

## **AUSTRALIA'S RELATIONSHIP WITH PAPUA NEW GUINEA**

### **SUBMISSION TO *SENATE FOREIGN AFFAIRS, DEFENCE, AND TRADE REFERENCES COMMITTEE***

BY

**TIMOTHY CURTIN**

*VISITING FELLOW, NATIONAL CENTRE FOR DEVELOPMENT STUDIES,  
AUSTRALIAN NATIONAL UNIVERSITY*

The possible emergence of a new government in Papua New Guinea by the end of this month raises important considerations for the Australian Government in the light of its previous close ties with the outgoing government of Sir Mekere Morauta. The most important of these is how far Australia should encourage the new government to continue the macro-economic policies of its predecessor.

Sir Mekere's willingness to accept external advice and to implement most – if not all – of the conditions attached to the Structural Adjustment Programme loans to which Australia was a major contributor led to some notable achievements, including the privatisation of the country's leading commercial bank, the granting of significant autonomy to the central bank, and the reform of the superannuation industry. These achievements at what could be called the micro level have been somewhat clouded by evident toleration of the corrupt dealings of many of the Morauta cabinet, a toleration terminated in some cases by the electorate, which has voted out such key figures as the Deputy PM (Ogio) and the Foreign Affairs Minister (Waiko), and in others by the Ombudsman, with his referrals of Sir Mekere's Finance and Planning Minister (Kumbakor) and other recent ministers like Zeming. Sir Mekere and his Chief Secretary (Igara) had acquiesced in Kumbakor's flagrant subversion of the Public Finances Management Act and dismissal of the Finance Secretary (Iamo). Kumbakor had presided over the failure to finalise the public accounts for 2001, and this is already having macro-economic consequences, with blowing out of the deficits in 2001 and 2002 to perhaps as much as 4 per cent of GDP.

It is therefore to be hoped that Australia will help PNG's new government to reestablish order in its public finances, and that conditions attached to any new financial support will include measures to give the Secretaries of the Treasury and Finance Departments the same autonomy and exemption from political interference as the Governor of the Bank of New Guinea.

In addition the Australian government should insist that any new Structural Adjustment loans – including those provided by the World Bank and other international agencies – should be structured along the same lines its own successful Ausaid programmes, that is, all new SAP loans (other than the IMF's for balance of payments support) should be provided only on a project basis. Previous SAP loans provided in the form in effect of blank cheques to PNG's treasury for its annual budget have not been used for the purposes intended, with demonstrable shortfalls in

spending on the Development Budget being used to finance the illicit ventures of Ogio, Kumbakor, Waiko, and others. It would indeed be instructive if the Senate were to require the Commonwealth Auditor General to investigate the actual uses of the SAP loans.

Finally, the Australian government should encourage the incoming government to review its predecessor's commitment to restrictive monetary policy and high domestic interest rates in its vain and futile effort to prevent or at least slow down the constant depreciation of the Kina (which even under the Morauta government has fallen from US\$0.38 and A\$0.58 in July 1999 to US\$0.25 and A\$0.45 in July 2002 – or 34 per cent and 22 per cent respectively). Throughout the tenure of the Morauta government private sector borrowers have been subjected to borrowing rates of as high as 20 per cent, and currently still 15 per cent. As the attached paper by this submitter (see Exhibit 1) points out, PNG's banking system has unused lending capacity of some A\$5 billion, far more than would ever be provided by a new SAP loan package. The paper shows that unlocking that capacity would require the following:

- Abandonment of the exchange rate as an explicit targeted variable (clearly the present policies have failed to secure its stability); and
- Use of new SAP loans to instigate a programme to facilitate collateralization of land so as to unlock the untapped lending capacity of PNG's domestic banking system.

Tim Curtin

As from: 3 Magrath Place  
Spence, ACT 2615  
T/Fax: 62595644

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