MEDIA RELEASE

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Another wave of inflation may be on the way in PNG

The overvalued Kina is one of the factors that contributes to the foreign exchange shortages in Papua New Guinea (PNG). The International Monetary Fund (IMF) program aims to restore Kina convertibility by moving toward a flexible exchange rate regime. The shortage of foreign reserves is expected to be addressed under the proposed regime, but prices of imported goods and services may go up.

The National Research Institute (NRI) spotlight Volume 16, Issue 13 titled ***"What will happen to inflation when PNG adopts the IMF's proposed exchange rate policy?"*** by Research Fellow, Thomas Wangi, states that IMF has approved PNG Government's request for US$918 million loan on 22 March 2023.

IMF has proposed several policy reforms as conditions for the loan and one of these is for the Bank of PNG to introduce a flexible exchange rate system.

The article states that under the proposed exchange rate regime, the Kina is expected to depreciate causing high prices for imported goods and services. The high prices will reduce the purchasing power of Kina and significantly affect the welfare of the people.

Mr. Thomas Wangi stated that according to historical data, exchange rate policy reform implemented in 1994 has led to a significant depreciation of the Kina and a sharp rise in prices of goods and services. The IMF's proposed regime is similar to the 1994 reform because the Kina exchange rate will be determined freely by the market forces of supply and demand.

Mr. Wangi said that fiscal policy such as price subsidies and import duty exemptions on selected goods can be used to ease the inflationary pressure. However, the policy may be too costly to the government.

Another policy option to consider for long-term inflation control is import substitution, Mr. Wangi said. Under the guide of the proposed government policies such as Customary Land Policy 2023 and Special Economic Zone Policy 2023 (when approved by the Government), the private sector in partnership with the government can utilise customary land for large-scale agriculture and livestock production. The produce from this sector can replace food imports, reduce imported inflation, as well as for exports to generate foreign exchange to address foreign exchange depletion.

The question of whether the proposed policy reform is appropriate for PNG at a time when inflation is already high, requires more discussions before the reform comes into effect this year.

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