

A range of other issues

Australia Papua New Guinea Business Council

- 4.1 Mr Chris Mackay, Executive Director of the Australia Papua New Guinea Business Council (APNGBC), stated that the Business Council has 63 members, largely representing larger corporations prepared to invest time and resources in PNG. Smaller companies, more concerned about ‘filling a container’ and securing payment, are less interested in joining such bodies.¹
- 4.2 He noted the support the Australian Government has provided to PNG over the years. He referred to difficult circumstances in PNG over this period, and to the contribution made by AusAID’s programs to such things as making processes transparent.²
- 4.3 He said that Australian companies are interested in the relationship with PNG for commercial and for social reasons. If there is a good relationship between business and government, companies will believe that there are less risks in investing in PNG. There is also the belief that the Australian Government will be more active in making representations during more difficult times.
- 4.4 Companies are also very alert to the well-being of their employees. Because of current law and order problems in PNG, there are concerns about the welfare of Australian citizens employed in that country. There is

1 Transcript, Mr Chris Mackay, 12 September 2000, p. 28.

2 Transcript, Mr Chris Mackay, 12 September 2000, p. 27.

a belief that the Australian Government will seek to assist in resolving these problems.³

- 4.5 He believed that law and order could be regarded as a management problem until there was either loss of goods, or loss of life. Thus, banks have experienced losses of goods and money for some time. Such problems could arise in any location, but he noted that there is a sense that maintenance of civil order is of the highest priority.⁴
- 4.6 Mr Mackay said that there was a need for a clear understanding of the Australian Government's intentions about protecting its citizens in PNG. If there were to be a major volcanic eruption in PNG, or a major social disruption, the capacity of many smaller Australian businesses there would be taxed.
- 4.7 There was also a need for business to understand the intentions of the Australian Government, should PNG's problems of economic management threaten regional stability.⁵
- 4.8 Mr Mackay pointed out that, outside the PNG Government, Australian business is the largest employer of Papua New Guineans, and this is complemented by the Australian Government's effort in the education sector. He believed that, through this combination of Australian business and education, PNG will build an economic capacity that will be translated into greater stability in the region.⁶
- 4.9 He noted that Australian companies had been very alert to the conduct of public affairs in PNG, and drew attention to what he saw was the continuation of this supportive approach.
- 4.10 Mr Mackay pointed out that there are considerable resources and a wealth of talent in PNG, so that commercial relationships with Australian companies could be highly profitable. This was likely to happen in the future.⁷
- 4.11 He added, on the other hand, that present business conditions are such that it is unlikely that any new, major investments outside the minerals and petroleum sectors will be made in PNG. Thus, because of existing conditions there, in the short term no major Australian company is likely to invest in a manufacturing plant. He also suggested that, except for

3 Transcript, Mr Chris Mackay, 12 September 2000, p. 24.

4 Transcript, Mr Chris Mackay, 12 September 2000, p. 28.

5 Transcript, Mr Chris Mackay, 12 September 2000, p. 25.

6 Transcript, Mr Chris Mackay, 12 September 2000, pp. 25-26.

7 Transcript, Mr Chris Mackay, 12 September 2000, p. 26.

certain consumer items, Australian companies will continue to withdraw from investments in PNG, but continue to trade there.⁸

- 4.12 Finally, Mr Mackay noted that very little revenue in PNG comes from personal domestic activity, implying that there is little ‘ownership’ of the process of acquiring and spending consolidated revenue at the national level. He suggested that a result of this lack of ownership of the process was a lack of pressure on politicians to spend funds in specific directions, inside PNG and related to the people taking charge of their lives, contributing to revenue and ‘owning’ their government.⁹
- 4.13 Mr Mackay’s evidence to the inquiry was valuable for the perspective it gave on the view of some elements of Australian business towards the relationship with PNG.

Buoyant Economies

- 4.14 Mr Leigh Harkness, Director, Buoyant Economies Pty Ltd, argued that the loan to PNG ‘was not in Australia’s national interest.’ He argued that it may be in Australia’s interest to support a program that restores stability to the PNG economy and bring about economic prosperity. Such a program would damage the bilateral relationship, however, if it required PNG to make sacrifices that bring misery and despair to its people and did not solve its problems.¹⁰
- 4.15 He asserted that the RBA’s swap was used to induce PNG to follow the IMF’s structural reform program and that governments need inducements to follow IMF programs, because they do not work: ‘They have not enabled any country to reduce its foreign debt and become prosperous.’ Even if a country has a fiscal surplus and implements an entire IMF program, he stated, this will not solve the imbalances that cause its foreign debt to rise.
- 4.16 Mr Harkness believed that the IMF implements ‘inappropriate policies’. While these may be good in theory, he stated that in fact they interfere with the economies they are meant to assist because they do not address the real problems. He suggested that the IMF gets involved in a range of activities, such as governance, health and education, which are the responsibility of the Government of PNG. In his view, this is in spite of the

8 Transcript, Mr Chris Mackay, APNGBC, 12 September 2000, p. 26.

9 Transcript, Mr Chris Mackay, APNGBC, 12 September 2000, p. 29.

10 Unless specified otherwise, material in this section was drawn from Submission No 1 from Buoyant Economies.

fact that it is seeking assistance for its balance of payments (BOP) problems.¹¹

- 4.17 He believed that the IMF's structural adjustment program will not solve PNG's problems and that it will not be able to repay this loan, unless Australia's development cooperation funds are used for this purpose. He thought that Australia was 'throwing good money after bad'.¹²
- 4.18 Mr Harkness suggested that, rather than relying on the IMF program, PNG should restrict bank credit and keep its foreign reserves at a high level, so that its external debt servicing obligations remain low and the debt service ratio at a low level. He argued that, although Australia has given money to PNG to assist with its BOP problems, PNG would solve its problems more effectively if his proposed mechanisms were adopted.
- 4.19 While the Committee was unable to accept that Mr Harkness' views reflected the complexity of PNG's situation, his evidence was important for the different view it gave of the involvement of the IMF in assisting its members.
- 4.20 Examination of the chronology of this loan in Chapter 3 shows that the Reserve Bank's swap was not used to induce PNG into adopting the IMF structural reform program. The sequence of events for the granting of this loan was not clear in the NIS, nor in Treasury's evidence at the public hearing. It is not surprising that there was some confusion about that sequence.¹³
- 4.21 At the Committee's request, Treasury commented upon a number of aspects of Mr Harkness' evidence.¹⁴
- 4.22 Treasury drew attention to the fact that PNG lacks the domestic savings to fund the large scale, capital intensive investments necessary to develop its natural resources. It suggested that restricting national investment to the level of national saving would result in lower economic growth than otherwise would be the case. This was likely to be the consequence of the capital rationing Mr Harkness appeared to have suggested. Treasury believed that to limit PNG's access to development capital in this way would not be in its interests, nor in Australia's.

11 Transcript, Mr Leigh Harkness, Buoyant Economies, 12 September 2000, pp. 32-33. It has been reported that the IMF is to draw up a new framework to involve private sector banks in future assistance packages: see *The Canberra Times*, 26 September 2000, p. 13.

12 Transcript, Mr Leigh Harkness, Buoyant Economies, 12 September 2000, p. 30. PNG's ability to repay this loan was addressed in paragraphs 3.28-3.29.

13 See paragraph 3.6.

14 The material below was drawn from the Submission No 5 from Treasury, pp. 1-3.

- 4.23 The alternative route, and the one followed in the granting of this loan, is for Australia to support the PNG Government's economic reforms. Treasury suggested that, by providing confidence that investments are soundly based, these reforms 'should support' a strengthening of investor confidence in the PNG economy. This would not require the sharp reduction in economic growth that Treasury believed would be associated with Mr Harkness' proposal.
- 4.24 Mr Harkness was also critical of the effectiveness of the IMF's structural adjustment programs, arguing that its program will not work in PNG. Treasury submitted that 'the bulk of evidence' suggested that the IMF's policies had 'been generally successful' in assisting member countries to address their macro-economic imbalances and resume economic growth.¹⁵
- 4.25 It was aware, however, that the IMF 'can do better', and Treasury said that it had urged that body to undertake further reforms to improve its effectiveness. It pointed out that, in the wake of the East Asian financial crisis, the IMF had initiated a comprehensive review of its policy framework, to ensure that it remains relevant in the globalised environment.
- 4.26 With reference to Mr Harkness' claim that the loan rescued the from a poor commercial decision, Treasury pointed out that the swap was not a commercial decision by the RBA. It followed a request from the Australian Government to provide short-term bridging finance to PNG, pending the IMF's agreement to the Stand-By Arrangement and the intention to make a Government loan after that matter had occurred.
- 4.27 Treasury noted that Australia's support for the PNG Government's reform program was deliberately linked to progress in meeting the IMF's reform benchmarks. This was judged to be the best way to ensure the effective use of Australian funds in support of sustained economic recovery in PNG. From early in the life of the Morauta Government, Australia made it clear that support for PNG was dependent on its progress in reaching agreement with the IMF, and would follow such an agreement.
- 4.28 Mr Harkness also questioned the legal authority of the RBA to enter the swap. Treasury stated that this authority 'was not and is not in question'. The Bank's Act confers powers to buy, sell and otherwise deal in foreign currency, in order to carry out its obligations under that Act or any other Act, including obligations that arise from acting as a financial agent of the Commonwealth.

15 See paragraph 4.16

Greenpeace Australia

- 4.29 Greenpeace Australia pointed out that PNG is home to some 28 million hectares of tropical forest, and has the largest ancient tropical rainforest in the Asia-Pacific region. It believes that these rainforests are essential to the well-being of ‘hundreds of distinct peoples’, as well as being home to some 5 per cent of the World’s terrestrial biodiversity.¹⁶
- 4.30 Greenpeace also believes that the greatest threat to PNG’s forests is illegal and destructive industrial logging. It asserted that, in 1998, the Skate Government fast-tracked the acquisition and tendering for concessions for the remaining operable forests in PNG, breaking its own laws in the process. It noted that, as part of the current structural adjustment program for PNG, a moratorium has been introduced on logging concessions to permit a comprehensive review of the forestry sector.
- 4.31 It drew attention to the actions of the PNG Government, in December 1999:
- introducing an immediate moratorium on all new licences, extensions to and conversions of concessions, and
 - a commitment to a review of all existing licences.
- 4.32 Greenpeace believes that the current moratorium on what it sees as the expansion of industrial forestry ‘is a sound and far-sighted policy instrument.’ It is seen as necessary to achieve meaningful reform, equity and sustainability in the forestry sector, and more broadly to improve governance, maintain stability and facilitate sustainable development in PNG.
- 4.33 Greenpeace estimated that the proposed concessions covered by the moratorium cover 4.3 million hectares, and represent ‘the last of PNG’s operable forests.’ Its submission drew attention to the damage logging does both to forests and to the resources for local communities. Compensation for this damage is rare but, because of bribery and intimidation, the impact of logging companies on good governance is more serious.
- 4.34 Logging companies are seen by Greenpeace as significant sources of cash for electoral candidates, with ‘guarantees’ of access if a candidate is successful. The organisation noted that such payments perpetuate a system whereby elections are won on the basis of how much candidates can deliver to a constituency in the short term, rather than on the quality of policies or record of public service. In addition, it suggested that, given

16 Material in this section is drawn from Submission No 3 from Greenpeace Australia.

a lack of an equitable revenue system and inequitable Forest Management Strategies, logging projects divide and exploit communities.

- 4.35 Greenpeace believes that it is in Australia's national interest for conditions to be imposed by the IMF and the World Bank, relating to environmental performance and governance on loans to PNG. If Australia imposed conditions on its loans and grants, it could play a strong role in protecting biodiversity in this region, promote sound management of PNG's natural resources and support good governance.
- 4.36 Greenpeace drew attention to the PNG election in 2002, noting that this will place significant pressure on the Government to open new areas to loggers. It saw this as having dire consequences for forests and governance in PNG, and that it would also undermine Australia's interests. It believes that the moratorium could be lifted with the disbursement of the second tranche of the World Bank loan, expected in the second quarter of 2001. The organisation believes that only a partial review of proposed new projects has been undertaken.
- 4.37 If the PNG Government is to maintain the moratorium, Greenpeace believes that it will be necessary to resist significant pressure from national and provincial politicians, landowners and loggers seeking new operations. It believes that it is critical that the Australian Government is prepared to use diplomatic and economic means to prevent further corruption of PNG's political system by a rapid liquidation of the remaining unallocated and intact forests. To this end, conditions on loans and programs to assist in the reform of the sector are seen as essential.
- 4.38 Greenpeace urged the Australian Government to do all in its power to ensure the protection and proper management of PNG's remaining ancient forests. This will assist their significant biodiversity, the value of the sustainable resource and the people whose lives these sustain.
- 4.39 Although Greenpeace provided information on only one matter, it dealt with an issue of some significance in a number of important areas, including governance in PNG.
- 4.40 It was reassuring to see a quotation in the submission from Greenpeace, from Sir Mekere's November 1999 Budget speech, about poor governance in forestry, the promotion of corrupt practices and the undermining of environmental sustainability through logging activities.

Panel from the ANU

The Morauta Government

- 4.41 Dr Ron May from the Australian National University (ANU) saw the Morauta Government as providing a breathing space and the possibility of reversing the trend to cronyism and politicisation of the bureaucracy. The process by which Sir Mekere was elected in 1999 could, just as easily, see him replaced. Despite recent attempts at political reform, he saw little evidence yet of a fundamental change in political behaviour in PNG. If this Government is to succeed in its efforts, he believed that external assistance was needed to support the process of structural adjustment and political reform.¹⁷
- 4.42 He believed that a large-scale change in the political culture was required. He saw a groundswell of public opinion against corruption, and against the perks of politicians in PNG, partly expressed through the growth of non-government organisations. As some of these have some influence, he saw this as a positive sign, as a cause for optimism, even though it does not ensure that basic behaviour will change. He suggested that, as corruption becomes more transparent, the PNG population will be less impressed and gradually put more pressure on politicians to change their behaviour.¹⁸
- 4.43 Dr May referred to Australia's significant stake in PNG, in terms of trade, investment, defence cooperation and the development cooperation program. In addition, he believed that Australia has a stake in PNG remaining a functioning democratic state, capable of managing threats to its internal and external security in a region increasingly prone to crisis. He stated that a loan supporting PNG's efforts to achieve a degree of financial stability, and thereby improve its capacity for sound economic, environmental and political management, 'has to be in Australia's interests.'¹⁹
- 4.44 Dr Bill Standish also referred to the political culture in PNG. He noted that under-lying political problems and sets of institutional problems prevented its Government from delivering what is expected by its citizens. While they emphasise the political basis of these problems being experienced by PNG, a number of economists believed that the nation could be extremely prosperous.
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17 See also Transcript, Mr John Oliver, DFAT, 12 September 2000, p. 14, on PNG's political culture.

18 Transcript, Dr Ron May, ANU, 12 September 2000, p. 44.

19 Transcript, Dr Ron May, ANU, 12 September 2000, pp. 38-39.

- 4.45 He said that there are a large number of constraints built into PNG's political system. There are therefore continuing challenges to the nation that relate to the political culture as it has developed in PNG, given the interaction of democratic institutions and its society. These challenges ultimately affected both its international position and its internal economic governance.²⁰
- 4.46 Dr Standish said that the weak capacity of the government to deliver basic services had led to the Rural Development Fund, and to all the deficiencies of that method of delivering services. There had been few if any controls on that funding, and the recent changes were seeking to introduce accountability into the expenditure.²¹
- 4.47 Until the country's administrative capacity is increased, he did not think that pressures on politicians would change. He noted that, unusually, for five or six years the World Bank had been trying to get PNG Governments to increase the amount spent on services. The blockage had been at the discretionary level in provincial governments which have not had the funds to spend on services, partly because of the amount allocated to politicians for spending at their discretion.²²
- 4.48 Dr May referred to the combination of an economic crisis and poor economic management in PNG in 1996/97, stating that what was required was support for a government that had the capacity and integrity to pursue a sensible economic policy. He saw the purpose of this Australian loan as partly to provide a degree of stability to give further support to a government that is firmly along a path towards sensible reforms. If it has that breathing space, its own sources of revenue and Australia's development cooperation program will be needed to address deficiencies in administration in the PNG Defence Force (PNGDF) and elsewhere.²³

The likely effectiveness of the loan

- 4.49 Dr Theo Levantis referred to research on development cooperation, pointing out that it suggests that it is counter-productive to assist a country that is poorly managed. On the other hand, where there is good governance, development cooperation acts to multiply the effects of improvements. Thus, he believed that the most fundamental factor for

20 Transcript, Dr Bill Standish, ANU, 12 September 2000, p. 39. See Exhibit No 2 for Dr Standish's September 1999 analysis of these constraints.

21 Transcript, Dr Bill Standish, ANU, 12 September 2000, p. 47.

22 Transcript, Dr Bill Standish, ANU, 12 September 2000, p. 48.

23 Transcript, Dr Ron May, ANU, 12 September 2000, p. 42.

economic development is the quality of the political system. If there is good governance, there will be a 'booming economy'.²⁴

- 4.50 He pointed out that the IMF has had 'virtually no influence' on the current policy framework in PNG. Policy is heavily influenced by the International Advisory Group, set up by the Prime Minister when he took office. In his view, this Group is giving the Government good advice. Dr Levantis added that there are also good people working for the PNG Government who are capable of formulating advice without it being imposed by either the World Bank or the IMF.²⁵
- 4.51 Dr Levantis stated that the PNG bureaucracy was now working well and that the mood in PNG was 'extremely positive'. He believed that the Morauta Government would deliver a positive return on Australia's 'investment' via this loan, because:
- having done a good job so far, it has a lot of public support, and
 - it is currently putting through the Parliament, with unanimous approval to date, reforms that will dramatically improve the political situation through the creation of a two-party system.²⁶
- 4.52 He stated that, as long as the PNG Government stays on track in terms of good governance, the Australian Government loan will reap a positive return for PNG.²⁷
- 4.53 He also noted that economic problems in PNG in the early 1990s had had nothing to do with monetary policy. These occurred because of fiscal mismanagement by the then Government: a mineral boom generated expectations of revenue that were not met. Spending and wasteful expenditure continued, and the result was a balance of payments crisis in 1994.²⁸
- 4.54 Dr Levantis said that the privatisation program was part of the overall reform movement, not simply a revenue raising measure. With particular reference to Air Niugini, he stated that privatisation would not occur unless there were guarantees of the services to be provided when it had been completed. He did not think the program would proceed far without the resolution of the latter issue in each case.²⁹

24 Transcript, Dr Theo Levantis, ANU, 12 September 2000, p. 40.

25 Transcript, Dr Theo Levantis, ANU, 12 September 2000, pp. 40, 43.

26 Transcript, Dr Theo Levantis, ANU, 12 September 2000, pp. 41-42. See paragraphs 2.27-2.30 for some information on these reforms.

27 Transcript, Dr Theo Levantis, ANU, 12 September 2000, p. 41.

28 Transcript, Dr Theo Levantis, ANU, 12 September 2000, pp. 40-41.

29 Transcript, Dr Theo Levantis, ANU, 12 September 2000, p. 43.

International views of PNG

- 4.55 Professor Nelson agreed with Dr Standish that PNG's international standing had increased remarkably since the middle of 1999. He had thought that impediments to its success were so strong that there could only have been slight improvements, and that there had been correspondingly greater advances than anticipated.³⁰
- 4.56 Dr Standish noted the interest by the Government of the People's Republic of China (PRC) since the aborted PNG connection with Taiwan in 1999. The PRC had been involved in the celebrations for the 25th anniversary of PNG independence in September 2000, and is funding a new foreign affairs building in Port Moresby.³¹
- 4.57 Dr May wondered whether the PRC interest in PNG was a result of that temporary connection with Taiwan. In the regional context, this had raised questions about the future of PNG's relationship with friends it needed in the Association of South-East Asian Nations (ASEAN). Combined with PNG's existing 'look north' foreign policy, he thought that a number of other countries would show an increasing interest in PNG if Australia's commitment diminished.³²
- 4.58 Dr Leventis observed that, to some extent, the world looked at PNG through Australian eyes. This was particularly so in terms of the perception of law and order in PNG. Because Australia had been positive towards the Morauta Government, he said that the world was following its example. This perception gave added importance to the Australia-PNG relationship.³³

PNG in the South Pacific

- 4.59 Dr Standish noted that, as the largest regional state, PNG has long been active in South Pacific affairs. It has considerable influence, and is usually well respected in this region. Other countries in the South Pacific, however, have long been concerned about the potential for instability in PNG, especially because of problems of public order and its reputation for corruption.
- 4.60 Until 1997, when the Bougainville peace process began, there was little sympathy among South Pacific nations for the policies of PNG Governments towards that situation. The Sandline mercenary affair in that

30 Transcript, Prof Hank Nelson, ANU, 12 September 2000, p. 48.

31 Transcript, Dr Bill Standish, ANU, 12 September 2000, p. 48, See *The Australian Financial Review*, 18 September 2000, p. 8.

32 Transcript, Dr Ron May, ANU, 12 September 2000, p. 49.

33 Transcript, Dr Theo Leventis, ANU, 12 September 2000, p. 49.

year caused ‘particular alarm’ in South Pacific countries. During 2000, significant internal governance problems have emerged in other parts of that region. Dr Standish believed that there are signs both of growing understanding of and sympathy for the problems faced by successive PNG Governments, and an awareness that PNG was not unique.³⁴

Summary

- 4.61 For a short inquiry on a narrow topic, this loan attracted quality evidence from a number of sources. All those who contributed made valuable contributions to this inquiry, adding to the Committee’s understanding of the current situation in PNG and giving some indication of how it might proceed.
- 4.62 Evidence from the panel from ANU was particularly significant because of the range of issues that were raised, and the depth of that coverage. This evidence was also notable for the optimistic view of the prospects for the Morauta Government.

34 See Submission No 2 from Dr Bill Standish, ANU.