Net portfolio investments	20	-73	31	-206	-23	-78	-79	-79	-79	-579
Public sector project loan disbursements	715	247	-456	161	703	731	1162	899	545	371
Other capital inflows (net)	-2525	-1736	-3895	-9222	-7096	-6318	-6391	-4548	-2919	-2186
Financing gap	**20**	**1456**	**1002**	**801**	**662**	**859**	**644**	**388**	**0**	**0**
Bilateral budget support[1]	0	558	732	531	386	508	224	224	0	0
Multilateral budget support[1] (excl. IMF)	20	520	270	270	100	96	92	0	0	0
IMF financing	0	378	0	0	176	255	327	164	0	0
RCF	0	378	0	0	0	0	0	0	0	0
EFF	0	0	0	0	117	170	218	109	0	0
ECF	0	0	0	0	59	85	109	55	0	0
Unidentified financing	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**
Memorandum items:										
Annual IMF financing (percent of quota)		100%	0%	0%	50%	72%	92%	46%	0%	0%
Cumulative IMF financing (percent of quota)		100%	100%	100%	150%	222%	304%	330%	309%	280%
IMF share of financing gap (percent)		26%	0%	0%	27%	30%	51%	42%	..	..

Sources: Papua New Guinea authorities and Fund staff estimates.

1/Includes loans and grants

Table 8. Papua New Guinea: Indicators of Capacity to Repay the IMF, 2023-2036[1]

	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034	2035	2036
IMF obligations based on existing credit (millions of SDRs)														
Principal	0.0	0.0	26.3	52.6	56.3	62.2	64.3	38.0	11.7	11.7	5.9	0.0	0.0	0.0
Charges and interest	4.4	17.4	17.4	17.4	17.4	17.1	16.7	16.3	16.0	15.6	15.2	15.2	15.2	15.2
Total obligations based on existing and prospective credit														
Principal														
Millions of SDRs	0.0	0.0	26.3	52.6	56.3	74.7	107.0	121.1	117.6	121.7	115.8	89.8	53.8	10.8
Millions of Kina	0.0	0.0	140.7	293.4	323.6	429.4	614.8	695.8	676.0	699.2	665.6	516.3	309.3	61.8
Percent of government revenue	0.0	0.0	0.6	1.2	1.2	1.5	2.1	2.2	2.0	2.0	1.8	1.3	0.7	0.1
Percent of exports of goods and services	0.0	0.0	0.2	0.5	0.5	0.6	0.9	0.9	0.9	0.9	0.8	0.6	0.4	0.1
Percent of GDP	0.0	0.0	0.1	0.2	0.2	0.3	0.4	0.4	0.4	0.4	0.3	0.2	0.1	0.0
Percent of quota	0.0	0.0	10.0	20.0	21.4	28.4	40.6	46.0	44.7	46.2	44.0	34.1	20.4	4.1
Charges and interest														
Millions of SDRs	4.6	22.5	29.9	37.2	38.3	37.9	36.5	33.8	30.1	26.3	22.4	19.0	16.5	15.3
Millions of Kina	22.9	114.7	159.8	207.3	220.2	217.9	209.7	194.5	173.1	150.9	128.7	109.0	94.8	88.0
Outstanding IMF credit														
Millions of SDRs	394.8	584.3	800.1	868.6	812.3	737.6	630.6	509.5	391.9	270.2	154.4	64.6	10.8	0.0
Millions of Kina	1972.0	2982.4	4277.3	4840.6	4668.3	4238.9	3624.1	2928.2	2252.2	1553.0	887.4	371.1	61.8	0.0
Percent of government revenue	10.7	14.8	19.2	20.3	18.0	15.1	12.3	9.4	6.8	4.4	2.4	0.9	0.1	0.0
Percent of exports of goods and services	4.0	5.6	7.4	7.9	7.2	6.2	5.1	4.0	3.0	2.0	1.1	0.4	0.1	0.0
Percent of GDP	1.8	2.4	3.3	3.5	3.2	2.8	2.2	1.7	1.2	0.8	0.4	0.2	0.0	0.0
Percent of quota	150.0	222.0	304.0	330.0	308.6	280.2	239.6	193.6	148.9	102.7	58.7	24.5	4.1	0.0
Percent of gross international reserves	15.6	24.6	33.9	33.3	30.3	34.8	31.1	24.5	17.1	10.3	5.6	2.1	0.3	0.0
Net use of IMF credit (millions of SDRs)														
Disbursements (including prospective ones)	131.6	189.5	242.1	121.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Repayments and repurchases	0.0	0.0	26.3	52.6	56.3	74.7	107.0	121.1	117.6	121.7	115.8	89.8	53.8	10.8
Memorandum items:														
Nominal GDP (billions of Kina)	112.2	122.9	130.4	137.0	144.3	153.5	162.5	172.3	183.4	195.6	209.0	222.9	238.1	254.6
Exports of goods and services (billions of Kina)	49.9	53.3	57.6	61.5	65.0	68.8	71.1	73.5	76.0	78.5	81.2	83.9	86.8	89.8
Government revenue (billions of Kina)	18.4	20.1	22.2	23.8	26.0	28.0	29.5	31.2	33.0	35.0	37.2	39.5	42.0	44.7
Kina / SDR (period average)	5.0	5.1	5.3	5.6	5.7	5.7	5.7	5.7	5.7	5.7	5.7	5.7	5.7	5.7
Quota (millions of SDRs)	263.2	263.2	263.2	263.2	263.2	263.2	263.2	263.2	263.2	263.2	263.2	263.2	263.2	263.2

Source: IMF Staff estimates and projections.

1/Data are projections.

Table 9a. Papua New Guinea: Summary Table of Projected External Borrowing Program January 1, 2023 to December 31, 2023[1]

PPG external debt	Volume of new debt in 2023		PV of new debt in 2023 (program purposes)		PV of new debt in 2023 (including negative GEs)	
	USD million	Percent	USD million	Percent	USD million	Percent
By sources of debt financing	**1130.9**	**100**	**943.0**	**100**	**946.9**	**100**
Concessional debt, of which	**116.6**	**10**	**71.3**	**8**	**71.3**	**8**
Multilateral debt	116.6	10	71.3	8	71.3	8
Bilateral debt	0.0	0	0.0	0	0.0	0
Other	0.0	0	0.0	0	0.0	0
Non-concessional debt, of which	**1014.4**	**90**	**871.7**	**92**	**875.6**	**92**
Semi-concessional	949.0	84	806.4	86	806.4	85
Commercial terms	65.3	6	65.3	7	69.2	7
By Creditor Type	**1130.9**	**100**	**943.0**	**100**	**946.9**	**100**
Multilateral	331.6	29	241.6	26	241.6	26
Bilateral - Paris Club	465.3	41	433.7	46	437.5	46
Bilateral - Non-Paris Club	237.6	21	173.5	18	173.5	18
Other	96.4	9	94.2	10	94.2	10
Uses of debt financing	**1130.9**	**100**	**943.0**	**100**	**946.9**	**100**
Infrastructure	525.1	46	432.1	46	436.0	46
Social Spending	105.9	9	76.4	8	76.4	8
Budget Financing	500.0	44	434.4	46	434.4	46
Other	0.0	0.0	0.0	0.0	0.0	0.0
Memo Items						
Indicative projections						
Year 2	**1263.0**		**1073.6**		**1114.5**	
Year 3	**272.4**		**231.6**		**231.6**	

[1] Present value calculations for January 1, 2023-December 31, 2023 period.

Table 9b. Papua New Guinea: Summary Table of Projected External Borrowing Program January 1, 2024 to December 31, 2024[1]

PPG external debt	Volume of new debt in 2024		PV of new debt in 2024 (program purposes)		PV of new debt in 2024 (including negative GEs)	
	USD million	Percent	USD million	Percent	USD million	Percent
By sources of debt financing	**1263.0**	**100**	**1071.9**	**100**	**1101.3**	**100**
Concessional debt, of which	**100.0**	**8**	**59.7**	**6**	**59.7**	**5**
Multilateral debt	100.0	8	59.7	6	59.7	5
Bilateral debt	0.0	0	0.0	0	0.0	0
Other	0.0	0	0.0	0	0.0	0
Non-concessional debt, of which	**1163.0**	**92**	**1012.2**	**94**	**1041.6**	**95**
Semi-concessional	831.1	66	680.3	63	680.3	62
Commercial terms	331.9	26	331.9	31	361.3	33
By Creditor Type	**1263.0**	**100**	**1071.9**	**100**	**1101.3**	**100**
Multilateral	322.8	26	217.4	20	217.4	20
Bilateral - Paris Club	890.2	70	816.6	76	846.0	77
Bilateral - Non-Paris Club	50.0	4	37.9	4	37.9	3
Other	0.0	0	0.0	0	0.0	0
Uses of debt financing	**1263.0**	**100**	**1071.9**	**100**	**1101.3**	**100**
Infrastructure	852.7	68	720.0	67	749.4	68
Social Spending	0.0	0	0.0	0	0.0	0
Budget Financing	410.3	32	351.9	33	351.9	32
Other	0.0	0.0	0.0	0.0	0.0	0.0
Memo Items						
Indicative projections						
Year 2	**272.4**		**231.6**		**231.6**	
Year 3	**203.4**		**168.1**		**168.1**	

[1] Present value calculations for January 1, 2024-December 31, 2024 period.

Table 10. Papua New Guinea: Quantitative Performance Criteria and Indicative Targets for 2023 and 2024
(In million kina unless otherwise specified)

	2022	2023							2024				
	December	March		June		September	December		March		June	September	December
		Indicative target		Test date		Indicative target	Test date		Indicative target		Test date	Indicative target	Test date
	Est.	Approved	**Outcome**	Approved	**Outcome**	Approved	Approved	**Proposed revision**	Approved	**Proposed revision**	Proposed	Proposed	Proposed
A. Quantitative performance criteria[1]													
Fiscal deficit of the government[2] (ceiling, cumulative from the beginning of the year)	5,985	1,646	**449**	3,092	**2,858**	4,239	4,985	**4,935**	1,586	**1,586**	3,014	4,132	4,810
Stock of net international reserves of the BPNG (floor, US$ millions)[3]	3,226	2,845	**2,996**	2,463	**2,831**	2,082	1,700	**2,650**	1,525	**2,500**	2,350	2,200	2,050
BPNG's gross credit to government (ceiling)	2,051	2,400	**1,913**	2,400	**2,032**	2,400	2,400	**2,400**	2,400	**2,400**	2,400	2,400	2,400
B. Continuous quantitative performance criteria (ceilings)[4]													
New external payment arrears of the government (ceiling, US$ millions)	0	0	**0**	0	**0**	0	0	**0**	0	**0**	0	0	0
Present value of new external debt contracted or guaranteed by the government[5] (ceiling, US$ millions)	-	1,405	**0**	1,405	**60**	1,405	1,405	**943**	-	**1,072**	1,072	1,072	1,072
C. Indicative Targets													
Non-resource tax revenue of the government (floor, cumulative from the beginning of the year)	10,831	2,512	**2,787**	5,023	**5,900**	9,167	12,558	**12,741**	2,807	**2,935**	5,871	10,714	14,677
New domestic payment arrears of the government (ceiling)[6]							0	**0**	0	**0**	0	0	0
Social and other priority spending (floor, cumulative from the beginning of the year)[7]	3,678	500	**998**	1,500	**2,069**	2,817	3,866	**3,866**	500	**525**	1,575	2,958	4,059
BPNG provision of foreign exchange to authorized FX dealers (floor, cumulative from the beginning of the year, US$ millions)	878	300	**300**	600	**773**	900	1,200	**1,200**					
Stock of unmet import-related FX orders (ceiling)										**150**	125	100	75

Sources: Papua New Guinea authorities and Fund staff estimates.

[1] Quantitative performance criteria listed under A. and indicative targets listed under C. are assessed as at the end of each reference month above.

[2] Central government until September 2023, Budgetary Central Government from December 2023 - see Technical Memorandum of Understanding for full definition.

[3] In the proposed revisions for end-December 2023 and end-March 2024 targets, as well as the proposed targets for the rest of 2024, the SDR allocation is no longer subtracted in the calculation, in line with the IMF safeguards assessment.

[4] Quantitative performance criteria listed under B. are effective continuously from program approval.

[5] Annual for 2023 and 2024.

[6] Due to an absence of definition in the previous Technical Memorandum of Understanding, this indicative target is measured from December 2023 onwards.

[7] Comprises government spending on health, education and law and order (both capital and operating expenses).

Table 11. Papua New Guinea: Structural Benchmarks (March 2023—October 2024)

Measure	Purpose/Macro-criticality	Implementation date	Status of implementation
Budget repair			
Complete HR Business Process workshops on staffing and remuneration guidelines with government departments accounting for the majority of government staff.	To ensure government departments are aware of HR rules on staffing and remuneration to strengthen compliance, avoid overspending and prevent payment arrears.	End-June 2023	Met.
Adopt a new Medium-term Revenue Strategy (MTRS), in consultation with Fund staff, based on technical assistance requested. The MTRS will be adopted once it has been endorsed by the National Executive Council.	To guide revenue administration reforms.	End-August 2023	Not met. *(implemented with delay in October 2023)*
Introduce amendments to the Income Tax Act to the Parliament aimed at strengthening revenue mobilization, streamlining its operation and ensuring consistency with the Tax Administration Act.	To strengthen domestic revenue mobilization.	End-December 2023	In progress.
Develop an initial worksheet of output-based key performance indicators to be applied at IRC's individual, team and division levels.	To enhance revenue administration and increase IRC's organizational productivity.	End-May 2024	Newly proposed.
Complete data cleansing over current payroll records in the AscenderPay IT system and produce a report on the outcome of the cleansing exercise, shared with the IMF.	To ensure integrity of payroll information and enhance payroll management.	End-August 2024	Newly proposed.
Submit to the Parliament amendments to the Internal Revenue Commission Act 2014, in consultation with the IMF, to establish a Board for IRC's oversight.	To strengthen IRC's governance.	End-October 2024	Newly proposed.
Governance and operations of the BPNG			
Modify the open market operations framework by introducing a fixed rate tender with full allotment to sterilize excess liquidity more effectively.	To address excess liquidity in the banking system, improve monetary policy effectiveness and strengthen the monetary policy transmission.	End-August 2023	Met.
Produce a sequenced roadmap with a concrete action plan and a timeline for (i) reforming monetary policy operations frameworks, and (ii) reforming exchange rate operations and regulations, in consultation with Fund staff.	To improve monetary policy effectiveness, reduce FX shortages and move towards a more flexible exchange rate.	End-August 2023	Met.
Set the parameters for the framework of the crawl-like exchange rate arrangement to be implemented starting in early December 2023: (i) anchor currency; (ii) modalities for the calculation of the rate of crawl; (iii) width of the crawl band; (iv) pace of regular reviews/updates; (v) strategy for communication of the arrangement to the market; (vi) modalities for FX interventions to support the arrangement.	To prepare the shift to a crawl-like exchange rate arrangement and enable the gradual return to kina convertibility by the end of the program.	End-November 2023	Newly proposed.
Appoint the Governor and Deputy Governors of the BPNG and fill out all vacancies at the BPNG Board.	To ensure sound governance of the BPNG and facilitate implementation of the roadmap.	End-November 2023	Newly proposed.
Submit to the Parliament amendments to the CBA, in consultation with Fund staff, to address the remaining issues related to mandate, governance, autonomy, transparency, and accountability of BPNG and improvements in financial regulation and supervision.	To strengthen BPNG's financial independence and governance and improve the operation of the financial system.	End-December 2023	In progress.

Table 11. Papua New Guinea: Structural Benchmarks (Concluded) (March 2023—October 2024)			
Measure	**Purpose/Macro-criticality**	**Implementation date**	**Status of implementation**
Publish all regulations and directives regarding the FX market on BPNG's website.	To increase transparency and level the playing field in the FX market.	End-December 2023	Newly proposed.
Eliminate BPNG's requirement of a tax clearance certificate to include FX orders related to intercompany loans obtained for import payments in the orderbook.	To increase transparency and level the playing field in the FX market.	End-December 2023	Newly proposed.
Align the rate used for the issuance of the 7-day central bank bills with the Kina Facility Rate.	To improve monetary policy effectiveness and strengthen the monetary policy transmission.	End-December 2023	Newly proposed.
Governance and Anti-corruption Framework			
Appoint a Commissioner and two Deputy Commissioners to the Independent Commission Against Corruption (ICAC) in line with the requirements of the applicable laws.	To enable the ICAC to begin activities to operationalize its mandate.	End-June 2023	Met.
Adopt key implementing regulations to the ICAC law.	To specify operational processes for ICAC to meet its preventive, investigative and prosecutorial mandates, and to ensure sharing of information across relevant entities.	End-December 2023	In progress.
Post details (including the names of the entities awarded the contract and their beneficial owners) of COVID-19 related procurements awarded on the government procurement website, at least covering 2020 and 2021.	To improve transparency in public procurement in COVID-related contracts, in line with commitments made under the disbursement under the Rapid Credit Facility.	End-December 2023	In progress.
Initiate an inter-agency working group on external sector statistics including representatives from the NSO, Treasury Department, PNG Customs Service and the BPNG.	To improve the consistency of external sector statistics with other official statistics.	End-June 2024	Newly proposed.

Annex I. Risk Assessment Matrix[1]

Sources of Risk	Relative Likelihood	Expected Impact	Staff Advice on Policy Response
Regional / Domestic Risks			
Natural disasters and extreme climate events.	**Medium**: PNG is highly vulnerable to natural disasters (flooding, landslides, earthquakes), climate change (droughts & sea level rise) and El Niño. Extreme climate events driven by rising temperatures cause loss of human lives, severe damage to infrastructure, supply disruptions, lower growth, and financial instability.	**Medium**: Negative impact on GDP growth, export and fiscal revenues, higher inflation.	Invest in disaster risk reduction and resilience with the help of development partners. Build fiscal and external buffers for post-disaster relief effort.
Widespread social discontent and political instability.	**Medium**: The limited capacity of the state and a high level of social fragmentation remain chronic sources of political instability. Reform implementation could be hampered by political developments, particularly once the grace period expires.	**Medium**: Adverse impact on foreign direct investment and confidence, negatively impacting growth. This can exacerbate pre-existing inequalities, causing socio-economic hardship (unemployment, poverty).	Focus on transparent and effective communication on key policies. Implement policies to support vulnerable households for which there is a need to build fiscal buffers through fiscal consolidation.
Major natural resource projects initiated; Higher LNG revenues over the medium term.	**High**: Some major projects are being negotiated, but not yet included in the baseline.	**High**: *Upside risk.* Favorable impact on GDP, external balance, and fiscal position.	Fast-track their implementation; Build fiscal and external buffers.

[1] The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly. "Short term" and "medium term" are meant to indicate that the risk could materialize within 1 year and 3 years, respectively.

Sources of Risk	Relative Likelihood	Expected Impact	Staff Advice on Policy Response
		Global Risks	
Cyberthreats.	**Medium**: Cyberattacks on physical or digital infrastructure trigger financial and economic instability. PNG had a ransomware attack in October 2021.	**Medium**: Can affect provision of Government service and trigger financial and economic instability or widespread disruptions in socio-economic activities.	Need to invest in advanced IT security systems and train key personnel on cyber/ ransomware attacks. Invest in business recovery sites and backup for important Government services and financial sector
Commodity price volatility.	**High**: A succession of supply disruptions (e.g., due to conflicts and export restrictions) and demand fluctuations causes recurrent commodity price volatility, external and fiscal pressures, contagion effects, and social and economic instability.	**High**: Volatility in commodity prices will have an impact on external position and fiscal balance. This leads to bouts of price and real sector volatility.	Higher resource revenue should help create fiscal space. Continue with fiscal spending to support the most vulnerable but ensure fiscal consolidation remains priority. Build buffers to prepare for lower commodity prices.
Abrupt global slowdown or recession, including in China.	**Medium:** Global and idiosyncratic risk factors combine to cause a synchronized sharp growth downturn, with recessions in some countries, adverse spillovers through trade and financial channels, and market fragmentation. In China, sharper-than-expected slowdown in the property sector, unexpected fiscal tightening due to local government financing stress and decline in investment, and/or rising geopolitical tensions disrupt economic activity.	**High:** Would lead to lower external demand and lower commodity prices.	Build buffers to support the economy and most vulnerable in the non-resource sector, as needed.

Annex II. Proposed Appropriate Exchange Rate Regime and Monetary Framework in PNG

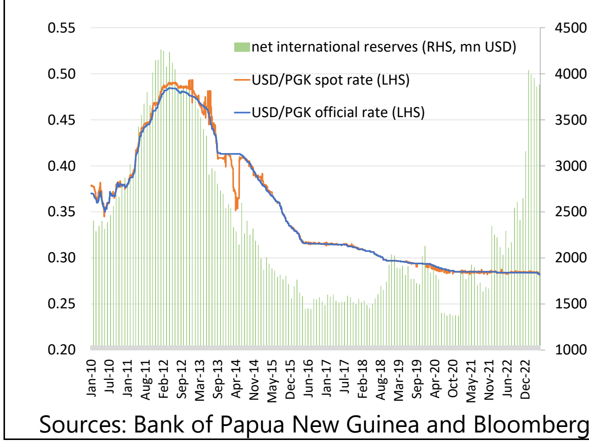
1. The transition to greater exchange rate flexibility is often a difficult and long process, with success dependent on coordinated action in many areas and on a carefully planned transition. This transition entails significant risks. To strive for success, taking stock of the initial conditions and what these imply for reform needs is a necessary starting point. Given its interconnections to monetary policy, the process also requires clearly articulating the monetary policy regime that is being aimed at. Based on a realistic evaluation of the initial conditions, the roadmap to greater exchange flexibility closely depends on the chosen nominal anchor.

2. There needs to be consistency between the exchange rate arrangement and the overall policy framework. From a macroeconomic perspective, the link is provided by the so-called impossible trinity (also known as the trilemma), which states that countries can only achieve two of the following three desired features at any given time: a fixed exchange rate, free capital movements, and an independent monetary policy. For example, in recent years, the BPNG has had monetary policy autonomy and maintained a stable exchange rate, and therefore PNG could not have free capital mobility. In addition, prudent fiscal policy is needed to support the exchange rate and monetary policy frameworks. Fiscal pressures, such as fiscal dominance or loose fiscal policy, can substantially complicate the conduct of monetary policy. On top of ensuring central bank independence, good monetary-fiscal coordination is needed to ensure adequate responses to the large external shocks which commodity exporters like PNG typically face. For instance, a fiscal rule along with effective sovereign wealth management will often be desirable to prevent excessive real exchange rate appreciation during commodity price booms (Casiraghi et al. 2022).

Current Framework

3. While PNG's *de jure* exchange rate regime is floating, its *de facto* exchange rate arrangement has been classified by the IMF as either "crawl-like" or "stabilized" arrangement relative to the US dollar since 2014. Formally, the exchange rate is determined daily by the FX market, with the publication of a reference rate on the BPNG website at the end of each working day. During the peak of the construction phase of the PNG LNG project (2010-2013), which triggered large foreign direct investment (FDI) inflows, the kina, which was floating since 1994, appreciated by about 25 percent (Figure 1). When the construction ended in 2013, FDI inflows stopped, and were not replaced by significant export proceeds, given the fiscal and financial advantages granted to the PNG LNG's private partner; this led to a rapid depreciation of the kina. As depreciation pressures mounted further in the context of the early 2014 commodity price bust, FX reserves were

Figure 1. Papua New Guinea: USD/PGK Official and Spot Market Exchange Rates and Net International Reserves



Sources: Bank of Papua New Guinea and Bloomberg.

diminishing and the gap between the official interbank rate, managed by BPNG, and the spot market rate, reflecting the market-clearing rate, widened. In May 2014, the BPNG introduced a trading band around the interbank rate, which led to a forced 17 percent appreciation of the spot market rate. This overvaluation led to an immediate mismatch between FX supply and demand, thus creating FX shortages. Since then, the exchange rate against the US dollar (USD) has been slowly depreciating in nominal terms with persistent and significant FX shortages.

4. **While formally implementing a reserve money targeting framework in support of the price stability objective, the BPNG has in practice relied on an implicit exchange rate anchor.** Twice a year, the Economics Department updates its monetary program to set quarterly base money targets, which remain a centerpiece of the macroeconomic projections by the BPNG, including on inflation. However, communication by the BPNG does not formally refer to reserve money targets; and the effect of changes in monetary aggregates on inflation is weak, in part owing to excess liquidity. Implicitly, the exchange rate has functioned as the nominal anchor and provided price stability, given the high pass-through to inflation.

Proposed Appropriate Framework for PNG

5. **The IMF's Monetary and Capital Markets (MCM) Department has listed a comprehensive set of criteria (Table 1) that can help inform the choice of an exchange rate arrangement.** These criteria can be organized into three groups: (1) macroeconomic initial conditions, such as inflation, foreign exchange reserve adequacy, and fiscal and external imbalances; (2) structural characteristics of the economy, including its size and openness, mobility and flexibility of factors of production, and type and frequency of shocks; and (3) institutional features and prospects for their development. Commodity exporters with relatively undiversified output, that are susceptible to large and frequent terms-of-trade shocks, may favor a more flexible exchange rate. Those that are very small, very open, and with undeveloped financial markets may prefer a fixed exchange rate. If country characteristics do not clearly support the choice of either a float or a peg, an intermediate arrangement—a crawling peg or a crawl-like arrangement—could be an appropriate choice. The chosen exchange rate regime should allow nominal stability, facilitate sustained economic growth and trade, ease external adjustment, and promote broad systemic stability.

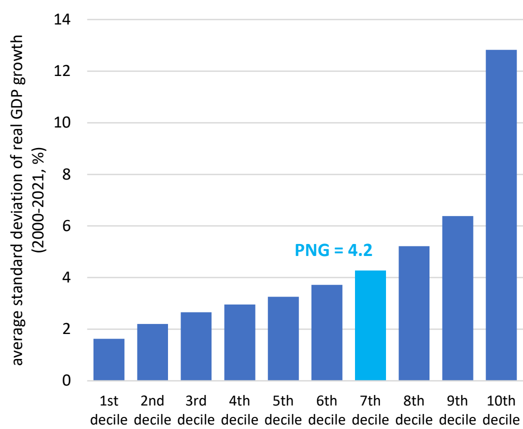
Table 1. Papua New Guinea: Key Criteria for Choosing an Exchange Rate Arrangement

Macroeconomic Initial Conditions	Characteristics of the Economy	Types of Shocks to the Economy
Level of inflation Size of external imbalances Foreign exchange reserves Financial system vulnerabilities Fiscal position Other macroeconomic policies	Size of the economy Openness Diversification of exports and output Trade and political integration Flexibility of labor markets Mobility of capital Dollarization Financial system development	Real shocks Volatile capital flows

Sources: Casiraghi M., K. Habermaier and T. Harjes. 2022. Choice of Exchange Rate Arrangement. MCM Technical Assistance Handbook, December 2022. International Monetary Fund. Washington, D.C.

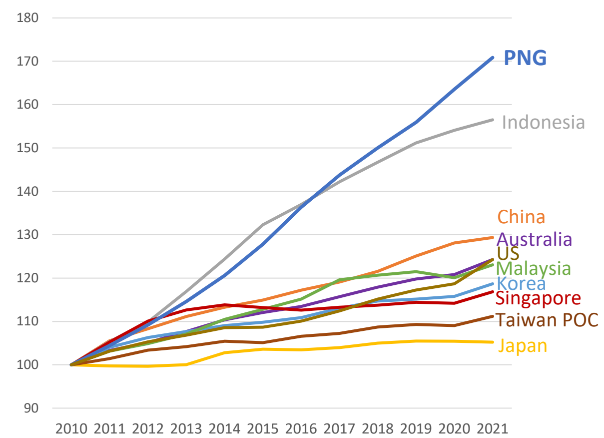
6. PNG's move from the current de facto stabilized exchange rate regime to a more flexible arrangement is supported by a set of key macroeconomic conditions and characteristics. PNG is a resource-dependent open economy, subject to high volatility due to its exposure to commodity price shocks as well as natural disasters and climate hazards (Figure 2). It has displayed higher average inflation than its main trading partners over the past decade (Figure 3), and the exchange rate has been overvalued for a decade. These factors all suggest that PNG could benefit from a more flexible exchange rate, which would also allow for the reduction of current and future misalignments of the exchange rate. More flexibility could also promote the development of an interbank FX market and of hedging tools, thus contributing to financial sector development.

Figure 2. Papua New Guinea: Distribution of Standard Deviation of Real GDP Growth (2000-2021)



Sources: IMF WEO, IMF staff estimates covering 196 countries.

Figure 3. Papua New Guinea: Consumer Price Index (2010 = 100)

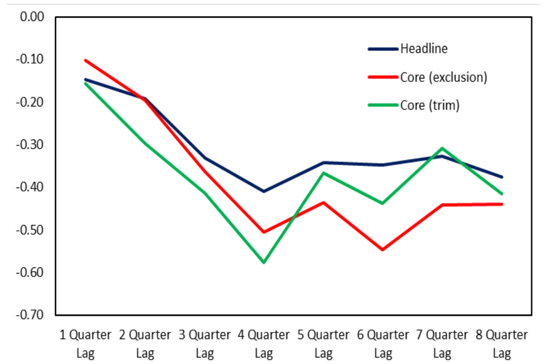


Source: Relevant economies' authorities. POC = Province of China.

7. A full de facto floating exchange rate is however not suitable for PNG at this point in time. PNG is a relatively small economy with a concentrated financial sector. Private and public debt are exposed to significant currency risks, meaning that large depreciations could be threats to financial stability and fiscal sustainability. The possibility of Dutch-disease-type mechanisms related to the forthcoming construction of new, large resource projects could also trigger an over-appreciation of the exchange rate, which could threaten competitiveness and hamper economic diversification.

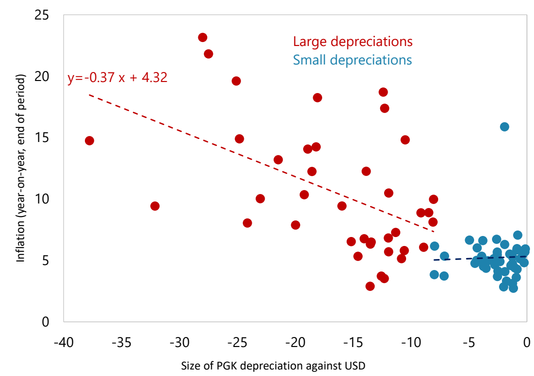
8. The shift to a *de facto* crawl-like arrangement, which would serve as the nominal anchor for monetary policy, is a suitable option for PNG to transition to a more flexible exchange rate. This arrangement should allow to reduce misalignments of the exchange rate by bringing it to levels closer to fundamentals, and allow for moderate fluctuations around it, while preventing exchange rate overshooting (both appreciation and depreciation). In addition, the estimated passthrough from the exchange rate to inflation is high, supporting the notion of managing the exchange rate for price stability purposes (Figure 4). According to IMF estimates, after a year, a 10 percent depreciation of the nominal effective exchange rate could lead to a 4 to 5 percentage-point increase in inflation, with results largely stable whether one consider headline or core CPI.[1] This correlation between the size of the depreciation and inflation is valid for large depreciations; there is however no clear correlation in case of smaller-size depreciations (Figure 5).

Figure 4. Papua New Guinea: Exchange Rate Passthrough Estimation (Up to 2-year lag)



Source: IMF staff estimates based on authorities' data. Auto-regressive distributed lag approach. 2001-2021 window. A value of -0.5 means for every 1.0 percent depreciation of the NEER, consumer goods measured using the CPI will increase in price by 0.5%.

Figure 5. Papua New Guinea: Inflation vs. Depreciation of the Kina (Percent)



Source: IMF staff estimates based on authorities' data. 1990Q1 to 2022Q4. A large depreciation of the kina against the US dollar is defined as a decrease of more than 8 percent in the exchange rate over the considered quarter.

9. Maintaining a well-communicated exchange rate anchor while emphasizing the primacy of the price stability mandate is a pertinent option in the early stages of PNG's transition to a more flexible exchange rate. As modernizing central banks have adopted price stability as the primary mandate for monetary policy, the role of the nominal exchange rate as an anchor has gradually diminished and increased exchange rate flexibility has ensued. This has in turn diminished exchange rate passthrough into domestic prices. In several countries, the transition involved the exchange rate moving away from being an intermediate target to becoming an important part of the transmission mechanism, and an information variable among others. While the experience of countries that have transitioned to greater flexibility has varied greatly, the most important is to liberalize the exchange rate within the context of a well-structured and clearly communicated strategy that emphasizes the primacy of the medium-term inflation objective. In addition, central banks need to have a clear and unified framework within which to evaluate monetary policy and exchange rate interventions decisions. This adds to the demands for greater analytical and operational capacity by the BPNG.

Parameters of the Crawl-like Arrangement

10. To be considered a crawl-like arrangement according to the definition used in the IMF's Annual Report on Exchange Arrangements and Exchange Restrictions (AREAER), the exchange rate arrangement would need to meet the following criteria:

[1] The passthrough appears higher for core measures of inflation, partly because these exclude regulated prices as well as food items, several of which, albeit volatile, are less susceptible to fluctuations in the currency.

- The exchange rate must remain within a narrow margin of 2 percent relative to a statistically identified trend for six months or more (with the exception of a specified number of outliers).
- The exchange rate arrangement cannot be considered as floating.
- Normally, a minimum rate of change greater than allowed under a stabilized (peg-like) arrangement is required. However, an arrangement will be considered crawl-like with an annualized rate of change of at least 1 percent, provided that the exchange rate appreciates or depreciates in a sufficiently monotonic and continuous manner.

11. **The design of such an arrangement involves the choice of several parameters.** MCM recommendations on some of these parameters are as follows. In addition, arrangements for implementation include the determination of domestic interest rates, money and foreign exchange market operations, foreign exchange regulations, and communications.

- ***Anchor currency/ies.*** First, the anchor should be important / relevant to the economy of the pegging country owing to its widespread use in trade and finance by economic agents of the pegging country. Second, it should be a convertible currency of a relatively large country that can be traded freely and at low cost in the domestic and global foreign exchange markets. Third, it should have a track record and good prospects of low and stable inflation. Fourth, its exchange rate should not be excessively unstable relative to other major currencies, although this consideration may be outweighed by its relevance to the pegging country.
- ***Rate of crawl.*** The annual rate of crawl should allow to both correct for the current misalignment of the exchange rate and avoid further misalignment due to inflation differentials with main trading partners. Once the annual rate has been established, equal linear daily steps can be established. The rate of crawl would be reviewed at least every six months, based on updated estimates of the exchange rate misalignment and domestic and global inflation projections.
- ***Width of the crawl band.*** Once the BPNG has defined the reference rate and computed the daily path for the rate, it should ensure that the exchange rate stays within +/- 1 percent of the daily reference rate, so as to remain consistent with a crawl-like arrangement.

Annex III. Alternative Scenario: Launch of Papua LNG

1. **This annex outlines an alternative scenario under which the construction of Papua LNG, a new major natural gas production project, kicks off by mid-2024.** The project's Gas Agreement was signed in 2019 and the Fiscal Stability Agreement in February 2021, allowing the project partners to complete the Front-End Engineering and Design (FEED) studies in March 2023 that will lead to the Final Investment Decision (FID) expected to take place in early 2024. The financial arrangements of the project are still being worked out; and the construction phase is expected to start soon after the signing of the FID.[1] It is assumed that the construction phase will take five years so the production would commence in 2029, having an operation life of 25 years. The project cost is estimated at US$10 billion for the construction phase and is a joint venture led by Total Energies (37.55 percent), with its partners Exxon Mobil (37.04 percent), Santos (22.83 percent) and JX Nippon (2.58 percent). The State has a back-in right of up to 22.5 percent of participating equity interest at the time of the FID. Gas resources are estimated at over 1 billion barrels of oil equivalent with an LNG production capacity of up to 6 million tons per year (mt/y). Under the Fiscal Stability Agreement, PNG government revenue will consist in: (i) corporate income tax: 32 percent of taxable profit, (ii) royalties: 2 percent of sales (wellhead value) with additional 2 percent of development levy and 2 percent of production levy, (iii) additional profit tax: 15 percent if post-tax internal rate of return is more than 15 percent.

2. **The estimated impact of the construction phase of Papua LNG is largely based on a backward-looking analysis of the effects of the construction of the comparable PNG LNG project (2010-2013), which started its production in 2014.** PNG LNG is the largest (and the only currently operating) petroleum project in PNG. The PNG LNG project costed US$19 billion in capital expenditure and is a joint venture led and operated by Exxon Mobil. The construction phase took place in 2010-13 and first production commenced in April 2014, with an originally estimated capacity of 6.9 mt/y. Given Papua LNG's similarities with PNG LNG, the exercise assumes that the effects of the new project on activity, fiscal accounts, and external accounts will be akin to those observed for PNG LNG, scaled down for the size of the project and corrected for inflation. The impact of the construction phase of the PNG LNG project is estimated by simulating a "business as usual" scenario (i.e., in the absence of PNG LNG) and comparing it with actual historical data over the period 2010-13.

- **Real and external sectors.** For the PNG LNG project, balance of payments and real sector statistics (Figures 1 and 2) indicate "leakage" reached close to 75 percent of the US$19 bn cost (i.e., the impact on domestic activity was about 25 percent of the investment). The local content of the investment (25 percent) directly benefitted the construction sector, with spillover effects mainly on services (financing, insurance, real estate, administrative and support professional and scientific, etc.) and transport and storage. In the case of Papua LNG, a lower leakage of 70

[1] This annex is based on public information and on staff assumptions. The final parameters might differ. Given the remaining uncertainties on costs, on financial arrangements and on the start date, the project will only be included in staff's and authorities' baselines once the FID is signed.

percent is estimated, based on the authorities' intention to negotiate higher domestic contents of the project. This leads to an estimated cumulative 25.5 percent increase in the level of real GDP over five years compared to 22.3 percent under the baseline projection, equivalent to an average 0.6 percentage point of additional annual growth. On the external side, during the investment phase, construction will require imports of goods and services, as well as primary income payments related to mining sector employment and operations. Together, these three items should lead to a worsening (vis-à-vis a non-investment baseline scenario) of the current account balance of around US$1.4 billion per year. On the financial account, FDI inflows related to the project would be on average US$2 billion per year for five years, so the net effect would be an additional accumulation of US$600 million in FX reserves per year. The additional US$3 billion in FX reserves accumulated during the construction of the project would correspond to 7-8 months of 2030 imports (or 10-11 months of non-mineral imports).

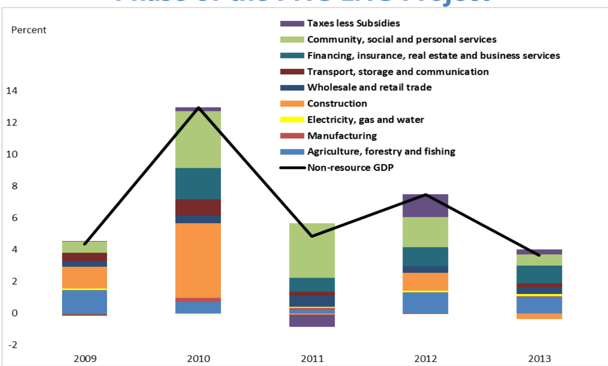
- **Exchange rate.** The PNG LNG project triggered a large appreciation of the kina (floating at the time) of about 25 percent against the USD in 2010-12 (Figure 3), stemming from FDI inflows. For the Papua LNG project, scaled-down appreciation pressures of about 10 percent are expected. However, the crawl-like arrangement will help avoid a rapid appreciation of the currency. And by offsetting the current overvaluation of the currency, the project will help reach the equilibrium exchange rate sooner, which, alongside the additional FX reserves, will support the elimination of FX shortages and enable the gradual removal of FX rationing.

- **Fiscal sector.** The project financing will be provided by the consortium of partner companies. The PNG estate (through Kumul Petroleum) would own between 1/5 and ¼ of the project. While the state is not expected to put its share of the investment upfront, but rather have it financed by the consortium and be repaid out of the project's dividends, it is assumed that the financiers will require sovereign guarantees to be put forward during the construction period. These are typically constituted gradually, as resources are disbursed during the construction period, and would lead to a gradual increase from 2024 to 2029 of public debt by some US$ 2.0-2.5 billion. The guarantees will be rolled back at the end of the construction phase, decreasing debt accordingly. As was observed during the PNG LNG project construction phase, the fiscal impact in terms of revenue as a share of GDP is expected to be marginal during the construction phase.

3. **Starting from 2029, the Papua LNG project will enter into operation.** While the sectors most involved in the construction phase will see their activity go back close to the baseline scenario, the volume of LNG exports will increase by 75 percent relative to the 2015-2022 average volume of exports. Imports will fall back to levels comparable to the baseline. Real GDP will be boosted by the significant increase in natural gas production during the early years of operations, and the trade balance will improve by USD 1.5-2 billion once production reaches its potential. From the experience of PNG LNG, direct fiscal revenue from the project is assumed to start coming in by 2029 in small amounts and gradually increase over the production phase: income tax revenue is expected to flow in as capital cost deductions are exhausted, while dividend payments will occur once the government loan contracted to finance its equity participation is repaid. The effect on the exchange rate is less certain: while the end of the construction phase would potentially reduce the demand for

kina, higher exports would tend to increase the supply of FX. Finally, this alternative scenario does not include the impact of other large resource projects in the pipeline, such as Wafi-Golpu gold mine or the P'nyang LNG project, which could both start in the second half of the decade.

Figure 1. Papua New Guinea: Non-Resource Real GDP Growth During the Construction Phase of the PNG LNG Project



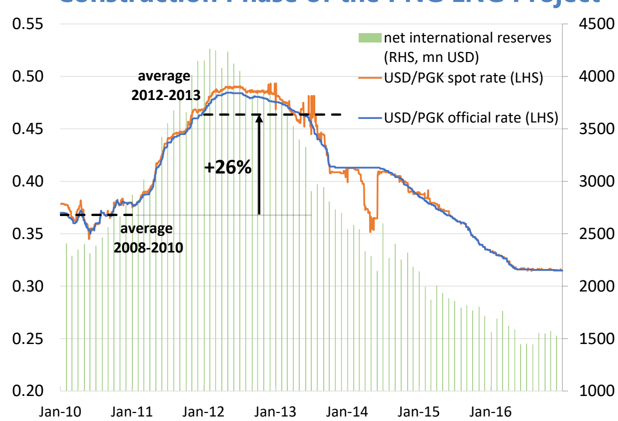
Source: IMF staff estimates.

Figure 2. Papua New Guinea: Estimated Annual Changes in Key External Sector Aggregates due to PNG LNG

USD billion	Construction ('11-'13)	Production ('14-'21)
Exports of G&S	-	**3.0**
Imports	**3.5**	**-**
Goods	1.6	-
Services	1.9	-
Primary Income	**0.8**	**-**

Sources: BPNG and IMF staff estimates.

Figure 3. Papua New Guinea: Exchange Rate (USD/Kina) and Foreign Exchange Reserves (USD million) During the Construction Phase of the PNG LNG Project



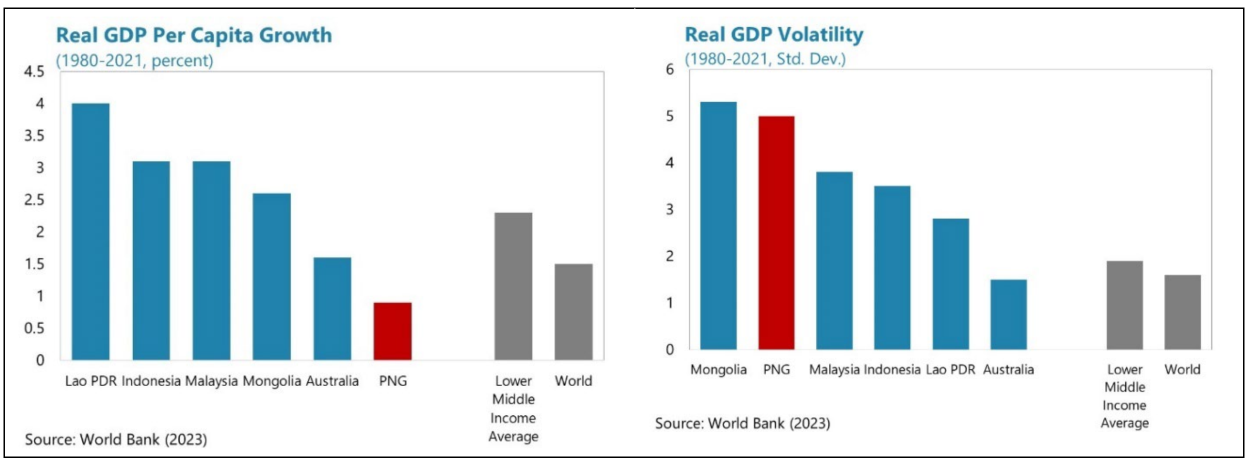
Sources: BPNG, Bloomberg and IMF staff estimates.

Annex IV. Country Engagement Strategy

In line with the IMF's Strategy for Fragile and Conflict-Affected States (FCS), this annex sets out a Country Engagement Strategy (CES) for Papua New Guinea (PNG). The main policy priorities focus on safeguarding fiscal sustainability and resilience to climate risks, addressing FX shortages and other structural impediments to inclusive growth, reforming central bank operations, and strengthening governance and transparency. These policies are aligned with the ECF/EFF program and form the basis of ongoing discussions with the authorities.

A. Sources of Economic and Social Resilience

1. There are social and economic-based sources of resilience inherent to PNG. A rural economy and traditional landownership provide some basis for sustained and relatively dependable household subsistence, while SMEs and the presence of a few large multinationals provide a basis for urban settlement. Social cohesion is also reinforced by a reliance on custom-based dispute resolution arrangements in rural settings. These historical community-based structures and networks help mitigate some risks, particularly those related to natural disasters and other climate change-related challenges.



B. Drivers and Impact of Fragility in Papua New Guinea

2. Nonetheless, PNG remains a fragile state vulnerable to natural disasters, terms of trade shocks, and bouts of political instability. Development needs remain significant, poverty and inequality are high, with much of the population in rural areas lacking access to basic infrastructure and services. While the authorities have adopted a national strategy to prevent and respond to gender-based violence, gender inequality and violence against women are still prevalent, which limit women's economic participation, and contribute to fragility.

3. The country's fragility stems from its geographic nature and historical contexts of nation-building. These factors have been exacerbated by corruption, which hampers inclusive and sustainable economic growth.

- **Natural disaster and climate change risks.** PNG is one of the most vulnerable countries in the world to natural disasters, based on the United Nations University's World Risk Report (2021). Vulnerabilities are high in terms of food security, ecosystem services, quality of human habitat, and health. Most of the population—more than 80 percent—is rural, highly exposed to climate risks. Hazards in PNG include sea level rise, coastal erosion, coastal and inland flooding, drought, landslides, heatwaves, earthquakes and inland frost, among others. Weak governance and corruption; insufficient transparency; and limited accountability in natural resources management and land administration increase vulnerability to climate risks. Tensions and contestations related to land and resources also play out across multiple levels.

- **Economic challenges.** Exports are concentrated in resource extraction, accounting for around 90 percent of total exports, and are capital-intensive, employing few local workers. Rent-seeking opportunities are particularly high in the extractive industries where the economic opportunities are concentrated among a few. PNG's structural dependence on global price-volatile commodities has knock-on effects on public finances and inward investment. Moreover, institutional arrangements to attenuate boom-bust patterns of economic growth are lacking; reliance on a few commodities and lack of diversification have contributed to boom-bust cycles, and a debt-to-GDP limit introduced in the Fiscal Responsibility Act of 2006 to insulate spending from commodity price swings has not effectively acted as a ceiling on government deficits or debt levels.[1]

- **Fragile national unity.** There are over a thousand ethnic groups and more than 800 indigenous languages. Fragmentation in society has triggered periods of political instability. Consequently, in the context of PNG's highly fragmented society, political parties do not serve as an effective means of collective action, producing challenges for governance.

- **Weak state institutions and governance challenges.** The quality of public sector management and institutions is among the lowest in the Asia and Pacific region. The World Bank's Country Policy and Institutional Assessment (CPIA) shows that PNG's overall CPIA has declined since 2010.

- **Law and Order.** PNG faces chronic sources of social unrest due to limited state capacity, corruption, and a high level of social fragmentation and youth disempowerment. Rural areas are plagued by tribal violence and youth disempowerment, while urban areas suffer from high crime rates and ethnic clashes.

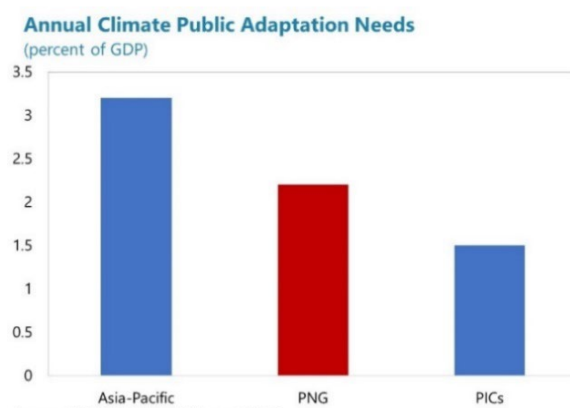
[1] The debt ceiling limit has been raised four times over its 15-year lifespan, most recently in the 2020 supplementary budget, where it was increased to 60 percent of GDP.

4. These fragility drivers translate into adverse economic outcomes, which reinforce the existing fragility:

- **Constrained fiscal space and sustainability risks**: High economic volatility from a reliance on the resource sector has led to public expenditure volatility, making budget planning and execution more challenging. Weaknesses in public financial management (PFM) have contributed to gaps in approved and executed spending in the composition of expenditure, which has negatively affected public service delivery. Multiple exogenous shocks, low government revenues coupled with lower revenue and higher spending caused by the COVID pandemic contributed to a buildup of public debt, which is assessed to be at high risk of distress according to the latest IMF/WB DSA. The elevated level of debt affects capital accumulation and economic growth through reduced investor confidence and elevated interest payments that crowds out productive public investment spending.

- **Exchange rate overvaluation and foreign exchange shortages:** A narrow export base, low commodity prices in 2014-20, a severe drought in 2015-16, and an exchange rate regime stabilized against the US dollar have resulted in an overvalued Kina, shortages of foreign exchange (FX), and the introduction of FX rationing measures, hindering foreign investment and growth. These developments have hindered FDI via damaged business confidence.

- **Constrained climate change adaptation capacity.** Given PNG's heavy reliance on climate-vulnerable sectors, the economic costs associated with the hazards of climate change are potentially steep, while climate adaptive capacity is low. Climate adaptation needs are estimated at about 2 percent of GDP annually for the next 10 years (IMF, 2021). Investment of 2 percent per year for climate adaptation are currently prohibitive for PNG given the lack of fiscal space, while adaptive capacity is one of the lowest in Asia Pacific, due to fragile health and education systems as well as insecurity of water supply.



Source: IMF PNG Article IV Report 2022.

- **Governance weaknesses and related corruption vulnerabilities, which affect adverse economic outcomes.** Weak governance, corruption and insufficient accountability for public spending have prevented efficient use of the budget and undermined intergenerational equity of resources. Weak governance structures, weaknesses in the rule of law, corruption and poor oversight over large-scale resource extraction projects also undermines trust in public institutions.

- **Challenges in achieving Sustainable Development Goals (SDGs):** Swings in commodity prices have hindered sustainably financing SDG commitments, while governance challenges from limited technical and financial capacities have resulted in a lack of coordination, poor accountability, and governance in development. Data weaknesses also make it challenging in tracking the progress of SDGs, which is compounded by rugged topography, limited capacity throughout the country and a lack of coordination.

C. Constraints to Reform and Policy Formulation

5. Challenges in state capacity and governance vulnerabilities linked to corruption constitute major constraints to reform. They prevent the government from effectively providing public services and making necessary investments to address low productivity, inequality, infrastructure gaps, and vulnerability to climate change.

6. Political and governance fragmentation makes consensus for reforms arduous. Geographic and social fragmentation of political constituencies, combined with a dispersed population, contributes to a thin state presence. Particularly at a local level, governance is patronage-based, which contributes to reliance on unstable arrangements.

D. Fund Program and Policies to Address the Sources of Fragility

7. In recent years PNG has extensively engaged with the Fund, through two SMPs, an RCF, and an ECF/EFF. In 2021, the emergency financing under the Rapid Credit Facility (RCF) and the SDR allocation supported the authorities' efforts to address the economic challenges from the COVID-19 pandemic. The current ECF/EFF arrangements build on progress under past SMPs (2020/21 and 2021/22) and support the authorities reform agenda on strengthening debt sustainability, alleviating FX shortages, and modernizing the operations of the central bank, and enhancing governance and strengthening anti-corruption frameworks.

8. FCS strategy informed ECF/EFF program design and conditionality. The program protects spending for society's most vulnerable, with program targets and timelines tailored to focus on macro criticality—FX shortages, fiscal sustainability, and governance—while accounting for the country's limited implementation capacity and risk of fast-changing circumstances, including political ownership of reforms, commodity price fluctuations and natural disasters. Realistic and streamlined conditionality in the program will be supported by capacity development (CD), which will be critical for successful implementation of a Fund-supported program.

9. The following policies ranging from short to medium-term measures under the program aim to mitigate the country's macro-financial fragility*, *support medium-term structural transformation, and improve functioning of the rule of law*:*

- **Ensuring macro-financial stability.** Stable macroeconomic environments underpinned by appropriate support for the vulnerable, strong fiscal discipline, and robust reserve buffers, underpinned by IMF resources, would allow the authorities to undertake necessary investments and reforms. The operationalization of the sovereign wealth fund law in the medium-term could help ensure macro-financial stability by creating financial buffers for contingencies, while also saving resources for future generations.

- **Safeguarding fiscal sustainability and strengthening public sector financial management.** Strengthening revenue collection is a key part of the fiscal consolidation strategy, including by developing a medium-term revenue strategy (MTRS), and simplifying and modernizing the tax system by rewriting the Income Tax Act (ITA). PFM reforms are also needed in the areas of budget planning, cash management, and transparency of public spending, which would enhance the quality and accountability of public expenditure in the medium term. Greater efficiency of spending will be critical in achieving SDGs.[2] Finally, spending for security and social programs that target the most vulnerable have been protected under the program. Against the backdrop of a deterioration in PFM—as reflected in the CPIA rating—the authorities have committed under the Fund program to improving transparency in public spending and procurement.

- **Moving to a market-determined exchange rate, easing FX shortages and modernizing operations of the central bank:** Movement toward a market-clearing exchange rate, removal of exchange restrictions and strengthening of the governance and management of the central bank are key planks of the program. Other features of the program include establishing a clear primacy for price stability as the central bank's mandate, clarifying the role of the board, filling central bank board and management vacancies and placing restraints on central bank profit advances to finance public spending.

- **Enhancing governance and transparency and improving functioning of the rule of law.** To address governance weaknesses linked to corruption and enhance transparency, a sustained, multi-year effort with close external support, including from the IMF, is needed. This should cover the areas of property rights, predictability and enforceability in contracting, and governmental effectiveness and transparency. The operationalization of the Independent Commission Against Corruption (ICAC), supported by the program, is critical in that respect.

E. Capacity Development Policies and Strategic Partnerships

10. The Fund's CD priorities are determined by program objectives and authorities' demand, while considering PNG's absorptive capacity. Fund CD delivery is closely coordinated with other PNG's partners to avoid duplication and increase synergy. Recent activities include the following, which are intended to support the program and address the sources of fragility:

- **Revenue mobilization.** The Fiscal Affairs Department (FAD) and the regional technical assistance center (PFTAC) have been delivering support to develop a MTRS, simplifying and modernizing the tax system and revenue administration, including debt management, and monitoring of fiscal risks.[3] The thrust of the MTRS will be to raise revenues in the medium term by a few percentage points of GDP to help sustainably narrow the fiscal deficit and put public

[2] See 'Fiscal Policy and Development: Human, Social, and Physical Investments for the SDGs', IMF Staff Discussion Note No. 2019/003.

[3] Against this backdrop, staff recommended to the authorities a Public Investment Management Assessment (PIMA) to ensure investments deliver quality projects at reasonable cost to strengthen potential growth and identify areas where to rebalance the composition of spending to emphasize delivery of frontline services and priority capital spending.

debt on a downward trajectory, while identified growth- and equity-enhancing expenditure priorities in infrastructure, health, education, social assistance and security are safeguarded.

- **Monetary policy and central bank governance.** Support from MCM, FIN, and LEG has helped the authorities produce a sequenced roadmap to move toward a market-clearing exchange rate, alleviate FX shortages and strengthen central bank risk management practices, including through a safeguards assessment. An IMF Financial Sector Stability Review (FSSR) is also being planned for early 2024—the country's first—that will aim to identify systemic financial risks and gaps in the financial supervision and regulatory framework of banks.

- **Governance and transparency.** The program includes steps to strengthen the legal and institutional frameworks for auditing and AML/CFT and protection of correspondent banking relationships. The Fund stands ready to discuss the possibilities of providing TA, complementing TA received from other partners.

- **Improving macro-financial data.** With regular in-person and virtual support from STA and PFTAC, the authorities are moving to improve the quality of timeliness of national and government financial accounts, and BOP.

- **Improving macro-fiscal forecasting.** ICD and PFTAC is providing TA to strengthen authorities forecasting capacity and policy evaluation.

11. The Fund has recently re-established an on the ground presence by opening a Resident Representative office. The office is the country's first IMF office in over two decades and will help improve country engagement and the real-time two-ways flow of information, ensuring the Fund is attune to the country's needs.

12. Close coordination with development partners is critical to ensure program success. Conventional partners such as the Asian Development Bank (ADB), World Bank, United Nations agencies, European Union, Australia, Japan, and the U.S. provide development assistance reflecting their respective mandate and expertise. The Fund has maintained close cooperation with those development partners, as well as non-governmental organizations. The team continues to explore synergies, such as with the World Bank on public financial management (PFM), the ADB on SME governance reforms, and the UN and EU on anti-corruption reforms.

13. Program engagement involves significant risks. Reform implementation could be hampered by political developments, particularly once the grace period precluding votes of no confidence in parliament expires. Even if there is no disruption, government reforms could stall before the general elections scheduled for early 2027. A deterioration of external economic conditions and natural disasters could undermine macro-financial stability, given dependence on commodities.

Annex V. Adopting BPM6 Standards in the Balance of Payments Statistics

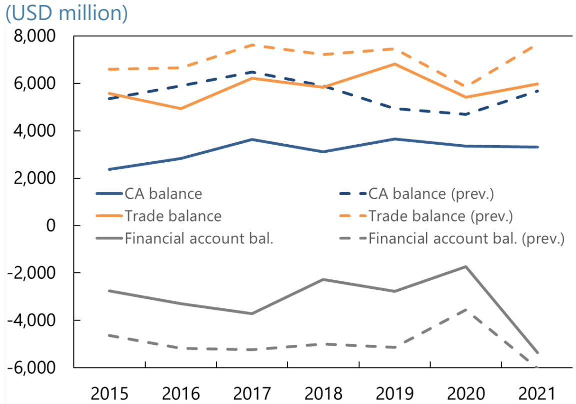
1. The authorities published BOP data based on BPM6 standards in 2023. IMF's CDOT provided technical assistance (TA) on external sector statistics (ESS) to the Bank of Papua New Guinea (BPNG) in 2022 to identify and to compile transactions in the current account, capital account and the financial account that are consistent with the Balance of Payments and International Investment Position Manual, sixth edition (BPM6). The TA also helped improve the compilation and classification of data. Following guidance from the mission, BPNG has produced balance of payments estimates for 2015 to 2022 in the BPM6 format, which were published earlier this year as part of the Quarterly Economic Bulletin Statistical Tables.

2. The revised series show more moderate current and financial account balances. The current account balance was lower than previously estimated (by an annual average of USD 2.4 billion between 2015 and 2021) given a smaller trade balance for goods and services (US$ 900 million, on average), while the income balance was also revised to the downside (US$ 700 million). On the latter, this account now includes all dividends to nonresident investors in the mining industry. Correspondingly, the financial account balance was also smaller, with significant changes in other investments (US$ 2.1 billion). The downward revision to this account reflects reductions in external deposits of the LNG sector.

3. While key improvements, such as on the recording of external transactions of the natural gas sector, were implemented, work on quality of statistics remains. Areas for future improvement include the measurement of external assets and liabilities for compilation of the international investment position (IIP), ensuring statistical consistency with national accounts and government financial statistics, and initiating an inter-agency working group with representatives from the NSO, Treasury Department, PNG Customs Service and the BPNG to improve the consistency of the ESS with other official statistics.

Revision of BoP Components

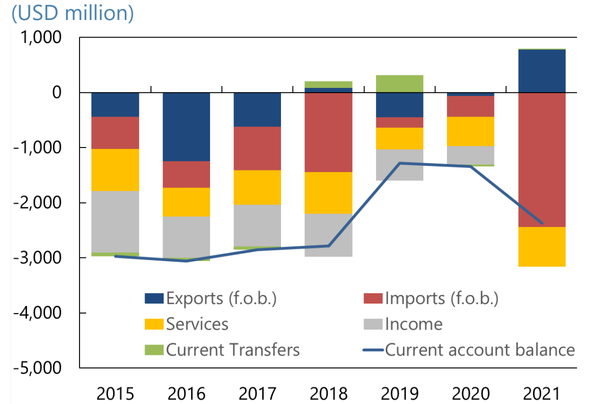
(USD million)



Sources: BPNG and IMF staff.

Drivers of the Revisions to the CAB

(USD million)



Sources: BPNG; Haver; and IMF staff estimates.

Annex VI. Alternative Models of the Exchange Rate Assessment

1. **The design and implementation of the Roadmap calls for a careful assessment and monitoring of the evolution of the equilibrium exchange rate.** EBA-lite models do not capture well PNG's country-specific characteristics as a fragile state prone to major shocks and economic transformation. Further, significant data revisions due to the move to BPM6 standards (see Annex V) and the need for higher frequency analysis for program implementation suggested seeking complementary models based on fundamental drivers of the REER, including terms of trade, economic activity, and financial conditions indicators.

2. **Following de Gregorio, *et. al.* (2005)[1], who study the behavior of the real exchange rate in the case of a commodity-intensive economy, we estimate time series models on quarterly frequency data.** The strategy seeks to derive empirical elasticities of the real exchange rate with respect to fundamental drivers. We estimate four variants of the equation as shown below:

$$e_t = \sum_{i=1}^{n} \alpha_i e_{t-i} + \sum_{i=0}^{n} \beta_i oil_{t-i} + \sum_{i=0}^{n} \gamma_i gas_{t-i} + \sum_{i=0}^{n} \delta_i gold_{t-i} + \varepsilon_t \; (1)$$

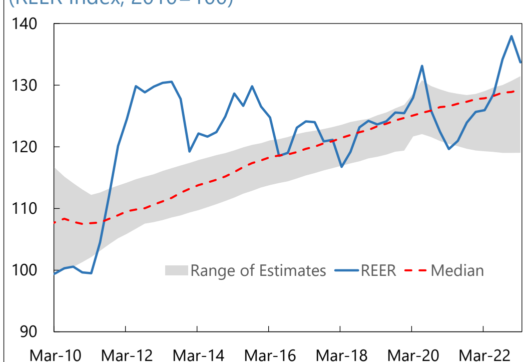
$$e_t = \sum_{i=1}^{n} \alpha_i e_{t-i} + \sum_{i=0}^{n} \beta_i oil_{t-i} + \sum_{i=0}^{n} \gamma_i gas_{t-i} + \sum_{i=0}^{n} \delta_i gold_{t-i} + \theta Dt + \varepsilon_t \; (2)$$

$$e_t = \sum_{i=1}^{n} \alpha_i e_{t-i} + \sum_{i=0}^{n} \beta_i oil_{t-i} + \sum_{i=0}^{n} \gamma_i gas_{t-i} + \sum_{i=0}^{n} \delta_i gold_{t-i} + \sum_{i=0}^{n} \rho_i dxy_{t-i} + \theta Dt + \varepsilon_t \; (3)$$

$$e_t = \sum_{i=1}^{n} \alpha_i e_{t-i} + \sum_{i=0}^{n} \beta_i oil_{t-i} + \sum_{i=0}^{n} \gamma_i gas_{t-i} + \sum_{i=0}^{n} \delta_i gold_{t-i} + \sum_{i=0}^{n} \rho_i dxy_{t-i} + \sum_{i=0}^{n} \varphi_i usgdp_{t-i} + \theta Dt + \varepsilon_t \; (4)$$

The lowercase variables in equations (1)-(4) stand for log differences of the real exchange rate, oil prices, gas prices, gold prices, the dollar index, and the US GDP. The dummy accounts for changes in global financial conditions— including the dot com crisis (2000), the global financial crisis (2008), and the COVID pandemic crisis (2020) — which typically constitute exogenous shocks to currency valuations. Finally, we estimate all equations with 1 through 4 lags. Instead of choosing a single specification among the 16 alternatives to fit the real exchange rate, we compute the median estimate among all of them for each period and infer the fitted real exchange rate (Figure 1).

Figure 1. Papua New Guinea: Fitted Kina
(REER Index, 2010=100)



Sources: BPNG; Haver; and IMF staff estimates.

3. **These alternative models indicate a milder overvaluation than the one arising from the EBA-lite analysis, with a relatively wide range of estimates.** The median overvaluation across these models is 7 percent, with estimates ranging between 5 and 15 percent) at end-2022. Estimates for the REER for the beginning of 2023 show overvaluation has moderated by 3 to 4 percentage points due to weaker US dollar and lower inflation in PNG.

[1] de Gregorio Rebeco, José, Hermann González, and Felipe Jaque. "Fluctuaciones del dólar, precio del cobre y términos de intercambio." Documentos de Trabajo (Banco Central de Chile) 310 (2005): 1.

Appendix I. Letter of Intent

Ms. Kristalina Georgieva
Managing Director
International Monetary Fund
Washington, D.C. 20431

November 4, 2023
Port Moresby

Dear Ms. Georgieva:

Papua New Guinea has continued a wide-ranging program of reforms, supported by the International Monetary Fund (IMF) and other international partners. This reform focus has allowed us to make significant strides in lifting the performance of the economy including starting to address some issues that have been outstanding for too long. These have comprised improving governance, including through reform of our state-owned enterprises (SOEs); redirecting economic policy effort towards the rural sector and SMEs; revamping public finance including seeking greater returns from our resources, investing in infrastructure, and containing wage bill expenditure; and restarting growth, especially with central banking reforms to deal with foreign exchange shortages, and crucially our 13 year program of budget repair with a return to budget surplus by 2027 and the option to repay all debt by 2034.

The support from the IMF through our previous Staff Monitored Programs and this program has been valuable in helping focus and build a coalition around our reforms. The previous programs supported us in getting international validation of our efforts and created a momentum for further work. We successfully completed the review of the second Staff Monitored Program, a six-month program, in June 2022, alongside our Article IV consultation with the IMF. This program saw us approve a budget in line with an agreed framework with the IMF, indeed with a lower deficit figure; pass our Tax Administration Act (TAA) amendments through Parliament to give it effect; strengthen the public debt committee; and prepare a staffing and establishment report as the groundwork for future payroll reforms. We also met all our quantitative targets, including on the deficit (recording a deficit that was 9 percent lower than our target), reserves (exceeding the target by 62 percent), and other areas.

Under the current Extended Fund Facility (ECF) and Extended Credit Facility (EFF) arrangements, we have continued to make significant strides in progressing our reform agenda to ensure sustainable growth and poverty reduction especially for rural areas. We have continued our progress on budget repair, overperforming against our mid-year deficit target by over K200 million, and have done it with an eye to maintaining the historically high level of capital investment that our country needs to build the connections between our major cities. In addition, on debt management, we successfully implemented the Guarantee Policy, upgraded the Commonwealth Debt Recording System to Meridian, and are finalizing the annual Debt Bulletin. We are also progressing on amendments to the Income Tax Act (ITA) and the Central Banking Act (CBA) and nearing the completion of regulations for the ICAC Act. During our engagement with the IMF, we have also made great strides in improving the financial reporting of our SOEs, and their governance arrangements. We have made further headway in controlling our salaries, and conducted a set of successful workshops with agencies to clearly set out arrangements and rules around salaries and payments. We have developed a comprehensive roadmap for the Bank of Papua New Guinea (BPNG) to address FX shortages and restore Kina convertibility, and strengthened the national governance framework by kickstarting the operationalization of the Independent Commission Against Corruption (ICAC). As of end-June 2023, all quantitative performance criteria were met. All structural benchmarks were also met in timely fashion, except for one, which was implemented with a slight delay. We remain committed to our targets and value our collaboration with the IMF. We have maintained consistent and timely reporting and engagement with the IMF. While much remains to be done, we have set the groundwork for a strong continuing reform agenda.

Despite tackling some key structural vulnerabilities, there remain many that we are proactively addressing: ensuring adequate financing to maintain our budget repair plan while protecting key social services; continuing governance reforms; dealing with our balance of payments imbalance; moving back towards a freely convertible Kina to help deal with a lack of predictable availability of foreign exchange for the private sector; and addressing an ongoing vulnerability to the effects of climate change for many parts of our country. Accordingly, our reform priorities will center on improving our cash management processes and ensuring we can control expenditures, for which we have requested IMF technical assistance; and raising domestic revenue. As a first step towards these we plan to pass amendments to the Income Tax Act to strengthen revenue mobilization; improve performance and governance arrangements at the Internal Revenue Commission; and complete cleansing of payroll records. We will also continue implementation of the monetary policy and exchange rate policy frameworks, as set out in our reform roadmap, and submit to Parliament further reforms to the CBA. And we will continue supporting the full operationalization of the ICAC and further improvements in governance and transparency. These will be the focus of our program, as set out in the attached Memorandum of Economic and Financial Policies (MEFP) and Technical Memorandum of Understanding (TMU).

Given our stronger-than-expected performance and steadfast commitment to our program objectives, we are adjusting the targets we had set for ourselves for net international reserves and the present value of new external debt for end December 2023. As well as in our supplementary budget we have adjusted the targets for the budget deficit.

We are confident that our policies are adequate to achieve the objectives of the program and will take any additional measures that may become appropriate for this purpose. We will consult with the IMF on the adoption of these measures, and in advance of any revision contained in the MEFP, in accordance with the IMF's policies on such consultation and will refrain from any policy that would not be consistent with the program's objectives and our commitments herein. Moreover, we will provide all information requested by the IMF to assess implementation of the program.

We request the completion of the First Review under the ECF and EFF arrangements and the release of the related purchase and disbursement. Upon approval of this request by the IMF Executive Board, we are requesting an immediate disbursement of SDR 65.81 million (25.0 percent of quota), of which SDR 21.94 million (8.3 percent of quota) under the ECF and SDR 43.87 million (16.7 percent of quota) under the EFF. This disbursement under the ECF/EFF program will help address balance of payments and budget financing needs, while smoothly achieving the next stage of our reform plan.

Underscoring our ongoing commitment to transparency, we consent to the publication of this letter, the MEFP, TMU and related board documents.

Yours Sincerely,

/s/

Hon. James Marape
Prime Minister of the Independent State of Papua New Guinea

/s/

Hon. Ian Ling-Stuckey, CMG. MP.

Treasurer of the Independent State of Papua New Guinea

/s/

Ms. Elizabeth Genia

Acting Governor, Bank of Papua New Guinea

c.c. Mr. Robert Nicholl, Executive Director for Papua New Guinea
Mr. Krishna Srinivasan, Director, Asia and Pacific Department

Attachment I. Memorandum of Economic and Financial Policies

A. Economic Developments and Outlook

1. **The Papua New Guinea (PNG) economy has seen strong growth since 2021, supported by the non-resource sector.** Real non-resource gross domestic product (GDP) growth has been strong since 2021 (4.8 percent in 2021, and 4.6 percent in 2022 and 2023), thanks to the reopening of the economy and recovery in the services sector. The resource sector is estimated to have grown by 3.7 percent in 2022, driven by mining and LNG production, but is expected to contract by 1.4 percent in 2023, as LNG production normalizes. Inflation slowed between Q3 2022 and Q2 2023, thanks to our March 2022 fiscal package to address the rising cost of living from inflationary shocks triggered by the Ukraine war. End-of-period inflation stood at 3.4 percent in 2022 and is projected to remain low at 3.5 percent in 2023 by the sustained effect of education subsidies in Q1 2023 and moderating global commodity and freight prices. In light of consistently falling inflation over the past quarters and of the appreciation of our nominal effective exchange rate, the Kina Facility Rate (KFR) has been lowered to 3 percent (from 3.5 percent) in September 2023.

2. **Excluding expected new resource projects, real growth is forecast at 5.0 percent in 2024, while inflation is expected to pick up.** The anticipated resumption of the Porgera mine is expected to boost resource sector growth (6.3 percent), while growth in the non-resource sector should remain strong at 4.6 percent, driven by the agriculture, forestry and fisheries (AFF) and service sectors, as well as by construction from the Connect PNG investment program. End-of-period headline inflation is projected to be 5.0 percent in 2024, as the base effect of our fiscal package fades.

3. **Over the medium term, we expect growth to be sustained on the back of higher private investment, supported by the government's public investment program (PIP).** The economy is projected to grow at an average 3.1 per cent annually, as mining production returns to normal and the non-resource sector is supported by increased production in the AFF sector, by the PIP – including the Connect PNG program, and by private sector investment.

4. **We recognize that the external environment is uncertain but there are both downside and upside risks to the outlook for growth, exports and the fiscal picture.** Downside risks largely stem from a sharp downturn in our main trading partners, tighter global financial conditions and exposure to natural disasters and climate change. However, we have been conservative in our baseline by excluding large extractive sector projects in the pipeline and with a high probability of approval. These projects would have a large positive impact on growth, investment, and, in the medium term, on exports and fiscal revenues.

B. The Government's Medium-Term Economic and Financial Reform Program

5. **PNG continues to face large developmental and financing needs.** Poverty remains high, with most of our people living in rural areas, with limited access to basic infrastructure and services.

We urgently need to invest in basic infrastructure, particularly power, utilities and transport links, as well as in the provision of critical social services such as education, health care and security. However, we also face constraints that necessitate continued reforms. Our public debt had been increasing even before the pandemic, rising from K8 billion in 2012, to K34 billion in 2019, with an attendant increase in payment arrears. This was worsened by the COVID-19 pandemic, which led to a major reduction of 20 per cent in domestic revenues. A 13-year fiscal reform plan has been put in place to reduce budget deficits and public debt ratios. This calls for hard choices as we seek to direct our resources to where the needs are greatest, namely addressing gaps in the delivery of critical social services, closing the infrastructure deficit, enhancing financial development and inclusion and strengthening the business climate to encourage investment and growth. Over time, progress in these areas will be the most durable way to reduce poverty and improve inclusion.

6. Our structural reform agenda is geared to preserve macroeconomic stability, foster sustainable growth and address our development needs. To that effect, we prioritize continuing budget repair, strengthening debt sustainability, ensuring growth in social spending to increase provision of service, addressing FX shortages and strengthening the overall governance framework in PNG.

Objectives And Performance Under the IMF-Supported Program

7. The Extended Credit Facility and Extended Fund Facility (ECF/EFF) arrangements approved in March 2023 are enabling us to make progress on our reform agenda to ensure sustainable growth and poverty reduction especially for rural areas. The program aims to ensure that we:

- Continue to make progress on our program of budget repair with the aim of strengthening domestic revenue mobilization, improving the quality and composition of public expenditure, lowering our fiscal deficit and debt to meet the requirements of our Fiscal Responsibility Act, and strengthen overall debt sustainability;
- Further modernize the governance and operations of the BPNG, thereby allowing us to durably address FX shortages and reinstate the convertibility of the Kina; and
- Strengthen the overall governance framework in PNG by operationalizing the Independent Commission Against Corruption (ICAC) and setting in place a program to improve our AML/CFT framework consistent with the Financial Action Task Force (FATF) standards, while ensuring our financial and payments systems are able to facilitate increased efficiencies and financial deepening and inclusion.

The program would contribute to these objectives through both agreement on a series of commitments with the Fund, which will galvanize domestic support, and Fund TA.

8. We started implementing critical reforms from date of program approval. All quantitative performance criteria (QPC) and indicative targets (IT) as of end-June 2023 were achieved (Table 1) and all five structural benchmarks (SB) due by end-August 2023 were met in timely fashion, with the exception of one SB met with delay. Our achievements include the following, in chronological order:

- We held Human Resources (HR) Business Process workshops with most government departments (March 2023), focusing on staffing and remuneration guidelines;
- We formally appointed the Commissioner and two Deputy Commissioners of the Independent Commission Against Corruption (ICAC), a reform that has been outstanding for a significant time (June 2023);
- We produced a sequenced roadmap for reforming monetary and foreign exchange frameworks and operations over the duration of the ECF/EFF programs (August 2023);
- We modernized liquidity management by implementing a fixed rate full allotment auction for the issuance of short-term central bank bills (August 2023).
- We adopted a new medium-term revenue strategy, which will guide our revenue policy and administration reforms through to 2027 (October 2023). This structural benchmark, which was due by end-August 2023, was met with a small delay.

9. We have made notable progress in strengthening debt management. This includes the successful implementation of the Guarantee Policy and its corresponding Guidance note and tools. Presently, efforts are concentrated on several areas. First, the upgrade and migration of the Commonwealth Debt Recording System to Meridian was completed. Simultaneously, the review of the on-lending policy is completed, with the intention of putting in place a strengthened policy framework. Lastly, there is a targeted initiative to enhance the reporting of Guarantees in alignment with the Government Finance Statistics (GFS) format, a project undertaken with the assistance of the Pacific Financial Technical Assistance Centre (PFTAC). Finally, we have completed a draft of the first annual Debt Bulletin, and intend to publish this year.

10. In addition, we are on track to meet the other structural benchmarks set at the time of the ECF/EFF approval and due in the coming months. We are preparing amendments to the Income Tax Act (ITA) with the aim to enhance revenue mobilization. In consultation with the IMF and informed by the Independent Advisory Group (IAG)'s recommendations, we are also preparing amendments to the Central Banking Act (CBA) to address outstanding issues relating to mandate, governance, autonomy, transparency and accountability of the BPNG. We are at an advanced stage in finalizing key implementing regulations to the ICAC Act. Lastly, we are readying the online publication of details on COVID-19 related procurements for years 2020 and 2021.

C. Government Policies Under the IMF-Supported Program

Fiscal Policies

11. Our 2023 Supplementary Budget has slightly reduced our deficit target relative to the initial budget, with limited changes in overall revenue and expenditure. Tax revenue overperformed in the first half of the year, thanks to stronger-than-expected corporate income tax (CIT) and mining and petroleum tax driven by higher profits, although this was partly offset by lower GST collection, due to faster processing of refunds. Consequently, the end-year tax revenue target will be revised upward by K1.4 billion. In contrast, non-tax revenues are projected to underperform overall, driven by lower dividend payments from the resource sector (-K0.7 billion). Overall, we expect a total revenue increase of K0.8 billion relative to the initial budget. We will use this additional revenue to help cover the expected increase in interest expenditure relative to the budget from higher global interest rates (K0.3 billion), provide financial support to PNG Power (K0.2 billion), pay for additional rental and utility costs (K0.2 billion) and allocate additional funds to clearing arrears (K0.1 billion). Our end-year deficit target is also slightly reduced to K4.935 billion (from K4.985 billion) (QPC). We expect to collect at least K12.8 bn of non-resource tax revenue by end-2023 (IT), while ensuring that at least K3.9 bn of priority spending, including social, is executed (IT).

12. In 2024, we intend to continue our consolidation effort, in line with our medium-term budget repair strategy. We will target a deficit of 3.9 percent of GDP in 2024, corresponding to a consolidation effort of 0.5 percentage point of GDP relative to 2023. We will aim to be more ambitious in reduction of expenditures in line with our 13-year plan. Revenue is expected to decline slightly relative to 2023 by 0.1 percentage point of GDP, from an expected fall in resource revenue driven by lower commodity prices, and more efficient processing of GST refunds thanks to the implementation of the GST monitoring system. This reduction will, however, be partly offset by revenue policy measures (+0.4 percentage point of GDP), including the rollout of the GST (Section 65A) to the Extractive and Finance sectors, the introduction of a dividend policy, reforms to sin taxes, and adjustments to income tax rules like fringe and dependent benefits and thresholds, and by the impact of key revenue administration enhancements, such as the modernization of IRC's tax administrative system and the implementation of the TAA. We will continue to rationalize current spending while preserving priority social spending, resulting in a 0.6 percentage point of GDP decline in total expenditure, and will seek to go further as feasible, in line with the 13-year plan objective of a balanced budget by 2027. We remain on track to achieve a balanced budget by 2027, supported by domestic revenue mobilization efforts and enhanced expenditure efficiency, reprioritizing spending in favor of poverty reduction and sustainable development. This will put public debt firmly on a downward trajectory, reducing risks.

13. We recognize our fiscal targets are ambitious but are confident they are reasonable and achievable. An indicative target (IT) is set on non-resource tax revenues, which ensures our focus on revenue mobilization throughout the program. We recognize that our fiscal framework hinges on our ability to carry out successful tax policy and revenue administration reforms that are in line with our new MTRS. We are subject to significant volatility regarding tax and non-tax resource revenue, and there is uncertainty around the amount of dividend payments expected to be remitted in 2023 and 2024. To remain conservative, we have significantly revised down our dividend collection expectations relative to the 2023 Budget. In the event dividend payments or other revenues overperform, we will use the additional amount to accelerate the clearance of the stock of domestic payment arrears, increase priority spending, and possibly reduce the deficit. In the event we experience significant revenue shortfalls, we will undertake expenditure adjustments to meet our fiscal deficit target. As part of the 2024 Budget preparation, we are identifying contingency measures consisting of spending items that could be reappropriated and programs that could be deferred, such as lower-priority investment projects and goods and services; we will communicate these measures to the Fund at the time of the 2024 Budget approval.

14. Improving domestic revenue mobilization remains a key plank of our fiscal reforms, guided by our new Medium-term Revenue Strategy (MTRS). The MTRS, which succeeds the first Strategy that ended in 2022, was prepared with the support of Fund TA, and approved by Cabinet on October 2023 (**SB met with delay**). It is intended to guide our revenue policies and administration reforms through to 2027 and has incorporated inputs from our key revenue collecting authorities including the Internal Revenue Commission (IRC), Customs and Departments of Treasury and Finance. The MTRS will serve as a reference for reform conditionalities for future program reviews. Under the MTRS, reforms will be aimed at broadening the tax base by reducing distortions, and addressing the policies that hinder the effectiveness and efficiency of tax compliance and services. The MTRS has identified several key legislative reforms to enhance tax and non-tax systems, among which are the implementation of the 2017 Tax Administration Act and the promulgation of a revised Income Tax Act (ITA). The ITA rewrite is intended to simplify and modernize our tax system, close loopholes that were not envisaged when the original legislation was prepared and broaden the base in some areas. We expect that the proposed amendments will be submitted to Parliament in November 2023 (**ongoing SB by end-December 2023**). The amended ITA, if successfully passed in Parliament, will enter into force in early 2025, giving time for the IRC to prepare for implementation. The modernization of the IRC and Customs' operations will also contribute to enhancing revenue administration. The IRC adopted its new organizational structure in July 2023 and will produce, in coordination with the IMF, an initial set of key output-based performance indicators to better monitor its administration and related revenue gains (**new SB by end-May 2024**). In addition, to enhance IRC's accountability, we will submit to the Parliament amendments to the Internal Revenue Commission Act 2014, in consultation with the IMF, to establish a Board for IRC's oversight (**new SB by end-October 2024**). Fund TA will continue to assist us in implementing our domestic revenue mobilization reform agenda.

15. While there are pressures to increase spending, we commit to maintaining our plan for budget repair, and reducing the overall spending envelope in real per capita terms while improving spending efficiency. Over the last five years, the budget has shifted to significantly expand the capital investment budget, which has been growing at a faster rate than the recurrent budget. Historic under-budgeting for personnel emoluments (PE), which reached 25 percent in 2018 prior to our budget repair program, has been resolved in 2023: over the first six months of 2023, PE spending has been in line with budget targets at end-June and is expected to remain so until end of year. However, we intend to go further to ensure that salary budgets are realistic and focused on service delivery. Moving forward, the government remains committed to its expenditure rule to reduce the recurrent budget as a share of non-resource GDP. However, we will increase in real terms the funding to recurrent to allow for a greater number of police, teachers and health care workers as part of the operation and maintenance costs stemming from the new capital investment. This process is being managed by providing greater increases in staff funding to these departments, while limiting increases elsewhere, coupled with the payroll reform efforts that include upgrades to the payroll system and ensuring staff are recorded under the correct appropriations. This structural realignment has been possible due to improved forecasting and budgeting for compensation of employees, and slower increases in recurrent spending on goods and services, even after allowing for one-off spending in 2020 and 2021 due to the pandemic and in 2022 for the elections. We also tightened the budget envelope for many of our government agencies, with goods and services expenditure being cut by over 40 per cent in non-priority or central agencies, emphasizing the need to spend more effectively in order to make room for other priority items. This does not include cuts to priority social programs included in the operating budget which have been quarantined or long-term fixed commitments like rentals, utilities and other items that cannot be easily reduced in year, to avoid the risk of arrears build up.

16. We have made important enhancements to the 2024 budget process, bringing in new reforms to aid in setting policy in the budget. We are working to assess the appropriate spending balance between the wages, goods and services, and sectoral capital components of sectoral spending, including working with the World Bank and other partners to review spending in the health and education sector with the aim of ensuring that operating funding is sufficient to meet expansion of service needs. We have also made progress developing pressures lists of pre-existing commitments to help determine the level of available resources for the budget. We also brought in the medium-term fiscal framework discussions into the strategic budget committee to help guide budget setting within a top-down limited framework. The aim is to strengthen the policy focus of the budget, enhance spending efficiency and provide early high-level guidance on the orientation of the budget.

17. Based on the findings of recent reviews, we have made headway in enhancing the management and efficiency of payroll expenditure and strengthening HR compliance. We have started implementing the findings of the 2022 Staffing and Establishment Review (SER) for all public sector employees (except teachers). To strengthen compliance with HR rules, in March 2023 we organized HR Business Process workshops on staffing and remuneration guidelines with most government departments (**SB met**). A large component of these workshops was to make departments aware of the importance of comprehensively capturing payroll and retirement information in the AscenderPay (previously called ALESCO) system; an instruction has been sent around from Department of Finance to ensure that all allowances and retirement exit payments - payments made to people upon leaving the public service - are entered each pay period. We also undertook a review of our HR practices and processes with a view to streamlining them to support higher compliance. In addition, we have undertaken the Staffing and Establishment Review for teachers and are in the process of validating the final report. The findings of this review will provide greater clarity on weaknesses in our payroll and HR management processes in the education sector and allow us to formulate and implement additional reforms. Finally, based on the proposals made in the payroll diagnostic review, led by Deloitte at the request of the Parliamentary Committee on Public Sector reforms, we will amend General Orders and HR policies with the aim to unify HR practices throughout government agencies, and will perform thorough data cleansing over current payroll IT records (**new SB by end-August 2024**) ahead of a forthcoming system upgrade.

18. We remain committed to actively verifying and clearing Government arrears accumulated in previous years and preventing new ones from arising. The Arrears Verification (AV) program established in January 2020 allows us to gradually clear the stock of arrears on goods and services. Since its creation, and as of August 2023, the AV Committee has examined claims amounting to K3.1 billion, and successfully verified and paid K1.2 billion. The remaining unverified stock of claims on goods and services under the AV program is K1.96 billion. We will accelerate the clearance process by increasing our budget allocation to the AV program from K300 million appropriated in the 2023 Budget to K400 million in the 2023 Supplementary Budget and a planned K500 million in the 2024 Budget. We also commit to increasing our budget allocation to the AV program in future initial and supplementary budgets, should revenue overperform. As part of our salary reforms work, we have also been clearing historic salary arrears, particularly on retirements and allowances. We also plan to allocate resources to continue clearing outstanding personnel emolument liabilities (stock of K0.6 billion as of end-June 2023). To prevent new domestic arrears from arising, we are requesting FAD TA to assist in strengthening expenditure controls throughout the expenditure chain and enabling more automated, timely and effective monitoring of budget execution. We are committed to not accumulating further payroll arrears and continuing to pay domestic debt on time (IT). We will extend that commitment to arrears on goods and services by the time of the second review, after receiving FAD TA advice.

19. We intend to also reduce our reliance on trust accounts to improve expenditure controls and management. Under our current decentralized framework, payments for a large number of government projects are being carried out through trust accounts in the BPNG and commercial banks, funded by transfers appropriated in the government budget. While we actively monitor and report cash movements on these accounts (consolidated balance of K1.1 billion at end-August 2023), these accounts create challenges for the government's active management of cash and for BPNG's liquidity management. We commit to close all remaining COVID trust accounts (remaining balance of K0.2 billion as of end-August 2023) by end-year 2023; in addition, we will seek FAD advice on how to gradually reduce cash balances on these accounts to optimize government cash management.

20. We are committed to modernizing our cash management practices, including by developing a treasury single account (TSA). To avoid the incurrence of arrears on external debt service payments, we build substantial cash reserves in a debt repayment account (on average K0.5 billion over the first six months of the program), which ensures timely payments but leads to interest charges on the overdraft, while large pockets of cash are idle elsewhere, including in trust accounts. That said, the passage of the Non-Tax Revenue Administration Act (NTRA) has already helped centralize statutory bodies' revenues into the Consolidated Revenue Fund at the BPNG. We will build upon this progress by initiating steps to fully bring government funds from the banking sector to the central bank, paving the way for a TSA. We will request TA from the IMF to assist in the preparation of a reform strategy by end-February 2024 for the implementation of a TSA and for enhanced cash management and forecasting.

21. We will continue to strengthen our debt recording and management capacity and maintain a prudent financing strategy to reduce costs and lower risks. This strategy has included the substitution of costly financing with concessional financing from multilateral and bilateral partners, which has improved PNG's debt profile. To ensure our financing strategy continues to carefully monitor and control risks, we are maintaining present value limits on new public external debt contracted in 2023 and in 2024 (continuous QPC for each year). We also remain committed to the non-accumulation of new external payment arrears during the program period (continuous QPC). More generally, we will continue to ensure that our borrowing plan will be closely linked to the financing needed to execute our budget. In line with our 2023 budget, the 2024 budget will envisage a transparent borrowing program and on-budget spending that allows this link to be easily monitored and tracked. Our future borrowing program will aim to lower the risk of debt distress, which will be closely guided by the results of updated Debt Sustainability Analyses undertaken by the IMF and World Bank, and our upcoming Medium-Term Debt Strategy. On the back of IMF TA, we aim at further developing debt management capacity, with the objective of expanding debt coverage to include SOEs.

Monetary and Exchange Rate Policies

22. We have developed a roadmap for monetary policy and exchange rate reform under the program. Controlling inflation and achieving price stability is at the heart of our monetary policy framework, contributing to maintaining macroeconomic stability. Our families are struggling with the overall high cost of living, and our businesses know that persistent foreign exchange shortages have seriously damaged their prospects to grow and create jobs. Ensuring kina convertibility and an appropriate exchange price for PNG's exports and imports is at the heart of our foreign exchange policy plans. Our roadmap, finalized in August 2023 (**SB met**), approved and formally announced in September as part of the Monetary Policy Statement, contains a series of reforms to be undertaken by the BPNG and other government bodies, to strengthen monetary policy and exchange policy frameworks and operations, to improve cash management and to aid the communication of monetary policy to the public. By helping financial markets develop, enhancing monetary transmission, making the exchange rate more flexible and improving capacity, implementing of this roadmap will lay the foundation for an inflation targeting approach for monetary policy. The roadmap was prepared with the technical support of the IMF and also follows from the work of the Independent Advisory Group (IAG). The consolidated status of progress on the roadmap will be provided to the Board of the BPNG on a monthly basis and shared for information with the IMF. The roadmap is an important commitment that will serve as a reference for reform conditionalities for future program reviews. We will request IMF TA and advice to help with the implementation of key elements of the roadmap.

23. We will implement a *de facto* crawl-like exchange rate arrangement to support the gradual return to kina convertibility by the end of the program. A crawl-like arrangement is an appropriate option to transition back to a more flexible exchange rate, in line with our *de jure* exchange rate regime. The kina has gradually depreciated since May 2023 (-0.8 percent per month against the US$); although there has been a small appreciation on a Trade Weighted basis due to strengthening of the US$. Going forward, the new arrangement will help us durably reduce the structural overvaluation of the kina and allow for gradual and moderate fluctuations. The exchange rate will serve as the nominal anchor for monetary policy to ensure sustainable growth through low and stable inflation. We are close to reaching a final decision on the key parameters of the framework for the crawl-like arrangement, in coordination with the IMF (**new SB by end-November 2023**), which we will implement starting early December 2023. The key parameters include: (i) the anchor currency, (ii) the modalities for the calculation of the rate of crawl (including methodologies on how to measure the exchange rate adjustment needed and how to apply judgment in interpreting the results), (iii) the width of the crawl band, (iv) the pace of regular reviews and updates of the rate of crawl, (v) the strategy for communication of the arrangement to the market and (vi) the modalities for FX interventions to support the arrangement. We will endeavor to fully resolve the misalignment of the kina gradually over the program and restore kina convertibility, which will help enhance the competitiveness of our agricultural exports and thus increase rural income.

24. To ensure a smooth transition, we are committed to a gradual elimination of FX rationing measures. To alleviate FX shortages, we have intervened with a monthly average of US$ 125 million since the beginning of 2023, which is above the indicative floor of the program (IT). However, the economy still faces a persistent mismatch between FX supply and demand; in addition, there is large pent-up FX demand from dividends waiting to be repatriated as well as portfolio external investment from domestic superannuation funds. From the beginning of the implementation of the new exchange rate arrangement, we will strive to carry out our FX interventions in amounts sufficient to clear essential payments. From January 1, 2024, we will monitor this with a new indicative ceiling on the stock of unmet import-related orders in the order book older than two months (**new IT**), replacing the indicative floor on BPNG's FX provision to the market. To avoid a disorderly transition, and as the exchange rate approaches its equilibrium level, we will proceed with a cautious, gradual removal of the FX rationing measures. We will review the current "Enhanced Due Diligence" reporting requirements issued in July 2022 as well as other regulations and directives on the FX market. This review will include the coverage of the requirements for tax clearance certificates on all import-related activities, both goods and services, as well as on BPNG currency purchases and on government payments. As a starting point, to level the playing field in the FX market, we will publish all regulations and directives regarding the FX market on the BPNG website (**new SB by end-December 2023**) and ensure that BPNG does not require a tax clearance certificate to include FX orders related to intercompany loans obtained for import payments in the orderbook (**new SB by end-December 2023**).

25. We will build on the successful implementation of the fixed rate full allotment (FRFA) tender to further enhance liquidity management and improve monetary transmission. Since program approval, BPNG has intensified its efforts to mop up excess liquidity: central bank bills have been issued in higher volumes, a 7-day tenor has been introduced, and the revenues of statutory bodies have been transferred from commercial banks to the central bank. In late August 2023, we have modified our open market operations framework by carrying out our first FRFA auction (**SB met**); a total of K1.9 billion of 7-day central bank bills were issued at our second auction, effectively mopping up most of the excess liquidity. The first FRFA auction was conducted at 2 percent, transitioning from the 7-day rate used prior to the move to the FRFA, but lower than the KFR, currently set at 3.0 percent. In order to enhance the effective transmission of monetary policy, we commit to gradually align the rate of issuance of the 7-day central bank bills with the KFR (**new SB by end-December 2023**). As per our roadmap, in line with international good practice on liquidity management, once the 7-day rate is aligned with the KFR, we will introduce a mid-rate corridor on the KFR, bounded by standing overnight facilities priced at +/- 150 bps around the KFR. We will also enhance the cash reserve requirement framework by introducing reserve averaging and extending the maintenance period by March 2024.

26. To support reform implementation and ensure the independence of the BPNG, we will fill the Governor and Deputy Governors positions and Board vacancies at BPNG by end-November 2023. Appointments have been delayed because of the need to ensure appropriate board composition for future reforms. We commit to fill out remaining Board vacancies and to appoint the Governor and Deputy Governors before the end of the calendar year (**new SB for end-November 2023**).

27. We remain committed to reinforcing the financial independence, mandate and autonomy of the BPNG. In 2023, we moved away from specifying BPNG dividends ex ante. Future dividend payments will be based on BPNG's realized profits, which will be determined after ensuring that BPNG has the financial resources needed to effectively implement monetary policy. We will continue to avoid monetary financing, which will be monitored through a QPC on the BPNG's gross credit to government. We are on track to deliver on our commitment to draft, in consultation with the IMF, and submit amendments to the Central Banking Act (CBA) to Parliament, that will address remaining issues related to mandate, governance, autonomy, transparency, and accountability of the BPNG (**ongoing SB by end-December 2023**). In particular, we will limit the provision of advances to the government; rank the mandates of the BPNG with price stability as the BPNG's primary objective; and clarify the role of the Board in monetary policy formulation. In July 2023, the BPNG underwent an updated safeguards assessment; we remain committed to making progress in implementing its recommendations, as per timelines indicated in the assessment report. This includes the above-mentioned legislative reforms, senior management and Board appointments, and the timely publication of financial statements. While the finalization of BPNG's audited financial statement for FY22 has faced delays due to the late appointment of auditors and the implementation of new IT systems, it will be published shortly, and we are committed to restoring timeliness of publication going forward.

Financial Sector Policies

28. Financial inclusion is critical to PNG's development, but should be balanced with preserving financial stability. In April 2023, the government published its financial inclusion strategy for 2023-2027. It provides a roadmap for PNG to accelerate financial inclusion efforts through collaboration with various stakeholders, international development partners and financial institutions, with the aim to reach 2 million unbanked population by 2027, including 50 percent of women, in particular in rural areas. Key strategic objectives include building financial competency through financial literacy and education, strengthening the regulatory environment, developing efficient digital infrastructure, promoting effective public and private sector engagement, developing an enabling environment for inclusive green finance and deepening financial service delivery through harnessing new emerging technology. We recognize that financial inclusion efforts need to be balanced with financial stability and, not giving up hard-won gains in strengthening our AML/CFT framework. The second phase of the CBA review is ongoing. It is aimed at examining the role of the BPNG as the financial regulator, with a view to supporting the development of the financial sector while maintaining its soundness. IAG's final report is expected by December 2023. The process for the IMF's financial sector stability review (FSSR) has also started, with a full report and recommendations expected for the second half of 2024.

29. We have started enhancing our capacity to analyze and monitor financial stability and have just completed the onsite visit for the APG (Asia/Pacific Group on Money Laundering) AML/CFT mutual evaluation. We have expanded and published our set of financial soundness indicators (FSIs) in accordance with the IMF's 2019 FSI compilation guide, with IMF TA support. We are also readying our first financial stability report, to be released in the coming months. Concurrently, after months of preparation, the APG mutual evaluation onsite visit took place in October 2023. Ahead of the onsite visit, BPNG's Financial Analysis and Supervision Unit (FASU) benefitted from an increase in staff capacity, enabling extensive awareness-raising and training activities with relevant stakeholders. Throughout 2023, FASU also carried out a dozen onsite inspections and off-site reviews of AML/CFT programs to strengthen the effective implementation of PNG's AML/CFT framework.

Governance

30. The Independent Commission Against Corruption (ICAC) is on track to deliver an effective anti-corruption framework, which will support inclusive economic growth. To make the ICAC a fully operational institution in 2024, we have appointed a Commissioner and two deputy Commissioners, all international (**SB met**), and have started recruiting staff, complementing domestic skills with global expertise. We are currently drafting the key implementing regulations to the ICAC law, based on best international practice, to specify processes for ICAC's preventive, investigative and prosecutorial mandates, and to ensure sharing of information across relevant agencies; we are on track to ensure their adoption by the end of the year (**ongoing SB for end-December 2023**). ICAC is also actively developing its internal policies and guidelines, setting up IT systems, developing communication materials for the general public, and enhancing cooperation with relevant anti-corruption bodies, including FASU. Going forward, we will ensure that ICAC receives sufficient budget allocations so that it can effectively deliver on its mandate.

31. We remain committed to strengthening transparency around procurement. As a key part of this, we are actively working to prepare the posting of details of COVID-19 related procurements on the government procurement website, including the names of the entities awarded the contract and their beneficial owners, in line with the commitments under the RCF from April 2020 at least for years 2020 and 2021 (**ongoing SB for end-December 2023**) to ensure full accountability for contracts entered into under emergency procedures. We have also completed an independent report into COVID spending and will share the report with the IMF. For contracts made under normal procurement processes, we will continue to account for these under the audit procedures undertaken by the AGO. We will ensure that the AGO is adequately staffed and funded to carry out its external audit mandate.

32. To enhance fiscal and financial transparency, we will extend the coverage of GFS reporting, and improve consistency of statistics. We have been enhancing our GFS reporting, with Fund support, including by releasing more comprehensive GFS tables in the budget book, and developing fully GFS compliant budget estimates volumes. This work was disrupted due to the issues with the IFMS system, however we intend to continue improving their coverage, so that the fiscal positions of the provincial and SOE sectors are well-reflected in the budget documentation. We continue to improve the quality and timeliness of our data. Recent Fund TA on external sector statistics has allowed us to re-state our BOP data from 2015 to 2022 in line with the recommendations of the 6th Balance of Payments Manual (BPM6). We have started publishing the revised data and will prepare subsequent data in accordance with the updated standard. To continue improving the consistency of external sector statistics with other official statistics, we will initiate an inter-agency group on external sector statistics, including representatives from the NSO, Treasury Department, PNG Customs Service and the BPNG (**new SB by end-June 2024**).

33. We continue improving the governance of state-owned enterprises (SOE). Since amending the legal and policy framework for SOEs with the support of the Asian Development Bank, we have strengthened their overarching financial and corporate governance. All SOEs under the portfolio of Kumul Consolidated Holdings have published their FY22 audited financial statements, most of which by end-June 2023. The appointment of SOE directors is now skill-based and more transparent, and the share of women appointed in executive boards of SOEs has increased. Going forward, we intend to unify and enhance procurement practices across SOEs, continue strengthening financial transparency and accountability, pass a dividend policy through the NEC, and improve the financial sustainability of SOEs while ensuring that Community Service Obligations are properly funded and improving access to public services in rural, remote areas.

Social Protections and Poverty Reduction

34. We remain committed to meeting the most pressing needs of our people, particularly the most vulnerable. In the 2023 Budget, the total allocation (current and capital) directed to the education, health and law and order sectors stood at K5.26 billion, an increase of 12.6 percent over 2022 and 46.9 percent from 2021. Execution after six months has been above the program target (IT). In 2024, we will continue to redirect our expenditure to these priority sectors to ensure we preserve recent gains in alleviating poverty. We will continue to work with our development partners to advance work on strengthening our social safety net programs, delivering better public services to our rural population, addressing urban youth unemployment, improving labor mobility and remove barriers to employment, addressing urgent needs in child nutrition, preventing the spread of communicable diseases, and continuing to support education through our Government Tuition Fee Subsidy scheme. The Government also introduced a Household Assistance package to support incomes during worldwide rises in inflation. This included a rise in the PIT threshold from K17,500 to

K20,000, an expansion of the GTFS to cover project fees for schools, and the temporary removal of excise and GST on fuel, which has now been unwound as prices moderated.

Climate Change

35. Papua New Guinea has vulnerabilities to climate change and needs to build resilience. We rely heavily on agriculture, especially at the subsistence level and for export, which remains vulnerable to shifts in the climate, flooding and extreme weather events. We are ranked 8th among countries for highest disaster risk in the world on the World Risk Report, 2020, that climate change will likely only exacerbate. Challenges persist in Papua New Guinea in understanding the scope of climate vulnerability given both a lack of study of localized historical and future climate conditions, and the limited social data. The World Bank in its 2021 Climate Risk Country Profile noted that hazards such as flash flooding, landslide, and coastal flooding are all likely to intensify. At the same time the population affected by river flooding is projected to double by 2030. The Government is committed to a robust program to tackle climate vulnerability, and the long run impacts of climate change. We are working closely with partners to develop climate mitigation and adaptation programs through the Green Climate Fund; develop green financing standards through the BPNG; and fund the UN Climate and Biodiversity Trust Fund in our 2023 budget. We recognize however that there is a continued and growing need for support in this area.

D. Financing Strategy and Program Monitoring

Financing Strategy

36. The program helps us address an immediate balance of payments need, allowing us to engage with our other development partners and build the buffers needed to support a more flexible exchange rate system. The Fund program is a critical component in reinforcing the Government's commitment to sound macroeconomic policies and needed structural reforms. These policies lay the ground for durable and sustainable growth and allow us to reduce poverty and strengthen inclusion. Further, the program is an important signal to our development partners that PNG is on the path to macro-financial sustainability. More directly, financing from the Fund program allows us to address near-term balance of payments needs, allowing the Government to build and maintain the international reserve buffer needed to safely address the demand-supply mismatches in the FX market; and allow for an ambitious but non-disruptive fiscal consolidation path that preserves needed social spending.

37. To this end, we are targeting an international gross reserves level of US$3.1 billion (6 months of imports) by end-2025. At end-June, our net international reserves (NIR), that is reserves net of IMF financing outstanding, were US$2.8 billion, about US$350 million above the floor set at program approval and we are aiming at a US$2.65 billion target for end-2023[1] (up from US$1.7 billion at program approval) (QPC). To achieve this level of reserves by end-2023, and given the external payment obligations we expect, we estimate our financing needs for the year to be US$662

[1] Including US$0.5 billion corresponding to our SDR allocation, no longer subtracted in our NIR calculation.

million, of which 27 percent will come from disbursements under the Fund program. These disbursements will continue to be channeled toward budget support, thereby allowing us to continue executing spending at a reasonable cost.

Program Monitoring

38. Test dates and program reviews. In line with the normal practice for disbursements under the Poverty Reduction and Growth Trust, we follow a 6-monthly review cycle based on quantitative performance criteria outlined in Table 1. The second, third and fourth reviews will take place on or after March 18, 2024, September 18, 2024 and March 28, 2025. Accordingly, our next three test dates would be December 31, 2023, June 30, 2024 and December 31, 2024 respectively. Subsequent test dates will be set in future program reviews. Further, we propose the inclusion of additional indicative targets for the interim periods (assessment dates of March 31, 2024 and September 30, 2024) to help guide program implementation. Tables 1 and 2 outline our proposed quantitative performance criteria, indicative targets and structural benchmarks for the next 12 months. Detailed definitions of the quantitative performance criteria and indicative targets are provided in the attached Technical Memorandum of Understanding.

39. Data and information sharing, and program coordination. The Program Monitoring Committee is active and allows to coordinate PNG's interactions with staff and the Fund. It holds regular meetings with Fund staff, at least every two weeks (and more if needed), to appraise them of developments, provide updates on data and program performance and request assistance from the Fund. Internally, the Committee, chaired by the Secretary of the Treasury, coordinates activities in PNG related to the program by bringing together the main stakeholders. In addition, we remain in close and frequent contact with the IMF Resident Representative on both program and other issues.

Table 1. Papua New Guinea: Quantitative Performance Criteria and Indicative Targets for 2023 and 2024

(In millions of Kina unless otherwise specified)

	2022 December	2023 March		2023 June		2023 September	2023 December		2024 March		2024 June	2024 September	2024 December
		Indicative target		Test date		Indicative target	Test date		Indicative target		Test date	Indicative target	Test date
	Est.	Approved	**Outcome**	Approved	**Outcome**	Approved	Approved	**Proposed revision**	Approved	**Proposed revision**	Proposed	Proposed	Proposed
A. Quantitative performance criteria[1]													
Fiscal deficit of the government[2] (ceiling, cumulative from the beginning of the year)	5,985	1,646	**449**	3,092	**2,858**	4,239	4,985	**4,935**	1,586	**1,586**	3,014	4,132	4,810
Stock of net international reserves of the BPNG (floor, US$ millions)[3]	3,226	2,845	**2,996**	2,463	**2,831**	2,082	1,700	**2,650**	1,525	**2,500**	2,350	2,200	2,050
BPNG's gross credit to government (ceiling)	2,051	2,400	**1,913**	2,400	**2,032**	2,400	2,400	**2,400**	2,400	**2,400**	2,400	2,400	2,400
B. Continuous quantitative performance criteria (ceilings)[4]													
New external payment arrears of the government (ceiling, US$ millions)	0	0	**0**	0	**0**	0	0	**0**	0	**0**	0	0	0
Present value of new external debt contracted or guaranteed by the government[5] (ceiling, US$ millions)	-	1,405	**0**	1,405	**60**	1,405	1,405	**943**	-	**1,072**	1,072	1,072	1,072
C. Indicative Targets													
Non-resource tax revenue of the government (floor, cumulative from the beginning of the year)	10,831	2,512	**2,787**	5,023	**5,900**	9,167	12,558	**12,741**	2,807	**2,935**	5,871	10,714	14,677
New domestic payment arrears of the government (ceiling)[6]							0	**0**	0	**0**	0	0	0
Social and other priority spending (floor, cumulative from the beginning of the year)[7]	3,678	500	**998**	1,500	**2,069**	2,817	3,866	**3,866**	500	**525**	1,575	2,958	4,059
BPNG provision of foreign exchange to authorized FX dealers (floor, cumulative from the beginning of the year, US$ millions)	878	300	**300**	600	**773**	900	1,200	**1,200**					
Stock of unmet import-related FX orders (ceiling)										**150**	125	100	75

Sources: Papua New Guinea authorities and Fund staff estimates.

[1] Quantitative performance criteria listed under A. and indicative targets listed under C. are assessed as at the end of each reference month above.

[2] Central government until September 2023, Budgetary Central Government from December 2023 - see Technical Memorandum of Understanding for full definition.

[3] In the proposed revisions for end-December 2023 and end-March 2024 targets, as well as the proposed targets for the rest of 2024, the SDR allocation is no longer subtracted in the calculation, in line with the IMF safeguards assessment.

[4] Quantitative performance criteria listed under B. are effective continuously from program approval.

[5] Annual for 2023 and 2024.

[6] Due to an absence of definition in the previous Technical Memorandum of Understanding, this indicative target is measured from December 2023 onwards.

[7] Comprises government spending on health, education and law and order (both capital and operating expenses).

Table 2. Papua New Guinea: Structural Benchmarks (November 2023—October 2024)			
No.	**Measure**	**Purpose/Macro-criticality**	**Implementation date**
	Budget repair		
1.	Introduce amendments to the Income Tax Act to the Parliament aimed at strengthening revenue mobilization, streamlining its operation and ensuring consistency with the Tax Administration Act.	To strengthen domestic revenue mobilization.	End-December 2023
2. Proposed	Develop an initial worksheet of output-based key performance indicators to be applied at IRC's individual, team and division levels.	To enhance revenue administration and increase IRC's organizational productivity.	End-May 2024
3. Proposed	Submit to the Parliament amendments to the Internal Revenue Commission Act 2014, in consultation with the IMF, to establish a Board for IRC's oversight.	To strengthen IRC's governance.	End-October 2024
4. Proposed	Complete data cleansing over current payroll records in the AscenderPay IT system and produce a report on the outcome of the cleansing exercise, shared with the IMF.	To ensure integrity of payroll information and enhance payroll management.	End-August 2024
	Governance and operations of the BPNG		
5.	Submit to the Parliament amendments to the CBA, in consultation with Fund staff, to address the remaining issues related to mandate, governance, autonomy, transparency, and accountability of BPNG and improvements in financial regulation and supervision.	To strengthen BPNG's financial independence and governance and improve the operation of the financial system.	End-December 2023
6. Proposed	Set the parameters for the framework of the crawl-like exchange rate arrangement to be implemented starting in early December 2023: (i) anchor currency; (ii) modalities for the calculation of the rate of crawl; (iii) width of the crawl band; (iv) pace of regular reviews/updates; (v) strategy for communication of the arrangement to the market; (vi) modalities for FX interventions to support the arrangement.	To prepare the shift to a crawl-like exchange rate arrangement and enable the gradual return to kina convertibility by the end of the program.	End-November 2023
7. Proposed	Publish all regulations and directives regarding the FX market on BPNG's website.	To increase transparency and level the playing field in the FX market.	End-December 2023
8. Proposed	Eliminate BPNG's requirement of a tax clearance certificate to include FX orders related to intercompany loans obtained for import payments in the orderbook.	To increase transparency and level the playing field in the FX market.	End-December 2023
9. Proposed	Align the rate used for the issuance of the 7-day central bank bills with the Kina Facility Rate.	To improve monetary policy effectiveness and strengthen the monetary policy transmission.	End-December 2023
10. Proposed	Appoint the Governor and Deputy Governors of the BPNG and fill out all vacancies at the BPNG Board.	To ensure sound governance of the BPNG and facilitate implementation of the roadmap.	End-November 2023
	Governance and Anti-corruption Framework		
11.	Adopt key implementing regulations to the ICAC law.	To specify operational processes for ICAC to meet its preventive, investigative and prosecutorial mandates, and to ensure sharing of information across relevant entities.	End-December 2023

Table 2. Papua New Guinea: Structural Benchmarks (Concluded)

(November 2023—October 2024)

No.	Measure	Purpose/Macro-criticality	Implementation date
12.	Post details (including the names of the entities awarded the contract and their beneficial owners) of COVID-19 related procurements awarded on the government procurement website, at least covering 2020 and 2021.	To improve transparency in public procurement in COVID-related contracts, in line with commitments made under the disbursement under the Rapid Credit Facility.	End-December 2023
13. Proposed	Initiate an inter-agency working group on external sector statistics including representatives from the NSO, Treasury Department, PNG Customs Service and the BPNG.	To improve the consistency of external sector statistics with other official statistics.	End-June 2024

Attachment II. Technical Memorandum of Understanding

This technical memorandum of understanding (TMU) sets out the understanding between the Papua New Guinea authorities and the International Monetary Fund (IMF) regarding the definitions of the performance criteria (PCs) and the indicative targets to be applied under PNG's 38-month Extended Credit Facility/Extended Fund Facility Program (ECF/EFF) spanning from March 2023 to May 2026, and should be read in conjunction with the Memorandum of Economic and Financial Policies (MEFP) that accompanies this TMU. It specifies the quantitative performance criteria and indicative targets on which the implementation of the ECF/EFF will be monitored in the period following completion of the First Review and until September 2024. In addition, the TMU reaffirms the terms and timeframe for transmitting the data that will enable IMF staff to assess program implementation and performance.

A. Assessment Criteria: Quantitative Targets

1. Assessment Criteria have been set as of test dates and performance under the program is assessed against those quantitative targets, unless otherwise specified. Specifically, the Second Review will assess the end-December 2023 test date and the Third Review will assess the end-June 2024 test date, etc. Indicative assessment dates have also been set at end-March 2024 and end-September 2024. The assessment criteria are specified in Table 1 of the MEFP.

Definitions

2. For the purposes of the ECF/EFF program, government is defined as the central government of the Independent State of Papua New Guinea. Central government is defined as the component of general government covered by the national budget and encompasses fundamental activities of the national executive, legislative and judiciary powers. It includes Extra Budgetary Units which have individual budgets not fully covered by the national budget, in particular trust accounts. The budgetary central government is defined as the central government excluding extra budgetary units. The general government represents: the national and provincial governments; the Autonomous Bougainville government; and the commercial and statutory authorities.

3. Exchange rates under the program. For the purposes of this TMU, the value of transactions denominated in foreign currencies will be converted into PNG's domestic currency (PGK) based on the key exchange rates below as of December 31, 2022 (Table 1).

Table 1. Papua New Guinea: Exchange Rates
(End of period, 2022)

PGK/USD	3.524
PGK/AUD	2.387
USD/SDR	1.330

4. Debt is defined for the program purposes in accordance with Executive Board Decision No. 15688-(14/107), Point 8(a) and (b), as published on the IMF website (https://www.imf.org/external/SelectedDecisions/Description.aspx?decision=15688-(14/107)). The term "debt" will be understood to mean all current, i.e. not contingent liabilities, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debts can take various forms; the primary ones being as follows:

(i) loans, i.e., advances of money to the obligor by the lender made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds, debentures, commercial loans and buyers' credits) and temporary exchanges of assets that are equivalent to fully collateralized loans under which the obligor is required to repay the funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements);

(ii) suppliers' credits, i.e., contracts where the supplier permits the obligor to defer payments after the date on which the goods are delivered or services are provided; and

(iii) leases, i.e., arrangements under which property is provided which the lessee has the right to use for one or more specified period(s) of time that are usually shorter than the total expected service life of the property, while the lessor retains the title to the property. For the purpose of these guidelines, the debt is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement excluding those payments that cover the operation, repair, or maintenance of the property.

(iv) Under the definition of debt set out in this paragraph, arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt are debt. Failure to make payment on a contractual obligation that is not considered debt under this definition (e.g., payment on delivery) will not give rise to debt.

5. For the purposes of this ECF/EFF program, debt shall include borrowing by, or that receives guarantees from, the central government and the Bank of Papua New Guinea (BPNG) as set out in paragraph 9. Accumulation of liabilities for the purposes of conducting monetary policy by the BPNG, including the issuance of securities or other marketable instruments such as central bank bills or notes, shall be excluded from the definition of debt.

6. External debt of the government is defined as a debt denominated, or requiring payment, in a currency other than the Kina. For program purposes, a debt and/or guarantee is considered contracted when all conditions for its coming into effect have been met, including approval by the Treasury. The contracting of credit lines with no predetermined disbursements schedules or with multiple disbursements will be also considered as contracting of debt. For the purposes of the program, the definition of "debt" is set forth in point No. 9 of the "Guidelines on Performance

Criteria with Respect to External Debt" (see Decision No. 6230-(79/140) as revised on August 3, 2009 (Decision No. 14416-(09/91)).

For program evaluation, performance criteria under the ECF/EFF have been set (see Table 1 of the MEFP) as follows:

Quantitative Performance Criteria (QPCs)

Ceiling on the Cumulative Fiscal Deficit of the Budgetary Central Government

7. The **fiscal deficit** is calculated on a cash basis, and will be calculated as the **net acquisition of financial assets less net incurrence of financial liabilities** by the budgetary central government from the start of the fiscal year on January 1, as set out in Table E ("Transactions in Assets and Liabilities") in the 2021 Final Budget Outcome published by the Government of PNG.

8. **Net acquisition of financial assets** will be calculated as the net change in domestic financial assets plus the net change in external financial assets of the budgetary central government.

9. **Net incurrence of liabilities** is defined as the sum of the net incurrence of domestic liabilities and net incurrence of external liabilities.

a. **Domestic liabilities** will include debt securities outstanding; loans received from residents of PNG; insurance, pension and standardized guarantee schemes; financial derivatives and employee stock options; and other accounts payable.

b. **External liabilities** will include debt securities outstanding; and loans received from lenders not resident of PNG; and any other liabilities that meet the definition of external debt as set out in paragraph 6 above.

10. **For the purpose of program performance assessment,** the cumulative fiscal deficits at end-June 2023 and December 2023 (PCs) and end-March 2023 and end-September 2023 (ITs) must be smaller than or equal to the amounts specified in Table 1 of the MEFP.

Floor on the Stock of Net International Reserves of BPNG

11. **Net international reserves** (stock) are defined as the difference between gross foreign assets and the use of IMF credit.

12. **Gross foreign assets are defined as the sum of:**

- The BPNG's holdings of monetary gold (excluding amounts pledged as collateral);
- Holding of Special Drawing Rights (SDRs);
- BPNG holdings of convertible currencies in cash or in nonresident financial institutions (deposits, securities, or other financial instruments);
- Papua New Guinea's reserve tranche position with the IMF.

13. Gross foreign assets exclude:

- Any foreign currency claims on residents;
- Capital subscriptions in international institutions;
- Assets obtained through currency swaps of less than three months duration;
- Pledged, swapped, or any encumbered reserve assets, including but not limited to reserve assets used as collateral or guarantees for third-party external liabilities;
- Precious metals other than gold, assets in nonconvertible currencies and illiquid foreign assets.

14. Starting from end-December 2023,[1] **the use of IMF credit includes** the credit outstanding under IMF financing programs with Papua New Guinea (including resulting from the ongoing ECF/EFF program).

15. For the purpose of program performance assessment, the stock of net international reserves at end-December 2023 and end-June 2024 must be equal or greater than specified in Table 1 of the MEFP.

Ceiling on BPNG's Gross Credit to Government

16. BPNG's gross credit to government is defined from December 2023 onwards[2] **as the sum of:**

- government securities held by BPNG at amortized cost, including T-bills and T-bonds,
- advances made by BPNG to the central government excluding temporary advances made within the Temporary Advance Facility (TAF); and
- loans made by BPNG to the central government excluding on-lent IMF or other external financing by BPNG to the government.

17. For the purpose of program performance assessment, BPNG's gross credit to government at end- December 2023 and end-June 2024 must be lower than or equal to the amounts specified in Table 1 of the MEFP.

Continuous Performance Criteria (PCs)

Ceiling on the Present Value (PV) on New External Debt Contracted or Guaranteed by the Government

18. The present value (PV) of any external borrowing by the government is defined as the stream of annual discounted future debt service payments for each loan, using a discount rate of 5 percent.

[1] For the definition prior to December, refer to IMF Country Report No. 23/126.

[2] For the definition prior to December, refer to IMF Country Report No. 23/126.

19. For debts carrying a variable interest rate in the form of a benchmark interest rate plus a fixed spread, the PV of the debt would be calculated using a program reference rate plus the fixed spread (in basis points) specified in the debt contract. The program reference rate for the six-month USD LIBOR is 2.73 percent and will remain fixed for the duration of the program. Where the variable rate is linked to a benchmark interest rate other than the six-month USD LIBOR, a spread reflecting the difference between the benchmark rate and the six-month USD LIBOR (rounded to the nearest 50 bps) will be added. For interest rates on the Australian Dollar, the spread over six-month USD LIBOR is 50 basis points.

20. For the purposes of program monitoring, a continuous ceiling in PV terms will apply to the contracting or guaranteeing of new external debt by the Government or the BPNG. The ceiling applies to debt contracted or guaranteed for which value has not yet been received, including private debt for which official guarantees have been extended.

21. An adjustor of up to 5 percent of the external debt ceiling set in PV terms applies to this ceiling, in case deviations from the performance criterion on the PV of new external debt are prompted by a change in the financing terms (interest, maturity, grace period, payment schedule, upfront commissions, management fees) of a debt or debts. The adjustor cannot be applied when deviations are prompted by an increase in the nominal amount of total debt contracted or guaranteed.

22. For program purposes, a debt is considered to be contracted when all conditions for its entry into effect have been met, including approval by Treasury. Contracting of credit lines (which can be drawn at any time and entered into effect) with no predetermined disbursement schedules or with multiple disbursements will be also considered as contracting of debt.

23. Government debt guarantee means an explicit legal obligation of the central government or the BPNG to service a debt in the event of nonpayment by the borrower.

Ceiling on New External Payment Arrears of the Government

24. For the purposes of the PC on the non-accumulation of new external payment arrears, **external payment arrears of the government** are defined as external debt obligations of the government that have not been paid when due in accordance with the relevant contractual terms (taking into account any contractual grace periods).

B. Other Assessment Criteria

25. During the program period, PNG will not:

a. Impose or intensify restrictions on the making of payments and transfers for current international transactions;

b. Introduce or modify multiple currency practices (MCPs);

c. Conclude bilateral payments agreements which are inconsistent with Article VIII of the IMF Articles of Agreement; and

d. Impose or intensify import restrictions for balance of payments reason.

C. Assessment Criteria: Indicative Targets

26. Indicative targets have been set for the test dates (end-December 2023 and end-June 2024). Indicative targets serve to assess progress under the program but are not binding quantitative criteria under which performance under the program is evaluated. The targets are specified in Table 1 of the MEFP. Targets have also been set at the indicative assessment dates (end-March 2024 and end-September 2024). For the calculation, monitoring and evaluation of the indicative targets, the following definitions will be used:

Definitions and Calculations

27. Non-resource tax revenues of the government are defined in line with the GFSM 2014 and consist of: (i) taxes on income, profits, and capital gains; (ii) taxes on payroll and workforce; (iii) taxes on property; (iv) taxes on goods and services; and (v) taxes on international trade and transactions but shall exclude mining and petroleum taxes.

28. New domestic payment arrears of the budgetary central government are overdue domestic payment obligations of the budgetary central government, owed to entities legally incorporated in Papua New Guinea and residents of Papua New Guinea. They include obligations to domestic service providers but exclude government liabilities to other public sector units. They exclude obligations related to purchases of goods and services. Except in case where the terms and conditions of the transaction stipulate a longer period, payments are deemed to be in arrears when:

- Domestic debt remains unpaid for more than 30 days after the due date stipulated in the agreement between the parties (creditor/debtor).

- Wages or pensions remain unpaid 90 days after their due date.

29. BPNG provision of foreign exchange to authorized foreign exchange dealers is defined as the amount of FX sold by BPNG to banks and other authorized FX dealers in PNG each month, with the intention to assist meeting the FX orders in the market. This indicative target will last be assessed at end-December 2023.

30. The stock of unmet import-related FX orders is defined as the total amount of FX orders related to imports of goods submitted by authorized foreign exchange dealers to BPNG's orderbook more than two months prior to the assessment date. This indicative target will first be assessed at end-March 2024.

31. Social and other policy priority spending is measured on a cash basis and comprises budgetary central government spending in the following areas: health, education and law and order (both capital and operating expenses).

D. Program Monitoring and Data Reporting

32. To facilitate the monitoring of program implementation, the Papua New Guinea authorities shall maintain a Program Monitoring Committee. The committee will be composed of senior officials from the Treasury and the Bank of Papua New Guinea, and shall be responsible for monitoring the performance of the program, informing the Fund regularly, and transmitting the supporting materials necessary for the evaluation of benchmarks. With respect to continuous QTs, the authorities will report any non-observance to the IMF promptly.

33. The Committee will prepare and provide to the Fund staff electronically the following information contained in the data reporting table below.

Table 2. Papua New Guinea: Data Reporting for Program Monitoring

Data Description	Type of Data	Reporting Agency	Reporting Frequency	Reporting Lag
Fiscal Sector				
Net acquisition of financial assets and net incurrence of financial liabilities, consisting of:	Budget operations	Treasury	Monthly	1 month
• External loans disbursed and external debt instruments issued, broken down by type of creditor or holder;	Debt	Treasury	Monthly	1 month
• External loans repaid and external debt instruments redeemed, broken down by type of creditor or holder;	Debt	Treasury	Monthly	1 month
• Domestic financial assets accumulated including deposits at the BPNG or other depository institutions;	Debt	Treasury	Bi-annual	1 month
• External financial assets accumulated, including FX deposits at the BPNG and other depository institutions, including foreign entities;	Debt	Treasury	Bi-annual	1 month
• Domestic loans disbursed;	Debt	Treasury	Monthly	1 month
• Domestic loans repaid;	Debt	Treasury	Monthly	1 month
• Domestic securities issued, broken down by original maturity, by face value and proceeds from issuance;	Debt	Treasury	Monthly	1 month
• Domestic securities redeemed by original maturity;	Debt	Treasury	Monthly	1 month
• Loans or advances from the BPNG (excluding any on-lending of external loans contracted with the Fund or other development partners);	Debt	Treasury	Monthly	1 month
• Any other long-term (exceeding 1 year) domestic liability of the central government.	Debt	Treasury	Monthly	1 month
Opening balance, closing balance, inflows and outflows of government trust accounts at end-month, both consolidated and detailed by trust account.	Cash	Treasury	Monthly	1 month
Payments incurred by the budgetary central government on education, health, and law and order (both capital and current spending).	Debt	Treasury	Monthly	1 month
Stock of domestic arrears: (i) total stock of verified and unverified claims under the Arrears Verification program; (ii) amount of claims verified and paid by the Arrears Verification Committee over the past month.	Domestic Arrears	Treasury	Monthly	1 month

Table 2. Papua New Guinea: Data Reporting for Program Monitoring (Continued)				
Data Description	**Type of Data**	**Reporting Agency**	**Reporting Frequency**	**Reporting Lag**
Table comparing the value of the personnel emolument liabilities incurred and the value of the personnel emolument payments made over the past month.	Domestic Arrears	Treasury	Monthly	1 month
Total non-resource tax revenues received by the central government, consisting of: • taxes on income, profits, and capital gains; • taxes on payroll and workforce; • taxes on property; • taxes on goods and services; and • taxes on international trade and transactions.	Revenue	Treasury	Monthly	6 weeks
Total resource revenue received by the central government, consisting of: • mining and petroleum taxes; • royalties levied on petroleum companies; • mining and petroleum dividends; and • any other resource revenue.	Revenue	Treasury	Monthly	6 weeks
Total non-resource non-tax revenue received by the central government, consisting of: • property income (interest, non-resource sector dividends, rent) • sales of goods and services • fines, penalties and forfeits • any other non-resource non-tax revenue.	Revenue	Treasury	Monthly	6 weeks
Monthly cash plan.	Cash	Treasury	Monthly	1 month
Stock of domestic debt, disbursements, amortization, interest, and other fees and charges; face value, maturity, interest rate, payment schedule and actual payments made over the past month.	Domestic debt	Treasury	Monthly	1 month
Stock of external debt, disbursements, amortization, interest, and other fees and charges; face value, maturity, interest rate, and payment schedule.	External debt	Treasury	Monthly	1 month
Details on amount and terms of disbursed external budget support and project grants and loans.	External debt	Treasury	Monthly	1 month
End of year external debt in U.S. dollars, by creditor, and originating currency.	External debt	Treasury	Monthly	1 month

Table 2. Papua New Guinea: Data Reporting for Program Monitoring (Continued)

Data Description	Type of Data	Reporting Agency	Reporting Frequency	Reporting Lag
Amount of new external debt contracted by Government.	External debt	Treasury	Monthly	1 month
All guarantees provided by the government including guarantees to public corporations and private sector.	External debt	Treasury	Monthly	1 month
Real Sector				
Consumer Price Index.	Economic indicators	NSO	Quarterly	3 months
National Accounts (breakdown of production) in real and nominal terms.	Economic indicators	NSO	Annual	24 months
Agricultural production data (volume/value of major products).	Economic indicators	Treasury	Quarterly	3 months
Mineral production data (volume/value of major products).	Economic indicators	Treasury	Quarterly	3 months
Structural Benchmarks				
Table with a description of the status of implementation of the structural measures in Table 2 of the MEFP.	Structural benchmarks	Treasury	Bi-annual	1 month
Monetary and Financial Sector				
Detailed balance sheet data of the BPNG submitted in the reporting template.	Monetary	BPNG	Monthly	1 month
Amount of government securities held by BPNG at amortized cost	Monetary	BPNG	Monthly	1 month
Cash flows of the Waigani Public Account, Debt Repayment Account, and the Temporary Advance Facility (TAF).	Cash	BPNG	Monthly	1 month
Daily sale of FX (in USD) by the BPNG to authorized FX dealers (detailed by dealer).	FX	BPNG	Weekly	1 week
Depository Corporations Survey.	Monetary	BPNG	Quarterly	3 months
Balance sheets and income statements by financial institutions (aggregate and by bank).	Financial	BPNG	Quarterly	3 months
Outstanding amount of unsatisfied requests for FX purchase to pay for current account (or authorized) transactions.	FX	BPNG	Weekly	1 week

Table 2. Papua New Guinea: Data Reporting for Program Monitoring (Concluded)

Data Description	Type of Data	Reporting Agency	Reporting Frequency	Reporting Lag
Monthly update report on the implementation of the monetary and FX reform roadmap.	Monetary / FX	BPNG	Monthly	1 month
Financial Soundness Indicators (aggregate and by bank).	Financial	BPNG	Quarterly	1 month
Lending activity of banks (by sector).	Financial	BPNG	Monthly	1 month
External Sector				
Balance of Payments data in the reporting template provided by IMF staff.	BOP	BPNG	Quarterly	3 months
Import and export data, by sectors.	BOP	BPNG	Quarterly	3 months
Net international reserves, including reserve assets/liabilities by original currency.	BOP	BPNG	Monthly	1 month
Foreign exchange flow data (by type of flow).	BOP	BPNG	Monthly	1 month
Banks' purchases and sales of foreign currency (specified by bank, sector and by type of flow).	FX	BPNG	Monthly	1 month
List of the foreign exchange allocation pipeline (orderbook) with information about length of time needed to fulfill order and type of orders (especially imports of goods and import-related intercompany loans).	FX	BPNG	Monthly	1 month

INTERNATIONAL MONETARY FUND

PAPUA NEW GUINEA

November 6, 2023

FIRST REVIEWS UNDER EXTENDED ARRANGEMENT UNDER THE EXTENDED FUND FACILITY AND AN ARRANGEMENT UNDER THE EXTENDED CREDIT FACILITY, AND REQUEST FOR MODIFICATION OF QUANTITATIVE PERFORMANCE CRITERIA —DEBT SUSTAINABILITY ANALYSIS

Approved By
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Prepared by the staff of the International Monetary Fund (IMF) and the International Development Association (IDA)

Papua New Guinea: Joint Bank-Fund Debt Sustainability Analysis	
Risk of external debt distress	*High*
Overall risk of debt distress	*High*
Granularity in the risk rating	*Sustainable*
Application of judgment	*No*

Papua New Guinea (PNG) remains at high risk of debt distress under the Low-Income Country Debt Sustainability Framework (LIC DSF), with weak debt-carrying capacity.[1, 2] *While the planned fiscal consolidation helps address debt vulnerabilities exacerbated by the global COVID-19 shock, the risk of both external and public debt distress continues to be assessed as high. Over the medium-term, public debt enters a downward trend and the projected temporary breaches of sustainability indicators can mostly be addressed by debt management operations as well as improvements in revenue generation. The Debt Sustainability Analysis (DSA) suggests that PNG is susceptible to trade-related and contingent liabilities shocks, underscoring downside risks to the debt outlook in a global environment of high uncertainty. To lower the risk of debt distress and ensure debt sustainability, gradual fiscal consolidation, including by boosting revenues, and steadfast structural reforms to promote private sector growth would be needed. Conditional on the implementation of the authorities' plans for further fiscal consolidation and conservative financing strategies, PNG's external and overall debt is judged as sustainable.*

[1] This Debt Sustainability Analysis has been prepared jointly by the International Monetary Fund and the World Bank, in accordance with the revised Debt Sustainability Framework for low-income countries approved by the Executive Boards of the IMF and the International Development Association.

[2] The Composite Indicator (CI) of 2.56 is based on the latest available CI information—April 2023 IMF World Economic Outlook (WEO) and the World Bank's Country Policy and Institutional Assessment (CPIA) for 2021 indicating a "weak" capacity to carry debt.

PUBLIC SECTOR DEBT COVERAGE

1. **The coverage of public debt in the DSA is unchanged from the previous (March 2023) DSA** (Text Table 1). The segments of the public sector captured in the DSA include the central government, state and local government, and guarantees to other entities in the public and private sector, including parts of state-owned enterprises (SOEs). However, debt numbers do not fully capture implicit government guaranteed debts of SOEs and unfunded superannuation liabilities relating to pensions.[3] For the purposes of this DSA, the coverage of public sector debt remains unchanged from the last DSA, which was prepared in March 2023 in the context of the IMF ECF/EFF program request. Given continued difficulties in capturing and assessing SOE risks, a contingent liabilities stress test is included in this DSA, assuming 9 percent of GDP as SOE debt is not captured in official public debt data (the stock of explicit government guarantees is around 1.3 percent of GDP), and 3 percent of GDP for other elements of general government (mainly unfunded superannuation liabilities related to pensions, which are projected to be 2.1 percent of GDP in 2023). Separately, according to the World Bank's PPP database, the PPP capital stock in PNG is zero and, therefore, no default shock is triggered. A financial market shock of 5 percent is added, reflecting the average fiscal cost of financial crisis in low-income countries. With these assumptions, the cumulative shock in the contingent liabilities stress test amounts to 17 percent of GDP—compared to 7 percent under default assumptions. Currency denomination is used to define external debt.

Text Table 1. Papua New Guinea: Coverage of Public Debt

	Subsectors of the public sector	Subsection Covered
1	Central government	X
2	State and local government	X
3	Other elements in the general government	
4	o/w: Social security fund	
5	o/w: Extra budgetary funds (EBFs)	
6	Guarantees (to other entities in the public and private sector, including to SOEs)	X
7	Central bank (borrowed on behalf of the government)	
8	Non-guaranteed SOE debt	

1	The country's coverage of public debt	The central, state, and local governments, government-guaranteed debt		
		Default	Used for the analysis	Reasons for deviations from the default settings
2	Other elements of the general government not captured in 1.	0 percent of GDP	3	Unfunded superannuation liabilities relating to pensions
3	SoE's debt (guaranteed and not guaranteed by the government) 1/	2 percent of GDP	9	SOE sovereign guarantee in dispute
4	PPP	35 percent of PPP stock	0	Default used
5	Financial market (the default value of 5 percent of GDP is the minimum value)	5 percent of GDP	5	Default used
	Total (2+3+4+5) (in percent of GDP)		17	

1/ The default shock of 2% of GDP will be triggered for countries whose government-guaranteed debt is not fully captured under the country's public debt definition (1.). If it is already included in the government debt (1.) and risks associated with SoE's debt not guaranteed by the government is assessed to be negligible, a country team may reduce this to 0%.

[3] Comprehensive data on the debt stock of SOEs in PNG is not publicly available. The ADB have been supporting the authorities with a three-year program (2020-2023) aiming to reform the governance of state-owned enterprises, increase their financial transparency and ensure financial sustainability. This included providing advice on the overarching policy and legal framework for SOEs, leading to the adoption of an amended Kumul Consolidated Holdings Act in 2021.

BACKGROUND ON DEBT

2. Between 2017 and 2022, the stock of public debt in PNG increased from around 24 billion Kina to more than 53 billion Kina. This was mainly due to external loans, while the creditor composition has been gradually shifting away from commercial loans towards official multilateral and bilateral financing (*Text Table 2*). However, expensive commercial loans have generally been replaced with official multilateral and bilateral financing at more favorable conditions. This has helped to improve debt sustainability indicators in the medium-term. Public and Publicly Guaranteed (PPG) external debt figures used for this DSA are consistent with the information in the World Bank's International Debt Statistics.

Text Table 2. Papua New Guinea: Decomposition of Public Debt Service by Creditors[1], 2022-2024

	Debt Stock (end of period) 2022			Debt Service					
				2022	2023	2024	2022	2023	2024
	(In US$ million)	*(Percent total debt)*	*(Percent GDP)*	*(In US$ million)*			*(Percent GDP)*		
Total	14969	100	47	5340	4654	4856	17	15	15
External	7426	50	24	717	408	575	2	1	2
Multilateral creditors[2,3]	3364	22	11	385	184	262	1	1	1
IMF	709	5	2	1	6	6	0	0	0
World Bank	545	4	2	134	33	47	0	0	0
ADB	2015	13	6	244	138	202	1	0	1
Other Multilaterals	95	1	0	6	7	8	0	0	0
Bilateral Creditors[2]	3482	23	11	273	165	265	1	1	1
Paris Club	1907	13	6	181	50	136	1	0	0
o/w: Australia	1397	9	4	172	35	122	1	0	0
Non-Paris Club	1575	11	5	93	115	129	0	0	0
o/w: China EXIM	1174	8	4	68	90	97	0	0	0
Bonds	500	3	2	42	42	42	0	0	0
Commercial creditors	80	1	0	17	17	7	0	0	0
Other international creditors	0	0	0	0	0	0	0	0	0
Domestic	7543	50	24	4623	4247	4281	15	14	13
Held by residents, total	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Held by non-residents, total	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
T-Bills	3479	23	11	3778	3698	3577	12	12	11
Bonds	3216	21	10	669	434	557	2	1	2
Loans	849	6	3	176	114	147	1	0	0
Memo items:									
Collateralized debt[2,4]	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Contingent liabilities	816	5	3	n/a	n/a	n/a	n/a	n/a	n/a
Nominal GDP	31533	n/a	100						

1/As reported by Country authorities according to their classification of creditors, including by official and commercial. Debt coverage is the same as the DSA.

2/Some public debt may not be shown in the table due to confidentiality clauses/capacity constraints.

3/Multilateral creditors" are simply institutions with more than one official shareholder and may not necessarily align with creditor classification under other IMF policies (e.g. Lending Into Arrears)

4/Debt is collateralized when the creditor has rights over an asset or revenue stream that would allow it, if the borrower defaults on its payment obligations, to rely on the asset or revenue stream to secure repayment of the debt. Collateralization entails a borrower granting liens over specific existing assets or future receivables to a lender as security against repayment of the loan. Collateral is "unrelated" when it has no relationship to a project financed by the loan. An example would be borrowing to finance the budget deficit, collateralized by oil revenue receipts. See the joint IMF-World Bank note for the G20 "Collateralized Transactions: Key Considerations for Public Lenders and Borrowers" for a discussion of issues raised by collateral.

3. The IMF's general allocation of Special Drawing Rights (SDRs) became effective in August 2021, with SDR 252 million (US$ 357 million, or 95.7 percent of quota) allocated to PNG. The authorities used the full SDR allocation to support the 2021 budget. They used the SDR allocation to replace costly financing, which has helped reduce the budget deficit. For the purpose of this DSA, the SDR allocation is included in total public debt while the associated debt service for the amount outstanding is also reflected.

4. The new 38-month IMF program, approved by the Board in March 2023 will support PNG's reform agenda, help protect the vulnerable and foster inclusive growth. These facilities total SDR 684.3 million under the IMF's Extended Credit Facility (ECF) and the Extended Fund Facility (EFF) arrangements. The program builds on progress under the past SMPs (2020/21 and 2021/22), focusing on addressing structural impediments to growth and poverty reduction. Program objectives focus on (i) strengthening debt sustainability through a multi-year fiscal consolidation program while making room to meet critical social and development needs, (ii) enhancing the legal and operational framework of the BPNG to alleviate FX shortages and transition to a market-clearing exchange rate, and (iii) build on improvements to governance and the anti-corruption framework.

5. PNG is an IDA blend country, with total IDA20 allocation at SDR 173.7 million. PNG is currently eligible to access the Regional Window, the Crisis Response Windows, and the Private Sector Window. However, PNG is not eligible for SUW-SMLS as the country has a set-aside in place due to unmet FY23 PPAs (see below). The IDA decision to graduate a country to IBRD-only status is based on an assessment of the country's macroeconomic prospects, risk of debt distress, vulnerability to shocks, institutional constraints, and levels of poverty and social indicators.

6. The IDA Sustainable Development Finance Policy (SDFP) supports PNG in addressing key debt vulnerabilities. As part of the SDFP, PNG is subject to debt-related Performance and Policy Actions (PPAs). For fiscal year 2022, these were aimed at limiting non-concessional borrowing and operationalizing the 2021 State Guarantee Policy, both of which were satisfactorily implemented. PNG had two SDFP PPAs for fiscal year 2023: (i) a US$ 1 billion PPG external borrowing limit for new non-concessional long-term contractual obligations, which applies continuously throughout FY23, and (ii) to improve management of fiscal risks by both approving a revised on-lending policy (which introduces credit risks assessments and strengthens enforcement arrangements, recording and reporting requirements) and refraining from any new on-lending until the revised policy is adopted. PNG missed both actions, so the country is subject to a set-aside of 20 percent from its FY24 IDA country allocation. Additionally, due to the breach of the non-concessional borrowing ceiling (NCB) in FY23, PNG is required to implement an additional PPA on fiscal sustainability in FY24. Recovery of the set-aside at the start of FY25 will be contingent on: (i) implementation of FY23 PPA2 (carry-over PPA), (ii) compliance with the NCB ceiling PPA; and (iii) implementation of the PPA on fiscal sustainability in FY24.

BACKGROUND ON MACROECONOMIC FORECASTS

7. Growth in 2023 would be driven by services in the non-resource sector (Text Table 3). After a strong recovery in 2022, real GDP growth is expected to remain elevated at 3.0 percent in 2023, driven by the non-resource sector (4.6 percent). Resource sector growth is forecasted to contract by 1.4 percent. In 2022, average headline inflation was significantly lower than expected at 5.3 percent (3.4 percent, year-on-year by yearend), helped by fiscal measures introduced by the government to address the cost-of-living impact following Russia's invasion of Ukraine and the decrease in seasonal item prices including alcoholic beverages and tobacco in the last quarter of the year. Headline inflation (period-average CPI) is forecasted to moderate to 2.2 percent in 2023, as global commodity prices slow and supply chain constraints ease. Following the transition to BPM6 from BPM5 and Fund TA support (see Annex VII of the SR), the BOP data has been substantially revised leading to a lower current account balance. Consequently, for 2023, the current account balance is expected to be significantly lower, by 5.4 percentage points of GDP, at 18.6 percent relative to the March 2023 projections. This follows the downwardly revised current account surplus of 22.8 percent of GDP in 2022.[4] This is the most substantial change since the 2022 Article IV and SMP review which projected a surplus of 23 percent of GDP. The immediate direct impact of the resource sector windfall on the fiscal balance is expected to be minimal. In 2022, goods exports volumes are estimated to have increased by 6.5 percent compared to 2021, with widespread increases across mineral resource export volumes, including gold, silver, copper and nickel. In addition, buoyant commodity prices in 2022 were supportive of export values, which increased by 49 percent compared to 2021. Expected lower commodity prices in 2023 underpin assumptions for a fall in nominal export growth in 2023.

Text Table 3. Papua New Guinea: DSA Vintages: Macroeconomic and Fiscal Assumptions, 2023-2028

	DSA Vintage	2023	2024	2025	2026-2028
Real GDP growth y/y (in percent)	**2023 ECF/EFF first rev.**	**3.0**	**5.0**	**3.1**	**3.1**
	2023 ECF/EFF program req.	3.7	4.4	3.1	3.1
Resource sector	2023 ECF/EFF first rev.	-1.4	6.3	0.1	0.1
	2023 ECF/EFF program req.	0.3	5.1	0.1	0.1
Non-resource sector	2023 ECF/EFF first rev.	4.6	4.6	4.1	4.0
	2023 ECF/EFF program req.	4.9	4.2	4.2	4.1
Inflation, annual average (consumer prices, percent)	**2023 ECF/EFF first rev.**	**2.2**	**4.0**	**4.8**	**4.6**
	2023 ECF/EFF program req.	5.4	4.9	4.6	4.5
Current account balance (percent of GDP)	**2023 ECF/EFF first rev.**	**18.6**	**16.3**	**16.7**	**12.3**
	2023 ECF/EFF program req.	24.0	22.4	24.8	23.0
Growth of exports of G&S (US$, in percent)	2023 ECF/EFF first rev.	-8.0	4.8	3.6	2.9
	2023 ECF/EFF program req.	-11.2	3.1	2.3	2.7
Growth of imports of G&S (US$, in percent)	2023 ECF/EFF first rev.	-2.5	0.5	3.1	2.9
	2023 ECF/EFF program req.	3.6	1.5	2.6	3.3
Primary balance (percent of GDP)	**2023 ECF/EFF first rev.**	**-1.9**	**-1.5**	**-0.2**	**1.8**
	2023 ECF/EFF program req.	-2.2	-1.2	0.3	2.2
Government revenues (excluding grants, percent of GDP)	2023 ECF/EFF first rev.	16.4	16.4	17.1	17.9
	2023 ECF/EFF program req.	15.3	15.1	15.6	16.0

Source: PNG authorities; IMF staff estimates and projections.

8. **The medium-term baseline macroeconomic forecast is broadly unchanged from the March 2023 DSA** (Text Table 3). At around 3 percent, the long-term potential real growth estimate remains little

[4] Previously published current account data in PNG likely overstated the balance due to long-standing challenges in classifying large income account outflows, including external debt service payments related to resource projects, under the financial account rather than the current account. Fund technical assistance (TA) in external sector statistics aimed at correcting this misclassification, while work is ongoing on improving quality of data. In this regard, authorities aim at initiating an inter-agency working group on external sector statistics including representatives from the NSO, Treasury Department, PNG Customs Service and the BPNG to improve the consistency of external sector statistics with other official statistics by mid-2024.

changed since the March 2023 DSA.[5] Inflation is projected to reach an annual average of 4.6 percent in the medium term. As strong global demand for PNG's export goods is expected to persist over the medium-term, the current account surplus is forecast to remain strong but slightly decrease to around 12 percent of GDP, in the medium-term.

9. The medium-term baseline also assumes rapid progress on fiscal consolidation, as envisaged by the authorities. This is appropriate to strengthen debt sustainability and build a fiscal buffer. While continued primary deficits are anticipated in the short-term (Text Tables 3 and 4), the projection builds in a significant amount of fiscal consolidation and primary surpluses in the second half of the projection period, consistent with the authorities' plans to meet the requirements of the Fiscal Responsibility Act, which specifies government debt should be maintained at no more than 40 percent of GDP over the long term. To contain expenditure growth, the authorities are committed to reducing current expenditure as a share of non-resource GDP, and to enhancing expenditure efficiency through payroll management improvements, stronger expenditure controls, and more efficient cash management practices. Meanwhile, revenue mobilization is a critical component of the planned consolidation in a context of elevated development needs. In the near-term, revenue is expected to increase following the Non-Tax Revenue Act (NTRA), and the updated dividend policy, which is expected to result in higher revenue from the resource sector. Immediate revenue reform priorities include implementation of the Tax Administration Act (TAA) and introducing amendments to the Income Tax Act (ITA). From 2026 onward, the authorities also project an increase in tax revenues from the PNG LNG project as tax exemptions expire. Further, the authorities see scope for significantly higher dividends after loan amortization for the project is completed but this is not yet included in the baseline in full. Achieving a balanced budget by 2027 would lower the risks from significant debt service obligations on external borrowing coming due in 2028.

10. The main downside risks to the baseline projection include: natural disasters, lower global growth, and social or political instability. PNG is vulnerable to natural disasters (flooding, landslides and earthquakes) as well as the impact of climate change (through droughts and sea level rises), and El Ninio.[6] Lower global growth would likely impact PNG through lower commodity prices, with adverse consequences for the balance of payments and budget through lower resource revenue. Although the 2022 general elections were accompanied by several violent disruptions, political and social risks appear to have fallen since then. With limited sources of financing available in an adverse scenario, and continued pressing social and development needs, the room for significant policy adjustment is relatively limited. Engagement with the IMF through the ECF/EFF program provides an important anchor for the authorities to advance their reform agenda. If growth deteriorated significantly compared to the projections, further debt buildup may be needed to finance the budget and maintain government services. Upside risks also exist and include higher-than-expected commodity prices, or start of any of several major projects,

[5] Expected new resource projects are not included in the (authorities' or staff's) baseline, explaining the low resource sector growth in the medium-term. Higher growth in the resource sector due to new projects is therefore a major upside risk to the baseline projection.

[6] Authorities are working closely with partners to develop climate mitigation and adaptation programs through the Green Climate Fund; develop green financing standards through the BPNG; and fund the UN Climate and Biodiversity Trust Fund in our 2023 budget. Moreover, there is a continued and growing need for support in this area.

including Papua LNG, P'nyang LNG or the Wafi Golpu mining, which are not yet in the baseline scenario (see Annex III of the SR).

Text Table 4. Papua New Guinea: Summary of Fiscal Operations, 2023-2025

	2023	2024	2025
Revenue and grants (percent of GDP)	**18.2**	**18.0**	**18.5**
Taxes	14.5	14.5	15.2
Grants	1.8	1.7	1.4
Other revenue	1.8	1.8	1.8
Expenditure (percent of GDP)	**22.6**	**22.0**	**21.0**
Expense	18.5	18.2	17.4
Compensation of employees	6.1	6.2	5.9
Use of goods and services	6.6	6.5	6.3
Interest	2.5	2.5	2.3
Other	3.3	3.1	2.8
Net acquisition of nonfinancial assets	4.1	3.8	3.6
	0.0	0.0	0.0
Gross operating balance	2.2	2.3	3.4
Net lending (+)/borrowing (-)	-4.4	-3.9	-2.5
Primary balance (percent of GDP)	**-1.9**	**-1.5**	**-0.2**

Source: PNG authorities; IMF staff estimates and projections.

11. The LIC DSA's realism tools indicate that the government's primary balance adjustment is moderately ambitious. At about 3.0 percent, the three-year cumulative adjustment of the primary balance is within the top 20 percent of historical experiences, relative to peers. Much of this adjustment has already taken place during 2023 (Figure 4). Baseline growth projection is broadly in line with the implied path consistent with the range fiscal multipliers. A low base, unwinding of Covid-19 and high commodity prices support activity while the Porgera gold mine is expected to reopen in 2024, further contributing to strong growth in the resource sector.

12. Financing mix: For domestic financing, the DSA assumes that the composition of T-bills and T-bonds is broadly similar to the past six years (*i.e.*, 75 percent of new issuances corresponding to T-bills) in the first half of the forecast horizon, but T-bill financing gradually decreases over time. For the near-term, the DSA considers all existing commitments. Although the profile of domestic debt, with a high concentration in short-term Treasury bills, raises concerns over rollover risks, short-term liquidity risks and reliance on domestic financing fall throughout the projection horizon because the level of newly issued debt falls markedly as fiscal deficits are replaced by surpluses, particularly after 2027. While the trend in the projection period remains constant, continued development of the domestic debt market is necessary to increase liquidity and transition towards greater reliance upon domestic financing sources, while shifting to longer maturities.

COUNTRY CLASSIFICATION AND DETERMINATION OF SCENARIO STRESS TEST

13. **PNG's debt carrying capacity is assessed as weak.** According to the April 2023 World Economic Outlook and the 2021 Country Policy and Institutional Assessment (CPIA), PNG's Composite Indicator (CI) is 2.56, indicating weak debt-carrying capacity (Text Table 5).[7] Hence, the applicable thresholds are 30 percent for the present value (PV) of external debt-to-GDP ratio; 140 percent for the PV of the external debt-to-exports ratio; 10 percent for the external debt service-to-exports ratio; 14 percent for the external debt service-to-revenue ratio; and 35 percent for the PV of public debt-to GDP ratio, respectively.

Text Table 5. Papua New Guinea: Composite Indicator and Applicable Thresholds

Components	Coefficients (A)	10-year average values (B)	CI Score components (A*B) = (C)	Contribution of components
CPIA	0.385	2.851	1.10	43%
Real growth rate (in percent)	2.719	2.304	0.06	2%
Import coverage of reserves (in percent)	4.052	55.959	2.27	88%
Import coverage of reserves^2 (in percent)	-3.990	31.314	-1.25	-49%
Remittances (in percent)	2.022	0.002	0.00	0%
World economic growth (in percent)	13.520	2.856	0.39	15%
CI Score			2.56	100%
CI rating			Weak	

Final	Classification based on current vintage	Classification based on the previous vintage	Classification based on the two previous vintage
Weak	Weak 2.56	Weak 2.58	Weak 2.62

Applicable thresholds

APPLICABLE	
EXTERNAL debt burden thresholds	
PV of debt in % of	
Exports	140
GDP	30
Debt service in % of	
Exports	10
Revenue	14

APPLICABLE	
TOTAL public debt benchmark	
PV of total public debt in percent of GDP	35

[7] At 2.56 PNG's CI is close to the weak/medium threshold of 2.69.

14. Scenario stress tests: As indicated in the section on public debt coverage, a contingent liabilities stress test is included to account for SOE debt not captured in official public debt data. [8] Further, given the size and importance of PNG's resource sector (with a share of commodities in total exports of goods and services of 96 percent), a commodity price shock is included in the DSA. Considering the high price volatility over the past few years, the fuel price shock is set at 35 percent (compared to the default shock of 58 percent), and the shock to non-fuel commodity prices is set to 24 percent—with 20 percent for base metals and precious metals, and 31 percent for agricultural commodities other than grain (price shocks to grain like wheat, corn, and soybeans, are not relevant for PNG and, therefore, not included in the stress test). Mitigating factors are included as well, and at default values (2 percent for fuel, and 27 percent for non-fuel). PNG's single outstanding Eurobond (maturing in 2028) activates the market financing module.

DEBT SUSTAINABILITY

A. External Debt Sustainability Analysis

15. Under the baseline scenario, the debt-service to revenue indicator is projected to breach its threshold. A relatively large breach in 2028 arises due to the bullet payment for the US$500 million Eurobond, which was issued in 2018. Marginal breaches arise in 2026, 2027 and 2029 as the debt-service-to-revenue ratio surpasses 14, the threshold value, due to higher official bilateral and multilateral debt service payments given tighter financial conditions, which is falling by 2030. In the baseline scenario, the present value of debt-to-GDP ratio as well as debt-to-exports and debt service-to-export ratios remain below their respective thresholds over the entire projection horizon. The solvency indicators are on a downwards trend in the latter half of the projection.

16. Stress tests point to vulnerabilities in PNG's external debt dynamics particularly with respect to exports shocks, which would cause threshold breaches for all four external sustainability indicators. Changes in policy and the structure of the economy manifests in some differences between the historical and the baseline scenarios. However, with the revision of the BOP data, the historical scenario is now closer to the baseline owing to the reclassification of some current account items. The market financing risk module indicates a moderate risk of heightened liquidity pressures primarily due to elevated GFNs. However, a heightened market stress event would not have a substantial impact of debt burden indicators as few future external debt disbursements are projected on commercial terms (Figure 5). PNG's relatively elevated sovereign spreads (which have dropped by close to 150 basis points since the ECF/EFF approval) likely reflect the perceived risks due to the country's characteristics (small and undiversified export base, small revenue base, vulnerability to shocks).

17. Although residuals remain relatively large, the current DSA shows an improvement to the assessment of debt dynamics with smaller residuals (Table 1 and Figure 3). With support of Fund TA, the recently published BOP data in BPM6 addressed some issues that led to overestimating the residuals,

[8] During the 2021 SMP, the authorities initiated an SOE reform program to reduce the backlog of audited annual financial statements and to strengthen SOE oversight and improve understanding of fiscal risks. This program includes a detailed review of SOE debt and government guarantees and is also expected to improve the reporting of public debt.

such as long-standing challenges in classifying large income account outflows, including external debt service payments related to resource projects, under the financial account rather than the current account. Some data quality issues persist, which likely continue to drive positive residuals from external financial flows which persist into the projection period as a consistent accounting framework is used.

B. Public Sector Debt Sustainability Analysis

18. Public debt PV ratios have increased substantially in recent years and are currently expected to increase to 47 percent of GDP for 2023. Starting from this level means that the public debt sustainability indicator is in breach of the threshold for countries with weak debt-carrying capacity (that is, 35 percent of GDP) during the first half of the projection horizon. Under the baseline scenario, the public debt-to-GDP ratio remains broadly stable just above 52 percent of GDP until 2025, before falling, more markedly in the second half of the projection. This downward trend in the public debt-to-GDP ratio arises through stronger real GDP growth and a smaller fiscal deficit than over the past 5 years, as growth headwinds wane and gradual fiscal consolidation continues (Figure 3). The profile of domestic debt, with a high concentration in short-term Treasury bills, raises concerns over rollover risks. Diversifying the issuance structure by issuing longer term Treasury bonds would lower these risks, make debt service costs more predictable and help with financial deepening effort (Figure 2).[9] In addition, the fall in the level of short-term debt, from a peak of 14.9bn Kina in 2022 to 8.6bn Kina in 2028, is a mitigating factor for liquidity risks. The substantial residuals from unidentified debt creating flows, arising largely in 2018, are not anticipated to be repeated (Figure 3) as the government has taken several steps to improve recording and reporting of debt.[10]

19. Stress tests point to several vulnerabilities for public debt (Figure 2 and Table 4). As for external debt, the most extreme shock impacting the PV of public debt is a shock to exports. Under this shock scenario, the PV of public debt-to-GDP ratio peaks at 62.1 percent of GDP in 2027, more than 1.5 times the 35 percent threshold value and substantially above the starting level of 22.4 percent of GDP in 2023, before gradually decreasing over the next years. The tailored stress test for the combined contingent liability shock causes a deterioration in public debt sustainability which is felt most acutely through the total public debt service-to-revenue measure. This analysis suggests contingent liabilities represent an important source of vulnerabilities in PNG. The trajectory of the PV of the public debt-to-revenue ratio is impacted most by the commodity price shock, reflecting the strong reliance upon commodity exports within PNG.

RISK RATING AND VULNERABILITIES

20. PNG remains at "high" risk of external and overall debt distress. The (mechanical) overall debt distress rating is "high", owing to the multiple breaches of sustainability thresholds under the baseline

[9] Authorities are assessing available options, including debt-for-nature swap operations, with analysis still at an exploratory stage.

[10] This includes the state guarantee policy initiated during the 2021 SMP.

scenario, as discussed in the previous section. Likewise, the external debt distress rating is unchanged from previous DSAs at high risk, given breaches in debt service-to-revenue discussed before.

21. Debt service on existing loans, paired with relatively weak revenue generation, are expected to almost double the debt service-to-revenue ratio by 2025. However, as debt service reduces and revenues increase, and barring further shocks to demand growth, the indicator enters a downward trend from this peak.

22. Stress tests show that adverse shocks to exports, commodity prices and contingent liabilities constitute the main risks to public debt sustainability. Further, the historical scenario indicates that it will be challenging to reduce debt from current levels and that reforms, including those already implemented during the recent SMPs, are essential for supporting the sustainability of public finances. Market financing risks continue to be relevant, with the GFN threshold breached, pointing to moderate market financing pressures.

23. Debt dynamics are assessed as sustainable. Public debt is expected to remain broadly stable in the near-term and to enter a clear downward path over the medium-term. Also, the projected temporary breaches of sustainability indicators can be prevented by debt management operations as well as by boosting revenue generation. External debt-to-GDP and debt-to-exports ratios are below their thresholds over the entire projection horizon. Public external and overall debt is judged to be sustainable conditional on the implementation of the authorities plans for further fiscal consolidation and conservative financing strategies (such as substituting costly financing with concessional financing from multilateral and bilateral partners). This baseline sustainability assessment also relies upon higher future resource revenue as tax exemptions expire from 2026 onwards.

AUTHORITIES' VIEWS

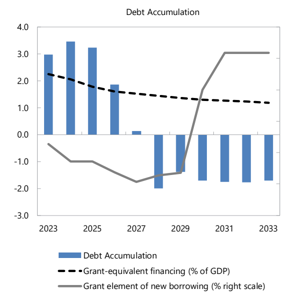
24. The authorities noted the Staff's assessment that PNG remains at high risk of debt distress but remains sustainable under the baseline projection. In discussions, the authorities agreed that large financing requirements to dampen the effects of the COVID-19 pandemic on PNG's economy have left their mark on public debt, and that redemption of the US$ 500 million Eurobond in 2028, issued in 2018, is a key risk. However, the authorities were more optimistic about their debt-carrying capacity and perceived a lower risk of debt distress, pointing to increased revenues by 2027 as debt payments for the PNG LNG project are completed. They highlighted their strategy in recent years to substitute costly financing with concessional financing from multilateral and bilateral partners, which has improved PNG's debt profile. The authorities noted interest costs of domestic securities have fallen over the past two and a half years. They also highlighted the importance of more favorable future contract negotiation and the medium-term revenue strategy as mitigating factors which will reduce risks in the medium-term. The authorities are committed to fiscal consolidation and conservative financing strategies to support the sustainability of PNG's debt going forward.

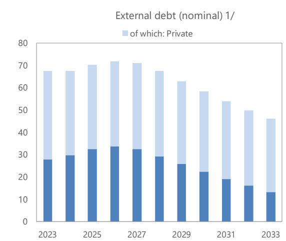
Table 1. Papua New Guinea: External Debt Sustainability Framework, Baseline Scenario, 2020-2043

(In percent of GDP, unless otherwise indicated)

	Actual			Projections																	Average 8/	
	2020	2021	2022	2023	2024	2025	2026	2027	2028	2033	2034	2035	2036	2037	2038	2039	2040	2041	2042	2043	Historical	Projections
External debt (nominal) 1/	69.0	68.5	60.7	67.5	67.5	70.2	71.7	70.9	67.4	46.0	42.7	39.7	37.3	35.2	33.3	31.6	30.0	27.7	25.6	23.8	77.2	62.4
of which: public and publicly guaranteed (PPG)	21.8	24.8	23.6	27.8	29.7	32.4	33.6	32.5	29.2	13.3	10.9	9.0	7.5	6.3	5.3	4.4	3.6	2.9	2.3	1.9	13.9	25.6
Change in external debt	7.3	-0.5	-7.8	6.8	0.0	2.7	1.5	-0.8	-3.4	-3.8	-3.3	-2.9	-2.4	-2.1	-1.9	-1.7	-1.6	-2.3	-2.1	-1.9		
Identified net debt-creating flows	-15.4	-26.1	-39.8	-22.2	-21.9	-21.1	-19.3	-16.3	-14.5	-12.8	-12.6	-12.5	-12.4	-12.4	-12.4	-12.3	-12.3	-12.4	-12.4	-12.4	-15.7	-16.6
Non-interest current account deficit	-17.4	-16.3	-25.2	-19.8	-17.5	-17.8	-15.9	-14.5	-12.8	-11.3	-11.1	-10.8	-10.5	-10.3	-10.1	-9.9	-9.6	-9.4	-9.2	-9.0	-14.3	-14.4
Deficit in balance of goods and services	-16.0	-16.3	-26.4	-24.3	-24.6	-25.1	-25.5	-25.6	-25.4	-21.9	-21.3	-20.6	-20.0	-19.4	-18.9	-18.3	-17.8	-17.2	-16.7	-16.2	-14.2	-24.3
Exports	38.5	43.5	46.1	44.4	43.4	44.2	44.9	45.0	44.8	38.8	37.8	36.7	35.7	34.7	33.8	32.9	32.0	31.1	30.3	29.5		
Imports	22.4	27.2	19.7	20.1	18.8	19.1	19.3	19.4	19.4	16.9	16.5	16.1	15.7	15.3	14.9	14.6	14.2	13.9	13.6	13.3		
Net current transfers (negative = inflow)	-1.1	-1.1	-0.8	-1.0	-0.9	-0.9	-0.9	-0.9	-0.8	-0.6	-0.6	-0.5	-0.5	-0.5	-0.4	-0.4	-0.4	-0.4	-0.3	-0.3	-1.0	-0.8
of which: official	-1.4	-1.7	-1.3	-1.3	-1.2	-1.2	-1.2	-1.1	-1.1	-0.8	-0.8	-0.7	-0.7	-0.6	-0.6	-0.6	-0.5	-0.5	-0.5	-0.4		
Other current account flows (negative = net inflow)	-0.2	1.1	2.0	5.5	8.0	8.1	10.5	11.9	13.4	11.2	10.8	10.4	10.0	9.6	9.2	8.9	8.5	8.2	7.9	7.6	0.9	10.7
Net FDI (negative = inflow)	-3.7	-6.5	-5.7	-1.6	-2.4	-2.3	-2.3	-2.3	-2.2	-1.8	-1.9	-2.1	-2.2	-2.4	-2.6	-2.8	-3.0	-3.2	-3.4	-3.6	-2.4	-2.0
Endogenous debt dynamics 2/	5.7	-3.3	-8.9	-0.7	-2.0	-0.9	-1.0	0.5	0.5	0.4	0.4	0.3	0.3	0.3	0.3	0.3	0.3	0.2	0.2	0.2		
Contribution from nominal interest rate	3.4	3.1	2.4	1.2	1.1	1.1	1.1	2.6	2.6	1.8	1.7	1.6	1.5	1.4	1.3	1.3	1.2	1.1	1.0	1.0		
Contribution from real GDP growth	2.0	0.0	-2.5	-1.9	-3.2	-2.1	-2.2	-2.1	-2.1	-1.5	-1.3	-1.3	-1.2	-1.1	-1.0	-1.0	-0.9	-0.9	-0.8	-0.8		
Contribution from price and exchange rate changes	0.3	-6.4	-8.9	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...		
Residual 3/	22.7	25.6	32.0	28.9	21.9	23.8	20.8	15.5	11.1	9.0	9.3	9.6	10.0	10.3	10.5	10.6	10.7	10.1	10.3	10.5	14.8	15.2
of which: exceptional financing	-1.6	0.0	0.0	-0.6	-0.8	-0.9	-0.3	0.2	0.2	0.3	0.2	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Sustainability indicators																						
PV of PPG external debt-to-GDP ratio	...	...	18.4	22.4	24.2	26.9	28.4	27.9	25.0	11.4	9.3	7.6	6.3	5.2	4.3	3.5	2.8	2.2	1.7	1.2		
PV of PPG external debt-to-exports ratio	...	...	40.0	50.5	55.6	60.9	63.3	61.9	55.8	29.3	24.6	20.6	17.5	15.0	12.7	10.7	8.7	7.0	5.5	4.2		
PPG debt service-to-exports ratio	12.7	8.1	5.3	3.1	3.8	4.9	5.9	6.3	9.6	6.0	5.2	4.5	3.4	2.9	2.5	2.3	2.1	1.9	1.6	1.4		
PPG debt service-to-revenue ratio	37.8	27.6	15.8	8.5	10.0	12.6	15.3	15.7	23.7	11.5	9.9	8.4	6.2	5.1	4.4	3.9	3.5	3.2	2.6	2.1		
Gross external financing need (Million of U.S. dollars)	-2228.1	-3230.2	-7126.1	-3994.9	-4137.9	-4137.1	-4243.4	-2713.0	-1707.9	-3096.4	-3512.1	-3963.2	-4538.6	-5041.4	-5542.7	-6052.1	-6600.3	-7199.9	-7891.7	-8621.7		
Key macroeconomic assumptions																						
Real GDP growth (in percent)	-3.2	0.1	4.3	3.0	5.0	3.1	3.1	3.0	3.1	3.1	3.1	3.1	3.1	3.1	3.1	3.1	3.1	3.1	3.1	3.1	3.8	3.3
GDP deflator in US dollar terms (change in percent)	-0.5	10.3	14.9	-7.3	2.1	-1.2	-1.8	-0.7	0.5	3.1	3.1	3.1	3.1	3.1	3.1	3.1	3.1	3.1	3.1	3.1	0.6	0.7
Effective interest rate (percent) 4/	5.2	5.0	4.2	1.8	1.8	1.7	1.6	3.7	3.8	3.9	3.9	4.0	4.0	4.0	4.1	4.1	4.1	4.0	4.0	4.0	4.8	3.0
Growth of exports of G&S (US dollar terms, in percent)	-18.4	24.8	26.9	-8.0	4.8	3.6	2.9	2.7	3.1	3.4	3.4	3.4	3.4	3.5	3.5	3.5	3.5	3.5	3.6	3.6	10.2	2.4
Growth of imports of G&S (US dollar terms, in percent)	-14.3	34.0	-13.3	-2.5	0.5	3.1	2.7	2.8	3.4	3.6	3.6	3.7	3.7	3.8	3.8	3.8	3.9	3.9	3.9	4.0	-1.9	2.5
Grant element of new public sector borrowing (in percent)	...	...	...	11.3	8.6	8.6	6.9	5.3	6.4	25.9	25.9	25.9	25.9	25.9	25.9	25.9	25.9	25.9	25.9	25.9	...	13.8
Government revenues (excluding grants, in percent of GDP)	12.9	12.8	15.4	16.4	16.4	17.1	17.4	18.0	18.2	20.1	20.0	19.8	19.7	19.6	19.5	19.4	19.2	19.1	19.0	18.9	15.4	18.4
Aid flows (in Million of US dollars) 5/	1736.2	1411.5	1043.1	727.3	678.5	556.8	526.6	531.2	523.0	571.7	589.4	605.2	624.0	642.2	662.2	682.2	703.5	725.1	747.7	770.9		
Grant-equivalent financing (in percent of GDP) 6/	...	...	...	2.3	2.0	1.8	1.6	1.5	1.4	1.2	1.2	1.1	1.1	1.0	1.0	1.0	1.0	0.9	0.9	0.9	...	1.5
Grant-equivalent financing (in percent of external financing) 6/	...	...	...	38.9	34.9	30.3	33.7	50.1	59.4	98.6	98.6	99.3	99.4	99.7	99.7	99.9	99.9	99.9	99.9	100.0	...	66.0
Nominal GDP (Million of US dollars)	23,848	26,312	31,533	30,104	32,268	32,869	33,273	34,044	35,269	48,010	51,065	54,313	57,769	61,444	65,353	69,511	73,933	78,637	83,640	88,961		
Nominal dollar GDP growth	-3.6	10.3	19.8	-4.5	7.2	1.9	1.2	2.3	3.6	6.4	6.4	6.4	6.4	6.4	6.4	6.4	6.4	6.4	6.4	6.4	4.3	4.0
Memorandum items:																						
PV of external debt 7/	...	...	55.6	62.1	61.9	64.7	66.5	66.3	63.2	44.1	41.0	38.3	36.1	34.1	32.3	30.7	29.1	26.9	24.9	23.1		
In percent of exports	...	...	120.6	139.8	142.6	146.4	148.2	147.1	140.9	113.5	108.6	104.3	101.0	98.2	95.7	93.3	91.1	86.5	82.3	78.3		
Total external debt service-to-exports ratio	30.6	24.1	17.9	18.4	16.2	17.2	12.2	19.6	22.7	17.2	16.2	15.1	13.8	13.0	12.4	11.9	11.5	11.0	10.4	9.8		
PV of PPG external debt (in Million of US dollars)			5814.7	6753.2	7796.0	8837.6	9450.4	9496.1	8814.4	5459.5	4747.6	4102.7	3616.0	3195.0	2809.3	2437.8	2066.9	1702.7	1383.9	1100.7		
(PVt-PVt-1)/GDPt-1 (in percent)				3.0	3.5	3.2	1.9	0.1	-2.0	-1.7	-1.5	-1.3	-0.9	-0.7	-0.6	-0.6	-0.5	-0.5	-0.4	-0.3		
Non-interest current account deficit that stabilizes debt ratio	-24.7	-15.8	-17.4	-26.6	-17.5	-20.6	-17.4	-13.7	-9.4	-7.5	-7.7	-7.9	-8.1	-8.2	-8.2	-8.1	-8.0	-7.1	-7.1	-7.1		

Definition of external/domestic debt	Residency-based
Is there a material difference between the two criteria?	No





Sources: Country authorities; and staff estimates and projections.

1/ Includes both public and private sector external debt.

2/ Derived as [r - g - ρ(1+g) + Ɛα (1+r)]/(1+g+ρ+gρ) times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, ρ = growth rate of GDP deflator in U.S. dollar terms, Ɛ=nominal appreciation of the local currency, and α= share of local currency-denominated external debt in total external debt.

3/ Includes exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets; and valuation adjustments. For projections also includes contribution from price and exchange rate changes.

4/ Current-year interest payments divided by previous period debt stock.

5/ Defined as grants, concessional loans, and debt relief.

6/ Grant-equivalent financing includes grants provided directly to the government and through new borrowing (difference between the face value and the PV of new debt).

7/ Assumes that PV of private sector debt is equivalent to its face value.

8/ Historical averages are generally derived over the past 10 years, subject to data availability, whereas projections averages are over the first year of projection and the next 10 years.

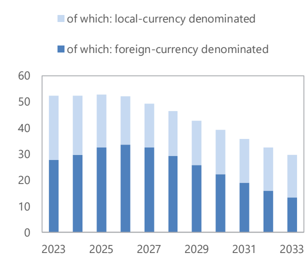
Table 2. Papua New Guinea: Public Sector Debt Sustainability Framework, Baseline Scenario, 2020-2043

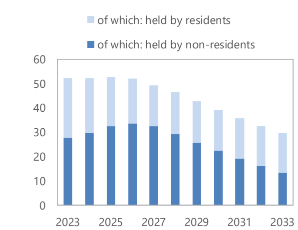
(In percent of GDP, unless otherwise indicated)

	Actual			Projections								Average 6/	
	2020	2021	2022	2023	2024	2025	2026	2027	2028	2033	2043	Historical	Projections
Public sector debt 1/	**48.7**	**52.2**	**48.4**	**52.4**	**52.2**	**52.7**	**52.1**	**49.2**	**46.5**	**29.6**	**14.1**	**37.4**	**44.1**
of which: external debt	**21.8**	**24.8**	**23.6**	**27.8**	**29.7**	**32.4**	**33.6**	**32.5**	**29.2**	**13.3**	**1.9**	**13.9**	**25.6**
Change in public sector debt	8.1	3.5	-3.8	4.0	-1.2	0.5	-0.6	-2.8		-2.9	-0.7		
Identified debt-creating flows	**9.7**	**1.6**	**-3.7**	**0.9**	**-1.3**	**-1.0**	**-1.8**	**-3.2**	**-2.9**	**-2.4**	**-0.7**	**3.2**	**-2.1**
Primary deficit	**6.2**	**4.4**	**3.0**	**1.9**	**1.5**	**0.2**	**-0.9**	**-2.5**	**-2.1**	**-2.0**	**-0.5**	**3.2**	**-1.1**
Revenue and grants	14.7	15.0	16.7	18.2	18.0	18.5	18.8	19.4	19.6	21.3	19.7	**17.2**	**19.8**
of which: grants	1.7	2.3	1.3	1.8	1.7	1.4	1.4	1.4	1.4	1.2	0.9		
Primary (noninterest) expenditure	20.9	19.4	19.7	20.1	19.5	18.7	17.8	16.9	17.6	19.3	19.2	**20.4**	**18.7**
Automatic debt dynamics	**3.5**	**-2.7**	**-6.6**	**-1.0**	**-2.8**	**-1.2**	**-0.9**	**-0.7**	**-0.8**	**-0.4**	**-0.1**		
Contribution from interest rate/growth differential	3.0	-1.2	-5.0	-1.0	-2.8	-1.2	-0.9	-0.7	-0.8	-0.4	-0.1		
of which: contribution from average real interest rate	1.7	-1.2	-2.8	0.4	-0.3	0.4	0.7	0.8	0.7	0.6	0.3		
of which: contribution from real GDP growth	1.3	0.0	-2.2	-1.4	-2.5	-1.6	-1.6	-1.5	-1.5	-1.0	-0.4		
Contribution from real exchange rate depreciation	0.5	-1.5	-1.6	...	...	...	...	...	...	...	...		
Other identified debt-creating flows	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Privatization receipts (negative)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Recognition of contingent liabilities (e.g., bank recapitalization)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Debt relief (HIPC and other)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Other debt creating or reducing flow (please specify)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Residual	**-1.7**	**1.9**	**-0.1**	**3.1**	**1.2**	**1.5**	**1.2**	**0.4**	**0.2**	**-0.5**	**-0.1**	**-0.3**	**0.4**
Sustainability indicators													
PV of public debt-to-GDP ratio 2/	**...**	**...**	**43.3**	**47.0**	**47.2**	**47.7**	**47.4**	**44.9**	**42.6**	**27.8**	**13.4**		
PV of public debt-to-revenue and grants ratio	**...**	**...**	**259.0**	**258.7**	**261.4**	**258.6**	**252.4**	**231.5**	**217.3**	**130.8**	**68.2**		
Debt service-to-revenue and grants ratio 3/	**133.8**	**122.3**	**101.4**	**85.1**	**83.4**	**83.1**	**79.5**	**69.9**	**68.0**	**40.0**	**27.5**		
Gross financing need 4/	25.8	22.7	19.9	17.4	16.5	15.5	14.0	11.0	11.2	6.5	4.9		
Key macroeconomic and fiscal assumptions													
Real GDP growth (in percent)	-3.2	0.1	4.3	3.0	5.0	3.1	3.1	3.0	3.1	3.1	3.1	**3.8**	**3.3**
Average nominal interest rate on external debt (in percent)	11.5	10.7	8.0	2.0	2.6	2.8	3.1	3.3	3.4	3.5	3.6	**18.7**	**3.1**
Average real interest rate on domestic debt (in percent)	-0.4	-9.2	-11.6	3.3	-1.5	0.5	1.7	2.0	1.1	1.8	2.2	**-0.6**	**1.4**
Real exchange rate depreciation (in percent, + indicates depreciation)	2.6	-6.5	-6.8	...	...	...	...	...	...	...	...	**2.4**	**...**
Inflation rate (GDP deflator, in percent)	1.6	11.8	15.2	-1.8	4.2	2.9	1.9	2.2	3.1	3.1	3.1	**5.8**	**2.6**
Growth of real primary spending (deflated by GDP deflator, in percent)	11.1	-7.2	5.9	5.4	1.9	-1.4	-1.4	-2.2	6.9	3.1	3.1	**3.5**	**3.2**
Primary deficit that stabilizes the debt-to-GDP ratio 5/	-1.9	0.9	6.8	-2.1	2.7	-0.3	-0.3	0.4	-2.1	0.9	0.2	**1.9**	**0.4**
PV of contingent liabilities (not included in public sector debt)	0.2	0.2	0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.0		

Definition of external/domestic debt	**Residency-based**
Is there a material difference between the two criteria?	**No**

Public sector debt 1/





Sources: Country authorities; and staff estimates and projections.

1/ Coverage of debt: The central, state, and local governments, government-guaranteed debt . Definition of external debt is Residency-based.

2/ The underlying PV of external debt-to-GDP ratio under the public DSA differs from the external DSA with the size of differences depending on exchange rates projections.

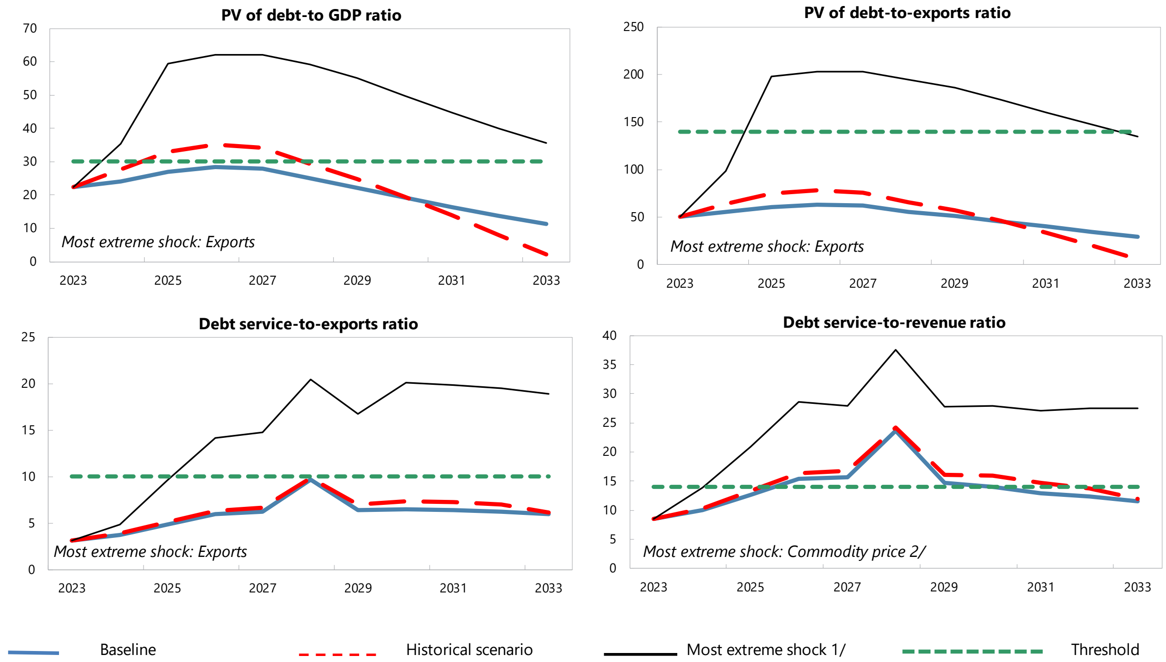
3/ Debt service is defined as the sum of interest and amortization of medium and long-term, and short-term debt.

4/ Gross financing need is defined as the primary deficit plus debt service plus the stock of short-term debt at the end of the last period and other debt creating/reducing flows.

5/ Defined as a primary deficit minus a change in the public debt-to-GDP ratio ((-): a primary surplus), which would stabilizes the debt ratio only in the year in question.

6/ Historical averages are generally derived over the past 10 years, subject to data availability, whereas projections averages are over the first year of projection and the next 10 years.

Figure 1. Papua New Guinea: Indicators of Public and Publicly Guaranteed External Debt Under Alternative Scenarios, 2023-2033



Customization of Default Settings	Size	Interactions
Tailored Stress		
Combined CL	Yes	
Natural disaster	n.a.	n.a.
Commodity price	Yes	No
Market financing	No	No

Note: "Yes" indicates any change to the size or interactions of the default settings for the stress tests. "n.a." indicates that the stress test does not apply.

Borrowing assumptions on additional financing needs resulting from the stress tests*	Default	User defined
Shares of marginal debt		
External PPG MLT debt	100%	
Terms of marginal debt		
Avg. nominal interest rate on new borrowing in USD	4.3%	4.3%
USD Discount rate	5.0%	5.0%
Avg. maturity (incl. grace period)	22	22
Avg. grace period	4	4

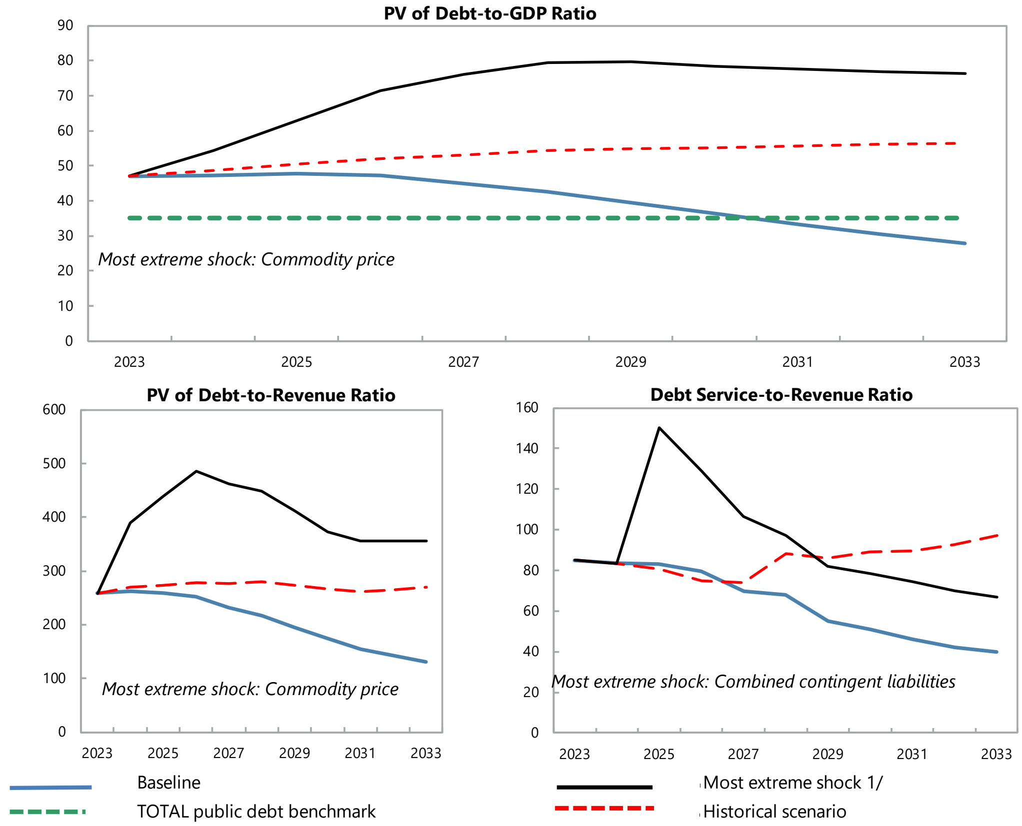
* Note: All the additional financing needs generated by the shocks under the stress tests are assumed to be covered by PPG external MLT debt in the external DSA. Default terms of marginal debt are based on baseline 10-year projections.

Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in or before 2033. The stress test with a one-off breach is also presented (if any), while the one-off breach is deemed away for mechanical signals. When a stress test with a one-off breach happens to be the most exterme shock even after disregarding the one-off breach, only that stress test (with a one-off breach) would be presented.

2/ The magnitude of shocks used for the commodity price shock stress test are based on the commodity prices outlook prepared by the IMF research department.

Figure 2. Papua New Guinea: Indicators of Public Debt Under Alternative Scenarios, 2023-2033



Borrowing assumptions on additional financing needs resulting from the stress tests*	Default	User defined
Shares of marginal debt		
External PPG medium and long-term	12%	12%
Domestic medium and long-term	15%	15%
Domestic short-term	73%	73%
Terms of marginal debt		
External MLT debt		
Avg. nominal interest rate on new borrowing in USD	4.3%	4.3%
Avg. maturity (incl. grace period)	22	22
Avg. grace period	4	4
Domestic MLT debt		
Avg. real interest rate on new borrowing	3.7%	3.7%
Avg. maturity (incl. grace period)	7	7
Avg. grace period	4	4
Domestic short-term debt		
Avg. real interest rate	1.0%	1.0%

* Note: The public DSA allows for domestic financing to cover the additional financing needs generated by the shocks under the stress tests in the public DSA. Default terms of marginal debt are based on baseline 10-year projections.

Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in or before 2033. The stress test with a one-off breach is also presented (if any), while the one-off breach is deemed away for mechanical signals. When a stress test with a one-off breach happens to be the most exterme shock even after disregarding the one-off breach, only that stress test (with a one-off breach) would be presented.

Table 3. Papua New Guinea: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2023-2033

(In percent)

	Projections 1/										
	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033
PV of debt-to GDP ratio											
Baseline	22	24	27	28	28	25	22	19	16	14	11
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	22	28	**33**	**35**	**34**	29	25	19	14	8	2
B. Bound Tests											
B1. Real GDP growth	22	26	**31**	**33**	**32**	29	26	22	19	16	13
B2. Primary balance	22	25	29	**31**	**31**	28	25	23	20	17	15
B3. Exports	22	**35**	**59**	**62**	**62**	**59**	**55**	**50**	**45**	**40**	**36**
B4. Other flows 3/	22	27	**32**	**34**	**34**	**31**	28	24	21	18	16
B5. Depreciation	22	**30**	**37**	**40**	**39**	**35**	**32**	28	24	21	17
B6. Combination of B1-B5	22	**33**	**40**	**42**	**42**	**39**	**35**	**31**	28	24	21
C. Tailored Tests											
C1. Combined contingent liabilities	22	26	**30**	**33**	**33**	**30**	28	25	23	20	18
C2. Natural disaster	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C3. Commodity price	22	**34**	**47**	**53**	**57**	**58**	**58**	**56**	**55**	**53**	**51**
C4. Market Financing	22	27	30	**32**	**31**	28	25	21	18	15	13
Threshold	30	30	30	30	30	30	30	30	30	30	30
PV of debt-to-exports ratio											
Baseline	51	56	61	63	62	56	51	46	40	35	29
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	51	64	75	78	76	65	57	46	34	20	6
B. Bound Tests											
B1. Real GDP growth	51	56	61	63	62	56	51	46	40	35	29
B2. Primary balance	51	57	65	69	68	63	58	53	48	43	38
B3. Exports	51	98	**198**	**203**	**203**	**194**	**186**	**173**	**160**	**147**	135
B4. Other flows 3/	51	62	73	76	75	69	64	58	52	46	40
B5. Depreciation	51	56	67	70	69	63	58	52	46	41	35
B6. Combination of B1-B5	51	78	81	107	105	98	91	84	76	68	60
C. Tailored Tests											
C1. Combined contingent liabilities	51	60	68	72	73	68	64	60	55	51	47
C2. Natural disaster	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C3. Commodity price	51	96	125	134	139	138	137	137	137	137	136
C4. Market Financing	51	56	61	63	62	56	51	46	40	35	29
Threshold	140	140	140	140	140	140	140	140	140	140	140
Debt service-to-exports ratio											
Baseline	3	4	5	6	6	10	6	6	6	6	6
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	3	4	5	6	7	10	7	7	7	7	6
B. Bound Tests											
B1. Real GDP growth	3	4	5	6	6	10	6	6	6	6	6
B2. Primary balance	3	4	5	6	7	10	7	7	7	7	7
B3. Exports	3	5	10	**14**	**15**	**20**	**17**	**20**	**20**	**20**	**19**
B4. Other flows 3/	3	4	5	6	7	**10**	7	8	8	7	7
B5. Depreciation	3	4	5	6	7	10	7	7	7	7	7
B6. Combination of B1-B5	3	4	7	9	9	**13**	**10**	**11**	**11**	**10**	10
C. Tailored Tests											
C1. Combined contingent liabilities	3	4	5	6	7	**10**	7	7	7	7	7
C2. Natural disaster	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C3. Commodity price	3	5	7	10	**10**	**14**	**12**	**13**	**14**	**14**	**15**
C4. Market Financing	3	4	5	6	6	10	6	6	6	6	6
Threshold	10	10	10	10	10	10	10	10	10	10	10
Debt service-to-revenue ratio											
Baseline	8	10	13	**15**	**16**	**24**	**15**	14	13	12	12
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	8	10	13	**16**	**17**	**24**	**16**	**16**	**15**	14	12
B. Bound Tests											
B1. Real GDP growth	8	11	**15**	**18**	**18**	**28**	**17**	**16**	**15**	**14**	13
B2. Primary balance	8	10	13	**16**	**16**	**25**	**16**	**15**	**14**	14	13
B3. Exports	8	11	**17**	**25**	**25**	**34**	**26**	**29**	**27**	**26**	**25**
B4. Other flows 3/	8	10	13	**17**	**17**	**25**	**17**	**17**	**15**	**15**	14
B5. Depreciation	8	13	**16**	**20**	**21**	**31**	**19**	**19**	**18**	**17**	**16**
B6. Combination of B1-B5	8	11	**16**	**20**	**20**	**29**	**21**	**20**	**19**	**18**	**17**
C. Tailored Tests											
C1. Combined contingent liabilities	8	10	13	**16**	**17**	**25**	**16**	**15**	**14**	14	13
C2. Natural disaster	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C3. Commodity price	8	14	**21**	**29**	**28**	**38**	**28**	**28**	**27**	**28**	**27**
C4. Market Financing	8	10	13	**15**	**16**	**24**	**15**	14	13	12	12
Threshold	14	14	14	14	14	14	14	14	14	14	14

Sources: Country authorities; and staff estimates and projections.
1/ A bold value indicates a breach of the threshold.
2/ Variables include real GDP growth, GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.
3/ Includes official and private transfers and FDI.

Table 4. Papua New Guinea: Sensitivity Analysis for Key Indicators of Public Debt, 2023-2033

	Projections 1/										
	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033
					PV of Debt-to-GDP Ratio						
Baseline	**47**	**47**	**48**	**47**	**45**	**43**	**39**	**36**	33	30	28
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	**47**	**49**	**50**	**52**	**53**	**54**	**55**	**55**	**56**	**56**	**57**
B. Bound Tests											
B1. Real GDP growth	**47**	**53**	**60**	**62**	**62**	**62**	**61**	**61**	**60**	**60**	**60**
B2. Primary balance	**47**	**51**	**57**	**57**	**54**	**52**	**49**	**45**	**42**	**39**	**37**
B3. Exports	**47**	**56**	**74**	**74**	**72**	**70**	**66**	**62**	**57**	**52**	**48**
B4. Other flows 3/	**47**	**50**	**53**	**53**	**51**	**49**	**45**	**42**	**38**	**35**	32
B5. Depreciation	**47**	**50**	**49**	**48**	**45**	**41**	**37**	33	29	25	21
B6. Combination of B1-B5	**47**	**49**	**55**	**55**	**53**	**51**	**49**	**46**	**43**	**40**	**38**
C. Tailored Tests											
C1. Combined contingent liabilities	**47**	**64**	**64**	**64**	**61**	**59**	**56**	**52**	**49**	**46**	**43**
C2. Natural disaster	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C3. Commodity price	**47**	**54**	**63**	**71**	**76**	**79**	**80**	**78**	**78**	**77**	**76**
C4. Market Financing	**47**	**47**	**48**	**47**	**45**	**43**	**39**	**36**	33	30	28
TOTAL public debt benchmark	35	35	35	35	35	35	35	35	35	35	35
					PV of Debt-to-Revenue Ratio						
Baseline	259	261	259	252	231	217	195	174	154	142	131
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	259	270	274	279	276	280	273	267	261	265	270
B. Bound Tests											
B1. Real GDP growth	259	292	320	327	316	313	300	287	276	276	278
B2. Primary balance	259	282	309	302	279	264	240	217	196	184	172
B3. Exports	259	312	400	396	373	359	328	294	263	245	227
B4. Other flows 3/	259	277	289	283	261	247	223	199	177	164	151
B5. Depreciation	259	279	268	257	231	211	184	158	133	116	99
B6. Combination of B1-B5	259	274	297	294	274	262	240	219	199	188	179
C. Tailored Tests											
C1. Combined contingent liabilities	259	355	348	340	316	301	275	250	227	215	204
C2. Natural disaster	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C3. Commodity price	259	390	438	485	462	448	411	372	356	356	356
C4. Market Financing	259	261	259	252	231	217	195	174	154	142	131
					Debt Service-to-Revenue Ratio						
Baseline	85	83	83	79	70	68	55	51	46	42	40
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2023-2033 2/	85	83	81	75	74	88	86	89	89	93	97
B. Bound Tests											
B1. Real GDP growth	85	90	102	107	102	105	95	95	93	95	98
B2. Primary balance	85	83	98	111	93	87	71	67	62	59	57
B3. Exports	85	83	85	86	76	74	63	63	57	52	50
B4. Other flows 3/	85	83	84	81	71	69	57	54	48	44	42
B5. Depreciation	85	79	81	78	69	70	55	51	45	41	39
B6. Combination of B1-B5	85	83	86	88	79	78	65	61	57	53	52
C. Tailored Tests											
C1. Combined contingent liabilities	85	83	150	129	106	97	82	78	74	70	67
C2. Natural disaster	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C3. Commodity price	85	112	115	114	118	119	100	90	83	80	83
C4. Market Financing	85	83	83	79	70	68	55	51	46	42	40

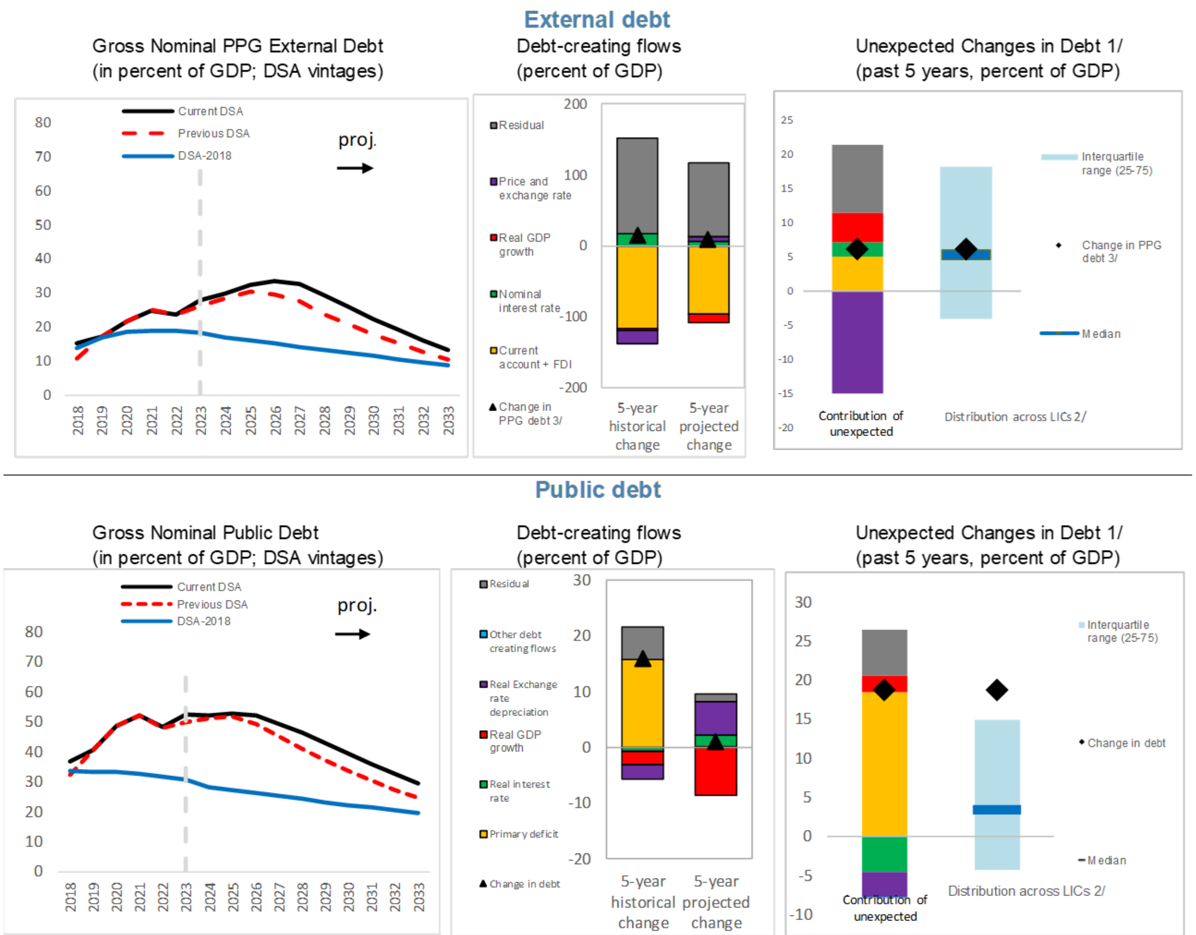
Sources: Country authorities; and staff estimates and projections.

1/ A bold value indicates a breach of the benchmark.

2/ Variables include real GDP growth, GDP deflator and primary deficit in percent of GDP.

3/ Includes official and private transfers and FDI.

Figure 3. Papua New Guinea: Drivers of Debt Dynamics – Baseline Scenario



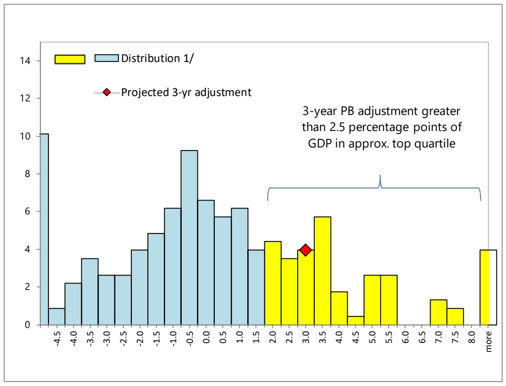
1/ Difference between anticipated and actual contributions on debt ratios.

2/ Distribution across LICs for which LIC DSAs were produced.

3/ Given the relatively low private external debt for average low-income countries, a ppt change in PPG external debt should be largely explained by the drivers of the external debt dynamics equation.

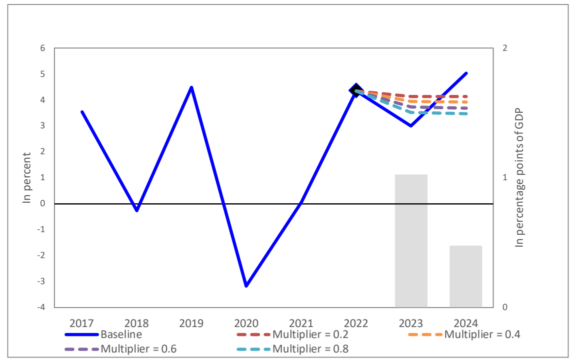
Figure 4. Papua New Guinea: Realism Tools

3-Year Adjustment in Primary Balance
(Percentage points of GDP)



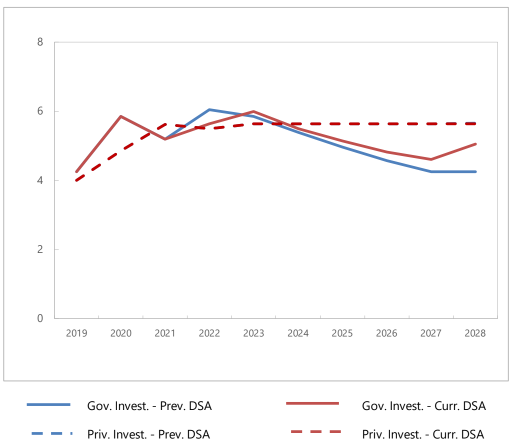
1/ Data cover Fund-supported programs for LICs (excluding emergency financing) approved since 1990. The size of 3-year adjustment from program inception is found on the horizontal axis; the percent of sample is found on the vertical axis.

Fiscal Adjustment and Possible Growth Paths 1/



1/ Bars refer to annual projected fiscal adjustment (right-hand side scale) and lines show possible real GDP growth paths under different fiscal multipliers (left-hand side scale).

Public and Private Investment Rates
(percent of GDP)



Contribution to Real GDP Growth
(percent, 5-year average)

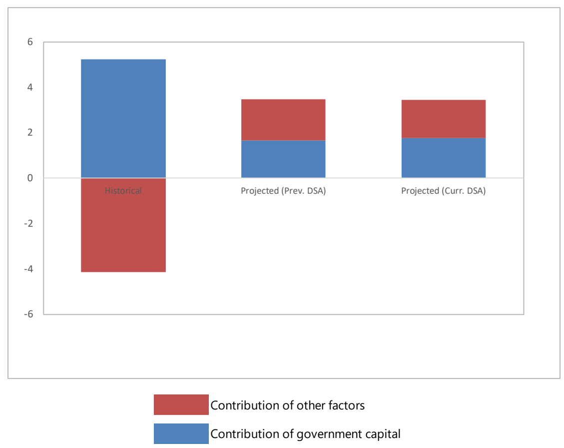
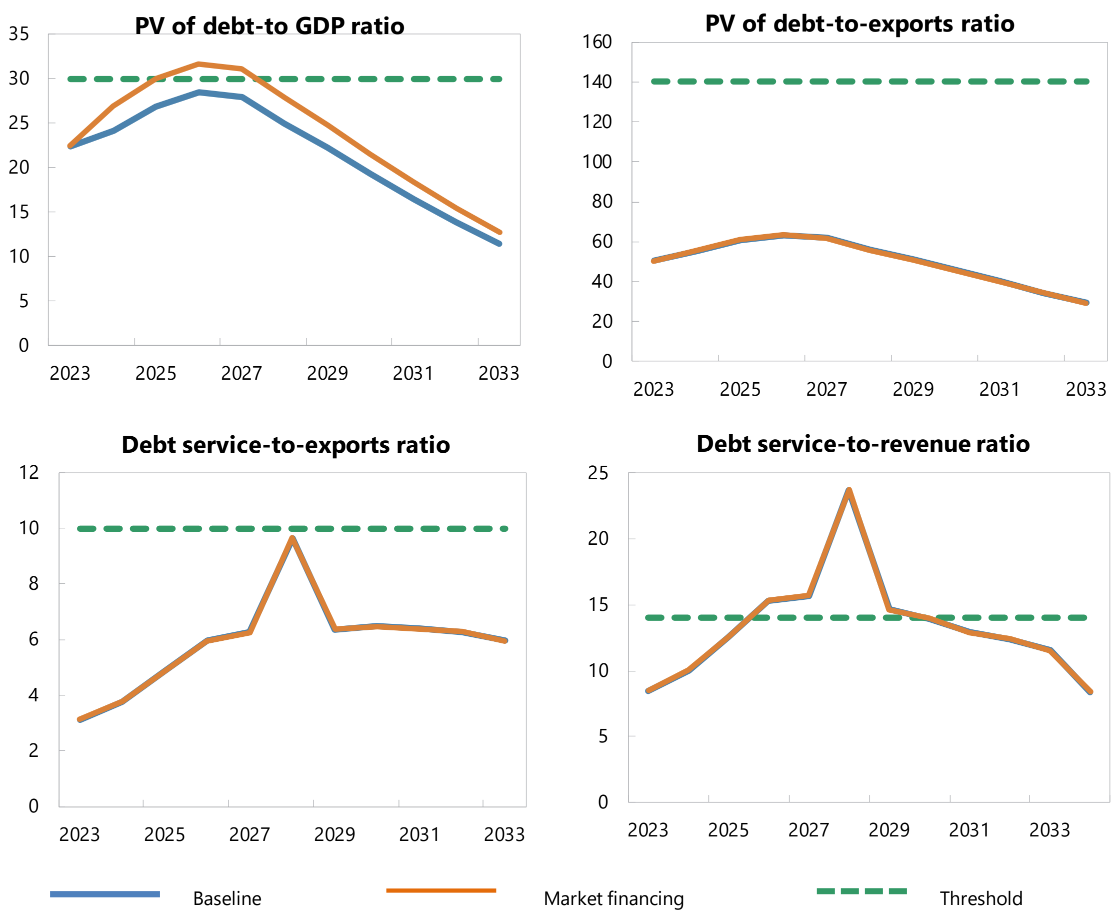


Figure 5. Papua New Guinea: Market-Financing Risk Indicators

	GFN 1/	EMBI 2/
Benchmarks	14	570
Values	17	557
Breach of benchmark	Yes	No
Potential heightened liquidity needs	Moderate	

1/ Maximum gross financing needs (GFN) over 3-year baseline projection horizon.
2/ EMBI spreads correspond to the latest available data.



Sources: Country authorities; and staff estimates and projections.

Statement by the IMF Staff Representative
November 22, 2023

This statement provides a factual update on developments since the Staff Report (SR) was finalized. The additional information does not change the thrust of the staff appraisal.

Program conditionality. The Bank of Papua New Guinea (BPNG) aligned the 7-day central bank bills rate with the Kina Facility Rate, implementing the related end-December 2023 structural benchmark (SB 9) under the program. To achieve this, the BPNG lowered the Kina Facility Rate (KFR) by 0.5 percentage point (from 3.0 to 2.5 percent), while simultaneously increasing the central bank bills rate by 0.5 percentage point (from 2.0 to 2.5 percent). The early implementation of the SB is a welcome step, as it was necessary to improve monetary transmission, avoid conflicting signals on the policy stance, and enable other liquidity management reforms outlined in the roadmap. Now that the two rates are aligned, the KFR will provide a more meaningful indication of the monetary policy stance going forward.

National Accounts. The authorities have recently published the 2021 and 2022 GDP outturns data. Although growth rates for 2021 and 2022 are slightly different than the estimates in the Staff Report, GDP levels are broadly similar leaving main ratios to GDP broadly unchanged.

- In 2021, real GDP growth outturn was -0.8 percent (versus 0.1 percent in the Staff Report). Nominal GDP increased by 11.0 percent (versus 11.9 percent in the Staff Report).

- In 2022, real GDP growth outturn was 5.2 percent (versus 4.3 percent in the Staff Report). Nominal GDP increased by 21.4 percent (versus 20.2 percent in the Staff Report). Nominal GDP was K111.2 billion, which is broadly in line with the estimate in the Staff Report (K111.0 billion).

Statement by Robert Nicholl, Executive Director for Papua New Guinea
Chris Becker, Advisor to Executive Director,
and Rhoda Karl, Advisor to Executive Director
November 22, 2023

We convey the sincere gratitude of our authorities to Mr. Saadi Sedik, the Mission Chief, and his team for their continued close and dynamic engagement since the approval of the blended Extended Credit Facility (ECF) and the Extended Fund Facility (EFF) arrangement, in March 2023. They also extend their gratitude to the MCM and FAD Technical Assistance (TA) teams. The authorities have met all quantitative performance criteria (QPC) and indicative targets (IT) for end-June 2023 and all five structural benchmarks (SB), except for one, which was met after a short delay. This progress demonstrates strong commitment to reforms by the authorities.

Overview

From the outset, the parameters of the program were ambitious, and difficult to achieve given domestic capacity and policy constraints. The successful completion of the first review has been demanding and a challenge to implement politically, with further challenges ahead.

PNG continues to face large development and financing needs. Poverty remains high, with a dispersed population throughout rural areas, and where access to basic infrastructure and services is limited because they are logistically difficult and very costly to provide. There is an urgent need to invest in basic infrastructure, particularly power, utilities, and transport links, as well as extending critical social services such as education and health care for the growing population; all of which are crucial to underpin further economic development. Following the effects of the pandemic and global inflationary pressures, difficult policy choices are focusing on directing resources to where needs are greatest, while maintaining social and political stability and reducing debt vulnerabilities. This is in addition to the structural reforms that are being progressed as part of the program.

The program will also continue to have a catalytic role by attracting resources from other multilateral and bilateral development partners. PNG recognizes that the program reforms are critical to strengthening its policy framework and is fundamental to supporting macroeconomic stability, broad-based growth, and economic resilience. While PNG remains firmly committed to the program objectives, continued strong capacity support from the Fund and other development partners will help PNG implement effectively the challenging reforms over the remainder of the program. However, in this regard the authorities remain aware of the structural improvements these reforms will deliver, even if the benefits will only be realized over time.

The Blended ECF/EFF Program Progress

PNG's financing program was built on the policy objectives of: fiscal consolidation; improved governance; and strengthening of the monetary policy and exchange rate policy frameworks, while addressing prospective balance of payments needs.

The Structural Benchmarks met under the first review are a critical reference point for reforms going forward.

Human Resource Business process workshops have identified reforms that will focus on staffing and enhancing payroll management and budgeting. The appointment of the Commissioner and two Deputy Commissioners of the Independent Commission Against Corruption (ICAC) is the first critical step that will enable full and effective operation of the ICAC office. The authorities are grateful for the excellent and comprehensive TA report on the Monetary Policy and Exchange Rate Framework that helped them develop a sequenced reform Roadmap. Similarly, the new Medium-Term Revenue Strategy (MTRS) for 2023-2027, put together with the help of Fund TA, will guide revenue policy and administrative reforms going forward.

The financing program will continue to build on these policy objectives with the authorities committing to additional benchmarks, criteria, and targets. They remain committed and are on track to meet the other structural benchmarks due in the coming months.

Economic Conditions

There has been a strong economic recovery since 2021, as the economy reopened and recovered, supported by the non-resource sector. Growth is expected to pick up further in 2024, initially driven by resumption of activity at the Porgera mine. Growth is then forecast to moderate over the medium term toward a long-run average rate. The economy is expected to remain underpinned by increased production in the agriculture, forestry and fisheries sectors, public investment programs - including the Connect PNG program – as well as 2 private sector investment. Inflation has slowed, mainly due to the 2022 fiscal package - which included policies such as zero-rating excise and Goods and Services Tax on fuel, staple foods, and hygiene products. End-of-period inflation for 2023 is projected to remain low due to the sustained effect of education subsidies and moderating global food and freight prices but is expected to pick up in 2024 as the base effect of the fiscal package fades.

Overall, the risks to growth are tilted to the downside, although there are notable upsides over the medium term relating to the commencement of new resource extractive projects and the possibility of large LNG revenue inflows if amortization and depreciation expenses fall earlier than the baseline forecast**.** The downside risks include weaker external demand for exports, high volatility in commodity prices, tighter global financial conditions, and exposure to natural disasters.

Fiscal Policy

PNG is committed to fiscal consolidation and its deficit for 2023 is expected to be slightly lower than at program approval. Higher-than-expected revenue performance will be used to cover the expected increase in interest expenditure driven by higher global interest rates, financial support to PNG Power, rental and utility costs, and for clearing payment arrears.

The fiscal consolidation effort will continue in 2024, consistent with the medium-term budget repair strategy, which aims to achieve a balanced budget by 2027 in line with a 13-year plan. The fiscal targets are ambitious, but the authorities are confident they are achievable. Importantly, they increase their domestic revenue mobilization efforts guided by the new MTRS and will enhance expenditure efficiency. This will put public debt firmly on a manageable trajectory, reducing debt vulnerabilities and exposures.

Notable progress has been made in strengthening debt recording and management with the implementation of the Guarantee Policy and data migration to a new system. The high sovereign debt distress risk is expected to subside when the LNG revenue picks up in 2027 and new resource projects come onstream. The substitution of costly borrowing with concessional financing from multilateral and bilateral partners has also improved PNG's debt profile. To carefully monitor and control risks, the present value limits on new public external debt contracted in 2023 and in 2024 are being maintained.

Monetary and Financial Policies

The authorities remain committed to strengthening the monetary policy and exchange rate framework and this is to be guided by the recently established Roadmap, an important commitment that will serve as a reference for reform conditionalities for future program reviews. BPNG requested long-term TA support at the 2023 Spring and Annual meetings and 3 are looking forward to the arrival of this valuable resource. BPNG will continue to seek capacity support with the implementation of key elements of the Roadmap, including a communication strategy.

The alignment of the monetary policy instruments is an important step to more effectively influence domestic market interest rates and improve the transmission of monetary policy. This will also entail the introduction of an interest rate corridor around the policy rate. BPNG is also making progress to determine the key parameters of the framework for the crawl-like exchange rate arrangement (new SB), which is consistent with a requirement of implementation by end-December 2023; this will support the gradual return to kina convertibility by the end of the program.

Work is progressing to strengthen the independence and governance of the BPNG by filling vacancies at the Board and senior management (new SB). The authorities are on track to amend the Central Banking Act (CBA) to address remaining weaknesses related to mandate, governance, autonomy, transparency, and accountability (ongoing SB).

Addressing risks to financial stability and strengthening financial inclusion remains critical. A new financial inclusion strategy for 2023-2027 which provides a roadmap to accelerate financial inclusion efforts has been published. The ongoing CBA review and the Financial Sector Stability Review (FSSR) will support this. The onsite Asia/Pacific Group on Money Laundering (APG) AML/CFT mutual evaluation in October will strengthen efforts for effective implementation of the AML/CFT framework.

Governance

The ICAC is on track to deliver an effective anti-corruption framework with the appointment of a commissioner, and two deputy Commissioners (all international experts). Work has also progressed in drafting the key implementation regulations for the ICAC law, based on best international practice. This will specify processes for ICAC's preventive, investigative and prosecutorial mandates, and ensure sharing of information across relevant agencies. Work is on track for their adoption by the end of the year (ongoing SB). ICAC is also actively developing its internal policies and guidelines, setting up IT systems, and enhancing cooperation with relevant anti-corruption bodies, including the Financial Analysis and Supervision Unit of BPNG.

Further, the authorities remain committed to strengthening transparency around procurement. They are working to prepare the posting of details of COVID-19 related procurements on the government procurement website, in line with the commitments under the RCF from April 4 2020 and 2021 (ongoing SB) to ensure full accountability for contracts entered under emergency procedures.

To enhance fiscal and financial transparency, authorities will extend the coverage of GFS reporting, and improve consistency of statistics. Recent Fund TA on external sector statistics has allowed them to re-state their BOP data from 2015 to 2022 in line with the recommendations of the 6th Balance of Payments Manual. To continue improving the consistency of external sector statistics with other official statistics, the authorities will initiate an inter-agency group on external sector statistics, including representatives from the NSO, Treasury Department, PNG Customs Service and the BPNG (new SB).

Capacity Support

The authorities recognize that the continued close engagement with the Fund and clear communication of the reforms to PNG's general public is critical for successful program implementation. They are committed to working closely, where appropriate, with the Fund on communication, to forge understanding on the benefits of the reforms. Continued clear guidance and timely technical assistance from Fund staff on specific reforms will be a valuable component to ensure policy advice is sufficiently tailored to PNG's specific circumstances and promote the overall likelihood of maximizing the benefits of the program.

Climate Change

PNG's vulnerabilities to climate change effects present significant challenges due to heavy reliance on agriculture at the subsistence level and for export. With large adaptation needs due to rising sea levels, coastal erosion, flooding, drought, and landslides, our authorities are making efforts to reduce emissions, protect the rainforest and adapt to climate change amidst financial constraints. According to the World Risk Report, 2020, PNG is ranked 8th among countries for highest disaster risk in the world, and this will continue to be exacerbated by climate change. The authorities are committed to tackle climate vulnerability, and the long run impact of climate change. They will continue to work closely with development partners on climate mitigation and adaptation programs