

# BTI 2012 | Papua New Guinea Country Report

<b>Status Index</b>	1-10	<b>5.66</b>	# 63 of 128	
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scale: 1 (lowest) to 10 (highest)    score    rank    trend

This report is part of the Bertelsmann Stiftung's Transformation Index (BTI) 2012. The BTI is a global assessment of transition processes in which the state of democracy and market economy as well as the quality of political management in 128 transformation and developing countries are evaluated.

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Please cite as follows: Bertelsmann Stiftung, BTI 2012 — Papua New Guinea Country Report. Gütersloh: Bertelsmann Stiftung, 2012.

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## Key Indicators

Population	mn.	6.9	HDI	0.466	GDP p.c.	\$	2472
Pop. growth <sup>1</sup>	% p.a.	2.3	HDI rank of 187	153	Gini Index		-
Life expectancy	years	62	UN Education Index	0.335	Poverty <sup>3</sup>	%	-
Urban population	%	12.5	Gender inequality <sup>2</sup>	0.674	Aid per capita	\$	61.4

Sources: The World Bank, World Development Indicators 2011 | UNDP, Human Development Report 2011. Footnotes: (1) Average annual growth rate. (2) Gender Inequality Index (GII). (3) Percentage of population living on less than \$2 a day.

## Executive Summary

During the period under review, Papua New Guinea (PNG) made little progress toward providing its citizens with greater freedom of choice by improving the state of democracy and its market-based economy. Although the economy continued to improve and the country experienced a decade of continuous growth, the lives of its ordinary citizens have not improved marginally. Poverty is still widespread. There have been some positive developments during the period under review. These include: Continuity in government leadership under Prime Minister Sir Michael Somare (Somare might complete a second five-year term despite the fact that most of his predecessors were forced from office within a two-year period); economic recovery; largely sound economic policies; stability in the exchange rate; an increase in foreign exchange reserves; peace on the war-torn island of Bougainville; nascent signs of stability in political parties and some improvements in civil society. The institutional hardware of a market economy is firmly in place. The most positive news in the period under review is the final signing of the liquefied natural gas project (LNG) project. This project is expected to pump \$30 billion into the PNG economy over the next 30 years and contribute an additional 20% to the country's GDP. Many observers were pleasantly surprised when the Somare government was able to secure the final signing despite earlier indications that landowner opposition might derail the project. Observers/commentators have expressed caution, saying that the LNG project is moving too fast with little leeway for the need to prepare ordinary people for its impact, especially its knock-on social effects in rural areas. If the money generated by the project is utilized properly, there is a real chance that the country can undergo a profound change for the better. Nevertheless, PNG continues to face some deep-rooted problems, such as its low level of socioeconomic development, tribal wars, law and order breakdown in most parts of the country, and high levels of corruption. Per capita income is currently lower than it was at the time of independence. As long as the problem of high-level corruption is not dealt with, and incumbent members of parliament and influential individuals benefit greatly from the political status quo, there are severe limits on genuine reform and therefore a high degree of change in general. With general

elections due in 2012, the country is heading towards a period of uncertainty. Elections in some parts of the country usually lead to violence and subsequently a change of government.

## History and Characteristics of Transformation

Since achieving independence from Australia in 1975, Papua New Guinea has nurtured a relatively open economy. Dual in nature, the economy includes a small formal economy and a much larger informal economy in which subsistence farming accounts for the bulk of economic activity. Nearly 85% of the population resides in rural areas, and annual population growth is relatively high at approximately 2.5%. The formal sector provides a rather narrow employment base for those engaged in mineral production, manufacturing, the public sector, and service industries such as finance, construction, transportation and utilities. The rapid urban growth underway since independence is related to high levels of urban unemployment, high crime rates and other related social problems. Papua New Guinea's economic growth has relied heavily on the mining and petroleum sectors. These two sectors combined generate approximately 20% of government revenue and 60% of export revenue. Agriculture, which accounts for about one quarter of exports, has in recent years expanded through cash crops such as coffee, palm oil, cocoa and copra. The other major export is raw timber logs. Politics in Papua New Guinea have been marked by two distinct features, the first being the fact that only one government (Somare's) has completed the full term for which it was elected. The second feature has been the high levels of corruption. On average, governments in Papua New Guinea last no longer than three years. Of the 12 governments elected since 1977, three governments have been ousted through votes of no confidence, seven have been removed through national elections, and the remaining two ejected for other reasons. During this period, the threat of no confidence votes jeopardized cabinet stability and durability. Weak political parties lacking a mass support-base created a situation in which members of parliament had little political legitimacy and were therefore susceptible to corruption. This pattern was broken by Prime Minister Sir Michael Somare, who was first elected in 2002 and again in 2007 for a second term. To facilitate stability, the government of Sir Mekere Morauta (1999 – 2002) introduced the Organic Law on Political Parties and Candidates (OLIPPAC), which makes it extremely difficult for members of parliament to switch parties or resign from their party. This law effectively makes it much more difficult to remove a sitting prime minister through a vote of no confidence which previously was often brought about by massive defections. The OLIPPAC itself had sections nullified by a Supreme Court ruling in 2010 on the grounds of breach of the National Constitution. Nevertheless, corruption is present at the top echelons of government and bureaucracy, and it is the single biggest cause of the country's decline since independence. Huge sums of money have disappeared into the pockets of politicians and public servants or have been misspent by successive governments. There is very little political will to fight corruption as it permeates every layer of society, politics and bureaucracy. PNG is widely regarded by the international community as a "weak" state.

The BTI combines text analysis and numerical assessments. The score for each question is provided below its respective title. The scale ranges from 10 (best) to 1 (worst).

## Transformation Status

### I. Political Transformation

#### 1 | Stateness

The state's monopoly on the use of force is established nationwide in principle but is challenged by criminal gangs referred to as "raskols" and tribal groups. Raskols operate mostly in urban centers and have access to high-powered weapons. These criminal gangs are also regularly found in rural areas, for example, near resource development sites such as mines. It is important to note that criminal gangs from urban centers are highly mobile and can easily relocate to other parts of the country for brief periods when opportunities arise for them to carry out their activities. Tribal wars are largely concentrated in the highlands. None of these groups are in a position to take over the country, although tribal groups are capable of taking over small territories for limited periods. During the period under review, several highland provinces suffered from tribal wars leading to a shutdown of several towns. The army had to be called in to maintain law and order. In major towns such as Port Moresby, Madang and Lae, raskols are increasing using high-powered guns to fight the police. In the period under review, there were six major bank holdups by raskols.

With the exception of the island of Bougainville, there are no regions in Papua New Guinea where problems with state identity arise. With an estimated 830 distinct linguistic groups, the country is highly fragmented in cultural terms. While the traditional division between the highlanders and those who live along the coast still exists, the country's demographic divisions are now much more fluid. Nevertheless, derogatory stereotypes of highlanders being violent and "backward" persist. As they are geographically as well as culturally closer to the Solomon Islands than mainland Papua New Guinea, the population of Bougainville tried unsuccessfully to gain their independence in the 1970s. In 1989, a war of secession broke out and in 2004, the Papua New Guinea government unveiled a new constitution for the island, granting Bougainvillians greater autonomy. In the period under review, an autonomous provincial government was established. Nevertheless, tensions between the central

Question

Score

Monopoly on the  
use of force

6

State identity

8

government and Bougainville remain, and many among the PNG elite believe that Bougainvillians still aim to create a separate state despite getting political autonomy.

Although the state is secular, the constitution does refer to PNG as a Christian country. Religious leaders from the Protestant and Roman Catholic churches and smaller Christian denominations remain influential. Many political parties claim to be guided by Christian principles. The political process is secular and freedom of religion, by and large, is respected. Because the overwhelming population is Christian (more than 90%), policymakers take church leaders' opinions seriously. Several priests have resigned from their duties with the Roman Catholic Church to pursue a full-time political career, the most prominent one being the former governor of Bougainville, John Momis. There is no manifestation of political rivalry that shows a religious divide. However, reservations are being expressed against other religions such as Islam in particular. There is one mosque in Port Moresby – possibly the only one in PNG.

No interference of religious dogmas  
8

Most analysts consider PNG a weak state in which the state apparatus cannot implement even the most basic policies. The government's most basic operational machinery is either dilapidated or non-existent in many rural areas and the highlands, where tribal conflicts continue. In the past two years, the ability of the state to provide basic services has deteriorated. The law and order situation has also worsened. Crime in all major cities has reached such a serious level that the government is thinking of using the army to undertake police work. Health care is not properly provided beyond the vicinity of major towns and provincial capitals. The tribal wars for which the highland areas are notorious do not occur because of a lack of government machinery, but emanate mainly from traditional animosities which predate the modern state system. However, the limited state presence has failed to stymie these conflicts. There are also cases of poorly designed laws that have curtailed good governance. Changes made to the provincial government system in 1995 further weakened the presence of the state mechanism in peripheral areas, which caused more problems for the central government.

Basic administration  
4

## 2 | Political Participation

Papua New Guinea is a parliamentary monarchy with Queen Elizabeth II as the head of state. She is represented in Papua New Guinea by a governor-general. The governor-general is elected by members of the national parliament and performs ceremonial functions. Executive power lies with the prime minister and the cabinet who depend politically on parliament. There have been both universal suffrage and regular elections since independence. In general, elections are free. In some districts, especially in the highlands and certain coastal regions, massive vote buying, ballot rigging, clan voting, violence, intimidation and cheating are

Free and fair elections  
7

widespread. The lack of security in the highlands and previous history suggests that a free and fair election is not possible in the highlands. Election-related violence occurs during virtually every general election. During the recent Kandep by-election, a dozen people were hurt in election-related violence. Nevertheless, the transfer of power takes place peacefully after election results are announced, and the military and the police have generally refrained from interfering with politics.

While elected leaders have the constitutionally mandated power to govern, this power is in practice often compromised by clan and regional loyalties, powerful business groups and interest groups such as landowners. The problem is compounded by high levels of corruption among senior politicians and a corrupt and inefficient bureaucracy that often lacks the capacity to carry out government decisions, or in some cases, is used by powerful individuals (referred to as “Big Men”) to subvert government policies.

Effective power to govern

5

There are no restrictions on asserting the constitutional right to assemble and establish associations. NGOs play an active role in voter education and civil society. Political and civil organizations such as trade unions can – and do – form freely.

Association / assembly rights

10

There are no restrictions on the freedom of expression for individuals or the mass media. The media often exposes corruption and criticizes national leaders. However, the business interests of media outlets’ owners often restrict content. “The National” daily, which is owned by the logging giant, Rimbunan Hijau (RH), never prints a negative story about RH or the logging industry in PNG. However, the ownership structure of the media is diversified, and there are other newspapers and electronic media that can provide balanced information.

Freedom of expression

10

### 3 | Rule of Law

There are no formal constraints on the separation of powers between key institutions and there is a system of mutual checks and balances in place. However, the weak parliament and strong executive under Sir Michael Somare renders the implementation of checks and balances sluggish and non-systematic.

Separation of powers

7

Therefore, there are problems with parliament’s oversight of the executive. More often than not, the executive branch dominates parliament. A new law has made removing the prime minister more difficult, which in effect enhances the powers of the prime minister to dictate his will to parliament. This law, the Organic Law on the Integrity of Political Parties and Candidates (OLIPPAC), was initiated by the government that preceded Sir Michael’s present reign, and was meant to curb coalition instability in Parliament. With hindsight, the law has had this unintended consequence of strengthening the arm of the executive. Sections of this law have since been repealed by a Supreme Court ruling in July 2010.

Nevertheless, parliament engages in vigorous debates in which government activities and policies are openly discussed. The executive branch's dominance over parliament ensures that most parliamentary committees cannot carry out the oversight responsibilities expected of them, especially as they are to be chaired by members of parliament who are not ministers. Worse still, in a move that facilitated corruption, sitting allowances are given to members of parliamentary committees whether they meet/sit or not.

In recent years, the Somare government tried to interfere in the work of the Ombudsman Commission to stop the Ombudsman from launching an investigation into allegations of breaches of PNG's leadership code.

In the past two years, the judiciary has been hampered by a lack of resources. There are reports of corruption at the lower levels, such as the magistrate level. Several magistrates have been charged with corruption in recent years. Many of the best legal minds stay in the private sector as the public sector does not pay well. Although in general, the judiciary is free of unconstitutional intervention, a recent case has caused concern. There are reports that Prime Minister Somare tried to stop a judicial investigation into his role in the "Moti Affair." The prime minister was accused of helping the then attorney general of the Solomon Islands, Julian Moti, who was wanted by the Australian authorities for child sex charges, to escape by ordering the PNG military to fly him out of the country before he could be arrested on an Australian warrant. There are mechanisms in place for the judicial review of legislative or executive acts, and parliamentarians often take pieces of legislations to the courts for review. Members of parliament have been seen interfering with the judiciary, although these are isolated instances compared to the executive's domination of the legislatures.

Independent  
judiciary

8

Many senior politicians continue to escape prosecution for corruption and abuse of power. Under PNG's Leadership Code, the moment an elected leader resigns, s/he cannot be prosecuted for misconduct even though they can face criminal charges if cases are put together against them. The reality is massive collusion between members of parliament and public servants who can cover for each other. Many senior civil servants who misused public money in the past two years were never charged. In 2009, a large amount of "leave fare" concessions for teachers was misappropriated by senior civil servants but no action was taken. A senior politician who was implicated in relation to massive losses by a national superannuation fund in the late 1990s became finance and treasury minister in 2010.

Prosecution of  
office abuse

4

PNG citizens enjoy full civil rights under the constitution but in reality, marginalized groups such as prisoners, women, children, people living with HIV/AIDS and people with physical disabilities are often openly discriminated against by society at large. There are numerous reports of police regularly beating up suspects and raping women held in custody. In the period under review, several

Civil rights

6

women were killed because they were HIV-positive. In another case, a woman was burned alive because she was accused of using sorcery. In the highlands, the army and police regularly establish “security” road blocks to extort money from travelers. In the past two years the situation has gotten worse, in part due to the coming general elections.

#### 4 | Stability of Democratic Institutions

In the past two years, all the key institutions of state were compromised or experienced interference by the executive. Sir Michael Somare has used his powers to try to stop an investigation into his conduct during the “Moti Affair,” to award “slash funds” from the budget to stop members of parliament defecting and used Parliamentary procedures to illegally re-elect the governor-general of PNG in June 2010. In December of the same year, the PNG Supreme Court ruled that the re-election was illegal. In December 2010, Sir Michael tried to stop the establishment of a Leadership Tribunal against him by going on “leave.” Within six weeks he was back as prime minister.

The sub-national governments have become dysfunctional since the mid-1990s when a new provincial government system was introduced which basically strengthened the arm of governors (and members of the National Parliament too) to control provincial affairs. In some provinces this further exacerbated corruption and poor governance at these levels of government. In effect, this law made the government more centrist than it was prior to 1995 when the law was introduced.

Most people still accept the legitimacy of institutions although they know corruption is rampant. More specific survey data is not available.

Performance of  
democratic  
institutions

3

Commitment to  
democratic  
institutions

7

#### 5 | Political and Social Integration

The PNG party system is fragile. Political parties tend to be driven by personalities and regional or clan ties. All political parties in PNG lack organization, a political philosophy or any real public policies. This state of affairs has resulted in a high level of voter volatility and a high attrition rate of incumbent parliamentarians (well above 50% for the last four elections). It is not uncommon for politicians to form their own parties even if they are the only elected representative. The Organic Law on Political Parties and Candidates (OLIPPAC), aimed at bringing stability to the incumbent government by preventing members of parliament from party-hopping and forcing a vote of no confidence against the prime minister, has not stopped members from defecting in the past two years. In 2010, Deputy Prime Minister Puka Temu defected from the governing coalition with three other members of

Party system

2



parliament. A few months earlier, three members of parliament from the PNG Party defected to the United Resource Party (URP). While the OLIPPAC improved cabinet durability, it did not facilitate the institutionalization of political parties and the national party system, which was not the intent driving the legislation. There are provisions in the legislation that allow political parties to fuse or coalesce with other parties. The larger goal is to establish a structural incentive to form fewer big political parties, and not several smaller parties.

Although there are plenty of interest groups and civil society organizations (CSOs) in PNG, only a handful of them have real access to power and policy-making. The powerful interest groups are those connected with business groups or commerce, based around a region or province and Christian groups. Important groups such as women's rights organizations are often left out of the decision-making process. A major problem for interest groups that individuals and rights organizations face is the lack of support by members of the wider public. They are frowned upon by government and its representatives and often simply lack the skills to properly air their views on issues.

Interest groups  
5

The consent to Western-style democracy among citizens is high, and the constitutional framework is fully accepted by most segments of society. At the same time, however, it is clear that in many regions of the island nation, people do not care much about the everyday functions of democracy. In recent years, some urban intellectuals have started to argue that Westminster-style democracy will not work in the country due to its culture, and that PNG should try "Melanesian" democracy although it is unclear what Melanesian democracy entails.

Approval of  
democracy  
7

There is a low level of trust among the population. Existing trust is still largely based on clan and tribal loyalties called the "wantok" (one talk) system. Women's and environmental groups constitute the most successful indigenous self-help organizations. The lack of trust is also due to people being disillusioned with the role of the government and its inability to provide basic service and development. Still, traditions of self-organization and cooperation are common in many island provinces where people in rural areas assist with community services which include a range of activities such as maintaining law and order, assisting the elderly and church activities.

Social capital  
5

## II. Economic Transformation

### 6 | Level of Socioeconomic Development

Question  
Score

Socioeconomic  
barriers  
4

Poverty and social exclusion are quantitatively and qualitatively extensive, and they are structurally embedded. PNG ranks 148th out of 182 countries on the 2010 HDI and 116th out of 135 developing countries on the Human Poverty Index. The Gini coefficient for PNG is 50.9. Unemployment is estimated to be higher than 70% and more than 80% of the population relies on subsistence farming or the informal economy for their daily needs. The World Bank estimated that in the period 1993 – 2002, approximately 57.4% of the population survived on less than \$2 a day, suggesting that 70% of the population live below poverty line. Infant mortality is ten times higher than in developed countries, and the prevalence of HIV and AIDS is increasing. The latest HIV/AIDS surveillance report says that about 20% of the male population in the highlands are HIV positive or exposed to HIV/AIDS through casual sex. Efforts to eradicate poverty have been hampered by corruption and poor governance. Moreover, ineffective policies, especially in the agricultural sector, have failed to assist the bulk of people living off the land. The coffee industry, which used to provide a lucrative cash crop in the highlands, has been decimated by years of government failure to invest in proper roads and machinery. Many small coffee growers cannot bring their beans to the market as there are no roads to transport them. It is often not economical to use planes.

Economic indicators		2007	2008	2009	2010
GDP	\$ mn.	6329.3	8010.4	7914.6	<b>9480.0</b>
GDP growth	%	7.2	6.7	5.5	<b>8.0</b>
Inflation (CPI)	%	0.9	10.8	6.9	<b>6.0</b>
Unemployment	%	-	-	-	-
Foreign direct investment	% of GDP	1.6	-0.4	5.3	<b>0.3</b>
Export growth	%	-	-	-	-
Import growth	%	-	-	-	-
Current account balance	\$ mn.	56.3	707.9	-585.1	<b>-633.0</b>

Economic indicators		2007	2008	2009	2010
Public debt	% of GDP	-	-	-	-
External debt	\$ mn.	1430.5	1417.5	1572.8	<b>5822.2</b>
Total debt service	\$ mn.	1007.2	974.2	542.8	<b>812.0</b>
Cash surplus or deficit	% of GDP	-	-	-	-
Tax revenue	% of GDP	-	-	-	-
Government consumption	% of GDP	11.3	10.3	10.7	<b>9.5</b>
Public expnd. on edu.	% of GDP	-	-	-	-
Public expnd. on health	% of GDP	3.1	3.2	3.1	-
R&D expenditure	% of GDP	-	-	-	-
Military expenditure	% of GDP	0.6	0.4	0.5	-

Sources: The World Bank, World Development Indicators 2011 | International Monetary Fund (IMF), World Economic Outlook 2011 | Stockholm International Peace Research Institute (SIPRI), Military Expenditure Database 2011.

## 7 | Organization of the Market and Competition

Market competition has a solid institutional framework, but the rules are not consistently or uniformly applied for all market participants. PNG's small economy means that there are oligopolies such as Trukai (rice supply) and firms supported by powerful politicians that often receive favorable treatment from the government. A prime example is the state-owned company Telekom, which uses its status to create barriers for competitors – particularly in the mobile phone and internet services-provider sector. There are also significant barriers to new market entrants, such as high costs in establishing a business, breakdowns in law and order, high banking costs, bureaucratic red tape and corruption, all of which interfere with the functions of a free market. The government's own Investment Promotion Authority (IPA) is jokingly nicknamed the Investment Prevention Agency by the foreign business community. The omnipresence of corrupt political leaders and an incompetent and corrupt bureaucracy often means that businesses willing to pay "facilitation money" compete unfairly. Commissions of inquiry have found numerous instances of public tenders being awarded to companies or individuals who have bribed officials. Large and well-established companies have a significant advantage over newcomers. In recent years, there has been a trend for major companies to buy their smaller competitors and create an even stronger market position for themselves. Examples include City Pharmacy's takeover of the Stop'N'Shop chain of supermarkets. Direct and indirect cross-ownership of businesses is frequent among top businessmen. For

Market-based  
competition

6

example, Mr. Kostas G. Constantinou, one of the most prominent property developers, is also chairman of the Bank South Pacific, chairman of the National Physical Planning Board and director of the one of the largest hotel chains in PNG. All these positions can help his property business. Such faulty corporate governance is the norm rather than the exception. In the period under review, market conditions have worsened as the big companies have consolidated their hold over the economy.

Although there is a formal office of Independent Consumer and Competition Commission (ICCC) in place to regulate against monopolistic behavior, the small size of the PNG economy and historical circumstances have ensured that some of the larger companies continue to operate as oligarchies and monopolies. For example, the state-owned enterprises PNG Power (electricity), Telekom and Ena Ranu (water utility) hold virtual monopolies in their respective sectors. Many of these large companies have strong political connections to protect their position. In the financial sector, three banks, Bank South Pacific (BSP), ANZ Bank and Westpac PNG control more than 90% of the financial market. BSP alone controls at least half.

Anti-monopoly  
policy  
5

The government encourages foreign trade, especially with those states participating in the Melanesian Spearhead Group (MSG) Preferential Trade Agreement, which includes Vanuatu, Papua New Guinea, the Solomon Islands and, recently, Fiji. However, bureaucratic red tape and the high cost of transportation between the island states constitute significant barriers to free trade and foreign investments. In practice, this means large and well-established companies have a distinct advantage over new entrants and small companies. Despite its public pronouncements, the country is not foreign-investor friendly. A maze of regulations and paperwork must be navigated before a foreign enterprise can start operations in Papua New Guinea. The Investment Promotions Authority (IPA), supposedly a “one-stop” center for foreign businessmen, is often sarcastically referred to as the “Investment Prevention Agency.” However, one must not overlook the fact that the country’s topography – particularly that of the island of New Guinea – is among the most rugged in the world. This means that the cost of building and maintaining infrastructure is extremely high, and the capital of Port Moresby is relatively isolated from the rest of the country, accessible primarily by air and sea. All of this must be factored into the high cost of doing business in PNG. The small size of the economy (In 2009, PNG’s share of world total GDP, adjusted by Purchasing Power Parity, was 0.02%) is also another factor impeding foreign trade.

Liberalization of  
foreign trade  
6

The banking system is sound on the whole. The central bank, the Bank of PNG, follows international standards and pursues best practices. However, given that there are only four privately operated banks in the country, there is an unofficial duopoly at work in the banking system. One of the four banks, Bank South Pacific (BSP), controls more than half of the market and is the only bank with branches

Banking system  
5

throughout the country. It thus holds an unofficial monopoly on rural banking. BSP is also arguably the only bank willing to take on the risks involved with investing in rural areas, particularly where banking is exposed to criminal activities. The other three banks, Australia New Zealand Bank (ANZ), Westpac PNG and Maybank Papua New Guinea, concentrate mostly on business clients and can be found only in the country's urban centers. Banks in Papua New Guinea are inefficient. For example, local checks require three working days to clear. Most businesses still prefer cash. Internet-banking facilities are only available to a few. With only 21 companies listed, the Port Moresby Stock Exchange (POMSOX) is small, and some of its key counters have dual listings on the Australian Stock Exchange. Market liquidity is a problem, as there is a limited number of local players and few international players. There are no restrictions on foreign capital entering and exiting the POMSOX. Many of the large players use the dual listing to move money to Australia.

## 8 | Currency and Price Stability

During the period under review, the Bank of Papua New Guinea maintained a tight monetary policy primarily aimed at curbing inflation and maintaining stability in the exchange rate as well as the macroeconomic environment. Inflation hovered at 6.9% in 2009 and 7.2% in 2010 and is expected to be about 7.2% in 2011. The central bank is independent of the government although the majority of its board members, including the central bank governor, are appointed by the government. It has a conservative history when it comes to monetary and fiscal policy. For most of 2009 and 2010, the PNG was fairly stable, trading in the range of approximately \$0.35 to \$0.39, thanks mostly to an earlier windfall of high commodity and oil prices. The signing of the multi-billion dollar LNG project gave a boost to the confidence of the kina. The construction phase of the LNG project, which started in 2010, will pump millions into the local economy and generate business opportunities across the economy. There are no major problems with remitting money into and out of PNG, although amounts greater than PGK 500,000 require clearance from the central bank. This is a vast improvement on the previous system in which all remittances required central bank clearance.

The government and central bank policy of macrostability is aimed at attracting foreign investors and maintaining stable prices. The central bank's independence has been crucial to achieving these goals. The public debt is estimated to be 29.7% of GDP in 2009 and 27.8% in 2010. In 2010, the budget deficit was approximately 1.6% of the GDP. The government has committed itself to a budget deficit of not more than 4% until 2012. One important feature of PNG budgetary process is the lack of monitoring. More often than not, ministers and members from the governing party are expected to bring development funding to their home areas, regardless of

Anti-inflation /  
forex policy

8

Macrostability

6

the area's economic potential. In many ministries, off-budget items are paid through "special purpose accounts" (SPA). In some instances, these accounts contain millions of kina for discretionary spending by the minister and are not subject to audit. The government is also prone to overspend during elections to buy support, and with general elections due in 2012, the deficit is expected to go up to 10% of the GDP.

## 9 | Private Property

Property rights are well defined legally. However, a generally weak bureaucracy and the state's weak monopoly on the use of force also mean that in some areas – especially the more remote highland territories, where there are no functioning public institutions – legal property rights cannot be enforced by courts or state authorities. Corruption has been rampant for many years in the department of lands which has resulted in a lot of prime land in the nation's capital and other urban centers being taken over by individuals (including former members of parliament) with connections to the government and big companies, some of them foreign-owned.

It is important to note that only about 3% of the landed area in PNG is titled and freehold. The other 97% are either not surveyed or are regarded as customary land.

Private companies constitute the backbone of the economy, but major utilities are run by state-owned companies such as Ena Rau (water supply), PNG Power (electricity) and Telekom (communications) that hold a virtual monopoly in their respective sectors. Some private companies, such the rice importer Trukai, also hold virtual monopoly power in their sectors. Private companies are viewed as engines of growth and are given legal safeguards. The privatization of state companies often suffers from political interests. State-owned enterprises in PNG have powerful trade unions. Many of the country's current political leaders were involved with creating these businesses and are inclined to argue for their continued preservation, regardless of their performance. The national airline, Air Nigiri, is one such example of an enterprise that has received economic and political support through good and bad times.

## 10 | Welfare Regime

There is no state safety net. However, the cultural norms involved with various social groupings – including nuclear/extended families, clan-based and wantok, which is a pidgin term ("one talk") – require that weaker members be looked after by such social safety networks. All programs helping those in need are undertaken by NGOs funded by foreign funds, rather than government. The Australian

Property rights  
6

Private enterprise  
6

Social safety nets  
3

government's overseas development aid program, AusAid, plays a major role in poverty and rural health program in PNG. Broad segments of the population do not have access to proper health care, clean water or electricity. Major hospitals around the country are routinely shut down or are forced to scale back services because they have not received their budget allocations on time. Hospital shutdowns due to unpaid staff or unpaid electricity and water bills are not uncommon. Many hospitals rely on foreign aid to fund equipment and medicine. In the period under review, three major hospitals (Tari, Madang & Port Moresby) experienced temporary shutdowns. Working adults in full-time employment are required to pay into a provident fund that is based on regular contributions from both the employee and employer. Prior to 2000, the state-operated National Provident Fund (NPF) was the only fund legally entitled to take contributions. This changed, however, when the NPF began losing millions of contributors' money to corruption. About a dozen private pension funds are now in place, but poor governance has caused some to lose their member's money through fraud.

Although there are equal opportunity laws, large sections of the population face open discrimination. Women in particular are discriminated against in all strata of society. Their access to education, medical care, employment opportunities and public office are limited, and they are rarely protected from domestic abuse. It has been estimated that only about half of the eligible female students actually proceed to high school. The literacy rate for the country is only about 60%. In the political arena, where women's participation is marginal, women suffer widespread discrimination and generally find it difficult to win an election. Currently, parliament has only one female member. A proposed law to reserve a provincial seat to women was rejected in 2010 along with the suggestion that a quota for female members of parliament be allocated. Cultural discrimination against women in parts of PNG is based on conservative beliefs which hold that men are born to lead and that women should look after the family and the household. In the highlands, where such beliefs are deeply rooted in the cultural environment, women in remote communities are subject to extreme social control. However, this set of beliefs is also prevalent among the educated ruling elite, and it is common to hear of members of parliament and other senior officials who have beaten their wives. While several ministers have been openly accused of domestic violence, most of these reports are not investigated by the police. Indeed, domestic violence is widespread. According to a national survey conducted by the PNG Law Reform Commission, 67% of rural women and 56% of urban women have been victims of some form of sexual harassment or assault. Poverty contributes to gender discrimination, since parents are more willing to spend limited resources on educating males rather than females.

Equal opportunity

4

## 11 | Economic Performance

The economy proved fairly resilient in the period under review, largely due to the rise in global commodity prices and confidence created by the finalization of the \$15 billion liquefied natural gas project (LNG) in 2010. When the LNG comes on line, it is expected to contribute an additional 20% to the country's GDP. The country depends heavily on exports of minerals, crude oil, and agricultural commodities. Following several years of contraction, the PNG economy has been growing since 2003. GDP growth was estimated at 5.5% in 2009 and 6.2% in 2010 and estimated to reach 7.7% in 2011, marking a decade of expansion averaging about 3%. During the period under review, services grew by an estimated 7.0%, mainly reflecting expansion in the communications and construction subsectors; industry grew by 4.6% and agriculture by 2.3%. Employment in the private non-mining formal sector increased by approximately 4% in 2009. The services sector saw particularly strong jobs growth, and employment in mining also rose. However, this formal sector accounts for only one fifth of the labor force. The bulk of the workforce is still in the informal sector, creating the huge problem with the tax base.

Output strength  
7

## 12 | Sustainability

Although there are strict laws on environmental protection, environmentally compatible growth receives almost no consideration. Many in the government believe that rapid growth requires compromises in environmental protection and quality. There is a department of environment (DOE), but often its work is compromised by more powerful ministries such as trade and industry. For years, NGOs have documented the failure of the department of forests to apply its own logging regulations in PNG. The government's office of climate change and sustainability (OCCS) within the department of environment and conservation was paralyzed when its director was caught trying to sell non-existent carbon credit in the international markets. Environmental protection is also compromised by greed and corruption which leads frequently to the violation of existing regulations.

Environmental  
policy  
4

There are four state universities and several private tertiary institutions, but they all underperform academically. Many of the state universities are persistently underfunded, and academic staff regularly strike over unpaid salaries and poor working conditions. Discipline among students is also a worry. During the period under review, there were major student disruptions at three institutions, the University of Papua New Guinea, the University of Technology and the University of Goroka. There were also tribal fights and shootings on campus during the period under review. The government allocates less than 2% of GDP to education. In many cases, the allocated sum is not paid out in full as the money is diverted to more

Education policy /  
R&D  
3



pressing political issues. There is almost no state investment in R&D. A high profile study involving former PNG prime minister Sir Rabbie Namaliu and Professor Ross Garnaut of the Australian National University was undertaken in 2010 with the primary aim of streamlining the services of tertiary institutions in order to suggest ways forward for tertiary education. The report has yet to be made public.

## Transformation Management

### I. Level of Difficulty

The structural constraints on governance are massive. Low levels of trust among government agencies, frequent changes among ministers, and the government bureaucracy itself is heavily politicized, inefficient and corrupt. Other constraints that have taken their toll on the country include: low education levels, a lack of infrastructure, a small and underperforming economy, aid dependency and ethnic conflicts. PNG is experiencing rapid, sustained population growth of about 2.7% annually, and it has the highest rate of reported AIDS/HIV cases in the region. Approximately 0.92% of the adult population in Papua New Guinea was living with HIV in 2009, according to new estimates from the National AIDS Council Secretariat. While some experts consider PNG to be a weak state, it is important to bear in mind that the modern state system has been superimposed on thousands of tribal groups across not only vast regions of rugged terrain, but hundreds of islands as well, with dramatic logistical difficulties for government and governance.

Structural  
constraints  
8

In general, civil society traditions are weak and mostly concentrated in urban areas where most of the educated population lives. However, cultural norms such as “wantok” and “payback,” which require entire clans or tribes to retaliate against another when a clan member is injured or harmed, supersede any forms of civil society norms. There is a very low level of trust between tribal groups and people beyond a given wantok.

Civil society  
traditions  
6

PNG society and its political elite are deeply split along the lines of social class, and tribal and regional groups. Rentseeking behavior inside the public bureaucracy is rampant. The Somare administration has been repeatedly accused of favoring Sepiks (Somare is a Sepik) in appointing senior public servants. There are also many groups challenging the state over the control of resources. The highland tribal groups, for example, are seeking control of the LNG project. Many “big man”

Conflict intensity  
6

politicians in the highlands keep private militias. Tribal groups also regularly extort people in transit along sections of the highland highway, claiming that they are merely collecting toll for the use of their land or compensation claims against the government. The issue of land ownership is a major source of conflict not only between local populations and the government, but also among clan and tribal groups. Most of the land in PNG is subject to customary tenure. By law, major government projects involving natural resources or infrastructure are required to pay millions of kina or dollars in royalties to landowners, which are usually comprised of distinct tribal or clan groups within a given geographical area. Many of these groups regularly attack government installations in the name of unpaid land compensation. The LNG project has been subject to many threats by tribal groups demanding compensation upfront. In one recent incident a senior expatriate from the oil company was seriously assaulted by villagers. As the LNG construction phase gets underway, many expect more violence.

## II. Management Performance

### 14 | Steering Capability

The political leadership tries to pursue long-term aims, but often postpones them in favor of short-term political benefits. However, with the general elections due in 2012, the government is expected to abandon any pretence of pursuing long-term policies and go for short-term gains in order to win the elections. Although the government regularly commits itself to five-year development plans, it does not have the capacity to carry them through. Weak institutional efficacy, a poorly functioning bureaucracy and the lamentable state of political parties exacerbate problems with coherent planning and policy prioritization.

With the turnover rate of members of parliament at more than 50% over the last four elections, it is clear to see why priorities are often planned for five years (i.e., the electoral cycle), so that members of parliament can do what they can to stand a better chance of re-election.

The Somare government adopted a bipartisan push in 2009 to adopt what is called a PNG Vision 2050 as a general (but ambitious) platform to guide planning until that date. Whether it is sustained in the short to medium term, and especially after this parliamentary term, is another matter.

The government regularly fails to implement most of its stated reform goals. This is due to the lack of political will and a lack of administrative capacity. Another major problem for the implementation of reforms is that senior politicians interfere

Question  
Score

Prioritization  
5

Implementation  
4

regularly in civil service operations. Senior public servants will often give conflicting orders to those given by regional governors. Most reforms are initiated by the prime minister's office but are often not implemented due to an inefficient civil service that is particularly weak outside major urban areas. A survey undertaken a few years ago revealed that more than two-thirds of cabinet decisions were either not carried out or were not carried out in full by the civil service. Reforms undertaken to make the civil service more effective have also failed in recent years. Despite various attempts at strengthening capacity such as the "Strongim Gavman" Program (SGP), which is Tok Pisin for "strengthening" or "empowering" government, and which involved using nearly 40 Australian officials as key advisors in the PNG bureaucracy, nothing has worked. Many PNG bureaucrats resent the presence of these Australians and many see them as the new colonizers. An earlier similar plan to use Australian federal police as advisors to the PNG constabulary also ended in failure.

Although policies are reviewed on a regular basis and reports undertaken, there is no real change or learning from past mistakes. The political leadership will respond with proposed changes to failed policies, but more often than not, policies remain stuck in the same routines. There is no political will to correct past mistakes as the core issue is usually corruption and fraud. The leadership is also more prone to adopt policies that offer little or no threat to them in their present positions.

Policy learning  
4

## 15 | Resource Efficiency

The central government uses only some of the available resources efficiently. Political expediency and interference means that public resources are wasted. In the provinces, the situation is even worse as many provincial governors treat the state (through their standing/authority in their respective provinces) as their personal fiefdom. Provincial governments, and to a lesser extent, the central government, are plagued by the mismanagement of funds, the dismissal of senior staff and "nepotistic" or wantok-based appointments. During the period under review, three provincial administrators were removed without notice. The problem is compounded by a lack of centralized monitoring for the provinces. In the highlands, for example, governors have an almost free hand to do what they want. What they want to do is to reward their political supporters and to use the state assets to get re-elected. Thus the entire government machinery is used to mobilize political support rather than develop the province.

Efficient use of  
assets  
3

The central government tries to coordinate policy-making through the Central Agencies Coordination Committee (CACC). However, ministers and senior politicians often interfere with the process by giving conflicting instructions. A weak, inefficient and corrupt civil service adds to the difficulty of policy coordination. The low quality of data available for policy-making is a related

Policy  
coordination  
4

problem. The department of planning and monitoring often relies on statistics that are suspected to be flawed and incomplete.

The government is not serious about corruption and nurturing good governance. As a former prime minister puts it, “Corruption is systemic and systematic.” The incumbent Prime Minister Somare has been accused of owning several properties with corrupt money in Queensland, Australia. It is almost impossible to carry out an effective anti-corruption policy. The Ombudsman Commission conducts investigations of political leaders suspected of corruption, but once a politician resigns, the commission can no longer legally investigate the case. At present it is seriously understaffed and has been underfunded for many years. While the Commission keeps its door open to assist members of parliament in any way, there is a history of mistrust between these two sides that goes back three decades or so. It is believed that the underfunding of the commission is done purposely to weaken and curtail its work.

Anti-corruption  
policy  
3

## 16 | Consensus-Building

All major political actors agree on the goals of building a market-based economy and liberal democracy. However, given the deficits observed in managing the democratic process and the transformation to a market economy, this consensus remains unattainable until the issue of high level corruption is dealt with.

Consensus on goals  
8

Reformers cannot prevent all of the powerful anti-democratic actors, such as tribal groups and regional political leaders, from seeking control of the state, but they can at least limit these groups from exercising their power. The basic cleavage between the highlanders and people living in the lowlands or coastal areas has dominated political conflicts since independence. Their mutual attempts to dominate the political process have not resulted in either side successfully controlling the state for any long period. General elections are held every five years ensuring a turnover of political leaders. The constant change in government and repeated shifts in cabinet members ensure that anti-democratic forces are held in check. It should be noted here that anti-democratic actors in PNG are mostly rent-seekers and opportunists rather than those who wish to replace liberal democracy with an authoritarian system. Furthermore, the coast-highlands divide was much more pronounced in the past.

Anti-democratic  
actors  
6

The political leadership does not seek to reduce existing divisions or prevent conflicts from escalating. Clan, tribal and regional loyalties form the basis of their political support. Moreover, there is a low level of trust between groups hence it is almost impossible to reduce existing divisions. Tribal wars and other acts of violence, especially in the highlands, occur on a regular basis. In some cases, political leaders encourage the cleavages in order to secure political power. For

Cleavage /  
conflict  
management  
5

example, it is common for politicians to form regional “blocs,” such as the island bloc, highlands bloc etc., to negotiate cabinet positions.

The allocation of ministries to regions has been a practice since the pre-independence years. It has been common for members of parliament to allude to regional groupings in recent times only when there were reshuffles in cabinet and some members reacted negatively to them, or when there was a need for more say by one region (over others) in line with the significance of activities in one region.

The political leadership frequently ignores civil society organizations (CSOs), seeing them as political rivals and anti-growth elements. More often than not, the government formulates its policy autonomously and secretly, especially when it comes to controversial policies. Examples of the government ignoring CSOs include its policies relating to logging and deforestation, and those relating to environmental protection and pollution control. The fact that many CSO leaders regularly run in elections compounds the problem, as it nurtures the widely held view that CSOs are just political parties in all but name.

Civil society  
participation  
5

The political leadership recognizes the need to deal with historical acts of injustice, but the process of reconciliation often fails. Land compensation claims constitute a prime example of a historical act of injustice. During the colonial administration, all land not issued with a title became state land. After independence, land with titles constituted less than 7% of all available land in PNG. This has led to numerous conflicts and tribal wars in which people have died fighting over land rights and compensation claims from the government. Because land ownership is such a sensitive issue, no government since independence has made any serious attempt to survey the land and issue titles. The only success observed in addressing a historical act of injustice in PNG is the reconciliation process that has taken place between the central government and the people of Bougainville. After more than a decade of civil war, the central government permitted an autonomous Bougainville government (ABG) to be established on the island. In the period under review, John Momis was elected second president of ABG. However, there are fears that this may not last as the ABG has failed to demonstrate any progress in advancing the goal of good governance. The previous ABG was accused of corruption, including the acceptance of free overseas travel from a business group seeking concessions on the island.

Reconciliation  
n/a

## 17 | International Cooperation

Since independence, PNG has cooperated with and received extensive help from several international bodies. Among the major players helping PNG develop are the UNDP, ADB, IMF, World Bank and AusAid. PNG receives one of the highest per capita levels of aid money. PNG is also an active member of the South Pacific

Effective use of  
support  
6

Forum and plays a leading role in the African, Caribbean and Pacific states (ACP countries) pact with the European Union. However, PNG's record of putting aid to effective use is mixed at best. Many aid programs have failed, and corruption has also had a severe effect. There are many cases in which foreign aid money has gone unused because the bureaucracy has been unable to comply with the paperwork.

PNG's international reputation is mixed in the international arena. Many countries see PNG as a weak state and therefore they do not have high expectations. They know that successive governments in Port Moresby have limited capacity. This is very obvious in border control. It is common knowledge that PNG cannot control or watch its borders with both Indonesia and Australia. Many governments hold the view that PNG cannot be a reliable partner in promoting democracy and the market until it resolves its governance and corruption issues.

Credibility  
5

The government actively cooperates with neighboring states and complies with the rules set by regional and international organizations as best it can. It takes part in all major international meetings. It is the unofficial leader of the Melanesian group of countries. In the period under review, Prime Minister Somare has taken an active stand internationally on climate change, hoping to be the voice of developing countries on this issue.

Regional  
cooperation  
6

## Strategic Outlook

During the period under review, Papua New Guinea made some progress on the economic front, but this was due more to the high oil and commodity prices than internal factors. The signing of the LNG project and the start of construction saw money flowing into the country. The semblance of political stability that has come with the re-election of Michael Somare as prime minister constitutes an improvement. In a country where prime ministers stay in office for two to three years on average, the fact that Somare was re-elected after having served one full term may be seen as a major milestone in PNG politics. In the short term, the biggest challenges facing the country are the need to stabilize its economy and maintain consistent growth. The key to PNG's long-term economic prosperity remains the LNG project. How the government handles the construction phase in the face of strong landowner disputes and overlapping claims of compensation remains a key challenge. The other key challenge is to ensure that revenue generated from the LNG project is used to cement long-term benefits. Another short-term challenge is to ensure that the 2012 general elections are held in an orderly manner. Elections in parts of PNG are prone to violence and this may affect the LNG project. In order to mitigate the challenges, the government should concentrate on ensuring private sector expansion and on reforming the bureaucracy to make it more efficient and private-sector friendly. The government must also take some concerted action to combat high-level corruption and to secure its monopoly on the use of force throughout the country. The government must undertake real reforms in order to reduce the cost of doing business in the country and open up the economy to foreign investors.