Financing Development in PNG in the Context of the GEC

Mark McGillivray
Chief Economist
AusAID
Introduction

- Will examine
  - Implications of the Global Economic Crisis (GEC) for development in PNG
  - Financing PNG’s development aspirations
    - Prioritisation of public sector expenditures
  - Importance of recurrent expenditure in supporting basic service delivery
PNG Context and Challenges

- Context
  - Limited progress towards the MDGs
  - Dualistic economy
    - Extractive sectors
      - mining, oil, logging, fishing and gas extraction
    - Indigenous sectors
      - subsistence agriculture, commercial and smallholder cash crops, and small manufacturing and services sectors.
PNG Context and Challenges

- Challenge for the PNG Government
  - To accelerate progress towards the MDGs by
    - converting the revenues received from the major resource projects into goods and services for the people of PNG
    - creating an environment in which the majority of Papua New Guineans can participate in the economy and earn income
      - broad based, MDG consistent economic growth
Global Economic Crisis

- **Global** GDP growth is forecast to be -2.7% in 2009, down by 8 percentage points from 2007.
- **Developed** country GDP growth is forecast to be -4.4% in 2009, down 6.7 percentage points from 2007.
  - Japan 6.6% in 2009, down by 8.6 percentage points.
- **Developing** country GDP growth is forecast to be 0.0% (excluding China and India) in 2009, down by 6 percentage points from 2007.
- Growth reductions in large part driven by declines in international trade.
Figure 1

going, going ... GONE: the collapse of global trade

Quarterly Merchandise Exports (billions of $US at current prices)
Global Economic Crisis

- Negative GDP per capita growth in many developing countries in 2009
  - 13 in Asia and the Pacific
- Up to 100 million extra people trapped in extreme income poverty in 2009, below $PPP1.25 per day
  - Slower progress towards MDG1
- An average of 200,000 to 400,000 more children a year – a total of 1.4 to 2.8 million – may die between 2009 and 2015 if the crisis persists.
  - Slower progress towards MDG4
PNG and the GEC

- PNG is relatively well positioned to deal with GEC
  - High GDP growth in recent years
    - 6.5% in 2007 and 7.2% in 2008
  - Current account surpluses
    - 8.7% GDP in 2008
  - Large reductions in government debt
    - 70% to 30% GDP
  - Windfall revenues in trust accounts
    - Around 3 billion Kina
  - Banking system with limited exposure to international financial markets
PNG and the GEC

- But it is highly exposed
- Growth driven by
  - high commodity prices
  - high overseas demand for extractive industry commodities
- Global demand has fallen
- Commodity prices have fallen
  - Crude oil fallen from $US140 per barrel in July 2008 to $US50 in March 2009
PNG and the GEC

- PNG Government in November 2008 predicted growth of 6.2% in 2009
  - Likely to be revised down
- ADB predicts growth of 4.0% in 2009, down by 3.2 percentage points from 2008
- Government budget deficit
  - 2.2% GDP in 2008 (worse than expected just a few months earlier)
- Decrease in government revenue
  - 25% decrease in 2009 compared to 2008
Responding to the GEC

- Requires strategic reprioritisation within the PNG budget combined with fiscal discipline
  - Development (capital) expenditure
  - Recurrent expenditure
- Trust funds can be used to smooth expenditures
  - Draw downs tend to be allocated to the development budget, infrastructure spending in particular
  - Good for sustaining economic growth
Responding to the GEC

- **Recurrent Budget**
  - Pays for salaries of teachers, nurses, doctors and community health workers
  - Pays for supplies and operating costs needed for these staff to do their jobs, to actually deliver services

- **Experience tells us that the second of these payments tends to be cut in lean budgetary times**
  - Not good for growth in the growth in general, for broad based growth or progress toward the MDGs
Responding to the GEC

- Budgetary reprioritisation should be such that expenditure on supplies and operating costs needed for actually delivering services be protected
PNG-Australia Partnership for Development

- PNG-Australia PPD signed in August 2008
- Provides for scaling up of Australian ODA to PNG that inter alia supports basic service delivery, especially in rural PNG
- Focus areas are education, health, transport, public service delivery and statistics
  - Education implementation schedule targets an increase in the primary school enrolment rate for 53% today to 70% in 2015, consistent with both the MDGs and PNG’s draft Universal Basis Education plan
    - Funds will increasingly go to the cost of education service provision
- PPD principles: mutual respect, mutual responsibility and mutual accountability for results
Financing PNG’s Development in the Context of the GEC

Mark McGillivray
Chief Economist
AusAID