1. Overview of the Papuan New Guinean Economy

Papua New Guinea (PNG) is richly endowed with natural resources, but exploitation has been hampered by rugged terrain, land tenure issues, and high cost of developing infrastructure. The economy has a small formal sector, focused mainly on the export of those natural resources, and an informal sector, employing the majority of the population. Agriculture provides a subsistence livelihood for 85% of the people. A consortium led by a major American oil company is constructing a liquefied natural gas (LNG) production facility that could begin exporting in 2014. As the largest investment project in the country's history, it has the potential to double GDP in the near-term and triple Papua New Guinea's export revenue.

The trends of GDP and GDP per capita for the last 11 years are shown in Figure 1 and 2:

**Figure 1: PNG GDP Trend 2000-2011**

The difficulties that PNG economy was facing at the beginning of the decade 2000 are reflected in the negative annual % GDP growth (-2.4 in 2000, -0.1 in 2001). From 2003 the GDP has started to grow steadily reaching an annual % growth of 8 in 2010 and 9 in 2011. The economic problems in the early 2000 were due to both internal and external factors such as the outbreak of civil war in Bougainville and the Asian financial crisis. Recovery started in 2003 thanks to the increase of price of the exported commodities, prudent monetary policy and improved fiscal policies.
Labelling PNG as ‘chronically poor’ is a new departure because it was long assumed that the state, even if dysfunctional, was at least developmental. That is, the nation’s capacity to turn profits from agriculture and natural resources into per capita growth was assumed, as was the effectiveness of its larger national development project. But now it is recognised that even as national GDP climbs (mostly a result of increases in resource revenue since 2003) underdevelopment at the national level and poverty at the local level deepen. Indeed, the UN recently classified PNG as a Least Developed Country (LDC), a label the government abhors though it is quite accurate. Concerns about the so-called Dutch Disease are rising against the new LNG project. ‘Dutch Disease’, or the ‘resource curse’, refers to an economic condition where a mineral boom leads to an appreciation of the real exchange rate, which in turn depresses output in the tradable sector. Numerous challenges still face PNG, including providing physical security for foreign investors, regaining investor confidence, restoring integrity to state institutions, promoting economic efficiency by privatizing moribund state institutions, and maintaining good relations with Australia, its former colonial ruler. Other socio-cultural challenges could upend the economy including chronic law and order and land tenure issues. The global financial crisis had little impact because of continued foreign demand for PNG's commodities.

2. Role of Services in the Papua New Guinean Economy

The evolution of the weight of the Services Sector in terms of value added (% GDP) in the PNG economy, with respect to the primary and secondary sectors, is shown in Figure 3.
The unsatisfactory performance of Services is further analysed with Figure 4 showing the annual % growth of Services Value Added. The high volatility that characterized the Services Sector in the first 10 years of 2000 seemed to have stopped in 2009 to settle at a 3% annual growth.

**Figure 4: Services Sector % Annual Growth**

In 2011 the value added as a % of GDP of the Services Sector in PNG didn’t even reach 20% (see Figure 5) much lower than the average for the Least Developed Countries that in 2011 was 48.4%. Among the reasons to explain in the difficult raise of the Services Sector in the country the weak institutional framework, the “Dutch disease” and lack of FDI play, certainly, an important role. It is believed that the Services that could grow more easily in the country and on which it would worthier to invest are the ones related to the exploitation of natural resources such as logistics and transports. Also tourism can be an important driver for the country’s economic growth but its development is at stake because of the unstable political situation. Figure 7, showing the main exported Services, helps understand which are the main Services Sub-Sectors and the most likely to develop thanks to technical assistance.

**Figure 5: PNG Economy Breakdown by sectors**  
**Figure 6: Employment by sector, 2000**

**PNG Economy Breakdown, 2011**

- Industry, value added (% of GDP): 45%
- Agriculture, value added (% of GDP): 36%
- Services, etc., value added (% of GDP): 19%

**Employment by sector, 2000**

- Employment in industry (% of total employment): 25%
- Employment in agriculture (% of total employment): 75%
- Employment in services (% of total employment): 0%

Except the residual category of Government services covering government service transactions (including those of international organizations), the principal exported services are transportation, financial services and construction services. Financial Services are likely to increase given that in 2011 and 2012, the National Parliament passed legislation that created an offshore Sovereign Wealth Fund (SWF) to manage all mineral revenue and put into practice stable public finance management.
3. The role of Foreign Direct Investment

Figure 8: PNG FDI Trend, 2000-2011

After reaching a peak in 2009 (probably due to investments in natural resources exploitation), FDI inflows decreased substantially; the net inflow as % of GDP in 2011 was -2.4. Explanations for these sizable fluctuations have to be sought in the country’s institutional framework and in the degree of openness of the economy. In general East Asia and the Pacific has more restrictions on foreign equity ownership in all sectors than any other region. At the same time, the region displays the greatest intra-regional variance, with less populous economies being more open. For example, Singapore and the Solomon Islands have few restrictions, while China and Indonesia impose foreign equity limits in many service sectors. Papua New Guinea restrictions are tight making it very complicated to start a new business or to hold foreign currency bank account; PNG, in particular, has not ratified the ICSID Convention for Settlement of Investment Disputes and the New York Convention on Recognition and Enforcement of Foreign Arbitral Awards. Papua New Guinea’s economy continues to be “mostly un-free”. Although it has been expanding due to high commodity prices and a construction boom, the prospects for long-term broad-based economic development are constrained by an inefficient legal system and lingering corruption that undercut the rule of law. Much-needed private-sector development is also held back by regulatory deficiencies and the lack of institutionalized open-market policies.

Figure 9 gives an idea of the lack of freedom Papua New Guinean economy suffers from, problem shared with other neighboring economies such as Vanuatu and Solomon Islands.

Source: 2013 Index of Economic Freedom
4. Trade in Services and Trading Partners

The share of Trade in Services for Papua New Guinea is in line with the average for the LDCs, in 2011: 32.35%. In the World Bank Indicator, Trade in Services, both imports and exports are included. A closer look to Papua New Guinea Balance of Payments, in particular for the Services Sector, shows the difficulties that the country is facing in exporting services. The debits exceed the credits for all the 11 years concerned (see Figure 10).

Figure 10: PNG Services Account 2000-2011

Source: Bank of Papua New Guinea

The main PNG trade partners (for goods and services) for 2011 are listed in figure 11

Figure 11: PNG Trade Partners, 2011

Source: EC Trade Statistics

5. Regional Integration

Like other countries, PNG has also stepped up policy processes, in particular trade policy, to measure up and take advantage of the merits of regional integration agreements and globalization.
PNG must keep on playing an active part in helping to shape—and in turn display respect for—developing global institutions and agreements in areas such as market liberalization, promoting sustainable use of the natural environment and human rights.

Over the years PNG has announced bold foreign policy initiatives such “Looked North” and “Work the Pacific” or gave priority to “Reinforcing Core Relationships” and make sure that such bold commitments produce real tangible results. This is encompassing stance that PNG has also embraced in relationships pertaining to economic cooperation. In particular, and more recently, PNG plays a more leading and prominent role in arrangements of political and economic cooperation the in the Pacific region.

One such very important initiative is the **Pacific Plan for Strengthening Regional Cooperation and Integration** of 2004 with the following priority goals—economic growth, sustainable development, good governance and security. Specifically, strengthening regional cooperation and integration should result in: increasing the levels of sustainable returns to the Pacific, ensuring the successful implementation of regional cooperation at national levels, meeting common responsibilities and providing services cost-effectively and developing partnerships with neighbors and beyond.

PNG’s trade relation with Australia, its major trading partner, is canvassed by the **South Pacific Regional Trade and Economic Co-operation (SPARTECA)** and with the other Pacific States by **The Pacific Islands Countries Agreement (PICTA)** and **Pacific Agreement on Closer Economic Relations (PACER)**. PACER is inclusive of Australia and New Zealand whereas the former is purely Pacific Island States.

PNG has **observer status on ASEAN**.

### 6. Institutional Framework

**PNG Department of Commerce and Industry**

The Department of Commerce and Industry was enacted to guide Papua New Guinea to maximize its potential in commerce and industry for achieving sustainable growth, employment creation and income earning opportunities through increased participation in the global trade and investment process.

The Department has the following functional responsibilities within the confines of the Mission Statement:

- Plan, research, formulate and co-ordinate policies and programs relevant to the development of trade, industry, commerce and investment that will guide PNG to diversify its economic base and tap into new markets for its local products
- Review and introduce appropriate policy options for the facilitation of trade, investment and industry development, including rural sector development
- Ensure that Government policies and programs tasked to the respective implementation agencies (IPA, SBDC, ICDC, NISIT) within the Ministry are implemented
- Formulate and monitor appropriate policies to assist in mobilising local landowner groups to fully participate in spin-off activities and related large commercial and industrial projects
- Play a leading role in the coordination and approval processes of major downstream processing and other industrial projects
- Facilitate the expansion of a strong industrial base through an integrated manufacturing and marketing process
- Provide business and industry extension and support services to rural communities & industries
- Pursue policy options with other line agencies to improve PNG’s trade advantage through international establishments in the likes of the Asia Pacific Economic
PNG Chamber of Commerce and Industry (PNGCCI)

Papua New Guinea Chamber of Commerce and Industry (PNGCCI) is a non-stock, non-profit, and non-government organization that plays an important role as representative, voice of the business communities in the country, by providing a unified approach to Government and other associations.

Its objectives:

- To serve as the voice of PNG business and be an independent forum for the development of a consensus among the business community on matters of national concern.
- To initiate, submit recommendations and assist in the formulation, development, implementation and evaluation of plans, policies, programs, and all other activities that will promote the interest of private business.
- To enhance the country's role and status in the community of nations.
- To establish and maintain linkages with global organizations representing agriculture, commerce and industry.
- To act as primary liaison and channel of communication between business and government on matters and issues of interest to both.

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