Papua New Guinea liquidity crisis sees new calls for Australian intervention

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The Papua New Guinea economy is headed for its fourth consecutive year of contraction, producing a full-blown liquidity crisis for the government of Prime Minister Sir Michael Somare. Treasury and Finance Minister Bart Philemon last month told the Business Council of PNG that the economy was still shrinking despite his previous forecast of two percent growth.

Facing a shortfall of K340 million ($US95 million) in the 2003 budget, the government has borrowed domestically at commercial rates just to pay the wages bill for doctors and teachers. The withholding of an Asian Development Bank (ADB) loan and lack of anticipated revenue from privatisation have intensified the government's problems.

Starved of government funds, hospitals and other service providers have been forced to scale down operations. According to the PNG newspaper *Post Courier*, at the end of May the Angau Hospital had no money for food while nationally 5,000 teachers, as well as all first-year doctors, had not been paid.

More generally, social infrastructure is rapidly deteriorating. The availability of rural health services has declined over the past decade. Primary education enrolment rates are well below the regional average with nearly 75 percent of young children leaving school between grades Eight and Twelve. Almost two-thirds of children in the poorest 25 percent of households are under-nourished.

The government's domestic borrowing has intensified the already rampant inflation. The cost of living rose by 6.9 percent in the three months to the end of March, sending the annual rate to 20.7 percent. Food, drinks and tobacco are the worst affected and have the greatest impact on households. Food costs rose by 23.7 percent in the 12 months to March.

These results will only worsen because PNG's major revenue earners, mining and petroleum, are in decline. Last year saw the poorest export results for a decade, almost K200 million less than 2001.

International financial pressure on the government is mounting. The ADB withheld the K140 million loan, accusing the government of replacing National Fisheries Authority head Dr Anthony Lewis, an expatriate Australian, with retrenched officer Molean Chappau as a political rather than merit-based appointment. The ADB and World Bank are intent on undermining PNG's old political ties and patronage and imposing economic restructuring.

A senior government official quoted in the *National* on June 5 highlighted the sharpness of the fiscal crisis. "The government has yet to come up with a contingency plan to save itself from inevitable collapse. Right now, we are struggling to get funds for basic things. There is no money to meet costs of recurrent expenditure. The public servants are not working, they are not performing because they have no resources to do their job."

A number of businessmen have publicly aired their dissatisfaction with the Somare government. PNG Chamber of Commerce and Industry president Michael Mayberry drew a pointed comparison with neighbouring Solomon Islands, where the economic and political structure has all but collapsed. "Businesses are really struggling. Tragically we're heading the same way as the Solomon Islands".

On May 6, an *Australian Financial Review* article observed that some interest rates had reached 33 percent and that the PNG business community, after giving the new government "eight months grace" was now raising "a despairing voice about the country's future".

The economic decline in PNG has been the subject of a number of Australian reports demanding a more aggressive approach from Canberra toward its former colony. In March the conservative Centre for Independent Studies (CIS) released the *Papua New Guinea on the Brink* report, advocating a "more activist approach".

If necessary, the Australian government should ignore "charges of neocolonialism" and intervene militarily to prevent the country descending into "terminal decline". This call caused a furore in PNG. One of the co-authors, Mike Manning, a major business figure in PNG, was hauled before a Parliamentary Privileges committee to face possible charges of contempt of parliament.

A month later, CIS Senior Fellow Professor Helen Hughes, previously a World Bank director of economic analysis, released another document, entitled *Aid has Failed the Pacific*. She argued that Australia should suspend all aid to PNG in order to force the government to impose harsher austerity measures. “Removing aid flows from budgets is essential if Pacific governments are to reform their economies and hence balance their budgets,” she insisted.

In PNG, where the health system relies on external funding, this policy would rapidly lead to the deaths of thousands of people. Hughes declared that such a policy change would be unlikely, saying, “radical policy changes will be difficult”.

Her next best option was for funds only to “be disbursed on the evidence of met targets and audited expenditures” and “under the principle of mutual obligation”. In other words, aid would be forthcoming only if PNG pursued even more energetically policies such as privatisation, cuts in government expenditure and the opening up of the economy to investment.

Another report, *Our Failing Neighbour*, released on June 10 by the Australian government’s Strategic Policy Institute called for a multinational force of about 150 police, led by Australia, to restore law-and-order in the Solomons. The report underscored the extent to which the Australian government has dispensed with formal adherence to national sovereignty. As the *Australian* pointed out, the new policy “sends an unmistakable message to the rest of the South Pacific: Australia is prepared to intervene if necessary”.

The Murdoch-owned *Australian* of 29 May put the case for intervention most bluntly: “Papua New Guinea, and even more so the Solomon Islands, have huge numbers of utterly alienated young men with poor education, no prospects, a violent society and access to guns in large numbers. If we have to help these societies it will almost certainly involve the army.”

Only eight months old, Somare’s shaky 13-party coalition government faces an intractable dilemma. It has vastly inadequate resources to deal with the massive social problems, including a predicted AIDS epidemic. At the same time, Australia holds the purse strings of desperately needed funds and is demanding the continued imposition of an IMF-backed Structural Adjustment program. These policies are creating the social nightmare that underpins PNG’s chronic instability.

The economic pressure has already exacerbated divisions within the ruling coalition. According to the *Post Courier*, Somare’s party the National Alliance has for some time operated as “three splinter groups”. During May, a rift opened up within the National Alliance between Somare and Philemon.

During one parliamentary session, Philemon took an open swipe at Somare when he was asked to explain the failure to raise the budgeted K200 million from the sale of government enterprises. “I really don’t know what the government position is,” he declared, knowing that Somare has equivocated on the selling of government assets and holds the privatisation portfolio.

Several articles in the PNG media predicted that Somare was about to reshuffle his cabinet, sacking Philemon. According to the *Post Courier*, it was a pre-emptive move against a potential leadership challenge.

The National Alliance’s failure to win any of the six seats up for grabs in the recently completed Southern Highlands election campaign added to the rifts. Not only was the result a slap in the face for Somare who campaigned personally in the final weeks of canvassing, it added to the instability by changing the balance of forces within the coalition. The Peoples Labour Party, Peoples Action Party and Peoples Progress Party each won a seat, making it likely they will expect more say in the allocation of major cabinet positions.

In a surprise move at the end of May, Somare announced that Philemon was not in line to be sacked and would eventually succeed him as National Alliance leader. This was warmly welcomed in the business community where Philemon is seen as pro-business, having served as treasurer in the previous right-wing Morauta government.

Rumblings are continuing within the government. In March, its parliamentary backbenchers threatened to withhold support for the government on major legislation because they had not received their Development Funds of K500,000 each. MPs’ control of these slush funds is regarded as crucial to securing re-election. While the government is legally obliged to pay the grants, it claims that there is simply not enough money in the coffers.

With the international financial pressure thus destabilising Somare’s coalition, the conditions are being created for an economic and political breakdown that could serve as the trigger for direct Australian intervention.