



WMRC Country Report: Papua New Guinea

19 December 2003

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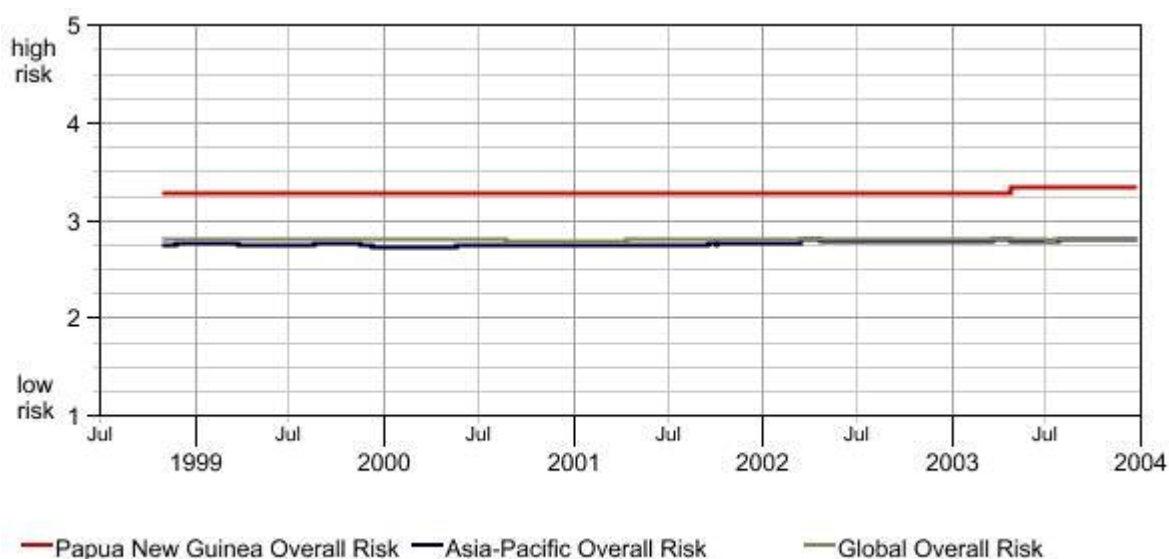
Overall

Papua New Guinea - Country Risk Summary

Nature of risk	Rating	Summary
Political risks	3.50	<p>The political environment is volatile, though the election of Sir Michael Somare in July 2002 should ensure a period of relative stability, as he is essentially ensured a full five-year term. Former Prime Minister Sir Mekere Morauta passed numerous political and economic reforms, and made substantial process in a long-stalled privatisation process, winning the support of donors and many investors in the country. However, the general election of 2002 returned the National Alliance to power, replacing Morauta with Somare. Despite public opposition to reform, the government is essentially bankrupt, and realistically will have to comply with donors' requests if it is to continue to finance its budget. Furthermore, it will probably have to implement economic reforms that will prove unpopular with the electorate. The breakaway province of Bougainville, although currently peaceful due to the presence of international observers, remains volatile as one of the more powerful rebel leaders refuses to disarm.</p>
Economic risks	3.50	<p>Papua New Guinea increased its average annual gross domestic product (GDP) growth from 1.9% in the 1980s to 4.5% in the 1990s through raised exports from the principal mineral sector. Papua New Guinea's economy is vulnerable, however, having neared collapse in 1999. Policy mismanagement in the 1990s led to a string of growing budget deficits, soaring public debt and a sharp collapse in the currency. The Morauta government showed a more responsible fiscal attitude and adhered to a structural programme laid down by multilaterals. Its successor, elected in July 2002, is slowly proving its economic credentials, despite early fears regarding economic mismanagement. Repayment of debt is a budgetary priority, and the government has plans to privatise a range of loss-making industries. However, external circumstances have conspired to undermine growth. Over the longer term, the country is overly dependent upon commodity exports, leaving it vulnerable to fluctuations in global commodity prices. Declining output from the mining sector is a major worry, as old projects reach the end of their lifespan and new ones fail to emerge to replace them. As such, in the medium-term, the government will have to adjust the economy to counter the declining minerals sector, while trying to buoy growth prospects and restore public confidence</p>
Legal risks	2.75	<p>Papua New Guinea places a number of restrictions on the type of business in which foreigners can engage. Nevertheless, the legal and judicial system works reasonably well.</p>
Tax risks	2.50	<p>Corporate tax rates are high, although the government does offer a</p>

		number of tax incentives to investors. There is a lack of experienced tax officials.
Operational risks	3.50	Official government policy towards foreign investment is welcoming. Nevertheless, major projects are often stalled by problems with approval at high levels. The bureaucracy is cumbersome, and corruption is on the increase. Land-owner disputes can cause particular headaches.
Security risks	4.25	Papua New Guinea suffers from chronic law-and-order difficulties, making the country an extremely dangerous place in which to operate. Crime in the cities is rampant and is generally accompanied by high levels of gratuitous violence. Law and order in the countryside is enforced only loosely, with certain regions in the Highlands bordering on anarchic. Violence in the Southern Highlands during the 2002 election campaign proved so endemic that many seats were unable to return a candidate. Secessionist activity has decreased in recent years; a peace process has been firmly established on the island of Bougainville, where most separatist activity was concentrated. Indonesian West Papua's insurgency continues to pose problems on the western border.
Overall risks	3.35 SIGNIFICANT	Papua New Guinea is very politically unstable. This factor, combined with the extremely risky security situation, has deterred most investors from locating there, save those in the mining industry. A particularly worrying development is the emergence of land-owner disputes, which, combined with the cumbersome bureaucracy, can slow down operations. The tax and legal systems require further development.

Comparative Historical Risk



Risk Change History

Papua New Guinea

	Overall Risk		Date Changed	Risk Change Article	Pol 25%	Eco 25%	Leg 15%	Tax 15%	Ope 10%	Sec 10%
1	3.29	SIGNIFICANT	01-Nov-98	-	3.50	3.50	2.50	2.50	3.50	4.00
2	3.35	SIGNIFICANT	24-Apr-03	View article	3.50	3.50	2.75	2.50	3.50	4.25

Papua New Guinea - Key Country Facts

Area (sq km)	452860
Capital	Port Moresby
Languages	English spoken by 1%-2%, pidgin English widespread, Motu spoken in Papua region Note: 715 indigenous languages
Ethnic Diversity	Melanesian, Papuan, Negrito, Micronesian, Polynesian
Religions	Roman Catholic 22%, Lutheran 16%, Presbyterian/Methodist/London Missionary Society 8%, Anglican 5%, Evangelical Alliance 4%, Seventh-Day Adventist 1%, other Protestant sects 10%, indigenous beliefs 34%
Currency	1 kina (K) = 100 toea

Papua New Guinea - Demographic Data (sourced from World Markets Healthcare)

	1990	1997	1998	1999	2000
Demographics					
Total population (m)	3.8	4.5	4.6	4.7	5.1
Population density (per sq km)	8.5	9.9	10.2	10.4	11.3
Total population under 15 years (m)	1.5	1.8	1.8	1.8	2.1
Total population 15-65 years (m)	2.2	2.6	2.7	2.7	2.9
Total population over 65 years (m)	0.1	0.1	0.1	0.1	0.1
Annual population growth (%)	2.2	2.3	2.2	2.2	2.4
Total rural population (m)	3.3	3.8	3.8	3.9	4.2
Total urban population (m)	0.6	0.7	0.8	0.8	0.9
Crude birth rate (per 1,000)	33.5	31.9	..	31.1	32.1
Crude death rate (per 1,000)	11.1	9.7	..	9.7	9.2
Total life expectancy at birth (years)	55.1	57.9	..	58.4	58.6
Total male life expectancy at birth (years)	54.4	57.2	..	57.6	57.8
Total female life expectancy at birth (years)	55.9	58.7	..	59.2	59.4

Source: World Bank, *World Development Indicators 2003*; IMF, *World Economic Outlook September 2001*; World Health Organisation, *WHO Estimates of Health Personnel*

Papua New Guinea - Key Macro-economic Data (sourced from World Markets Country Analysis and Forecast)

	1999	2000	2001	2002e	2003f
Domestic Data					
A - GDP Growth %	7.6	-1.3	-3.4	-3.1	1.6
J - Inflation %	14.9	15.6	10.2	7.5	6.5
N - GDP \$bn	3.44	3.41	2.94	2.93	2.96
Q - GDP Per Capita \$	696	669	558	545	538

Country Report - Papua New Guinea (Country Analysis)

Political Environment

Current as of Thu 18 Dec 2003

Political risks: 3.50

The political environment is volatile, though the election of Sir Michael Somare in July 2002 should ensure a period of relative stability, as he is essentially ensured a full five-year term. Former Prime Minister Sir Mekere Morauta passed numerous political and economic reforms, and made substantial process in a long-stalled privatisation process, winning the support of donors and many investors in the country. However, the general election of 2002 returned the National Alliance to power, replacing Morauta with Somare. Despite public opposition to reform, the government is essentially bankrupt, and realistically will have to comply with donors' requests if it is to continue to finance its budget. Furthermore, it will probably have to implement economic reforms that will prove unpopular with the electorate. The breakaway province of Bougainville, although currently peaceful due to the presence of international observers, remains volatile as one of the more powerful rebel leaders refuses to disarm.

Current Highlights

- **After two weeks in the job, Deputy Prime Minister Andrew Baing was dismissed in November 2003. After Baing refused to vote on constitutional changes to guarantee Prime Minister Sir Michael Somare up to three years in power without the possibility of an opposition no-confidence motion, Somare swiftly replaced him with Agriculture Minister Moses Maladina.**
- **Prior to Baing's dismissal, Somare sacked two other senior ministers in November 2003, for not backing his agenda. Industrial Relations Minister Peter Yama was removed for not supporting Somare over the no-confidence issue, while Allan Marat, Baing's predecessor as Deputy Prime Minister, was fired after he lost his leadership of the People's Progress Party (PPP), one of the parties in the ruling coalition.**
- **In a move that will impact substantially on the political and economic spheres, US energy company Chevron Texaco announced in April 2003 that it is pulling out of Papua New Guinea by October. This is bad news for the government, which is trying to stabilise an economy that remains heavily dependent on the extractive sector.**
- **Australia, PNG's most important strategic ally and its biggest single source of foreign aid, is demanding sweeping internal reforms in order for PNG to continue receiving more than A\$300m (US\$193m) in aid annually. Australia is calling on PNG to embrace higher standards of governance and to get tough on corruption. Canberra wants to put its own officials into key positions within the PNG government system, as it has done in the Solomon Islands, as a condition for the continuation of aid.**
- **The European Union (EU) has demanded an accounting of K14.3m (US\$4.2m) in missing aid money, given to the PNG government. A failure to show that the aid was spent as intended will result in the government having to reimburse the missing funds in full. The money in question came from the EU's fifth Structural Adjustment Support Program, which totals K30m (US\$8.9m).**
- **The government reacted strongly to an independent report that was published in March 2003, which claimed that Papua New Guinea was rapidly becoming a failed state and, as a result, could potentially act as a base for terrorists intent on attacking Australia. The report argued that deficit spending and ill-planned government borrowing had deprived funding for the police, legal system and armed forces. As a result, violent crime had become a major problem, rendering some parts of the country uncontrollable while land and sea borders remain**

unmonitored.

- In March 2003, Somare suspended Tourism Minister Alois Kingsley over allegations that Kingsley threatened to shoot a university professor. Violence is rife in the country, and MPs routinely carry weapons for protection against crime or, in some cases, to intimidate their political rivals. Kingsley was the second minister to be removed from the Cabinet since Somare and his party came to office.
- In December 2002 Morauta was ousted as the country's opposition leader. The relatively unknown Bulolo MP John Muingnepe was appointed opposition leader, following a vote by the People's Democratic Movement (PDM). Rumours that Morauta might consider joining the ruling National Alliance weren't realised, and in February 2003 he was reinstated as party leader.
- A National Alliance-led government, headed by the former Prime Minister Sir Michael Somare, was returned to power in August 2002, replacing the PDM administration led by Morauta. The election suffered the usual problems of a widely-split vote, poor turnout, extremely low incumbency and widespread corruption. Political reforms passed in 2000 may help in the long term, but had little impact on the 2002 election. In addition to the usual failures, the 2002 election campaign was also generally acknowledged to have been the most violent on record.
- The Bougainville peace process continues to edge forward. In March 2002 parliament passed a series of bills giving legal effect to the peace agreement signed between the government and the rebels. Bougainville receives a high degree of autonomy under the measures, with its own police force, judiciary and tax regime, and will be able to vote in 10-15 years on a referendum which will include full independence as an option.
- Unrest in the army over redundancy plans has sparked mutinies, the most recent of which was at Moem barracks in Wewak in March 2002. This mutiny was much smaller than the one that brought chaos to the capital in March 2001, and failed to force any suspension of the streamlining policy, unlike the earlier unrest. In December 2002 a court found guilty 24 out of the 27 soldiers involved. The mutiny highlighted the need to rationalise the armed forces, ensuring that there are enough funds to turn the military into a more professional body.

Division of Power

Papua New Guinea became an independent state in 1975, prior to which it was a combined United Nations (UN) trusteeship/colonial possession under Australian rule.

Papua New Guinea is a parliamentary democracy within the UK Commonwealth. The head of state is the UK monarch, currently Queen Elizabeth II. Her representative on the island is the governor general, who is nominated by parliament for a six-year term. This position is largely ceremonial.

Legislative power is vested in the single legislative house known as the National Parliament, which is made up of 109 members from all parts of the country. Of these, 89 seats represent open constituencies and 20 provincial constituencies. Members are elected by universal suffrage. Elections are held every five years. The head of government is the prime minister, who is elected by parliament. The prime minister appoints ministers from his/her party or coalition. Policy is determined by the National Executive Council (the cabinet).

Main Political Parties

The main political parties are:

- **National Alliance (NA):** Led by Sir Michael Somare, the NA was forced from the cabinet in 2000 for making remarks against the PDM. It was broadly supportive of the PDM's economic reforms when it was in government under Prime Minister Morauta, but has taken a more nationalist-populist line under Prime Minister Somare, with the suspension of the privatisation process in August 2002.
- **People's Democratic Movement (PDM):** Led by Sir Mekere Morauta, the PDM was the dominant force in the outgoing parliament, and it is still the second-largest party. It is broadly supportive of the economic reform advocated by the prime minister. Paias Wingti
- **People's National Congress Party (PNCP):** Led by former Prime Minister Bill Skate, who is currently the parliamentary speaker. The PNCP's strength has been much eroded since Skate was forced from power, though it still won six seats in 2002. It takes a populist line and is opposed to recent reforms.
- **Pangu:** Pangu is led by Chris Havieta. Historically the party with the widest support base, Pangu was badly affected when the NA broke from it in 1997. It retains support in the Papuan and Highlands regions, but its popularity has fallen in the Momase and Islands regions.
- **People's Action Party (PAP):** Party leader Ted Diro, a former leader of the national armed forces, is regarded as a strong negotiator and has served in many national governments.

- **People's Progress Party (PPP):** The PPP is led by Andrew Baing, who was the deputy prime minister for two weeks in November 2003, until he was dismissed from that post for not supporting Somare's constitutional agenda. The party's position in PNG politics was secured by previous leader Dr Allan Marat, despite the departure of the party's high-profile founder and spiritual mentor, former Prime Minister Sir Julius Chan, from its leadership. The PPP was previously allied with the PDM.
- **The Melanesian Alliance (MA):** Led by Bernard Narokobi, the MA is a party with only a few MPs, but they tend to hold disproportionate influence. The party was dissolved in 2001, when its leader backed the PDM's decision to sack the rest of its MPs, but it was reformed for the 2002 elections with yet more influential figures.
- **People's Labour Party (PLP):** Under its leader Peter Yama, the party came to prominence in the 2002 election, sweeping from nowhere to take four seats on the back of union anger with the economic reform programme.

Key Political Players

Prime Minister	Sir Michael Somare (NA)	Somare has nationalist roots, as the country's first post-independence prime minister, and some suspect that he may be trying to push a nationalist-populist agenda. Somare and his NA were part of the PDM government until they were forced out in 2000. He has previously been accused of pursuing consensus at the expense of cohesive policies.
Opposition Leader	Sir Mekere Morauta (PDM)	Morauta, a former head of the Central Bank, is respected by the international community and donors. His government lost the 2002 election largely because of its implementation of an unpopular economic-reform package. Morauta did not enter politics until 1997, but managed to achieve remarkable control of the PDM and the governing coalition despite his lack of a political background.
Minister for Foreign Affairs	Sir Rabbie Namaliu (Pangu)	Namaliu was prime minister between 1988 and 1992, and is respected on the international stage.
Secretary for Petroleum and Energy	Sir Moi Avei (NA)	Avei was the minister who successfully oversaw the peace process on the troubled island of Bougainville.
Speaker and Former Prime Minister	Bill Skate (PNCP)	Skate was the former PDM government's most vocal opponent, but his own term as prime minister was disastrous. His health has become fragile in recent years.
Treasurer	Bart Philemon	Philemon is seen as a competent manager, but faces a difficult task in trying to control the government's burgeoning debt crisis. Prime Minister Somare is likely to wield heavy influence over economic matters.
Central Bank Governor	Wilson Kamit	Kamit is well-regarded, but power over monetary policy lies more with the prime minister.
Governor General	Sir Silas Atopare	Atopare's position is essentially ceremonial. He was appointed in 1997.

Political Stability

Politics in Papua New Guinea are inherently unstable, for the following reasons:

- **Traditionally, political units in Papua New Guinea have always been small, clan-based entities. Since independence, regional loyalties have remained strong and this has interfered**

significantly with efforts to establish a national identity. The petty localism of some politicians is enhanced by the large per-capita number of MPs - roughly one per 6,000 citizens. This compares with one politician per 50,000 in Australia, and one per 60,000 in the UK.

- The constitution does not restrict the number of parliamentary candidates competing for seats in general elections. In the last election there were over 2,000 candidates competing for only 109 seats. The situation does not appear to be that much better in 2002, with over 1,700 candidates running. This means that MPs can often be elected with less than 10% of the total vote in their region. Less than half of MPs survive more than one electoral term. Problems are compounded by the 'first-past-the-post' electoral system and by multi-member constituencies, both of which work poorly in climates where party systems are weak and there is a multiplicity of candidates. Since the 2002 general election a preferential system of voting has come into force - replacing the 'first-past-the-post' system - for by-elections and future general elections. This should be a substantial help in ending the fragmentation of votes and encouraging co-operation within politics at both national and village levels.
- Political parties tend to be based on personalities rather than policies, and the political system is based largely on patronage. As a result of the low importance of ideology in forming political groups, parties tend not to be very cohesive and can therefore fracture easily. Governing coalitions have proven particularly fluid and unstable, though the PDM has been better than most. The new laws to prevent party-hopping between elections should help reduce this problem.

No prime minister of Papua New Guinea has ever served a full term. Frequent changes of government led to a constitutional amendment, passed in 1994, which extended the 'grace period' before a government could be subject to a vote of no confidence from six to 18 months.

Recent Elections

Prime Minister Sir Mekere Morauta took over in July 1999, after the previous premier, Bill Skate, was toppled. Skate had united the opposition (suspending the parliament for six months) and irked his allies, and his financial policy had proved an unmitigated disaster. In the end it was a scandal involving the exchange of diplomatic recognition for US\$2.3bn in aid from Taiwan that finally finished his turbulent term in office.

General elections in 2002 were generally admitted to be the most violent and chaotic since independence. Voting in the Southern Highlands, in particular, descended into anarchy, and over 30 people died in the course of election-related violence. Balloting in several seats in the Highlands was annulled. In the main cities, in contrast, voting was quite well organised, by traditional standards. To the small extent that policies rather than personalities can be said to dominate an election in Papua New Guinea, the campaign was dominated by the government's unpopular economic reform programme, and the PDM suffered losses at the ballot box. The NA emerged as the largest party and was able to form the new government, winning 88 of the 103 votes available at the start of the new parliament. However, independents and single-seat parties form by far the largest segment of parliament.

2002 Election Results			
Party	Confirmed Seats	Interim Results	Probable Total
Independents and Single Seat Parties	24	2	26
National Alliance (NA)	18	1	19
People's Democratic Movement (PDM)	10	2	12
People's National Congress Party	2	0	2
Pangu	6	0	6
People's Action Party (PAP)	5	0	5
People's Progress Party (PPP)	6	0	6
Melanesian Alliance	3	0	3
People's Labour Party	3	1	4
Other	17	0	17
Undeclared	9	-	9
Total	-	-	109

The Somare Government

Somare's administration began on a worrying note, as he cancelled the sale of the national telecoms monopoly - which the Morauta government had agreed in its final hours - and suspended other privatisations of national utility companies and Air Niugini. Especially unsettling was Somare's statement, which accompanied the policy shift, in which he declared that many of these state companies had made money when he was last in office, and he did not see why the situation had changed. This appeared to be a somewhat naive comment, but is likely to have been a populist ploy. The government, as it showed in its November 2002 budget, is prepared to pursue similar policies

to those set out under the Morauta government and the international community will continue to pressure it to implement austerity measures. Stability in the new administration is likely to be enhanced by the political reforms passed by Morauta's government, but some remain wary of Somare's past tendency to sacrifice bold policy moves, which are certainly needed in PNG, for the sake of coalition cohesiveness.

Relations between Somare and Australian Prime Minister Howard took a sour turn during the 2003 Pacific Islands leaders' conference, when Howard threatened to cut financial aid to Pacific island countries - including PNG - and pressured the members of the Pacific Islands Forum to appoint Australian Greg Urwin as its new Secretary-General, replacing Papua New Guinean Noel Levi. Other undercurrents that are beginning to surface also indicate that Sir Michael's dislike of Australia started during the last general elections, when he was informed, through intelligence reports, that the Australian government would have preferred then-Prime Minister Sir Mekere Morauta to remain in office. Australia is PNG's most important strategic partner.

China has emerged as a potential strategic ally, offering a higher level of aid in response to the country's financial woes and the political rift with Australia. In the spring of 2003, PNG also signed the Pacific Island Countries Trade Agreement (PICTA) and the Pacific Agreement on Closer Economic Relations (PACER), which will phase in free trade between Pacific island nations over the next 10 years. The eventual goal is the creation of a regional market that would include 7m people, with an increase in regional trade co-operation and the flow of goods between nations. It is also hoped that the agreements will increase the region's attractiveness to foreign investors. PNG has had a bilateral free trade agreement (FTA) with Australia since 1977.

The Landmark Morauta Government Reforms

At the beginning of Morauta's term he proved more effective than many of his predecessors, supported by an unusually united parliament. He showed an ability to use the existing laws to maximise the chances of his government passing laws and staying in power - for example, following the passage of the budget in December 2000, parliament was suspended for six months during the window of time when the opposition could launch a no-confidence vote (after the 18-month grace period and before the further six-month grace that must, constitutionally, precede an election). The prime minister also managed to pass the Political Parties and Candidates Integrity Bill, making it harder for MPs to switch parties mid-election by requiring their move to be sanctioned in a by-election. Crucially, it will strengthen the power of the prime minister, making it harder to remove him via a no-confidence vote and ensuring a wider support base for his initial election. In addition, the country now has a system of preferential voting for by-elections and general elections. There were also provisions relating to the funding of political parties. These should enhance the chances of a government surviving between elections, and, in the long term, if they enhance the power of parties they may also improve stability during elections.

Privatisation was another area in which the Morauta government made progress. Papua New Guinea Banking Corporation, formed from the former state-owned enterprise (SOE) Finance Pacific, was sold to a local company, the Bank South Pacific, in November 2001. PNG Telikom (the monopoly telecoms service provider) was sold at the end of Morauta's tenure in August 2002. Air Niugini (the national carrier), Elcom (the monopoly electricity provider) and the water utility were also brought close to sale point. However, workers and many politicians strongly opposed the process, and the new Somare government suspended the process, reversing the Telikom sale.

The Military

The Papua New Guinea Defence Force (PNGDF) is a potent source of instability in the country, despite numbering only about 4,150. In 1997, when the government attempted to bring in foreign mercenaries to fight the Bougainville insurgency, the army, backed by popular support, staged a messy uprising that overthrew the then prime minister, Julius Chan. It has since been involved in a number of destabilising incidents, including a rampage in September 2000 after a soldier was shot dead by police while participating in an armed robbery - looting broke out throughout the capital, and parliament had to be shut down as scared MPs stayed away. More seriously, in March 2001 the PNGDF mutinied over plans to reduce its size to around 1,900. Although additional political demands were made - such as expelling IMF, World Bank and Australian advisors and recalling parliament - it seems that the crux of the dispute lay over the redundancy proposals. After Morauta retracted the plan, the dispute was brought rapidly to a close. Similarly, outrage at government attempts to press forward with the redundancy scheme in 2002 caused several troops at the Moem barracks in Wewak to seize an armoury and take over their compound. However, the rebellion was contained and gradually brought to a close without any repercussions for civil order or the future of military-restructuring plans. However, the PNGDF's unruliness merely highlights the need to reform

the service - restructuring has been delayed rather than cancelled.

Civil Unrest

In late June 2001, student-led protests against the government's economic policies, and against the continued presence of foreign economic advisors - especially from Australia, the IMF and World Bank - descended into violence in which three students were shot dead by the police. The unrest led to the imposition of a curfew and, occurring so shortly after the army's March mutiny, once again highlighted the government's fragile grip on civil order in the country.

Bougainville

The Bougainville peace process took a huge leap forward in March 2002, when parliament gave legal force to government commitments made as part of a deal that turned a ceasefire with the island's rebels into a fully-fledged peace deal. The measures allow Bougainville wide-ranging autonomy, with the island now able to establish its own tax regime, judiciary and police force. The PNGDF will have only a tiny presence on Bougainville. In addition, the island has been guaranteed a referendum in 10-15 years' time, in which full independence will be an option. The deal has defused tension significantly between the former rebel movement and the government, though some of the insurgency's leaders have bowed out rather than deal with the government. For more information on the root causes of the insurgency see Papua New Guinea: [Security Environment](#).

External Relations

Papua New Guinea retains fairly strong links with its former colonial power, Australia, as well as strong economic ties. Should these bonds be threatened Papua New Guinea would lose large amounts of aid, threatening economic difficulties.

Outlook

The adoption of preferential voting in future elections will be welcome, and in the long term the political reforms that the Morauta government implemented are likely to strengthen the role that parties play in the political system, leading to a gradual rise in their ability to push their candidates to victory over independents. However, in the short term, fluid coalitions will probably remain the norm.

Many foreign investors, including Australia's Oil Search Ltd and Highlands Pacific Ltd, had warned that Morauta's continued survival was essential for the confidence of their community. Sir Michael Somare is reasonably well regarded by the business community, but he is far from a match for the investor- and donor-friendly Morauta. However, policy is recovering from the unstable start caused by Somare's decision to suspend the privatisation programme. There is little prospect that Somare's government will prove any more capable of successfully tackling the country's myriad problems than that of Morauta. To achieve an economic turnaround, the administration will need to implement unpopular reforms. Given Somare's populist background, this looks an unlikely policy line.


Useful Links


- PNG government online: www.pngonline.gov.pg
- Office of the prime minister: www.pm.gov.pg/pmsoffice/pmsoffice.nsf?Open
- PNG Electoral Commission: www.pngec.gov.pg/


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14. 12/08/2003 -  **COUNTRY** **Bougainville Peace Process Reaches Milestone in Papua New Guinea**(In Brief)

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Economic Environment

Current as of Thu 18 Dec 2003

Economic risks: 3.50

Papua New Guinea increased its average annual gross domestic product (GDP) growth from 1.9% in the 1980s to 4.5% in the 1990s through raised exports from the principal mineral sector. Papua New Guinea's economy is vulnerable, however, having neared collapse in 1999. Policy mismanagement in the 1990s led to a string of growing budget deficits, soaring public debt and a sharp collapse in the currency. The Morauta government showed a more responsible fiscal attitude and adhered to a structural programme laid down by multilaterals. Its successor, elected in July 2002, is slowly proving its economic credentials, despite early fears regarding economic mismanagement. Repayment of debt is a budgetary priority, and the government has plans to privatise a range of loss-making industries. However, external circumstances have conspired to undermine growth. Over the longer term, the country is overly dependent upon commodity exports, leaving it vulnerable to fluctuations in global commodity prices. Declining output from the mining sector is a major worry, as old projects reach the end of their lifespan and new ones fail to emerge to replace them. As such, in the medium-term, the government will have to adjust the economy to counter the declining minerals sector, while trying to buoy growth prospects and restore public confidence

Papua New Guinea - Economic Data

	1997	1998	1999	2000	2001	2002e	2003f
Domestic Data							
A - GDP Growth %	-3.9	-3.8	7.6	-1.3	-3.4	-3.1	1.6
F - Agriculture % GDP	..	..	28.71	27.45	25.97	26.3	26.72
G - Industry % GDP	..	..	9.08	8.28	7.98	9.03	9.11
H - Services % GDP	..	..	33.16	31.5	32.02	31.01	29.87
J - Inflation %	3.9	13.6	14.9	15.6	10.2	7.5	6.5
K - Budget Balance % GDP	-6.1	-7.7	-8.4	-7	-9.4	-10.4	-8
N - GDP \$bn	4.9	3.8	3.44	3.41	2.94	2.93	2.96
O - GDP % of UK	0.4	0.3	0.24	0.24	0.21	0.19	0.18
P - GDP % of US	0.1	0	0.04	0.03	0.03	0.03	0.03
Q - GDP Per Capita \$	1146.7	815.8	696	669	558	545	538
R - GDP Per Capita % of UK	5.1	3.4	2.84	2.77	2.35	2.13	1.97
S - GDP Per Capita % of US	3.7	2.5	2.05	1.91	1.58	1.5	1.44
T - Population m	..	..	5.01	5.13	5.25	5.38	5.5
External Data							
X - \$ to Currency	1.75	2.1	2.57	2.78	3.39	3.93	4.17
AA - Exports \$m	2186	1849	2019	2214	1878	1624	1915
AB - Export Growth %, y-on-y	-14.6	-15.4	9.25	9.66	-15.18	-13.53	17.92
AC - Imports \$m	-1972	-1425	-1525	-1503	-1269	-1225	-1298
AD - Import Growth %, y-on-y	-2	-27.7	7.02	-1.44	-15.57	-3.47	5.96
AE - Trade Balance \$m	214	424	494	711	609	399	617
AF - Total Export Earnings \$m	..	..	2248	2369	2108	2134	2285
AG - Current Account Balance \$m	-192.2	-28.9	114	353	281	-31	200
AH - Current Account % GDP	-3.9	-0.8	3.31	10.35	9.57	-1.06	6.76
AJ - Capital Account Balance \$m	..	..	16	-254	-99	-73	-90

AK - Reserves (minus gold) \$m	362.7	192.9	205.14	308.48	438.86	340	260
AL - Reserve Import Cover - Months	2.2	1.6	1.61	2.46	4.15	3.33	2.4
AM - Foreign Direct Investment \$m	28.6	109.6	296	96	74	16	91
AN - Foreign Direct Investment % GDP	0.6	2.9	8.61	2.81	2.52	0.55	3.07
AO - Total External Debt \$m	1310	1346	1348	1349	1483	1425	1350
AP - Short Term Debt \$m	154	156.7	97	49	68	39	46
AQ - Total Debt Service \$m	..	..	182	282	262	331	346
AR - Total Debt % GDP	26.6	35.6	39.14	39.55	50.51	48.63	45.61
AS - Debt Service Ratio % Total Exports	20.5	8.6	8.09	11.89	12.44	15.51	15.14
AT - Total Debt % Total Exports	59.9	72.8	59.96	56.95	70.35	66.78	59.08
AU - Short Term Debt % Total Debt	5.9	5.8	7.23	3.67	4.61	2.74	3.41
AV - Short Term Debt % Reserves	42.5	81.2	47.51	16.04	15.57	11.47	17.69
AW - Interest Payment Arrears \$m	..	..	0	0	0	0	0
AX - Grants \$m	..	..	95	98	70	112	100
AY - Debt Forgiveness + Rescheduling \$m	..	..	0	0	0	0	0
AZ - External Assets \$m	..	..	371	230	313	402	421
BA - External Liquidity Gap % Total Exports	..	..	-0.7	-12.45	-9.66	3.1	-6.39

Notes: J - (aop) Average over period X - US\$: PNG Kina to US\$, eop

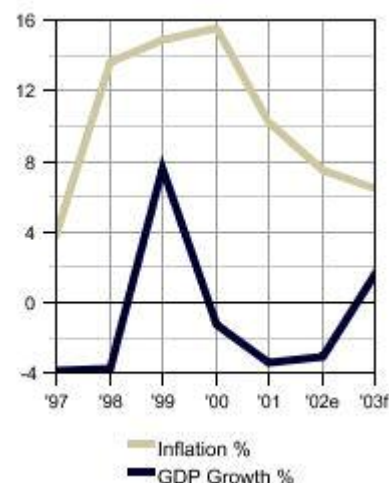
[Table Key](#)

[WMRC Forecasting Methodology](#)

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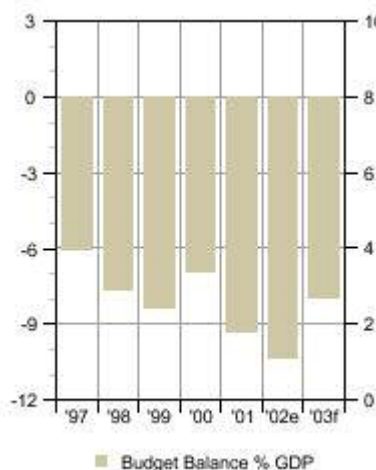
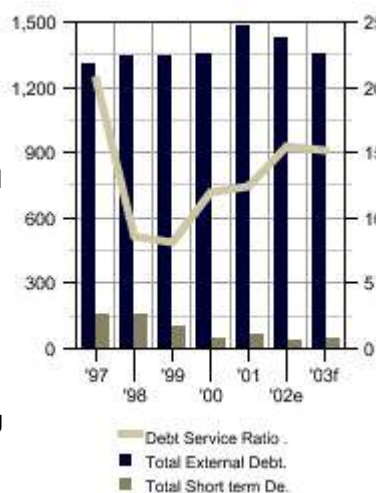
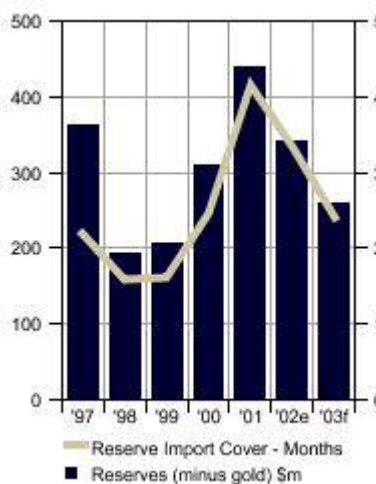
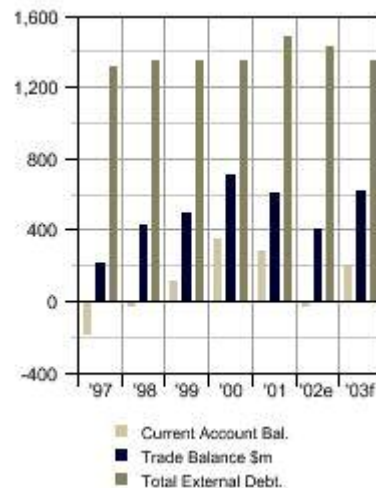
Current Highlights

- **The conflict in the Gulf has had mixed effects on the economy.** It provided something of a fillip through increased prices for the two most valuable export commodities, gold and oil, but warnings were sounded regarding the likely longer-term impact it would have on exports in light of the slowdown in the worldwide market.
- **2002 marks a return to growth?** WMRC estimates that 2002 will see 1.2% GDP growth, ending the period of contraction that ran almost uninterrupted from 1997-2001. Weak commodity prices and demand worldwide, declining mining output and weak domestic demand combined to produce a 3.4% contraction in growth in 2001, but it is hoped that this figure will turn positive in 2002 and 2003 as the agriculture sector expands.
- **The government of Prime Minister Michael Somare presented its first budget in November 2002.** The 2003 budget, which was passed



in December 2002, aimed to stabilise the national currency, the kina, to reduce inflation, to stabilise foreign-currency reserve levels and to prioritise the funding of projects likely to have a positive economic and social impact. It was regarded as the beginning of a long process to try to return the country to economic and social health.

- **Somare's government suspended the privatisation process in August 2002.** Somare was probably trying to start his term in office with a populist move, rather than to deliberately derail the country's economic fortunes. As a result, however, foreign investors and donors continue to watch the government keenly, particularly as Somare's previous government was renowned for its appalling economic management and corruption.
- **The government was warned in August 2002 that its spending levels were unsustainable and that a financial crisis was looming.** High rates of government borrowing, rising inflation and falling output from the resources sector continue to fuel the country's economic problems. Debt repayment, both external and domestic, continues to be a major problem for the government.
- **Unemployment remains a damaging social and economic problem.** Unemployment, while difficult to measure, remains at very high levels, estimated at 30-50% of the population. Besides leading to crime and other social ills, this represents a massive waste of economic resources.
- **Major adjustments need to be made in the economy to overcome the substantial depletion of mining and oil resources within a decade.** The government needs to address weaknesses in physical and social infrastructure as well as adopting an acceptable reform of the land laws. This is important because the current situation underlies much of the social unrest and business-risk perception in the country.



Economic Performance and Prospects

Historical Growth Performance has Deteriorated from the Early 1990s

Papua New Guinea (PNG) achieved only minimal growth in the 1980s; between 1979 and 1989 GDP growth averaged just 1.9%. However, as the country began the 1990s, strong regional demand for the country's export goods, previously diversified into cash crops and boosted by increased mineral production, helped push up growth rates. Over the 1989-1999 period growth averaged a respectable 4.8%, and the economy was characterised by current-account surpluses. Papua New Guinea has an unusually high level of trade for a low income nation; exports amount to close to 50% of GDP in 1999 and are commonly seen as the primary driver of growth. As the decade wore on, however, corruption and political instability gradually soured investors' view of the country, and new foreign investment in key export industries dried up. This, combined with a series of natural disasters, including a tidal wave and drought and external shocks such as the Asia crisis, led GDP to decline by 3.9% in 1997, by 3.8% in 1998, by 0.8% in 2000 and by 3.4% in 2001.

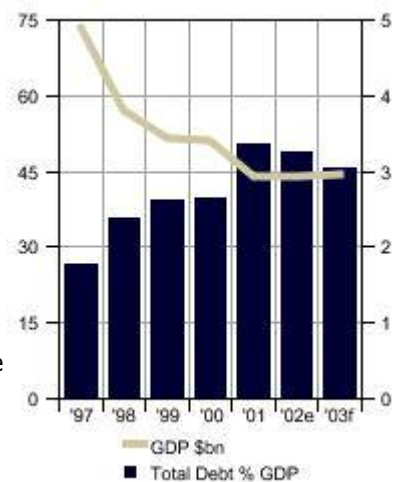
Investor and Consumer Confidence Remain Low

Investors abandoned Papua New Guinea at the end of the 1990s. Lax government monetary policies led to soaring inflation, which compounded the problems of corruption, a steadily weakening currency and political instability. Consumer confidence was also weak, amid a climate of rising crime, political volatility, poor harvests and high inflation. Government spending helped prop up GDP but had such an inflationary impact as to have an overall negative effect on real growth. Poor export performance compounded the problem.

Structural Changes Necessary

Questions remain regarding the direction of economic policy under the Somare government. Structural adjustment, however, appears to be

continuing. The contribution of the mining and oil sector to GDP is projected to weaken over the medium term as mining and oil resources are depleted, but this should be countered by the expansion of agricultural, forestry and fishery industries. That said, the gradually falling output of minerals and continued weakness in global prices for vegetable agricultural goods (as opposed to meat products) bode ill for a rapid recovery of exports. There are some prospects for a slight rise, as new projects come online and if a proposed oil pipeline to Australia is built it would be a massive boost, though the outlook for the pipeline is cloudy at best. However, investors continue to be deterred by high crime levels, poor political stability, corruption and relatively unattractive tax levels. There is, then, little prospect for a surge in investment over the short term and in fact, the opposite is likely, as the large mineral sector projects that kept the public-sector afloat during the 1990s are phased out as resources deplete. This, and the possible absence of new projects, will impact negatively on the trade surplus, posing further major challenges for the long-term health of the economy.



PNG is ill-equipped to deal with the additional exchange rate and reserve instability that would most likely accompany current-account deficits. Consumption spending remains constrained by high poverty levels, and government spending is constrained by the need to bring down high debt levels. Growth is forecast to edge back into positive territory, but this will be exceeded by population growth, leading to no improvement in per capita GDP. Furthermore, the economy remains weak and exposed to macro-economic shocks.

Improved Political Stability would Bring Massive Benefits

The situation could be quite different if the political climate were to improve. The country retains significant natural advantages, including virtually untapped maritime resources. Stability would attract new investment in the country's undoubted mineral wealth. Government spending is also likely to increase once levels of public debt are reduced to more manageable levels. This will allow resources to be spent on more development projects to aid the country's infrastructure, providing a boost to the country's businesses and internal markets and possibly laying the foundation for a virtuous growth cycle.

Macro-Economic Policies

Monetary Policy has been Kept Tight

The Morauta government was forced to keep monetary policy tight after the previous administration's lax monetary policy saw inflation peaking at 22% in 1998 - a sharp diversion from the historical trend under which inflation has been low. This austere policy, coupled with weak demand, paid dividends, resulting in inflation falling to below 10% at the end of 2001. This remained the situation into the first half of 2002; inflation remained just under 10%; the balance of payments was in surplus; and net reserves were at the equivalent of 2.8 months of non-mineral imports. Mid-year elections prompted some problems, which the Somare government has since sought to take in hand. In its 2003 budget, the government promised to keep a tight control on expenditure at all levels. Pressure was brought upon government departments and associated bodies to control expenditure, and Finance Minister Bart Philemon announced reductions in the civil service, beginning in 2004. Doubts remain, however, as to whether the same degree of pressure will be brought to bear on politicians; one of the most serious factors contributing to overspending in the past has been unplanned expenditures resulting from political interference.

The Central Bank has considerable independence from the government, as well as autonomy over the instruments it uses to control monetary policy. However, the government has occasionally breached legal ceilings on domestic borrowing (though Morauta claimed ignorance and admonished ministers who allowed this to happen), and it is unclear just how much

security laws guaranteeing Central Bank independence provide.

The currency has suffered heavily between 1997 and 1999, deteriorating from K1.8:US\$1 to K2.7:US\$1. In 1999-2000 the kina strengthened on the arrival of the Morauta government, a surge in current account surpluses and the resumption of IMF support. However, in line with other regional currencies it slipped against the US dollar in 2001, depreciating by 24% between end-2001 and end-October 2002. One of the primary goals of the 2003 budget was to stabilise the kina. Furthermore, the government has also been seeking to stabilise foreign-reserve levels. Reserves have risen substantially from a low of US\$89m in mid-1999 to over US\$300m by the end of 2001. The Central Bank frequently intervenes to support the currency, a strategy necessary in a trading country of PNG's size, as the market for the kina is generally illiquid and suffers from rapid swings in demand and supply. However, the Bank lacks the resources to challenge the market's will, even if it wished to.

Fiscal Policy Constrained by Inflation and High Public Debt

The Morauta government pursued a strategy of paying down debt and focusing tightened spending on development areas. The budget deficit stood at a manageable 2.6% in 2001. Preliminary estimates, provided by the Bank of Papua New Guinea in March 2003, showed that there was an overall deficit of K454.3m in 2002, a substantial rise on the K359.4m that was recorded the previous year. As such, the budget deficit represented 4.1% of GDP, significantly above the estimated 3.4%. The overspend came as a result of greater spending during the first half of the year, which, had it continued, would have prompted a deficit of around 6%. Attempts by the Somare government to curb government spending were largely successful, and the Somare government appears similarly determined not to overshoot targets, with revenue shortfalls being made up for by expenditure cuts. With the government needing to maintain multilateral support, it is likely that efforts to keep the deficit down will be maintained.

Creditor Relations Uneasy

Relations with PNG's main creditors improved under the Morauta government, which proved more committed than its predecessor to reducing the budget deficit and implemented a programme of multilateral-advocated fiscal and structural reform, backing it up with political reforms designed to aid stability. This response led to a generally positive reception for the government among creditors, though many of the reforms remained half-implemented as a result of opposition from the public and politicians. Fears have been expressed regarding the economic commitment of Somare's government, and primary donor Australia was quick to dismiss government requests for debt rescheduling in November 2002, arguing that such a move would be counter-productive.

The degree of aid that Australia provides is testament to the close historical and business ties between the two nations. However, it has also raised nationalist concerns in PNG, where many accuse Australia of trying to buy PNG or acting like an imperial power. PNG also maintains a network of other donors, mostly nation states, known as the 'Friends of Papua New Guinea', which include Japan and the European Union (EU). China is an increasingly prominent donor. Further donor aid comes from multilaterals, including the IMF, the World Bank and the Asian Development Bank (ADB).

Caught in a Debt Trap

External debt is fairly well balanced between long- and short-term obligations. The country is, however, caught in a debt trap, as the 1999 financial crisis highlighted. Much of the country's export earnings, which at 43% of GDP in 2000 are relatively large for a country of PNG's economic stature, flow straight back out of the economy to meet debt obligations. This puts pressure on foreign-exchange reserves. A deep deficit was run up during 1997-1998, which the government financed through short-term debt. The country's

reserves, which are heavily dependent on commodity prices, proved insufficient when short-term debt amounted to over 120% of reserves. Currency instability is a debilitating consequence of such debt pressures. This is a cyclical phenomenon, which will not be broken until the government either stops financing its deficits through short-term debt or implements structural reforms in order to make the country less commodity-dependent. The Somare government is seeking an IMF-led financial package to help it tackle its budgetary problems, which are likely to increase as further projects are financed.

Financial Markets

Birth of the POMSoX

Papua New Guinea's financial sector is not strong. Demand for credit is weak, as interest rates remain relatively high at over 10%. The country formerly opened a small stock exchange, the Port Moresby Stock Exchange (POMSoX), in April 1999. This is not expected to act as a major boost to the country's capital markets, at least not in the short to medium term. The Central Bank has the responsibility for regulating the financial system.

Economic Development

High Hopes Dashed Amid a Climate of Instability and Growing Corruption

Papua New Guinea, like many resource-rich countries gaining independence, began its life as an independent democracy in 1975 with high economic hopes. However, underlying economic problems have combined with specific shocks to ensure that although GDP has increased from US\$0.6bn in 1970 to US\$4.2bn in 2000, few benefits have filtered through to the domestic economy. Key long-term problems have included growing corruption, epitomised by a case in 1991 when the Governor General was forced to resign after refusing to sack the Deputy Prime Minister who had been found guilty on 81 corruption and misconduct charges, the prominence of inefficient state-owned industries and rising foreign debt. Unbroken political instability, symbolised in the fact that no Prime Minister has ever completed a term of office, has also deterred long-term investment. The most significant shock and probably the biggest single cause of national economic decline, was the Bougainville war of secession, which caused more than 20,000 deaths and cost the government tens of millions of dollars over the ten years that it lasted, between 1988 and 1998. The war forced the closure of the Bougainville copper mine, then the source of around 40% of the country's export earnings. Other external shocks since independence include droughts, flooding, tidal waves and the 1997-1998 Asian Financial Crisis.

Massive Unemployment Compounds Instability

Unemployment is a key issue for the country. Over 80% of the population live in the countryside, the majority eking out their living by subsistence farming. Open urban unemployment is estimated at around 30%, leading to high rates of crime, especially violent crime, that add to security costs and deter foreign investors. Open rural unemployment is thought to be even higher, with a national rate estimated at close to 40%. This group of jobless represents lost economic potential, increases political instability and is a drain on the government's thin social security resources. Over 37% of the country lives at or below the official global poverty line of earning US\$1 per day, and illiteracy rates are high - close to 30% among men and 44% among women. The rapid inflow of new labour as a result of extremely high population growth rates is a major problem that compounds both unemployment and poverty rates.

Tied to the Fortunes of the Mineral Sector

Papua New Guinea's economy has become inextricably tied to the vacillating

fortunes of the mineral sector. GDP growth fluctuates to an astounding degree depending on the sector's fortunes. In the early 1990s, as new mines opened, growth hit 9.6% (1990), 13.8% (1991) and 18.2% (1992), before plunging again to -3.9% (1997), -3.7% (1998) and -2.5% (2001), as global commodity prices sagged in the wake of events such as the Asian crisis. This instability does not help long-term economic planning, and hinders the government's efforts to promote development and steady tax revenue income streams. Mineral output continues to decline in the absence of new projects, though officials hope that falling oil production at fields in Kutubu and Gobe will be at least partly offset by rising output in the Moran fields. The government has recognised that there is a considerable problem, and, increasingly, suggestions are being made that the rural sector should be further developed as a means of diversifying the economy's base. There is cause for some optimism in the fact that key commodities, particularly coffee and cocoa, have been growing. That said, productivity in most sectors continues to be a problem because of a lack of response to higher prices, the poor quality of infrastructure, and continuing law and order problems.

Privatisation Judders Forward

Privatisation has been a core element of the government's reform programme and is necessary to help pay down the large public debt. It remains generally unpopular and there have been many examples of failed or stalled sell-offs. Air Niugini is a case in point, having been brought to the point of sale, which initially stalled following a lack of investor interest. The Morauta government agreed its sale before being voted out of office in July 2002, after which the government of Prime Minister Michael Somare suspended the deal. In addition, as a complementary part of an IMF structural adjustment programme, the civil service and army are being slimmed down, although lay-offs in the army slowed following mutinous unrest provoked by the downsizing programme in early 2001. Further privatisation attempts are likely to be blighted by financial problems that continue to hamper Air Niugini's otherwise robust performance, as well as increasing industry concerns regarding the financial status of state communications company, Telikom.

Significant Sectors to Watch

- **Agriculture:** The Government's forecast for economic expansion currently rests on growth in the agriculture sector. The sector has largely recovered from the natural disasters of the late 1990s. The country's marine resources are particularly impressive, if under-exploited, and are said to be the world's richest fishing grounds, capable of sustaining a daily catch of up to 1m tons. The government is keen to capitalise on this and new fish canning plants are being completed in Wewak and Lae. Agricultural industries of global standard include cocoa, coffee, copra, sweet potatoes and palm oil, as well as a range of exotic fruit. There is still substantial room for increased efficiency in investment and production in these industries. The town of Tokua has attracted substantial agricultural investments, and officials talk of expanding trade with northern neighbours, such as Indonesia.
- **Mining:** Mining is already the nation's primary foreign-exchange earner (not to mention growth driver). Major gold mines include Ok Tedi and Porgera. Copper is also abundant, although since the closure of the Bougainville mine, output has slumped considerably. The Ramu nickel and cobalt mine, opened in 2000, is the first major new project in several years. However, Papua New Guinea still has substantial untapped resources. Key limitations on the sector's further development include geographic difficulties in reaching and exploiting new mines, environmental concerns, which have dogged the Ok Tedi mine in particular, and an activist, lawsuit-happy land-owner movement keen to squeeze as much out of mining companies as possible, wherever new projects are mooted.
- **Energy:** Papua New Guinea offers many opportunities for energy-sector investors. Extraction is a declining industry, but oil and gas are still produced in large quantities. The nation's major oilfield is located at Kutubu, and the Gobe oilfield is still in operation. The Moran field

produces both oil and gas. A US\$3.2bn pipeline connecting Kutubu to the state of Queensland in Australia is under consideration, but the project faces an uncertain future. Prospects are mixed: the Morauta government secured a US\$700,000 Asian Development Bank (ADB) loan to help PNG finance its role in the pipeline and its entry into the project, led by Japan's Itochu Corporation, and in June 2002 the government and several leading energy companies signed agreements on fiscal and legal arrangements for the project. That said, the overall outlook for the scheme is still weak, especially as ExxonMobil, a project participant, has now lost a key energy contract in Queensland. On a brighter note, drilling began at one of several exploration wells planned by InterOil in March 2003. PNG also offers prospects for the generating and distribution industries, though with a largely rural population that is scattered over extremely inaccessible terrain, the immediate focus for most electricity companies will be the cities. Papua New Guinea suffers from a substantial energy shortage; most leading enterprises and multinationals have their own generators.

- **Tourism:** Large parts of Papua New Guinea are unspoilt paradises, and there are many opportunities for investors willing to cater to Australian, Japanese and other arrivals. The town of Madang has been called the nation's tourist capital. However, with violent crime a massive problem, tourism is likely to remain concentrated in small outlying island resorts for the near future.

Papua New Guinea: Economic Structure 2000			
Export Partners	%	Import Partners	%
Australia	30	Australia	50
Japan	11	Singapore	20
China	6	Japan	4
Germany	4	New Zealand	4
South Korea	4	Indonesia	3
UK	3	Malaysia	3
Philippines	1	US	2
US	1	-	
Export commodities: oil, gold, copper ore, palm oil, coffee, cocoa, crayfish, prawns			
Import commodities: machinery, transport equipment, manufactured goods, food, fuels, chemicals			


Papua New Guinea (Country Analysis) : Economic - Recent Updates


1. 03/12/2003 - **COUNTRY** Prime Minister of Papua New Guinea Threatens to Default on Foreign Loans(Main Story)


2. 26/11/2003 - **COUNTRY** Government of Papua New Guinea to Impose Temporary Tax on Imports(In Brief)

3. 19/11/2003 - **COUNTRY** Independent Audit in PNG Reveals Budget Deficit(In Brief)


4. 27/10/2003 -  **COUNTRY** **Malaysia Courting Papua New Guinea Away from Australia** (In Brief)


5. 22/10/2003 -  **COUNTRY** **US\$30m Processing Plant Planned for Papua New Guinea** (In Brief)


6. 09/10/2003 -  **COUNTRY** **Summit of Industry Leaders in Papua New Guinea Calls for Reform**(In Brief)


7. 08/10/2003 -  **COUNTRY** **Rumours of Lost Gold in Papua New Guinea Jungle Could Do More Harm than Good**(In Brief)


8. 07/10/2003 -  **COUNTRY** **Crisis Brewing in Papua New Guinea Over Issue of Work Permits to Foreigners**(In Brief)

9. 25/09/2003 -  **COUNTRY** **Federal Budget Woes in Papua New Guinea Will Require Further Spending Cuts**(In Brief)


10. 18/09/2003 -  **COUNTRY** **Failure to Adopt Trade Reforms Costs Papua New Guinea US\$220m Annually**(In Brief)

11. 17/09/2003 -  **COUNTRY** **Sale of Government-Run Businesses in Papua New Guinea Raises US\$240m** (In Brief)

12. 01/09/2003 -  **COUNTRY** **Australia Outlines New Approach to Relationship with Papua New Guinea**(In Brief)

13. 21/08/2003 -  **COUNTRY** **Tax Increases Likely in Papua New Guinea as Government's Financial Crisis Deepens**(In Brief)

14. 13/08/2003 -  **COUNTRY** **Two Regional Trade Agreements Ratified by Papua New Guinea**(In Brief)

15. 25/07/2003 -  **COUNTRY** **Mining Industry Leaders in Papua New Guinea Optimistic About New Opportunities**(In Brief)

Legal Environment

Current as of Thu 18 Dec 2003

Legal risks: 2.75

Papua New Guinea places a number of restrictions on the type of business in which foreigners can engage. Nevertheless, the legal and judicial system works reasonably well.

Papua New Guinea has a Western legal system inherited primarily from Australia and based on UK common law. The national judicial system comprises the Supreme Court, the National Court and other courts in the country. The Supreme Court is responsible for all matters concerning the interpretation of the constitution and is the final court of appeal.

A foreign enterprise (one that is 50% or more owned by non-citizens or that is controlled by non-citizens) must be certified by the Investment Promotion Agency (IPA) before it may conduct business. In addition, any large-scale investment proposal requires consultation with a number of government departments and may also be regulated by specific sectoral legislation.

Certain activities are reserved for locally-owned or joint-venture enterprises. Generally, the restrictions relate to the scale of the activity. Therefore, small-scale agriculture, hunting and coastal fishing, the manufacture of artefacts and the operation of small retail outlets are restricted. Of more relevance to the foreign investor are restrictions on companies that provide various mining and construction services, and on the coastal transportation of bulk products or goods. As part of a World Bank Structural Adjustment Programme (SAP), the government has pledged to eliminate the Reserved List progressively. Business activities relating to manufacturing and construction were removed from the Reserved List in 1995. Elimination of the Reserved List has been one of the more controversial aspects of the SAP and there has been little additional progress in reducing the number of reserved activities.

The legal system works reasonably well. The courts do not suffer from government interference, and thus provide a meaningful forum in which to enforce property and contractual rights, though the country does not have a written commercial code.

The APEC Network of Minerals and Energy Data (ANMED) Legal and Regulatory Framework also covers enterprises outside the minerals business and is at <http://www.bmr.gov.au/anmed/png/pngleg.html>

Papua New Guinea (Country Analysis) : Legal - Recent Updates

1. 18/11/2003 -  **COUNTRY** **Government of Papua New Guinea Proposing New Media Ownership Rules**(In Brief)
 2. 28/01/2003 -  **COUNTRY** **Threat to Shut Down Major Mine Grows in Papua New Guinea**(In Brief)
 3. 16/10/2002 -  **COUNTRY** **Supreme Court Ruling Averts Financial Crisis** (In Brief)
 4. 13/07/2001 -  **COUNTRY** **Court Orders Arrest of Opposition Leader** (In Brief)
 5. 11/04/2001 -  **COUNTRY** **Rebel Leader Takes Fight to Court** (In Brief)
 6. 09/04/2001 -  **COUNTRY** **Government Borrowing Illegally from Central Bank** (In Brief)
 7. 22/11/2000 -  **COUNTRY** **Australian Mining Firm Faces New Landowners Lawsuit** (In Brief)
 8. 31/07/2000 -  **COUNTRY** **Free Trade Zones Established** (In Brief)
-

Tax Environment

Current as of Thu 18 Dec 2003

Tax risks: 2.50

Corporate tax rates are high, although the government does offer a number of tax incentives to investors. There is a lack of experienced tax officials.

Tax and Duty Rates

Tax Rates			
Residents		Tax on column one	Percentage on excess
0	K6,000	0	0
K6,000	K16,000	0	25
K16,000	K70,000	K2,500	35
K70,000	K95,000	K21,400	40
K95,000		K31,400	47
Non-residents		Tax on column one	Percentage on excess
0	K16,000	0	25
K16,000	K70,000	K4,000	35
K70,000	K95,000	K22,900	40
K95,000		K32,900	47

Corporate tax rates on non-mining, non-petroleum taxable income are 30% for resident companies and 48% for non-resident companies. Resident companies are also liable to pay dividend tax at the rate of 17%, bringing the effective tax on distributed profits of resident companies to 37.75%.

Taxable income from mining operations is assessed at the rate of 35% for resident companies and 48% for non-residents. The dividend tax raises the effective rate of tax on distributed mining income to 46.05% for resident companies.

Taxable income from petroleum operations is assessed at the rate of 50% for both resident and non-resident companies. There is no liability for dividend tax with respect to dividends paid out of petroleum income.

Customs and duties are the most significant form of indirect taxation in Papua New Guinea. The rates of customs duties range from 0% to 75%. Provincial governments have the right to levy sales tax, although only a limited number do so. Rates range from 1% to 6.5% of the retail selling price of goods, and, in some instances, services. Value-added tax (VAT) was designed to be revenue-neutral when it was introduced in 1999. A Supreme Court ruling in October 2002 threw the system into doubt. The court initially ruled that the VAT system was unconstitutional but later in the same month it overturned this ruling, allowing the system to remain in place until July 2003. VAT revenue accounts for around 25% of total government revenue; had the government been obliged to abide by the earlier ruling it would have prompted a financial crisis.

2003 Budget Highlights

Company tax increased to 30%

Additional Profits Tax (APT) for the mining sector abolished

First tier of APT in the petroleum sector set at 15%, abolished for all petroleum projects

Customs duty removed from major imports for construction of gas projects and set at rates that will start in 2006 for all other imports

No changes to personal income tax rates, but a 25% increase imposed on the taxable values of housing and vehicles

Log export tax set in US dollar values

New bank debits tax to replace current cheque duties, charged at 0.01% on all withdrawals

Fringe benefit tax raised to 25%

The government is facing a ballooning budget deficit and declining revenue projections for fiscal year (FY) 2004, due in part to the massive tax concessions made to the mining and agricultural industries through the so-called Somare Green Revolution initiative. In order to cover shortfalls in the 2003/2004 budgets, the government is considering an unspecified increase in the rate of personal income tax and a 5% increase in sales and services taxes, currently 10% and 15% respectively. The government has already established a new 0.01% fee on all withdrawals from commercial banks. Adding to the financial burden at federal level is the concession made to provincial governments, allowing them to retain 80% of collected goods and services taxes, leaving the federal government with the remaining 20%. The federal government has already had to borrow K\$300m (US\$89m) to bridge budget shortfalls in the current fiscal year, as a result of unreleased loan guarantees from the Asian Development Bank (ADB) and the World Bank. To make matters worse, ongoing concern from Australia - PNG's largest donor country - over widespread public corruption has led the Canberra government to announce a reassessment of how it allocates over A\$300m (K\$600m/US\$178m) in annual aid. These ongoing financial woes are a direct result of the government's inability to exercise strong fiscal discipline and political leadership.

The government offers a number of incentives involving exemption from or deferment of tax liability for investors. These include:

- an export-income incentive;
- a pioneer-industries scheme;
- a rural-development incentive;
- a wage subsidy;
- tax relief for staff-training costs; and
- import-duty exemptions and drawbacks.

All these incentives are subject to certain conditions.

Many mining companies were irked by the imposition of a special tax on the industry. However, under former Prime Minister Morauta the government committed to phasing out the mining levy over the period to year-end 2005. It is not yet clear whether the new government will stick to this target, but in its 2003 budget it abolished APT for the sector. The levy was reduced by one-quarter in the 2002 budget, with a view to removing it entirely within four years. New projects will not be subject to the levy. Taxes on the forestry sector are being reassessed; in the 2002 budget, plantation logs were made exempt from log export tax and the log export tax itself was cut by 5% across the board, while the 2003 budget implemented a policy in which export taxes on logs were set in US dollar values.

The Morauta government made progress towards passing a fiscal stability clause that would ensure tax stability for major projects over a period of many years, though there are questions as to how companies could counter any state decision to revoke such a clause. Again, the Somare government's position on this issue is unclear.

Vanimu, near the border with Irian Jaya, Indonesia, is one of a number of centres with free-trade-zone status, including Daru in Western Province, Buka in North Solomons Province and Kerema in Gulf Province. The zones are in a very early stage of development and as yet they have garnered little foreign interest.

A shortage of trained and experienced officials handling taxation matters can create difficulties. However, these problems are generally not insurmountable.

Papua New Guinea (Country Analysis) : Tax - Recent Updates

1. 26/11/2003 -  **COUNTRY** **Government of Papua New Guinea to Impose Temporary Tax on Imports**(In Brief)

2. 19/11/2003 -  **COUNTRY** **Independent Audit in PNG Reveals Budget Deficit**(In Brief)

3. 13/11/2003 -  **COUNTRY** **Government of Papua New Guinea Proposes New Local Tax**(In Brief)

4. 21/08/2003 -  **COUNTRY** **Tax Increases Likely in Papua New Guinea as Government's Financial Crisis Deepens**(In Brief)

5. 19/06/2003 -  **COUNTRY** **Customs Officers Seize Goods Entering Papua New Guinea from Australia**(In Brief)

6. 01/10/2002 -  **COUNTRY** **Supreme Court Rules VAT Unconstitutional** (In Brief)

7. 28/11/2001 -  **COUNTRY** **Budget 2001: Free Education Pledge Takes Centre Stage**(In Brief)

8. 25/05/2001 -  **COUNTRY** **Mining Giant Slams Tax Environment** (In Brief)

9. 31/07/2000 -  **COUNTRY** **Free Trade Zones Established** (In Brief)

Operational Environment

Current as of Thu 18 Dec 2003

Operational risks: 3.50

Official government policy towards foreign investment is welcoming. Nevertheless, major projects are often stalled by problems with approval at high levels. The bureaucracy is cumbersome, and corruption is on the increase. Land-owner disputes can cause particular headaches.

Attitudes to Foreign Investment

The government of Papua New Guinea (PNG) officially welcomes foreign investment, subject to conditions set out in the Investment Promotion Act. Large-scale investment is generally concentrated in the mining and petroleum sectors. The country is also rich in renewable natural resources, including forests and fisheries. The government places a premium on increasing the downstream processing of these resources. In addition, government policy favours the privatisation of public business entities. In reality, progress towards this goal has been slow.

Despite its welcoming attitude to foreign investment, those investors who are not deterred by the poor law and order situation find the process of trying to enter the market frustrating. Large-scale developments tend to be contentious and quickly become political issues necessitating cabinet decisions. Decision-makers have frequently been charged with corruption by the local and Australian media. Nevertheless, the government has shown that it is prepared to introduce legislation to protect foreign businesses that are in the country's interest. The most important example of this is the Compensation (Prohibition of Foreign Legal Proceedings) Act 1995, which was initiated by the Department of Mining and Petroleum because of the importance of mining and petroleum projects for Papua New Guinea. It feared that a foreign court could assess damages that could be greatly in excess of what would be appropriate in Papua New Guinea and that could have a serious effect on the country's economy.

In 1992 the government created the Investment Promotion Authority (IPA) in order to facilitate and certify foreign investment. The IPA is often the first point of contact for potential investors and provides them with information and assistance in obtaining relevant government approvals (see website address below).

The accession of Sir Mekere Morauta to the post of prime minister in July 1999 saw a more dramatic shift in favour of foreign investment. The replacement of Morauta by Michael Somare following elections in July 2002 has been a cause for concern, with investors fearing that Somare will govern much as he did during his previous tenure as prime minister, largely with little regard for sound economic management. That said, the NA was a key member of Morauta's ruling coalition prior to May 2001, and delivered a considered and well received first budget in November 2002. Investors will judge the NA on its ability to deal with the key issues afflicting the economy and the nation as a whole, tackling corruption and sustaining economic reform being the two main tasks that need to be addressed. Morauta introduced a phased reduction of the controversial mining levy, which should be abolished by 2006. New projects will not be subject to the tax. In addition, progress has been made towards the passage of a fiscal stability clause that would guarantee a stable tax regime over several years for major projects.

In 2000 the cabinet adopted a preliminary report by the International Advisory Group for Privatisation that recommended sweeping privatisation of government-owned enterprises. Those mentioned by name as 'eating tax payers money' included Finance Pacific, the telecoms provider Telikom, the national carrier Air Niugini and electricity provider Elcom. The only real achievement on the privatisation front to date has been the sale of the PNG Banking Corporation; in his new role, Somare suspended the privatisation of the national telecoms company, PNG Telikom, the national airline, Air Niugini, and the state power and water utilities in September 2002. In an apparently populist move, Somare declared that the companies made money for the government the last time he was in power and that he could therefore see no reason why they should suddenly be making losses and need to be sold. Considering the economy's poor state and donor pressure, however, Somare is likely to be forced into a rapid policy reversal on this issue.

Labour

Papua New Guinea suffers from high levels of illiteracy, and skilled labour is in short supply. Only 1-2% of the population speak English, despite it being the national language. Unskilled labour is, however, in plentiful supply. The union movement is weak, but strikes still occur occasionally. In May 2002 the PNG Waterside

Workers Union (PNGWWU) downed tools in a strike for higher wages, affecting port operations in Port Moresby and Lae, and further undermining the country's reputation among international traders. Wages are deregulated, subject to a low minimum wage, though labour costs for skilled workers especially are high by regional standards. Many overseas firms import management personnel.

Australian researchers have suggested that Papua New Guinea may be on the verge of an AIDS epidemic, which could reduce the size of the potential workforce by 40% in the next 18 years. If African examples of AIDS crises are any example, companies would be expected to bear a significant proportion of the costs of treating their workforce as employees fall sick. Real GDP could be cut by 7.5%. However, these findings are speculative, based on cultural trends rather than current infection rates, which remain low by regional standards.

Bureaucracy

Investors often complain that the bureaucracy in Papua New Guinea is cumbersome, with difficulties and delays in obtaining necessary clearances to do business. The weak bureaucracy is a result of a skills shortage and a lack of effective discipline.

Corruption

Corruption by public officials is frequently reported in the media and appears to be increasing. Some US firms have attributed delays in receiving investment approval to the fact that they have refused to pay bribes. Bribery is infrequently prosecuted. Various independent investigations have reported the failure of national and provincial government officials to follow normal competitive tendering procedures in awarding contracts for major infrastructure projects. The Woods tribunal, which purported to investigate corruption among politicians, was treated with contempt by many in early 2002. Several legislators, knowing that they would probably lose at the next election anyway due to extremely low incumbency rates, simply stepped down early, as the tribunal was only mandated to question sitting MPs.

There are regular corruption scandals. The most high-profile of these include the arrest of a former World Bank official in 1999, who was later charged with misappropriating US\$45m of funds; an inquiry in 2000 into the collapse of the National Provident Fund, during which it emerged that the Fund chairman had extorted US\$896,000 in commissions and kickbacks from Japanese contractors, Kumagai Group; and the revelation in 2001 that US\$21m, most of it intended for road maintenance work, had been lost through fraud and bogus claims.

Infrastructure

Communications

International telephone, telegraph, telex, facsimile and postal services are reasonably reliable. Cellular telephone services were introduced in the Port Moresby area in 1996. Internet access is available, but at high cost.

Air Travel

There is one international airport at Port Moresby known as Jackson Field. In addition, there are over 400 other airports and airstrips throughout the country. The national carrier, Air Niugini, operates scheduled domestic cargo and passenger services within the country and international services to Australia, Indonesia, the Solomon Islands, Manila, Singapore and Hong Kong. Several smaller carriers offer scheduled domestic services and charters. Qantas flies regularly to Port Moresby from Sydney, Brisbane and Cairns. Most internal travel of any distance has to be done by air as the road network is limited.

Road Travel

There has been little road development in Papua New Guinea. The maintenance of existing roads is poor. Road transportation is further complicated during wet weather when roads and bridges can be closed due to landslides and floods.

Ports

Sea-freight costs to and from Papua New Guinea are high because the country does not lie on any major sea routes and generates little cargo itself. Therefore service to and from the rest of the world is infrequent.

The two main ports in Papua New Guinea are Port Moresby and Lae, which together handle around 70% of the country's imports. Other important ports include Madang, Wewak and Rabaul. Because of the lack of roads between major population centres, products must be unloaded at various ports and then transported inland by road. Port Moresby serves the National Capital District and Central Province, Lae serves Morobe province and the Highlands.

Electricity

Electric power reaches only about 12% of the population. In addition, electricity costs are high, and power is subject to interruption and fluctuations. The major supplier is the state-owned Electricity Commission of PNG (Elcom). Hydroelectric schemes provide around 30% of power, with major plants being located at Port Moresby, Ramu River and Gazelle Peninsular.

Natural Hazards

Papua New Guinea suffers from numerous natural hazards. It has been hit by volcanic eruptions, tidal waves, storms and flooding through the 1980s and 1990s. Moreover, in the late 1990s the worst drought for 50 years had a substantial economic impact, forcing Porgera mine to cease milling operations, due to water shortages, and Ok Tedi mine to stop shipping concentrate. Similar drought fears in 2002 resulted in production warnings, again from the Ok Tedi mine.

Activism

Land Disputes

Land disputes are endemic in Papua New Guinea because most land is communally held, and there is no widely established system of land registration. Therefore investors must be careful to pay particular attention to landowner concerns and community relations. Demands for compensation by landowners are increasingly accompanied by threats of violence or sabotage.

Landowner activity began in 1988 with protests by Bougainville landowners against the Panguna copper mine, run by Australian mining company CRA. Panguna copper-mine landowners have staged a series of campaigns demanding compensation from foreign companies for alleged environmental abuses or higher stakes from the government in projects that affect their livelihood. The latest twist in their campaign was revealed in April 2001, when it was announced that they would be suing mining giant Rio Tinto (which was formed out of a merger involving CRA) in the US courts on a range of charges from murder to massive environmental damage.

Other incidents include:

- In August 1996 landowners who were dissatisfied with the operators of the Porgera gold mine staged a number of civil disturbances. The conflict was over the distribution of compensation payments under the Water Resources Act. The disturbances resulted in damage to some Porgera joint venture (JV) property and the death of two local people. However, there was no disruption of production at the mine.
- In early 1996 landowner groups threatened to disrupt operations at the Kutubu petroleum project (operated by Chevron Niugini), unless the government met their demands that additional equity in the project be transferred to them from the state's share. The dispute was eventually resolved amicably, without any disruption to production at the oil field.
- In the mid-1990s the Ok Tedi mine run by BHP Billiton in Western Province became the focus of a US\$3bn compensation action. The claim was made on behalf of villagers who said that they had suffered from pollution from the mine. The case was dropped in 1996 after BHP Billiton drew up a major compensation settlement with the villagers.

Land Disputes Case Study

In January 2001 'landowners' occupied wells in the Moran oil field, forcing owner Chevron Niugini to shut down production and causing lost production of 13,000 barrels per day.

The clash came despite close co-operation with the government and land owner representatives - who had signed agreements earlier in the month giving the go ahead for the project. The rival group of landowners was supposedly invited to the discussions that led to these agreements but is said to have refused to attend.

However, with government and local support - and extra police flown to the area - the disputers were swiftly forced to withdraw. Production was able to resume within a week.

The Ok Tedi case aroused international interest and made landowners in Papua New Guinea more politically

aware. This has led to a spate of speculative claims by landowners at other projects. Campaigns are becoming more sophisticated, and claims are moving towards demands for greater equity stakes in major projects.

The Ok Tedi dispute reopened in the Australian courts after landowners claimed that BHP Billiton had not ceased dumping poisonous waste products into local rivers. In the end the case was dropped in lieu of the villagers receiving shares. Even this has proved contentious, and in January 2003 Bob Danaya, the governor of the Western Province, threatened to join landowners and shut down the Ok Tedi mine unless its owners, WRML, provided information regarding the company that owns 52% of shares in the project. BHP Billiton transferred the shares to Singapore-based PNG Sustainable Development Program Ltd (PNGSDP) during a deal struck with the previous government in 2002. PNGSDP now holds the shares in trust, but Danaya feels that the provincial government should be involved in the process to ensure that the shares remain safe when OTML leaves, allowing the provincial government to take over management of the process.

Practical Advice

- English is the language of business and government, but it is nevertheless spoken by less than 2% of the population.
- The use of first names in business is common, and attitudes towards punctuality can be similarly casual.
- While there is little interest in national affairs in many areas, tribal and local allegiances remain strong and may have to be negotiated sensitively in the conduct of deals.
- Papua New Guinea is host to many tropical diseases, and the latest medical advice should be sought on which vaccines are needed before travelling to the country. Typhoid and Hepatitis-A and -B are particularly prevalent.


Useful Links

- Government Investment Promotion Agency: www.ipa.gov.pg
- Department Responsible for Mining: www.mineral.gov.pg
- Port Moresby Chamber of Commerce and Industry: www.pomcci.org.pg

Papua New Guinea (Country Analysis) : Operational - Recent Updates


1. 02/12/2003 -  **COUNTRY** **AIDS Report Ranks Papua New Guinea Highest in the Pacific**(In Brief)
2. 13/10/2003 -  **COUNTRY** **Journalists Investigating Claims of Papua New Guinea Gold Cache are Seized by Police**(In Brief)
3. 09/10/2003 -  **COUNTRY** **Summit of Industry Leaders in Papua New Guinea Calls for Reform**(In Brief)
4. 08/10/2003 -  **COUNTRY** **Rumours of Lost Gold in Papua New Guinea Jungle Could Do More Harm than Good**(In Brief)
5. 07/10/2003 -  **COUNTRY** **Crisis Brewing in Papua New Guinea Over Issue of Work Permits to Foreigners**(In Brief)
6. 03/10/2003 -  **COUNTRY** **Flood of Illegal Immigrants to Papua New Guinea May Prompt Crackdown**(In Brief)
7. 18/09/2003 -  **COUNTRY** **Failure to Adopt Trade Reforms Costs Papua New Guinea US\$220m Annually**(In Brief)
8. 11/09/2003 -  **COUNTRY** **Security Minister in Papua New Guinea Calls for Overhaul of Police Force**(In Brief)
9. 27/08/2003 -  **COUNTRY** **European Union Issues Ultimatum to Papua New Guinea Over Missing Aid Money**(In Brief)

10. 13/08/2003 -  **COUNTRY** **Two Regional Trade Agreements Ratified by Papua New Guinea**(In Brief)

11. 06/08/2003 -  **COUNTRY** **Australia Rules out Intervention Force for Papua New Guinea**(In Brief)

12. 30/06/2003 -  **COUNTRY** **PNG Power Declared Insolvent** (In Brief)

13. 19/06/2003 -  **COUNTRY** **Customs Officers Seize Goods Entering Papua New Guinea from Australia**(In Brief)

14. 06/06/2003 -  **COUNTRY** **Prime Minister Announces Measures to Revitalise Papua New Guinea's Agricultural Sector**
(In Brief)

15. 15/04/2003 -  **COUNTRY** **US Oil Company Pulls Out of Papua New Guinea, Raising Industry Fears**(In Brief)

Security Environment

Current as of Thu 18 Dec 2003

Security risks: 4.25

Papua New Guinea suffers from chronic law-and-order difficulties, making the country an extremely dangerous place in which to operate. Crime in the cities is rampant and is generally accompanied by high levels of gratuitous violence. Law and order in the countryside is enforced only loosely, with certain regions in the Highlands bordering on anarchic. Violence in the Southern Highlands during the 2002 election campaign proved so endemic that many seats were unable to return a candidate. Secessionist activity has decreased in recent years; a peace process has been firmly established on the island of Bougainville, where most separatist activity was concentrated. Indonesian West Papua's insurgency continues to pose problems on the western border.

Key Security Threats and Areas to Avoid

- The highest level of security awareness is necessary from the moment of arrival in the country.
- Cities are especially dangerous, notably Port Moresby and Lae. Ethnic clashes in February 2003 resulted in gun fights in Lae, during which six people died and many more were injured before the police managed to bring the situation under control. The countryside can be safer, but a local companion or guide is essential on all journeys.
- Law enforcement is weak, and some police forces may have connections with criminal gangs. Control in the highlands regions is particularly poor.
- Crime is frequently accompanied by extreme and gratuitous violence. Women are shown no particular mercy, and many foreigners have been shot, stabbed and even raped in the course of robberies.
- Tribal warfare sometimes erupts in the countryside, though foreigners are rarely affected.
- The Bougainville civil war has calmed with the success of the peace process, and travel to the island is possible with appropriate precautions. Visitors should be sensitive to the fact that 'exploitation' by a foreign company was the spark for the civil war.

Crime

The high level of crime in Papua New Guinea, and its often violent nature, represents a major problem for foreign business. It arises from a number of factors, including social deprivation, a history of tribal warfare, tensions between the police and the military and the existence of the 'payback' system. Payback involves relatives of victims (for example from road accidents) feeling morally bound to meet out physical retribution as revenge. Car drivers in particular should remember that legal fault does not need to be established.

The main centre of criminal activity is the capital, Port Moresby, although other urban centres, such as Lae, are also subject to major problems. In addition, law and order is enforced only loosely in the countryside, where highway robbery at roadblocks has been a common problem for businesses transporting goods.

Both foreigners and locals are targets of crime. Attacks can be purely opportunistic or specifically targeted. Women are especially vulnerable; they should dress conservatively and avoid travelling alone. No-one should travel alone at night. Disturbingly, even the most secure premises are sometimes affected; in January 2003 a group of armed men targeted the home of an Australian expatriate, forcing open a corrugated security fence before using a car jack to open an iron security grill on the window and removing louvre blades to gain access to the house. The house was burgled and the expatriate beaten to death. Perhaps the most unpleasant feature of crime in the country is that it is often accompanied by gratuitous and extreme violence. Firearms or more primitive weapons (knives and spears) are used frequently in robberies, and female robbery victims are also often raped. Foreigners should conceal any valuables carried.

Raskol gangs (armed criminals) are responsible for most of the crime. They are involved in large-scale theft from private residences and commercial enterprises, hold-ups, car-thefts, rapes, muggings and the drug trade. There are, on average, three armed robberies in Port Moresby each day. By night there are an estimated 40 house robberies. In addition, it is believed that politicians and local businessmen are using *raskols* to exact 'paybacks' on their rivals. Police efforts to prevent *raskols* moving in and out of the city have been largely unsuccessful.

Most visitors will avoid public transport. Passengers in cars or taxis must take specific precautions, keeping windows wound up and doors locked whenever their vehicle stops, not stopping too close to the vehicle in front at traffic lights and being especially vigilant when entering or leaving the vehicle. If involved in an accident they

should not stop, but should instead continue driving and report the incident immediately at the nearest police station.

It is possible to carry out business, but requisite security precautions add to the cost significantly. Companies must implement extensive measures to protect assets and employees, including security guards and high fences.

Pyramid schemes have caused severe trouble in some parts of the country, with investors being fleeced of several million dollars worth of funds.

Extortion

Extortion is rare in Papua New Guinea.

Kidnapping

Kidnapping is rare in Papua New Guinea.

Terrorism

There is no threat from terrorism within Papua New Guinea. However, a report that was released in March 2003 suggested that Papua New Guinea was rapidly becoming a failed state and, as such, could potentially act as a base for terrorists intent on attacking Australia. The report stated that violent crime had become a major problem, rendering some parts of the country uncontrollable, and that land and sea borders remain unmonitored.

Political and Ethnic Violence

Election Violence

At least 30 people were killed in violence related to the 2002 general election. Almost all the deaths occurred in the Highlands region and took place as rival candidates attempted to burn or steal ballot boxes. Some candidates in the region were kidnapped and held hostage, often along with their supporters. Retaliation included killings and gang-rapes. Security forces were unable to restore order in the region over a period of several weeks; indeed, a few soldiers were themselves subsequently arrested for stealing ballot boxes. Worst affected were the Southern Highlands, especially Chimbu province. Voting in Port Moresby and Lae passed relatively peacefully. Fresh elections in May 2003 passed off relatively peacefully, with the government ensuring much higher levels of security.

Secessionist Groups

The Bougainville Revolutionary Army (BRA) led the fight for secession for the island of Bougainville. The insurgency grew out of a violent landowner campaign against the Panguna copper mine in 1988, although the island had declared itself independent as early as two weeks before PNG's independence in 1975. The BRA is thought to have around 1,000 active members. A permanent ceasefire agreement was signed between the BRA and the government in January 1998, and progress towards peace has been gradual but constant. In early 2002 PNG's parliament finally completed voting that gave legal force to the autonomy deal which underpinned the peace settlement and formally drew a line under the rebellion. This grants the island wide-ranging autonomy in areas like policing, tax and judicial systems, as well as essentially removing the PNG army presence from Bougainville. Bougainville will also be able to vote on a referendum including full independence as an option within 10-15 years. In the meantime, rebel arms are being gradually decommissioned - a process that - as of May 2003 - was said to have netted more than 90% of the weapons thought to be in circulation. International peace monitoring groups are scheduled to leave the island at the end of June 2003, which has prompted fears of emerging power struggles between former rebel groups, vying for leadership positions.

The Free Papua Movement (OPM) campaigns for the independence of the West Papua region of Indonesia, known previously as Irian Jaya. The people of West Papua are ethnically related to the Papuans. The OPM operates on the western border of Papua New Guinea.

Muslim Minority

In November 2002 attackers targeted the main mosque in the capital, Port Moresby, prompting fear among the Muslim community of a new-found religious intolerance. The attack followed Deputy Prime Minister Allan

Marat's comments that some religions should be banned because they were violent. At the time it was speculated that he was referring to Islam and that consequently the comments and the attack might be related. Port Moresby's law-and-order problems are related more to the social situation and it is unusual for individuals to be targeted because of their ethnicity. If the mosque attack represented the beginning of an anti-Muslim campaign, this would add a further dimension to the country's already-poor security conditions.

Civil Disorder

Security concerns were raised by the army's March 2001 mutiny and the descent into violence of the June 2001 student-led protests against the economic reform programme. Three students were shot dead in the latter event, and many more were injured, though there were no casualties during the mutiny. Foreigners were not targeted or injured in either of the two incidents, but travel warnings were issued by governments whose citizens travel frequently to the country - notably Australia and New Zealand, warning against non-essential travel and advising resident citizens to keep to their homes during the crises. While anti-government protests have traditionally been relatively peaceful in Papua New Guinea, the accompanying lapses in civil order can be dangerous for those caught up in them, and caution is advised at times when government control is challenged by mass demonstrations. The smaller-scale mutiny in March 2002 at the Moem barracks in Wewak had fewer implications for civil order, confined as it was to the military compound.

External Threats

The country is located within the so-called 'arc of instability' that encompasses much of the South Pacific, including Fiji and the Solomon Islands. PNG itself has been fairly stable since the signing of the Bougainville peace accords.

On the Indonesian side of the 'arc', there are concerns over the stability of Indonesian West Papua. While the independence movement there has yet to become as violent as others in Indonesia, if tensions were to escalate dramatically PNG may face an influx of refugees. It is doubtful that Papua New Guinea's finances would be able to cope with the resulting demands placed on it without substantial international assistance.


Useful Links

- Australian Department of Foreign Affairs and Trade Travel Advice: www.dfat.gov.au/consular/advice
- US State Department Travel Warnings: travel.state.gov/travel_warnings.html
- UK Foreign Office Travel Advice: www.fco.gov.uk/travel/countryadvice.asp

Papua New Guinea (Country Analysis) : Security - Recent Updates

1. 08/12/2003 -  **COUNTRY** **New Zealand Police Deployed to Papua New Guinea's Restive Bougainville Province**(In Brief)
 2. 18/11/2003 -  **COUNTRY** **Government of Papua New Guinea Proposing New Media Ownership Rules**(In Brief)
 3. 14/11/2003 -  **COUNTRY** **Villagers March on Lae to Protest PNG Lawlessness** (In Brief)
 4. 07/11/2003 -  **COUNTRY** **Renewed Violence Befalls Bougainville Province in Papua New Guinea**(In Brief)
 5. 13/10/2003 -  **COUNTRY** **Journalists Investigating Claims of Papua New Guinea Gold Cache are Seized by Police**(In Brief)
 6. 08/10/2003 -  **COUNTRY** **Rumours of Lost Gold in Papua New Guinea Jungle Could Do More Harm than Good**(In Brief)
 7. 03/10/2003 -  **COUNTRY** **Flood of Illegal Immigrants to Papua New Guinea May Prompt Crackdown**(In Brief)
 8. 11/09/2003 -  **COUNTRY** **Security Minister in Papua New Guinea Calls for Overhaul of Police Force**(In Brief)
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9. 12/08/2003 -  **COUNTRY** **Bougainville Peace Process Reaches Milestone in Papua New Guinea**(In Brief)

10. 06/08/2003 -  **COUNTRY** **Australia Rules out Intervention Force for Papua New Guinea**(In Brief)

11. 03/07/2003 -  **COUNTRY** **Bougainville Hardliners Threaten to Disrupt Fragile Peace in Papua New Guinea**(In Brief)

12. 18/06/2003 -  **COUNTRY** **Another Step Towards Lasting Peace in Bougainville** (In Brief)

13. 12/03/2003 -  **COUNTRY** **Report Warns Papua New Guinea's Failure Poses Terror Risk to Australia**(In Brief)

14. 11/03/2003 -  **COUNTRY** **Minister Suspended on Gun Charges in Papua New Guinea**(In Brief)

15. 06/02/2003 -  **COUNTRY** **Six Die in Fighting in Papua New Guinea's Second-Largest City**(In Brief)

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