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The Governor of the Bank of Papua New Guinea, Mr. L. Wilson Kamit, CBE, today (15 January 2001) released the second semi-annual Monetary Policy Statement covering the first six months of 2001 in accordance with the Central Banking Act 2000.

OBJECTIVES OF THE CENTRAL BANK

"For the advantage of the people of Papua New Guinea, the objectives of the Central Bank are -

(a) to formulate and implement monetary policy with a view to achieving and maintaining price stability; and
(b) to formulate financial regulation and prudential standards to ensure stability of the financial system in Papua New Guinea; and
(c) to promote an efficient national and international payments system; and
(d) subject to the above, to promote macro-economic stability and economic growth in Papua New Guinea."

Central Banking Act 2000, Section 7

POLICY STATEMENTS

"The Governor shall, within one month of the coming into operation of this Act, and every six months thereafter, issue a policy statement setting out the monetary policy of the Central Bank to achieve and maintain price stability for the following six months."

Central Banking Act 2000, Section 11, Sub-section 1

SEMI-ANNUAL MONETARY POLICY STATEMENT, JANUARY 2001

INTRODUCTION

This semi-annual Monetary Policy Statement is the second under the Central Banking Act 2000, which came into effect on 16 June 2000. This and the following Statements, to be presented every six months, represent a key element of the transparency and accountability arrangements of the Central Banking Act 2000. This Policy Statement is presented in 2 sections. The first covers economic developments in 2000 and projections for 2001. Section two sets out the rationale for the monetary policy stance for the first half of 2001 and the conduct of monetary policy.

1. DEVELOPMENTS IN 2000 AND PROJECTED DEVELOPMENTS FOR 2001

In designing monetary policy for 2001, the Central Bank considered actual and projected developments in five main areas, and their impact on the monetary aggregates, exchange rate and prices:

a) The World Economy;
b) Domestic Economic Activity;
c) Balance of Payments;
d) Fiscal Operations of the Government;
e) Inflation; and
f) Monetary and Financial Market Developments.

(a) The World Economy

World economic growth as measured by Gross Domestic Product (GDP) is projected to increase by 4.5 percent in 2000 and 3.7 percent in 2001, compared to 3.4 percent in 1999. The slower growth in 2001 is due to the effects of higher oil prices in 2000, a sharp fall in equity prices and the lagged effects of the tight monetary policy regimes pursued in the major economies. The core inflation rate is expected to increase gradually, while headline inflation is projected to subside in line with the projected decline in oil prices.

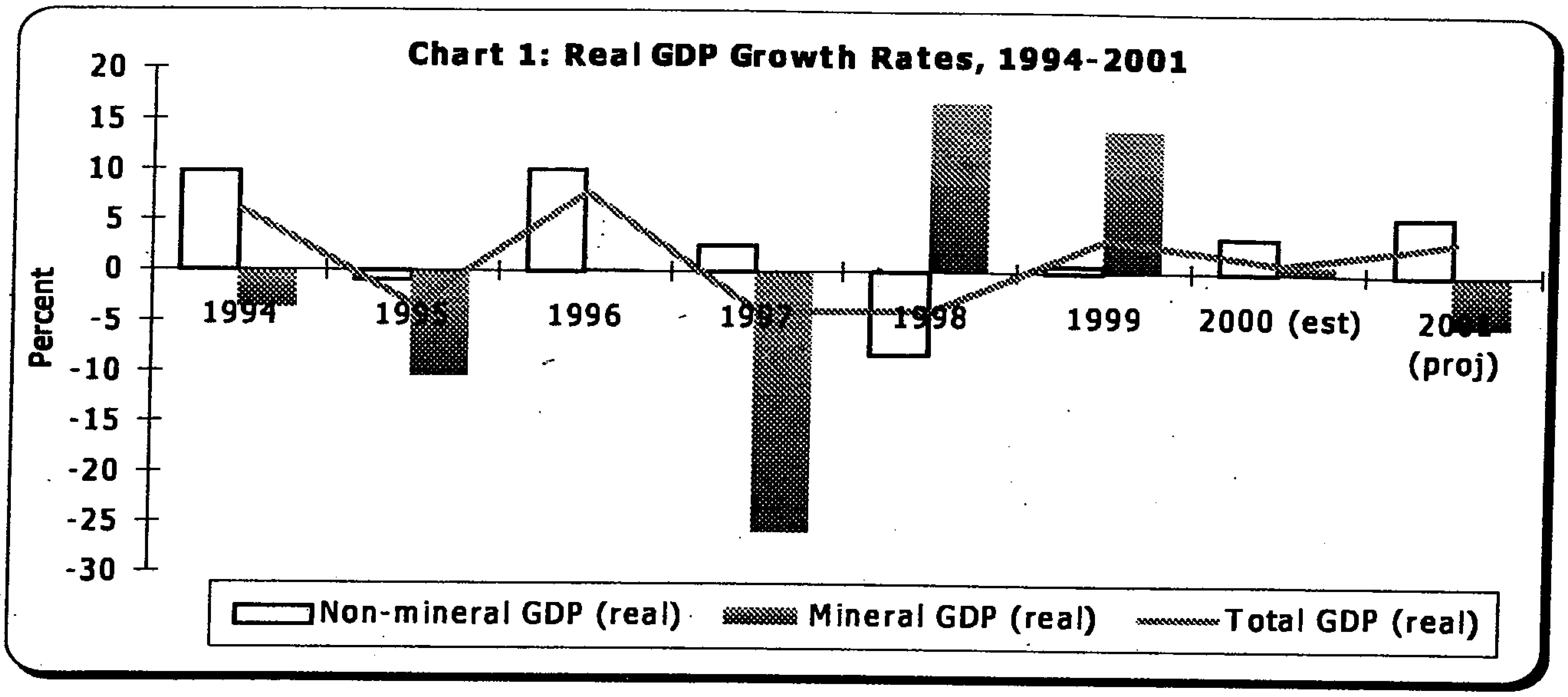
Major Central Banks maintained a tight monetary policy stance. The US Federal Reserve Bank surprised the market at the start of 2001 with a cut in the Federal Funds rate by 50 basis points to 6.0 percent. This action was taken as the Federal Reserve Bank concluded that the risk of recession is higher than that of an increase in inflation. The Bank of Japan is expected to maintain the present call rate at 0.25 percent in 2001, while the European Central Bank is expected to leave its refinance rate unchanged at 4.75 percent for the foreseeable future. In Australia, the Reserve Bank announced no change to its interest rate policy, as the slowdown in domestic activity is likely to be offset by stronger exports, and projected overall growth.

In the global financial markets, the US dollar has come under pressure against all the major currencies re-

BOX 1: OBJECTIVE OF MONETARY POLICY

The Bank of Papua New Guinea has opted to target price stability, compared to the previous broad goal of monetary stability. The main reason for setting price stability as the primary goal for monetary policy is the experiences in both developing and industrialised economies that low inflation helps to promote economic efficiency and growth in the long run, while the adverse impact of high inflation on the economy has been recognised. Maintaining price stability in a small open economy like Papua New Guinea requires amongst other things, relative stability in the exchange rate. Downward pressure on the kina exchange rate can arise from domestic sources, most commonly fiscal imbalances and increased private sector credit, and from external sources, such as developments in international markets or natural disasters.

The appropriate monetary policy response to a depreciating currency and rising inflation is a tightening of monetary conditions. In Papua New Guinea, tight monetary conditions are meant to encourage domestic residents to keep their wealth in kina denominated assets, and discourage domestic consumption and import demand. A less desirable side effect, but one which also tends to reduce imports and thus downward pressure on the exchange rate, is the decline in domestic investment. The reduction in consumption and investment will in turn impact negatively on private sector activity and growth. To obviate these negative effects of tight monetary policy, it is essential that a responsible fiscal policy that limits spending and borrowing from the domestic banking system, be adopted. This will limit the "crowding out" effect on the private sector and increase public confidence in the management of the economy.



cently, due to the increasing signs of a slowdown in economic activity, the prospects for lower interest rates in the near future, weaker US stock markets, and concerns about the size of the US current account deficit, which now exceeds 4.0 percent of GDP. The Euro, the Australian dollar and gold prices have benefited from the weakness of the US dollar.

b) Domestic Economic Activity

Preliminary estimates of economic activity indicate that total real GDP increased by around 0.8 percent in 2000 (see Chart 1), following a growth of about 3.2 percent in 1999. The year on year decline in the growth rate was due to subdued activity in the mineral sector. In 2000, production in the mineral sector is expected to fall by 7.9 percent.

In 2001, real GDP is projected to increase by 3.1 percent with growth in mining and non-mineral sectors. Growth in the agriculture/forestry/fisheries sector is forecast to accelerate to 6.5 percent in 2001, reflecting continued strong growth in cocoa production and a recovery in coffee production. Most other sectors are forecast to record growth rates consistent with their estimated long run potential in 2001. This will represent an improvement in economic conditions with better employment opportunities. Mineral production is forecast to fall by 6.5 percent in 2001.

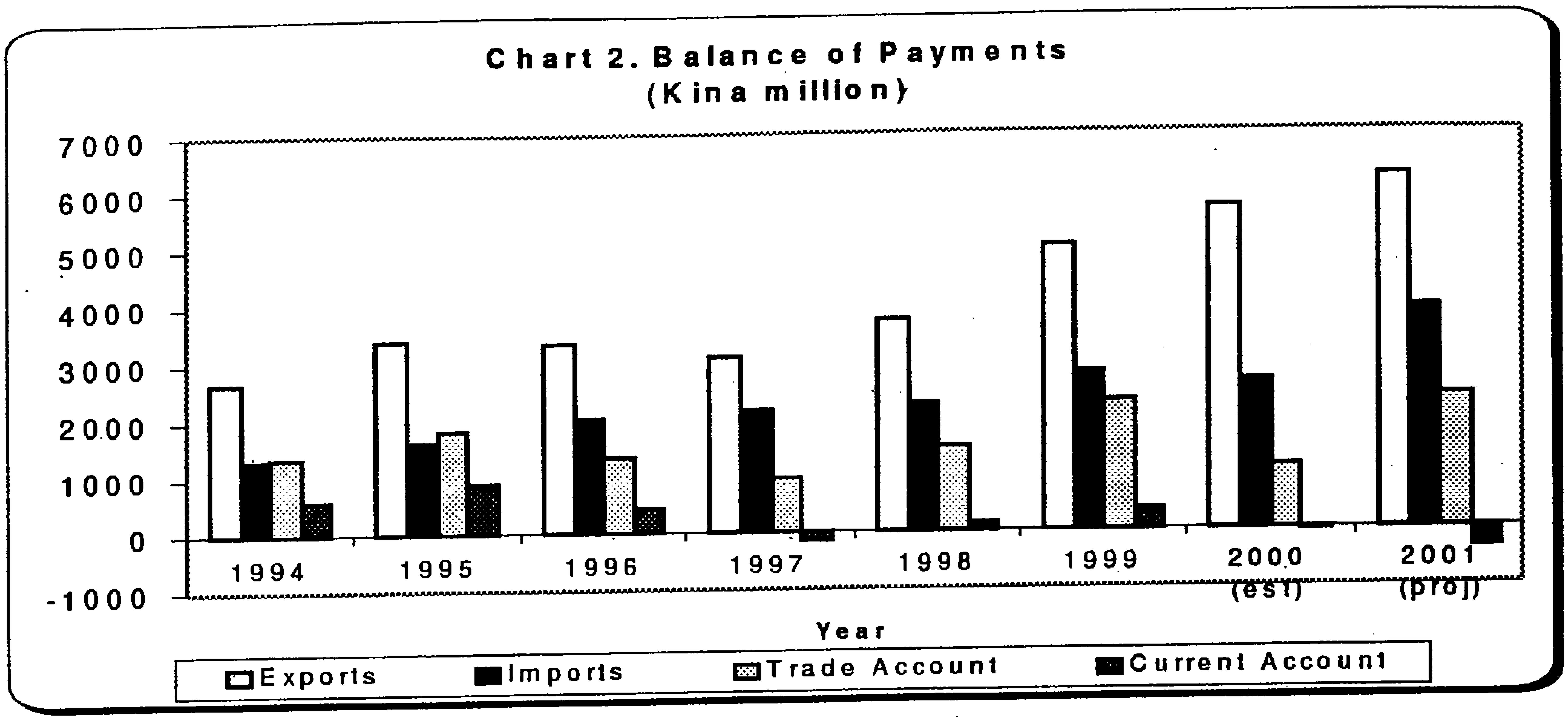
c) Balance of Payments

The balance of payments for 2000, which includes extraordinary financing associated with the Structural Adjustment Programme (SAP) is projected to show a surplus of K281 (US$92) million, compared to a surplus of K160 (US$63) million in 1999. In 2001, the surplus is projected to increase to K497 (US$162) million, reflecting surpluses in both the capital and current accounts. Extraordinary financing is projected to total K515 (US$170) million, which includes US$30 million carry-forward from 2000, and concessionary borrowings of K135 (US$45) million.

d) Fiscal operations of the Government

The fiscal strategy for the 2001 National Budget passed by Parliament in December 2000 continues to aim at providing a fiscal framework for sustainable economic growth. Its main objectives are to promote macroeconomic stabilisation in order to stimulate recovery of the economy through various reform programmes. These objectives will be funded entirely from revenue and grants, with no allowance for general budgetary financing from domestic sources.

The projected headline Budget deficit of K141 million for 2001 is 1.3 percent of GDP (Table 1), compared to an estimated 1.8 percent of GDP for 2000. The 2001 headline deficit comprises of payment of arrears of K62 million, K66 million in payments relating to structural adjustment and an underlying deficit of K14 million in the Budget. Development expenditure represents 10 percent of GDP. Net external loan draw downs of K231 million are budgeted, comprising of extraordinary financing of K424 million and net repay-



ments of K194 million in concessionary and commercial loans, respectively. Net external loan draw downs will be used to finance the fiscal deficit of K141 million and reduce K90 million in domestic debt. In addition, the budgeted asset sales receipt of K178 million will also be used to retire domestic debt. This would lead to a total net domestic debt reduction of K268 million.

e) Inflation

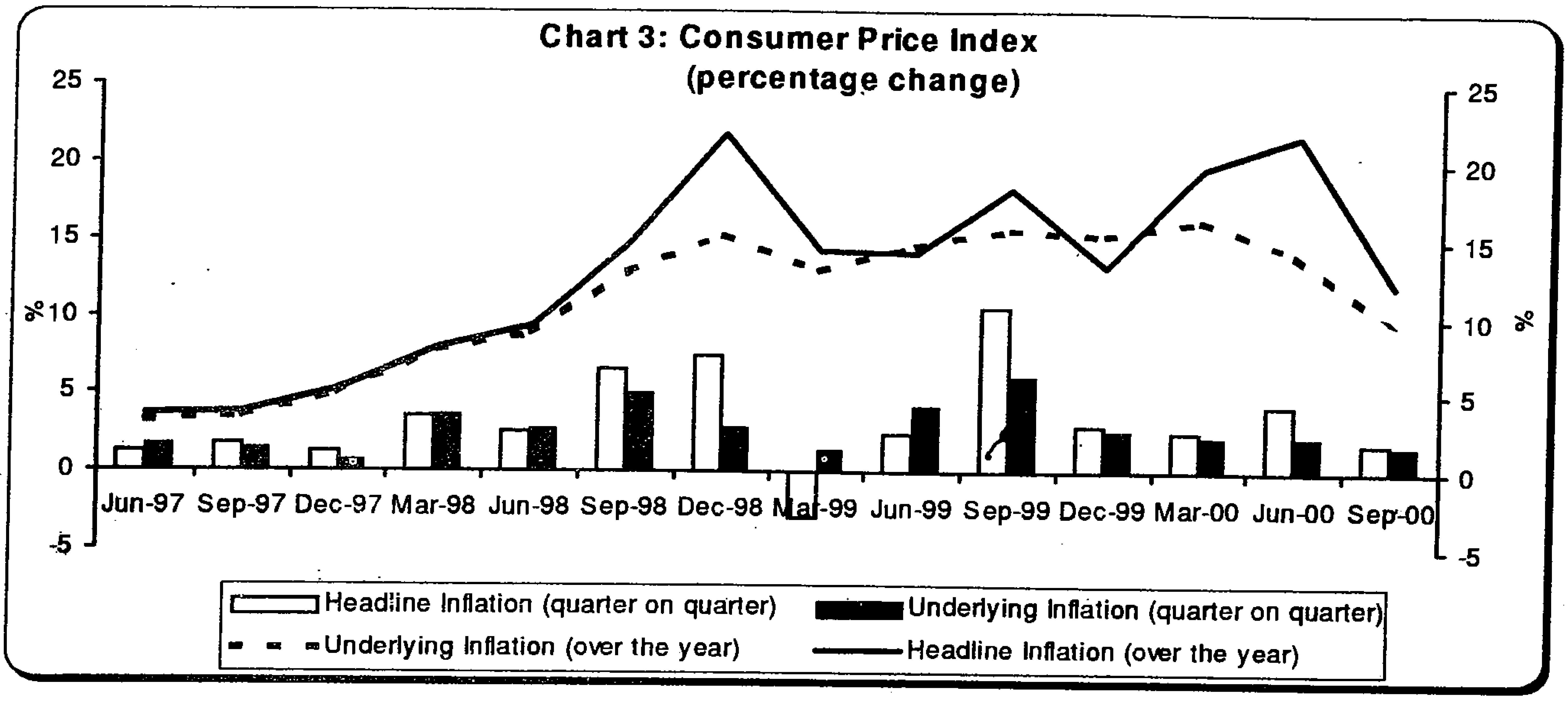
Headline Inflation

During the September quarter of 2000, headline inflation, as measured by the CPI, increased by 1.8 percent, compared with June and by 12.2 percent over

Table 1: Summary of Fiscal Operations of Government
(Kina million)

	1995	1996	1997	1998	1999	2000 Budget	Nov-00 (a)(p)	2001 Budget
Total Revenue & Grants	1722	1898	2024	1991	2569	2867	2625	3223
Total Expenditure	1756	1860	2009	2129	2801	3082	2564	3364
Deficit/ Surplus	-34	37	15	-137	-232	-215	87	-141
Percentage of GDP (%)	-0.6	0.5	0.2	-1.7	-2.5	-1.8	0.9	-1.3
Financing (net)	34	-37	-15	138	232	215	-87	141
External	-44	10	-73	-116	178	343	-43	231
Domestic	78	-47	58	254	54	-128	-44	-90
Asset Sales Financing								178
Domestic Debt Repayment								-268
BPNG	-185	-243	177	410	-35	-128	-276	n/a
Commercial Banks	266	325	-77	-350	9	0	189	n/a
Other Domestic Financing	-3	-129	-42	194	80	0	43	n/a

Source: *Quarterly Economic Bulletin*, Bank of PNG.
(a) Budget surplus may not add up due to rounding.
(p) Preliminary.



the year[1]. This compared to 4.4 percent in the June quarter of 2000 and 21.8 percent over the year to June 2000 (Table 2 and Chart 3). The lower increase in inflation can be attributed to:

- Imported inflation: The movement in the exchange rate is the most influential factor impacting on headline and underlying inflation. From September 1999 to September 2000 the daily kina exchange rate appreciated by 6.8 percent against the US dollar and 22.5 percent against the Australian dollar. The appreciation of the kina and its impact on import prices contributed significantly to the lower rate of inflation, due to Papua New Guinea's high import dependence.
- Domestic Inflation: The main factor that impacted on domestic inflation was the dropping out of the policy factors of 1999 (including the introduction of the Value Added Tax (VAT) in July 1999 and increases in excise rates in the Supplementary Budget in August 1999, which had increased inflation rates in 1999 and the first half of 2000.

Underlying Inflation

During the September quarter of 2000, underlying inflation (See Box 2), which excludes the effects of excise duties and fluctuations in the price of betelnut and fruit and vegetables on consumer prices, increased by 0.7 percent, compared with June and by 9.2 percent over the year. This compared to 2.5 percent in the June quarter of 2000 and 5.0 percent over the year to June 2000 (Table 2 and Chart 3).

Inflation Projections

Inflation is expected to be lower in the December quarter of 2000 due to the appreciation of the kina from

Table 2: Measures of Consumer Prices
(Percentage change)

		Actual 1999	Projected 2000	Projected 2001
Headline CPI	Year on Year	14.9	15.8	11.4
	Over the Year	13.2	10.6	11.9
Underlying CPI	Year on Year	16.0	12.3	9.3
	Over the Year	16.1	8.6	8.8

BOX 2: MEASURES OF INFLATION

The analysis of price changes becomes central to the assessment of macroeconomic conditions and the conduct of monetary policy, given the Central Bank's objective of achieving and maintaining price stability. The Consumer Price Index (CPI), published by the National Statistical Office, measures the changes in the cost of purchases made by households in urban centres, and is a key indicator of price changes. It has been used as the measure of 'headline' inflation in Papua New Guinea and although it is an adequate indicator for inflation over the long-term, it is not a good measure of underlying inflationary pressures that are acting on the economy over the short-term. This is because a large number of items in the CPI basket of goods and services are affected by highly volatile factors, Government policy decisions and seasonal factors. The movements in the prices of such items mask the 'underlying' or 'core' rate of inflation. An underlying rate of inflation measures the inflationary pressures in the economy that are predominantly due to market forces, i.e. changes in prices that reflect only the longer-run supply and demand conditions in the economy. As a monetary authority with the primary objective of achieving and maintaining price stability, the Central Bank has to distinguish between monetary policy action and its lagged influence on inflation. Due to this lag, monetary policy must gauge and respond appropriately to the underlying rate of inflation by removing the effect of factors assessed as temporary from the measured headline inflation rate. As a result of research conducted by the Central Bank, as of September 2000, the CPI sub-grouping of fruit and vegetables, in addition to the price effects of betelnut, excise tax and VAT increases, were excluded from the calculations of underlying inflation. The justification for these exclusions is that any monetary policy changes should be driven by longer-run supply and demand conditions, and not by the short-term effects of unpredictable seasonal commodities and Government interventions. The CPI commodity item of betelnut and sub-grouping of fruit and vegetables impact significantly on headline inflation, due to their relatively large weightings as a proportion of the total household expenditure on the CPI basket (2.7 percent and 7.0 percent for betelnut and fruit and vegetable respectively).

the end of March 2000 to the end of June 2000, which offset the carry-over effects of high inflation in the June quarter of 2000. Based on these assumptions, the projected over the year and year on year[2] headline inflation rates for 2000 are 10.6 percent and 15.8 percent, respectively.

For 2001, the projected over the year and year on year headline inflation rates are 11.9 percent and 11.4 percent respectively. These projections are based on the assumption that seasonal increases in major primary commodity exports between March and September 2001 will partially negate the lagged effect of high depreciation of the kina in the last quarter of 2000, carry-over effects of expected increases in public sector wages and a marginal increase in excise duties. Consequently, inflation is expected to decline in the second half of 2001.

The projected year on year and over the year underlying inflation rates, for 2001, are 9.3 percent and 8.8 percent, respectively compared to 12.3 percent and 8.6 percent, respectively for 2000. These rates compare favourably with the projected headline rates because projected seasonal price changes of betelnut and fruit and vegetables are higher than the average price changes in the other commodity items in the CPI basket. In addition, Government excise rates introduced on alcohol and tobacco during 2001 have also been excluded.

f) Monetary and Financial Market Developments

The Central Bank reaffirmed its commitment to maintain a tight monetary policy stance in the second half of 2000, in a continued effort to mitigate downward pressure on the exchange rate. In the September quarter, inflation declined as a result of the appreciation of the kina in the June quarter, but not by as much as earlier expected. Official interest rates declined (Chart 6) with the 182 days treasury bill rate falling from

[1] Over the year is a point on point percentage increase. Example, for the September quarter of 2000, the over the year percentage increase in headline inflation is the percentage change in the September quarter 2000, on the September quarter 1999.

[2] Year on year inflation is the percentage increase in the average quarterly inflation indices for two consecutive years. Example, for the December quarter of 2000, the percentage change in the average quarterly price indices over 2000 against the average quarterly price indices over 1999.

16.0 percent in July to 14.9 percent at the end of December 2000. Consistent with the decline in the official rates, the weighted average lending and deposit rates also declined from 17.4 and 15.5 percent in July to 17.1 and 12.5 percent respectively, in November 2000. In addition, some of the commercial banks reduced their indicative lending rates in the second half of the year.

The decline in interest rates was a result of the downward adjustment in inflation expectations by the market and a reduction in domestic financing requirement of the Government in 2000. The reduction in interest rates did not signal any easing of the monetary policy stance by the Central Bank, which remained unchanged as a result of the unexpected adverse developments in the foreign exchange market following the decline in receipts from major agricultural exports. Based on these developments, an easing of the monetary policy stance by the Central Bank in the second half of 2000 was considered to be inappropriate.

The level of broad money (M3) increased by 5.6 percent between July and November 2000 (see Chart 4), as a result of an increase in net foreign assets of the banking system, which more than offset a decline in net credit extended by the banking system.

The Central Bank continued to utilise its open market operation instruments in implementing monetary policy in the second six months of 2000, with no changes made to both the CRR and the Minimum Liquid Assets Ratio (MLAR).

From end June 2000 to end December 2000, the kina depreciated by 20 percent against the US dollar, by 14 percent against the Australian dollar, by 13 percent against the Japanese yen and by 18 percent against the Euro (see Chart 5). The Central Bank intervened in the foreign exchange market to smooth out short-term volatility in the exchange rates.

2. MONETARY POLICY

(a) Monetary Policy Stance

In line with its objective of achieving and maintaining price stability, the Central Bank will continue to assess market developments and key macroeconomic indicators that impact materially on future inflation performance. This includes:

- Previous and prospective movements in the exchange rate;
- Maintenance of positive (forecast) real interest rates over the reference period;
- Developments in relevant money and credit aggregates;
- Implementation of the 2001 National Budget, including draw down of the external extraordinary financing and implementation of the privatisation programme; and
- Retirement of domestic debt by the Government.

The depreciation of the kina in the second half of 2000, which was mainly caused by unfavourable international prices for Papua New Guinea's major exports and a poor coffee crop, implies that there is a risk of inflationary pressure in 2001. Consequently, the Cen-

Chart 4: Monetary Aggregates (Kina million)

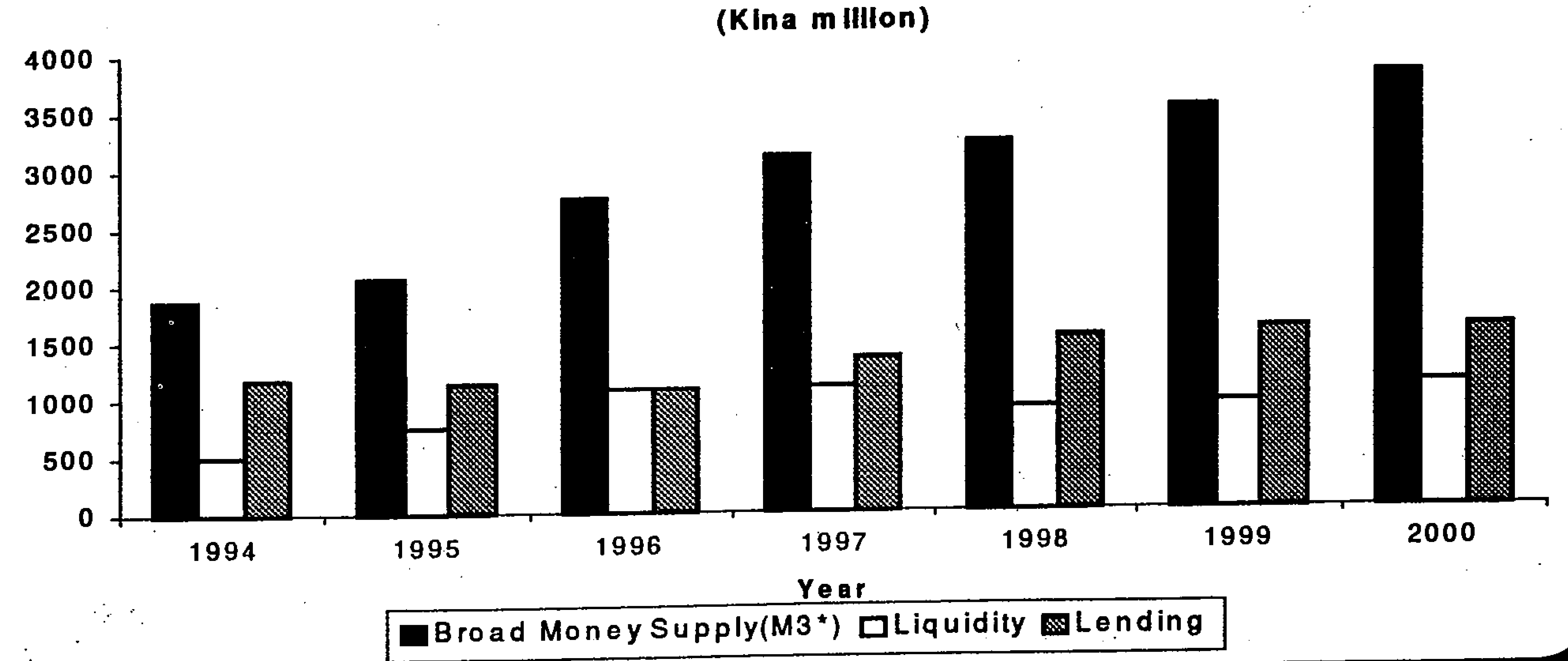
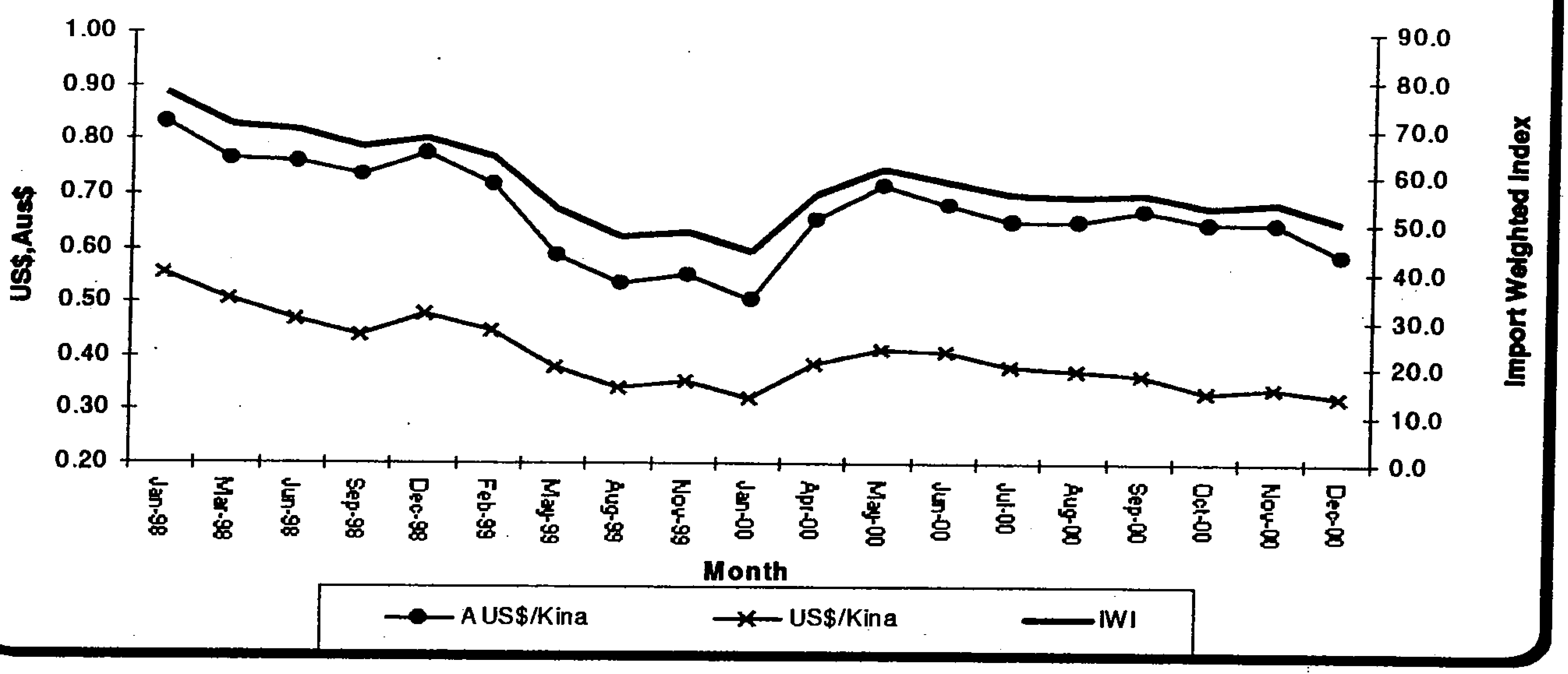


Chart 5: Kina exchange rate against US$,Aus$ and Import Weighted Index



tral Bank will take a cautious approach to any easing of monetary policy stance during the period covered in this statement. However, in 2001 the underlying inflation rate is expected to trend downwards, with the average and over the year underlying inflation rates projected at around 9 percent, which compares favourably to inflation rates in 2000. It is important to note that the projected lower underlying inflation rate for 2001 is based on the following assumptions:

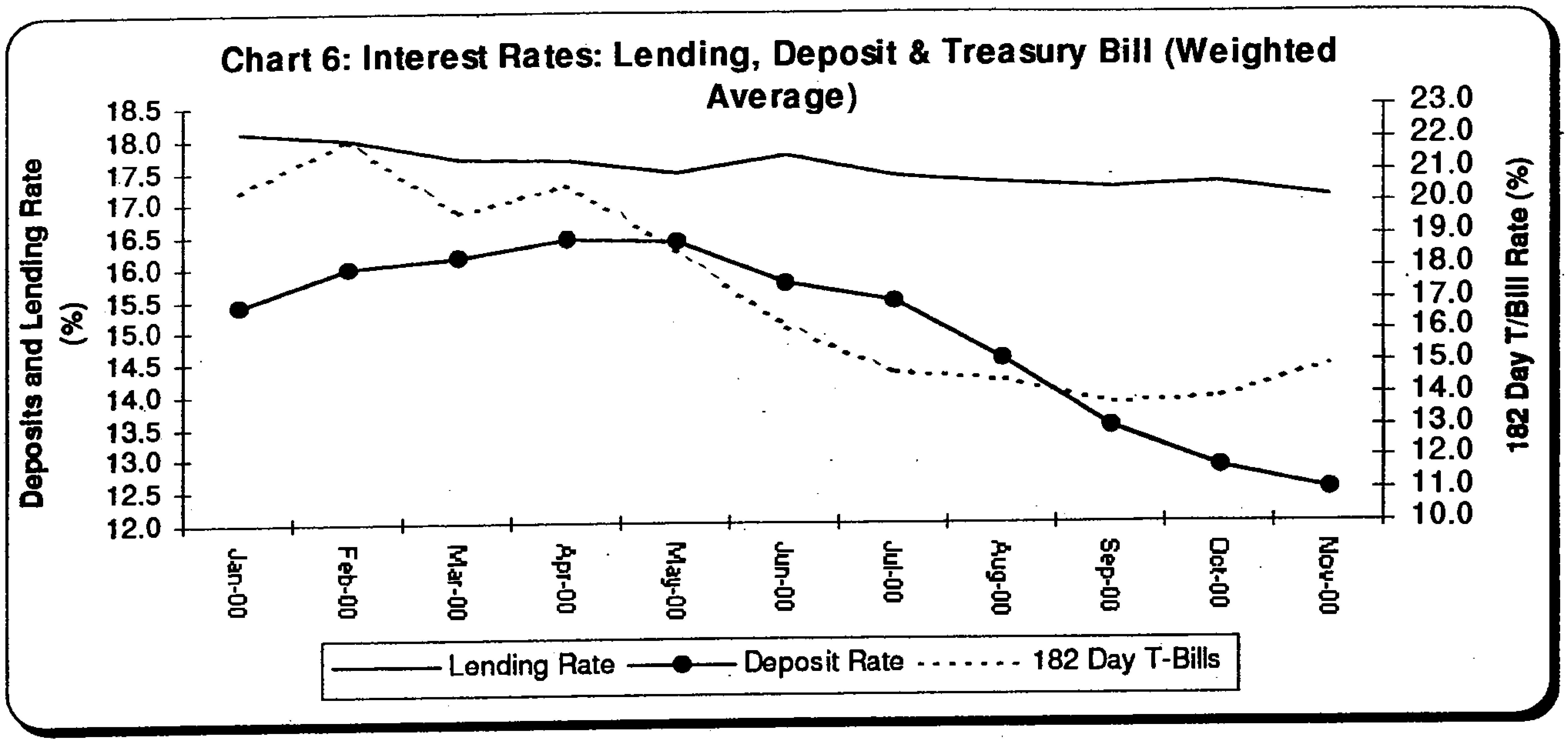
- Strengthening of the balance of payments, mainly as result of recovery of primary commodity exports and improvement in the capital account;
- Macroeconomic stabilisation and structural reform programme remaining on track, including draw down of K515 (US$170) million in external financing (including US$30 million carry-forward from 2000), realisation of budgeted privatisation receipts and retiring of domestic debt as per the 2001 Budget; and
- Maintaining of a responsible fiscal stance by the Government (e.g. minimising of the fiscal deficit, continued strengthening of expenditure controls, improvements in tax administration and collections, and less reliance on domestic financing of the Budget deficit).

If these assumptions hold, the Central Bank will be able to begin to gradually ease monetary conditions in 2001 by lowering official interest rates. The gradual easing of interest rates would be consistent with lower inflation expectations for 2001 and would stimulate real growth in private sector credit, which is essential to achieve the projected real non-mineral GDP growth of 3.1 percent in 2001. By using privatisation proceeds and foreign financing to retire domestic debt the Government will significantly reduce 'crowding out' of the private sector on the domestic financial market and increase available funds for productive private sector investment. In this framework monetary and credit aggregates are expected to develop as follows in 2001:

- Growth in broad money (M3) of 7 percent;
- Growth in reserve money of 12 percent;
- Expansion in credit to the private sector of 12 percent, consistent with the objective of growth in the non-mineral private sector; and
- Decline in net domestic credit to Government of 20 percent by the banking system.

The Central Bank will reassess inflation expectations and adjust the timing and extent of monetary easing in the event of any adverse developments in the key macroeconomic conditions underpinning inflation projections and monetary developments. The risk factors that can lead to instability in the kina exchange rate and a break-out in inflationary pressures include any unexpected adverse developments in the foreign exchange market. This would occur if agricultural export inflows are lower than expected.

In summary, there have been a number of positive developments in key macroeconomic indicators in the



second half of 2000, including: an increase in mineral sector exports, a decline in net domestic credit to Government and a downward trend in the inflation rate. However, there was a decline in agricultural exports, which resulted in the depreciation of the kina. Although inflation trended downward, it did not fall by as much as expected. Consequently, the Central Bank does not expect an immediate easing to monetary conditions. However, if the assumptions that underpin the downward trend in underlying inflation in 2001 hold, the Bank will be able to gradually ease its monetary policy stance. The pace and extent of adjustment will be strongly influenced by the risks associated with the sustainable achievement and maintenance of price stability in Papua New Guinea.

b) Conduct of Monetary Policy

Consistent with the Bank of Papua New Guinea's objective of achieving and maintaining price stability, the conduct of monetary policy will be operated within a reserve money framework. Reserve money is defined as currency in circulation and deposits of commercial banks with the Central Bank and, along with the level of liquid assets in relation to statutory requirements, is an indicator of the capacity of the banking system to finance new lending. This affects demand and ultimately inflation, especially through the influence of the balance of payments on the exchange rate. During 2001, reserve money is expected to increase by 12 percent following a decrease of 19 percent in 2000, as a result of the tight stance of monetary policy pursued by the Central Bank. The expected growth in reserve money is likely to have minimal impact on inflation, and the Central Bank will continue to use its open market instruments to sterilise any excess reserve money in the banking system.

In line with the policy to reduce domestic debt, the Government retired a net of K55 million in treasury bills to November 2000. However, in December 2000 the Government issued K80 million of new treasury bills. The stock of treasury bills is expected to fall further as the Government retires additional debt in 2001.

To improve efficiency of transmission of the monetary policy stance, the Central Bank will introduce a new price based signalling mechanism from 5 February 2001. Under the new system, the Central Bank will announce the Kina Auction Rate (KAR) to the market on the first Monday of each month as a benchmark rate. Any changes to the KAR will reflect the monetary policy stance taken by the Central Bank based on prevailing economic conditions and expected developments. At its inception, the KAR will be based around the weighted average rate for 28 days treasury bill set at the previous week's (week ending 2 February 2001) auction.

The Kina Auction Facility will remain a seven (7) day facility. To counter arbitrage opportunities and prevent the KAR from becoming a substitute for investment in Government securities and trading in the inter-bank market, a margin below the KAR will be applied to

BOX 3: RELATIONSHIP WITH GOVERNMENT

The following changes were made in the relationship between the Government and Central Bank consistent with the requirements under the Central Banking Act 2000, in order to strengthen the transparency of the commercial relationship between the Government and Central Bank and facilitate the achievement and maintenance of price stability:

In line with the separation of debt management from the conduct of monetary policy, which commenced in 2000, the Government and Central Bank agreed in August 2000 to use the weighted average interest rates for different maturities, determined at the Government's weekly treasury bill auction, for payment of interest on the Bank's holdings of treasury bills. The use of this market determined rate provides for the Central Bank to be considered as a market participant for trading in Government securities.

Consistent with Section 55 of the Central Banking Act 2000, the Government and Central Bank agreed on an Operational Arrangement relating to the terms and conditions of the Temporary Advance Facility, effective from 02 January 2001. The Arrangement provides for the advances to the Government to be determined from the daily net balances in the operational accounts held with the Central Bank, and to ensure that the operational overdraft limit of K100 million is not breached and the amount fully repaid within six months of the initial disbursement. The Central Bank will charge interest on the daily outstanding balance of Temporary Advance based on the 182 days treasury bill rate determined at the previous week's auction conducted for Government. In addition, the Central Bank will pay interest on daily net credit balance of the Government's operational accounts only in cases where there is no outstanding balance of Temporary Advance. The interest will be based on the average rate for on-call deposits in the previous week determined from the daily returns of commercial banks.

funds deposited with the Central Bank (buy kina), while a margin above the KAR will be charged for lending (sell kina) to the commercial banks. During the transition period, and to prevent the Kina Auction Facility from being the main source of lending and investment of liquidity by the banking system, purchases and sales under the facility will be limited. In addition, all relevant market interest rates are expected to move in synchronisation with any change in the KAR.

To strengthen the signalling mechanism of monetary policy and ensure that the market interest rates and transactions are conducted around the announced KAR, the Central Bank will also introduce a Stand-by Repurchase Facility (SRF) on 5 February 2001 for daily liquidity management. This liquidity management instrument will be used at the discretion of the Central Bank with the buy and sell margins set around the KAR. The SRF will involve assignment of Government securities as collateral against any over-night lending and borrowing transaction between the commercial banks and the Central Bank, which are reversed on the following working day. The Central Bank will initially limit the volumes under the SRF, so that the banks are encouraged to utilise the inter-bank over-night market to fund their liquidity requirements. The price based signalling mechanism combined with the complementary SRF are expected to realign the linkage between treasury bills, deposits and lending rates to increase the efficiency in transmission of monetary policy, facilitate a downward shift in the entire interest rate structure and result in a predictable yield curve.

The tap facility continues to encourage purchases of treasury bills by the non-bank entities and individuals directly from the Central Bank at interest rates which are 1.0 percentage point below those obtained during the weekly auction. Its existence also enhances competition for funds, thereby making deposits and lending rates more responsive to changes in treasury bill yields. The Central Bank will retain the facility in 2001 to actively promote the sale of treasury bills on tap to the non-bank financial sector. The Kina Auction Facility and SRF will be utilised for short-term liquidity management, while the MLAR and CRR will be continuously reviewed to determine their appropriate levels consistent with the stance of monetary policy.

Copies of the semi-annual Monetary Policy Statement can be obtained from the Manager, Public Information Unit at the Bank of Papua New Guinea on telephone number 3227 326 or fax number 3200 757.

Box 4. STRUCTURAL REFORMS AT THE BANK OF PAPUA NEW GUINEA

As part of the financial sector reform of the Government in 2000, structural reforms of the Bank of Papua New Guinea were considered necessary to achieve stability of the economy in the medium term. A new Central Banking Act (CBA 2000) was passed by Parliament and became effective on 16 June 2000, while the revised Banks and Financial Institutions Act (BFIA 2000) was passed by Parliament in April 2000. In addition, new Life Insurance and Superannuation Acts were passed by Parliament in November/December 2000, which enables the Central Bank to regulate and supervise the life insurance and superannuation industries. These new responsibilities will be initially taken over by the Central Bank with a view to separate it out in the future.

Under the CBA 2000, significant changes were made in the relationship between the Bank and the Government, which include: introducing price stability as the monetary policy objective; separating debt management from the conduct of monetary policy; limiting Central Bank credit to the Government to an operating overdraft of up to K100 million; and appointment of the Governor for a fixed term of five to seven years.

Greater independence and stronger powers to the Central Bank and the Governor demands greater accountability and transparency to Parliament and the public. The Central Bank is therefore required to publish semi-annual monetary policy statements, outlining developments, projections and the policy stance, which will enhance the effectiveness of the transmission of monetary policy. The first statement was released on 14 July 2000, and this is the second statement. The new Board of the Central Bank, comprising the Governor, two Deputy Governors, the PNG Trade Union Congress, PNG Council of Churches, Securities Commission, PNG Chamber of Commerce and Institute of Accountants, as well as two appointees by the Minister, is responsible for advising and reviewing the performance of the Governor. The Governor is now responsible for Monetary Policy and the Regulation of Banks and Financial Institutions. Besides an annual audit, the Minister for Finance and Treasury may at any time call for an external managerial or financial audit of the Bank. Conditions relating to the dismissal of the Governor and the Deputy Governors are more streamlined, but with any removal transparent and open.

The BFIA 2000 aims to broaden the scope and improve the effectiveness of financial sector regulation, drawing on international best practices. The Act:

- Gives full responsibility to the Central Bank for licensing and supervising banks and other authorised deposit taking institutions;
- Strengthens information gathering and investigative powers;
- Enables vetting of directors and senior managers of financial authorised institutions;
- Effectively prohibits pyramid schemes which have been a major problem in recent times; and
- Introduces stronger and more credible penalties.

In August 2000, the Central Bank used the new Act to remove the Board of the PNG Banking Corporation, Nambawan Finance, Village Finance and Rural Development Bank over concerns of their weak governance, breach of exposure limits and short-comings in their management structure and capabilities. The Central Bank also undertook legal action against several fast-money schemes, but could not prevent many people being deceived by them, despite an intensive campaign. Two such schemes were liquidated in 2000. In 2000, the Central Bank, through a liquidator, liquidated 76 dormant savings and loan societies as part of its revitalisation programme.

Problems have also emerged in the pension industry. The National Provident Fund is currently under review by a Commission of Enquiry appointed by Government.

The new Superannuation legislation creates a licensing, prudential and supervisory regime for superannuation funds, trustees, investment managers and fund administrators operating in the industry. The new Act:

- Requires authorised superannuation funds or licence holder to provide the Central Bank with information including financial statements and details of the officers of the corporate entity;
- Ensures compliance with prudential standards issued by the Central Bank;
- The Central Bank may appoint a competent person to investigate a licence holder;
- The Central Bank can issue directions to regulate activities of a licence holder if it has contravened a prudential standard or condition of its licence; and
- The Central Bank may appoint a statutory manager to take control of a licence holder.

The new Life Insurance Act establishes a framework for the regulation of the life insurance industry and entities operating as life insurance companies or brokers. The Act:

- Imposes conditions on any licence holder;
- Ensures compliance with prudential standards issued by the Central Bank;
- Requires a licence holder to provide information to the Central Bank;
- The Central Bank may appoint a competent person to investigate a licence holder;
- The Central Bank can issue directions to regulate the activities of a licence holder; and
- The Central Bank can appoint a statutory manager to take control of a licence holder.

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