

# PAPUA NEW GUINEA

SEVEN SNAPSHOTS OF A NATION

Edited by Jonathan Pryke



LOWY INSTITUTE



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The papers in this report are part of a series produced by the Lowy Institute with the support of ExxonMobil to provide a country assessment of Papua New Guinea. The papers are authored by experts in their respective fields, drawing upon the best available evidence and data to support their judgements about key conditions and trends. The report is intended to provide insights about the likely and possible future implications of each area on the future of Papua New Guinea.

The views expressed are entirely the authors' own and not those of the Lowy Institute.

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# PAPUA NEW GUINEA'S POLITICAL CONDITION AND TRENDS THROUGH TO 2025

BAL KAMA

## INTRODUCTION

Papua New Guinea entered its 2017 National Election after a tumultuous period in the country's politics and economy, and there remains much uncertainty about the election process, with significant implications for the country's future.<sup>1</sup> In the last ten years key political, bureaucratic, and regulatory institutions have struggled and in some cases, failed. These struggles have been more profound under the O'Neill government despite some tangible advances in the country's ambitious *Vision 2050* roadmap.<sup>2</sup>

There is a widespread desire across the country for robust and independent institutions to ensure economic gains are transparently and sustainably managed. The ultimate question for many voters in the 2017 general elections was not who would form the next government, but who would be the most credible leader.<sup>3</sup> With elections now over, and the O'Neill government returning for a second term, what does Papua New Guinea expect of the new government and those in power?

This analysis attempts to address how key trends in PNG's politics will impact upon both the bureaucracy and regulatory environment. It will identify some of the key actors and how they are likely to change. It will discuss current political trends, their impact on the regulatory and legislative environments and how likely they are to continue in the future. Finally, it assesses the prospects of continuing dysfunction in PNG politics, the further marginalisation and deterioration of the bureaucracy, and how this destructive course might be avoided.

## **SECTION 1: WHO ARE THE KEY ACTORS IN POLITICS AND THE BUREAUCRACY, AND HOW IS THIS LIKELY TO CHANGE IN THE FUTURE?**

### **PETER O'NEILL**

Prime Minister Peter O'Neill has been the most dominant political player in PNG politics this decade. The dramatic events of the 2011 constitutional crisis resulted in the unexpected elevation of O'Neill into power. He quickly became revered among his peers as an experienced combatant of the country's hostile politics.<sup>4</sup>

O'Neill maintained strong populist support in the early years of his government by promising free health and education programs and infrastructure development, backed by a strong anti-corruption focus in the form of the Investigative Task Force Sweep.<sup>5</sup> However, his prolonged resistance against his arrest warrant for official corruption has contributed to the deterioration of regulatory and enforcement institutions as well as reducing confidence in his political longevity.<sup>6</sup>

With mounting allegations against him, O'Neill influenced key political allies and swayed the appointment of key bureaucrats whose loyalty helped consolidate his grip on power.

O'Neill's influential political allies include William Duma,<sup>7</sup> Dr Fabian Pok,<sup>8</sup> Peter Ipatas,<sup>9</sup> James Marape<sup>10</sup> and Mao Zeming.<sup>11</sup> Playing into existing regionalist sentiment within PNG politics, O'Neill maintains a firm inner circle of Highlands MPs<sup>12</sup> and ensures that controversies involving them are subdued.<sup>13</sup> Other key players in O'Neill's ascension include former Prime Minister Pais Wingti,<sup>14</sup> Speaker of Parliament Theo Zurenouc, Don Polye,<sup>15</sup> Patrick Pruaitch,<sup>16</sup> and Ben Micah.<sup>17</sup> Polye, Pruaitch and Micah were key allies in the early period of O'Neill's government and were rewarded with senior ministerial portfolios until their falling-out with O'Neill led them to the Opposition. Don Polye and Ben Micah lost their seats in the 2017 election.

O'Neill's political party, the People's National Congress (PNC), also suffered losses of influential political figures such as the former Deputy Prime Minister Leo Dion, Mao Zeming and Theo Zurenouc. The latter two were critical, as in the past they leveraged support for O'Neill from MPs in the mainland coastal region (Momase).

Unlike his previous government, O'Neill initially faced an uphill battle against a resurgent Opposition group with 46 MPs. However, some members in the Opposition have defected to join O'Neill since his election as the country's Prime Minister in August 2017. With the looming vote of no-confidence in the next 15 months, O'Neill will do whatever he can to retain support.<sup>18</sup>

### **CHARLES ABEL**

The appointment of Charles Abel as Deputy Prime Minister is an attempt to retain support from the coastal MPs as well as redirect attention from O'Neill to a competent partner. In the last government, O'Neill played a prominent role while the Deputy Prime Minister was almost non-existent on the national scene. However, that is likely to change.



Abel has already been proactive in engaging with national issues and will be using his experience in trade and commerce to try and restore investor confidence. While Abel reports to O'Neill, he should be able to influence the Cabinet unlike his predecessor Leo Dion. Being relatively young and from the coastal region, Abel may also challenge and foster consensus among his peers and outspoken MPs in the likes of Gary Juffa, Allan Bird and Bryan Kramer in the Opposition, reducing the attention on O'Neill while presenting a credible image of O'Neill's government.

## **OTHER INFLUENTIAL MEMBERS OF GOVERNMENT**

Peter O'Neill has appointed a Cabinet of 33 members, the largest in Papua New Guinea's history.<sup>19</sup> Key Ministers within his Cabinet include James Marape, a loyal lieutenant who retains his finance portfolio; William Duma, a controversial figure who brought with him critical numbers to the government; Justin Tkatchenko, who holds the portfolio of Lands & Physical Planning; and Puka Temu, a leader of the 'Papuan Bloc' who holds the health portfolio. Other key members of government include Sir Julius Chan, a former Prime Minister and Governor of New Ireland province who crucially sided with PNC soon after the election. Job Pomat was also appointed speaker of Parliament, a position which brings with it significant influence. Pais Wingti and Peter Ipatas join Sir Julius Chan as senior politicians providing clam and stability among O'Neill's alliances.

## **SAM BASIL**

Basil's leadership in the Opposition and strong voice on important national issues has initially gained the respect of both sides of parliament. He led the resurgence in one of the oldest parties in Papua New Guinea, Pangu Pati, with the highest number of MPs in The Alliance, and hoped to be nominated as Prime Minister by the opposing coalition camp in the event of a change in government.

However, the elevation of Patrick Pruaitch as the Opposition Leader unsettled his ambition leading to his defection to join O'Neill in the government. Since a key campaign platform for Pangu Pati during the 2017 national election was to remove O'Neill, Basil's defection together with 14 other Pangu Pati MPs, appeared to discredit Pangu Pati's image among loyal supporters.

But Basil's move may also be strategic to support any move within the government to unseat O'Neill. A common reason provided by all who have defected, including Basil, is the challenge in accessing the electoral development funds as an Opposition MP. While that continues to be an issue, Basil's standing and the timing of his move is disappointing for the resurgent Opposition.

## **SIR MEKERE MORAUTA**

The return of Sir Mekere Morauta from retirement to national politics presents a significant threat to O'Neill's continued dominance. Morauta's intellectual leadership and statesmanship inspires unity among the parties opposed to O'Neill. Morauta and fellow Independent MPs have recently joined the Pangu Pati, allowing Pangu the highest number of MPs in the Opposition before the defection of its members to the government. The official position of Pangu Pati is unclear as its members in both the government and the

Opposition claim to represent the party. Morauta inadvertently assumes leadership of the Opposition faction of the party.

Morauta leads a 'redeeming plan' that starts with the replacement of O'Neill.<sup>20</sup> However, his long vendetta against O'Neill over the PNG Sustainable Development Programme (PNGSDP) funds, which O'Neill has sought to control by removing Morauta as Chairman, may invite closer scrutiny of Morauta's past controversies.

## **PATRICK PRUAITCH**

Patrick Pruaitch is the party leader of the National Alliance (NA), the second most well-established political party to Peter O'Neill's PNC party and the current Opposition Leader.<sup>21</sup> Founded by Sir Michael Somare, the NA-led government stayed in power for two terms prior to O'Neill's takeover in August 2011. NA is well financed, with close links to foreign logging companies. However, partners in the Opposition doubt NA as trustworthy due to alleged mismanagement of the country during their term in government. It is one of the likely reasons for Sam Basil's defection to join the O'Neill government after Pruaitch was elevated as the leader of the Opposition. It appears the appointment was more out of convenience to keep the NA Members in the Opposition.

While NA has publicly stated its opposition to O'Neill during their fallout in February 2017, key elements within the coalition continue to question Pruaitch's leadership.<sup>22</sup> Pruaitch was part of the infamous 'kitchen cabinet', alleged to be responsible for the country's mismanagement during Somare's reign.<sup>23</sup> He was also Treasurer in the final years of O'Neill's first term, when the economy was considerably mismanaged. Newly elected and well respected MPs Allan Bird and Walter Schnaubelt promise to instil some credibility in the NA party but this will not be immediate.

## **OTHER INFLUENTIAL MEMBERS OF THE OPPOSITION**

Kerenga Kua is outspoken on complex legal issues associated with governance in PNG's highly litigious environment. As one of the country's most senior lawyers, Kua commands the respect of both parliament and the general public. A change in government would see him reignite anti-corruption efforts and ensure the completion of investigations against O'Neill. Kua's ascension will likely see a restoration of confidence in the legal system.<sup>24</sup>

Gary Juffa commands strong populist support and addresses issues such as unscrupulous foreign businesses, illegal immigrants and the West Papuan conflict with patriotic overtones that sometimes may appear contentious.

As a former army captain revered for his role in ousting the Sandline mercenaries, Belden Namah may come across as undiplomatic at times, but many regard his straight-shooting approach as necessary to ensuring accountability in a highly predatory political environment.

Another player, Bryan Kramer, is PNG's most influential blogger with a significant social media presence due to his anti-corruption campaigns. Elected for Madang Open, Kramer is likely to be a leading voice for reform while engaging directly with the public on the inner workings of parliament and the government systems.

## FORMATION OF COALITION GOVERNMENT

The existence of multiple political parties has meant that O'Neill had to form a coalition government, as has been the case for all governments since independence.<sup>25</sup> There are at least three key drivers that influence MPs in the formation of government, in order of importance:

- Which 'camp' has the numbers to form the new government?
- What can I gain from joining a 'camp'?
- Is the proposed Prime Minister a credible person?

By this hierarchy, the credibility of Peter O'Neill as a Prime Minister is the least consideration for MPs despite outstanding serious criminal investigations against him. For some MPs, it is assumed that leadership will change during the term of the parliament through a vote of no confidence or other permissible means.<sup>26</sup> The primary concern for MPs is to be in government rather than in the Opposition.<sup>27</sup> Joining the Opposition means a loss of privileges, including the potential for ministerial portfolios, as well as difficulties in accessing the electoral development funds (District Service Improvement Program and Provincial Service Improvement Program).<sup>28</sup>

The process of choosing the Prime Minister continues to be undermined not only by accusations of manipulation and inducements but increasingly it tends to be about what the MPs gets in return for their support, not the people of Papua New Guinea. With a high level of fluidity in MPs' movements, this trend only adds to the anxiety that in PNG politics, 'there are no permanent enemies or friends, only permanent interests'.

## KEY ACTORS IN BUREAUCRACY AND REGULATORY INSTITUTIONS

Some key players within the bureaucracy and state institutions have been able to exert power and have direct impact on political outcomes and the regulatory and legislative environment.

### ISAAC LUPARI

The Chief Secretary to the Government, Isaac Lupari, oversees the entire public service machinery and is one of O'Neill's most trusted allies. He is an important asset for the government, with extensive experience and networks within the echelons of PNG bureaucracy.<sup>29</sup>

However, Lupari's position is untenable. He was implicated in the Finance Inquiry, which uncovered a multimillion fraud syndicate involving very senior public servants, MPs and private companies associated with the Department of Finance.<sup>30</sup> The Commission recommended Lupari for criminal charges but none have yet been laid.<sup>31</sup>

Using his insights into the public service machinery, Lupari influences O'Neill and his Cabinet in the appointment of departmental heads. Lupari continues as Chief Secretary under the O'Neil government although a potential change in government may affect the pending criminal investigations against him.

## **OTHER IMPORTANT ACTORS**

Other key actors directly contributing to or affecting the regulatory and legislative environment include:

- Police Commissioner Gari Baki
- Judges and Lawyers
- Defence Force Commander Brigadier-General Gilbert Toropo
- Ombudsman Commissioners
- Public Prosecutors
- The Secretaries of Finance, Treasury and Planning
- Provincial and District Administrators

The following analysis identifies these actors, considers their impact on institutions and the resulting trends. In the last ten years it appears that having influence within the security forces is imperative to the continuation of political power. Further, having access to funds through the finance, treasury and planning departments, and local government administrators assist in the misuse of public funds. The conduct of the Ombudsman Commission, the Public Prosecutor and those within the judicial system appears to be relatively robust, but assisting them in addressing their many challenges will enable them to operate more effectively in a politically volatile and highly litigious environment.

## **SECTION 2: HOW ARE THESE ACTORS LIKELY TO SHAPE THE LEGISLATIVE AND REGULATORY ENVIRONMENT?**

The key legislative and regulatory agencies in Papua New Guinea include the parliament, the police, the Ombudsman Commission, the courts, and departmental agencies such as the Financial Intelligence Unit (FIU) within the Department of Finance. Political actors have been able to influence these agencies with a common purpose of limiting their impact on political and personal agendas. There are weaknesses in each of these institutions, which need to be addressed in order to bolster the integrity of PNG's legislative and regulatory framework.

### **WEAK PARLIAMENT**

The Papua New Guinea parliament was envisaged to play a 'central role' in shaping the country's democracy both through its law-making function and as the leading forum for debate on national issues.<sup>32</sup> Papua New Guinea's parliament has been complimented for its stability in recent years, but this has come at the cost of robust debate.

The parliament has been riven with controversy since the 1980s when the vote of no confidence scheme was first activated, leading to significant parliamentary instability. Successive governments have used their numerical strength to thwart the legislative process as well as suppress fair debates and parliamentary proceedings in order to, not only remain in power, but also maximise predatory political interests knowing they might not retain their seat in the next election.<sup>33</sup>

As parliamentary stability has resumed, the PNG Supreme Court has observed over the years a growing trend to “bulldoze legislation through because there [has been] an absence of Opposition or their voices not entered in Parliament”,<sup>34</sup> cautioning that “Parliament ... should never be a ‘rubber stamp’ for the executive, and that any legislative programme of the executive should be subjected to the closest scrutiny”.<sup>35</sup> Similar assertions were made of O’Neill’s government when overturning the changes made to the Constitution in the Manus Island detention centre case.<sup>36</sup>

## THE COMPROMISED ROLE OF THE SPEAKER

The Speaker of Parliament has been a prime cause for weakening the parliament. Because parliamentary proceedings are non-justiciable (meaning they cannot themselves be a cause for litigation), the Speaker is left unrestrained to engage in questionable practices.<sup>37</sup> In the 2011 constitutional crisis, the Supreme Court found that “the Speaker [Jeffery Nape] contributed enormously to the crisis” by failing to remain “neutral and impartial”.<sup>38</sup> The Court noted that “the actions of the Speaker appeared to have been motivated by power and political expediency”<sup>39</sup> and were “harsh and oppressive”.<sup>40</sup>

Backed by his contentious spiritual beliefs, the Speaker under the O’Neill government, (now ousted) Theo Zurenouc, is credited with restoring some credibility to the parliament, but his conduct has not escaped similar accusations of bias.<sup>41</sup> This issue is most likely to continue in the new government with even Zurenouc admitting that it is a “dangerous trend [that] needs to be proactively addressed”.<sup>42</sup>

## VOTE OF NO CONFIDENCE THREATENS STABILITY

Under the PNG Constitution, a government can be subject to a vote of no confidence after 18 months in power.<sup>43</sup> The threat of a vote of no confidence often immobilises ‘normal executive and legislative functions’ leading to increased ‘corruption and patronage’ despite appearances of stability.<sup>44</sup> Former Prime Minister Sir Julius Chan confessed that the vote of no confidence system means a prime minister “has to spend a quite disproportionate amount of his time and energy keeping individual politicians ‘happy’”.<sup>45</sup> The Speaker can manipulate the proceedings in order to give unfair advantage to a party.<sup>46</sup> While this system remains in place, incoming governments continue to face instability after the grace period.<sup>47</sup>

## PARTY HOPPING

Papua New Guinea has never had a strong political party system, and with 45 political parties participating in the 2017 elections, this continues to be a challenge.<sup>48</sup> Once in parliament, political parties exist “solely as parliamentary factions”<sup>49</sup> without firm ideological premises and party discipline. It allows MPs to hop between parties – leading to tradition of instability and growing urgency to address it.<sup>50</sup>

An attempt was made in 2010 under the *Organic Law on the Integrity of Political Parties and Candidates* (OLIPPAC) to control the movement of MPs but the Supreme Court declared it to be unconstitutional on the basis that the penalties prescribed under the law against MPs were harsh and oppressive of their freedom to make political decisions.<sup>51</sup> As evidenced by the near doubling of O'Neill's PNC party during its first term in government, this trend will likely continue.<sup>52</sup> The Registry of Political Parties has prepared an amended version of the OLIPPAC but is yet to be passed by the parliament.

While the country remains vulnerable to 'party-hopping', some key indicators, however, suggest that this is likely to change over the next decade.

First, voters over the years have developed an increased awareness and sensitivity to political parties. In the 2012 elections, Somare's NA party lost more than three-quarters of their seats as voters became distrustful of the party. In 2017, O'Neill's PNC party faced similar challenges, losing almost half of its MPs while some of its serving MPs ran as Independent candidates or even refused to state on their campaign posters that they were endorsed by the PNC. In contrast, newly revived political parties, such as Pangu Pati, campaigned successfully on the platform of being the oldest and reliable political party without the backing of wealth or senior political figures.

Second, because voters are becoming more sensitive to political parties, they are quick to hold their MPs accountable for their choices in joining a political faction. This was evident in the 2017 election where many voters expressed their dissatisfaction over their MP's decision to join O'Neill.<sup>53</sup>

Third, political parties are becoming more established and well connected to businesses and government opportunities, which means there are incentives, both inside and outside of politics, for MPs to remain committed to a party.

Fourth, major political parties are becoming wealthier and have the ability to induce and retain their MPs, and to finance new candidates in increasingly expensive election campaigning.

Despite these trends there will still be a strong focus on election candidates to run as independents so that if they are to win they can 'keep their options open' and extract the greatest benefit from a political party. More than half of the candidates in the 2017 election ran as independents.

## USING ELECTORAL FUNDING TO CONTROL MPS' BEHAVIOUR

A primary factor in PNG's political stability in recent years is the government's control and distribution of the electoral development funds under the District Service Improvement Program (DSIP) and Provincial Service Improvement Program (PSIP). The Vice Minister for Provincial and Local-level Government Affairs has made clear the reason why multiple attempts to change the prime minister have been unsuccessful:



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**“The reason is because DSIP is there that’s why we will be in the government and support the O’Neill-Dion government. It’s not about your number of qualifications you have to lead the government, so long as you have the money, you will master the numbers.”<sup>54</sup>**

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The annual funding for districts (DSIP) is currently K10 million, with provinces receiving K5 million for each district within that province (PSIP).<sup>55</sup> The funds are intended for service and infrastructure developments, but the implementation of these programs in many electorates is highly questionable.<sup>56</sup> The legislation provides for the funds’ allocation, but the amounts, and their timing, is at the discretion of the executive government through its influence on the state’s finance department.<sup>57</sup>

This discretion allows the executive to influence MPs’ behaviour. This trend is likely to continue but will vary according to the government in place. While the system may be unsound and undemocratic, the funds restrain the movement of MPs, thus minimising political instability.

## **LACK OF POLITICAL WILL AT THE NATIONAL LEVEL**

Due to strong localised pressure and expectations from tribal, district and provincial forces, a majority of the MPs are committed to representing these interests at the national level than investing in addressing national concerns. This leaves a vacuum for a handful of political elites to take advantage at the national level. As long as they can keep the locally focused MPs ‘happy’ with what they need for their electorates, then they can have them bandwagon on any policy decisions, legislations or reforms.

This behaviour is slowly changing as local expectations are increasingly connected to national issues and as people become more informed through platforms such as social media on the importance of their MPs addressing national issues. But until that is fully realised, local pressures will continue to affect an MP’s behaviour, which, at times, can be detrimental to the national interest.

## **LEGAL SYSTEM**

Papua New Guinea is one of the most litigious societies in the world. While the trend to suppress high-profile cases casts doubt over the efficacy of the legal system, courts continue to play a pivotal role against a powerful executive government. The Supreme Court has reinforced its unwavering intention that “abuse of power by the [Executive] NEC must not be tolerated by the Court”.<sup>58</sup>

The PNG judiciary comprises the Village, District, National and Supreme courts, with the National and Supreme Courts forming an appellate structure with jurisdiction over serious cases including constitutional matters. The judiciary currently consists of 39 judges, including two on secondment from the Australian Federal Court, an increase from the initial 34 judges in the last ten years.<sup>59</sup>

Chief Justice Sir Salamo Injia aims to have between 80 and 100 judges on the bench by 2020.<sup>60</sup> This positive development would increase the number of resident judges in the country's 21 provinces, as well as judges serving in the proposed Court of Appeal, a new court to sit between the National and the Supreme courts.<sup>61</sup>

Parliament has yet to approve and legislate the proposal. The proposed Court of Appeal hopes to decrease congestion in the court system and increase judges' specialisation, but "staffing such a structure with judges of suitable ability and experience would be difficult for Papua New Guinea alone at its present stage of development".<sup>62</sup> Some fear that an extra layer of the courts may increase unnecessary appeals, already rife in the current system, although this would not be insurmountable for a robust and independent judiciary.

The Court has taken an active approach against what it perceives as a 'creeping tyranny' in parliament, when it granted 'standing' to the Opposition Leader and senior public servants in 2014 to challenge constitutional amendments in Court.<sup>63</sup> The Supreme Court allowed former Opposition Leader Belden Namah to prosecute the Manus Island detention centre case after he failed to defeat the constitutional amendment that sanctioned the Australia–PNG bilateral arrangement in parliament.<sup>64</sup> Such is unheard of in comparable democracies but the Court has deemed it necessary against the fundamental inefficiencies of the Parliament. This precedent is likely to continue.

However, PNG's courts do remain vulnerable to political interference.<sup>65</sup> Successive political leaders and public servants have exploited the legal system in attempts to undermine legitimate investigations against them. For instance, Prime Minister O'Neill applied to the National Court in 2014 for a stay of an arrest warrant against him, on the basis that it was the work of "rogue policemen". The Court refused, citing a lack of evidence of rogue policing or political motivation.<sup>66</sup>

This trend of obstructing justice continues, with political actors and bureaucrats remaining in office even when implicated in serious offences that would warrant resignation or suspension until the completion of investigations.<sup>67</sup>

These actions also reflect poorly on the role of the lawyers advising their clients in such cases. Legal practice in Papua New Guinea has become more insular and ethically questionable, with a client-driven approach that takes little heed of the consequent risks to the rule of law.<sup>68,69</sup> PNG judges may themselves be perpetuating these challenges through inconsistent judgments, unnecessary interventions, persistent delays and devotion to conservative interpretation of the law absent socio-political considerations.<sup>70</sup>

Despite concerns, the PNG judiciary has made important strides over the years and remains relatively robust and independent. A progress was the establishment of the Fraud and Corruption Offences Track to respond to the increase in corruption cases and delays in court hearings.<sup>71</sup>

The independence of the judiciary is reinforced through the appointments process. The Judicial and Legal Services Commission (JLSC) appoint all judges except the Chief Justice. The JLSC is an independent body comprised of the Attorney General, the Chief Justice, the Deputy Chief Justice, the Chief Ombudsman and a member of the parliamentary

permanent appointments committee. The JLSC appoints judges to three- and ten-year tenure.<sup>72</sup> According to the Constitution, the appointing body (JLSC) "is not subject to direction or control by any person or authority".<sup>73</sup> This arrangement is different from Australia's in which Federal and High Court judges are appointed by government and with life tenure.<sup>74</sup>

In Papua New Guinea, the government appoints the Chief Justice for a term of 10 years, and Chief Justice Injia's term expires in 2018.<sup>75</sup> Despite the contentious relationship between Prime Minister O'Neill and the Chief Justice in 2011, key actors within the O'Neill-led cabinet are likely to vouch for his reappointment.

Irrespective of the outcome, the widespread view is that the judiciary is PNG's 'last bastion of hope', and this sentiment is likely to sustain the judiciary's continuing independence.<sup>76</sup> The Chief Justice reinforced this resolve in his address to his colleagues when opening PNG's 2017 Legal Year: "The future security of our country is in your hands and my hands. Politics will come and go, you and I will remain steadfast and continue to uphold the Constitution with our responsibilities."<sup>77</sup>

## PNG POLICE

The PNG police have a challenging role in maintaining law and order in a deeply fragmented and often volatile country. The recent shooting of police officers in Wabag town and Southern Highlands in election-related violence is evidence of the high risks of policing.<sup>78</sup>

Police powers pose a threat to political actors, as successful prosecutions would mean jail time as well as loss of political power. As a consequence, politicians are increasingly interfering with and influencing police operations. Control of the police can facilitate political power. For example, when Peter O'Neill seized power from Somare in 2011, he replaced then Police Commissioner Fred Yakasa (Somare's appointee) with Toami Kulunga.<sup>79</sup> O'Neill then forced Kulunga's resignation in 2014 for authorising an arrest warrant against him, installing Jeffery Vaki who immediately recalled all investigations against O'Neill and went to great lengths to frustrate legal processes.<sup>80</sup> The current police commissioner Gari Baki has continued the process, securing O'Neill's term in office while gagging other potential high profile investigations through an internal 'vetting committee'.<sup>81</sup>

Nonetheless, the public retains a degree of trust in police work, particularly because of the successes of the anti-corruption work by the Fraud Squad and the Investigative Task Force Sweep despite O'Neill's accusations that they are "politically compromised".<sup>82</sup>

Since the case of Paul Tiensten, a former senior government minister sentenced to nine years imprisonment in 2014, criminal law amendments have increased penalties from the previous maximum of 10 years to 50 years, with life imprisonment for corruption of K1 million or more.<sup>83</sup> Aware of these risks, political actors are wary of criminal investigations, eager to establish closer relations with the police, and interfere in its work where possible.

O'Neill's return has already spurred efforts to further stifle the corruption cases against him while the Police Commissioner faces increased pressure from the public to effect the arrest warrant.<sup>84</sup>

## OMBUDSMAN COMMISSION

The Ombudsman Commission (OC) administers the Leadership Code that prescribes the proper conduct of political leaders and senior bureaucrats.<sup>85</sup> The OC's recent intervention in extending the 2017 return of writs demonstrates its continuing value in the conduct of PNG's democracy.<sup>86</sup>

An independent committee comprised of bi-partisan members including the Chief Justice appoints the commissioners. The OC investigates potential breaches of the Leadership Code and makes recommendations for the Public Prosecutor to undertake court proceedings through a Leadership Tribunal. The Tribunal applies civil penalties, such as dismissing an MP from office, as well as recommending criminal investigations.<sup>87</sup>

The wide-ranging powers of the OC extend to issuing quasi-enforceable directives to financial institutions to halt the release of DSIP and PSIP funds.<sup>88</sup> It also has automatic 'standing' to challenge laws and constitutional amendments passed by the PNG parliament – a function used to significant effect but in varying degree over the years.<sup>89</sup> These wide-ranging powers render it vulnerable to attack by political leaders. The most notable example of this was the *Maladina Amendments*, a sweeping set of changes aimed at restricting the OC's investigative and directive issuing powers.<sup>90</sup> Public protests and a successful court action scotched the Maladina proposal, but political interference in the OC remains a risk.<sup>91</sup>

Frustrated by their inability to limit the OC's extensive powers or interfere with the appointment of independent Ombudsman Commissioners, political actors have instead tried to limit its funding, affecting its ability to function effectively.<sup>92</sup>

## APPOINTMENTS OF DEPARTMENTAL HEADS

Political interferences in the appointments of departmental heads have undermined the proper functioning of the public service.<sup>93</sup> Appointments were once the responsibility of the Public Service Commission, a three-member independent body appointed to maintain a high standard of merit-based appointments.<sup>94</sup>

However, the O'Neill government replaced this structure with the Ministerial Executive Appointments Committee chaired by the Minister responsible for the department and comprising other government ministers and public servants.<sup>95</sup> This arrangement is arguably unconstitutional, and suggests a direct political interference in the appointment process. The new arrangement has kept departmental and statutory heads such as the Police Commissioner and the Secretary of Finance and Treasury subservient to the government.

The Public Service Commission is currently challenging the constitutionality of the arrangement in the Supreme Court but until the case is determined, ministerial appointments will continue to hinder the independent functions of the public service.<sup>96</sup>

A similar arrangement is in place for the appointment of district administrators.<sup>97</sup> The *District Development Authority Act 2014* gives MPs increased funding and influence over the appointment of district administrators to suit their political agendas, leading to greater abuses.<sup>98</sup>

## CHALLENGES WITH AUTONOMY

Bougainville is due for referendum seeking complete autonomy in 2019 as part of the Peace Agreement. One of the primary conditions for autonomy is for the Bougainville government to exercise control over its own natural resources. However, this has inspired other provinces to seek similar outcomes. Sir Julius Chan, for instance, is seeking some autonomy for the New Ireland province, which will no doubt be given serious consideration considering how important his support was to O'Neill's PNC party early in the forming of government period. There are similar talks among some prominent leaders in the Highlands provinces but Peter O'Neill's ascension has kept a lid on it.

Looking into 2025, these talks may become more evident especially in Southern Highlands and Enga provinces if changes are made to current key political actors and existing landowner issues are not adequately addressed.

The push for autonomy is largely a result from frustrations that the national government has mismanaged the resource revenues and failed to deliver on the expected benefits. It may play into existing regional and provincial fragmentations as well as revive historic secessionist movements. For investors in extractive and natural resource industry, this is likely to pose a challenge. These considerations, however, should not derail Bougainville's referendum.

## WOMEN IN POLITICS

There were 165 female candidates, out of the 3324 candidates that contested in the 2017 national elections, but none were successful in securing a seat in parliament. It is a setback to many who advocated for equal political representation. The disappointing election outcome demands a reassessment of the political culture and its perception of women as political actors.

One of the main reasons identified was that women were disadvantaged because of the increased bribery and election fraud or the aggressive campaign techniques employed by their male counterparts. These issues certainly affected the integrity of the whole election. But the women candidates must be credited for withstanding these electoral malfeasances and for some, even having a close contest.

A pressing issue evident in all the elections so far is the perception of voters on whether or not women are capable of representing their interests in a highly contested, predatory and sometimes, bloody political environment. This perception is influenced by factors quite different to those promoting a safe and tolerant political space for women in Western democracies.

An avenue to effectively address this perception issue is to encourage women to be involved at the local government as councillors, presidents for local level government (LLG), or even as district or provincial administrators. Currently, only a few women are councillors, none, however, are LLG presidents or district and provincial administrators as far as this paper is concerned. These are politically charged positions. Being in these positions would allow women to demonstrate their competency, and seeing their success in these positions would contribute largely to altering the public perception of women in political leadership.

The Prime Minister promised to revisit the proposal for the 22 reserve seats in parliament which, unfortunately, was not supported by MPs, including the three women MPs, in the last government.<sup>99</sup> The proposal sought to allow each of the 21 provinces and the National Capital District to have a male and female governor. It remains to be seen how the governors of each province, who are often jealous of their powers, will respond to this power sharing arrangement if the reserve seats were to be enacted.

To advance the point earlier, an alternative would be to propose reserve seats at the local level government, allowing women as council presidents and pressuring the government to appoint women as district and provincial administrators. Given the current political environment, such an arrangement is likely to gain more political support from the MPs than the current proposal for reserve seats in the national parliament.

It is important to approach this issue with openness for incremental changes, starting with the local political institutions creating a network of strong women leaders as role models, which will inspire more substantive reform at the national level all the while advancing the national conversation for equal political representation.

## **SECTION 3: RECOMMENDATIONS AND CONCLUSION**

### **RECOMMENDATIONS**

#### **PARLIAMENTARY STABILITY**

The role of the Speaker of Parliament should be better defined and endowed with less discretion.<sup>100</sup> Papua New Guinea should consider a bipartisan appointment of a non-parliamentarian to be the Speaker.<sup>101</sup> Despite the shortcomings of the *Organic Law on Political Parties and Candidates* to regulate political parties and movement of MPs within political factions, legislation still remains the best chance of countering the fluid party political system.<sup>102</sup> But increased awareness of the importance of political parties among electors and candidates is positively impacting the behaviour of MPs.

#### **DSIP AND PSIP AS CONSTITUTIONAL GRANTS**

MPs' access to electoral funds is contentious but will most likely remain a permanent part of the political system.<sup>103</sup> The Constitution should be amended to have the funds as constitutional grants, with MPs given the right to seek enforcement if the government fails to equitably manage its distribution. Direct control over district development funds blurs MP's functions as legislators and project managers and raises the possibility of a future constitutional challenge.<sup>104</sup> A province-based inter-agency oversight mechanism should be established to improve the transparency and accountability of expenditure.

Lack of proper management of development funds has also created expectations and greater reliance on investors and donors to undertake development work and build infrastructures. While it may be part of the investor's contractual responsibility, it risks encouraging the abuse of public funds.



## **PUBLIC SERVICE APPOINTMENTS**

If PNG's bureaucracy is to remain relevant and credible, the appointment of departmental heads should revert to the Public Service Commission as sole appointing body, restoring its constitutional role.<sup>105</sup> Cronyism, as exemplified by the police force, hamstringing the entire system. It has created distrust in the public service machinery, forcing people including investors, to bypass the state system to deal directly with the political elites.

## **OMBUDSMAN COMMISSION AND PUBLIC PROSECUTOR**

Government funding for the OC and Public Prosecutor needs to be maintained at a level sufficient for effective operations. They need to attract and retain competitive staffs able to represent the agencies against the highly skilled private lawyers often hired by politicians. Acting appointments in these agencies should be abolished or only for a defined period, as job insecurity have been argued to compromise performance.

## **JUDICIARY AND LEGAL SYSTEM**

Judges must be consistent and coherent in their judgments. Inconsistency has created a culture of 'judge-shopping' among litigants, exposing the courts to exploitation to the detriment of the legal system.<sup>106</sup> Legalistic judgments or court proceedings that take little or no account of surrounding socio-economic and political circumstances could be provocative and inconvenient to the course of justice. This includes the mediation proceedings between landowners and investors where court's intervention may not always lead to a just outcome.<sup>107</sup>

The PNG Law Society needs to be proactive in disciplining lawyers who breach ethical standards. With more Australian lawyers in the country, there is also a need for Australia to be proactive in regulating the practices of its lawyers who are often called into question.<sup>108</sup>

## **PNG POLICE AND ANTI-CORRUPTION INVESTIGATIONS**

It is critical that an independent body similar to the Ombudsman Commission appoints the Police Commissioner with security of tenure so that the Commissioner remains independent from political influence. The proposed Independent Commission Against Corruption looks promising, following its incorporation into the PNG Constitution.<sup>109</sup> While its functions are as yet unclear, it is most likely to have a greater independence and continue the work of Investigation Task Force Sweep (ITFS). The successes of ITFS in countering corruption remain unparalleled to any anti-corruption agency in Papua New Guinea. Although discredited and rejected by the current government, ITFS' model must be revisited if Papua New Guinea is to successfully combat corruption.

## **CONCLUSION**

There is a real risk that PNG politics will become increasingly dysfunctional under the current structures and conditions. With the threat of a vote of no confidence looming large over any new government, the need to keep coalition parties 'happy' rivals the responsibility to govern.<sup>110</sup> Distribution of the electoral funds (DSIP and PSIP) appears to be the single most important factor in consolidating political power against potential challenges.<sup>111</sup>

But misuses of these development funds often create expectations for investors and donor agencies to step in and provide basic government services leading to questions of dependency and sustainability. Underfunded state institutions, with some subjected to internal interferences and overt political sway over of departmental appointments contributes to the decline of current statutory and bureaucratic environment.

Over the next decade, investors may be confronted with two narratives – whether Papua New Guinea is increasingly becoming a failing State with a highly predatory elite or whether Papua New Guinea, being a relatively young democracy, is still undergoing a highly complex process of state formation and the issues described here are part of that process. Neither of these narratives offers any assurance except to suggest that these challenges are likely to persist but in varying degrees in the future. However, there are also key indicators that suggest things may change for better as the country heads into 2025 and beyond.

First, the people of Papua New Guinea have shown to be highly resilient despite systemic inefficiencies and instability. For instance, during the 2011 constitutional crisis, the country had ‘two’ prime ministers for nearly seven months, and key accountability institutions were almost inoperable. Yet, the country overall was stable and the Constitution unbroken. Political instability as a result of issues identified here is often contained at the national level. The sub-national and local levels remain unhindered using both formal and informal institutions to aid their governance systems.

Second, key accountability institutions continue to demonstrate their resilience amid challenges and political interferences. The courts, the Ombudsman Commission and now the parliament, initially with 46 Opposition MPs – the highest number in the history of the country’s parliament – and despite some recent defection, continues to maintain credibility. Choosing to be in the Opposition and missing out on the perks and privileges of being with the government is an important behavioural change indicating commitment to good governance and potential for better leadership in the future.

Third, general elections in the last ten years have indicated that voting behaviours are gradually changing. People are increasingly aware of the ill effects of ‘money-politics’ and unscrupulous political campaigns and are sensitive to the reputations of political parties. These factors have influenced the high turnover of MPs in the last ten years. While the management of the electoral system have been a failure, the voters are increasingly better informed to make good political choices.

A major part of this shift is access to contemporary political platforms. Social media is transforming politics from being tribal and disparate to an institution capable of forging collective national interests. Increasingly, prominent political players are accessing social media forums, and are involved in the sharing of ideas and concerns in the hope that a politically informed population will encourage public scrutiny of political leaders.<sup>112</sup> While social media may not translate to effective change, it is a positive influence. It helps shape collective views on critical national issues while dismantling the cleavages that perpetuate cronyism and shelter perpetrators responsible for the country’s decline.

Having an unbroken Constitution, and regarded as one of the established democracies in the world, Papua New Guinea certainly has the potential to see its democratic project flourish. Strengthening the public service mechanism would be imperative to its resurgence. Over the years, the public service has been reconfigured to make politics its epicentre. Domestic and foreign interests bypass the formal state to deal directly with political actors — further legitimising this reconfiguration. It will require a sustained effort of political re-engineering — re-crafting the institutional rules of the game — to steer the country forward.<sup>113</sup> Current indicators suggest this is possible.

With the controversies of the 2017 elections behind it, the largely disenfranchised but resilient population of Papua New Guinea now waits anxiously to see how its elected 'male' leaders will navigate these challenges and bolster the country's democratic resolve.

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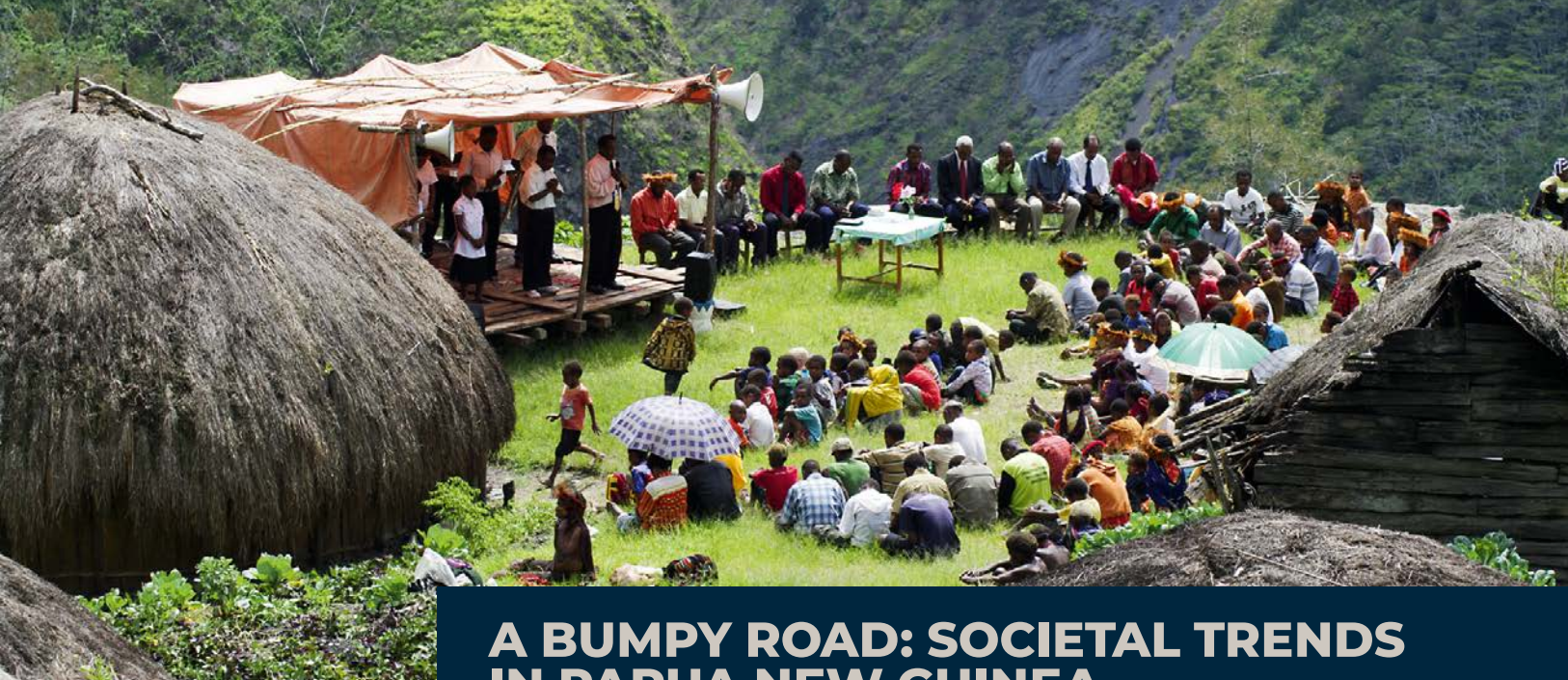
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# A BUMPY ROAD: SOCIETAL TRENDS IN PAPUA NEW GUINEA

JONATHAN PRYKE AND PAUL BARKER

## INTRODUCTION

On many indicators, Papua New Guinea's rapid population growth is outpacing development progress. Service delivery across the country is in decline. Growing urbanisation is increasing the burden on service providers as people who move from rural areas generally lose access to their customary land and become less self-sufficient. More than 40 per cent of the population is under the age of 14.

The resulting youth bulge is outstripping very limited formal sector employment opportunities. The needs of the private sector are evolving, and skills development is critical. New immigrant groups are moving in to Papua New Guinea and taking over small and medium businesses that have typically been run by locals, adding further societal and employment pressures.

This paper will chart these trends in Papua New Guinea, and the impact they will have on political stability, policymaking and development. It will look at trends in service delivery, employment, and skills development. It will look at the role of new immigrants in Papua New Guinea and future workforce capacity, and assess the government's capacity to deal with these challenges.

## SNAPSHOT OF PAPUA NEW GUINEA

Table 1: Papua New Guinea at a glance

Land area	461,937 km <sup>2</sup>
Marine jurisdiction	3.1 million km <sup>2</sup>
Population	8.251 million (est) <sup>1</sup>
Population growth rate	3.1% (2015)
Human Development Index	0.516 (2015), ranked 154 out of 188 countries <sup>2</sup>
GDP	US\$ 21.2 billion (2015) <sup>3</sup>
GDP growth rate	2.5% (2017) <sup>4</sup>
GDP per capita	US\$ 2,745 (2015) <sup>5</sup>
Structure of economy (top 5)	Extractive industry: 24%; Agriculture, Forestry and Fishing: 18%; Retail trade: 10%; Construction: 8%; Administrative and Support services: 7% (2016) <sup>6</sup>
Composition of exports (top 5)	LNG: 33%; Gold: 27%; Agricultural, marine and other non-mineral: 12%; Oil/petroleum: 8%; Nickel/copper/cobalt: 8% (2016) <sup>7</sup>
Poverty (Basic Needs Poverty)	39.9% (2009) <sup>8</sup>
Employment	61.6% (2009) <sup>9</sup>
Infant Mortality Rate	58/1,000 (2009) <sup>10</sup>
Maternal Mortality Rate	733/100,000 (2009) <sup>11</sup>
HIV/AIDS Prevalence Rate	0.8% (2015) <sup>12</sup>
Gender Inequality Index	0.595 (2015), ranked 143 out of 157 countries <sup>13</sup>
Women in Parliament	0 (2017, decreased from 3 in 2012 elections)
Primary enrolment rate	50.9% (net 2009) <sup>14</sup>
Secondary enrolment rate	28.1% (net 2009) <sup>15</sup>
Access to potable water	25.8% (2009) <sup>16</sup>

On a wide range of social indicators Papua New Guinea remains one of the world's most underdeveloped nations. More than a decade of strong economic growth has not improved the welfare of most Papua New Guineans. GDP per capita is little different from that at independence 42 years ago. Incomes are also growing increasingly unequal, meaning that some are likely to be significantly worse off. Papua New Guinea will need decades more high and inclusive growth to offset its rapidly growing population. There will need to be better implementation of progressive social policies to translate inconsistent benefits of natural resource wealth to an improved standard of living for all people.



Improving Papua New Guinean welfare is not easy. It is a very young country made up of a patchwork of thousands of different cultures, its people largely living in rural areas, many of which are relatively inaccessible. The tension between traditional society, which still underpins the welfare system for most of the population, and the 'modern' world makes economic, social, environmental, and cultural development in Papua New Guinea complex. Papua New Guinean identity remains tenuous, with most citizens retaining a stronger allegiance to, and trust in, sub-national groupings, notably clans or *wantoks*, than at a national level.

In an effort to address these challenges, Papua New Guinea has developed a complex and decentralised system of government, with three tiers of government (national, provincial, and local), and four levels of administration (national, provincial, district, and Local Level Government (LLG)). In recent years District Development Authorities, chaired by the local MP and including the council presidents, have emerged as another prominent tier of government, often better resourced than other decentralised levels. In total the country is divided into four regions, 21 provinces (plus the National Capital District), 89 districts and 319 LLGs. The national government also maintains 33 ministries and over 140 departments and agencies, some with seemingly overlapping responsibilities and unclear or ambiguous lines of reporting. This has created significant confusion about who is responsible for what, making it difficult for communities to hold leadership to account:

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**“Today the PNG nation-state functions in a dysfunctional manner... because many of our politicians and bureaucrats are still learning how to manage public institutions independently of personal benefit and kingship loyalties.”**

Dr Joseph Ketan<sup>17</sup>

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Altogether the Auditor General is expected to audit nearly 1000 public institutions each year, including state-owned enterprises. Despite this proliferation of agencies, the public service is not much larger than at independence, while the population has nearly tripled, with some functions, such as police capacity, particularly lagging on a per capita basis.

Papua New Guinea is also a pluralistic nation. Its urban centres do not reflect the lifestyles, employment practices, and incomes of the 88 per cent of the population that live in rural areas. The United Nations Development Programme estimates Papua New Guinea to have the second-highest rural–urban population balance in the world after Burundi.<sup>18</sup> PNG's Director of the Office of Urbanisation notes that this partly reflects the outdated delineation of urban boundaries as towns and cities have grown, with urban populations having expanded significantly over recent years.<sup>19</sup>

According to best available evidence, the proportion of the population living below the basic needs poverty line rose from 34 per cent in 1996 to 36.2 per cent in 2009/10, meaning approximately 2.43 million people are living in hardship.<sup>20</sup> The majority of the population live in areas of poor infrastructure and often rugged terrain, which gives them little or no access to basic services, such as health, education, sanitation, and safe drinking water.

Poverty remains a contested concept in Papua New Guinea. The abject poverty seen in many parts of the world is largely absent from Papua New Guinea, or at least hidden by subsistence food production which also masks the high levels of malnutrition and stunting prevalent in rural Papua New Guinea.<sup>21</sup> The poverty experienced by more than 2.4 million people in Papua New Guinea is rather one of opportunity and income. Papua New Guinea has yet to meet any of the Millennium Development Goals.

## SERVICE DELIVERY

Services are delivered in Papua New Guinea through a patchwork of government agencies, non-government organisations and, critically, church and faith-based organisations. The country benefits from a very strong network of churches that, with government funding, run about half of the country's health and education systems, particularly in rural areas.<sup>22</sup> Services across many parts of the country are perceived to have diminished over the past two decades. Progressive cash shortages, a weakening of institutional capabilities, the marginalisation of government departments, growing prevalence of corrupt practices (including in public procurement) and lack of clarity with poor coordination of responsibilities present enormous challenges. These combine with inadequate investment in education and skills development from the mid-1990s and decline in recruitment and mentoring of successor staff, leading to an erosion of skills in the service delivery workforce, and the decline of infrastructure and materials. All these factors contribute to the shrinking role of the state.

The PNG Government's *Vision 2050* report notes that "PNG's global Human Development Indicators (HDI) ranking dropped from 128 out of 175 countries in 1994 to 145 out of 179 countries in 2005. This reflects our worsening social indicators and marked improvements in other countries' socioeconomic indicators."<sup>23</sup> Papua New Guinea's HDI ranking puts it higher than only Timor-Leste and Afghanistan in the Asia-Pacific region.

A recent National Research Institute–Australian National University survey of schools and health clinics around Papua New Guinea, in both rural and urban areas, found a more nuanced and mixed progress in 2012 compared to 2002.<sup>24</sup> Schools were on average in better condition and had more students and teachers. Health clinics on the other hand showed no growth at all in the number of patients using them, despite population growth of about 30 per cent over the decade. The O'Neill government's commitments to free health and education for all PNG citizens have yet to translate into tangible improvements.

Expenditure in critical services, as well as vital infrastructure that supports service delivery, has also been slashed in recent years as the government battles considerable fiscal challenges and cash shortages and seems unduly focused on urban 'status' projects (notably the Pacific Games and APEC 2018).

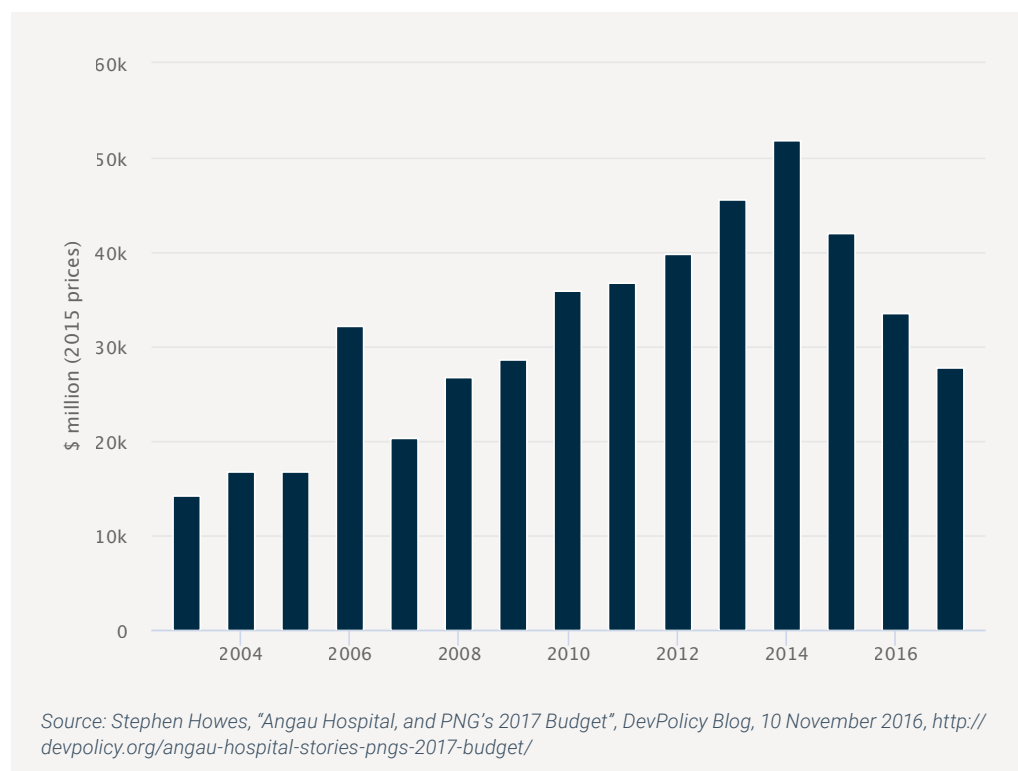


## HEALTH

Papua New Guinea's human capital development and labour productivity are hindered by deficiencies in basic nutrition, health, and education. The overall state of citizen health in Papua New Guinea is poor, and has declined since 1975. Papua New Guinea has the lowest level of health care expenditure in the region, equivalent to about 3.5 per cent of GDP in 2014.<sup>25</sup> Clinic capacity is significantly impaired — 30 per cent of staff are not paid on time, 43 per cent of clinics need significant maintenance, 60 per cent do not have electricity or refrigeration, 73 per cent conduct no patrols in the local community.<sup>26</sup> Urban health infrastructure is also not faring well, with marginal investment despite growing urban populations. The Asian Development Bank has forecast that per capita spending on health in 2005 was half what it had been in 1975.<sup>27</sup>

With strong support from development partners, non-government organisations and the private sector, some progress has been achieved in restraining the country's burgeoning HIV/AIDS infection rate, malaria incidence, and by making anti-retroviral drugs available. Tuberculosis, where Papua New Guinea exhibits some of the highest rates in the world with an increasing prevalence of multi-drug resistant strains, and other diseases strain the poor health infrastructure. Life expectancy is increasing, but is still the lowest in the region. Although statistics are unreliable, Papua New Guinea does appear to have achieved a steady decline in under-five mortality rates during the last two decades, but the rate of reduction is much lower than in other Asian countries. If health indicators are not improved soon there is considerable risk that more than 50 per cent of the population in the future will suffer from some effect of stunting.

**Figure 1: An illustration of funding constraints: Angau hospital (Lae) allocated budget**



There is, as in education, a variation in performance between provinces, with better innovation and coordination of effort and utilisation of resources in some, which could act as potential role models for others. The introduction of Provincial Health Authorities has enabled better coordination between provincial hospitals and rural health services, but coordination of responsibilities with the new District Development Authorities will be critical if they are not to impose a further stumbling block or overlap of duties.

## EDUCATION

One of the key determinants of a household's welfare level in Papua New Guinea, in addition to women's education and empowerment, is the education level of the household head.<sup>28</sup> However, the consensus from progressive reviews is that the quality of Papua New Guinea's education and technical training facilities has been deteriorating for at least 20 years.<sup>29</sup> This has resulted in a decline in the quality of the workforce and dramatically increased the cost of internal business training.<sup>30</sup> Although the elite schools in a few main urban centres, often church run, have relatively high standards, the majority of PNG's citizens are not educated beyond Grade 10, and those achieving Grade 12 from many provincial schools fail to achieve satisfactory standards, even in some core subjects. While intake and retention rates have risen, students are becoming progressively less equipped to meet the changing and higher skills-based requirements of PNG's workforce. A survey of financial literacy in Papua New Guinea undertaken with the Bank of Papua New Guinea (albeit with a relatively small sample) found that although younger people were more competent at using formal and IT-based financial services, older respondents were more competent at most aspects of managing money, and more likely to have had financial literacy training. Competency in the use of English language was a major factor, if not determinant, in financial literacy and access to financial services, with women and especially rural women having markedly lower levels of English and financial literacy and access to financial services.<sup>31</sup>

Despite these poor educational outcomes, public expenditure on education is not low by international standards and compares relatively well against other countries in the region,<sup>32</sup> averaging around 5 per cent of GDP and 15 per cent of the national budget. Distribution of these resources remains a critical issue, as does the proportion absorbed by wages and administration. Technical and vocational education and training (TVET) have also been badly under-resourced for decades, even though many students, particularly males, seek greater emphasis on practical work skills during school years.<sup>33</sup>

There has been some improvement since the implementation of Tuition Fee-Free education. Student entry and retention have increased, but limited infrastructure, a lack of trained teachers (especially at elementary level), overfilled classes, deficiencies in curriculum, inspection, and support capacity have eroded standards and the perceived utility of education.

A recent review of aspects of education policy has prompted some positive reforms, including to the much-derided elementary education, which will now require properly trained teachers for younger children in their critical learning years. Other positive initiatives include upgrading qualifications of primary school teachers to three-year degrees, removing older students from lower primary grades, and providing greater support for separate adult and distance learning education. These measures will be resource-intensive, however, and vulnerable to budget pressures.

## DEMOGRAPHICS

Service delivery challenges in Papua New Guinea are exacerbated by rapid population growth. Papua New Guinea has one of the fastest-growing populations in the world. With an average annual growth rate of 3.1 per cent at the 2011 Census, PNG's population increased by more than two million people between 2000 and 2011, and more than doubled from independence in 1975 to 2011. If current growth rates continue, the population will more than double again by 2040.

Compounding these demographic challenges is the changing breakdown of the population. Papua New Guinea is a very young country. Its median age is 21.7, half that of high-income countries and two-thirds that of middle-income countries. More than 40 per cent of its population are under the age of 15. However, population growth shows signs of slowing, with the number under 5 years old falling from 16 per cent in 1980 to 12 per cent in 2011. Counterbalancing this trend, the population over 65 is also rising, albeit at a slower rate.

Despite the pressures this population growth places on services and infrastructure, the PNG Government has paid little attention to population policy and planning. While a new National Population Policy for 2015–2024 made some constructive recommendations, it requires resources, coordination and commitment to implementation, all of which remain elusive.

**Figure 2: Papua New Guinea's population 2000–2040**

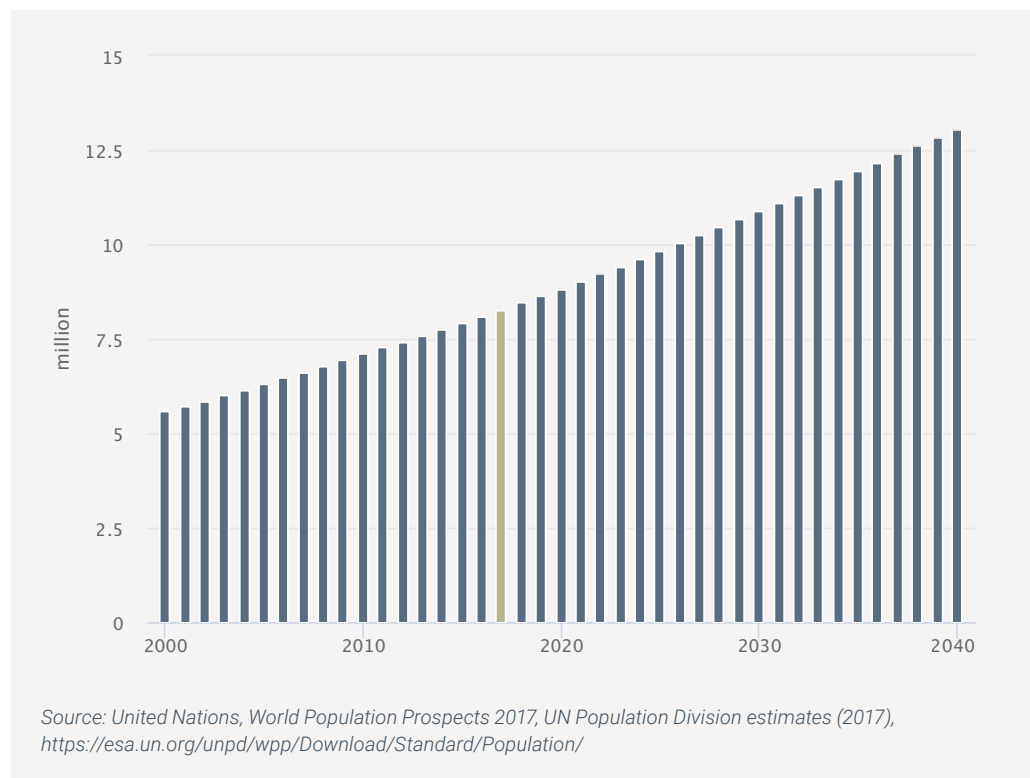
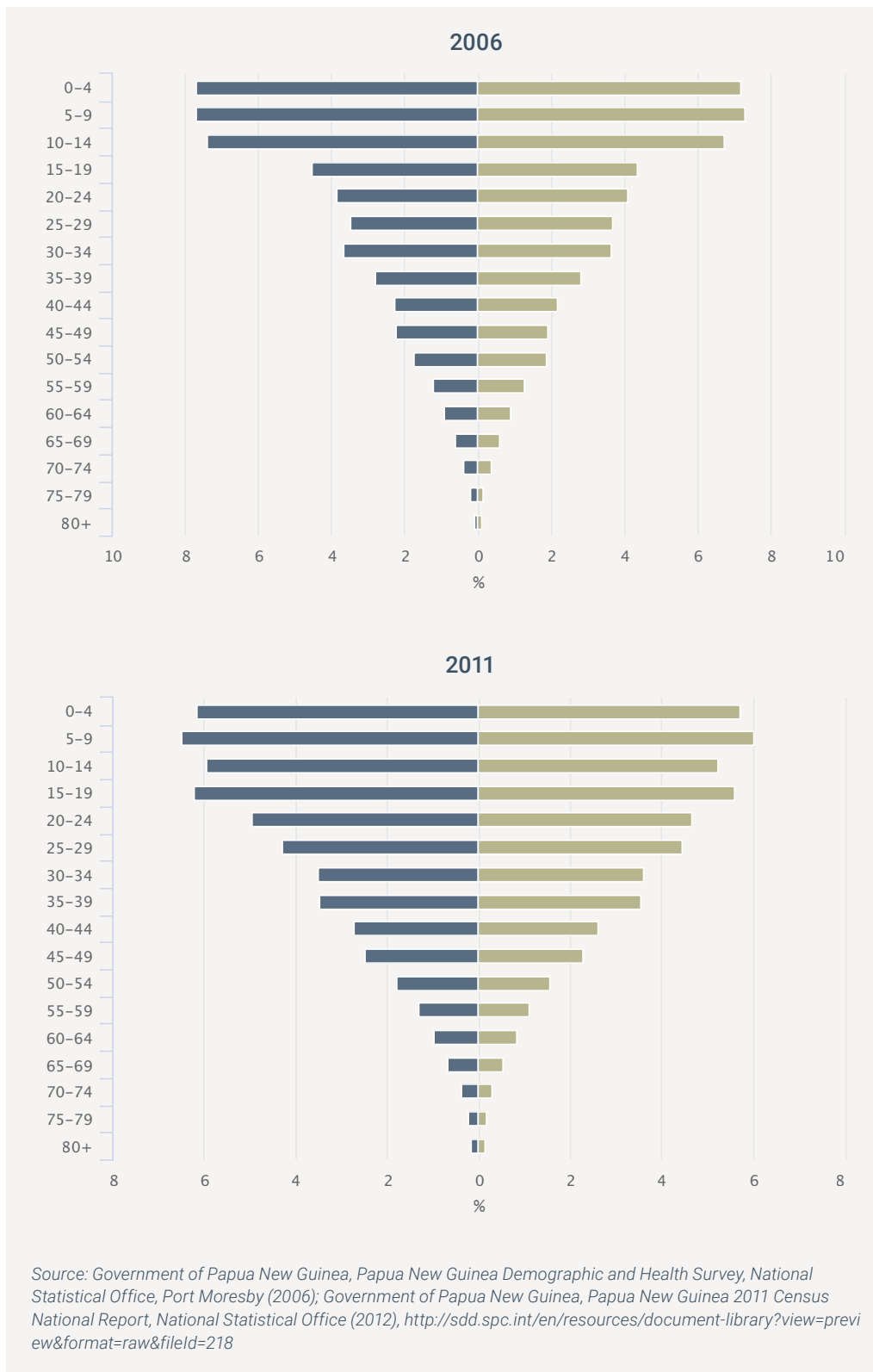


Figure 3: Moving up – PNG population pyramid 2006 and 2011



## URBANISATION

According to 2011 Census data, 40 per cent of the population in urban areas were not born there, indicating a major shift to urban centres, even though these centres are modest compared with peer developing countries.<sup>34</sup> Urban boundary definitions make it difficult to quantify the rate of urbanisation in Papua New Guinea, however, and the real shift may be substantially greater when those living in the growing hinterlands of the cities are included.

This urbanisation has placed pressure on employment. The urban rate of unemployment is relatively high at 16.2 per cent, while the rural rate (including informal employment) is only 5.2 per cent.<sup>35</sup> The labour force participation rate in urban areas is more than 22 per cent lower than the national average, due primarily to the low participation rate in the National Capital District.<sup>36</sup>

This lack of opportunity experienced by many migrating to urban areas in search of formal waged employment is a likely contributor to the ongoing security dynamics in Papua New Guinea's urban centres.

## GENDER

Gender inequality in Papua New Guinea is perhaps its single largest development challenge. Violence against women is extremely high, while PNG's systems of family and community relationships often exclude women from leadership and decision-making roles. Papua New Guinea is now one of only five countries in the world with no female members of parliament, despite a record number competing in the 2017 elections.

Men are twice as likely as women to hold a job in the formal sector, while women in that sector earn on average less than half that reported by men.<sup>37</sup> With such a large number of PNG's potential workforce disadvantaged and disenfranchised, the country's development potential is impaired. The government urgently needs to prioritise gender inclusivity, starting with parliamentary representation.

## EMPLOYMENT TRENDS IN PAPUA NEW GUINEA

Official PNG data indicate a very high level of employment. However, because they include subsistence employment, they mask the very low level of formal wage employment, which is less than 6 per cent of the total population, and extremely low for people below the age of 20.<sup>38</sup> Best estimates put the size of the formal employment market in PNG at 465 000 in 2014<sup>39</sup> meaning that only about 10 per cent of household heads are engaged in wage employment,<sup>40</sup> with 15 per cent of the country's working-age population employed in the formal sector.<sup>41</sup>

**Table 2: Estimate of the 2014 labour force**

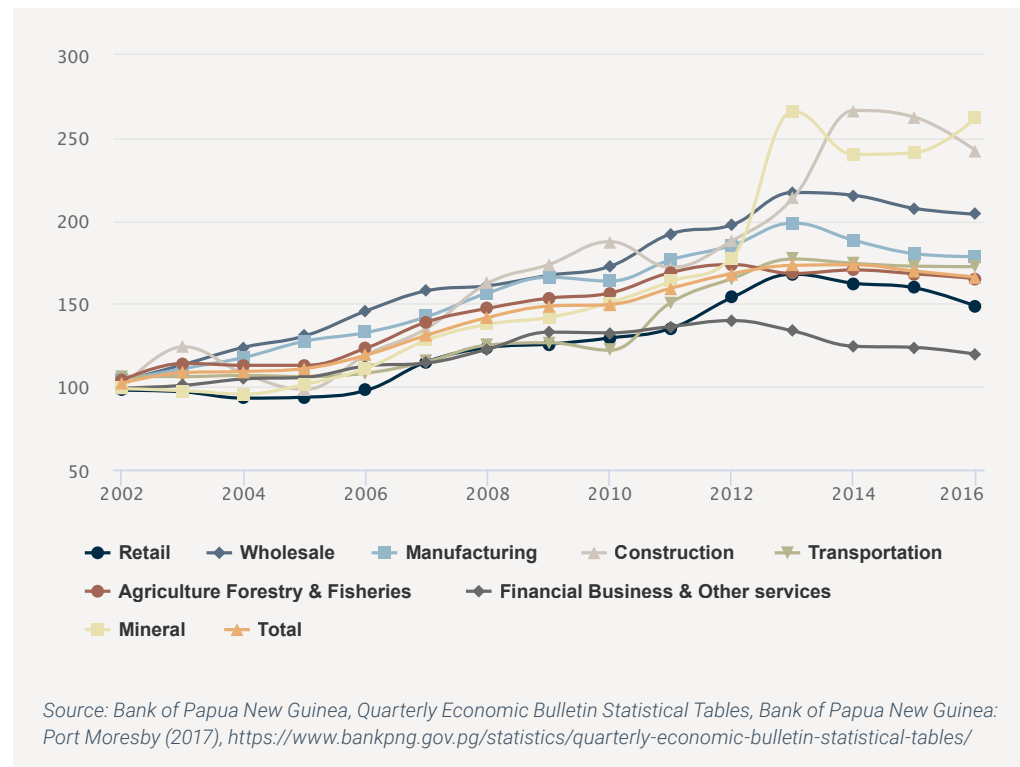
	Measured 15–64 years	%
<b>Projected total in-scope population</b>	4,584,341	
<b>Labour force</b>	3,071,509	67%
<b>Employed [economically active]</b>	2,979,363	97%
<b>Formal wage employment</b>	465,000	15%
<b>Informal employment [incl. subsistence employment]</b>	2,514,363	82%
<b>Wage unemployed [actively seeking wage employment]</b>	92,145	3%

Source: Luke Jones and Paul McGavin, "Grappling Afresh with Labour Resource Challenges in Papua New Guinea: A Framework for Moving Forward", Institute of National Affairs Discussion Paper 96, June 2015

The majority of employment opportunities are limited to just four industrial sectors: education (15 per cent), construction (11 per cent) and mining and quarrying (13 per cent). These sectors account for 52 per cent of all formal wage employees. The mining and quarrying sector (including hydrocarbons) provides just 2 per cent of formal wage employment but supports a significant amount of wage employment in other sectors of the economy.<sup>42</sup>

While very low, formal employment growth grew by 66 per cent between 2002 and 2016 (compared with population growth of 42 per cent). PNG's nominal GDP (both mining and non-mining) has tripled over the same period. However, employment levels have diminished since 2014 as economic growth continues to slow.

This employment growth masks difficult realities for PNG's young population. The ADB estimates that over 50 000 youths enter the labour market each year, while only a few thousand formal jobs are being created.<sup>43</sup> The figure of 50 000 has been routinely quoted since the 1990s, and is in need of revision. The Department of Education reports that 23 692 students completed Grade 12 in 2016,<sup>44</sup> competing for roughly 5000 places in tertiary institutions.<sup>45</sup> Considering the majority of Papua New Guineans do not make it to Grade 12, the estimate of 50 000 youths entering the labour market each year is likely an underestimate.

**Figure 4: Employment growth in PNG**

There is no information available on labour force productivity, and limited information on other key labour force statistics. The most comprehensive data available is from a 2014 labour market survey. Table 3 and Table 4 show the distribution of salary in the PNG workforce from that survey.

**Table 3: Estimated annual average salary by sector July 2014 (nominal kina)**

	Mean	Min	Max
<b>All sectors</b>	21,330	208	4,133,100
<b>Government</b>	22,106	4,379	320,941
<b>Private</b>	19,459	286	4,133,100
<b>Private – Informal</b>	32,523.34	208	675,844
<b>Private – Unregulated employee</b>	5,942.91	2,330	13,104

Note: Data from these tables is not drawn from a random sample and, therefore, cannot be used to estimate national wage and income levels. A total of 135 610 (including employers) did respond to this survey, making it the most robust source of information available.

Source: Luke Jones and Paul McGavin, "Grappling Afresh with Labour Resource Challenges in Papua New Guinea: A Framework for Moving Forward", Institute of National Affairs Discussion Paper 96, June 2015



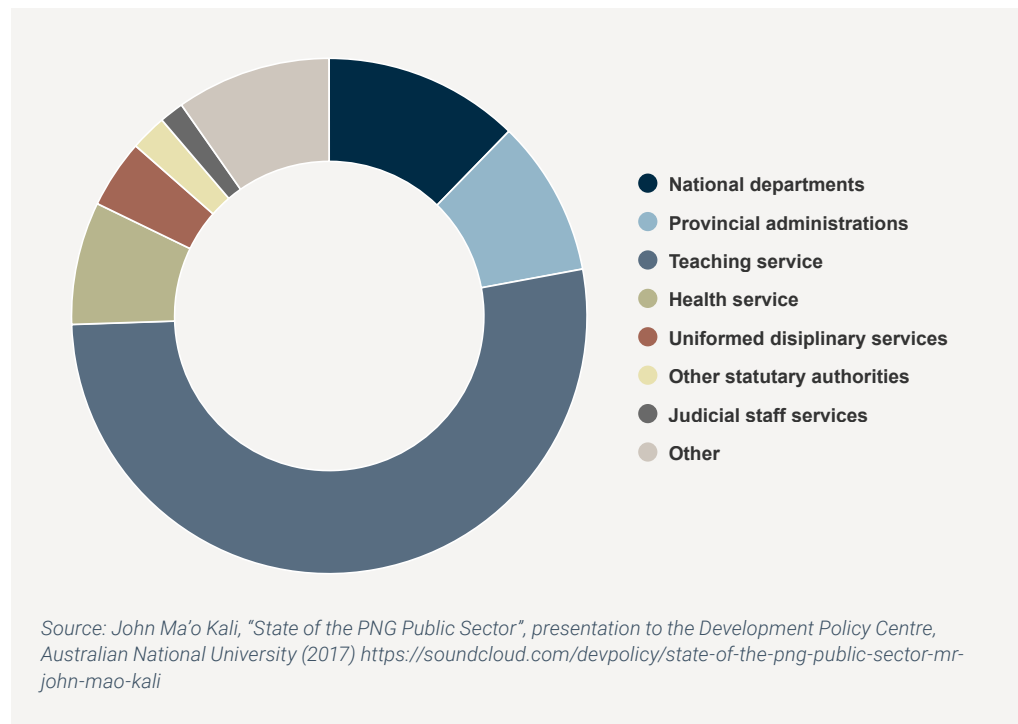
**Table 4: Average gross fortnightly salary by occupation July 2014 (nominal kina)**

	Mean	Min	Max
<b>Armed forces occupations</b>	983	229	2,512
<b>Managers</b>	3,511	133	1,617
<b>Professionals</b>	825	168	59,053
<b>Technical and associate professionals</b>	1,123	132	13,902
<b>Clerical support workers</b>	715	41	5,424
<b>Services and sales workers</b>	665	35	12,653
<b>Skilled agricultural, forestry and fisheries workers</b>	431	19	167
<b>Craft and related trade workers</b>	772	90	3,779
<b>Plant and machine operators and assemblers</b>	667	19	4,146
<b>Elementary occupations</b>	337	8	15,026
<b>Other</b>	903	18	17,331

*Note: Data from these tables is not drawn from a random sample and, therefore, cannot be used to estimate national wage and income levels. A total of 135 610 did respond to this survey, making it the most robust source of information available. (Note: the perhaps surprising low average salary for professionals is largely because teachers comprise the majority of this category, with a large portion on relatively modest salaries).*

*Source: Luke Jones and Paul McGavin, "Grappling Afresh with Labour Resource Challenges in Papua New Guinea: A Framework for Moving Forward", Institute of National Affairs Discussion Paper 96, June 2015*

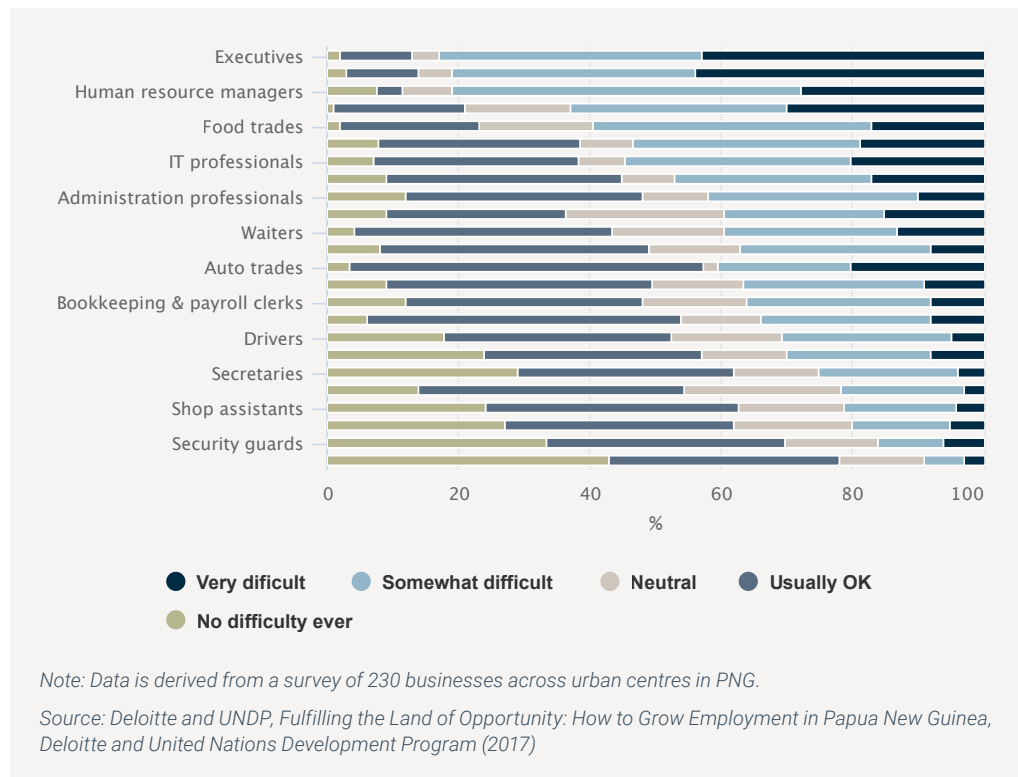
At 105 000 strong, the public service makes up just under a quarter of Papua New Guinea's formal waged employment opportunities and is by far the largest employer in the country. Despite its importance to formal sector employment, its overall numbers have not kept pace with population growth. The total number of public servants in the central government at independence was 25 951, more than present day. In addition, there were 4034 government-funded teachers (in 1971–72) and 6137 health workers (1972–73). The increase to over 100 000 can almost wholly be accounted for by the increase in the number of teachers.<sup>46</sup>

**Figure 5: Size and composition of the public service**

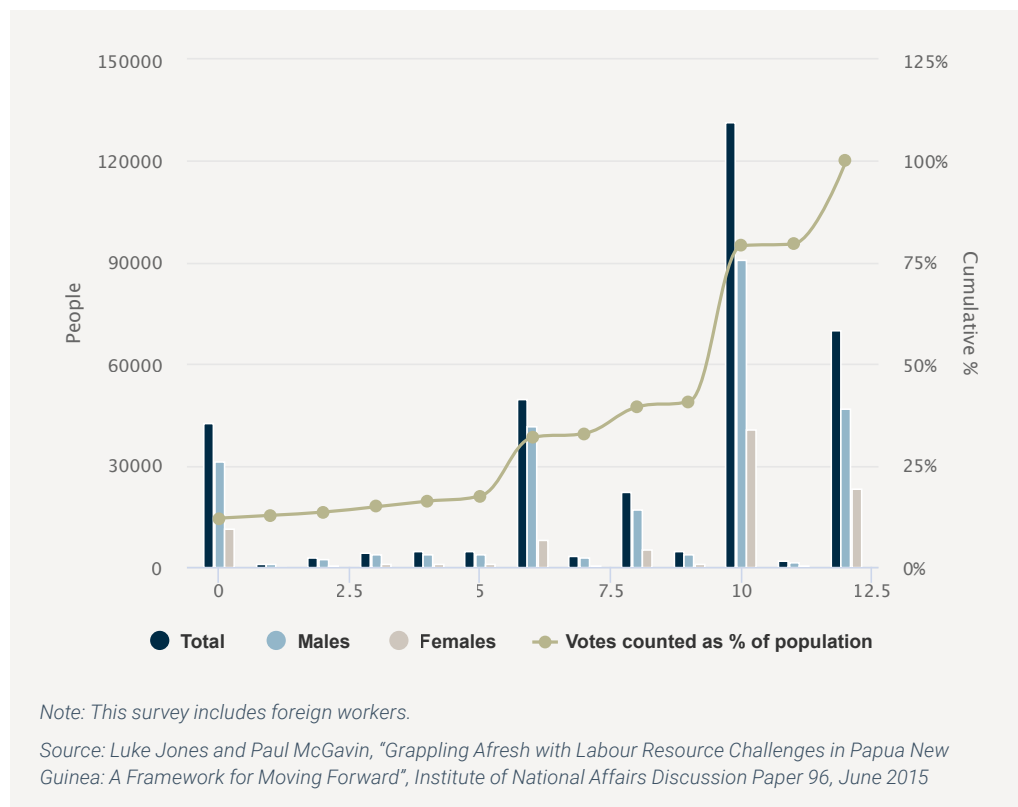
While investment and formal business activity would provide further employment opportunities in Papua New Guinea, numerous business surveys have found that they face myriad constraints:<sup>47</sup> law and order, corruption, poor transport infrastructure, poor telecommunications and electricity infrastructure, availability of skilled labour, political uncertainty and stability of rules. In 2017, access to foreign exchange has become a leading constraint, and skills shortages are cited by most businesses as a key issue.<sup>4849</sup>

Any labour market gains have been small, and concentrated in Port Moresby.<sup>50</sup> In addition, the indigenous Papua New Guinean workforce has not fully benefitted from the country's recent economic growth and private sector expansion due to skills shortages in the workforce. The low rate of tertiary graduates, combined with limited technical and vocational opportunities in the country have resulted in a deficient domestic availability of skilled labour. Papua New Guinean engineers, qualified accountants, executives, and other skilled technicians are scarce.<sup>51</sup>

**Figure 6: Recruitment difficulties across occupations**



**Figure 7: Highest grade of schooling completed by formal wage employees**



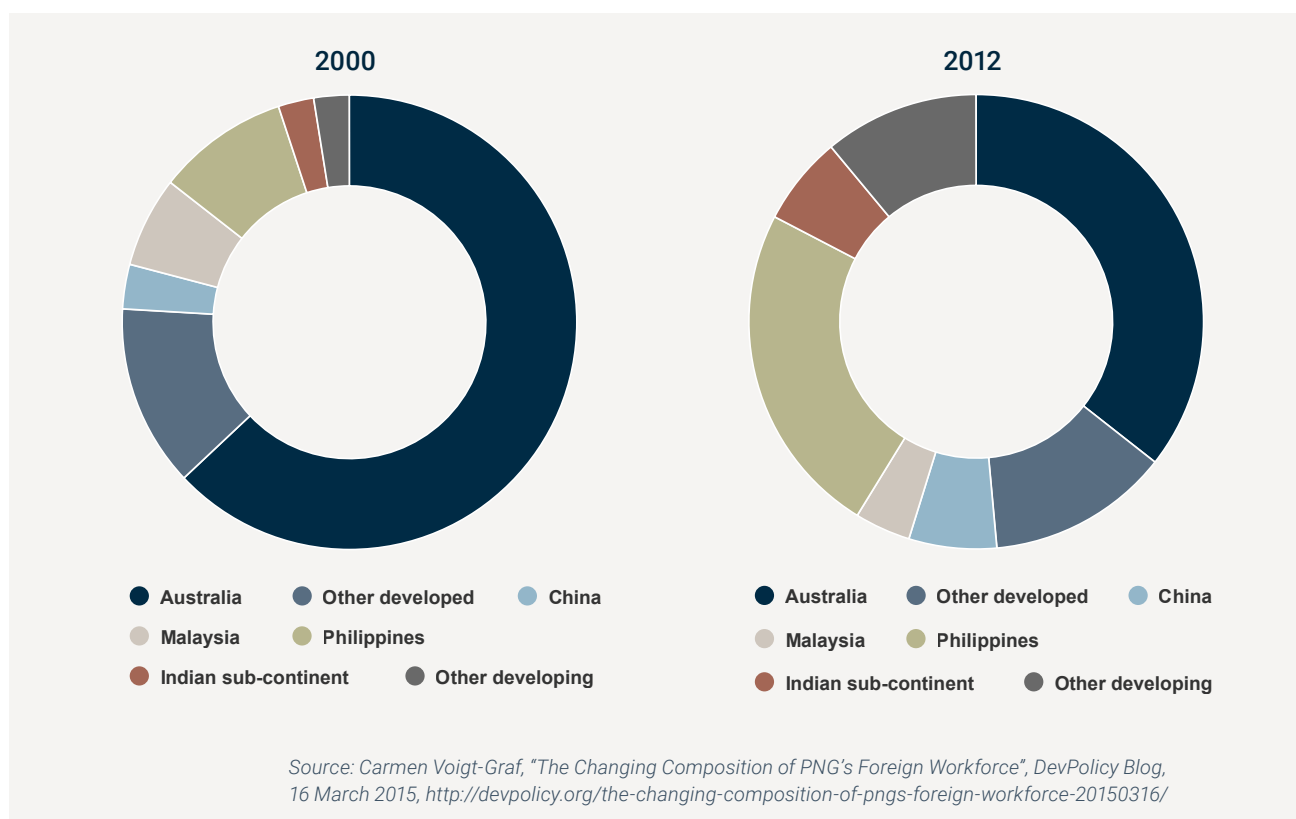
The private sector's response to this skills shortage (complementing efforts by state and development partners) has been to employ foreign workers and to provide a range of in-house and formal training and skills development, although some businesses take the responsibility of staff training markedly more seriously than others. Very high staff turnover limits the impact of these training schemes, thereby further increasing a reliance on foreign workers.<sup>52</sup>

## FOREIGN WORKFORCE

Papua New Guinea's foreign workforce makes up a significant component of formal sector employment in Papua New Guinea. Between 2010 and 2014 a total of 103 394 work permits were issued by the Department of Labour and Industrial Relations<sup>53</sup>, indicating a foreign workforce of at least 20 000 individuals. Arrival and departure data has shown an explosion of employment arrivals from 13 000 in 2000 to 63 000 in 2012. These numbers, however, include workers that routinely return home during the year, such as fly-in-fly-out Australians.<sup>54</sup>

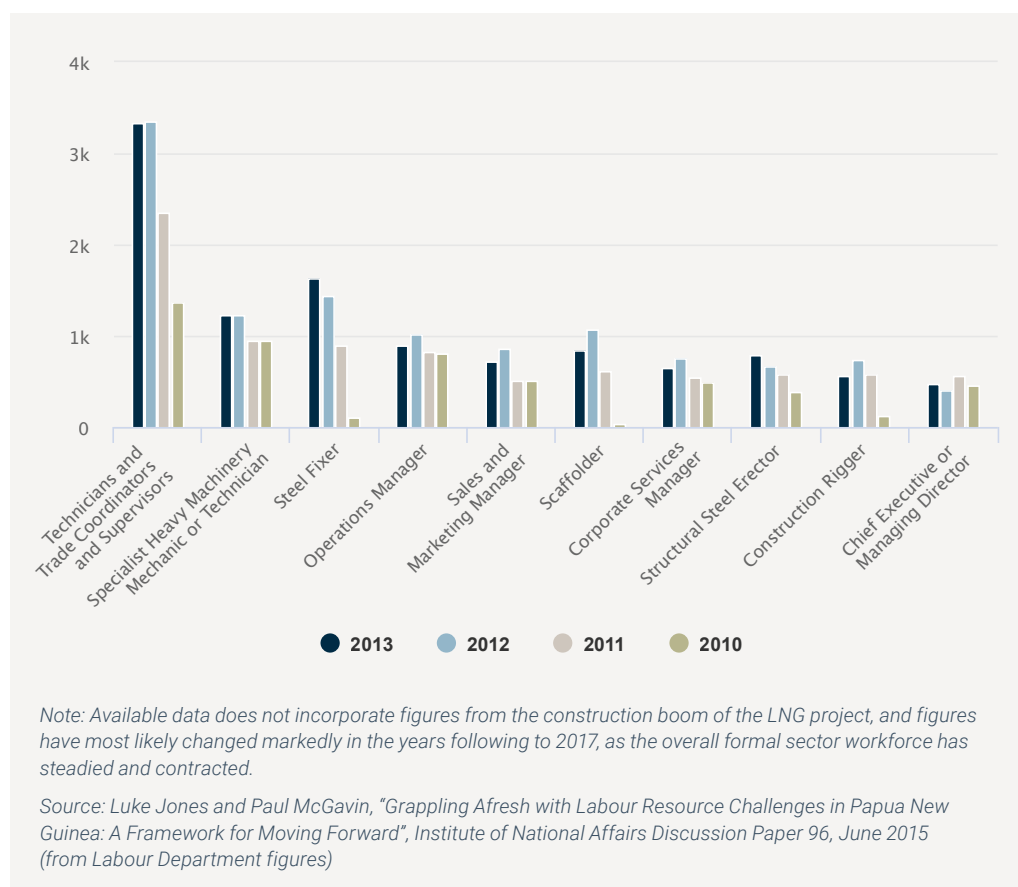
The composition of PNG's foreign workforce is also changing. While Australia is the main source country of new foreign employees, workers from the Philippines are increasing rapidly in number, and may soon become the largest single source of employment.<sup>55</sup>

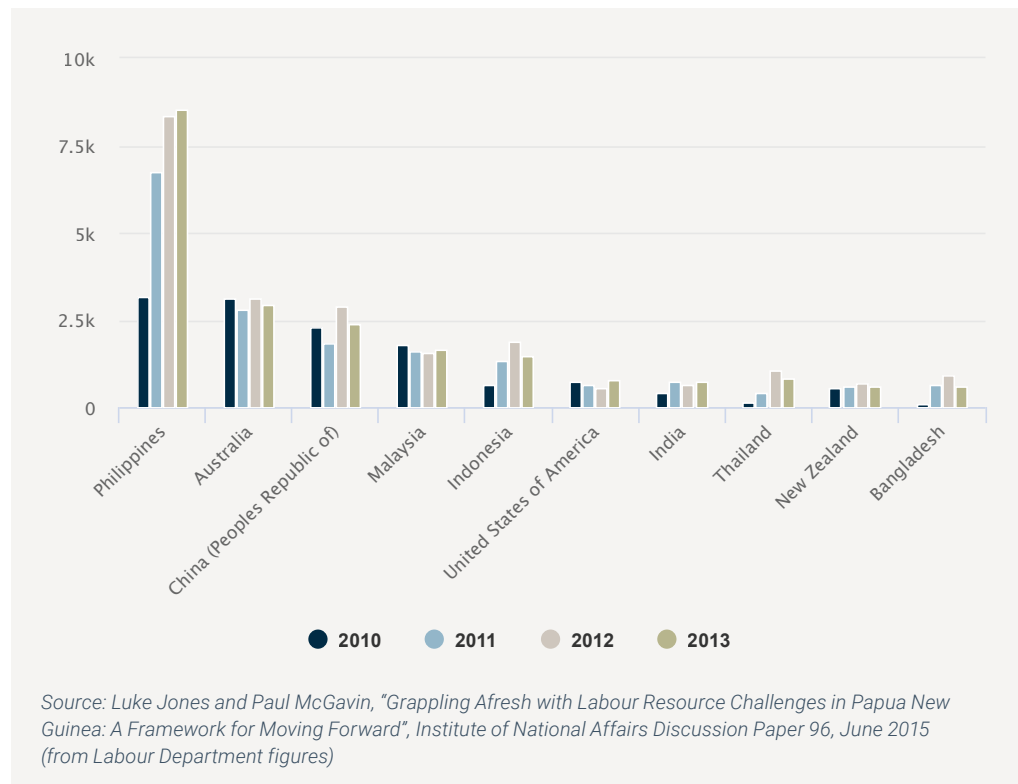
**Figure 8: Changing configuration of PNG's foreign workforce**



Official numbers also may omit significant numbers of illegal immigrants, those without work permits and those mis-specifying their migration details, such as labelling themselves as tourists or on business visas, when coming for longer-term work and as small-scale investors.

**Figure 9: Top 10 nationalities for which work permits were issued, 2010–2013**



**Figure 10: Top 10 job types for which work permits were issued, 2010–2013**

PNG's growing economy has attracted an increasing number of highly skilled and vocational and technical workers (particularly in the trades), both of which are in short supply in Papua New Guinea. As Jones and McGavin point out, "many of the skill sets brought into PNG over the 2010-13 period were ones that might well have been performed by Papua New Guineans".<sup>56</sup>

Foreign ownership of small and medium business in Papua New Guinea is also growing at a disturbing rate. Anecdotal evidence suggests that many businesses that were traditionally owned by Papua New Guineans are now being taken over by foreign individuals, notably new generation Chinese and more recently Bangladeshi migrants. Some of these small or micro-enterprises are owned in partnership or under the nominal ownership of a local partner, and found even in some of PNG's more remote communities such as around major logging and associated projects. While they provide useful services, and may be less risk-averse than PNG locals, there is evidence they may operate uncompetitively by accessing goods without being subject to import duties, for example. These so-called 'unregulated businesses' largely bypass income tax, GST, and other rules such as labour laws.

Apart from the loss of revenue to government, the risk is that PNG citizens become progressively excluded from the domestic labour market. The government has proposed various responses, many of which are enshrined in their Small and Medium Business Policy Proposal. The private sector has responded favourably to some of these policies, but are concerned that others will curb the future foreign investment which is critical for Papua New Guinea's continued development.<sup>57</sup> The consensus, however, is that some level of

further protections must be put in place to ensure opportunities for Papua New Guinea's domestic workforce. For example, the SME policy extends the existing list of 'restricted businesses' in which only Papua New Guineans may participate, although such restrictions have proven difficult to enforce. These changes run the risk of becoming overly nationalistic, too expensive, and scaring off much needed positive foreign direct investment.

The priority for government is to invest in technical and vocational training, as well as facilitating financial services for small businesses, while managing business policy carefully to ensure the private sector continues to grow and fuel job creation.

## LOOKING FORWARD

The outlook for societal trends in Papua New Guinea is bumpy at best. The combined headwinds of a youth bulge approaching its peak, few formal sector employment opportunities and weak service delivery will be difficult to overcome. The government will need to redouble its efforts to implement existing policies and develop new ones that will ensure growing opportunities for Papua New Guineans.

Despite these challenges, there are also significant opportunities, whether from education, skills development, private sector regulation, health and addressing gender disadvantage, as well as other actions to remove constraints on business and investment. The education sector is not underfunded by regional standards, but expenditure needs to be better targeted and utilised, including investment into quality education, TVET, and improving PNG's tertiary institutions (including enhanced teacher training), so that PNG's growing number of graduates are properly prepared to meet the demands of the workforce. The government could find some easy wins in health by improving immunisation coverage, health awareness, improved pharmaceutical procurement and distribution, and actively promoting family planning. Recent reviews of the health, education, tax, and SME sectors should be considered by government, after close consultation with the private sector and civil society groups (including churches), to ensure that they can support both Papua New Guinea and private sector development. The government should focus its efforts on enhancing gender inclusivity, improving data quality to guide better investment decisions, improving teacher training, improving the primary education system, and reinforcing and streamlining governance and accountability systems across the board.

The government has produced a substantial number of plans to address the development challenges of Papua New Guinea.<sup>58</sup> In some cases these need revising or refining, in partnership with stakeholders. But generally, what is needed is to turn these plans into action, and to implement policy effectively across the extremely complex systems of government. Above all the government must refocus its attention and expenditure away from status projects and back to the basics: the country's greatest natural resource, its people.



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## INTERNAL SECURITY IN PAPUA NEW GUINEA: TRENDS AND PROSPECTS

SINCLAIR DINNEN

### INTRODUCTION

Concerns about personal security have been prominent in Papua New Guinea for many years. Personal security figures regularly in travel advisories issued by foreign governments. International news coverage of Papua New Guinea is often about violence or crime, reinforcing the country's reputation as a dangerous and lawless place. A visitor to Port Moresby, the sprawling national capital, sees evidence of this in the elaborate security arrangements that shape the urban landscape. Drivers of insecurity in this young nation are complex and multidimensional, stemming from the legacies of a recent colonial past, along with the ongoing challenges of state consolidation and the uneven effects of economic globalisation.

The main security threats are non-traditional, including urban crime, gender-based violence, corruption, arms trafficking, border protection, resource poaching, climate change, natural disasters, and transnational crime. Although some view China's growing presence as a potential threat, its activities in Papua New Guinea have been largely confined to diplomacy, development assistance and investment. Prime Minister Peter O'Neill has acknowledged the absence of any "distinct conventional external threat",<sup>1</sup> while PNG's National Security Policy recognises the developmental and political character of the country's security challenges.

Papua New Guinea is one of the world's most complex development environments. Its population of almost 8 million people is dispersed across a vast and challenging topography, rendering effective administration and economies of scale hard to achieve. Around 85 per cent live in rural areas, reliant on a combination of subsistence agriculture and cash-cropping. Although it has the lowest urbanisation rate among Pacific Island countries, Papua New Guinea has the biggest urban population, at around 800 000 to 1 000 000 people.<sup>2</sup> Well over half this number live in Port Moresby,

making it the largest city in the region. While its population has more than trebled since independence in 1975, shortage of land and affordable housing has led to the growth of large and poorly serviced informal settlements. Limited employment opportunities and the high cost of living add to the hardships facing many urban residents.

Papua New Guinea is richly endowed in natural resources, ranging from fisheries and timber to oil, gas and high-value metals such as copper, gold, and nickel. However, despite over a decade of sustained economic growth — averaging 6.2 per cent from 2002 to 2014 — resource poaching, corruption, and maladministration have diluted the economic benefits and these have not been converted into broader development gains. While there has been progress in some areas, social and economic indicators remain disappointing, with Papua New Guinea ranked a lowly 154 out of 185 countries in the 2016 Human Development Index. Although by no means inevitable, large-scale extractive projects in Papua New Guinea have also been associated with conflict stresses and social corrosion, as demonstrated most vividly in the Bougainville Crisis.

Disappointing development outcomes highlight the fragilities of the PNG state and the politics that have shaped its post-independence development. Much has been said about Melanesian politics, including its ‘unbounded’ character with weak parties, and lack of policy coherence. A growing proportion of public resources have been channelled into poorly regulated discretionary funds controlled by individual politicians. This political reordering has undermined bureaucratic systems of service delivery, reinforced patterns of uneven development, and facilitated corruption by entrenching patronage as the main mechanism for the delivery of ‘development’ and other services.

The small Papua New Guinea Defence Force (PNGDF) has extremely limited capabilities. Policing and justice services are also thinly spread, leaving issues of security and dispute resolution to be managed informally in many areas, through resort to quasi-traditional approaches embedded in local communities. In areas of large-scale resource development, extractive companies often provide security services and engage with locally based police and other law and justice actors. The RPNGC has long struggled against growing problems of insecurity, with manifestly inadequate numbers and resources. Police have also been implicated in the perpetuation of violence and serious human rights abuses. The exponential growth of private security — considered by some to be the country’s third-largest source of employment — reflects the security concerns of the well-off and diminishing confidence in the police.

This paper examines some of the key trends in PNG’s security environment with a view to considering how they are likely to affect the country’s political and economic stability. The following section briefly considers PNG’s external and internal security environments and the respective challenges they pose. An outline of the most pressing ‘law and order’ issues follows. An examination of the struggles of public policing and rise of private security indicates the shifting landscape of security governance in Papua New Guinea and the risks and opportunities it presents.

## MAIN THREATS TO SECURITY AND STABILITY: EXTERNAL AND INTERNAL

There is broad consensus that while Papua New Guinea lacks any serious external threats it is faced with increasing non-traditional threats and an urgent need to strengthen its security agencies. Papua New Guinea's National Security Policy, launched in 2013, identified the most immediate challenges as: law and order; graft, corruption and good governance; human rights abuses and gender-based violence; lack of border control; natural disasters and climate change; arms trafficking and proliferation; illegal poaching of resources; drugs, alcohol and substance abuse; microbial attacks on plants, animals and human lives; and medical emergencies including HIV and AIDS, tuberculosis and malaria. Second order threats include external and internal military aggression, cyberattacks, food security, land security, population growth, and climate change.

In the absence of conventional threats, the PNGDF has struggled to carve out a traditional security role or establish a niche function such as Fiji's international peacekeeping operations. A long history of disciplinary problems is believed to stem more from leadership issues and grievances over working conditions than from overt political ambitions. Even during the tumultuous Sandline Affair in 1997, when the PNGDF rebelled against a decision to deploy foreign mercenaries in Bougainville, no attempt was made to take over government. The prospect of a military coup in Papua New Guinea is unlikely as such a small force — just over 2000 personnel — would not achieve anything more than a temporary and geographically circumscribed takeover of government in such a large and politically fractious country.

Arguably the most critical role for the PNGDF is in protecting PNG's land and maritime borders from the non-traditional challenges, such as resource poaching and gun smuggling, identified in the 2013 White Paper. Such a task is complicated by the small size of the PNGDF and PNG's extensive maritime economic exclusive zone (EEZ), as well as its long land border with Indonesia. Although Australian-supplied patrol boats have greatly assisted maritime surveillance, lost fishing revenues from illegal, unreported, and unregulated fishing in the zone are believed to be considerable. Likewise, smuggling in illicit goods such as guns across PNG's only land border is common and has contributed to the proliferation of illegal firearms. In response to these risks, the 2013 White Paper proposed to significantly increase the size of the PNGDF, with a target of 10 000 personnel by 2030. Analysts have cautioned that a much larger force might be tempted to adopt a more political role,<sup>3</sup> while the actual prospects of such an expansion have receded with the deterioration of PNG's fiscal position.

The PNGDF also assists civil authorities, notably the police, in providing security for significant national events, such as PNG's elections and the forthcoming APEC summit. It has been legally possible for the PNGDF to deploy internationally since 2010, with its most significant off-shore deployment in recent years being the Regional Assistance Mission to Solomon Islands (RAMSI).



## LAW AND ORDER CHALLENGES

Law and order problems are identified in the National Security Policy as posing a “grave and immediate danger to national life”.<sup>4</sup> This broad term is commonly used to cover crime, violence and insecurity, as well as government responses to these problems. In this section, I briefly consider some of these problems, including some of their newer manifestations such as transnational crime.

### URBAN VIOLENCE

Concerns over a growing urban crime problem began back in the 1960s as the colonial restrictions over the movement of Papua New Guineans were removed and young rural migrants flocked to Port Moresby. Papua New Guinea’s towns have since acquired notoriety as violent and crime-ridden places, with Port Moresby and Lae labelled as two of the world’s most dangerous cities.<sup>5</sup> Insecurity is evident in the fortifications, razor-wire, and proliferation of private security. In Port Moresby, violent crime has been long been attributed to the activities of *raskol* gangs, comprising disaffected young men from the city’s burgeoning settlements. During the 1980s and 1990s cyclical patterns of localised crime waves followed by heavy-handed police operations played out violently in the national capital.

The full scale of crime and violence in Papua New Guinea is difficult to assess, given the limited coverage and poor quality of police and other data. Although survey findings and the weight of anecdotal evidence suggest that violence victimisation rates are high by global standards, other research indicates there was an overall reduction and stabilisation of crime during the first decade of the new millennium.<sup>6</sup> Levels of unreported crime, including rape and other sexual offences, are extremely high, particularly in rural areas where access to police is limited. Significant variations exist between urban and rural settings, as well as within regional, rural, and urban contexts.

### ILLEGAL FIREARMS

Illegal firearms, home-made and factory produced, are used regularly in criminal activities and tribal conflicts. Tribal conflict, still predominantly a Highlands phenomenon, has changed considerably over the years. The use of high-powered weapons, along with mercenaries or ‘hire men’ and guerrilla tactics, has dramatically altered the ground rules of tribal fighting and fuelled escalating cycles of conflict that are difficult to resolve through either policing interventions or traditional peacemaking.<sup>7</sup> Higher numbers of casualties associated with the new technologies of violence make it harder to achieve the equivalence between warring factions that was integral to traditional approaches. In addition to familiar triggers such as land disputes, PNG’s volatile elections and intense local contestation around resource development projects provide newer settings for this kind of conflict.

### GENDER-BASED VIOLENCE

Gender-based violence is endemic throughout Papua New Guinea. Recent years have seen important interventions in law reform, public awareness, and an array of practical programs involving community groups, NGOs, government agencies, businesses and international donors. However, violence against women and girls, including sexual abuse,

remains an enormous challenge. Socially embedded attitudes are slow and difficult to change, while the adverse effects of economic globalisation, including deepening inequalities, disproportionately affect women. Human Rights Watch claims that family violence has reached ‘emergency’ levels in Papua New Guinea, with more than two-thirds of women experiencing some form of it, and, in some areas, 80 per cent of men admitting to committing sexual violence against their partners.<sup>8</sup> An Australian Federal Police officer attached to the RPNGC described levels of domestic violence as “pandemic, equalling something in a war zone”.<sup>9</sup> Reporting rates for crimes of violence against women are extremely low, reflecting, in part, a lack of confidence in police follow-up. Sorcery-related violence, often directed at women, has become another major concern and precipitated a concerted campaign of law reform, awareness, and other interventions by government, churches, donors and NGOs.<sup>10</sup>

## **GRAFT AND CORRUPTION**

The National Security Policy identifies ‘graft and corruption’ as a major threat that if left unaddressed “will destroy PNG government and [its] institutions, ruin development programs, create instability and ultimately cause [it] to become a failed state”.<sup>11</sup> Few would disagree. Corruption has been described by a former PNG Prime Minister as “systematic and systemic”. The Parliamentary Public Accounts Committee found “evidence of misappropriation, fraud, negligence and disregard for the law and for the welfare of the state by public servants at every level”.<sup>12</sup> The same body estimated that around 25 per cent of the country’s GDP is siphoned off through corruption.<sup>13</sup> Windfall revenues associated with the recent mining boom, and the weakening of institutional oversight and regulation, have contributed to heightened levels of corruption. However, there are also signs of growing levels of public anger and demands for action, as demonstrated in the 2016 student-led protests.

## **TRANSNATIONAL CRIME**

Papua New Guinea’s connectivity into the global maritime network has improved and it has now become a regional shipping hub. This has increased its vulnerability to transnational crime, as accentuated by its relatively porous borders and weak institutions. This is another area where there is little reliable data. Economic globalisation has brought growing opportunities for money laundering involving politics and local and transnational networks. In 2012, the head of PNG’s anti-corruption agency Investigation Task Force Sweep drew international attention to the millions of PNG kina that had allegedly been laundered into Australia by PNG elites, much of it ending up in the north Queensland property market. For its role in harbouring illicit funds, Australia was dubbed the ‘Cayman Islands of the Pacific’.<sup>14</sup>

## **RESOURCE POACHING**

The National Security Policy identifies “illegal poaching of resources” as another major threat to PNG’s national security.<sup>15</sup> This has been a problem for many years, particularly in the logging and fisheries sectors. The cost of transfer pricing in PNG’s logging industry has recently been estimated at more than US\$100 million in lost tax revenue per annum,<sup>16</sup> and the UK-based Chatham House claims that 70 per cent of logging in Papua New Guinea is illegal.<sup>17</sup> This has been facilitated by collusion between corrupt officials and, mainly



Malaysian, logging companies, and in recent years through a legal mechanism called the Special Agriculture and Business Leases (SABLS). No decisive steps have been taken to stop the deceptive land deals that enable illegal logging. There have, however, been signs of improvement in the management of the country's fisheries.<sup>18</sup>

## SECURITY GOVERNANCE

### THE RPNGC

Policing was an integral part of the system of colonial administration that was aimed primarily at extending and consolidating government authority.<sup>19</sup> This system was personified in the highly mobile patrol officer or *kiap* who administered a form of rudimentary community policing to widely dispersed and largely self-regulating rural populations. This approach worked reasonably well because it involved pragmatic accommodations with local forms of authority.<sup>20</sup> *Kiaps*, who were few in number and underfunded, relied on the acquiescence of local leaders in order to accomplish their broad policing task. The RPNGC adopted their current organisational form in the 1960s as part of the larger process of institutional modernisation. For some observers, this institutional transition led to an effective withdrawal of government in many rural areas that contributed to the revival of violent forms of self-help including tribal fighting. At independence, police coverage extended to only 10 per cent of the country's land area and 40 per cent of the population.<sup>21</sup>

The travails of the RPNGC have provoked two broad critiques. One has been largely technical and focused on organisational aspects, such as training, management systems, budgeting, operational skills, leadership, and professionalism. This has been the orientation of successive donor-funded police capacity-building programs. Prompted by the modest outcomes of these engagements, the other critique has raised more fundamental questions around the 'fit' and 'relevance' of the current policing model in PNG's distinctive social and geographical terrain. The institutional legacy of the past is still evident in contemporary policing, and the criminal justice system more broadly: small numbers; centralisation of budget and personnel; uneven distribution of resources; violent mobile squad policing; the continuing role of informal justice practices; and the tiny proportion of cases ending up in formal court process.

The reach of the RPNGC has, if anything, diminished since independence. Although the overall population has more than trebled, the RPNGC has only grown by around 30 per cent.<sup>22</sup> Figures from 2013 indicate a force of 5387 sworn uniformed officers,<sup>23</sup> while unconfirmed estimates put its present size at around 7000. The police-to-population ratio is small by both regional and global standards, with a 2012 estimate suggesting that it was less than half the UN's recommended minimum. Government pledges to increase the size of the RPNGC to more than 13 000 by 2020 and to 24 000 by 2030 remain unrealistic in the current fiscal climate,<sup>24</sup> with new recruitment suspended in early 2017.<sup>25</sup>

Limited recruitment helps explain the rapidly ageing workforce. In 2014 it was estimated around 15 per cent of serving officers had passed mandatory retirement age, while another 29 per cent would reach that age by 2018.<sup>26</sup> Responses to insufficient numbers have included reliance on auxiliary and reserve police drawn from the wider community. These voluntary police work alongside regular officers. They may be sponsored by private businesses that

provide allowances, uniforms, and other kinds of support. Serious allegations of corruption and other abuses have been levelled at both reserve and auxiliary police.

Most rural-based citizens rely on extended families and informal community-based approaches for everyday dispute resolution and security. Even where accessible, the police are widely viewed as unresponsive. Lack of funds to buy fuel for police vehicles is a common reason (or excuse) provided and payment is often a precondition for rendering assistance. Flat-lined police budgets cover salaries but leave little to fund operational expenses, encouraging officers to seek out informal local revenue opportunities. This can include payment for 'turning a blind eye' to alleged infringements and illegal on-the-spot fines. It also renders the police susceptible to reliance on external patrons with the risks this poses to integrity.

The growing penetration of the RPNGC by patronage networks linked to senior political actors has affected senior appointments and the conduct of investigations, and contributed to growing factionalism within the organisation. Manifestations include the high turnover of police commissioners and the dismissal or marginalisation of officers investigating serious allegations against powerful figures. The blatant obstruction faced recently by PNG's Task Force Sweep and the police anti-fraud squad is an example of an alarming trend that has damaged the standing of the RPNGC and demoralised many of its members.<sup>27</sup>

Lack of public confidence also reflects fear of the police among many citizens. Police brutality and excessive use of force has been a consistent complaint over the years. Various reports have documented serious abuses of human rights, depicting an entrenched culture of criminal behaviour, brutality, and impunity within police ranks.<sup>28</sup> The last major government review of the RPNGC noted that outstanding legal claims against the state arising from police actions amounted to more than double the total police budget in 2004.<sup>29</sup> The review found substandard police leadership, inadequate resourcing, poor budgeting, a culture of indiscipline and unaccountability, political interference in police operations, and an almost complete breakdown in public trust.

## **FILLING THE GAP? THE RISE OF PRIVATE SECURITY**

Private security has emerged as a way of filling the security gap. The corporate and business sector has been a major driver of security services, both as a consumer and supplier. The number of firms identifying crime as a major constraint to their businesses in Papua New Guinea is more than four times the regional average in East Asia and the Pacific, and comparable with countries such as El Salvador, Venezuela, and the Democratic Republic of Congo.<sup>30</sup> Business investment in security personnel and infrastructure is significantly higher in Papua New Guinea than the average for the East Asia and Pacific, Sub-Saharan Africa and Latin American regions.

## **RAPID GROWTH OF THE SECTOR**

The number of companies licensed by PNG's Security Industries Authority (SIA) grew from 173 in 2006 to 462 in 2014 with a total workforce of around 30 000 security guards.<sup>31</sup> In December 2016, there were 464 licensed companies, while the number of guards had dropped to around 27 709 with the winding down of the LNG construction phase.

The number of guards employed by licensed companies is over three times the number of serving police officers and more than the combined strength of PNG's three 'disciplined' services (RPNGC, PNGDF and the correctional service). These figures do not include the large number of unlicensed security companies and personnel, estimated by the SIA to be around 219 unlicensed companies with 7649 guards.

Companies vary from transnational security corporations with global reach, large locally owned firms, through to numerous small operators. The three largest companies in 2016 were Guard Dog Security (around 3622 guards), G4S Secure Solutions Ltd (around 3390) and Black Swan International (around 780). Security at the controversial Australian-funded refugee processing centre on Manus is provided by Wilsons Security, which had around 622 employees on the island in 2013. Companies are concentrated in PNG's urban centres, but also operate in rural areas where major resource projects are located. Services provided include static asset protection, escorting mobile assets, close personal protection, security training, security assessments, emergency evacuations, rapid response capabilities, and the supply and monitoring of electronic surveillance systems. The value of the industry has been estimated as between PNGK800 and PNGK1 billion.<sup>32</sup> Large extractive companies also often have substantial in-house security capabilities, for example in 2015 around 500 security personnel were employed at the Porgera mine.

## REGULATION OF THE SECTOR

Papua New Guinea is one of two Pacific Island countries that have dedicated legislation to regulate the private security industry (the other being Tonga). The *Security (Protection) Industry Act 2004* established the SIA, with responsibility for issuing and revoking operating licences. Its effectiveness in practice has been hampered by limited capacity and the pace of industry growth.

The relationship between the private security sector and the RPNGC is generally close, particularly with larger companies. This has been viewed as a potential opportunity for assisting the under-resourced police, but also as a potential threat to their integrity. Strong informal networks exist between private security companies and the RPNGC, with many senior industry employees having previous police (or military) experience in Papua New Guinea or overseas. Bigger operators regularly assist the RPNGC by, for example, providing fuel and tyres for vehicles, while informal networks facilitate intelligence sharing. Collaboration between the police and business community has a long history in Papua New Guinea. This includes policing services provided to logging and mining projects operating in remote rural locations. These are often covered by formal agreements between the parties and might include the payment of allowances, transport costs, and provision of meals and accommodation. Beyond these authorised arrangements, allegations are regularly made of serving officers illegally moonlighting as private security, often while wearing uniforms and using police equipment.

There are concerns about the potentially negative effects of the expanding private security sector on the RPNGC. These include sensitivities about private providers encroaching on areas that should remain the preserve of the police, concerns that the growing prominence of private providers diverts attention away from the need to strengthen the police, as well as perceptions that public-private security collaborations might entail privileging powerful

business interests over responsibilities to ordinary citizens. For example, the National Security Policy stated foreign-owned security companies engaging “in areas designed for PNG state agencies” is a concern and risks undermining “the state’s ability and authority to deliver public safety and security”.<sup>33</sup>

## RISKS AND OPPORTUNITIES

The growth in private security is connected to broader changes in PNG’s political economy. Increasing demand for private security presents an attractive opportunity for both foreign and local investors, as well as creating significant numbers of low-paid jobs for Papua New Guineans. The proliferation of security companies is not just a result of foreign companies entering the market but also the growth of domestic investment and entrepreneurship, ranging from landowner groups to wealthy members of PNG’s political and business elite who have established or bought into some of the larger companies.

Growing elite investment in private security raises the critical issue of the disincentive this may present to invest in public security agencies. While investing in effective law enforcement capabilities might be viewed cynically as not in the interests of the more predatory elements of the political elite, the growing investment in private security might be another factor behind the long-term disinvestment in public security. Another issue that would merit further research is the extent to which individual MPs are using their constituency development funds on private security provision. Broader concerns about the potential for conflict of interests and corruption among the political actors controlling such funds apply equally in the case of security expenditure.

For a major donor such as Australia that has invested millions of dollars into capacity-building engagements with the RPNGC over the years, the massive expansion of private security and its impact on public policing has attracted surprisingly little interest. While there are many potential risks, the growth of private security also presents opportunities for addressing some of PNG’s problems of insecurity. This would mean moving beyond viewing private security primarily as a gap-filling response to the inadequacies of public policing by those who can afford such services. Instead consideration could be given to how more deliberate and regulated engagement between the two sectors might contribute to developing the capabilities of the RPNGC and improving the quality and reach of security provision for all Papua New Guineans, particularly its most vulnerable groups.

## CONCLUSION

The major changes being experienced in Papua New Guinea associated with rapid economic globalisation are likely to continue to generate stresses and divisions and these will contribute to many of the kinds of insecurity touched upon in this paper. It is unlikely that these will be overcome anytime soon. As the National Security Policy recognised, holistic responses to PNG’s security threats need to go beyond conventional law and order responses. Many of PNG’s law and order problems are symptomatic of more complex processes of change and contestation that are essentially developmental and political in character. There are no easy or quick fixes. Ultimately, a system of government and political leadership capable and committed to delivering more equitable development outcomes and improved social and economic opportunities for all Papua New Guineans will see a

diminution in many sources of contemporary stress. There are few signs of that happening in the near future.

In terms of the security governance issues that have been a major focus of this paper, it has long been clear that PNG's security agencies have extremely limited capabilities, particularly the police as the frontline agency in internal security. Many years of government neglect has left the RPNGC ill equipped to police PNG's complex and rapidly changing social landscape. Patronage networks and increasing factionalism have damaged the standing and integrity of an already weak organisation. The growth of private security provides an alternative to those who can afford such services, but does little to directly address the security needs of those who cannot. Moreover, there is a real risk that increasing investment in private security on the part of PNG's political elite provides a disincentive to invest in public security, thereby perpetuating the continued decline of public policing.

Such a scenario would lead to an increasingly fragmented security landscape and one where the police become increasingly beholden to political and other powerful patrons. This would leave PNG's poorest and weakest groups most vulnerable to insecurity. While the growth of private security presents a number of risks, it is also important to see it as providing opportunities to develop more holistic approaches to security governance. More considered and regulated engagement between private and public providers could contribute to both improving the capabilities and performance of the RPNGC and the quality and reach of security provision for all Papua New Guineans.

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# ECONOMIC ANALYSIS OF PAPUA NEW GUINEA

DAVID OSBORNE, ROBERT HARDEN AND CHRISTOPHER HOY

## INTRODUCTION

This paper analyses the PNG economy by considering (1) macroeconomic stability; and (2) fiscal policy and debt.

From 2003 to 2015, Papua New Guinea experienced comparatively robust economic growth which underpinned increased formal sector employment and strong growth in government revenue. This performance was aided by high prices for PNG's commodity exports, supportive macroeconomic policy settings, and developments in the resources sector, the most notable being the construction of the PNG LNG Project and the first gas exports in 2014.<sup>1</sup>

This prolonged period of robust economic growth has not, however, translated into improved social indicators or improved standards of living, particularly for PNG's rural majority (around 80 to 85 per cent of the population). Papua New Guinea failed to achieve any of the Millennium Development Goals and it is currently ranked a lowly 154 out of 188 countries on the UN Human Development Index, compared with Fiji's ranking of 91, Vanuatu's of 134 and Solomon Islands' of 156.

The robust economic performance fuelled rapid growth in government expenditure, which increased from K3 681 million in 2003 to K13 789 million in 2015 (nominal terms). However, the effectiveness of the greatly expanded government expenditure program is questionable, with concerns that too much has been spent on 'prestige' projects rather than on projects which will expand the productive capacity of the economy. Even the PNG Treasury has raised concerns over the effectiveness of funds transferred to the Provinces and Districts.<sup>2</sup>

Following years of relatively strong economic growth, Papua New Guinea is now confronting a period of significantly weaker growth. This reflects a number of factors: weaker international commodity prices, declining oil production due to maturing oil fields, and the one-off boost in GDP growth due to gas exports which has passed. Over the medium term, the PNG Treasury is projecting modest economic growth of around 2.7 per cent, which is significantly below the estimated population growth rate of 3.1 per cent.<sup>3</sup>

## SECTION 1: MACROECONOMIC STABILITY

### KEY FINDINGS

- On three occasions since Independence, the PNG Government has sought external assistance from the International Monetary Fund (IMF) and the World Bank to deal with unsustainable pressures fuelled by budget deficits on the external accounts.
- Since 2013 Papua New Guinea has experienced a sudden reversal of its current account deficit precipitated by a significant reduction in FDI and a rapidly increasing trade surplus (from new LNG exports and significantly reduced merchandise imports).
- From 2012, fiscal policy settings began to deteriorate and the budget deficit increased markedly. While the end of the commodity price boom was a contributing factor, the government also adopted expansionary fiscal policies in order to maintain economic activity as the construction phase of the PNG LNG project approached completion.
- Over the course of 2016, the Central Bank was hopeful that the imbalance in PNG's foreign exchange market would be cleared. Commodity prices had improved somewhat, and mineral and petroleum exports increased as did exports from the agriculture sector.
- The strength of the PNG exchange rate over the last ten years could be considered a missed opportunity that reserves had not increased further.

### ENSURING EXTERNAL BALANCE IN PAPUA NEW GUINEA: BACKGROUND INFORMATION

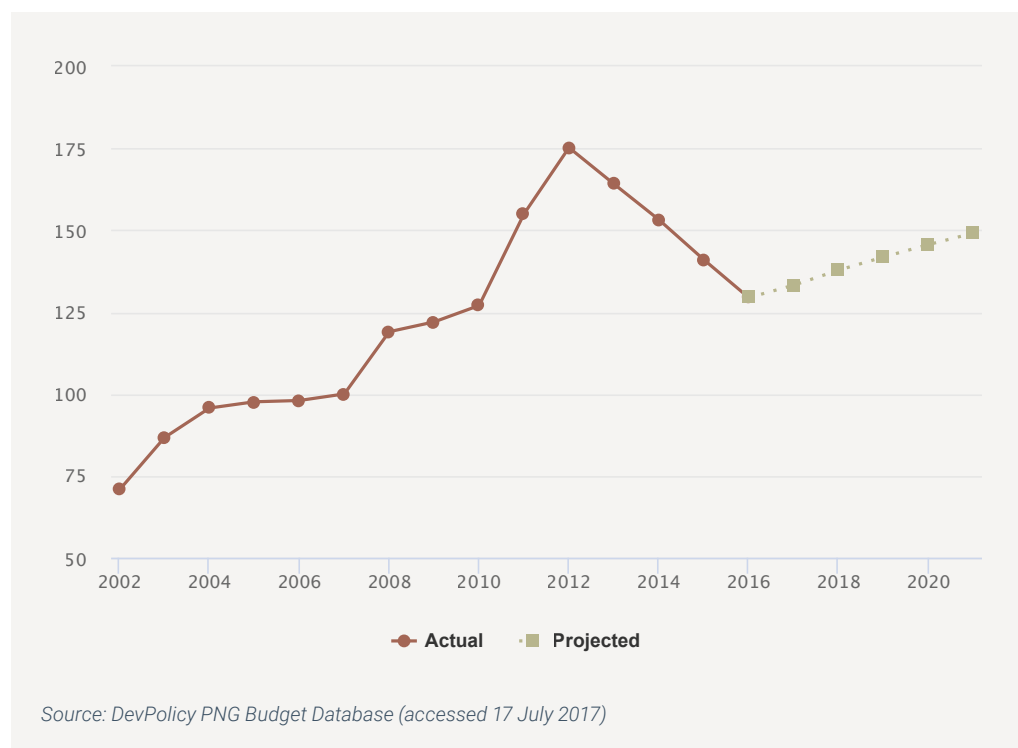
In broad terms, external balance is characterised by a comfortable level of external reserves,<sup>4</sup> a floating, albeit relatively stable exchange rate, and a readily convertible kina.<sup>5</sup> A major premise of macroeconomic management in Papua New Guinea since independence is that external balance is best achieved through the conduct of responsible macroeconomic policies, and especially fiscal policy.

The relationship between fiscal policy and external balance in Papua New Guinea is relatively straightforward. A fiscal deficit is normally financed by the government borrowing from the domestic banking sector, including the Central Bank (as has been the case recently). Because the banking system in Papua New Guinea is characterised by high levels of excess liquidity, the borrowings and subsequent expenditure of the funds through the annual budget adds directly to aggregate demand in the economy. With PNG's heavy dependence on imported goods, the increase in aggregate demand (or aggregate expenditure) will be reflected in an increase in demand for foreign currency. The subsequent imbalance between demand for foreign currency and the supply of foreign currency will manifest in a widening balance of payments deficit. The Central Bank can manage these pressures for

a period of time by selling its holdings of foreign currency (i.e. external reserves) and by allowing the exchange rate to depreciate. However, PNG foreign currency reserves are low when compared with like countries, particularly given the relative strength of the exchange rate over the past 14 years, reducing its ability to use this lever.

From 2002, the kina appreciated against a weighted average of foreign currencies (note that over this same time period other resource-dependent developing countries saw a 50 per cent depreciation of their currencies, relative to the US dollar). Between 2012 and 2016 the kina depreciated 26 per cent against the index (Figure 1).

**Figure 1: Real exchange rate index (2007 =100)**



On three occasions since independence, the PNG Government has sought external assistance from the International Monetary Fund (IMF) and the World Bank<sup>6</sup> to address unsustainable pressures on the external accounts fuelled by budget deficits. This occurred in 1990, 1995 and 2000 (the more recent pressure on PNG's external position is discussed below). Under an IMF Standby Facility, the Fund stands ready to directly lend foreign currency to PNG's Central Bank in order to bolster its holdings of external reserves, thereby enabling the Bank to manage the imbalance in foreign exchange demand and supply in a more orderly fashion.<sup>7</sup>

## RECENT DEVELOPMENTS IN PNG'S MACROECONOMIC ENVIRONMENT: THE CURRENT ACCOUNT AND FOREIGN CURRENCY SHORTAGES

From 2003 to 2011, Papua New Guinea experienced comparatively healthy macroeconomic conditions. International prices for PNG's commodity exports were very high, and from around 2008 to 2011 the domestic economy received a major boost through the construction of the PNG LNG Project. For much of this period, strong revenue growth enabled the government to target modest fiscal deficits despite significant growth in government expenditure.<sup>8</sup> However, from 2012, fiscal policy settings began to deteriorate and the budget deficit increased markedly. The end of the commodity price boom was a contributing factor but the government also adopted expansionary fiscal policies in order to maintain economic activity as the construction phase of the PNG LNG project approached completion. Combined with a marked slowdown in foreign exchange inflows,<sup>9</sup> the increased budget deficits and lower commodity prices placed pressure on PNG's external accounts. External reserves fell due to the Central Bank selling foreign exchange to address unmet demand, and the kina began depreciating (see Figure 1). Concerned in particular by the depreciation of the kina, in late 2013 the Central Bank moved to restrict the capacity of resident importers to enter into forward foreign exchange contracts.

Given the widening imbalance in the foreign exchange market, the Central Bank was concerned that the commercial banks were selling foreign currency to internal clients at heavily depreciated kina rates compared to the official rate. In June 2014, the Central Bank moved to curb this practice by imposing a trading band around the official exchange rate, directing banks to trade within this range. In March 2015, the Central Bank issued further directives in an effort to improve the inflow of foreign currency into the PNG banking system. Key directives included a three-month limit for PNG exporters to hold foreign currency offshore,<sup>10</sup> an embargo on the opening of new offshore accounts for PNG residents, and a requirement that all foreign currency transactions be undertaken in-country by resident PNG banks.

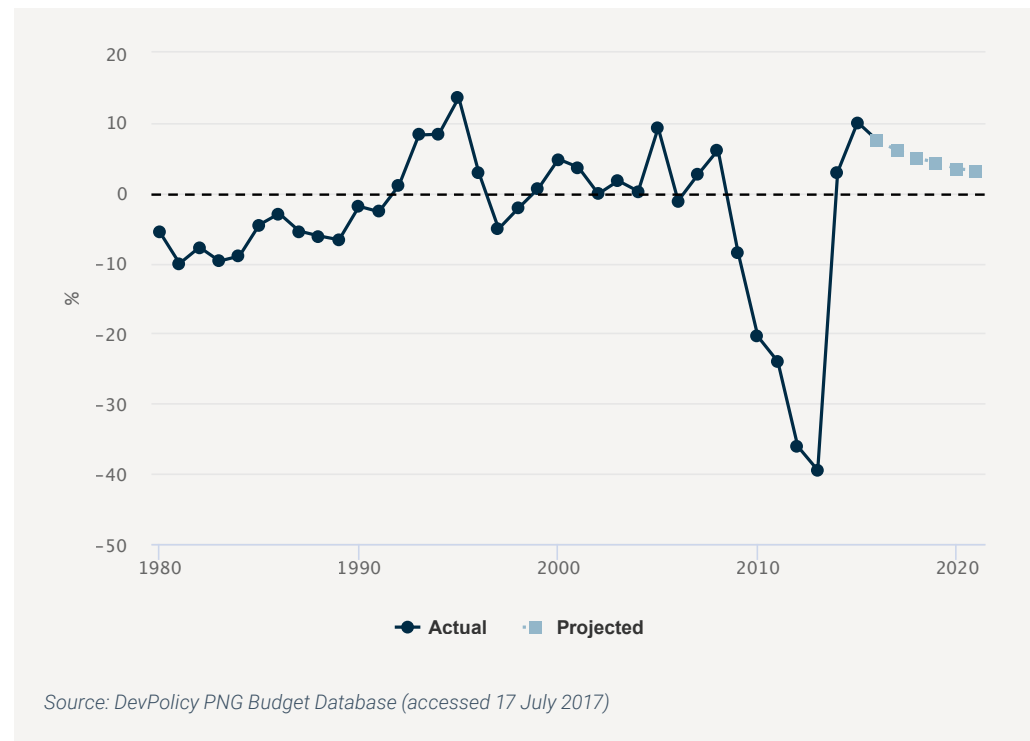
Notwithstanding these measures, and the continued sale of foreign currency (external reserves) by the Central Bank, the imbalance in PNG's foreign exchange market persisted, with demand for foreign currency significantly outstripping supply.<sup>11</sup> Even so, the Central Bank was hopeful during 2016 that the imbalance would be cleared. Commodity prices had improved somewhat, and mineral and petroleum exports increased as did exports from the agriculture sector. The government also secured an external loan of US\$200 million, drawn down in the third quarter of 2016. However, the backlog of demand for foreign currency was not cleared, for which the Central Bank blamed the re-emergence of forward foreign exchange contracts for importers and other practices by resident commercial banks.

Papua New Guinea's current account balance over this period tells an interesting story (Figure 2). During the global financial crisis, starting in 2007, many countries experienced a rapid and damaging reversal of their current account deficits due to the withdrawal of private financing. Papua New Guinea saw the opposite, and then from 2013 experienced a sudden reversal of its current account deficit precipitated by a significant reduction in FDI and a rapidly increasing trade surplus from new LNG exports and significantly reduced merchandise imports.<sup>12</sup> A sharp reduction in current account deficit can indicate a



recession, as imports decline and stronger markets demand exports. A devalued currency (as was the case in Papua New Guinea) can also lead to a reduction of imports, shrinking the deficit more than expected under the prevailing economic conditions.

**Figure 2: Current account balance (% of GDP)**



Papua New Guinea, like many developing countries with ample investment opportunities and low rates of domestic savings, needs to run a current account deficit to support economic growth. However, the borrowed foreign funds need to achieve a higher rate of return than the interest rate payable on the liabilities. Papua New Guinea ran current account surpluses between 1992 and 2008, and again from 2014 after a large adjustment in the current account balance through the commodity price boom, the construction phase of the ExxonMobil LNG project, and the start of LNG exports. Papua New Guinea was therefore able to weather the recent reductions in commodity prices and the related economic slowdown, as it had sufficient capacity to increase its exposure to foreign liabilities. The problem now will be the degree to which FDI and imports turn around to stimulate economic growth.

## CONSEQUENCES AND OUTLOOK

The imbalance in PNG's foreign currency market, evident since 2013, will be very damaging to the PNG economy and investor sentiment. Resident companies that rely heavily on imports to service the domestic economy will have been particularly hard hit by the ongoing imbalance. In comparison, resident export companies should be relatively immune from the foreign exchange imbalance, as they can service their foreign liabilities from their internal generation of foreign currency.

The shortage of foreign currency is reflected in the substantial reduction in value of PNG's imports. Merchandise imports for the September quarter 2016 were valued at K876 million, a fall of 70 per cent since the September quarter 2013.

The shortage of foreign currency has been a serious concern for many Australian companies with operations in Papua New Guinea. Foreign exchange access was a key issue raised by the Australia Papua New Guinea Business Council during a dialogue with members of the Australia PNG Ministerial Forum in March 2017. The difficulty of accessing foreign currency to meet foreign liabilities and obligations (payment for imports including services and profit repatriation) is a key consideration in assessing the sovereign risk of doing business in a foreign country. The foreign currency shortages could increase international perceptions of sovereign risk in Papua New Guinea.<sup>13</sup>

The IMF has disputed the Central Bank's view that the current exchange rate regime remains consistent with a "floating" regime. The IMF has consequently reclassified the regime as a "crawl-like" arrangement, and the IMF Executive Board urges greater exchange rate flexibility and a more efficient and transparent foreign exchange allocation mechanism.<sup>14</sup>

Recent developments clearly demonstrate that the Central Bank cannot address the foreign currency imbalance through action or regulation. Indeed, it may have accentuated the imbalance, as resident exporters appear to have developed more imaginative ways of holding foreign currency offshore (defying the Central Bank's three-month rule), in anticipation of a further sharp fall in the value of the kina. However, slightly higher commodity prices and improved exports from the mining and agricultural sectors may provide some relief, as would greater exchange rate flexibility through further depreciation of the kina, as recommended by the IMF. The government could also request direct financial support from the IMF and the World Bank, but this option may be politically unpalatable.

All things being equal, for macroeconomic stability to continue in Papua New Guinea the fiscal deficit will need to be brought back into a sustainable position to reduce pressure on foreign reserves and to re-establish equilibrium in the balance of payments. A more flexible exchange rate would also assist; however, this would require a change in government policy. Increased FDI would also assist in achieving macroeconomic stability.

## SECTION 2: FISCAL POLICY AND DEBT

### KEY POINTS

- Papua New Guinea has not effectively managed volatility in revenue and expenditure.
- As a result, government expenditure is unpredictable from one year to the next, reducing its ability to undertake medium to longer term planning for service delivery, reforms and infrastructure development.
- The projected fall in expenditure as a share of GDP is below 20 per cent, the lowest level in over 30 years and well below the long-term average of approximately 32 per cent.



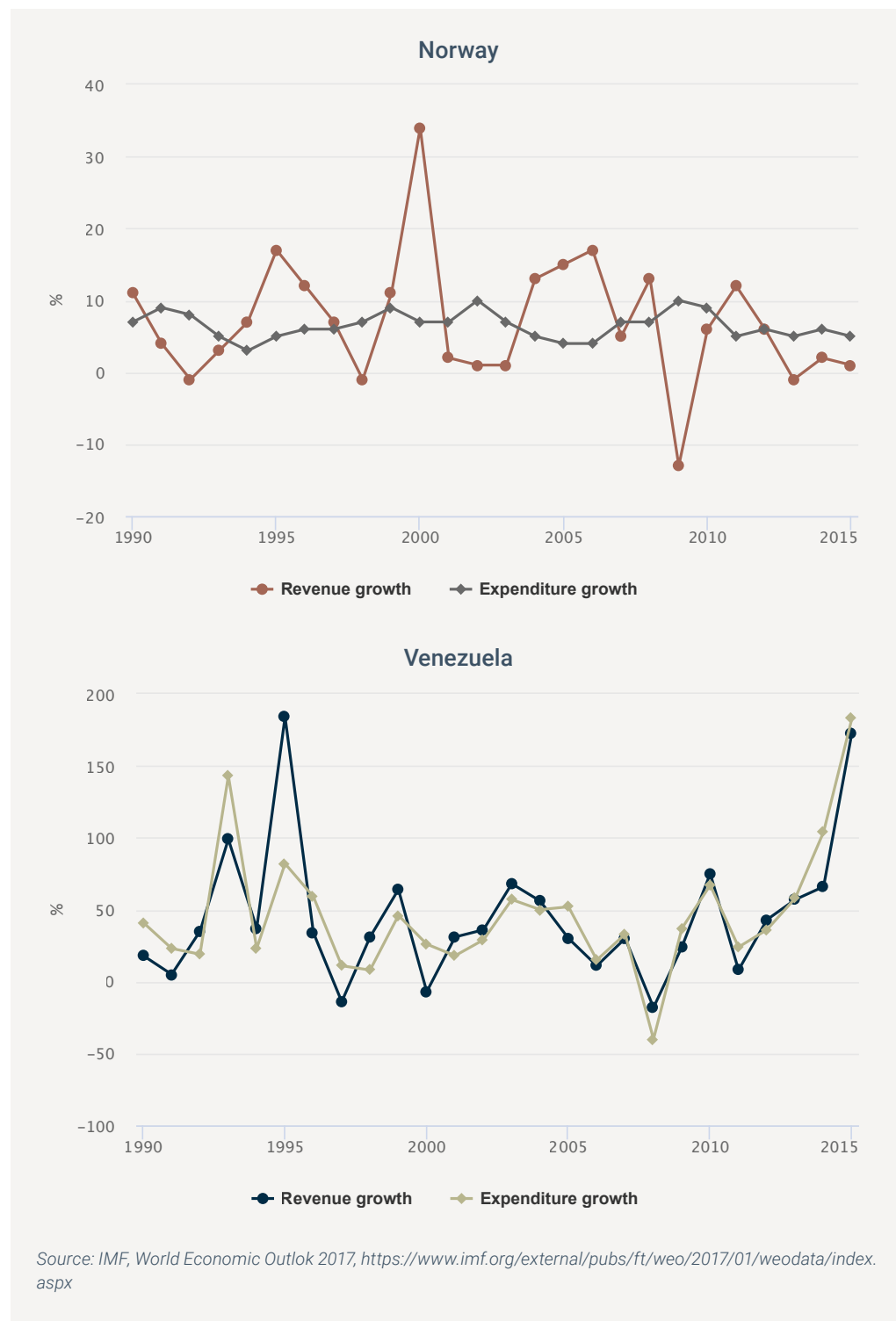
- From 2003 to 2013, PNG's expenditure as a share of GDP increased by 45 per cent, while revenue grew only 1 per cent, making it one of the worst performers among other resource-based developing countries.
- Papua New Guinea's Sovereign Wealth Fund (SWF) will need to be closely integrated with the policies and legislation governing Kumul Consolidated Holdings (the holding company of PNG's state owned enterprises), and its related entities, as they control dividends for the state. The SWF should align with the objectives of PNG's current and future Medium Term Fiscal Strategy, Medium Term Debt Strategy and annual National Budget, and vice versa.
- The IMF's 2016 Debt Sustainability Analysis of PNG concluded that "PNG's risk of external debt distress remains low but the overall risk of public debt distress is heightened".<sup>15</sup> A rising number of short-term Treasury bills combined with less concessionary external debt since 2014 (increasing exposure to US interest rates) have contributed to this heightened risk.

## FISCAL POLICY: FOCUSING ON STABILITY

Resource economies such as Papua New Guinea need to manage revenue and expenditure volatility to maintain debt sustainability. There are a number of possible approaches, such as strong macroeconomic frameworks with fiscal rules and special purpose funds (natural resource funds or sovereign wealth funds) to smooth and/or constrain government expenditure and maintain sustainable levels of debt. Papua New Guinea has a history of applying such mechanisms: the Mineral Resources Stabilisation Fund, the PNG Sustainable Development Program with its development and long-term funds, and now the PNG SWF. It has also used trust accounts to smooth expenditure, and medium-term fiscal strategies with fiscal rules to constrain expenditure growth and minimise debt.

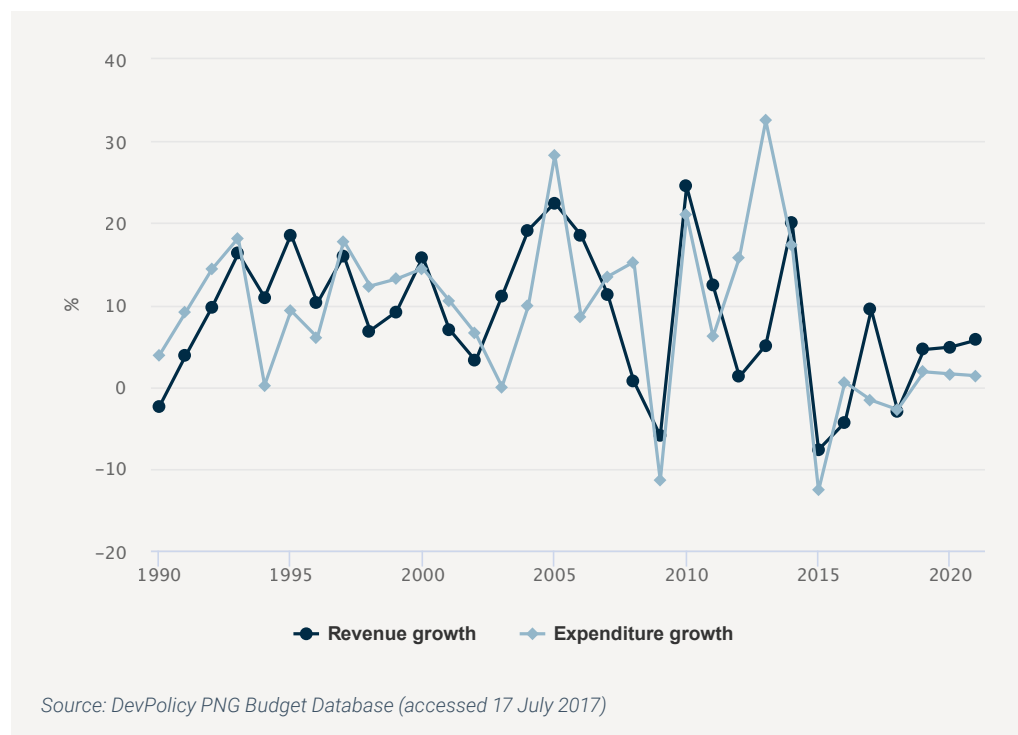
The effect of fiscal rules and tools on revenue and expenditure volatility can be seen in revenue and expenditure growth rates. Figure 3 compares fiscal management in Norway and Venezuela. Norway has a fiscal rule and Natural Resource Fund that stabilises the revenue available for budget expenditure. The fiscal tools stabilise (or smooth) expenditure despite volatility in revenue growth rates. By contrast, Venezuela has no effective fiscal rule to manage volatility, and expenditure mirrors revenue volatility. This makes budgeting very difficult.

**Figure 3: Using fiscal tools to reduce volatility: Norway vs Venezuela**  
(government revenue and expenditure growth rates)



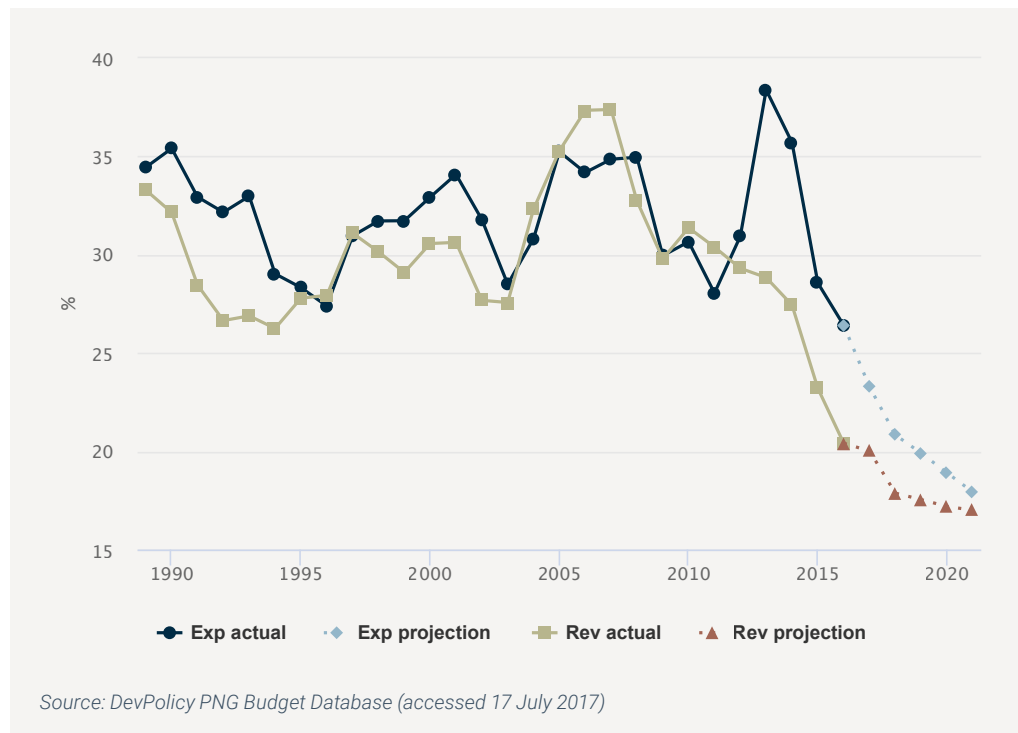
Papua New Guinea appears to manage volatility in revenue and expenditure like Venezuela, rather than Norway (Figure 4). It has made attempts to improve the management of volatility but they have been neither long-lasting nor very effective. In consequence, government expenditure is unpredictable from one year to the next, reducing the ability for government to undertake medium to longer term planning for service delivery and infrastructure development.

**Figure 4: Revenue and expenditure growth rates**



From 2003 to 2013, PNG's share of revenue to GDP remained steady at approximately 28 per cent, while the share of expenditure to GDP increased from 28 per cent to 38 per cent, indicating a worsening fiscal position, with the majority of the change occurring in 2012 and 2013. Since 2013 both revenue and expenditure have been falling in both kina terms and as a share of GDP (Figure 5).

The recent and projected fall in revenue and expenditure to GDP reduces the government's ability to provide basic services and to invest in reforms and infrastructure to stimulate future growth. The projected fall in expenditure as a share of GDP to below 20 per cent is the lowest level in over 30 years (Figure 5), and well below the long-term average of approximately 32 per cent.

**Figure 5: Revenue and expenditure (share of GDP)**

## FISCAL TOOLS

Papua New Guinea needs appropriate fiscal tools to manage revenue and expenditure volatility. It is a resource-dependent developing country that faces a *resource curse*. Fiscal tools must not only be capable of implementation but also take into account political realities.

They must also be coordinated. An effective SWF must be integrated within a country's broader fiscal policy and coordinated with all related fiscal policy tools.<sup>16</sup> For example, a savings fund would only be effective if there was a genuine increase in government saving, not offset by increased borrowing). PNG's SWF will need to be closely integrated with the policies established under Kumul Consolidated Holdings and related entities, controlling resource equity and related dividends for the state. Logically, the SWF should align with the objectives of PNG's current and future Medium Term Fiscal Strategy, Medium Term Debt Strategy and annual National Budget, and vice versa.

In the past, growth in PNG's revenue and corresponding rise in expenditure was largely absorbed through the use of trust accounts, as the economy was unable to expand in line with growing expenditure. The government allocated funds through the annual budget cycle and supplementary budgets, and held the funds in trust accounts. The trust accounts had a 'smoothing' effect, holding funds until the economy had sufficient capacity to implement the designated project or program. However, there have been questions over missing funds from many trust accounts, and allegations that funds were not used effectively or for their intended purposes.

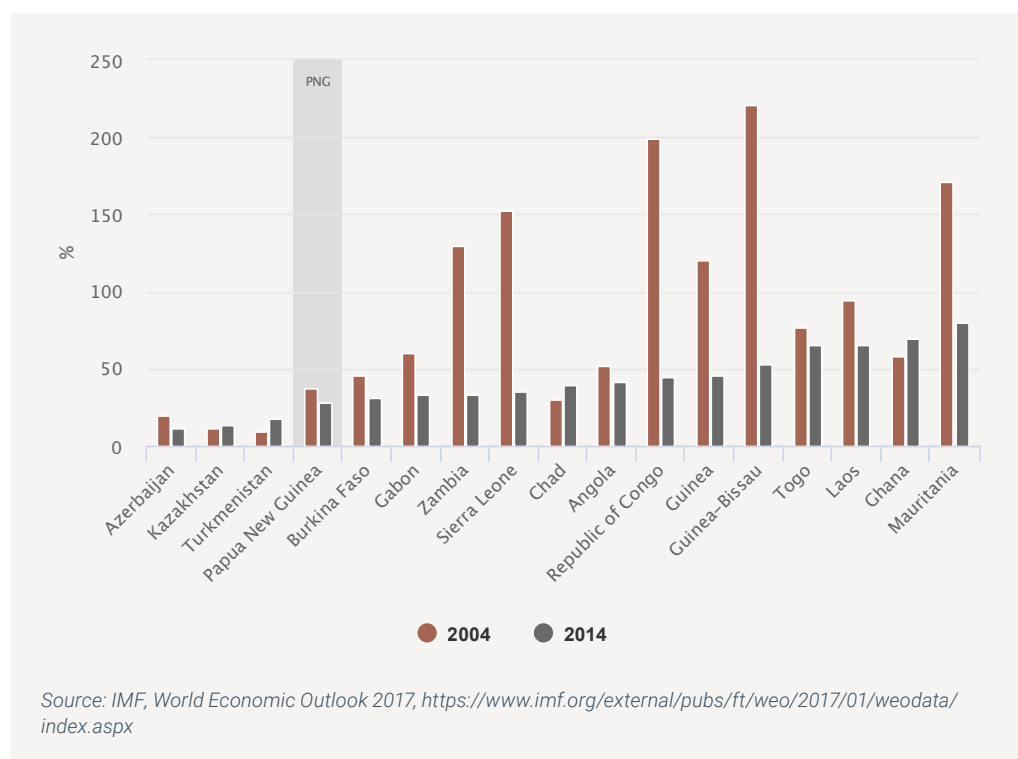
Papua New Guinea's fiscal framework now needs to be positioned to respond to economic events. Trust accounts should not be the default mechanism, and their use should be minimised. Keeping funds 'on-budget' and clearly within formal public financial management systems would enhance international and public confidence. Global commodity prices may have stabilised for now, but history indicates that increased prices or expanded output will return.

The new government will be required to formulate and approve a new Medium Term Fiscal Strategy for 2018–2022. The government therefore has the opportunity to consider options for an accelerated fiscal consolidation program, and better integrate fiscal policy with exchange rate policy and foreign exchange management.

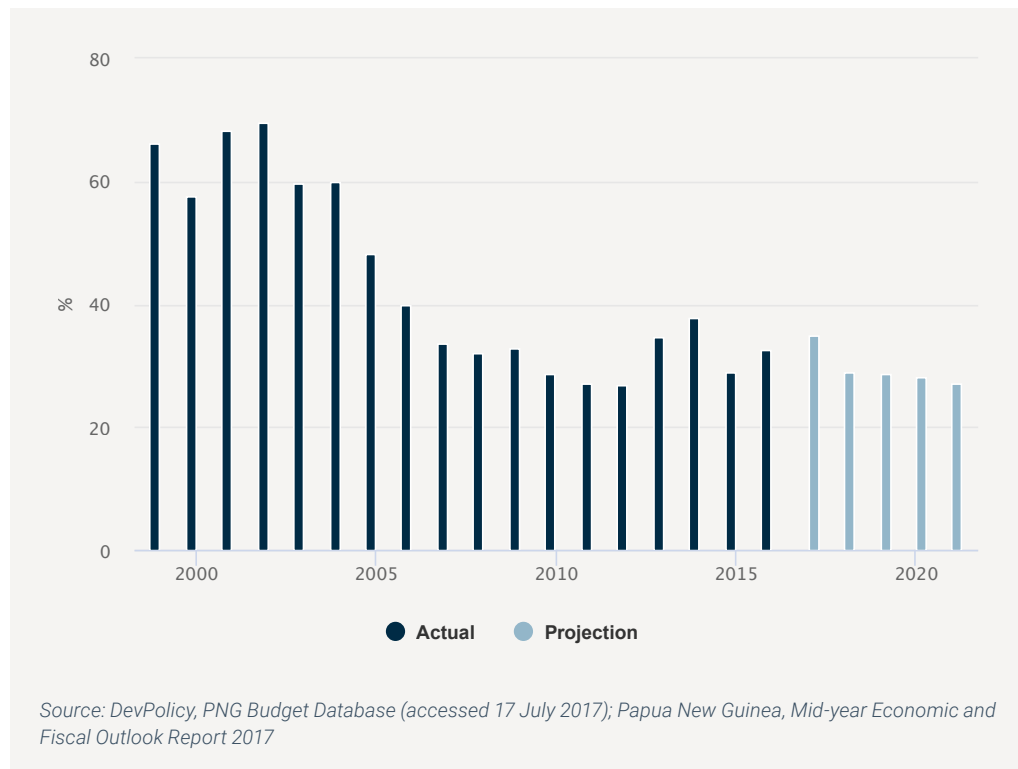
## DEBT PROFILE

Papua New Guinea's current stock of debt is approximately 33 per cent of GDP (see Figure 6), which is above the guideline of 30 per cent in the *Papua New Guinea Fiscal Responsibility Act 2006*. This debt is within historical levels and remains low compared to 'peer' countries.

**Figure 6: Resource exporters, debt to GDP**



In its 2016 Debt Sustainability Analysis of Papua New Guinea, the IMF concluded that "PNG's risk of external debt distress remains low but the overall risk of public debt distress is heightened".<sup>17</sup> A rising share of short-term Treasury bills, combined with less concessionary external debt since 2014 (increasing exposure to US interest rates) have contributed to this heightened risk.

**Figure 7: Total public debt as a share of GDP**

If PNG's projections are realistic and recent downward revisions to both revenue and expenditure are realised, then debt as a share of GDP will remain at historically low levels. However, sudden and large reductions in government expenditure will have a significant impact on service delivery, activity in the broader economy, and livelihoods.

Papua New Guinea is confronted with a prolonged period of low revenue growth as it faces some of its greatest development challenges. The process of expenditure prioritisation and the return it achieves from social and economic investments will determine the sustainability of its current fiscal deficits and related debt. If money is wasted on low priority and low return initiatives then it will be hard to see how human development indicators can improve over the next decade. There is a strong case for PNG to establish a fiscal management regime that manages its budget volatility so that expenditure is more stable and predictable, allowing both the public and private sectors to undertake longer term investment and planning.

## ENDNOTES

- 1 The ramp up in the construction phase of the project contributed to overall real economic growth of over 10 per cent in 2010, while the first full year of gas exports contributed to overall economic growth of over 12 per cent in 2014.
- 2 The Treasury noted in the 2013 National Budget that: "The quality of expenditure must also be increased. This means some lower priority or wasteful expenditure will need to be cut, while high priority expenditure, such as on health, education, law and order, and infrastructure, [will need to be] increased and made more effective": PNG, *2013 National Budget: Volume 1 – Economic and Development Policies*, 41.
- 3 The 2011 Census estimated PNG's population at 7,275 million. With a growth rate of 3.1 per cent, PNG's population will double in 23 years.
- 4 Foreign currency holdings by the Bank of Papua New Guinea (the Central Bank).
- 5 Meaning PNG residents and resident companies can readily purchase foreign currency with kina.
- 6 Bilateral partners, including Australia, also provided financial assistance under these programs.
- 7 A fundamental policy condition of IMF Standby programs is a requirement to address the original and primary source of the external account pressures; that is, by returning the fiscal account to balance. World Bank Structural Adjustment programs directly fund reforms aimed at improving the efficiency of government and the business operating environment.
- 8 From 2008 to 2011 PNG's external position was greatly assisted by foreign exchange inflows associated with the construction of the PNG Gas pipeline, as reflected by an appreciating exchange rate and increasing external reserves.
- 9 Also associated with the winding down of the construction phase of the PNG LNG project.
- 10 Meaning that resident exporters can hold foreign currency proceeds offshore for a period of three months and can use those proceeds to meet their foreign liabilities. However, after three months, any surplus of foreign currency proceeds must be repatriated to PNG.
- 11 While 2014 heralded the first full year of gas exports, the resulting inflow of foreign currency into Papua New Guinea was not substantial. The foreign currency earnings from the project are, in the first instance, predominately used to service the project's offshore loan commitments.
- 12 World Trade Organization, Trade Statistics database, accessed 14 June 2017.
- 13 In April 2016, the credit rating agency Moody's downgraded the PNG government's foreign currency and local currency issuer ratings. This decision was made in large part by "Strains on foreign currency reserve adequacy due to heightened balance of payments pressures that will continue over the next two years": Moody's Investor Service, "Moody's downgrades Papua New Guinea's Rating to B2 with Stable Outlook", Global Credit Research, 25 Apr 2016.
- 14 International Monetary Fund, 2016 Article IV Consultation, Papua New Guinea, IMF Country Reports 17/22.
- 15 International Monetary Fund, 2016 Article IV Consultation, Papua New Guinea, IMF Country Reports 17/22.
- 16 Phil Garton and David Gruen (2012), "The Role of Sovereign Wealth Funds in Managing Resource Booms: A Comparison of Australia and Norway", Address to the Third Annual Asia Central Bank and Sovereign Wealth Fund Conference, 23 February.
- 17 International Monetary Fund, 2016 Article IV Consultation, Papua New Guinea, IMF Country Reports 17/22.







# INFRASTRUCTURE CHALLENGES FOR PAPUA NEW GUINEA'S FUTURE

CRAIG LAWRENCE

## INTRODUCTION

Climate, topography, population, culture, economics, and finance all conspire to raise significant barriers to providing economic and social infrastructure critical to Papua New Guinea's future development. Compared to developed economies, the physical stock of infrastructure assets in Papua New Guinea is insufficient to deliver the economic and social services needed to drive faster economic growth and improve human development. It faces significant choices as a result that may also be influenced by the public infrastructure requirements of foreign direct investment in export oriented extractive resource sectors. A lack of effective national infrastructure planning and funding constrain PNG's economy and its ability to improve the lives of its citizens through provision of these infrastructure services.

This paper briefly reviews several key infrastructure sectors — telecommunications, transport, energy, and urban water — to provide snapshots of their status, identify challenges, and where possible make relevant international comparisons.<sup>1</sup>

It also looks at ways to improve the delivery of relevant economic infrastructure: (i) effective planning and prioritisation; (ii) funding strategies for infrastructure investment; (iii) funding of ongoing infrastructure operations; and (iv) consideration of infrastructure life cycle issues. In addition, in the future effective economic regulation of PNG commercialised infrastructure services will help ensure that consumers benefit from these services. The Independent Consumer and Competition Commission will therefore have an increasingly important role to play.

## TELECOMMUNICATIONS

Telecommunications in Papua New Guinea has improved significantly. Economic deregulation and the 2008 rollout of Digicell's network connected millions of PNG citizens to the internet. Despite this, service outages are commonplace and penetration remains among the lowest level in the world. Papua New Guinea was ranked 163 out of 169 countries by the International Telecommunications Union (ITU) in 2013 in terms of internet affordability.<sup>2</sup>

Papua New Guinea faces a number of telecommunications challenges. Internal prices are too high, limiting access and imposing undue costs on all levels of society. Entry-level internet packages appear to be above the ITU's benchmark required to accelerate internet penetration (i.e. less than 3–5 per cent of monthly average income).

To increase capacity, Papua New Guinea needs new international internet bandwidth. It also needs secure, reliable high-speed domestic connectivity infrastructure.<sup>3</sup>

These challenges are driven in part by the current performance of the PNG telecommunications market, which can be explained in terms of population penetration, connectivity, and market structure (Table 1).

**Table 1: PNG telecommunication market overview**

Population penetration		Connectivity	
<b>Wireless:</b>	47%	Submarine cables:	2 (APNG-2 and PPC-1)
<b>Fixed:</b>	1.9%	Active IXP:	1 ongoing project
<b>3G/4G:</b>	16%	International	
<b>Broadband:</b>	0.15% (fixed broadband)	broadband:	~ 2.5 Gbps
Market structure			
<b>Mobile</b>		Internet	
<b>Digicell</b>	(Digicel)	Telecom PNG	(KCH)
<b>BMobile</b>	(KCH 85%, ADB)	Digicel	(Digicel)
<b>Telecom PNG</b>	(KCH)	Global Internet	(Global Tech)
		Daltron	(Carpenter Group)
Fixed Line		Wireless	
<b>Telecom PNG</b>	(KCH)	Dataco	(KCH)

*Note: ADB (Asian Development Bank), IXP (Internet Exchange Point), KCH (Kumul Consolidated Holdings).*

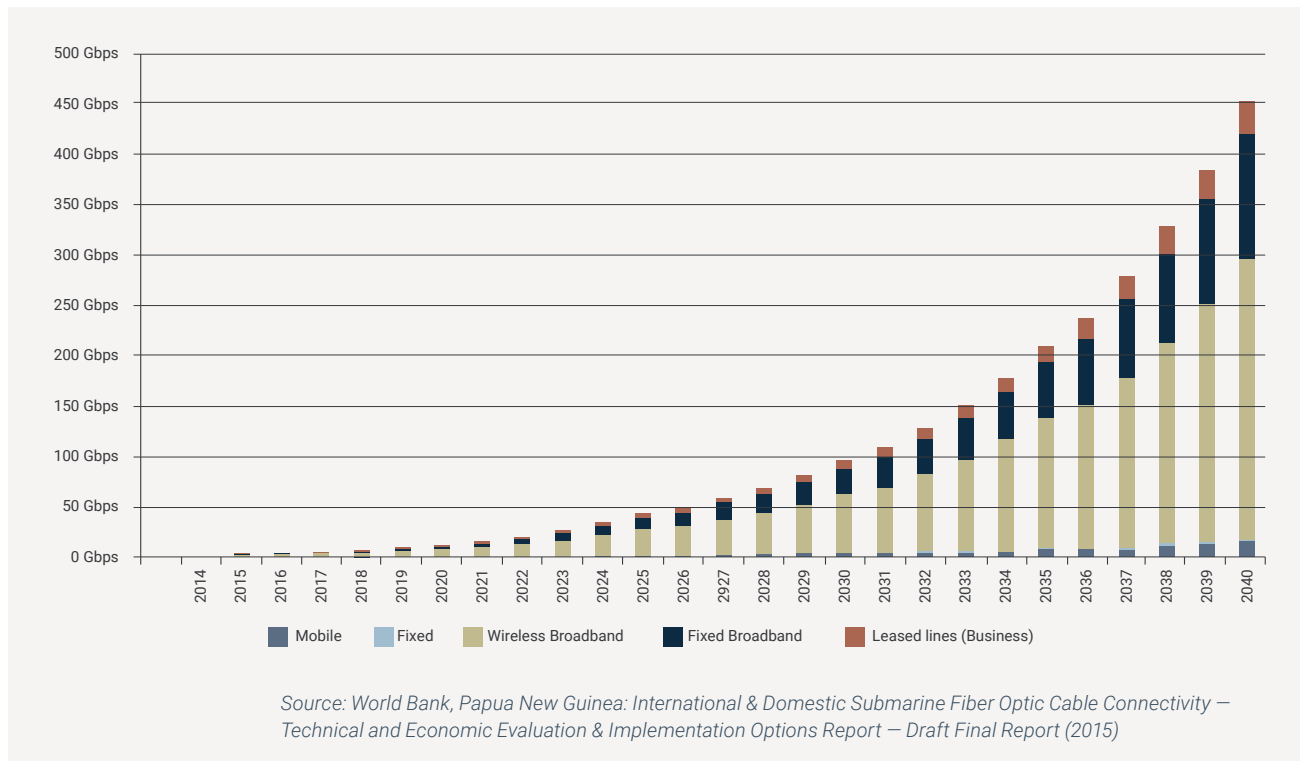
*Source: World Bank, Papua New Guinea: International & Domestic Submarine Fiber Optic Cable Connectivity – Technical and Economic Evaluation & Implementation Options Report – Draft Final Report (2015)*

Current demand for services is constrained by several factors. Fixed broadband penetration is essentially almost zero. Even though nearly half the population has wireless access, 3G/4G services across the country are scant as are fixed-line services. The latter may not be as relevant if the cost of establishing wireless services enables Papua New Guinea to 'skip' a generation of telephony infrastructure by avoiding copper wire installation and going direct to digital services.

Access to broadband is also determined by global connectivity. For a population of approximately 7.6 million, Papua New Guinea has two submarine cables providing approximately 2.5 Gbps of capacity. In contrast, Singapore, a high-income economy with a population of around 5.5 million, has 15 submarine cables landed at three separate locations providing bandwidth that exceeds 56.1Tbps.

Demand for bandwidth is rising in Papua New Guinea, and expected to grow from 2.5 Gbps at present to just over 450 Gbps by 2040 (medium scenario).<sup>4</sup> Given all the limits of its current infrastructure, Papua New Guinea will not be able to meet this demand (Figure 1).

**Figure 1: Demand for internet bandwidth, PNG (medium scenario)**



Several weaknesses of PNG telecommunications infrastructure need to be improved:

1. **Capacity for Port Moresby:** currently it has only 1 Gbps of submarine international cable bandwidth and some limited satellite/terrestrial fibre capacity. Demand is expected to increase in the next 15 years to around 10 Gbps.
2. **The domestic internet backbone:** the Madang–Port Moresby microwave connection has 1 Gbps with a planned upgrade to 3 Gbps. However, it regularly experiences outages that often last for several weeks. An upgrade is needed to improve both reliability and capacity as PNG's future bandwidth needs are expected to approach 100 Gbps over the next 15 years.
3. **Connectivity to island and western provinces:** telecommunication availability and intermittency are issues in PNG's island and western provinces. In contrast to some

other Pacific countries, PNG's geographic interior and dispersed communities pose challenges to ensuring landed international telecommunications services are accessible by large sections of the population.

The role that public institutions can play in Papua New Guinea requires careful consideration because the telecommunications sector comprises both highly corporatised government entities and current and potential commercial participants. Government should:

1. serve as a catalyst to bring stakeholders together in a common project they might not otherwise do alone;
2. provide some financial support where projects are financially challenging or have significant social impact;
3. influence the selection of project ownership and governance in a way that promotes competition to stimulate both market development and ensure downward price pressure is put on participants; and
4. influence project scope and design to better achieve economic, social and political goals where straightforward financial returns may not necessarily provide sufficient incentive.

Similarly, private telecommunications firms can play a role in Papua New Guinea where there is a conducive business climate that attracts investment capital and reduces public finance reliance. The attraction of having private sector engagement is the potential for rapid skill transfer and development in the field of information and communication technology. These firms can introduce business expertise and innovation in planning and design to ensure financial viability and customer focus. They can exert more financial and commercial discipline in telecommunications projects.

Telecommunications public-private partnerships (PPPs) integrate some of the advantages that the public and private sectors bring to these kinds of projects, provided there are appropriate trade-offs between public and private objectives in selecting, designing, and delivering telecommunications projects.

In Papua New Guinea, the introduction of new private sector network operators may encourage greater aggregation across geographic markets and cost sharing across all operator investors. However, new international or domestic telecommunications ventures will face challenging market economics and financial viability risks. Even where total demand generates sufficient revenue to cover total costs, the average cost per unit may still be high, use of new facilities inefficient and high prices charged. Effective economic regulation will need to address not only managing risks of monopolistic behaviour but also commercially relevant price paths that encourage greater competition and foster stronger consumer responses.

## TRANSPORT

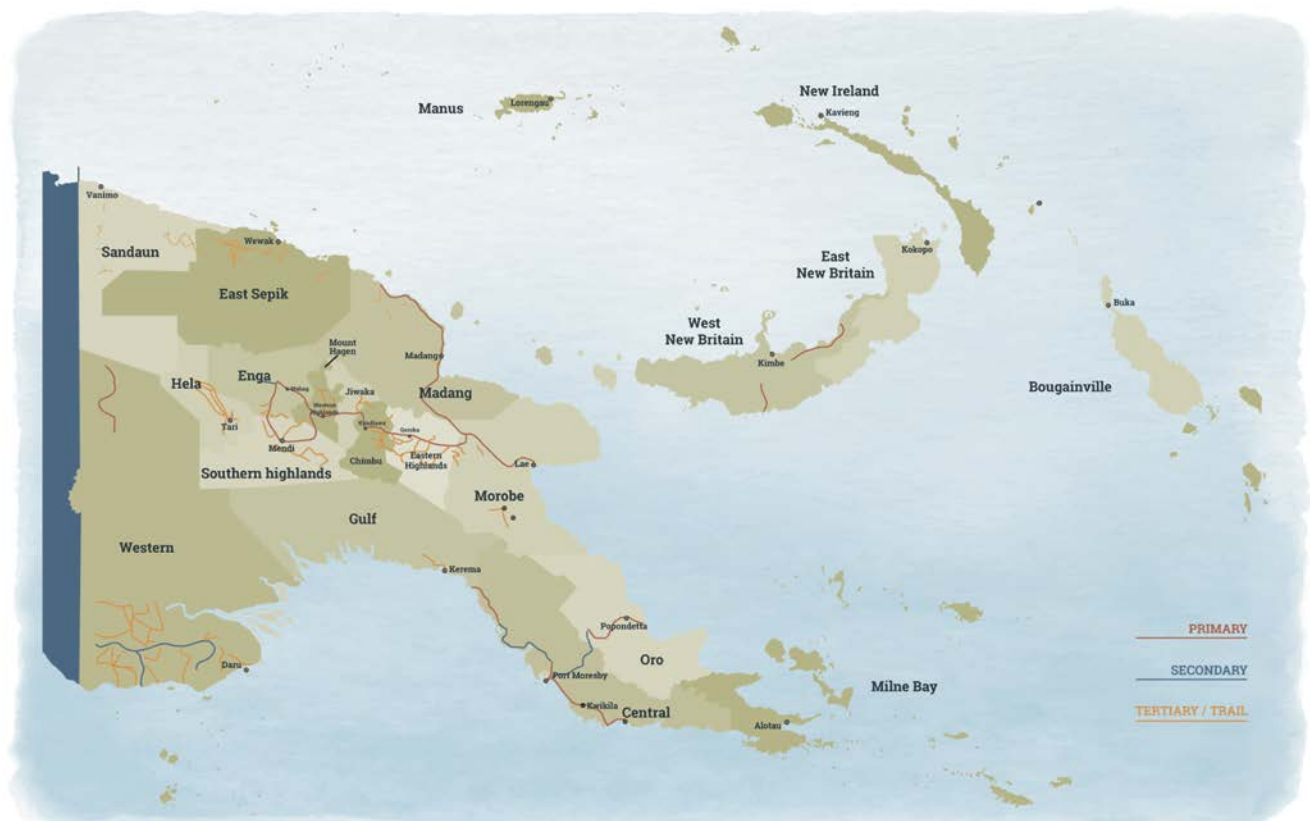
Transport infrastructure (road/water/air) and services are also restraining inclusive economic growth in Papua New Guinea. This holds back living standards and hampers measures to reduce poverty.

With some 600 islands and a topography that rises from sea level to 4500 metres, providing and improving transport infrastructure is a significant challenge in rural areas. Large sections of the population are isolated from social services, regional markets and income earning opportunities because of geography and poor transport infrastructure networks. The coverage and quality of PNG's transport networks lag far behind most other countries in Asia and the Pacific. The sustainability of transport infrastructure is also affected by climate change risk.

Transport infrastructure is unequally distributed across Papua New Guinea, resulting in unequal access to economic opportunities. It is not possible to travel by land between most provinces or ports. Coastal shipping services and aviation attempt to overcome these network gaps, but many of these services are not cost-effective.

**Road transport.**<sup>5</sup> The National Transport Strategy considers maintenance of the national priority roads the transport sector's greatest priority. Papua New Guinea contains approximately 22 000 kilometres of roads. The national road network comprises 8738 kilometres, only 40 per cent of which is sealed (Figure 2). The Department of Works is responsible for major road improvements and rehabilitation while the National Roads Authority is responsible for maintenance, with cooperation from the Department of Works.

**Figure 2: Papua New Guinea road network**



Source: WFP Logistics, Papua New Guinea Logistics Infrastructure, "Papua New Guinea Road Assessment"



The focus of most road planning is the 4256 kilometres of national priority roads (i.e. half of all national roads, both sealed and unsealed) in 16 separate alignments. The condition of these roads has improved in recent years: 33 per cent of the national priority road network was in good condition in 2007, rising to 46 per cent by 2011. However, more than 75 per cent of national, provincial, and district roads become impassable at some time during the year. Rural accessibility to roads is low; just 68 per cent of the rural population living within 2 kilometres of access to an all-season road.<sup>6</sup> Estimates indicate that the frequency of crashes is very high by Pacific standards.

There are no main highways between the country's biggest city Port Moresby and the Highlands region, which is home to around 40 per cent of the population. And there are no major roads between Moresby and the Morobe–Madang–Sepik region in the northwest of the country. The ability to utilise alternative ports to meet the national freight task is therefore restricted and the national freight and logistics system has less resilience to natural disasters than would otherwise be the case.

**Water transport.**<sup>7</sup> Approximately 60 per cent of the population of Papua New Guinea resides on 6500 kilometres of coastline and waterways, many without access to roads. Water transport predominates in these areas, especially on smaller islands. With its dispersed population, PNG's coastal shipping services take on special significance in providing access to rural communities. Innumerable small wharves, jetties and beach landings provide the basic infrastructure for maritime services, but the majority of these is in poor condition and carries very little traffic.<sup>8</sup> Deaths due to the sinking of overloaded ferries are not uncommon. More than 100 people are estimated to die in small craft every year.

The state-owned PNG Ports Corporation (PNGPCL) operates 16 ports, while private corporations operate at least five more. Lae port handles nearly half the country's maritime freight. Port Moresby and Kimbe are the next largest ports and operate on a cost-recovery basis; the remaining 13 ports incur losses. The PNGPCL's domestic ports have generally low cargo processing costs and the national shipping market is competitive.

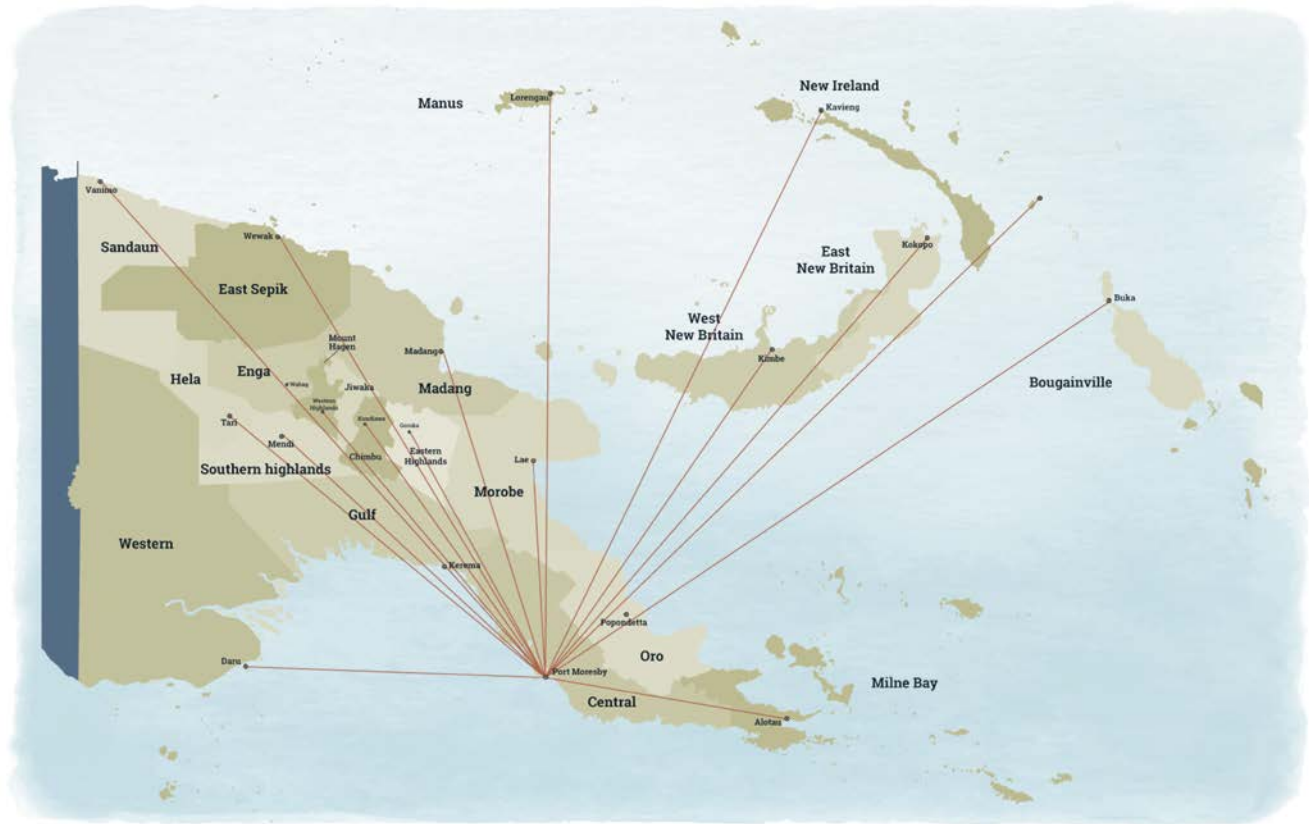
While export distances are aligned with the regional average, PNG's international shipping is among the most expensive in the Pacific region, with lack of competition driving costs. It takes 23 days to export goods from Papua New Guinea (the same as the regional average).

**Air transport.**<sup>9</sup> In addition to the 22 international and regional airports owned and managed by the National Airports Corporation (NAC) (Figure 3), Papua New Guinea has hundreds of rural airstrips.

While recent investments financed by the Asian Development Bank have helped to lift standards, the overall condition of the NAC's airports has deteriorated over time and they are beginning to pose threats to safety. PNG Air Services (PNGASL) provides navigation services.

International air traffic serving the country's international gateway (Port Moresby's Jackson's International Airport) is very expensive with unit costs (per passenger, per nautical mile) on flights to Australia the most expensive in the Pacific. Air Niugini's unit cost on Asian routes is more than 2.5 times that of inter-Asian flights.



**Figure 3: Papua New Guinea airports**

Source: WFP Logistics, Papua New Guinea Logistics Infrastructure

## ENERGY

Papua New Guinea is an energy resource rich country with a diversified portfolio of potential energy assets. Its self-sufficiency in fossil fuels is unusual among Pacific nations. It also has a large hydro potential, estimated to be about 15 000 mW. Despite this energy abundance, Papua New Guinea is the least energy-intensive economy in the APEC region.<sup>10</sup> The major policy drivers facing Papua New Guinea are to develop gas reserves for LNG exports, increase gas use for electricity and develop renewable options for rural electrification focused on hydro.

Demand for electricity in Papua New Guinea is growing.<sup>11</sup> As economic growth translates into increasing household disposable income, consumption is expected to rise by 2.55 per cent per annum. Assuming population growth of 3 per cent per annum,<sup>12</sup> this implies an annual increase in demand for electricity of around 5.5 per cent per annum, putting considerable pressure on existing electricity systems.

Yet like much of PNG's infrastructure, the energy sector performs poorly and energy planning is inadequate. The sector is highly fragmented, with ageing and inadequate plant and distribution systems that will struggle to address PNG's future energy needs.

Electricity in Papua New Guinea is distributed through three main networks: (i) the Port Moresby system; (ii) the Ramu system serving the load centres of Lae, Mt Hagen, Madang, Goroka, Kainantu, Kundiawa, Yonki, Wabag, Mendi, and Gusap; and (iii) the Gazelle system that services the communities of Rabaul, Kerevat, and Kokopo (Figure 4). In addition, there are a number of relatively large, isolated industrial developments. The government also established around 150–200 ‘C’ centres in the 1980s for the purpose of electrifying rural areas; however, very few of them remain operational.<sup>13</sup> The current unconnected nature of PNG’s networks should be addressed. While an interconnection is not currently considered feasible between the Port Moresby grid and the Ramu system, increasing demand and the need for network resilience in the future may require an intervention.

### Figure 4: Papua New Guinea power networks



Source: VisionRI Connexion Services Pvt Ltd, Power Sector Development Plan: Final Report – Main Report, TA 4932-PNG (Asian Development Bank and Department of Power and Energy (PNG), April 2009)

The Department of Power and Energy is notionally responsible for PNG's energy policy and planning. However, the state-owned and corporatised PNG Power Ltd (PPL) is almost by default the energy planner in Papua New Guinea by virtue of its technical capabilities and position at the centre of the major sources of electricity generation and network arrangements. Its commercial charter is not necessarily aligned with the economic development priorities of the nation. For example, prioritising a commercial return on the network addressing Port Moresby's energy needs may not meet the government's desire for more rural electrification.

PPL has been granted exclusivity for loads within 10 kilometres of its existing networks and individual customer loads of up to 10 mW within its network areas. It is a first step towards retail competition, because the maximum size of loads can be decreased over time as retail competition is extended. Significant areas of the country remain unserved, so exclusivity provisions are unlikely to be onerous for potential market entrants. Third-party access at the retail level to existing electricity grids is likely to be more problematic, requiring careful consideration by the Independent Consumer and Competition Commission.

Many PPL generating stations require overhaul and maintenance. System losses have continued to increase, mainly caused by a poor power factor,<sup>14</sup> but also because of ageing transmission and distribution lines and inadequate and out-dated substations. The poor performance of the electricity sector has been driven by several factors in recent years:

1. a disregard for the long-term capital budget in PPL's Ten Year Power Development program, meaning that capacity expansions and operational improvements have not been achieved;
2. tariffs set below regulatory allowable revenue levels, which has created chronic underfunding in the sector; and
3. ineffective regulatory controls, coupled with direct political interference in the operation of PPL, stymieing the development of the sector.

To date, private sector participation in the power sector has not involved significant generation, transmission or distribution of electricity for retail customers (households, commercial businesses or industrial businesses). Participation has focused more on capital generation sources to support isolated industrial sites (primarily mining operations).

Some isolated power projects have been undertaken in the Western Province. Six mini-grids were established by PNGSEL, a fifty-fifty joint venture between PNG Sustainable Development Program (PNGSDP) and Snowy Mountains Engineering Corporation (SMEC).

PNG policymakers face a number of challenges in the energy sector:

1. **Pursuing rural electrification through renewable sources.** The current approach to rural electrification seeks to develop renewable energy sources. Renewable technologies will be critical in providing PNG's rural population with affordable, sustainable, safe, robust, and reliable electricity.
2. **Seeking PPP opportunities in generation and distribution.** PPP opportunities are considered more likely in the generation and distribution/wholesale sub-sectors than in the supply/retail sub-sector. Independent power producers are more likely to engage in PPPs, potentially under concession arrangements with public sector partners. By contrast, captive generation projects are more likely to be fully private ventures with little public dimension to them.
3. **Improving land management to realise small-scale opportunities.** PNG's significant hydro resources would favour small-scale generation projects. However, land management will be a critical issue in ensuring their success, and where they are not stand-alone projects, negotiation of feed-in tariffs to PPL systems will also be important.

4. **Pursuing a regulatory approach to encourage more investment in distribution.** Private sector participation in distribution and supply is currently minimal. Attracting private investment will require an enforceable regulatory regime that balances the consumer interest in reasonable tariffs with the need to ensure a sufficient and predictable commercial return to attract private investment.<sup>15</sup>

A range of factors are limiting the creation of PPPs in PNG's energy sector. The highly dispersed electricity market and thin population density makes power distribution away from generation sources more costly. Independent power producers engage mainly with PPL, and so lack credit-worthy purchasers of their services. This thin market condition makes it challenging for independent power producers to develop viable projects that are not aligned with PPL's own commercial objectives. Most independent power producers are dedicated to specific resource projects rather than a heterogeneous customer base. Uniform tariffs and political considerations influence tariff increases, reducing revenues and making it difficult to improve the sector's creditworthiness and attract PPPs in the distribution sub-sector.

The role of non-government organisations and community organisations in rural access to electricity is often overlooked. These groups are critical in provision of stand-alone energy services such as solar and mini-hydro to remote areas in Papua New Guinea.

## **WATER**

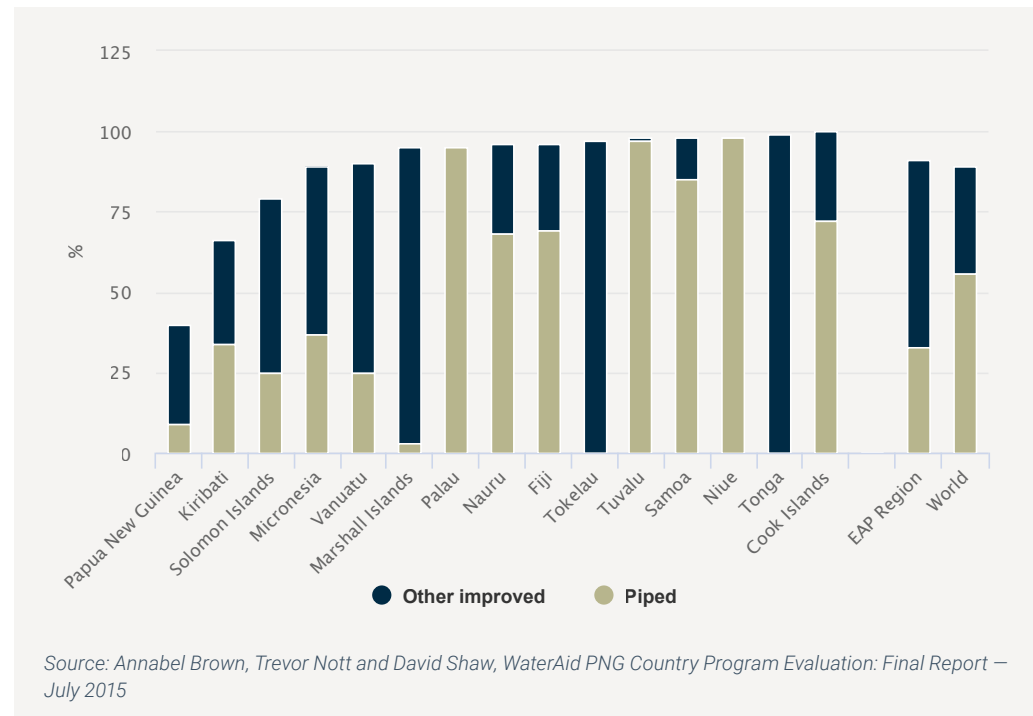
Basic water supply and sanitation are significant challenges for Papua New Guinea. Approximately 61 per cent of the population do not have access to safe water and 55 per cent do not have access to improved sanitation. Papua New Guinea is therefore denied many of the benefits that increased access to water and sanitation can provide: improved health of people through reduction in diarrhoea, malnutrition, and stunting; increased time and household income through safe and convenient water supply; greater productivity leading to economic development and higher rates of gross domestic product; and business and tourism development.

PNG's progress in improving the water and sanitation sector is held back by a number of impediments:<sup>16</sup>

1. the overall framework for service delivery and implementation<sup>17</sup>
2. weak policy on water and sanitation;
3. unclear institutional roles in the sector;
4. lack of budget mechanisms for allocating and tracking expenditures to rural and urban water and sanitation;
5. insufficient finance allocated to the sector;
6. weak monitoring systems; and
7. a scarcity of qualified technicians and managers.

**Comparisons.** Papua New Guinea has the lowest national water coverage of the Pacific region and is significantly below East Asia and Pacific and world comparators (Figure 5). Only the Marshall Islands has a lower percentage of piped coverage than Papua New Guinea. PNG's percentage of other improved water coverage is less than the world average and is the lowest for Pacific countries — a significant infrastructure challenge.

**Figure 5: Water coverage — Pacific countries**



Sanitation coverage is also very low in Papua New Guinea, with significant implications for water supply and public health. PNG's coverage is less than one-third of East Asia and Pacific and world averages and is the lowest among the Pacific nations (Figure 6). All but three other Pacific nations have three times the level of coverage available to PNG citizens.

Figure 6: Sanitation coverage – Pacific countries

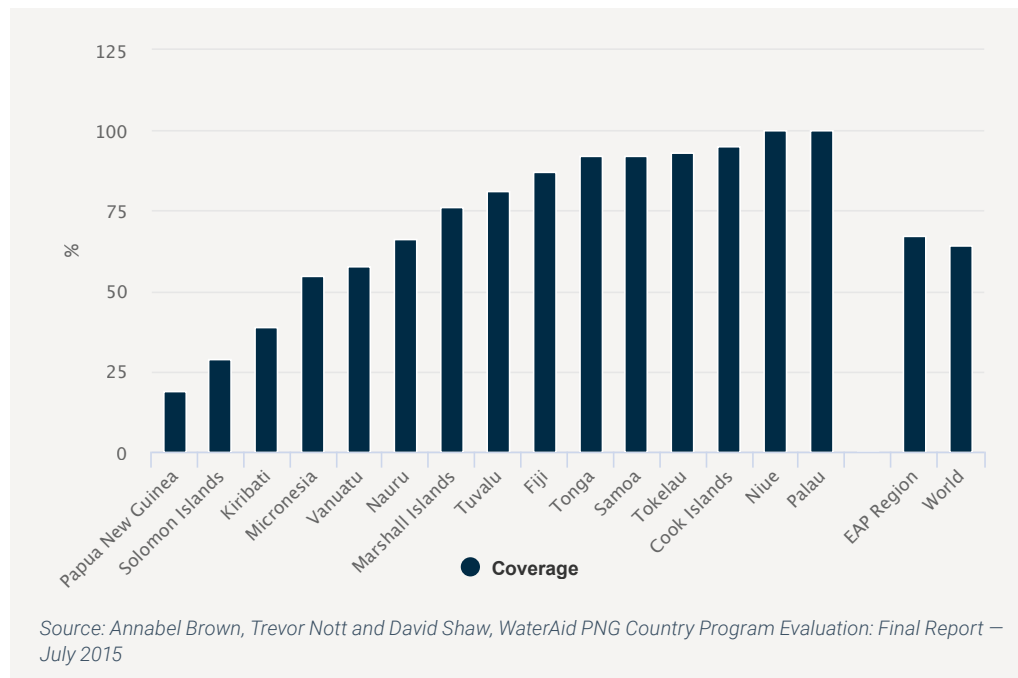
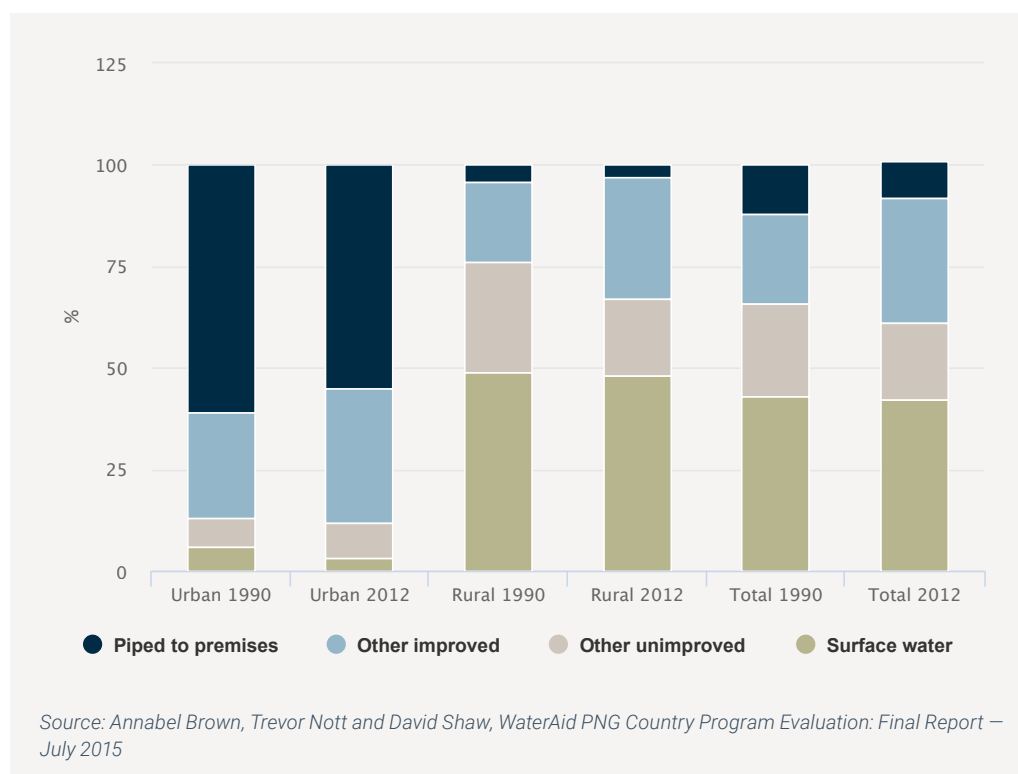


Figure 7: Changes in urban and rural water provision, PNG 1990–2012



Over time, population growth has resulted in declining coverage in provision of water piped to the premises, falling nationally from 12 per cent to 9 per cent of the population between 1990 and 2012.

Within Papua New Guinea, there is a significant divide between urban and rural areas. While more than half the urban population receives water piped to the premises, the coverage in rural areas (where more than 80 per cent of the population live) is 15–18 times lower.

Only a small proportion of the population benefit from improved water. The main improvement has been in 'Other improved' provision which has risen from 22 per cent of the population to 31 per cent between 1990 and 2012. However, the proportion of people accessing surface water has remained largely unchanged over a 20-year period, with continuing implications for public health.

Papua New Guinea faces a number of critical challenges in providing water infrastructure:

1. **Land tenure systems affect water charging regimes.** Uncertainty in land tenure in and around major population centres in Papua New Guinea is a major impediment to establishing an effective system of water rates for network-based storage, transmission, and distribution of water. This affects the ability of utilities to derive a cost-reflective stream of revenue from their assets.
2. **Water is perceived as free.** A strong, traditional perspective about water consumption in Papua New Guinea is that it is free of charge. Users do not perceive the value of infrastructure-based service delivery when they have access to natural water systems.<sup>18</sup>
3. **Water is seen as a communal service.** Water services have been seen as a communal service based on access to a common (and free) natural resource, particularly in rural areas and settlements.
4. **Challenges in achieving scale economies.** Scale economies in water delivery can be difficult to achieve because infrastructure and services are frequently local, small-scale and standalone systems servicing a highly decentralised population. These are often gifted to local communities to operate and maintain.
5. **Lack of formal infrastructure charging regimes.** There is no formal infrastructure charging regime for urban and peri-urban areas regarding provision of greenfield infrastructure. The absence of a defined developer contribution scheme creates a lot of uncertainty around infrastructure provision and identification of attributable costs. There is also no implemented policy on network capacity augmentations or expansions.
6. **Asset maintenance is difficult.** Asset maintenance and management is challenging. Water utilities will install assets, but do not retain ownership or control and will not necessarily maintain them. Local communities rarely have the technical capability to maintain these assets on their own.
7. **Rate payers cross subsidise other users.** There are significant informal cross subsidies between different user groups, with some revenues from rate payers being used to provide water services to peri-urban areas including townships where there is little or no user charging.



Water provision and sanitation are costly. Based on government targets for 2030, Papua New Guinea needs to spend on average US\$31 million each year on water supply and US\$70 million per year on sanitation. A further US\$22 million per year is needed to finance the operation and maintenance of current and future infrastructure. Yet PNG's investment in the sector has averaged 0.3 per cent of GDP in recent years — just a third of the internationally recognised minimum allocation of 1 per cent.<sup>19</sup>

## IMPROVING PNG INFRASTRUCTURE

Papua New Guinea needs to move on from its build-neglect-rebuild paradigm and develop a significantly different approach to infrastructure development. This has to consider the full life cycle of infrastructure assets to ensure the expected benefits are realised for PNG, as this will drive sustainable growth and improve living standards. Government needs to devise robust long-term plans based on clearly defined national and local aspirations. It needs medium-term budgeting to support the development of a pipeline of well-conceived projects. It should focus more on maintenance and service enhancement through high-value/low-cost projects. Early user and community engagement, with increased transparency in decision-making, can potentially de-risk projects. This should be accompanied by early definition of land-use needs for new infrastructure corridors, followed by adequate land use control and acquisition.

**Effective planning and prioritisation.** Investment in infrastructure requires large amounts of capital, creates long-lived assets, produces long-term streams of benefits and has significant impacts — both positive and negative — on people, the environment, and the economy.

Once infrastructure is delivered, reversing it is difficult and expensive. Proper planning and prioritisation are vital, and are more cost-effective than ad hoc, opportunistic approaches to infrastructure.

Infrastructure projects have long lead times to marshal both the physical and human resources for delivery. Effective planning and prioritisation provides government and industry with a clear, predictable pathway to properly manage these large projects, and creates the conditions for a credible pipeline of public infrastructure projects. With proper planning, the PNG Government would be in a position to engage more effectively with the private sector for support in project development, design, funding, delivery, operation and maintenance, and pursue feasible PPPs that are more in PNG's national interest.

**Life cycle infrastructure issues.** Like many Pacific nations, Papua New Guinea does not place strong emphasis on a full life cycle focus for its public infrastructure assets. The Pacific Regional Infrastructure Facility (PRIF) has estimated that Pacific Island countries need to spend an average of 6 per cent of GDP just to maintain existing infrastructure. They also need to address a backlog of delayed maintenance and establish budgets for planned infrastructure maintenance (Table 2).<sup>20</sup>

**Table 2: Indicative infrastructure life cycle costs per \$100 of asset**

Stage	Rate (%)	Construct/ supply only (\$)	+ Other upfront (\$)	20-year maintenance <sup>5</sup> (\$)
Concept and planning	2–5		2–5	
Detailed design specification	5–10		5–10	
Construction/supply		100	100	
Contingency/escalation	10		10	
Contract supervision	2–5		2–5	
Operating <sup>1</sup>	variable			
Maintenance – routine <sup>2</sup>	0–5			
Maintenance – periodic <sup>3</sup>	5–10			
Disposal and decommissioning <sup>4</sup>	variable			
<b>Total</b>		<b>100</b>	<b>120–130</b>	<b>10–120</b>

Notes: 1. Varies from zero (e.g. for buried pipes) to 20% pa for mobile plant and equipment

2. Varies from close to zero (e.g. for buried pipes) to 5% pa for routine maintenance of assets such as gravel roads

3. Based on 20-year asset life with periodic maintenance every seven years

4. Varies from close to zero to 100% (e.g. clean-up of toxic chemical sites)

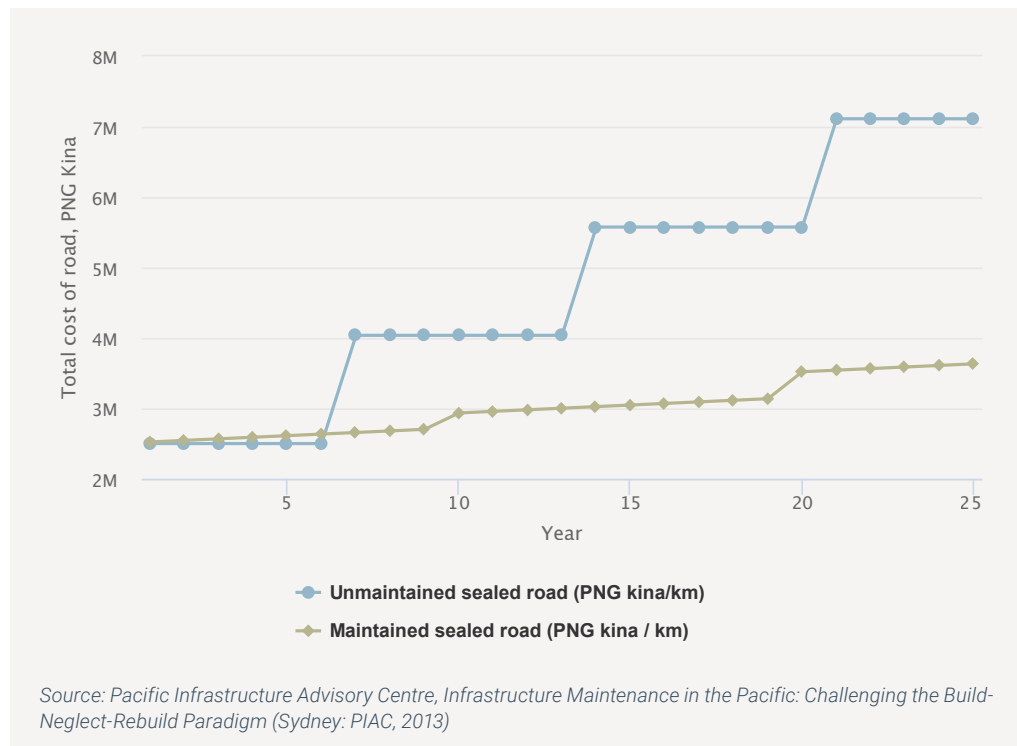
5. Varies based on infrastructure in question and across sectors

Source: Pacific Infrastructure Advisory Centre, *Infrastructure Maintenance in the Pacific: Challenging the Build-Neglect-Rebuild Paradigm* (Sydney: PIAC, 2013)

By failing to undertake preventative maintenance of its infrastructure, Papua New Guinea is missing significant savings opportunities. Figure 8 shows a simple 'least cost' analysis of PNG road maintenance.

This example illustrates that preventative maintenance is far more cost-effective on a total life cycle cost over a 25-year period. While a no-maintenance approach delivers short-term savings, over the long term it is four times as expensive as a preventative maintenance strategy.

An effective framework for asset management would ensure that there is sufficient and appropriate planning to ensure the right assets are available to deliver required services. It would also include effective maintenance planning to maximise the services delivered from those assets, and minimise the cost of their delivery. Maintenance programs would include routine, periodic and urgent maintenance, as well as provision for rehabilitation or refurbishment instead of replacement. Further, assets should be adapted/developed to meet progressively changing needs of users and to take advantage of technological change.

**Figure 8: Cost of maintaining a sealed section of PNG national road in service**

**Funding strategies for infrastructure investment.** PNG's recent resource boom was intended to be channelled, in part, towards significant infrastructure investment. It spurred the establishment of Kumul Consolidated Holdings, which placed a number of government business enterprises under a commercial structure. However, budget revenues (or their management) have been insufficient to maintain existing infrastructure and make the necessary investments to grow the public asset base of the nation.

PNG's planned spending on infrastructure (Table 3) drops away significantly over the forward estimates and is less (from 2018 to 2020) on an annual basis than public investment in administration. Spending in provinces over the five-year period is double that on infrastructure and by 2020 it is nearly six times the infrastructure investment. Papua New Guinea is not unique in its infrastructure problems. Developed economies have significant demand for infrastructure that cannot be met solely from the public purse. However, developed economies have a proportionately larger installed base of assets, more developed infrastructure markets, and a stronger acceptance of user pays to enable a more diverse set of funding streams.

The PNG Government does not have sufficient financial resources to fund the infrastructure necessary to drive further economic development and social progress. Other funding avenues need to be developed, whether investments by government agencies, investments by public or semi-public business enterprises, or investment by the private sector. Investment by PNG government business enterprises has been limited, because they operate in relatively undeveloped commercial markets with weak acceptance of the user pays principle.

Engagement with the private sector is most likely where the market for infrastructure services is most commercial. In Papua New Guinea, examples are the rapid expansion of mobile telephony and, to a lesser extent, some transport terminal operations (sea ports and airports)

that have commercially oriented facility users. The future engagement of the private sector in Papua New Guinea will depend on establishing an attractive business environment, and clear justification that use of private capital will lower life cycle costs on a risk-adjusted basis.

**Table 3: Sectoral distribution – Total Public Investment Program, 2016–2020 (kina m)**

Sector		5-year total	2016	2017	2018	2019	2020
Code	Description						
01	Economic	364.5	364.5	0.0	0.0	0.0	
02	Infrastructure	3269.9	1229.0	967.2	551.4	313.0	209.2
03	Social services	2777.2	1015.8	636.4	423.2	390.7	311.2
04	Law and order	1277.3	179.9	389.9	365.2	339.2	3.0
05	Administrative	3073.4	759.4	651.8	594.5	557.5	510.4
06	Provinces	6654.1	1547.4	1408.4	1271.0	1183.3	1244.0
<b>Total</b>		<b>17,416.4</b>	<b>5,096.0</b>	<b>4053.7</b>	<b>3205.3</b>	<b>2783.7</b>	<b>2277.8</b>

Source: PNG Budget Papers, Public Investment Program, 2016

## CONCLUSION

PNG's budget position and relatively undeveloped markets for infrastructure services present major issues that affect funding of ongoing infrastructure operations. The significant decline in the number of 'C' class power generation facilities and the underfunding of the national road network are key challenges. Full life cycle analysis of infrastructure is not being done consistently across major economic and social infrastructure assets. Further, funding streams for operations are not always identified and secured at the time investment decisions are made. Finally, revenue models that attract and reward private sector participation are not strong enough to sustain the private revenue streams.

Opportunities to address the most critical infrastructure challenges identified in this paper are:

1. **Transport** — improve planning and funding for maintenance of the national highway network and develop a national infrastructure strategy to strengthen PNG's freight and logistics systems.
2. **Electricity** — push forward on sustainable, rural electrification and commence planning for a more resilient national electricity grid.
3. **Water** — complete implementation of a national water, sanitation, and hygiene project management unit and push for greater planning of water distribution and reticulation in PNG's emerging urban areas.
4. **Telecommunications** — land more international fibre optic cable to improve PNG's connectivity to international telecommunications and improve the national telecom backbone in order to build greater resilience.
5. **Economic regulation** — increasing the role and scope of the Independent Consumer and Competition Commission to ensure price paths for economic infrastructure services meet the commercial agendas imposed on infrastructure bodies as well as PNG's broader national development goals.

## ENDNOTES

- 1 While this paper considers these infrastructure issues from a national perspective, it is clear that significant challenges also exist at the sub-national level, particularly in terms of effective planning and coordination of infrastructure, as well as funding. The parliamentary basis for district funding and lack of a range of technical skills at the district level appear to constrain effective and sustained provision of infrastructure and related services.
- 2 The National Research Institute, *Why Are Internet Prices High in Papua New Guinea?* Discussion Paper No 148, October 2016, prepared by Deloitte Touche Tohmatsu. Entry-level fixed broadband packages were estimated to cost 266 per cent of gross national income per capita. Since 2013 broadband wholesale prices have fallen by around 70 per cent, and over the last two years a 1GB package has fallen from 20–80 per cent of GNI per capita to around 10 per cent of GNI per capita.
- 3 World Bank, *Papua New Guinea: International & Domestic Submarine Fiber Optic Cable Connectivity – Technical and Economic Evaluation & Implementation Options Report – Draft Final Report* (2015).
- 4 Ibid.
- 5 Asian Development Bank, “Sector Assessment (Summary): Transport”, in *Country Partnership Strategy: Papua New Guinea 2016–2020* (Manila: ADB, 2015), <https://www.adb.org/documents/papua-new-guinea-country-partnership-strategy-2016-2020>.
- 6 It is clear that Papua New Guinea continues to under-resource maintenance, as budgeted funding for road maintenance is insufficient to address the task and allocated funding has reduced in recent years.
- 7 Asian Development Bank, “Sector Assessment (Summary): Transport”, in *Country Partnership Strategy: Papua New Guinea 2016–2020*.
- 8 WFP Logistics, *Papua New Guinea Logistics Infrastructure*, “Papua New Guinea Port Assessment”, <http://dlca.logcluster.org/display/public/DLCA/2.1+Papua+New+Guinea+Port+Assessment>.
- 9 Asian Development Bank, “Sector Assessment (Summary): Transport”, in *Country Partnership Strategy: Papua New Guinea 2016–2020*.
- 10 APEC *APEC Energy Demand and Supply Outlook*, 6th Edition (2016).
- 11 VisionRI Connexion Services Pvt Ltd, *Power Sector Development Plan: Final Report – Main Report*, TA 4932-PNG (Asian Development Bank and Department of Power and Energy (PNG), April 2009).
- 12 PNG’s population increased by an average of 3.1 per cent per annum between the 2000 Census and 2011 Census. Between 1980 and 2011 the population more than doubled from 3 million to 7.3 million: PNG National Statistical Office, “Population: Summary of Findings”, 2017, <https://www.nso.gov.pg/index.php/population-and-social/other-indicators>.
- 13 These electricity supplies were mainly for government institutions and public servant housing, with any spare capacity being made available to the public, church and mission organisations, and commercial businesses. However, most ‘C’ centres did not provide spare capacity.
- 14 The power factor is the ratio of real power flowing to a load to the apparent power in the system.
- 15 VisionRI Connexion Services Pvt Ltd, *Power Sector Development Plan: Final Report – Main Report*.
- 16 Contextual factors such as political volatility, poor access from a lack of roads, no electricity, customary land ownership, and ethnic conflict also hamper progress.
- 17 The establishment of a water, sanitation, and hygiene (WASH) project management unit within the Department of National Planning and Monitoring supported by the World Bank, the Asian Development Bank and Japan International Cooperation Agency with the intention of developing an improved service delivery framework is an important step.
- 18 In some instances, increasing population has put stress on natural water systems.
- 19 International Bank for Reconstruction and Development and World Bank, *Water Supply and Sanitation in Papua New Guinea: Turning Finance into Services for the Future*, Service Delivery Assessment, July 2013 (PNG Department of National Planning and Monitoring, PNG Department of Health, Water PNG, Eda Ranu, WaterAid, World Bank Group and Water and Sanitation Program, 2015).
- 20 Pacific Infrastructure Advisory Centre, *Infrastructure Maintenance in the Pacific: Challenging the Build-Neglect-Rebuild Paradigm* (Sydney: PIAC, 2013).



# **CHANGING GEOPOLITICAL DYNAMICS FOR PAPUA NEW GUINEA**

JENNY HAYWARD-JONES

## **INTRODUCTION**

The new O'Neill government faces a rapidly changing external environment as it struggles to manage a significant domestic economic downturn and unprecedented pressures on the national budget. Australia remains Papua New Guinea's closest foreign partner; by far its largest bilateral aid partner, trading partner and foreign investor, but its influence is diminishing as that of other actors is growing. China is an increasingly important player — as a trade partner, investor in infrastructure and source of foreign loans, as well as in the small to medium business sector. Relations with other Asian nations are expanding. Large foreign companies are exerting more influence on government policy than most nation state development and trade partners of Papua New Guinea can hope to exercise. These relationships are likely to come into sharper focus over the next year, as the PNG government prepares to host APEC in 2018. It is not clear that the new PNG government has the capacity to pursue the national interest abroad while it is preoccupied with a complex set of challenges at home.

## **HOW PAPUA NEW GUINEA INTERACTS WITH THE WORLD**

The Pacific Islands region, once remote from the global centre of economic gravity, is now benefiting from its proximity to the centre of global growth that is China, East Asia, and India. The neglected and relatively poor Pacific Islands end of the Asia-Pacific region is increasingly attracting the attention of outside powers as its neighbourhood has grown wealthier. China's profile in the Pacific Islands has grown enormously. China's interests in Papua New Guinea have predominantly focused on trade and investment but in the last year Beijing has for the first time leveraged these interests to put public pressure on the PNG government and other governments in the region to support its actions in the South China Sea, signalling a shift in dynamics in its relations with the island states.

Papua New Guinea, the largest, most resource-rich and most populous state in the Pacific Islands region, has the potential to be the most influential player in the region. While it takes its responsibilities in the Pacific Islands region very seriously, Papua New Guinea has been more interested in recent years in improving relations with Asian countries, where there are more opportunities to expand trade and attract investment. A member of APEC as well as the Pacific Islands Forum, Papua New Guinea has longstanding trading relationships with key Asian economies China and Japan, and growing trade relations with other East Asian nations, including Indonesia with which it shares a land border. The shift of PNG's connectedness into Asia and away from Australia is exhibited in Figure 1 (see p.91).

As PNG's relations with Asian countries have been strengthening, it struggles to play a consistent leadership role within the Pacific Islands region. This is in part because Papua New Guinea lacks the financial capacity to support a more ambitious regional policy. The budget of the Department of Foreign Affairs and Trade has steadily declined since 2013 and there is no indication that more resources will be available to the Department in the near future. The Department's actual expenditure totalled PGK68million in 2015, down from PGK75million in 2013, and the appropriation for the Department in 2016 was reduced to PGK59.3million and in 2017 to PGK44million.<sup>1</sup>

Papua New Guinea's 21 foreign missions appear to be struggling with reduced funding. The most obvious consequence of this was Papua New Guinea losing its right to vote at the United Nations in early 2017 after failing to pay its United Nations dues.<sup>2</sup> Following media reporting of the issue, the PNG government eventually paid the outstanding sum of US\$100 891 to regain its voting rights.<sup>3</sup>

Papua New Guinea is also constrained by Fiji, which has traditionally played the role of regional leader and continues to seek to do so with some success, particularly in global advocacy on climate change. Fiji currently holds the Presidency of the COP23 UN negotiations on climate change. As Suva hosts the Pacific Islands Forum, the University of the South Pacific (the regional university) and other regional organisations, Fiji is often better able than Papua New Guinea to persuade the rest of the world that it represents the Pacific Islands region.

Papua New Guinea's foreign policy has been driven by Prime Minister Peter O'Neill. In the first few years of his prime ministership, Peter O'Neill was active in promoting Papua New Guinea to the world, impressing foreign leaders with his can-do leadership style and PNG's strong economic growth story. O'Neill worked particularly hard on improving relations with the Australia Government, and in turn it was prepared to work more closely with the O'Neill government than had been the case during the Howard-Somare years. While relations with Australia have been coloured by the Refugee Resettlement Arrangement since 2013, O'Neill has maintained close ties with successive Australian prime ministers. O'Neill also worked to improve PNG's relations with its nearest neighbour, Indonesia, hosting a visit by President Jokowi in May 2015 and expanding relations with several Southeast Asian states, including the Philippines and Thailand, in addition to seeking a more substantial relationship with China.



## CHINA'S AMBITIONS IN PAPUA NEW GUINEA

The growth of China's interests and influence in the Pacific Islands is the biggest story of the decade in the region. In the past few years, China has become the region's second-largest trading partner and a significant investor.<sup>4</sup> Although China delivers aid very differently from the region's traditional donors and mostly through loans rather than grants, Lowy Institute research shows that China could be the region's third most significant aid partner.<sup>5</sup> It is a remarkable advance from the situation a decade ago when China's interests in Pacific Island states were largely motivated by its competition with Taiwan for diplomatic recognition and its aid contributions characterised as 'chequebook diplomacy'.

China's presence in the region has undergone a significant shift over the past decade. Beijing now competes with more established players such as Australia, New Zealand, and France for influence with Pacific Island governments. But while China's interests in Pacific Island states appear to be substantial, it is worth recognising that these interests are only a small element of the global story of China's rise. China is the world's leading exporter, is seeking to be a more relevant aid partner in the developing world, and is growing its portfolio of foreign investments. No Pacific Island country ranks in China's top 50 trading partners. Papua New Guinea is ranked 124 on the list of countries China exports to and 66 on the list of countries from which China imports goods.<sup>6</sup>

Papua New Guinea's size and its resources sector make it China's most significant partner in the Pacific Islands region. China–PNG trade totalled some US\$2.3 billion in 2016.<sup>7</sup> This represents about a twelvefold increase since 2000. While PNG's trade with Australia is worth considerably more than its trade with China in 2016, China's trade prospects are on a growth trend and Australia's are declining. China's direct investments in Papua New Guinea totalled US\$496 million in 2015.<sup>8</sup> Chinese investment and the Chinese nationals who work in Papua New Guinea on Chinese projects tend to attract much attention but the value of these projects is not about to overtake the value of individual investments of major resources companies or Australian foreign direct investment.

According to Lowy Institute research, China's aid to Papua New Guinea since 2006 totals approximately US\$632 million.<sup>9</sup> This pales into insignificance if compared with cumulative Australian aid to Papua New Guinea over the same period (in excess of US\$3.4 billion). However, the majority of China's aid is delivered through loans, so cannot be directly compared to aid delivered by other partners. Chinese aid includes projects in vocational training, communications, fisheries, agricultural technical cooperation, and infrastructure such as a military hospital upgrade, university dormitories and roads. China has a patchy record of aid project implementation in Papua New Guinea, with some projects such as university dormitories praised for their high quality and other promised infrastructure not ever delivered.

Beyond its trade, investment and aid links, China has a diaspora, both old and new, in Papua New Guinea, which has helped to expand its influence. It has also invested in soft power, including in television broadcasting and in scholarships, which signals its interest in building a long-term relationship with the people of Papua New Guinea.

Chinese aid, trade and investment has traditionally been perceived in Papua New Guinea to come with ‘no strings attached’ but that assumption has been challenged in the past two years. While China has made more loans available to Pacific Island countries, Papua New Guinea has not rushed to take these up, cautious about the debt obligations that will follow. Prime Minister Peter O’Neill visited Beijing in July 2016, during a period where Chinese diplomats had been putting pressure on Pacific Island states to support its position in the South China Sea. For the first time, O’Neill agreed to respect China’s position and agreed to the issue of a joint press release that asserted China’s “legitimate and lawful rights and interest in the South China Sea, and its right to independently choose the means of dispute settlement in accordance with law”.<sup>10</sup> Although O’Neill clarified that Papua New Guinea thought maritime disputes should be resolved under international law, his apparent bowing to China’s pressure on this key strategic dilemma for the Asia-Pacific was a departure from PNG’s longstanding tradition of avoiding involvement in great power debates or aligning with Australia and other Western powers.

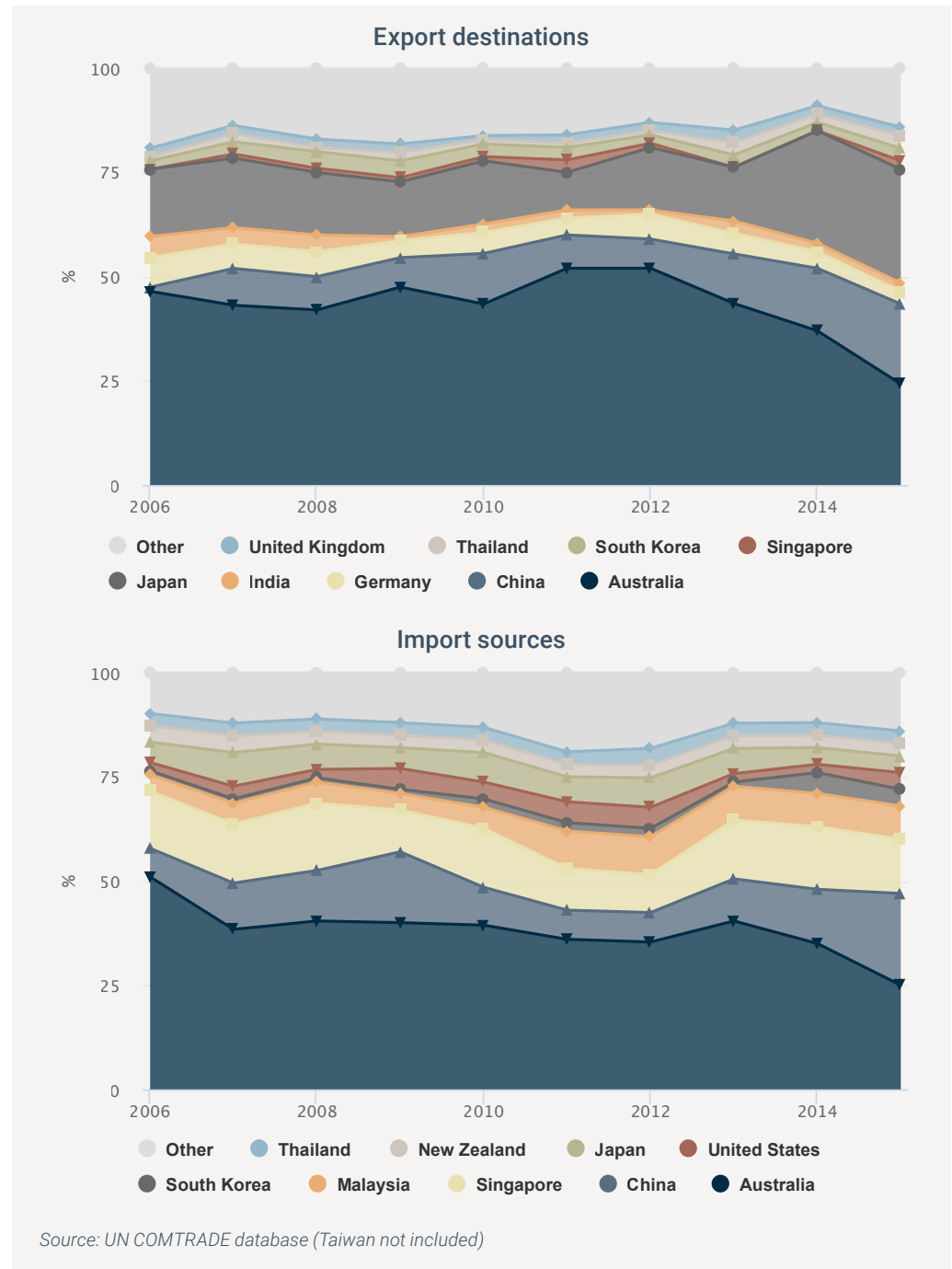
China’s willingness to put public rather than private pressure on Papua New Guinea to align itself with its position on such a critical strategic issue suggests that it is no longer content with its image as a generous and altruistic partner and will be making more public calls on Papua New Guinea for support for United Nations votes or in other regional disputes. A more demanding China could create difficulties for PNG’s ambitions to strengthen its relations with other East Asian states.

## **WHAT IS DRIVING THE INTERESTS OF OTHER NEW PLAYERS?**

Growing trade ties between Papua New Guinea and East Asian states beyond China often go largely unnoticed in debate about PNG’s international profile. According to IMF data from 2016, Asian states comprise seven of PNG’s top ten trading partners, with Singapore second, China third, Japan fourth, Taiwan sixth, Malaysia seventh, India eighth, and Thailand tenth.<sup>11</sup>

Despite these poor educational outcomes, public expenditure on education is not low by international standards and compares relatively well against other countries in the region, averaging around 5 per cent of GDP and 15 per cent of the national budget. Distribution of these resources remains a critical issue, as does the proportion absorbed by wages and administration. Technical and vocational education and training (TVET) have also been badly under-resourced for decades even though many students, particularly males, seek greater emphasis on practical work skills during school years.

With the \$19 billion PNG LNG project coming on line in May 2014 PNG’s exporting landscape has dramatically changed, with Japan, Taiwan, and China competing with Australia as primary exporting markets for Papua New Guinea.

**Figure 1: PNG's rapidly changing trade portfolio**

With Asian countries such as China, Singapore, and the Philippines offering more opportunities for education, training, trade, and technical cooperation, PNG's attention is increasingly directed to Asia. Asian businesses, large and small, have been setting up in Papua New Guinea in recent years and helping to strengthen ties with Asia. Increasing numbers of workers from Asian countries have been coming to Papua New Guinea for employment over the past five years, with Philippines, India, China, and Malaysia the main

source countries.<sup>12</sup> PNG students have been increasingly seeking out education in the Philippines as it is cheaper than Australia and has the advantage of English-language instruction and direct flights. In turn, the Philippines has become the second-largest source of foreign workers for Papua New Guinea.

While PNG's trade relationships with East Asian countries are growing, the interests of these countries in Papua New Guinea are as yet largely limited to trade, investment, and employment. There are opportunities to strengthen technical cooperation and education links that could be of significant benefit to Papua New Guineans but these sorts of ties are only in the very early stages of development.

## **INFLUENCE OF NON-STATE EXTERNAL ACTORS**

The resource-dependent nature of PNG's economy means that major resources companies wield influence in Papua New Guinea exceeding that of nation state partners. This influence matters because the actions of major resources and logging companies play a critical role in determining the trajectory of the PNG economy. The direction of PNG's exports and the development of future investment potential are largely determined by a select group of major foreign investors in Papua New Guinea which helps to guide the government's foreign and trade policy priorities. This gives multinational and foreign companies strategic significance in Papua New Guinea that deserves greater recognition.

In addition to their extraction activities, resources and logging companies fulfil a role that in most nations would be more properly assumed by the state, for example building infrastructure, and delivering health and education services in the communities in which they operate. Foreign investors in Papua New Guinea are expected to deliver on social development outcomes in the rural areas in which they operate as part of the agreement they make with government when they invest. This has been the case with a number of major companies, including Oil Search, Ok Tedi, Steamships, Rimbunan Hijau and, latterly, ExxonMobil. The size of their investment and the contribution multinationals make to national development priorities makes it difficult for the PNG Government to resist their influence.

While many multinational or foreign companies in the resources, logging, and finance sectors wield influence in Papua New Guinea, the size and scope of US multinational ExxonMobil's investment gives it a dominant position in the country. ExxonMobil's initial investment in PNG LNG exceeds US\$19 billion. Its operations, which commenced in 2014, include gas production and processing facilities, onshore and offshore pipelines, and liquefaction facilities.

ExxonMobil ships liquefied natural gas from Papua New Guinea to customers in Asia. In 2016 ExxonMobil produced 7.9 million tonnes of LNG – an increase of 14 per cent from the original design specification of 6.9 million tonnes per annum.<sup>13</sup> The company employs 2500 people, 80 per cent of whom are Papua New Guinean nationals. In the rural communities in which it operates, ExxonMobil has invested more than PGK800 million (US\$247 million) on building infrastructure and developing social programs focusing on education, health and environment, women's economic empowerment, and agriculture.

The company also invests to improve access to education and in a community health program in its project areas.<sup>14</sup>

The size of Exxon's investment in Papua New Guinea exceeds the current size of the stock of Australian foreign direct investment in the country. Combined with the representation of exports from Exxon's operations in PNG's annual exports, Exxon could be considered a more significant economic and strategic player in Papua New Guinea than Australia. It already is clearly more important to Papua New Guinea than any one Asian nation, including China. Exxon's influence is evident not only through the close relationship it has to have with the PNG Government and its contribution to the direction of trade, but also through its ability to determine confidence in the PNG economy and to inspire or dissuade other new investments in Papua New Guinea.

Corporate influence on government is by its very nature opaque, is exercised during private meetings, and usually excludes the public. Managing the diverse range of demands and advice from corporate players is challenging for PNG ministers and officials. But the PNG Government could do more to ensure that the influence of foreign investors delivers results for the people, not financial returns for individual decision-makers.

## **LIKELY IMPACT OF PNG'S HOSTING OF THE APEC SUMMIT IN 2018**

Hosting the APEC Leaders' Meeting offers a unique opportunity for the government and business community of Papua New Guinea to market the potential of the nation to other APEC nations. It will be the first time Papua New Guinea hosts a summit of this size and significance and the first time it will host international media beyond the region.

If leveraged to its maximum benefit by the PNG Government, successfully hosting the summit could assist in raising PNG's profile in the APEC region and improve awareness of PNG's economic potential. But if it is poorly managed, PNG's hosting of the summit is more likely to reinforce the image of Papua New Guinea as an outlier in APEC and worse, raise doubts about its reliability as a trade and investment partner.

It is already clear that Papua New Guinea cannot afford to host the APEC Leaders' Meeting in 2018. Backing out of its commitment is highly unlikely at this stage. Public criticism is likely to persist, given that budgets for essential government services are under huge pressure and already being diverted to pay for an event that provides no immediate direct benefit for the population.<sup>15</sup>

The Australian Government is contributing approximately one-third of the costs of hosting the Leaders' Meeting. Papua New Guinea has reportedly budgeted PGK800 million (A\$330 million) for the APEC summit. This does not include the construction of the purpose-built APEC Haus convention centre, which is being constructed by LNG producer Oil Search through a tax-credit scheme.<sup>16</sup>

Papua New Guinea has form on poor budgeting for events. Its expenditure on hosting the Pacific Games in 2015 came under considerable domestic criticism. Many of the venues were unfinished or only just finished when the Games began. But more worryingly, the

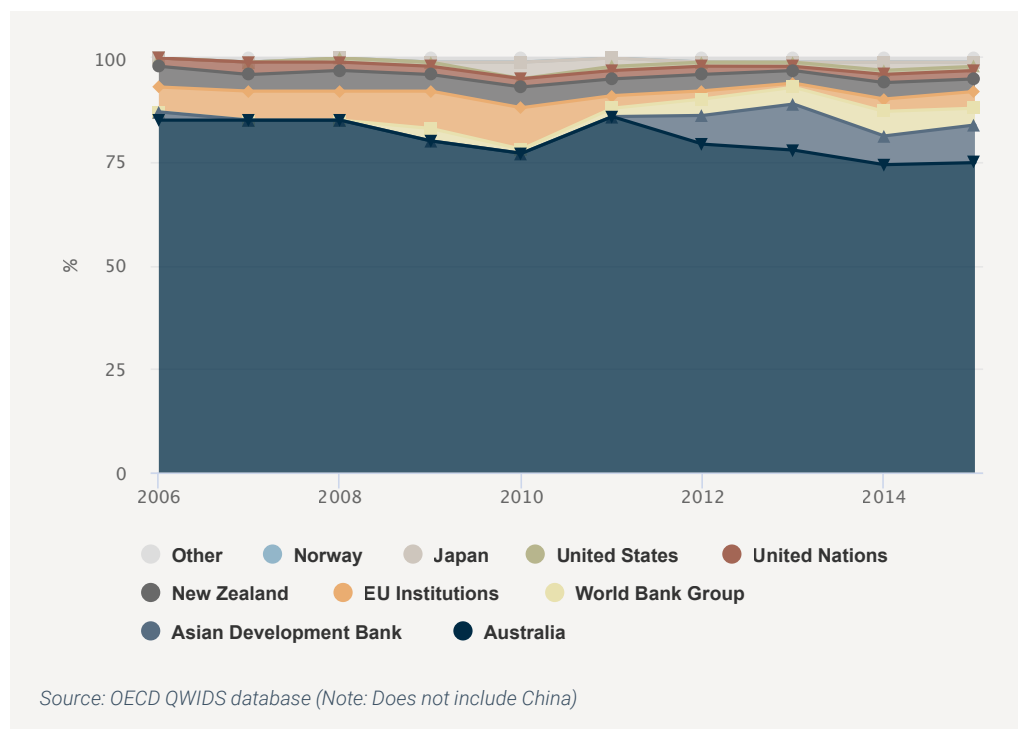
government cut budgets for essential services to ensure construction of Games venues was finished. This pattern has been repeated, with health and education budgets said to be taking a hit that they cannot afford and which will cause suffering in the rural population.

The PNG Government will need to work harder to persuade the population that there are long-term benefits to the nation in using this event to enhance its links with Asian partners and build international interest in Papua New Guinea. Working closely with the business community in this task, as the O'Neill government is doing, should help but more transparency is also needed.

## PROSPECTS FOR IMPROVING THE AUSTRALIA-PNG BILATERAL RELATIONSHIP

Australia's relationship with Papua New Guinea appears to be strong on the surface. Australia's High Commission in Port Moresby is one of the largest Australian diplomatic missions in the world and has more attachéd agencies than any other mission, demonstrating the breadth of Australian Government engagement with Papua New Guinea. A bilateral Papua New Guinea Ministerial Forum is convened on an annual basis. There are numerous bilateral agreements supporting the relationship. Trade, investment, defence, and aid ties are strong and enduring. Australia enjoys a dominance in the delivery of aid to Papua New Guinea that is almost unheard of in international development (see Figure 2). Australia's Department of Foreign Affairs and Trade describes the bilateral relationship as an "economic and strategic partnership".<sup>17</sup>

Figure 2: Aid flows to Papua New Guinea



In the 2016 Australian Defence White Paper a high priority was placed on Australia's defence relationship with Papua New Guinea. The White Paper committed to "increase [its] cooperation with the Papua New Guinea Defence Force and Department of Defence in the decade ahead".<sup>18</sup> After a secure Australia, the White Paper identifies Australia's second strategic interest as a secure nearer region including Papua New Guinea and says Australia will continue to be PNG's principal security partner. The White Paper also asserts that "geographical proximity means the security, stability and cohesion of Papua New Guinea contributes to a secure, resilient Australia with secure northern approaches".<sup>19</sup> Despite weaknesses in the capacity of PNG's security forces, the Australia–PNG defence relationship is a strong one and has potential for growth.

Australian investment in Papua New Guinea totalled almost A\$18 billion in 2016, of which A\$15.8 billion was foreign direct investment. Bilateral merchandise trade was worth A\$5.3 billion in 2016.<sup>20</sup> According to data collected by DFAT, Australia was PNG's largest source of imports and second-largest export destination in 2015.<sup>21</sup>

Australia will spend approximately \$546 million in official development assistance or "aid" to Papua New Guinea in 2017–18. This is almost \$200 million more than Australia will spend on aid to Indonesia, the second-largest recipient of Australian aid over the same period. Australia's complex aid program supports three broad objectives: promoting effective governance, enabling economic growth and enhancing human development.<sup>22</sup> Although the PNG economy is not aid-dependent, Australian aid is still in high demand.

With strong pillars holding up the bilateral relationship, the future of the relationship under the new O'Neill government has good potential. But there are fissures in the relationship. The Refugee Resettlement Agreement signed by Prime Ministers Kevin Rudd and Peter O'Neill changed the balance of power in the bilateral relationship. Canberra's dependence on O'Neill to continue to detain asylum seekers and ensure they never entered Australia gave the PNG Prime Minister confidence to dictate terms in the relationship and made it impossible for Australian ministers and officials to say or do anything about allegations of corruption against the O'Neill government. And until the fate of asylum seekers on Manus is certain, the issue will remain a barrier to genuinely improving the bilateral relationship. Limited public awareness of Papua New Guinea in Australia and the tiny size of the PNG diaspora in Australia means there is not a strong lobby group to push Canberra to improve relations.

However, even if relations can be improved under a new government, there are likely always to be tensions. Australia's colonial legacy and the contemporary breadth of coverage of Australia's aid program means the Australian Government will likely remain a convenient whipping boy, rightly or wrongly, when things go wrong in Papua New Guinea. The difficulties Papua New Guineans have in obtaining visas to visit Australia are highly unlikely to be addressed during the term of the next PNG Government and will continue to be an irritant in the bilateral relationship.



## CHALLENGES FOR A NEW PNG GOVERNMENT IN MANAGING GROWING INTERESTS OF EXISTING AND NEW PLAYERS

The new O'Neill government faces very different challenges following this election to those it faced following the 2012 elections. The fast-declining national economy, combined with major failings in funding essential service delivery — particularly in health — creates a sense of urgency for action. Allegations of corruption against O'Neill himself have yet to be addressed in court and will remain a festering sore on the Prime Minister's leadership. The rural majority has found ways around the elections to protest its frustration with the government's failings to deliver even basic development and is likely to continue to voice concerns, especially as there is little chance things will improve. The business community continues to protest restrictions on foreign exchange, which appear to have no resolution. The short-term outlook for the country is decidedly negative.

The government will be tempted to look for quick funding fixes. Seeking new loan arrangements from the multilateral banks or even from China could be on the agenda. Another approach to Australia for budget support is also likely. The government will continue to seek private sector support for building infrastructure and for service delivery.

The government will need to focus on attracting new investment in resources at a time when global prices for PNG's resources are low. With a crisis in health funding forcing serious cutbacks in hospital and other critical health services, the role of the private sector in assisting the government to deliver health services to the communities in which they operate will become even more pronounced.

Readying Port Moresby to host the APEC meetings in 2018 will be an immediate priority. Cost over-runs are likely, even with Australian support.

Despite its financial problems, the good work the PNG Government has done in expanding relations with Asian states in recent years means there are opportunities to deepen trade and investment ties with the stronger economies of East Asia and with India.

Managing Beijing's expectations provides its own challenges. China is likely to exert pressure on a weak Papua New Guinea to again support its questionable international actions in the South China Sea. Australia has concerns about China's growing influence in the region and in Papua New Guinea, which may create new tensions in the Australia–PNG relationship if Australia seeks to put the brakes on China's capacity to influence the PNG Government. Other East Asian nations, particularly Japan, are also concerned about how China exerts its influence in the region. Papua New Guinea will need to ensure it is maintaining friendly relations with all its partners and avoid being drawn into disputes.

Papua New Guinea does not have sufficient resources right now to expend on enhancing its diplomatic profile in Asia. It should focus on strengthening trade and investment ties and encouraging technical cooperation and education links which will provide more opportunities to its population. To this end, the PNG Government would benefit from seeking to facilitate more development cooperation between China and other bilateral partners to help the people of Papua New Guinea. This would make it clear to China that

its domestic development takes priority over any involvement in international disputes and enable Papua New Guinea to better determine its own foreign policy.

## CONCLUSION

Managing a range of existing and evolving foreign interests will be difficult for a financially constrained O'Neill government that is rightly preoccupied with more important domestic challenges. But for all the difficulties, there are also opportunities. Hosting the APEC Summit in 2018 will bring a concentration of international attention to Papua New Guinea's potential that would otherwise take years to attract. Much good preparatory work to strengthen relations with Asia has already been done. Papua New Guinea maintains the respect of other Pacific Island countries and could seek to lead on regional issues where Fiji cannot. Papua New Guinea's economic fortunes are suffering now but there are good long-term prospects being recognised by international investors. Continued growth in trade and investment links with China can assist in spurring economic growth in Papua New Guinea. Australia will remain Papua New Guinea's closest partner, friend, and protector but there is work to be done on both sides to improve the bilateral relationship and deliver better dividends from Australia's commitment to Papua New Guineans.

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# FUTURE SCENARIOS FOR PAPUA NEW GUINEA

JONATHAN PRYKE

## INTRODUCTION

Until recently, visitors making their way to the immigration checkpoint at Jacksons International Airport in Port Moresby were greeted with a sign exclaiming, “Welcome to Papua New Guinea: The land of the unexpected”. In a nation that is so self-aware of its unpredictability, forecasting future scenarios is like staring into a crystal ball. Quality data is scarce and incomplete, trends are difficult to establish and validate, and prognostications on PNG’s future are often dogmatic and politicised.

Over the past 42 years Papua New Guinea has defied many of the most negative projections for its future, and navigated a huge number of ‘crossroad’ situations. Even before 1975, some were arguing that independence would be an unmitigated disaster, and the risk of Papua New Guinea becoming a failed state is a question that has permeated its short history.<sup>1</sup> It is a question that is now being asked more frequently.<sup>2</sup> On one view, Papua New Guinea has managed to “muddle through”, largely on the strength of its peoples’ resilience in the face of adversity.<sup>3</sup> However, this resilience may be dwindling, and rather than “muddling through”, Papua New Guinea may instead be on a “muddling down” trajectory.<sup>4</sup> Its politicians, on the other hand, claim that the country’s prospects have never been better.

In a nation with so many development challenges and such porous data, it is difficult to identify future scenarios, let alone determine which is most likely. How does one define a failed state in Papua New Guinea, where most of the nation is not dependent on a properly functioning state? Without accurate data, how can one track trends in human development over decades? Should the focus be placed on the country as a whole, or on urban areas, on rural areas, or areas critical for economic development? How can new technological advancements be appropriately accounted for?

Drawing on the papers in this series, five variables from each of the sectors addressed in the papers have been identified as critical influences on PNG's development over the next ten years and beyond. From these variables, three potential scenarios emerge, with the most likely scenario that Papua New Guinea will continue to 'muddle through' as it has in the past, failing to meet many expectations of development but defying the country's many detractors, and avoiding state failure.

## RECAP OF PAPUA NEW GUINEA'S DEVELOPMENT CHALLENGES

Papua New Guinea, with its vast endowment of resources and young population, should be looking forward to increasing the living standards of its people over the long term. But current trends, many of which are mutually enforcing, are tempering optimism about the nation's short-, medium- and long-term prospects.

Bal Kama discusses the state of **politics** in his paper, arguing that the country's recent political stability has come at the cost of weakened legislative authority of the parliament. This has been exacerbated by the government's moves to control critical electoral funding (through the District Service Improvement Program and Provincial Service Improvement Program), thereby controlling MPs' behaviour. While the legal system remains robust, cracks are appearing as the system suffers under the strain of one of the most litigious societies in the world. Kama foresees a growing political dysfunction, intensified by a marginalisation of the traditional bureaucracy. The results of the 2017 election indicate a rising regional factionalisation among the political elite that could further complicate a messy process of decentralisation.

Jonathan Pryke and Paul Barker discuss the bumpy road of progress in Papua New Guinean **society**. On many indicators, PNG's rapid population growth is outpacing development progress and service delivery is struggling to keep up. Growing urbanisation is increasing the burden on service providers. More than 40 per cent of the population is under the age of 14 and soon to enter an already underemployed workforce. Women are severely marginalised. The small formal sector is growing, but its employment needs are not being met because the domestic workforce is underskilled. Without significant investment and smart policy implementation focused on developing the human capital of Papua New Guinea, future generations lack opportunities and will be further marginalised. The country has some policies and legislation in place to turn things around, but resources and implementation have been lacking.

Sinclair Dinnen discusses **internal security** trends and prospects, outlining the prevalence of crime and interpersonal violence, corruption, illegal firearms, resource poaching, and transnational crime. While the drivers of these problems are complex and multidimensional, they are being exacerbated by the neglect and politicisation of the PNG police force. Ineffective public policing and widespread insecurity have spurred rapid growth of the private security sector, which now outnumbered police 3:1. The expansion of private security forces threatens to further undermine investment in public security, but may prompt government to engage in security governance in a more holistic way.

A collection of experts, led by David Osborne, examines the current state of PNG's **economy**. Their paper provides an assessment of macroeconomic stability, and an assessment of fiscal policy and debt. On macroeconomic stability, the authors chart the deterioration of PNG's monetary situation and argue for greater exchange rate flexibility to restore equilibrium and investor confidence. On fiscal policy and debt, revenue and expenditure volatility, combined with revenue leakage, has been a critical destabiliser for effective planning and expenditure. The chances of debt distress are currently low but of growing concern.

Craig Lawrence provides an overview of the state of **infrastructure** in Papua New Guinea, focusing on telecommunications, transport, energy, and urban water. He argues that the physical stock of infrastructure assets in Papua New Guinea is insufficient to deliver the economic and social services needed to drive faster economic growth and improve human development. Effective national infrastructure planning and funding, and the role of the Independent Consumer and Competition Commission, will be critical for infrastructure improvement in the years ahead.

Finally, Jenny Hayward-Jones discusses the changing nature of **geopolitics** in Papua New Guinea. Acknowledging that geopolitics in the Pacific are typically benign, she argues that this is beginning to change with the emergence of China as a growing power in the region. Meanwhile, the PNG government is financially constrained and focused on domestic challenges, and its ability to manage a range of existing and foreign interests is very limited. The APEC Leaders' Summit in 2018 does provide an opportunity to market the economic potential of the nation, but could damage PNG's international reputation if not managed effectively. Australia will assist with this, but will need to work harder to maintain its legitimacy as PNG's closest partner.

All of these papers highlight a great number of challenges, as well as opportunities, for Papua New Guinea over the next decade. The government, and other actors in Papua New Guinea, will not be able to address them all. Some variables will also have more of an impact than others on PNG's future.

## **DETERMINING CRITICAL VARIABLES FOR THE NEXT 10 YEARS**

In order to determine the critical variables that will affect Papua New Guinea over the next decade, the Lowy Institute convened a workshop with 20 stakeholders from academia, civil society, the private sector and government in Port Moresby in August 2017. Stakeholders discussed the six papers prepared as part of the program and debated the importance of each variable. The following matrix of variables was the product of this process.



**Table 1: Matrix of key variables**

Politics	Society	Economics
1. Centralisation of power	1. Service delivery	1. Managing fiscal/debt
2. Decentralisation of process	2. Demographics	2. Monetary stability
3. Independent and accountable institutions	3. National identity	3. Regulatory framework and predictability
4. Legislative compliance and enforcement	4. Livelihoods	4. Linkages/coordination
5. Civil society/ social media	5. Gender inclusivity	5. Wealth transfer
6. Human capacity		
Infrastructure	Security	Geopolitics
1. Infrastructure management	1. Quality of police force	1. Growing influence of Asia
2. Maintenance	2. Private security	2. Role of multinationals
3. Funding	3. Tribal conflict	3. Australia–PNG relationship
4. Politicisation	4. Decentralisation of security	4. APEC 2018
5. Responsibility	5. Transnational crime	5. Interpersonal relationships

*Note: Society generated an extra variable because participants could not agree on which one should be removed.*

After identifying this matrix of variables, workshop participants engaged in a process to determine a hierarchy of importance. A voting system identified the top 10 variables overall, and further deliberation produced a hierarchy.<sup>5</sup>

This hierarchy incorporates significant bias. Some participants are subject matter experts in certain fields (i.e. infrastructure), potentially skewing their perspectives. The sample size of participants was small, and oriented towards professionals and the private sector. The workshop did not have gender parity nor equal Papua New Guinean representation. These limitations aside, the exercise remains a useful tool for cutting through the swathe of possible challenges in order to identify what variables are most critical.



**Table 2: Hierarchy of key variables**

	Variable	Sector	Vote share
1	<b>Human capacity</b> Diminishing quality of education and health services in PNG is reducing the country's capacity to provide human capital to fill both private and public sector workforce needs and to deliver employment opportunities for a growing and increasingly urban population.	Society	21%
2	<b>Independent and accountable institutions</b> Independent institutions face the significant threat of politicisation or marginalisation. Many institutions are also not being held accountable for their mandated responsibilities.	Politics	14%
3	<b>Infrastructure management</b> Infrastructure investment routinely takes place outside of planning, against predetermined priorities and without proper cost-benefit analysis. The build-neglect-replace paradigm also needs to be broken.	Infrastructure	14%
4	<b>Legislative compliance and enforcement</b> The legislative environment in PNG is sound; what is needed is further compliance and enforcement. Enforcement agencies face regular budget cuts instead of further support. Those companies that do comply are often further penalised for quick-fix revenue collection purposes, disincentivising future compliance.	Politics	12%
5	<b>Managing fiscal/debt</b> The volatility of the country's revenue and expenditure, combined with revenue collection, is severely destabilising. Deficits cannot readily be funded and debt is rising.	Economy	11%
6	<b>Regulatory framework and predictability</b> Components of new legislative proposals (i.e. SME and land policies) threaten to undermine already weak business sentiment and further reduce incentives for foreign investment. They lack appropriate stakeholder consultation.	Economy	8%
7	<b>Gender inclusivity</b> From violence in the household to exclusion from the workforce, gender inequality is perhaps the single largest societal development challenge in Papua New Guinea.	Society	7%

	Variable	Sector	Vote share
8	<b>Service delivery</b> Health and education services across the country are in retreat from a mixture of funding availability, a breakdown in infrastructure, declining governance capabilities and quality of service delivery practitioners.	Society	5%
9	<b>Wealth transfer</b> Papua New Guinea is becoming an increasingly unequal society. The country has not figured out how to transfer the benefits of vast natural resource wealth and exploitation to the broader population.	Economy	5%
10	<b>Quality of police force</b> The Royal Papua New Guinea Constabulary (RPNGC) has been neglected for years, with inadequate numbers and resources, low morale, serious discipline problems, and increasing levels of internal factionalisation.	Security	5%

This hierarchy of variables is telling. No geopolitical variables appear in the top 10. Only one variable from both infrastructure and security qualify. The critical issues which have been identified are largely concentrated in the political, societal, and economic sectors. Over 70 per cent of total votes were concentrated in the top five results, illustrating the dominance of these five variables, according to participants' assessments.

## SCENARIOS

The way these five variables change over the coming decade will underpin the three scenarios identified in this paper. These work on the assumption that other external factors, or one-off events (such as APEC or the looming Bougainville referendum), will not cause significant disruption to the trends that have been established in Papua New Guinea and identified by the papers in this series.

### 1. GRADUAL IMPROVEMENT

Under this scenario, the government will focus considerable effort on improving the quality of service delivery and investing significantly in human capacity development. It will do this by reinvigorating TVET (technical, vocational education training), tertiary institutions, and teacher training facilities. Evidence of improvement will be a growing number of tertiary enrolments aligned to workforce demand, a gradual reduction in demand for foreign workers, and better results in business workforce surveys. Investment in human capacity is multi-generational, and the impact of these investments will only begin to appear in a decade's time.

More immediately noticeable will be the government's renewed commitment to the independence of key institutions and the bureaucracy. Institutions such as the Bank of

Papua New Guinea, the Ombudsman Commission, the public prosecutor, the Independent Consumer and Competition Commission, the Auditor General, and the newly established Independent Commission Against Corruption will all have their independence reinforced and funding expanded. State-owned enterprises and government trusts will be made much more accountable by requirements to publish their performance through independently audited annual accounts.

At the same time the government will focus on implementing recent reviews on tax, decentralisation, and elements of the proposed small and medium enterprise policy. It will significantly empower the Internal Revenue Commission through additional funding and donor cooperation to both broaden the tax base and stop revenue leakage, resulting in the revenue to GDP ratio improving towards the historical average of 32 per cent.

Infrastructure investment and maintenance will be streamlined and made far more accountable and transparent. Investments will be driven by the National Transport Strategy, the Department of Works, the National Road Authority and the Infrastructure Development Authority with minimal political interference. Critical new infrastructure (such as a new fibre-optic cable) will be secured with concessional finance through the support of multilateral donors. Funding of maintenance will be prioritised over new investments.

All of this will be made possible by a significant shift in fiscal policy. The International Monetary Fund will be invited by the government to help accelerate reform and provide finance for the budget deficit and new funding priorities. Decentralisation will need to be slowed to give the government flexibility for investments in human capital and independent institutions. Excluding critical government commitments, such as APEC, the Bougainville referendum, and the 2022 election, no new major funding announcements will be made. The Sovereign Wealth Fund will be implemented and, once PNG LNG assets have been fully depreciated and LNG-collateralised debt is repaid, revenue from the natural resource sector will flow through it in an open and transparent manner, rather than through state-owned enterprises.

All of this demands a great deal from a government that has already spent five years in power and, beyond their Deputy Prime Minister's bold 100-day plan, shown little appetite for a course correction. While all observers of Papua New Guinea should remain hopeful that this scenario will come to pass, it remains unlikely.

## 2. MUDDLING THROUGH

Under this scenario, the course of government policy will continue much as it has over the past decade. The government will remain committed to its Tuition Fee Free education and free health policies, at the expense of quality service delivery. Tertiary and TVET institutions will continue to be neglected. There will be progress in some areas, such as student enrolments, but decline in others, such as availability of medicines. The private sector workforce will continue to be supplemented by foreign workers, and labour demands will remain relatively consistent.

Key institutions will remain marginalised or politicised, with the government preferring to operate through decentralised mechanisms of government. Some public sector reform measures will be implemented, but key agencies will still not receive adequate support.

State-owned enterprises will continue to operate with opacity and impunity. There will be tokenistic efforts to curb corruption. The state will continue to function, but the quality and performance of institutions will not improve.

The government will make little progress in implementing recent reviews effectively, and will instead focus its energy on new reviews and legislation that are also unlikely to be implemented. The Internal Revenue Commission will not succeed in broadening the tax base, and compliant businesses will be put under further pressure to help finance the government's dire fiscal position.

Infrastructure investment will continue to be determined by political actors, and will largely be focused on Port Moresby. Critical infrastructure will be allowed to continue to deteriorate, and the government will allocate most new spending to projects of largesse rather than necessity. Maintenance will remain underfunded. Donors and multilateral banks will help plug the gap.

Fiscal policy will continue much as it has over the past decade. The government will set far too generous revenue expectations each year, and when they fail to eventuate it will react by reducing the budgets to core services while protecting key initiatives such as decentralisation and Tuition Fee Free. Revenue and expenditure will continue their extreme volatility, undermining decision-making and national investment strategies. Supplementary budgets will become routine, and cash shortages as a result of un-financeable deficits will be the norm.

Some may look at this scenario and assess it as being a 'muddle down' rather than a 'muddle through'. It is certainly messy, but will not result in the collapse of any critical component of the state or affect the ability of business to effectively operate in Papua New Guinea. It is also the most likely scenario.

### 3. ACCELERATED DECLINE

Under this scenario, government policy will become more regressive, and institutions, the bureaucracy and broader service delivery will start to crack under the strain. The public health and education system will rapidly deteriorate. Teachers will stop showing up to work, and health clinics will close. The elite will rely more heavily on private institutions, and inequality will grow. TVET and tertiary institutions will fall into complete disrepair, and enrolment numbers will drop. Workforce demands will continue to be met by foreign workers. Inequality will accelerate, creating significant social tension.

Institutions will remain marginalised or politicised. More expenditure decisions will be made outside the budget decision-making process and through state-owned enterprises. Decentralisation will accelerate, with more funding channelled through mechanisms that lack accountability or transparency. Crucial independent agencies will see routine funding cuts, and will stop functioning. Elite capture of institutions will result in many not operating, and others operating with impunity.

As a result, corruption will increase. Compliant companies will be exploited to a degree that many foreign companies will start to leave, and foreign investment will shrink. Companies with more dubious reputations will remain, operating with impunity because of their collusion with

the political elite. The government will react to their shrinking revenue base by implementing nationalistic policies that will further restrict the appetite for foreign investment.

Infrastructure investments will become completely captured by political interests. The private sector will be expected to take a larger role in meeting their infrastructure needs. Critical public infrastructure, such as power, telecommunications and road networks, will begin to fail. The government will look to finance its opaque decision-making through dubious loans with questionable rates of interest. Maintenance will be completely disregarded.

Fiscal policy will become even more erratic. Revenue targets will become ever more ambitious, while expenditure will be further allocated towards big-ticket items. More expenditure will be funnelled out of the budget process. Supplementary budgets will not be introduced or followed. Expenditure will become driven by cash on hand and the priority of the day. New mechanisms of expenditure will be created that lack transparency and accountability, enabling further elite capture of the budget process.

Under this scenario, in a decade's time the PNG state will be seen as barely functioning. Completely captured by elites, expenditure and decision-making will not align with the needs of the people. The country will regress on numerous development indicators, and civil unrest will rise. More observers will start calling Papua New Guinea a failed state. But even under this scenario it is likely that major enterprise, particularly the natural resource sector, will still be able to operate.

## SUMMING UP

Papua New Guinea's future prospects are driven by a large array of variables that are mutually enforcing. While the scenarios outlined above draw on assumptions about how key variables may change, there are many other variables that will no doubt affect the nation over the next decade.

In addition, there are a number of critical events (internal and external) in the coming years that could have as much impact, if not more, than any one of the variables identified in this paper. The APEC Leaders' Summit could see a significant boost for the country if it is a success, or could be a national embarrassment and scare off future investment if it fails. The Bougainville referendum in 2019 has significant potential to lead to major civil unrest. A constitutional crisis, public servants not being paid, a natural disaster, major riots in Port Moresby, or any other unpredictable crisis could be equally destabilising. The next national elections in 2022 will need to be effectively managed to assuage unease about the process in 2017. Finally, another major natural resource investment may completely change any future scenario for the country, at least in the short-term.

It is for all of these reasons that predicting future scenarios for Papua New Guinea is a fraught business. While this paper has attempted to put some rigour around the exercise, the progress of development will always be complex and unpredictable in a country such as Papua New Guinea with so many mutually enforcing challenges. The most likely scenario is that the nation will continue to muddle through, drawing on the resilience and entrepreneurialism of its people. It is unlikely to collapse, but is also unlikely to find a sure footing. Given time, it may slowly mature and find a stable development pathway, but this will take generations.

## ENDNOTES

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- 5 For example, a participant could allocate ten votes to human capacity. Another participant could choose to allocate five to infrastructure management and another five to managing fiscal/debt. Another participant could choose to allocate a single vote to ten different variables.





## ABOUT THE AUTHORS

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