



PACIFIC ECONOMIC AND MARKET INSIGHTS

December 2022 Quarter

Key trends at a glance

GLOBAL ECONOMY SLOWS DOWN



- Global inflation was 8.8% in 2022 and is expected to slow to 6.5% in 2023. In 2023, advanced and developing economies' inflation rates are projected at 4.4% and 8.1% respectively.
- Global GDP growth is expected to slow significantly from 2.9% in 2022, to 1.7% in 2023. Monetary policy action is a key factor in determining global output.
- Factors stemming from the Russia-Ukraine conflict are expected to stifle growth in 2023, as central banks look to balance fighting inflation without tipping their economies into recession.



COMMODITIES PRICE TRENDS



- Energy prices fell sharply in Q4-22 as global inflationary pressures subside and growth falters.
- Precious metals inched higher as a response to a lower USD as the US Fed slowed the pace of interest rate hikes in Dec-22.
- Coffee and palm oil prices were lower in Q4-22, driven by an expected record coffee yield in Brazil and high palm oil inventories.
- Nickel prices are still extremely volatile, following the historic surge in March, with small shifts in supply and demand sparking large price movements as seen in late 2022.



PNG BOOSTED BY RESOURCE PRICES



- PNG's 2022 GDP growth increased to 4.6% from 0.1% in 2021, due to higher oil and gas production, as developers sought to capitalise on higher prices. Production is expected to normalise in 2023, leading to lower growth of 4.0%.
- Non-resource GDP growth is estimated at 4.5% in 2022, and 4.6% projected for 2023. Resource sector GDP growth in 2023 is projected at 1.2%.
- There is some upside with project negotiations expected to reach successful conclusions in 2023 and 2024. Reports indicate groundwork is being initiated by developers in anticipation.
- Headline inflation was estimated at 6.3% for the 2022 September quarter and is expected to reach 6.6% for the year.
- Inflation throughout the year was driven largely by imported inflation for crude oil and consumables. Given PNG's reliance on imports, the country was prone to the effects of heightened global inflation.
- BPNG is expected to maintain its contractionary stance on monetary policy through 2023, as inflation persists.
- The Kina Facility Rate was increased from 3.25% in July 2022 to 3.5% in January 2023. The Cash Reserve Requirement has also been increased steadily and is currently at 10%.



ECONOMIC GROWTH FOR THE SOUTH PACIFIC

- South Pacific countries' 2022 economic growth was estimated to be 5.3%, mainly driven by growth in PNG's mineral sector and Fiji's tourism sector.
- Samoa and Solomon Islands were impacted by lingering COVID-19 effects, resulting in negative growth in 2022.
- In 2023, all Pacific economies are expected to post positive GDP growth, with regional growth of 4.8% as the recovery in some countries stabilises.

REAL GDP GROWTH

	2021	2022	2023
	-4.1%	+14.5%	+5.6%
	-0.5%	-4.2%	+3.0%
	-7.1%	-6.0%	+2.0%
	-2.7%	-2.2%	+2.5%
	+1.0%	+2.0%	+4.0%
	-29.1%	+10.5%	+11.2%

Source: ADB December 2022 Economic Forecasts.

BSP's economic and market views



Ronesh Dayal

Acting Group Chief Executive Officer

What were the key operational highlights for the Group in 2022?

- *Through the course of the year, and with the reopening of borders across the Pacific, we have seen marked improvement in economic activity across the Group compared to the COVID-19 period. ADB projects economic growth at 5.3% for the Pacific in 2022, which will serve as a platform for further growth in 2023.*
- *BSP saw high demand for cash during the PNG election period, as campaign-related spending progressed in the lead up and during the elections. Our staff were able to meet this surge in demand and deliver to customers across the country throughout this period.*

How will the increase in Bank Income Tax rates to 45% affect the banking sector?

- *We appreciate the fiscal mandate to raise revenue in order to progress the development of the country. As a Group, BSP is committed to supporting the economic growth and success of all the markets in which we operate.*
- *Differentiated industry corporate income tax rates can be particularly damaging for emerging economies such as PNG. Such tax policies are detrimental to the proper functioning of market forces and conflicts with modern economic theory.*
- *Further, the tax rate increase on commercial banks comes at a time when locally-grown financial institutions are looking to obtain commercial banking licenses. The timing is unfortunate, and will nullify any momentum towards the expansion of the financial sector and investment (new branches and digital offerings) in PNG.*

What were the key economic highlights of 2022, and what can we expect in 2023?

- *In the medium-to-long term, the government stated commitment to supporting agriculture outputs and attracting foreign direct investment (FDI) bodes well for PNG's economic prospects in 2023. However, in early 2023 we need to see tangible FDI commitments particularly from the extractives sector before we see PNG's economic recovery commence.*
- *In short, the progression of the key extractive projects, as well as the re-opening of Porgera, are needed to boost business sentiment and expenditure that will underpin economic growth in 2023 and into 2024.*
- *The Bank of Papua New Guinea (BPNG) has adopted a contractionary stance to monetary policy, in response to high inflation. BPNG has increased the Kina Facility Rate (KFR) from 3.25% in July 2022 to 3.50% in January 2023. The Cash Reserve Requirement (CRR) has been increased through a series of hikes as well, from 7% in June 2022 to 10% by year end. We expect that BPNG will maintain the contractionary stance throughout 2023.*
- *The increases in the KFR and CRR have the intended effect of restricting lending to reduce spending in the economy, thereby addressing inflation. Increasing these rates also has the effect of cooling the PNG economy and subdues growth.*

BSP's economic and market views



Peter Beswick

Group General Manager – Corporate Bank

Do you have any concerns regarding inflation?

- *Inflation remains the primary concern for the Bank of PNG (BPNG), businesses and consumers. BPNG increased the Cash Reserve Requirement (CRR) to reduce market liquidity on 12 December 2022, as a further measure to counter imported inflation BPNG signaled a further increase in interest rates with its third lift in the Kina Facility Rate by 25 basis points on 3 January 2023. This is likely to dampen investment and consumer spending.*
- *Strong demand and ongoing supply issues, continue to boost goods price inflation. Key inflation drivers remain unchanged with elevated price levels ascribed to supply-chain disruptions, logistics costs and fuel prices.*
- *Foreign currency reserves have hit multi-year highs at USD3.6 billion, delivering strong coverage for government foreign currency loan repayment obligations and BPNG intervention for importers throughout 2023.*

What recent trends have you seen in business confidence?

- *Business and consumer confidence continues to lift through Q4, with anecdotal evidence across a broad section of our retailers who experienced record pre and post Christmas sales activity.*
- *Increased business and leisure travel has seen hotel occupancies reach pre-COVID levels, with many facilities at near full occupancy and our customers are projecting this demand momentum to continue throughout 2023.*
- *Papua LNG is “go” with FID expected in late 2023 and this will deliver significant opportunities through Local Content for Landowner and PNG companies ... either directly or through JVs, with global engineering procurement and construction contractors. At end 2022, five large tender packages were released to the market in the lead-up to FID. Papua LNG, Government infrastructure projects (ports and roads) plus our delayed resource opportunities (Porgera, Wafi-Golpu, P’nyang, Twinza) are leading multiple customers to build people and resource capacity.*
- *Globally, there is a shortage of skilled and unskilled labour and our customers are focusing on looking after their best people, with retention strategies now critical.*



Rohan George

Group General Manager – Treasury

How was foreign exchange liquidity and the Kina in the Final Quarter of 2022?

- *FX market turnover in the December quarter rose 2% from the September quarter 2022. FX turnover for 2022 increased by 17.3%, compared to the prior year. This was supported by strong commodity prices, in particular Oil, Copper, Palm Oil, and Coffee. Firmer commodity prices assisted to offset the lost FX inflows from the closure of the Porgera gold mine.*
- *Outstanding FX orders with BSP fell by 70% in the past quarter, with large end of year FX inflows and Central Bank interventions more than offsetting large crude oil imports and pre-Christmas stocking.*
- *BPNG FX intervention in the December quarter 2022 rose 51% compared to September quarter.*
- *The Kina mid-rate was stable against the U.S. dollar at 0.2840. Recessionary fears amid a tightening of monetary policy in Australia and widening unfavorable interest rate differentials, weakened the Australian dollar early in the quarter, but it rebounded at years end, and remained broadly unchanged over the quarter.*
- *BPNG raised the CRR of commercial banks to 10% of total deposits, a tightening monetary policy to combat inflation, with the intent of reduced system liquidity, higher interest rates and reduced demand.*

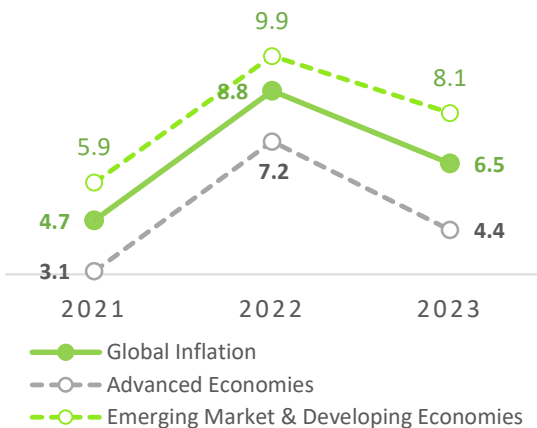
What's the outlook for FX inflows for the upcoming quarter and how should Corporate and Retail customers manage volatility in foreign currency inflows?

- *After strong FX inflows in the December quarter, we expect post-Christmas import orders to increase in January and February, with FX inflows gaining momentum into the end of March.*
- *To manage volatility in foreign currency flows, businesses should place FX orders (with correct documentation), as soon as possible, ensure orders are cash backed whilst awaiting execution, tax clearance certificates are current and reflect the expected FX order execution time.*

Global growth outlook

Fighting inflation will be the main concern for monetary authorities around the globe, and it is expected that global inflation will ease in 2023. However, cooling inflation also has the added effect of stifling economic growth, leading to lower projected global output in 2023.

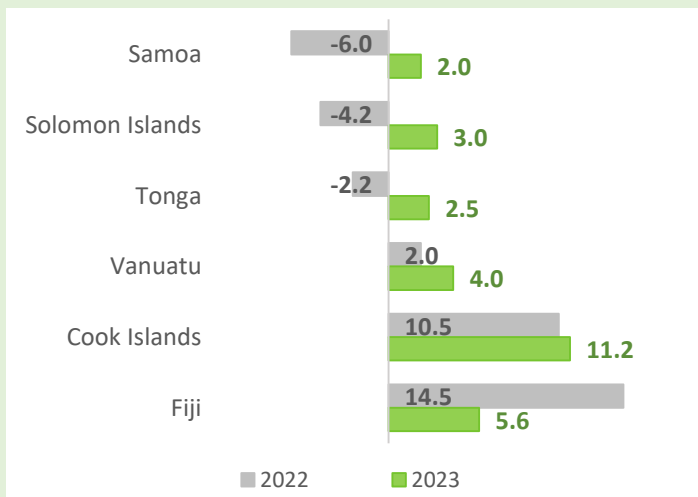
GLOBAL INFLATION (%)



GLOBAL GDP GROWTH (%)



PACIFIC GDP GROWTH (%)



- Global inflation is estimated to be 8.8% in 2022, with the developing world being affected most due to being largely net importers. In 2023, advanced and developing economies' inflation rates are projected at 4.4% and 8.1% respectively.
- Real Global GDP growth is expected to slow significantly from 2.9% in 2022 to 1.7% in 2023. It is expected that inflation-fighting measures will continue in major economies, which will see global economic activity slow down in 2023.
- Advanced economies are expected to slow down more than developing economies in 2023, with 0.5% and 3.4% growth projected respectively.

- Natural disaster incidents and lingering COVID-19 effects in early 2022, posed some downside risk. However, through the course of the year, and with the reopening of borders, there has been a marked improvement in economic activity across the Pacific.
- The Asian Development Bank projects economic growth at 5.3% for the Pacific in 2022, which will serve as a platform for further growth in 2023. All Pacific economies are expected to post positive GDP growth in 2023.

Source: World Bank July GDP forecasts, Euromontor Economic Outlook Q3-2022

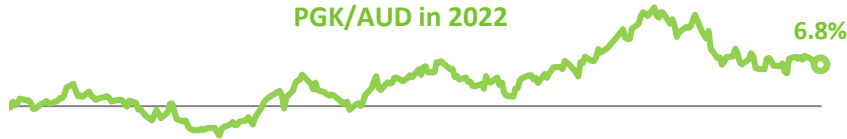
FX markets

The size and speed of the US Federal Reserve’s interest rate hikes, relative other major economies, has caused the USD to strengthen to record highs in 2022. The strengthening of the USD also provides uplift for the PGK, which finished the year stronger against the AUD, NZD, EUR, and other major currencies.

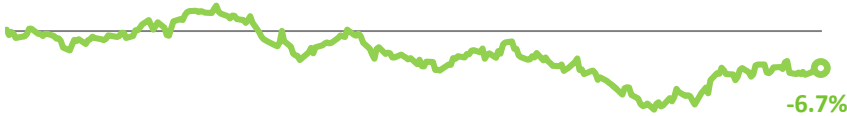
PGK/USD in 2022



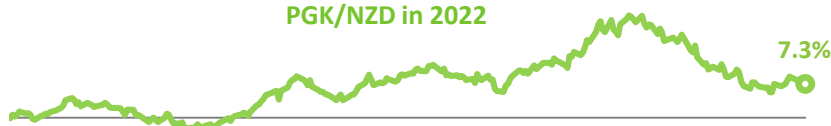
PGK/AUD in 2022



AUD/USD in 2022



PGK/NZD in 2022



NOTES ON CURRENCY MOVEMENTS









- **USD** – Monetary policy action and a flight to quality has aided in strengthening the USD in 2022. The US dollar index finished the year 9.3% stronger against a basket of currencies despite losses in Q4-22. The USD will likely weaken as the Federal Reserve is expected to slow its interest rate hikes in 2023.
- **PGK** – In Q4-22, the PGK/USD reference mid-rate closed at 0.2840, remaining unchanged over the quarter, but showed a 0.4% reduction from the start of 2022. The PGK finished higher in 2022 against major currencies due to the cross currency effect of the strong USD.
- **AUD** – The AUD gained momentum against the USD in Q4-22 and continued making up lost ground into 2023. However, in 2022, the AUD finished 6.7% weaker against the USD and 6.8% weaker against the PGK by extension.
- **NZD** – The NZD made gains against the USD towards the close of Q4-22 similar to the AUD, but finished 6.7% weaker on a year-to-date basis. The PGK was also 7.3% stronger against the NZD at the close of the year.

03-Jan-22 03-Feb-22 03-Mar-22 03-Apr-22 03-May-22 03-Jun-22 03-Jul-22 03-Aug-22 03-Sep-22 03-Oct-22 03-Nov-22 03-Dec-22

Source: Reuters, CNBC, Yahoo! Finance,

Commodity price trends

In Q4, both energy and non-energy prices dropped, as global inflationary pressures subside. Conversely, precious metals inched higher, as a response to a lower USD and the US Fed indicating a potential slowing of its interest rate hiking cycle.

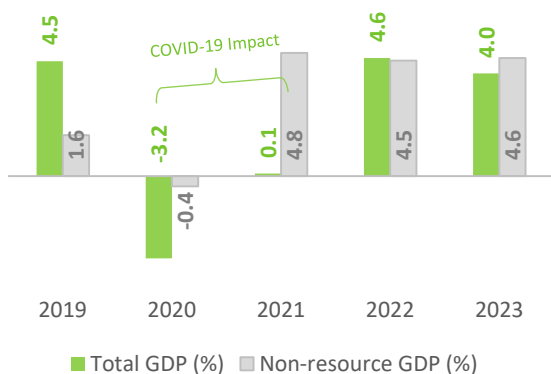
COMMODITY	Q4-2022 (Average price)	Q3-2022 (Average price)	CHANGE (%)	TREND	COMMENTS
Crude Oil, Brent [\$/bbl.]	88.4	99.2	(10.9)		Brent prices continued its downward trend in Q4-22, as global inflation pressures start to ease (particularly in the US) and Russia looks able to continue to sell oil to the Asian market. A rebound of the USD will further weigh on prices.
LNG, Japan [\$/MMBtu]	20.3	21.3	(4.6)		LNG prices fell steadily, due to high LNG inventories in the Northeast Asian region, falling European gas prices and market participants watching the potential impact of a European market correction mechanism.
Gold [\$/troy oz.]	1,729.0	1,726.0	0.2		Gold inched higher in Q4-22, as the US Federal Reserve indicated a potential slowing of its interest rate hiking cycle. The US Federal Reserve outlook nevertheless remains hawkish and continues to weigh on the metal.
Nickel [\$/MT]	25,514.1	22,132.4	15.4		Nickel prices spiked briefly in November, due to a now-refuted report about a blast at a nickel plant in Indonesia. Illiquid trading conditions resulting from the historic surge in March, meaning small shifts in supply and demand can spark large price movements.
Copper [\$/MT]	8,025.5	7,759.6	3.5		In Q4-22, copper began to recover as investors once again flocked to cyclical metals in response to a lower USD and rising prospects for a China reopening. The outlook for copper is mixed with the metal's price dependence on the situation in China.
Palm Oil [\$/MT]	925.0	997.3	(7.2)		Palm Oil prices fell further in Q4-22, despite higher imports from India. This was driven by high inventory levels and steep discounts to rival soy oil and sunflower oil prices.
Arabica Coffee [\$/kg]	4.9	5.8	(16.1)		Arabica Coffee prices were under pressure in Q4-22, on concerns that global economic growth is faltering just as top producer Brazil is expected to produce a record crop.
Cocoa [\$/kg]	2.4	2.3	5.4		Cocoa inched higher, supported by a weaker dollar, robust demand, low inventories, and supply concerns. Cocoa farmers continue to struggle with the lack of fertilizer and pesticides as the war in Ukraine has limited Russian exports of potash and other fertilizers worldwide.

Source: Bloomberg, capital, fxstreet, globallnghub, reuters, tradingeconomics, World Bank

PNG's economic outlook

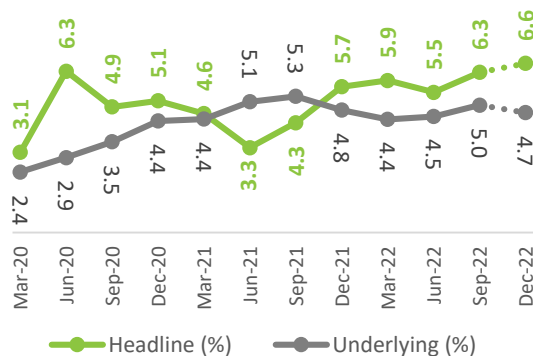
Government support for agriculture outputs and attracting foreign direct investment bodes well for PNG's economic prospects in 2023 including progress towards the re-opening of Porgera Gold Mine, the finalising of Papua LNG, as well as other projects being progressed into 2024.

REAL GDP GROWTH



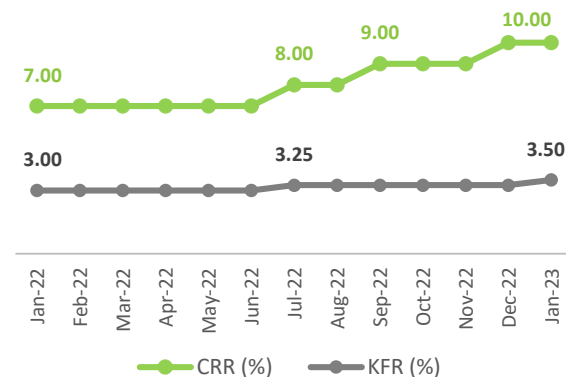
- GDP growth has recovered after the COVID-19 period and is projected at 4.6% in 2022, up from 0.1% the prior year.
- Growth in 2022 was boosted by higher production of oil and gas, as developers sought to capitalise on high prices.
- Non-resource GDP is estimated at 4.5% growth in 2022, and 4.6% projected for 2023. Resource sector GDP growth in 2023 is projected at 1.2%, but there is some upside with project negotiations expected to reach successful conclusions in 2023 and 2024.

INFLATION



- Headline inflation was estimated at 6.3% for the September quarter in 2022 and is expected to reach 6.6% for the year.
- Inflation throughout the year was driven largely by imported inflation for crude oil and consumables. Given PNG's reliance on imports, the country is prone to the effects of heightened global inflation.
- Although global inflation is expected to subside, BPNG expects that external prices will remain elevated and will not immediately lower imported inflation.

MONETARY POLICY



- BPNG is expected to maintain its contractionary stance on monetary policy through 2023, while inflation persists.
- Monetary policy tools like the Kina Facility Rate (KFR) and the Cash Reserve Requirement (CRR) have been used to tighten money supply and combat inflation.
- The KFR was increased from 3.00% to 3.25% in July 2022, then to 3.50% in January 2023.
- The CRR has also been increased steadily in 2022 reaching 10% (pre-COVID levels) by the end of 2022.

Source: BPNG Monetary Statement Sept, 2022, 2023 National Budget, Vol. 1, National Statistics Office Sept-Qtr 2022 CPI Report,

Resource sector updates

Growth in the resource sector was underpinned by a favourable performance in the mining and quarrying sector, which recorded a 13.5 per cent growth in 2022. Major mines such as Ok Tedi, Lihir and Simberi have recovered strongly from production disruptions in 2021.

EXTRACTIVE RESOURCE SECTOR



POGERA MINE

- New Porgera Limited (NPL) was incorporated on 22 September 2022, following execution of the New Porgera Shareholders agreement. The company intends to apply for a new Special Mining Lease (SML) once certain conditions have been met.
- Resumption of the Porgera mine is expected in the second quarter of 2023 (Budget Strategy Paper).

WAFI-GOLPU MINE

- The SML for the K18.5 billion gold-copper Wafi-Golpu project is expected to be executed in early 2023 according to Morobe Governor Luther Wenge.
- The Wafi-Golpu would sustain PNG's copper production in the event that the Ok Tedi mine in Western Province reaches its end-of-life in 2030.

OIL & GAS

- In Q3-22, Kumul Petroleum submitted a binding conditional offer of \$1.4billion to Santos for an additional 5% equity in the PNG LNG project.
- Kumul has paid an amount of \$55million to Santos which is held in escrow to be released for part payment if the deal goes through. Santos has agreed to extend the exclusivity period from Dec 22 to April 23.
- The offer is conditional on Kumul obtaining waivers of certain pre-emptive rights by each of the other PNG LNG project participants.

NON-EXTRACTIVE RESOURCE SECTOR









AGRIBUSINESS

- The Agriculture, Fisheries and Forestry sector, is projected to grow at 2.9 per cent in 2023. This growth would be driven by increased coffee and log production.

Source: 2023 Budget Strategy Paper, Barrick (Niugini) Limited press release, naturalgasworld, The National

South Pacific economic outlook

Economic growth in the Pacific is expected to expand by 5.3% in 2022 and 4.8% in 2023. The brighter outlook in 2022 was driven by stronger-than-expected tourism recovery in Fiji and a combination of election related spending and a recovery in the minerals sector in PNG. All countries are expected to post positive GDP growth in 2023.

REAL GDP GROWTH [%]				
	2021e	2022p	2023p	COMMENTARIES
	-4.1%	+14.5	+5.6%	Real GDP growth for 2022 was adjusted upward to 14.5%, driven by higher-than-expected visitor arrivals from Australia, New Zealand, and North America and aided by streamlined entry requirements into Fiji. The 2023 growth forecast was revised down to 5.6%, as tourism activity is expected to stabilise in 2023 (ADB, December 2022).
	-0.5%	-4.2%	+3.0%	According to the ADB, real GDP is expected to contract by 4.2% in 2022, due to the economic fallout from COVID-19 restrictions ... but rebound by 3.0% in 2023. Recovery will be driven by continued loosening of COVID-19 related social restrictions and a boost to investment as the country hosts the 2023 Pacific Games and donors provide financial support for large-scale infrastructure projects.
	-7.1%	-6.0%	+2.0%	Samoa's GDP contracted by 6.0% in 2022, due to economic impacts of COVID-19 restrictions. Since re-opening its borders on 1 August 2022, domestic activities across all sectors have picked up and the ADB forecasts a return to positive growth in 2023. The CBS confirmed in December 2022 that it will support economic growth by continuing to pursue an expansionary monetary policy.
	-2.7%	-2.2%	+2.5%	The impact of the volcanic eruption in January 2022 has been more severe than expected, downward revisions to the outlook for Tonga in 2022 and 2023 were released by ADB in its December Pacific Economic Update. Growth is expected to decline by 2.2% in 2022 before returning to positive growth of 2.5% in 2023.
	+1.0%	+2.0%	+4.0%	ADB forecast GDP growth of 2.0% in 2022 and 4.0% in 2023. Since opening its international borders on 1 July 2021, Vanuatu has gradually reclaimed about 10% to 11% of its usual tourist numbers from both Australia and New Zealand. Growth in 2023 will also be supported by trade opportunities after the country officially became the 10th member of Pacific Agreement on Closer Economic Relations (Pacer+) in Q4-22.
	-29.1%	+10.5%	+11.2%	Cook Islands real GDP is forecast to grow by 10.5% in 2022 and 11.2% in 2023 (ADB, December 2022). Growth has been driven by a strong recovery in tourism despite reduced flights and seats into the country and New Zealand being their only significant source of business. The announcement of direct flights from Rarotonga to Sydney and Honolulu commencing in May 2023 will provide access to the North American and Australian market and support further economic growth.

Source: ADB Pacific Economic Monitor December 2022; CBS, Fitch solutions, RBV, RNZ

Recovery in the Pacific

All South Pacific countries have reopened their borders to international tourists and are expected to return to positive GDP growth in 2023, despite the gloomy world economic outlook. Tourism recovery, stronger remittances and expansionary monetary policies in the smaller island nations will support growth in 2023.

ECONOMIC OUTLOOK 2023

- The Asian Development Bank projects economic growth at 5.3% for the Pacific in 2022, which will serve as a platform for further growth in 2023. All Pacific economies are expected to post positive GDP growth in 2023.



TOURISM

- Tourism recovery in the Pacific has been uneven in 2022. Fiji and the Cook Islands had stronger-than-expected tourism driven economic growth, while visitor arrivals in Samoa and Tonga in 2022 remained below pre-pandemic levels, by -95% and -91% respectively.



SOCIAL PROTECTION IN THE PACIFIC

- Government expenditure on social protection is variable across the Pacific. Papua New Guinea, Solomon Islands and Vanuatu rely on informal social safety nets.
- Expanding social protection can help address persistent levels of poverty, stimulate inclusive economic development and mitigate the impacts of future economic shocks.



STRONGER REMITTANCES

- Remittances are an important part of household income and informal safety nets in Samoa and Tonga. With the reopening of borders by Samoa and Tonga, labor migration has resumed, bringing with it the opportunity for further remittance growth.



MONETARY POLICY

- While Papua New Guinea continues to tighten monetary policy to curb inflation, other economies like Samoa which contracted in 2022 have prioritized economic growth and will maintain expansionary monetary stances.



INFLATION

- Inflation is forecast to rise steeply, as international prices remain elevated. Smaller island economies account for the biggest upward adjustments with their narrow economic bases and high import dependency, making them particularly sensitive to international price movements.



Source: ADB PEM report December 2022, CBS

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