



# TECHNICAL ASSISTANCE REPORT

## PAPUA NEW GUINEA

### Financial Sector Stability Review

**September 2024**

**Prepared By**

Vassili Prokopenko (mission chief), Safari Kasiyanto (both – MCM), Geoffrey Bascand, Vern McKinley, Paula Oliveira, Rodolfo Wehrhahn (all – MCM STXs), and Nelson Rutto (STA)

**Authoring Department:**

**Monetary and Capital Markets  
Department**

Nexus Reference: **15464396**

Mission ID: **25MMD60**

Funding Program ID: **STA\_IMF\_2018\_01, MCM FSSR MAIN (MCM\_IMF\_2018\_12)**

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International Monetary Fund, IMF Publications  
P.O. Box 92780, Washington, DC 20090, U.S.A.  
T. +(1) 202.623.7430 • F. +(1) 202.623.7201  
[publications@IMF.org](mailto:publications@IMF.org)  
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# Acknowledgments

## FSSF

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This technical assistance mission was made possible thanks to the financial support of Financial Sector Stability Fund (FSSF). The FSSF is a thematic fund whose overall objective is to promote financial sector stability in low and lower-middle income countries and fragile and conflict-affected states. The FSSF Phase I has nine donor-partners: China, European Investment Bank, Germany, Italy, Luxembourg, Saudi Arabia, Sweden, Switzerland, and UK.

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# Glossary

|        |                                                         |
|--------|---------------------------------------------------------|
| ACH    | Automated Clearing House                                |
| ANZB   | Australia and New Zealand Banking Group                 |
| ASF    | Authorized Superannuation Fund                          |
| BFIA   | Banks and Financial Institutions Act                    |
| BPNG   | Bank of Papua New Guinea                                |
| BSP    | Bank of South Pacific                                   |
| CAMELS | Capital Asset Management Earnings Liquidity Sensitivity |
| CBA    | Central Banking Act                                     |
| ELA    | Emergency Liquidity Assistance                          |
| FIRRM  | Financial Institutions Risk Rating Model                |
| FSC    | Financial Stability Committee                           |
| FSIs   | Financial Soundness Indicators                          |
| FSR    | Financial Stability Report                              |
| FSSR   | Financial Sector Stability Review                       |
| IAG    | Independent Advisory Group                              |
| ICCC   | Independent Consumer and Competition Commission         |
| IPT    | Instant Payment Transactions                            |
| KATS   | Kina Automated Transfers Systems                        |
| LFA    | Licensed Fund Administrator                             |
| LIM    | Licensed Investment Manager                             |
| MCM    | IMF's Monetary and Capital Markets Department           |
| MoU    | Memorandum of Understanding                             |
| MPSU   | Macro-Prudential Supervision Unit                       |
| NPC    | National Payment Council                                |
| NPS    | National Payment Systems                                |
| PGK    | Papua New Guinean Kina                                  |
| PSO    | Payment Systems Operators                               |
| PSOD   | BPNG's Payment System Operation Department              |
| PSODF  | BPNG's Payment System Oversight Function Department     |
| PSP    | Payment Service Provider                                |
| REPS   | Retail Electronic Payment Systems                       |
| RTGS   | Real-Time Gross Settlement                              |
| S&LSs  | Savings and Loans Societies                             |
| STA    | IMF's Statistics Department                             |

# Preface

At the request of the Bank of Papua New Guinea (BPNG), a Financial Sector Stability Review (FSSR) mission from the IMF's Monetary and Capital Markets Department (MCM) and Statistics Department (STA) visited Port Moresby, Papua New Guinea, during the period June 20-July 1, 2024. The main objective of the FSSR diagnostic mission is to help countries build a roadmap of technical assistance (TA) to address identified financial sector needs and gaps, with a view to strengthen resilience of financial institutions and to enhance the policy framework.

The mission team held discussions with Governor Genia, management, and staff from BPNG, Department of Treasury, Office of Insurance Commissioner, and representatives from financial institutions. The team is grateful to the BPNG's management and staff for the excellent organization of the mission and their warm hospitality.

# Executive Summary

**Over the past few years, the PNG authorities have made efforts to strengthen the financial sector stability framework.** Guided by the Financial Sector Development Strategy 2018-30, the Bank of Papua New Guinea (BPNG) embarked on several reforms, which included development of key elements of the macroprudential policy framework, adoption of several banking regulations, launch of a new bank rating model, and modernization of its payment systems. Work is under way to strengthen the legal framework, including by adopting amendments to the Central Bank Act and several other overarching laws, which should further enhance the policy framework.

**Despite progress, many weaknesses and challenges remain.** The mission found that BPNG should improve the effectiveness and impact of the systemic risk analysis and macroprudential policymaking in the areas of risk reporting, stress testing, public communication, and internal organization. Work should continue to upgrade the regulatory and supervisory frameworks for deposit-taking financial institutions, superannuation funds, and insurance companies. Many aspects of the financial safety net and crisis preparedness framework need improvement, including broadening the resolution powers of BPNG and enhancing the emergency liquidity assistance arrangements. The payment system policy and oversight functions require strengthening. A comprehensive prudential regulation for e-money providers should be established. Further improving the compilation and management of financial sector data will also be important.

**This report highlights key areas that require improvement and delivers a roadmap of possible technical assistance (TA) to support financial sector reforms (Table 1 and Annex I).** The recommendations are grouped into six areas: (i) macroprudential policy; (ii) regulation and supervision of banks and other deposit-taking financial institutions; (iii) regulation and supervision of insurance companies and pension funds; (iv) financial safety net and crisis preparedness framework; (v) financial market infrastructure; and (vi) financial sector statistics.

**Several important preconditions are required for the successful implementation of the proposed TA activities.** These preconditions include a supporting legal framework and an adequate TA absorption capacity. While these issues are mentioned in the report, it should be noted upfront that any recommended legal changes may take an unpredictable amount of time. As to absorption capacity, the BPNG faces high staff turnover in some departments responsible for financial stability work, and the Office of Insurance Commissioner is also facing human resource constraints. These issues may necessitate adjustments to the pace and focus of the proposed TA activities.

**Table 1. Key FSSR Recommendations**

| Recommendations                                                                                                                          | Priority | Timeframe 1/ |
|------------------------------------------------------------------------------------------------------------------------------------------|----------|--------------|
| <b>Systemic Risk Analysis</b>                                                                                                            |          |              |
| Operationalize a Financial Stability Committee with supporting charter and procedures                                                    | High     | Short term   |
| Develop more systematic and structured systemic risk reporting for regular FSC review                                                    | High     | Short term   |
| Develop the capacity to undertake stress testing by ensuring adequate models, data availability, and trained staff                       | High     | Medium term  |
| Adopt a communications strategy for financial stability                                                                                  | Medium   | Short term   |
| <b>Regulation and Supervision of Deposit-Taking Financial Institutions</b>                                                               |          |              |
| Amend the BFIA to broaden the range of corrective measures and facilitate consolidated supervision                                       | Medium   | Medium term  |
| Effectively implement the regulations developed with the assistance from PFTAC                                                           | High     | Short term   |
| Improve the supervisory data management at BPNG                                                                                          | High     | Short term   |
| <b>Regulation and Supervision of Insurance Companies</b>                                                                                 |          |              |
| Harmonize the regulations and supervisory methods for insurers                                                                           | High     | Medium term  |
| Upgrade the capital requirement for both life and general insurers                                                                       | Medium   | Medium term  |
| Transition into a risk-based supervision framework                                                                                       | Medium   | Medium term  |
| <b>Financial Safety Net and Crisis Management</b>                                                                                        |          |              |
| Amend the BFIA to address resolution powers; recovery and resolution plans; and cross-border resolution coordination, among other topics | Medium   | Medium term  |
| Operationalize the Financial Services Council                                                                                            | High     | Short term   |
| Finalize procedures for emergency liquidity assistance                                                                                   | High     | Short term   |
| Develop recovery and resolution plans for the systemically important Bank South Pacific                                                  | Medium   | Medium term  |
| <b>Financial Market Infrastructure</b>                                                                                                   |          |              |
| Strengthening the oversight functions of payment systems                                                                                 | High     | Short term   |
| Establish comprehensive prudential regulation for e-money providers                                                                      | Medium   | Medium term  |
| <b>Financial Statistics</b>                                                                                                              |          |              |
| Improve the quality of financial soundness indicators data                                                                               | High     | Short term   |
| Improve quality of central bank monetary and financial statistics data including recording of Fund accounts                              | High     | Short term   |

1/ Short term: < 12 months; Medium term: 12 to 24 months.

# Background

## A. Overview of the Financial Sector

1. **The PNG's financial sector is relatively small and bank-dominated (Table 2).** As of March 2024, total financial sector assets stood at around PGK 80 billion or 70 percent of GDP. There are four commercial banks—two domestically owned (two thirds of the system) and two subsidiaries of large Australian banks—which account for 67 percent of the total financial system assets. Four Authorized Superannuation Funds (ASFs) account for another 24 percent of the system. There is a very small insurance sector and around thirty small nonbank deposit-taking financial institutions. Financial inclusion is limited, with 75 percent of Papua New Guineans excluded from the formal financial system.<sup>1</sup>

**Table 2. Papua New Guinea: Structure of the Financial Sector**  
(as of March 2024)

| Financial Corporations                         | No. of institutions | Total assets (Million, Kina) | Share in Total assets (Percent) |
|------------------------------------------------|---------------------|------------------------------|---------------------------------|
| <b>Deposit Takers</b>                          | <b>32</b>           | <b>57,947</b>                | <b>73</b>                       |
| Commercial banks                               | 4                   | 53,115                       | 67                              |
| <i>o/w domestically controlled</i>             | 2                   | 42,129                       | 53                              |
| <i>o/w foreign controlled subsidiary</i>       | 2                   | 10,983                       | 14                              |
| Licensed financial institutions                | 8                   | 2,473                        | 3                               |
| <i>o/w FX Dealers</i>                          | 2                   | n.a.                         | n.a.                            |
| Savings/credit cooperatives                    | 16                  | 1,810                        | 2                               |
| Microfinance institutions                      | 4                   | 549                          | 1                               |
| <b>Other Financial Corporations</b>            | <b>51</b>           | <b>21,170</b>                | <b>27</b>                       |
| Pensions/Authorised Superannuation Funds (ASF) | 4                   | 18,349                       | 23                              |
| Insurance Companies                            | 19                  | 1,915                        | 2                               |
| <i>o/w life insurance (LICs)</i>               | 4                   | 340                          | 0                               |
| <i>o/w nonlife insurance (NLICs)</i>           | 15                  | 1,575                        | 2                               |
| State-owned bank                               | 1                   | 631                          | 1                               |
| Fund Administrators*                           | 3                   | 56                           | 0                               |
| Investment Managers*                           | 5                   | 37                           | 0                               |
| Life Insurance Brokers*                        | 6                   | 184                          | 0                               |
| Money Changers                                 | 9                   | n.a.                         | n.a.                            |
| Money Remitters                                | 3                   | n.a.                         | n.a.                            |
| Mobile Network Operators                       | 1                   | n.a.                         | n.a.                            |
| <b>Total</b>                                   | <b>83</b>           | <b>79,117</b>                | <b>100</b>                      |
| * as at Dec 2023; 'n.a' - Data not available   |                     |                              |                                 |

Source: BPNG

<sup>1</sup> Source: Papua New Guinea Department of Treasury (2019). National Financial Inclusion Policy. Port Moresby; <https://www.thecefi.org/wp-content/uploads/2019/01/17-Jan-NFI-Policy.pdf>

**Table 3. Papua New Guinea: Financial Soundness Indicators 2020Q4-2024Q1\***  
(in percent)

|                                                                                       | 2020   | 2021.0 | 2022   | 2023   | 2024   |
|---------------------------------------------------------------------------------------|--------|--------|--------|--------|--------|
|                                                                                       | Q4     | Q4     | Q4     | Q4     | Q1     |
|                                                                                       | 2020Q4 | 2021Q4 | 2022Q4 | 2023Q4 | 2024Q1 |
| <b>Core FSIs for Deposit takers</b>                                                   |        |        |        |        |        |
| Regulatory capital to risk-weighted assets                                            | 41.8   | 44.4   | 30.4   | 39.6   | 37.3   |
| Tier 1 capital to risk-weighted assets                                                | 31.9   | 32.5   | 21.9   | 29.6   | 31.0   |
| Nonperforming loans net of provisions to capital                                      | 8.2    | 8.6    | 9.8    | 8.2    | 7.9    |
| Tier 1 capital to assets                                                              | 14.5   | 13.5   | 9.1    | 12.3   | 13.0   |
| Nonperforming loans to total gross loans                                              | 5.3    | 6.1    | 4.8    | 5.4    | 5.4    |
| Provisions to nonperforming loans                                                     | 38.2   | 40.2   | 39.6   | 41.1   | 46.4   |
| Return on assets                                                                      | 3.9    | 4.4    | 3.9    | 4.0    | 4.9    |
| Return on equity                                                                      | 14.5   | 16.6   | 16.4   | 15.0   | 17.6   |
| Interest margin to gross income                                                       | 65.4   | 65.6   | 63.9   | 63.0   | 60.7   |
| Noninterest expenses to gross income                                                  | 42.4   | 42.3   | 44.4   | 42.4   | 40.6   |
| Liquid assets to total assets                                                         | 18.3   | 18.9   | 22.5   | 19.2   | 18.9   |
| Liquid assets to short-term liabilities                                               | 25.1   | 25.5   | 28.6   | 25.0   | 24.6   |
| Net open position in foreign exchange to capital                                      | 12.6   | 15.3   | 20.6   | 10.8   | 15.0   |
| Residential real estate prices (Percentage change/last 12 months)                     |        |        |        |        |        |
| <b>Additional FSIs</b>                                                                |        |        |        |        |        |
| <b>Deposit takers</b>                                                                 |        |        |        |        |        |
| Large exposures to capital                                                            | 53.1   | 51.1   | 85.5   | 56.4   | 73.0   |
| Trading income to total income                                                        | 4.4    | 4.2    | 3.0    | 7.9    | 18.5   |
| Personnel expenses to noninterest expenses                                            | 41.4   | 41.0   | 41.0   | 41.0   | 39.4   |
| Spread between reference lending and deposit rates (base points)                      | 805.3  | 806.0  | 744.5  | 823.1  | 991.7  |
| Customer deposits to total (noninterbank) loans                                       | 153.5  | 167.8  | 180.1  | 180.2  | 177.7  |
| Foreign-currency-denominated loans to total loans                                     | 4.7    | 4.7    | 1.9    | 2.3    | 2.2    |
| Foreign-currency-denominated liabilities to total liabilities                         | 2.9    | 2.6    | 2.6    | 2.8    |        |
| Credit growth to private sector                                                       | 4.1    | 2.0    | 4.6    | 17.6   | 16.6   |
| <b>Other financial corporations</b>                                                   |        |        |        |        |        |
| <b>OFCs' assets to total financial assets</b>                                         |        |        |        |        |        |
| OFCs' assets to total financial system assets: total OFCs                             | 21.3   | 20.7   | 28.4   | 25.8   | 25.8   |
| OFCs' assets to total financial system assets: Insurance Corporation                  | 1.9    | 1.8    | 1.8    | 1.4    | 1.6    |
| OFCs' assets to total financial system assets: Pension Funds                          | 19.4   | 19.0   | 26.6   | 24.4   | 24.3   |
| OFCs' assets to gross domestic product: OFCs                                          | 14.2   | 13.5   | 16.0   | 17.7   | 16.1   |
| OFCs' assets to gross domestic product: Insurance Corporations                        | 1.3    | 1.2    | 1.0    | 1.0    | 1.0    |
| OFCs' assets to gross domestic product: Pension Funds                                 | 12.9   | 12.3   | 15.0   | 16.8   | 15.1   |
| <b>Insurance Corporations</b>                                                         |        |        |        |        |        |
| Shareholder equity to total invested assets (Life insurance only)                     | 44.2   | 46.1   | 53.3   | 53.0   | 55.4   |
| Shareholder equity to total invested assets (Nonlife insurance only)                  | 50.2   | 52.6   | 56.1   | 57.7   | 57.4   |
| Shareholder equity to total invested assets (Life insurance & nonlife insurance only) | 64.2   | 68.8   | 71.4   | 81.0   | 78.7   |
| Return on assets (Life insurance only)                                                | 34.9   | 36.9   | 16.0   | 7.4    | 5.7    |
| Return on equity (Life insurance only)                                                | 86.3   | 87.8   | 33.0   | 15.8   | 10.8   |
| <b>Pension Funds</b>                                                                  |        |        |        |        |        |
| Liquid assets to estimated pension payments in the next year                          | 97.1   | 79.7   | 54.4   | 96.2   | 78.9   |
| Return on assets                                                                      | 11.4   | 14.9   | 4.5    | 11.4   | 4.3    |
| <b>Real estate markets</b>                                                            |        |        |        |        |        |
| Residential real estate loans to total gross loans                                    | 13.6   | 13.9   | 15.2   | 14.1   | 14.2   |
| Commercial real estate loans to total gross loans                                     | 5.0    | 4.8    | 4.0    | 2.3    | 2.3    |

Source: BPNG

\* Based on 2019 FSI Guide Methodology.

2. **The performance of financial institutions, as captured by the financial soundness indicators, is good (Table 3).** As of end-March 2024, capital adequacy ratios of banks are well above the prudential minimums, banks are very profitable, and have ample liquidity. The nonperforming loans ratio increased slightly in 2023 but remains below the level recorded at the height of the COVID-19 pandemic in 2020-21. Total bank loans to the private sector account for only around 14 percent of GDP. Bank-sovereign nexus is high with the large amounts of government securities held in commercial banks (33 percent of total bank assets).

3. **BPNG is the main financial regulatory and supervisory authority.** BPNG is responsible for the regulation and oversight of the most important segments of the financial sector, specifically the banks, nonbank deposit-taking financial institutions, superannuation funds, and life insurance companies. These entities comprise 95 percent of the financial sector. The Office of Insurance Commissioner supervises general insurance companies but there are plans to absorb this entity into BPNG.

4. **The authorities are making progress in strengthening the policy framework for financial stability.** In 2017, the government adopted the Financial Sector Development Strategy 2018–30, which outlines priorities for building a resilient and inclusive financial sector in PNG. The strategy focuses on four areas: (i) financial sector regulation and supervision; (ii) capital market development; (iii) payment system development; and (iv) financial inclusion. Several legal and regulatory amendments are currently discussed following a report by the Independent Advisory Group (IAG)—a group of independent experts established by the Minister of Finance in 2022 with the goal of reviewing the regulatory framework for the financial sector. At a regional level, several initiatives are under way, including the Pacific Banking Forum, which aim at coordinating efforts to deal with the risk of declining correspondent banking relationships.

## B. Recent MCM Technical Assistance

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5. **In recent years, MCM TA to PNG on financial sector issues was delivered through the PFTAC activities on regulation and supervision.** A series of short-term missions from PFTAC since 2018 aimed at helping to align the regulatory framework for deposit-taking institutions with the Basel standards and enhancing BPNG's risk-based supervisory methods. Several new regulations were reviewed or developed. Guidance was provided on the harmonization of prudential standards across all deposit taking institutions. TA also covered the implementation of consolidated supervision across all categories of financial institutions in PNG.

6. **The implementation of the TA advice has put weight on resources and human capacity at BPNG.** TA on bank regulation and supervision has been very comprehensive and provided detailed material to the authorities. Given the substantial regulatory revisions, the application of standards on both a solo and consolidated basis, and the extension of banking standards to other larger credit institutions, it was recommended to carefully assess the impact of changes on different financial institutions. However, the conduct of quantitative impact studies has been constrained by the available resources.

# The Diagnostic Review

## C. Systemic Risk Analysis

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### Current situation

7. **PNG has in place several elements of the institutional framework for effective systemic risk analysis.** Financial stability is a key objective of BPNG under the Central Banking Act (CBA). BPNG has established a dedicated Macro-Prudential Supervision Unit (MPSU) within the Financial System Stability Group, responsible for macroprudential risk surveillance and policy advice. The MPSU is responsible for the regular publication of Financial Soundness Indicators (FSIs) and their quarterly analysis. It also took lead in preparing the first edition of the Financial Stability Report (FSR), which has not been published. There are plans to establish an internal Financial Stability Committee (FSC) and a draft charter has been prepared. The formation of a cross-agency Financial Services Council—comprising BPNG Governor (Chair), Secretary of the Department of Treasury, and Chair of the Securities and Exchange Commission—has also been discussed for several years.

8. **Important elements of the framework are still to be finalized and operationalized.** The draft FSC charter needs to be amended to reflect recent governance changes in BPNG, and the FSC is yet to meet in practice. The FSR has been re-drafted several times in the past few years but not approved or disseminated, in part due to the absence of a functioning FSC, the intended reviewing body. The Financial Services Council, which would be a useful body for cross-government communication on regulatory and macro-financial matters, has not yet been inaugurated.

9. **Legal authority for macroprudential policy is satisfactorily provided by the CBA.** Whilst there is no explicit provision for macroprudential policy, the financial stability objective is comprehensively expressed in the CBA: “formulate financial regulation and prudential standards to ensure stability and development of the financial system in Papua New Guinea”. The authorities are confident that there are no legal barriers to the enactment of any potential macroprudential measures applying to authorized financial institutions or their lending and financing arrangements with other sectors of the economy.

10. **Cementing the financial stability focus of the central bank is important.** In this regard, it has been mooted that BPNG might assume the responsibility for consumer protection in respect of financial services from the Independent Consumer and Competition Commission (ICCC). Such a change would create risks of diverting BPNG’s prudential focus to the potentially extensive responsibilities associated with fair treatment of consumers. It could also create potential conflicts between prudential supervision and consumer protection.

11. **Regular systemic risk surveillance and analysis is based around monitoring of FSIs.** Core FSIs are reported quarterly, with the most recently published indicators as of December 2023. Additional FSIs are also reported for banks as well as life insurance and pension corporations, providing expanded information on large exposures, sectoral lending activity, and return on equity for pension funds, amongst other items.

**12. Data quality appears reasonably sound and there is adequate access to data by the MPSU.**

FSIs are drawn from a common data collection process and forms, also used for micro prudential analysis. However, monetary statistical reporting has more disaggregated data which MPSU is encouraged to use for FSI compilation purposes. While MPSU has access to the monetary data reporting system and the micro prudential data system, separation of databases is at times cumbersome and has potential for reconciliation errors.

**13. Systemic risk analysis based around the FSIs is reported to senior management and later disseminated publicly through the Quarterly Economic Bulletin prepared by the Monetary Policy Group.** The quarterly report describes international and domestic economic and financial market developments, at some length. MPSU prepares a section of the report on FSI developments that evaluates the soundness of the financial system and identifies risks to its stability as revealed by these core metrics. For example, the June 2023 report (last published) reported strong FSIs for banks, but also noted risks from large exposures, high and increasing net open FX positions, and low liquidity of pension funds relative to prospective payments. The report covers the banking, life insurance, and superannuation sectors. While PNG's capital market is small, BPNG should keep it within the scope of its macroprudential surveillance.

**14. Systemic risk reporting to senior management has several weaknesses.** The quarterly report is heavily focused on core solvency, profitability and liquidity metrics, largely overlooking broader macro-financial indicators (e.g. credit/GDP) and some important risks are omitted from the quarterly report (e.g. infrastructure and operational risks). The materiality and acuteness of risks is unclear; for example, whether the risks highlighted are severe or mild, likely or unlikely to materialize, worsening or stable in nature.

**15. The FSR is expected to provide a more comprehensive risk analysis.** The publication of the FSR promises an important uplift in BPNG's financial stability oversight. The draft FSR provides a thorough description of the savings and lending sectors and distinguishes between structural (cross sectional) and time varying risks. It identifies the more severe risks as structural ones, including concentration risks; the inter-connectedness and exposure of the sector to the public sector (around 35 percent of bank assets); foreign exchange shortages; and resilience of the payments and clearing infrastructure. The macroeconomic context is discussed extensively, although the ramifications of the macroeconomic developments for the financial sector risks could be described more sharply. There is relatively little discussion of the potential risks arising from lending to the non-financial corporate sector (around 23 percent of total bank assets). The report would also benefit from more comparative analysis, for instance metrics in similar economies and the relativities of indicators to benchmarks such as regulatory limits, as well as better identification of risk trends and severity.

**16. Stress testing of the financial system is a valuable component of macroprudential surveillance but is not yet conducted by BPNG.** The Research Unit in the BPNG's Economics Department has undertaken some preliminary stress testing modeling work which focused on the resilience of BPNG's balance sheet to economic shocks. However, stress testing of the broader financial sector has not yet been developed and some upskilling would be required to do so.

**17. Macroprudential policy measures are not formally defined in legislation or a strategy document but are well-understood by BPNG as prudential measures that address systemic risks.**

Macroprudential measures can potentially be deployed via prudential standards. The Banks and Financial Institutions Act (BFIA) (that pre-dates the resurgence of global thinking on macroprudential policy frameworks) provides for prudential standards to be applied to all banks or licensed financial institutions or a specified class of them or to a subset, and to address situations or activities that are necessary to ensure the general stability and effective working of the financial system. It is therefore sufficiently empowering, in conjunction with the key objectives of the CBA.

18. **Two macroprudential policy measures (as per the IMF classification) have been instituted and further potential measures to mitigate financial stability risks are identified in the draft FSR.** BPNG has introduced an overall limit on net open foreign exchange position of banks at 15 percent of capital (or 10 percent in a single currency) and a minimum leverage ratio of Tier 1 capital to total assets at 6 percent has been applied since 2016. Time varying policy measures have not been adjudged as required. The more severe risks are identified as structural. Some such as concentration risk could be addressed by macroprudential policy, and this has been mooted in the past. Several of the potential structural policy measures would require cross-government actions. Some recommended actions, such as development of a secondary market for government securities and cyber security in the payments/clearing systems, also require infrastructure investment.

19. **The FSC is intended to be the governing mechanism for formulating and adopting macroprudential policy measures.** The draft FSC charter envisages oversight of all micro prudential and macroprudential regulation matters that affect financial stability. Cooperation between the micro prudential policy and macroprudential policy units appears constructive, supporting discussion of possible policy interventions. Both units are within the Financial System Stability Group, reporting to a shared Assistant Governor, facilitating coordination of micro- and macro-prudential measures, such as capital or liquidity overlays if required.

20. **The macroprudential surveillance function would be satisfactorily resourced when fully staffed.** The current 40 percent vacancy rate (2 of 5 establishment positions are vacant) is an impediment to finalizing the FSR and a severe hindrance to deeper analysis. While BPNG is considered as an attractive employer, turnover has been high in MPSU as analytical skills are in demand in both the public and private sectors. Current staff are heavily focused on FSI reporting and insights. MPSU's work relies on cooperation with the Financial System Policy Unit for policy development and the Economics Department for assessment of macroeconomic developments. Filling vacancies with technically competent (economic/financial skills) staff and additional training would be required to support more extensive analytical work such as stress testing or evaluation of non-traditional risks such as climate risk.

21. **Public communication of the BPNG's financial stability objectives and macroprudential responsibilities is relatively modest at this stage.** The Financial Sector Development Strategy 2018-2030 recognizes financial stability as fundamental to sustainable economic development and acknowledges the role of macroprudential policy and BPNG's responsibilities in this regard. The Strategy proposes the establishment of the Financial Services Council to foster communication and coordination across government and regulators, but the Council has not yet been inaugurated, potentially hindering action to address systemic risks. Financial stability objectives and functions are outlined on the BPNG website but discussion of systemic risk and macroprudential dimensions is scant. The FSI Developments section in the Quarterly Economic Bulletin, which is the main regular communication vehicle, is limited in

scope. The absence of a published FSR may inhibit wider understanding of systemic risks to financial stability and the benefits of macroprudential policy.

## Scope for future TA

22. **There is room for BPNG to improve the effectiveness and impact of its macroprudential surveillance.** A key step is establishing the FSC and its operation on a regular basis. It is important to finalize the draft terms of reference for FSC and its operating procedures. All macroprudential risk assessments and policy matters should be coordinated in the FSC before being submitted, if required, to the Board of BPNG. Regular meetings of the FSC members will support the development of macroprudential practice through building the mandate of MPSU inside BPNG; supporting robust risk review and clarity on whether risks are escalating or decreasing; and facilitating discussion and monitoring of progress on any policy actions. Establishing the FSC will remove a major impediment to finalization and publication of an FSR.

23. **Surveillance and analysis of systemic financial stability risks could be strengthened in several ways.** A regular systemic risk report should be developed which would be more comprehensive and systematic in its risk assessment than the current FSI developments report. Reporting should ensure that the materiality and acuteness of risks is easily understood so that senior management can focus effectively on the mitigating actions. A heat map could be a useful device. Risk scrutiny would be enhanced by more systematic risk rating (likelihood and impact), identification of trends (improving, deteriorating, stable) and comparisons to relevant benchmarks. There are well developed models and practices internationally that can be drawn on, perhaps with further technical assistance, recognizing that the maturity and complexity of risk analysis should be appropriate for BPNG.<sup>2</sup>

24. **The draft FSR could benefit from expert review.** FSRs need to build understanding of the financial stability mandate and the connections between the financial system and the wider economy; promote understanding of macro financial risks; support understanding of potential policy measures to mitigate risks; and deliver accountability in terms of reporting and evaluating past policy actions. The FSR should be a broader and deeper assessment of financial sector risks than the regular internal risk reporting but demonstrate continuity and consistency with the condensed version. Balancing comprehensiveness with clarity of messaging is a challenge for FSRs. The current draft FSR has some strengths but also some shortcomings. Expert review, perhaps in association with the development of enhanced systemic risk reporting, could assist senior management in finalizing this important document for the BPNG.

25. **Monitoring and control of liquidity risk could be enhanced through extended liquidity measures.** While liquidity risk appears modest when assessing liquid assets to total assets and to short-term liabilities, additional liquidity indicators may provide a richer picture. BPNG has started work on developing a liquidity coverage ratio and a core funding ratio—like a net stable funding ratio—has also been mooted. Introducing this into risk reporting will be useful, with a view to future adoption of these

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<sup>2</sup> PFTAC TA Report of June 2022 on Prudential and Risk Management Standards has sketched out some preliminary suggestions for improved risk reporting.

ratios as regulatory measures. Also, the development of a secondary trading market for government securities will be an important initiative to alleviate risks that securities cannot be sold when needed.

26. **BPNG should strengthen its systemic risk analysis by developing the capacity to stress test the resilience of the financial system to plausible but severe macroeconomic and, at a later stage, natural event (climate or seismic) shocks.** Stress testing of financial institutions' solvency and liquidity is now a standard practice in most supervisory entities and central banks, adding confidence to financial stability reporting or spurring additional forward-looking resilience measures where weaknesses are found. While PNG's financial system appears stable under normal or minor disruptions, interconnections within the financial sector and between it and the public sector are high. Many segments of the economic and financial system are vulnerable to a common economic or natural shock that could threaten debt sustainability. Solvency stress tests should be the initial priority, followed by liquidity. At a later stage, stress tests could be enhanced by adding natural event risks. Evaluating bank soundness under alternative capital risk-weighting and funding scenarios is also advisable. Basel applies zero capital weighting to sovereign debt but the risk of default or debt restructuring for PNG is unlikely to be zero. Both liquidity and solvency metrics could be analyzed for sensitivity purposes with alternative assumptions.

27. **Building stress testing models, data sets, and analytical skills could be usefully supported by further focused technical assistance.** While there has been some preliminary model development in the Monetary Policy Group, it is important for understanding financial stability risks to build capability in the Financial System Stability Group and to contribute its understanding of the financial institutions and their reaction functions to bear on the modelling work. Cooperation between departments is essential, as is the recruitment of appropriate technically skilled staff. Training for MPSU staff in stress testing techniques and practices would be highly beneficial. Supervisory data are understood to be adequate for solvency stress testing (but potentially require expansion for liquidity testing), although this may only be fully determined as modeling is undertaken. Improving macroeconomic statistics (especially GFS, IIP and balance sheet reconciliations, as elaborated in section H) is important for enhanced systemic risk analysis and could be supported by technical assistance.

28. **TA on developing macroprudential policy measures does not appear to be required at this stage but should be kept under consideration as the BPNG's financial stability function matures.** At present, it appears that any near-term policy interventions would likely be met by adjustments to existing standard micro prudential measures, for example limits on large exposures or supplementary capital requirements to address concentration risks. For now, risks arising from the household sector are modest and do not necessitate any measures. Corporate sector risks are not fully understood but at face value appear unlikely to threaten financial stability. However, these perspectives should be closely watched and if new measures are required then assistance may be warranted.

29. **Standard micro prudential instruments can be adjusted or tightened to address macroprudential risks.** Regulatory (micro prudential) policy, in general terms, is set to limit typical levels and sources of risk and to support the soundness of financial institutions. However, these minimum requirements may not be enough to protect the financial system and wider economy during periods or circumstances of heightened systemic risks. Macroprudential policies may be used to create buffers and help mitigate the impact from the materialization of cyclical or structural risks. More importantly, micro

prudential instruments can also be re-calibrated to be used for macroprudential purposes to address or mitigate emerging or heightened systemic risks (via the issuing of an amended prudential standard). The bottom line is to ensure that the risk is addressed by an appropriately targeted action and policy inaction does not allow risks to become critical issues.

30. **In the longer term, developing macroprudential policy tools, particularly a capital buffers regime, will be beneficial.** Concentration risk is a pertinent consideration. A draft report from 2018 identified one bank as systemically important but that designation has not been confirmed. For now, if warranted, concentration risk could be addressed via a revision to the capital adequacy regulation (since BPNG may apply a prudential standard including supplementary capital to a specific licensed financial institution).<sup>3</sup> However, in the longer term, given the ongoing structural risk arising from the domestic systemic importance of PNG's large banks, the Basel III capital buffers regime (in particular, systemically important bank buffer) warrants development of a transparent mechanism. TA may be required to support the introduction of Basel III measures.

31. **Developing and publishing a macroprudential policy strategy should be a medium-term goal for BPNG.** The macroprudential strategy would: explain the objectives of macroprudential policy; elaborate how macroprudential policy interacts with other mandates of the central bank for micro prudential regulation and monetary policy; outline macro-financial risks and the risk assessment process; and lay out the principles that guide BPNG's macroprudential policy approach; and identify the macroprudential policy toolkit.

32. **A plan for financial stability communications should be developed and integrated with the BPNG's overall communications framework.** To date, financial stability communication has been sparse, in part because of the fear of adverse public reaction and the absence of developed communication processes. Communication about macroprudential policy, including via release of an FSR, and in the longer term a macroprudential policy strategy, should aim at supporting the financial stability goal and maintaining confidence in the BPNG. Such communication should focus on building understanding of financial stability and educating the public on systemic risks, with the intended reinforcement that greater awareness will help smooth the path for any required policy actions. Additional goals include enhancing public confidence in any measures BPNG is taking to protect the financial system, along with accountability for BPNG's actions. The communication approach needs to take account of the potential perverse consequences of escalating stability risks through heightened alarm. TA could be helpful in developing BPNG's communication strategy, also in conjunction with the establishment of the FSC.

## D. Regulation and Supervision of Deposit-Taking Financial Institutions

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### Current situation

33. **BPNG supervision and regulation of the financial system are under the umbrella of the Financial System Stability Group (FSSG, Figure 1).** The Banking Supervision Department (BSD) is

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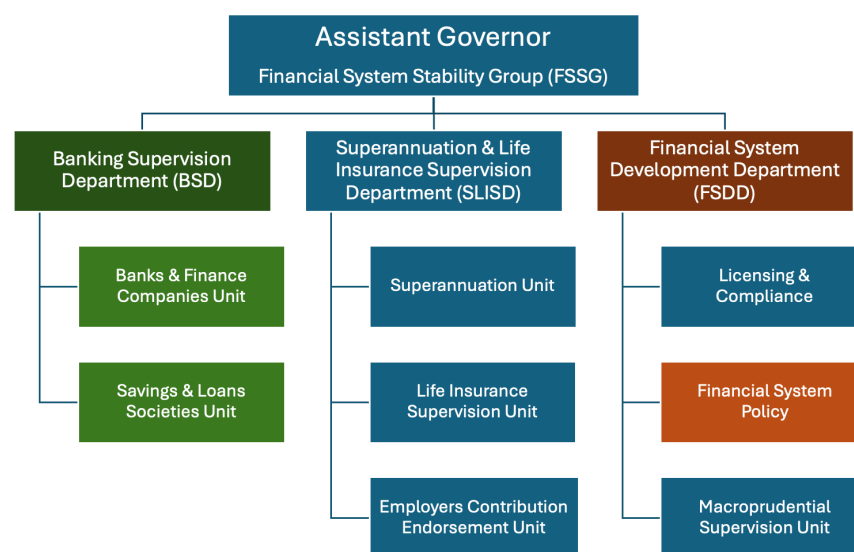
<sup>3</sup> Central Bank Act, 7(b) and Banks and Financial Institutions Act, Part V S27(1) & (2).

responsible for the supervision of all authorized deposit-taking institutions (ADIs) and is composed of two units: (i) banks and finance companies' unit, which supervises commercial banks, LFI, and microfinance institutions; and (ii) savings and loans societies (S&LSs) unit.<sup>4</sup> Prudential regulation is conducted by the financial system policy unit of the Financial System Development Department (FSDD). The FSDD is responsible for issuing prudential standards, licensing, compliance enforcements, macro-prudential supervision, and development functions, including financial inclusion and financial literacy.

34. **BSD teams are organized to conduct on-site and off-site supervision on a solo basis for ADIs of different sizes and types.** Three teams are responsible for the supervision of 4 banks, 11 LFI and 4 microfinance institutions, and two teams are responsible for 16 S&LSs. Each team is responsible for a similar number of ADIs of comparable size. Proportionality is used at supervisor's discretion for the assessment of smaller institutions, as all institutions are subject to the same prudential standards. Off-site supervision is conducted based on the quarterly reported data. The quarterly summary assessment report contains recommendations for supervisory action. The frequency of on-site examinations depends on the size and risk characteristics of each institution. There are also targeted inspections for banks. For the largest bank, Bank of South Pacific, a targeted onsite examination is conducted on an annual basis.

35. **Banks do not pay a supervisory levy to BPNG.** The superannuation funds are the only supervised entities by BPNG which contribute to the supervision costs with levies linked to their assets under management (0.143 percent of assets), resulting in annual contributions of several millions kina for the largest funds. On the other hand, the banks pay a licensing fee and an annual registration fee that is fixed at PGK 15,000. BPNG should consider an equitable structure of supervisory levies for all financial institutions.

**Figure 1. BPNG: Financial System Stability Group**



Source: BPNG

<sup>4</sup> S&LSs are cooperative societies owned by the members, which take deposits and are subject to the Savings and Loan Societies Act.

36. **Supported by TA from PFTAC, the authorities have been making efforts to improve the regulatory framework for financial institutions.** Over the last few years, several prudential regulations were reviewed or developed relating to: (i) definition of capital and the use of standardized approaches to credit and operational risk for calculating capital requirements; (ii) risk management requirements for operational risk, credit risk, market risk, liquidity risk, cyber security risk, and IT risk; (iii) limits on foreign currency open positions; (iv) large exposures and association with related parties; and (v) the management of interest rate risk in the banking book. BPNG has started work on harmonizing prudential standards among all deposit-taking institutions. The harmonization exercise—which is expected to be concluded by December 2024—consists of extending the banking prudential standards to all deposit-taking institutions in a proportional manner.

37. **The implementation of prudential standards developed with the assistance of PFTAC TA should be carefully planned.** Apart from the complexity of some new metrics involved, which would require increased expertise of the FSDD policy team, the alignment with Basel standards would also require review and updates to the current prudential reports, and the implementation of several entirely new reports on topics such as interest rate risk in the banking book, liquidity coverage ratio, and the capital requirement for operational risk. The new prudential framework should be discussed with the financial institutions and the impact of its implementation must be assessed and prioritized, taking into account potential compliance gaps and the operational capacity of financial institutions and BPNG itself.<sup>5</sup>

38. **Progress has also been made in terms of supervisory procedures.** BSD teams are currently organized to conduct on-site and off-site supervision on a solo basis for a number of ADIs, of different sizes and types. The distribution of ADIs aims at an equilibrium of tasks and responsibilities among the teams.<sup>6</sup> The compliance-oriented CAMELS rating model was replaced by the Financial Institutions Risk Rating Model (FIRRM) in 2020. The ratings under FIRRM are based on the risk characteristics of each supervised institution. A few supervisors are being trained to enhance their skills in specific issues, like IT risk of liquidity risk, to join the supervisors' team during examinations where their expertise is required. This represents a significant improvement although some of the new processes and routines are not yet documented as a supervision manual. PFTAC continues to support BPNG in improving the risk analysis based on the new supervision approach, including by reviewing, improving, and adequately documenting the new processes. PFTAC TA also helped with the implementation of consolidated supervision mainly at the regulatory level<sup>7</sup>, however, the impact on the supervisory framework and processes have not been thoroughly discussed. For the implementation of a consolidated supervision approach, the current

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<sup>5</sup> In general, BPNG shares the draft prudential standards with the banks to get their feedback. The new prudential standards are typically fully implemented within a year from the date of their issuance.

<sup>6</sup> Proportionality is used at supervisor's discretion for the assessment of smaller institutions, as all institutions are subject to the same prudential standards. Off-site routines are conducted with the same frequency of reported data (quarterly) and summarized in an assessment report that provides recommendations for supervisory action, when applicable. The frequency of on-site examinations depends on the size and risk characteristics of each institution.

<sup>7</sup> According to the PFTAC TA Report of June/2022 on Prudential and Risk Management Standards, "Section 27 (1) (f) of the BFIA provides powers to BPNG to issue prudential standards to the groups of which AIs are members. BPNG could use these powers to introduce consolidated supervision of AIs in PNG. However, it would be better to provide specific provisions in the Act to facilitate consolidated supervision in an effective manner across both AIs and other financial institutions."

supervisory teams' framework shall be reviewed to ensure that all institutions of a group are under the responsibility of a single supervisory team, and on-site/off-site supervisory procedures will need to comprehend the institutions' assessment at the solo and consolidated levels.

**39. The BSD procedures as home and host supervisor are well established and functional.**

Activities as home supervisor are supported by MoUs with respective supervisory authorities where the international activities of BSP are operational. As host supervisor, BPNG has an agreement with Australian Prudential and Regulatory Authority for data sharing and participation in colleges. The Australian supervisors contact BSD in the event of on-site examination in the subsidiaries of the two Australian banks in PNG. Foreign subsidiaries are required to comply with all BPNG prudential standards and are submitted to the same supervision process applied to domestic institutions.

**40. Prudential reports submitted by banks to BSD are automatically received and stored, but there are no automated tools for data assessment.**

The reports are submitted by banks through an automated system, and data are validated at the arrival of the report. The system has the capacity to generate the received information in Excel or PDF forms for undertaking financial risk analysis, but the data assessment is done by off-site supervisors manually. The on-site examinations results and the FIRRM rating assessments are also not integrated in the system.

**41. The corrective actions by BPNG are relatively limited.**

Supervisory powers to apply corrective actions are restricted to sanctions in the form of fines in the amount of up to PGK 500,000 or imprisonment for up to 10 years<sup>8</sup>, and, in both cases, it is mandatory to appeal to court for its application (the judge establishes the amount to be paid or the term of imprisonment). To avoid such a long process, supervisors prefer to make use of moral suasion, and have reported no major concerns on delays or non-submission of information to BSD, nor eventual attempt of obstructions of investigation. This TA, however, recommends that supervisory powers be reinforced with a more timely and effective range of corrective measures at the administrative level, to be applied both to the institution and its employees, such as limits or restrictions to certain operations or exposures, and suspension or prohibition of certain activities, to permit supervisors timely correct irregularities that could affect the bank's soundness or trigger financial stability consequences. The creation of an administrative instance for penalties application, however, would imply the review of the supervisory processes and framework, both to establish a gradation of severity on the application of penalties, and to establish a formal process for its application<sup>9</sup>.

**42. The data management at the BPNG is compartmentalized.**

Each BPNG department creates and manages its own database and data sharing practices across departments are mostly limited to activities that would require system-wide analysis. For example, the MPSU has access to the monetary data reporting system (from Financial Markets Department) and the micro prudential data system (from BSD), but BSD does not have automatic access to the monetary data, which may potentially impede

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<sup>8</sup> According to BFIA, an AI which fails to supply information to BPNG or a person who intentionally obstructs supervisory works or fails to comply with any requirement imposed by the supervisor is guilty of an offense and may be subject to those sanctions.

<sup>9</sup> Supervisors would need to formalize the sanctions in an Administrative Proceeding and submit to higher hierarchy level to the analysis of merits. A separate component should be created to follow the Administrative Proceeding's execution.

timely response to adverse liquidity developments. The limits on data sharing among BPNG departments is also likely to increase the costs of data submission for financial institutions.

43. **BSD considers the current supervisory framework as adequate but is concerned about its capacity to absorb increasing demand and complexity.** Currently, there are three new applications for a bank license, and S&LSs have been developing products to provide payment facilities to their customers. The ongoing enhancements to the regulatory framework will inevitably raise complexity of supervisory activities, due to the new metrics for the calculation of prudential standards and increased amount of reported data.

## Scope for future TA

44. **Legal reforms will be an important pre-condition for strengthening the regulatory and supervisory frameworks.** Amendments to the BFIA should support the implementation of consolidated supervision, the effective application of supervisory sanctioning powers, and the harmonization of bank-like standards with S&LSs institutions. A review of the Savings and Loans Societies Act may also be necessary for the harmonization of bank-like standards with the S&LSs. Regarding consolidated supervision, BFIA already provides powers to BPNG to issue prudential standards to the groups in which supervised institutions are members, and BPNG can use these powers to conduct consolidated supervision. However, ensuring specific provisions in the Act would help facilitate consolidated supervision in an effective manner.

45. **FSDD and BSD may need follow-up support with the implementation of the past PFTAC recommendations.** The effective implementation of the past PFTAC recommendations necessitates discussions with ADIs regarding QIS results, public consultation on the new draft regulations; and strategic planning for the implementation of the regulatory changes, considering the relevance and complexity, compliance gaps, and ADIs and BPNG operational capacity. A strategic plan for the alignment of PNG prudential standards with the Basel framework should be prepared by a task force with participants from the regulation and supervision areas. Future TA could be considered in the following areas: (i) assessing the QIS results and public consultation returns; (ii) improving skills of the BPNG regulation and supervision teams in the standards to be implemented; and (iii) developing a strategic plan for the implementation of prudential standards.

46. **Enhancing prudential standards not covered by the PFTAC TA may be required in the medium term.** Prudential standards reviewed by PFTAC TA were prioritized reflecting their relevance to the PNG financial market. Public disclosure requirements, the capital requirement for market risk, the liquidity requirements (liquidity coverage ratio and net stable funding ratio), and the leverage ratio were left out of the scope of the PFTAC TA. BPNG capital requirements remain aligned with Basel I, which establishes a minimum ratio of capital to risk-weighted assets of 8 percent. The FIRRM rating model covers several aspects of Pillar 2, such as the assessment of the bank's risk management and controls. BPNG is likely to adopt and implement most or all these requirements as the financial markets develop over time. Future TA could target: (i) reviewing existing regulations and assisting in drafting new regulations; (ii) assessing the QIS results and public consultation returns; (iii) reviewing of on-site/off-site activities, documentation, systems and tools, impacted by the new/revised regulations; and (iv) improving the skills of the BPNG supervision teams in the standards to be implemented.

47. **Work on the implementation of consolidated supervision should continue.** The implementation of consolidated supervision will involve the review of supervisory regulation, framework and processes, with significant impact on on-site and off-site activities. 15 prudential standards and 11 reports will be required on a solo and consolidated basis, and calculation of ratios and monitoring tools will increase in complexity, which may require improvements on the supervisory skills. Scope of future TA could target: (i) reviewing the supervisory approach and framework; (ii) reviewing off-site processes, including processes for data quality; (iii) reviewing on-site processes; (iv) assisting in drafting the supervision manual (integrated documentation of on-site/off-site processes); and (v) improving the supervision team's skills in the consolidated supervision approach.

48. **There is room to improve data sharing practices at the BPNG.** The current compartmentalized arrangements for data management are inefficient and may delay timely action. The enhanced supervisory processes will require access to data that are not currently shared. The BSD may need to assume the responsibility with respect to data reported to supervision, such as user authorization control or data curatorship. Data curators must have sufficient skills and commitment to ensure data quality. They are responsible for: ensuring and controlling data quality, such as the definition of prerequisites, business rules and metrics for data quality assessment; assisting users regarding data analysis and the improvement of its quality; identifying and solving any issue regarding data; setting reference values for data attributes; keeping updated all documentation (metadata); defining rules for data access; and assuring to all users that data suits their needs. The regulation team may also need a better data sharing environment to access relevant information. TA could focus on: (i) improving data governance and policies; (ii) enhancing skills of regulation and supervision teams in data management, including the use of supotech and regtech models; (iii) assessing the impact of new data sources on off-site supervision activities, documentation, systems, and tools; and (iv) incorporating the use of shared data in the regulation drafting process.

## E. Regulation and Supervision of Insurance Companies and Pension Funds

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### Current situation

#### Superannuation funds

49. **The defined contribution superannuation funds have grown strongly in PNG over the past several decades partly reflecting the young age of the local workforce.**<sup>10</sup> Overall, the superannuation funds enjoyed a total positive cash inflow even though some small funds have sometimes negative cash flows. The system has not matured, and the inflow of contributions exceeds the outflow of benefits for the whole system. However, the situation can be different in case of a surge in unemployment since the ASF benefits include unemployment payouts of initially 50 percent of the account value and if the unemployment persists, the total account value is paid out. The significant reduction in the positive cash inflow during the years of COVID-19 pandemic partly reflected the payouts for unemployment.

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<sup>10</sup> The median age of the population in PNG was 22.2 years in 2023.

50. **The Superannuation General Provisions Act 2000 (SGP Act) amended in 2002 regulates the sector.** The Act is written in a principle-based manner that allows the BPNG to take the necessary actions in case of misbehavior of the licensees, and the BPNG has done so by removing the board of the defense force pension fund recently. There are investment guidelines in place as well as provisions to minimize conflict of interest. The Act also requires the funds to comply, if not specifically exempt, with the Life insurance Act. This Act contains fit and proper provisions as well and the structure of the board committees. The BPNG can and has issued prudential standards on risk management, investment guidelines, etc. There are no risk capital requirements, and the members bear the risks in the form of lower returns.

51. **The SGP Act has a strong focus on the governance issues of the system.** The Act requires that the Board of the Trustee managing the affairs of the ASF should have an external Licensed Investment Manager (LIM) and external Licensed Fund Administrators (LFA). All three entities require a license from the BPNG. This separation of duties increasing the oversight and improving governance showed effectiveness in 2019 when the whole board of the Trustee of one ASF was removed and replaced after setting the ASF under provisional administration because of their acting in contradiction to the LIM recommendations.

52. **The supervision of the ASFs includes offsite assessments and onsite inspections.** The offsite supervision uses the digital information received from the ASFs. A quarterly report discusses the changes in net assets and any matters that require attention or necessitate a supervisory plan. The annual analytical report includes the assessment of the balance sheet, income statement, the statement of cash flows, the operating statement, as well as the comments from the board and external auditor. It covers related party investments, valuations used, changes in accounting practices, reporting discrepancies, among other items. The onsite inspection cycle is two yearly and includes a full scope assessment.

## Insurance companies

53. **The insurance sector in PNG is very small.** There are 16 insurance companies with assets accounting for 1.5 percent of the financial system assets. The insurance companies are strongly interconnected with the rest of the financial sector through ownership rights. There are three pending insurance license applications. Overall, the insurance sector is profitable.

54. **The supervision of the insurance sector is carried out by two separate supervisors with two different approaches.** The BPNG supervises the life sector, and the Office of the Insurance Commissioner supervises the general insurers. The life insurance supervision follows the same pattern as the supervision of the ASF discussed above while the supervision of the general insurers has been arms-length if not absent in recent years with only limited reactions impaired by delayed data submissions.

55. **The mandatory third-party liability insurance dominates the market and is exclusively provided by the state-owned Motor Vehicle Insurance Limited (MVIL).** Enacted in 1974, the Third-Party Insurance Act mandates third party liability insurance for all vehicle owners covering bodily injury and death due to car accidents. In 2021, the Third-Party Insurance Act was amended expanding the coverage to all vehicles and increasing the death benefit to PGK 10,000 for all persons (until then males had a PGK 5,000 benefit and females and children a PGK 2,500 benefit). MVIL fully owns the only local

reinsurer PAC Re as well as the insurance company PMMI that offers both general and life insurance. Poor management of both companies, specially of PMMI, and inadequate oversight resulted in significant losses and the need for MVIL to inject capital in these companies of around PGK 100 million. Notwithstanding these costs, MVIL's contribution to the government in the form of dividends, taxes, and services was around PGK 570 million during 2018-22.

## Scope for future TA

56. **The payout phase of the ASF does not offer annuities, a critical element of an effective old-age income protection scheme.** The purpose of the ASFs to provide old age income is incomplete with only a lump sum payment at retirement age available to the members. The complex issues of longevity risk as well as the regular stream of income are left to the individuals to address. This situation can potentially lead to an impoverished elderly population or fiscal stress. Consideration should be given to introducing a regulation to create a cost-efficient annuity as a central retirement benefit of the ASF's system. Such annuities should be offered by sufficiently capitalized life insurers.

57. **The market data are not readily available to the public.** The supervisors of the ASF and insurers do not publish market data and their web pages do not provide sufficient information for the public to make an educated decision on where to insure or where and how to file a complaint in case of issues with their insurance providers. The only source for individual company information is the annual report of the supervised entities. However, the annual reports are either not available to the public at all or are issued with a delay of over 6 months. The institutionalization of regular and timely market data publication and establishing a warehouse for supervisory data will be critical for the integrity and reliance of the reported data.

58. **The contracts with the LIM and LFA should be strengthening including provisions for compensating the fund in case of wrongful advice or poor performance.** The ASF regulation rightfully does not relieve the Trustee board from the responsibility of losses incurred due to wrongful or unprofessional advice given by the LIM nor of losses due to operational errors attributable to the LFA. The important protection for the Trustee board and ultimately the members against inadequate advice or operational errors is left to the service contract entered with the providers. Furthermore, there are no capital requirements for the LIM and the LFA that would guarantee a compensation to the ASF in case of losses due to operational errors or poor advice. A regulation should be drafted and enacted to require including provisions for compensating the fund in case of wrongful /unprofessional advice (the LIM contract) and in case of operational errors caused (the LFA contract) and the need to require capital to the LIM and LFA should be evaluated.

59. **There are no regulations on the compensation to the Trustee board members.** The alignment of interest of the Trustee board with the performance of the ASF is of critical importance. A compensation framework that encourages excessive risk taking can result in significant losses to the participants. BPNG should draft and enact a regulation requiring remuneration of the Trustee board members to be aligned with the long-term performance of the ASFs.

60. **The significant differences in the regulations applicable to life insurers and general insurers hinder effective supervision of the sector.** The differences relate to the level of operational independence of the supervisor, the reporting requirements, and the prudential and market conduct standards. As an example, the general insurers are subject to risk-based capital requirements while the

life insurers remain with only a commercial capital requirement; on the other hand, unlike the general insurers, the life insurers are required to abide by governance and risk management statutory standards. The harmonization of the regulatory framework for the insurance sector would be desirable.

61. **The capital requirement for both life and general insurers should be upgraded.** The capital requirement for life insurers is not risk sensitive: life insurers are required to have a minimum capital of PGK 4 million and simply hold more assets than liabilities, like any other commercial company. As a result, the capital and solvency ratios may not illustrate the true level of resilience of the life insurers. The capital requirement for general insurers is risk-based but the capital charges are very low with a charge for unlisted equity of only 10 percent or a charge for assets like office equipment of only 15 percent. The development of a risk-based capital regime for life insurers and the calibration to a higher level of charges for general insurers would be important.

62. **The supervision is compliance-based.** The ASFs as well as insurers are supervised at the same intensity without taking any preventive measures. There is no risk profiling assessment nor an early warning system in place. Stress testing is not conducted limiting the ability of the supervisor to take a forward-looking view of risks. In line with the recommendation of the International Association of Insurance Supervisors, a risk-based supervision framework for insurance companies should be implemented.

63. **Group supervision is not carried out.** While there are several insurance and financial groups in PNG, both local as well as international, there is no group supervision framework in place, leaving important risks potentially overlooked. Furthermore, the interaction with insurance supervisors from other jurisdictions does not take place (although there is one supervisory college in place that includes insurance, it has a strong focus on banking). This should be addressed by developing a group supervision framework for insurance companies, including setting up of supervisory colleges where relevant.

64. **The supervision of the investment strategy lacks a forward view.** There is no methodology to assess the quality of the investment strategy set by the ASFs, and the supervisor can only determine the adequacy of the investment plans developed by the ASFs after the results are announced. This generated significant criticism by the public when the returns credited to the individual savings accounts turned below 2 percent or negative. It is recommended to develop a supervisory tool to assess the probability of the investment strategy to deliver the expected yield.

65. **There are no formal communication requirements between the two insurance supervisors resulting in inefficiencies.** Notwithstanding the declared intention by the government to merge the insurance supervision, the two supervisors continue acting with minimal coordination and communication. The lack of communication between the life insurance supervisor and the general insurance supervisor does not allow an integrated approach to the supervision of the insurance sector both for prudential and market conduct issues. For instance, the costs to a transition to an enhanced risk-based supervision or risk-based capital regime would need to be carried out by each supervisor. A formal protocol of communication between the two supervisors should be established, which would facilitate continuous dialogue, joint activities, and unfettered access to information on the supervised entities.

66. **The general insurance supervision lacks intrusiveness, and the life insurance supervision is understaffed.** The general insurance supervision is not supported by inspections and the reporting frequency while required to be monthly is de facto annual for some companies. There is no feedback to the sector and even in critical situations the presence of the supervisor is obscure. The life insurance supervision is staffed with 3 analysts and is not supported by digital tools. The insurance supervision infrastructure should be upgraded with a transition plan that ensures continuity and determines the adequate number of resources.

67. **The necessary capacity to implement the new accounting standard has not been built.** The accounting standards IFRS17 for the reporting of the insurance sector has been introduced in 2023. However, the supervisors have not received the required training to be able to supervise the new financial statements under IFRS17. Furthermore, the financial reports remain to be adjusted to the new accounting standard.

68. **The enforcement of sanctions should be strengthened.** While the insurance supervisors have the power to fine entities and individuals that do not comply with the requirements, sanctions have been limited to fines and required a court decision. The process to issue administrative fines and sanctions to supervised entities and individuals should be revised to allow for this supervisory tool to be effective.

## F. Financial Safety Net and Crisis Management

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### Current situation

69. **The PNG financial system has not experienced a systemic crisis for decades and this long-lasting stability is notable.** No banks have failed in recent memory. A small S&LS underwent a compulsory merger in 2018: after the measures by BPNG to allow the institution to recover did not succeed, BPNG appointed a statutory manager, and the failing institution was ultimately absorbed by another S&LS. More recently, a microfinance institution with poor asset quality and mismanagement also approached failure and was compelled to merge with another microfinance institution.

70. **The implementation of the resolution regime is led by the BPNG, but the National Court must issue an order to wind up an institution.** According to the BFIA, a key power available to the BPNG is to take control of an institution or appoint an administrator as a statutory manager. The BPNG or the manager have full and exclusive power of the directors of the financial institution. A resolution transaction can be undertaken by the statutory manager who may “sell or otherwise dispose of the whole or any part of business of the authorized institution...”<sup>11</sup> This power has not, however, been operationalized by developing procedures for the sale of business. Upon application of the BPNG and when recovery of an institution is not likely due to insolvency, the National Court is responsible for issuing an order to wind up an institution.<sup>12</sup> To date, there have been no cases of the appointment of a statutory manager for a bank.

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<sup>11</sup> Section 36 (power to take control or appoint an administrator) and sub-section 38.4 (power to sell or dispose of the institution) of the BFIA.

<sup>12</sup> Subsection 48(2) of the BFIA.

71. **The establishment of an inter-agency FSC has been under consideration since 2018.** The Council, which was referenced in the Financial Sector Development Strategy 2018-30, is intended to become a coordinating body to drive financial sector reforms and monitor financial sector stability. The coordination is always necessary when decision-making powers are allocated across several authorities. The proposed Council would have under its remit not only matters of systemic risk prevention but also crisis preparedness and management, including communications. Regarding the latter, the BPNG does not currently have a dedicated unit in charge of communications.

72. **Bank of South Pacific (BSP) represents a significant issue for safety net, bank resolution, and crisis management consideration in PNG.** Partially state-owned, BSP dominates the banking industry with a market share of close to 60 percent. Although BSP has not been officially designated as a domestic systemically important bank, a 2018 internal BPNG analysis concluded that it possesses the characteristics of a systemic bank. BSP plays an important role in the payment system and holds deposits of large financial institutions. BSP has a significant cross-border network of subsidiaries in neighboring jurisdictions, owing mostly to its recent purchases of entities in the region from Australia-based Westpac.

73. **Two of the four banks currently in operation in PNG are subsidiaries of foreign bank groups and BSP has operations in multiple jurisdictions outside of PNG, highlighting the importance of cross-border cooperation.** The Australia and New Zealand Banking Group (ANZB) and Westpac Banking Corporation, both headquartered in Australia, are required to meet all the supervisory and regulatory requirements that the domestic banks are required to meet. Neither is considered as systemic. There are no legislative provisions in the BFIA specific to cross-border resolution. The BPNG participates in the supervisory college for ANZB, which was constituted by the Australian Prudential Regulation Authority without a formal MoU. BPNG has a multilateral MoUs for cross-border supervision of BSP through a supervisory college with the Reserve Bank of Fiji and the Central Bank of the Solomon Islands. Other supervisory authorities include those of the Reserve Bank of Vanuatu, National Bank of Tonga, Central Bank of Samoa, and Financial System Commission of Cook Islands. The MoUs address information and assistance exchanges, confidentiality, and meetings, but not resolution planning or crisis and resolution coordination.

74. **There is overlapping and potentially conflicting jurisdiction for the decision-making process for the voluntary sale or compulsory resolution of banks between the BPNG and the ICCC.** A recent case of the proposed voluntary sale by Australian-based Westpac of its PNG operations is instructive. Westpac attempted to extract itself from the PNG market, primarily through a proposed sale of operations to Kina Bank, but the ICCC applied its powers to reject the sale. Therefore, it seems likely the ICCC would also have the discretion to apply its powers in the event of a bank resolution. The BPNG emphasized during the mission that the decision was made by the ICCC in consultation with the BPNG.

75. **BPNG has discretionary authority to provide Emergency Liquidity Assistance (ELA) to banks or financial institutions.** Under Section 76 of the CBA, ELA can be extended if necessary to “safeguard monetary stability,” “promote the smooth operation of the payment system” or “maintain a stable financial system.” There have been no extensions of ELA under this provision. Terms are open-ended and can be “on such conditions as [the BPNG] thinks proper.” This provision opens the possibility of unsecured lending; does not mention the need for solvency or corrective measures; makes no

reference to a penalty interest rate; or circumstances under which a supporting government guarantee would be required. There are no procedures for ELA to guide decision-making.

76. **The BPNG possesses a broad range of powers which may create conflicts of interest.** In a resolution, the BPNG could have multiple roles: provider of ELA, authority resolving (selling) a failed bank, and supervisor of both the failing bank and a potential buyer. This concentration of powers could lead to potential conflicts of interest that should be addressed through structural separation through: (i) ensuring separate lines of reporting for each key functional department at the top of the BPNG; (ii) enabling a structure of standing committees with functional mandates as part of the governing structure of the BPNG; (iii) providing sufficient staff and resources; and (iv) formalizing a comprehensive protocol of coordination among functions. Presently there are no staff dedicated for resolution, so if experts are needed to work on resolution plans or manuals, they would be drawn from within the supervision department.

77. **PNG does not have a deposit insurance system and it is only in the earliest stages of consideration of whether to initiate such a scheme.** The IAG draft report stated that a system of deposit insurance “is not recommended” but the analysis was limited in scope and was focused on existing capital and liquidity in the banking system, without consideration of the possibility of future deterioration in that current healthy position. Contingency plans should be in place to address any failures, given this time to design the system, draft the legislation, shepherd the legislation through the approval process, operationalize the system, and build up the fund balance to a sufficient level.

78. **The BPNG has never compiled a Financial Crisis Management Plan.** Such a plan would be the primary reference material for crisis preparedness and management methodologies. Some elements of a crisis preparedness and management framework are in place at the BPNG, but in the form of disparate legal provisions. In an environment of limited resources, detailed planning becomes particularly important.

## Scope for future TA

79. **Legal reforms are needed to support an effective resolution regime.** The BFIA has not been amended since its adoption in 2000, predating the global financial crisis when resolution best practices have been entirely rethought. The amendments to the BFIA should specify that the BPNG is the administrative bank resolution authority, provide the BPNG with the range of resolution tools, including for a temporary bridge bank, require recovery and resolution plans, clarify the protocols for addressing a cross-border resolution, and clarify the roles for the National Court and the ICCC. If the BPNG cannot quickly dispose of an institution, bridge bank authority will allow the central bank to transfer the institution’s critical functions and ensure their continuity in cases where a buyer cannot be located.

80. **The BPNG’s resolution powers should be brought in line with the Key Attributes of Effective Resolution Regimes.** Migrating from a system with a role for the National Courts toward an entirely administrative resolution process and revisiting the scope of the ICCC’s powers will be particularly important. The need for updating the regime and transitioning to a fully administrative system is acknowledged in the draft FSR. Once it is recognized as the bank resolution authority, BPNG should have exclusive power for approving bank resolution transactions.

81. **Once the amended BFIA is adopted, the sale of business should be deployed as the primary resolution tool, complemented by bridge bank as an alternative.** BPNG should focus on operationalizing the sale of business tool as the preferred resolution strategy. Only if there is no buyer willing to participate in a full/partial sale, and if it is considered that liquidation could pose financial stability risks, a bridge bank may be a necessary, temporary solution. As part of the application of these powers, the BPNG will need to build capacity to conduct a 'no creditor worse off' analysis to support its chosen resolution option.

82. **Structural separation of the reporting lines within BPNG should be adopted.** Currently, the BSD houses bank supervisory authority, resolution authority, and some decision-making for ELA. Structural separation of the lines of reporting would help avoid the conflicts of interest.

83. **The resolution function of BPNG should be adequately staffed.** Demands for resolution resources are modest during periods of stability and there is a need for increased resources during a resolution or crisis. The BPNG should commit a few core staff to the resolution function to initiate the needed work on resolution plans and development of resolution procedures. A pop-up resolution function should also be planned whereby resolution staffing can be increased during a crisis, given scarce resources.

84. **The new resolution regime will necessitate development of a resolution manual.** A resolution manual is a document that sets out policies and procedures for undertaking the key organizational functions of a resolution authority. The procedures specify decision points that are essential in applying resolution powers and tools. The resolution manual should address not only procedures that have to be implemented but also must envision contingency procedures. A resolution manual also needs to incorporate policies adopted by the decision-making bodies of the BPNG.

85. **The BPNG will also need to develop a resolution training program for capacity building.** Once the resolution function is staffed and the resolution manual has been drafted, a training program will be needed as a priority matter for those assigned to the resolution unit and for staff outside the unit in need of training on resolution topics. The resolution manual would be available as a ready source for much of the needed training material. Simulation exercises on a domestic and cross-border basis would need to be integrated into the resolution training program to identify gaps in staffing, procedures and the legal framework.

86. **BPNG must develop recovery and resolution plans for BSP.** The purpose of a recovery plan is to identify measures that would likely be taken to correct a situation of financial distress. The purpose of a resolution plan is to collect necessary information for the BPNG to be prepared for an orderly resolution, should the trigger for a resolution be met. There are no legislative mandates or procedures for banks to develop recovery or resolution plans under the current BFIA. Given its dominant position in the banking system, BSP would be a logical starting point to begin to develop a process for recovery and resolution plans. This exercise could start before the mandate for recovery and resolution plans is codified under law, based on existing powers for requiring submission of information. Resolution plans should also address continuity of access to critical financial market infrastructures.

87. **The Financial Services Council should be inaugurated based on a multilateral MoU.** Current ad hoc methods of bilateral cooperation and information exchange should continue until the Council is

operationalized through an MoU. The MoU would address protocols for coordination on crisis preparedness and management based on powers of the participating authorities. The Council should meet regularly at prescribed minimum frequencies e.g., quarterly. Confidentiality must be preserved throughout the crisis coordination process. A crisis communications plan, with an expert to implement it, will be a necessary element of Council development.

**88. Further coordination and planning are necessary to prepare for a cross-border resolution.**

Beyond the existing supervisory college that BPNG participates in with Australian Prudential and Regulatory Authority, consideration should be given to agreeing to an MoU which would address cooperation and information-sharing, with emphasis on recovery and resolution planning and crisis management. The MoU could also address simulations regarding how the instability of a PNG-based subsidiary of an Australian banking group or the banking group itself could be managed. There is an increased degree of complexity in the case of a cross-border resolution as compared to a domestic resolution. Additionally, the existing MoU between the members of the BSP supervisory college could be expanded to address recovery and resolution planning, detailed information sharing for a troubled institution and crisis management. As part of the update, it should be inclusive of all current members of the college.

**89. The ELA framework could be enhanced in several areas.** It would be important to adopt supporting documentation for ELA consisting of (i) public instructions and (ii) internal procedures. The public instructions should discuss objectives, conditions, and parameters of ELA, while internal guidelines should describe the task allocation, internal processes, organizational considerations, potential conflicts of interest for ELA (structural separation), and technical indicators, such as the BPNG's priority order for the selection of collateral. In addition, the option for providing ELA in resolution should be addressed under the amended CBA. A troubled but viable bank undergoing resolution may have liquidity needs because an announcement of resolution may disrupt depositor confidence leading to a drain on deposits. Procedures should detail preconditions under which lending can be pursued in resolution and an exit strategy from the ELA extension.

**90. A comprehensive analysis should facilitate the decision on introducing a deposit insurance system.** This analysis would consider the structure and health of the PNG banking sector, evaluate the prerequisites for introducing a deposit insurance system, inform the design of an effective deposit insurance, and detail a plan to operationalize it (including an effective financial backstop). TA should be contemplated for the introduction of deposit insurance.

**91. All crisis preparedness-related procedures should be formalized into a financial crisis preparedness and management plan.** Since some of the protocols and procedures are not yet in place, the BPNG should develop a census of all existing crisis management documents, determine which gaps are evident, and develop those procedures that are lacking.

## G. Financial Market Infrastructure

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### Current situation

92. **PNG has made significant progress in modernizing its payment systems since the formulation of its National Payment System Development Strategy in 2008, and its revised version in 2015-18.** The BPNG serves as the regulator, overseer, operator, and catalyst for the payment systems. In 2013, the BPNG implemented a Real-time Gross Settlement (RTGS) system within the Kina Automated Transfers Systems (KATS). This system includes an Automated Clearing House (ACH) for processing cheque truncations from both businesses and government agencies, as well as direct credit transfer systems.<sup>13</sup> In 2019, the BPNG launched Retail Electronic Payment Systems (REPS), also known as the 'national switch', which processes domestic debit card transactions and instant payment transactions (IPT). Additionally, outside the BPNG, there is one licensed payment service provider (PSP) operating mobile money. The current payment landscape and key metrics for development in PNG are shown in Figure 2.

93. **PNG has a sound legal basis for the development and oversight of its NPS.** The CBA designates the establishment of efficient national and international payment systems as one of the BPNG's core functions. The NPS Act 2013 empowers the BPNG to oversee and operate the NPS, promoting financial system stability. Critical legal principles such as the finality of settlement (including an exemption from zero-hour rule in case of insolvency), protection from third-party interference, legal recognition and evidence of electronic transfers, and the central bank's authority to initiate legal proceedings are enshrined in this framework. The National Payment Council (NPC) further solidifies the regulatory environment. Four secondary legislative measures issued in 2019 provide directives on oversight (01/2019), electronic funds transfers (02/2019), agents (03/2019), and retail payment instruments (04/2019), and aim at implementing the central bank's regulatory, operational, and oversight powers of NPS.

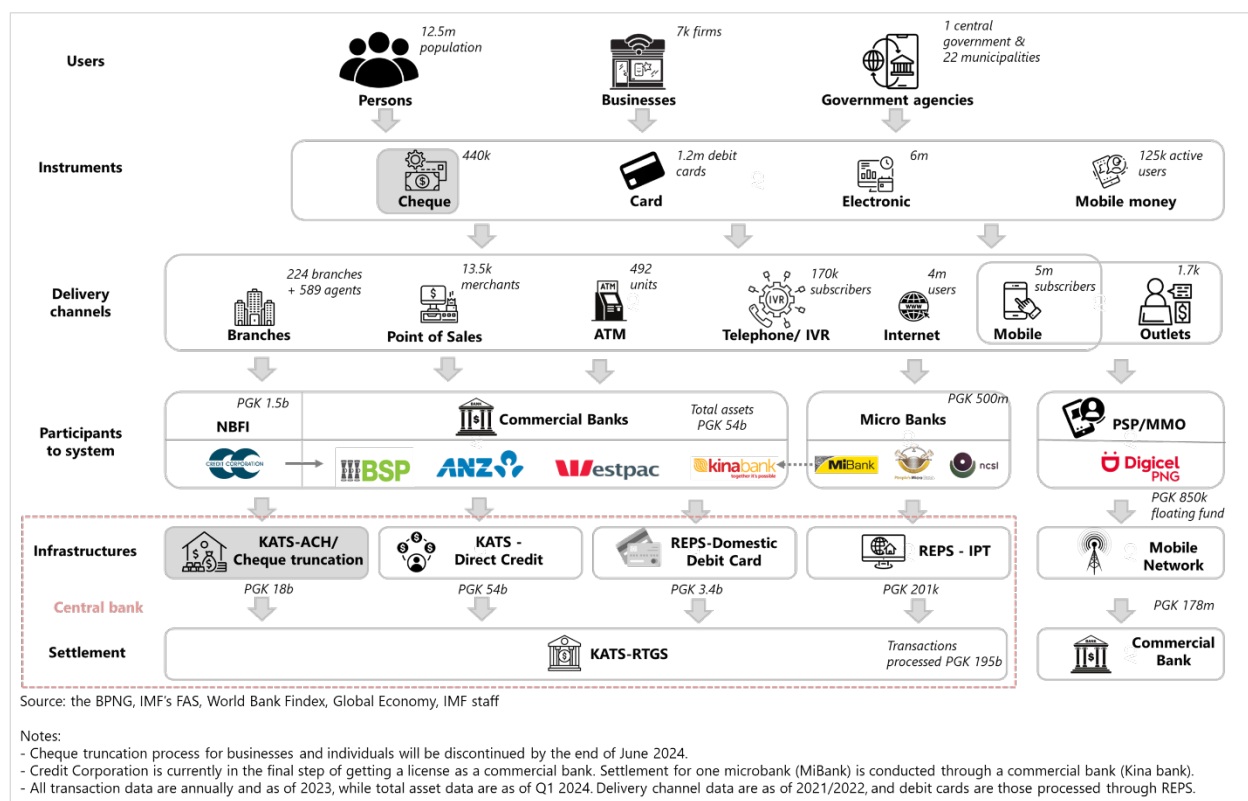
94. **Despite these reforms, there are areas where the legal framework for NPS could be further strengthened.** The NPS Act lacks provisions for cross-border payments and remittances, which are crucial economic sectors in PNG.<sup>14</sup> The Act's provisions granting the BPNG the power to prosecute offences may conflict with the general prosecutor's authority, rooted in the Criminal Code and Constitution. Although these provisions have not been tested by the BPNG, a similar case in another sector saw the BPNG defer to the general prosecutor after a market player contested the central bank's authority. Furthermore, the NPS Act is not fully clear on regulating e-money schemes. It recognizes PSPs and payment systems operators (PSOs) but also includes a brief section ruling that "...no person, other than a bank, may issue electronic money without having obtained a license from the Central Bank". This highlights the need for clearer regulatory definitions and scopes.

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<sup>13</sup> In July 2024, the BPNG discontinued the cheque truncation process for businesses and individuals. Cheque processing for government agencies has not been affected.

<sup>14</sup> In Q1 2024, cross-border payments via SWIFT recorded nearly PGK 8 billion, with 90 percent being outward transactions.

**Figure 2. Papua New Guinea: Payment Landscape and Development**



95. **The secondary legislative instruments supporting NPS development and oversight also require enhancement to provide clear implementation guidelines.** The current four directives are relatively high-level, leading to uncertainties during implementation. There is a notable lack of formal rules, procedures, or guidelines accompanying these directives. For example, Directive 01/2019 on oversight offers a general framework without detailed guiding principles, comprehensive guidelines, or risk-based assessment methodologies tailored to different payment systems, services, or instruments. Given the rapid evolution of digital payments, a detailed oversight framework, including specific assessment methodologies,<sup>15</sup> is essential for effective and efficient oversight. Strengthening these secondary legislative instruments will ensure that PNG's payment systems can adapt to technological advancements and maintain robust regulatory standards.

96. **The BPNG's Payment System Oversight Function Department (PSOFD) and Payment System Operation Department (PSOD) are not functioning optimally due to understaffing.** These departments are under the Finance and Payments Group. The PSOFD comprises three units responsible for formulating payment systems policy, reporting and analytics (off-site), and assessment and compliance (on-site). Presently, all three positions in the payment systems policy unit are vacant. The

<sup>15</sup> European Union for instance has formulated and implemented a comprehensive oversight framework for electronic payment instruments, schemes and arrangements (PISA): [https://www.ecb.europa.eu/paym/pdf/consultations/ecb.PISAPublicconsultation202111\\_1.en.pdf](https://www.ecb.europa.eu/paym/pdf/consultations/ecb.PISAPublicconsultation202111_1.en.pdf) and its detailed methodology assessments: [https://www.ecb.europa.eu/paym/pdf/consultations/ecb.PISAPublicconsultation202111\\_2.fr.pdf](https://www.ecb.europa.eu/paym/pdf/consultations/ecb.PISAPublicconsultation202111_2.fr.pdf).

financial system development policy unit under the FSDD is handling policy formulation, including the issuance of four directives in 2019. The FSDD is under the Financial Stability Group. This arrangement necessitates smooth collaboration between the PSOD and FSDD, with the latter already managing a wide range of tasks, including regulation of financial institutions. The PSOD consists of two units, each for operating KATS and REPS. The systems operated by the central bank seem well-run, but procedures and rules should be made comprehensive and in accordance with international risk management standards (Principles for Financial Market Infrastructure or PFMI).

97. **The BPNG oversees payment systems but has yet to formally identify and designate systemically important payment systems (SIPS).** The BPNG has not yet developed a framework for SIPS designation. Without this framework, SIPS are not subject to higher international risk-management standards - PFMI. The BPNG has also not conducted self-assessments of SIPS against PFMI. However, the BPNG plans to conduct a self-assessment for KATS-RTGS, with TA from the World Bank.

98. **The overall payment systems oversight function needs to be strengthened.** A clear and comprehensive oversight framework, accompanied by a detailed assessment methodology for each system, is essential. This should include identifying PFMI principles to assess embedded risks. The PSOD drafted a payment system oversight framework in 2018, but it has not been finalized or issued. Consequently, oversight staff independently develop on-site supervision modules, which poses risks of inconsistency and potential reputational risks. While the BPNG has developed financial network analytics (FNA), integration with banking reports, especially for PSP banks, is necessary. Enhanced coordination between payment oversight and banking supervision is also crucial to improve the central bank's regulatory and supervisory effectiveness. For instance, the Central Bank of Brazil developed a contagion model using payment system data to investigate the bankruptcy of many non-financial companies which led to high unemployment in 2014.<sup>16</sup> Close coordination between two supervisory functions could also reduce market confusion. There are also no dedicated IT experts for payment systems oversight.

99. **The efficiency of the licensing process for PSPs could be enhanced.** The licensing process for PSPs is centralized at FSDD, which offers many benefits like a single point of contact and clarity for market players. However, the process could be more efficient, involving close coordination with the PSOD. Currently, all licensing submissions and processes are manual, which is cumbersome. Despite the BPNG being professional and transparent in its licensing process, manual document submissions require significant resources for verification. Given the rapid development of technology and innovation in payment systems, the licensing unit also needs continuous updates from payment oversight and policy units.

100. **The BPNG has issued one license to a PSP, which is an e-money provider.**<sup>17</sup> This PSP has been operational since 2013 and covers all provinces in PNG, thus holding significant potential to support financial inclusion initiatives. The licensing guidelines do not cover other payment activities such as merchant acquisition and payment aggregation. This gap may create uncertainty in the market.

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<sup>16</sup> See Oliveira P. and Vivan G. (2023), "The New Frontiers of Supervision".

<sup>17</sup> Digicel Financial Services Ltd., a PNG based firm having subsidiaries in Pacific Island countries.

Nevertheless, the NPS Act empowers the BPNG with registration authority<sup>18</sup> that can be leveraged for less risky payment activities, potentially reducing market uncertainty, and enhancing regulatory clarity.

101. **The KATS system rules include provisions for contingency events, but disaster recovery arrangements are not clearly defined.** The disaster recovery is treated as a business-as-usual activity by the Information & Communication Technology Department. Annual disaster recovery tests are performed, with a successful test involving all participants conducted in April 2024. Despite these efforts, the KATS rules should explicitly outline disaster recovery plans and business continuity requirements for both operators and participants. A clear link between KATS rules issued by the PSOD and the business-as-usual disaster recovery arrangements by the Information & Communication Technology Department should be established to increase transparency. This alignment is required by Principle 17 of the PFMI, which obliges the FMI operator to disclose the operating rules of the system and to have a business continuity management plan that includes a disaster recovery plan.

102. **The IPT system requires enhancement to realize the full benefits of a Fast Payment System for consumers and the economy.** The system has been developed to enable payments where the funds are available to the customer in an immediate or near immediate time frame. For settlement, it uses deferred net settlement to KATS by next day. However, since its inception in 2021, uptake has been very slow (Figure 3). Participation in the system is very limited, with only two microbanks (Nationwide Microbank Ltd and People's Microbank Ltd) and one S&LS (Nashfund Saving & Loan Ltd) onboarded. Commercial banks have yet to join the system. The BPNG charges a small transaction fee to participants, and does not influence participant-to-customer pricing. The combined processing of IPT and domestic debit card transactions on the same platform may also hinder performance. Separating these platforms could increase speed and reliability, making IPT more competitive, as suggested by the ongoing review of the NPS Strategy 2024-2026.

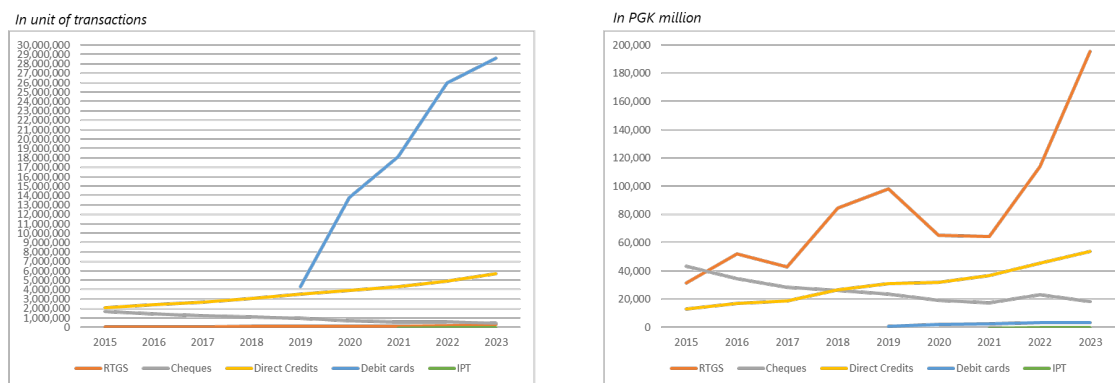
103. **The 2019 electronic fund transfers directive includes a section on technology and information security, but the BPNG has not issued specific IT security guidelines for PSPs and PSOs.** The directive lacks comprehensive cyber resilience requirements, such as a cyber resilience framework, governance, response and recovery plans, and specific cyber testing with key service providers. Aligning these guidelines with the CPMI-IOSCO Guidance on Cyber Resilience for FMI, the central bank's overall cybersecurity policies and strategies, and banking regulations for PSP banks is

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<sup>18</sup> Section 4(3) and 4(4) of the NPS Act: The Central Bank may substitute the requirement of licensing with registration when the activity of a specific category of payment services providers – (a) does not involve specific risks for the market; or (b) would strongly compromise competitiveness. This measure shall not generate discrimination among payment services providers offering the same services.

crucial to enhance the security of electronic fund transfers.<sup>19</sup> Once the guidelines have been issued, they need to be updated on a regular basis.

**Figure 3. Papua New Guinea: Volume and Value of Processed Payments**



Source: the BPNG

104. **Other FMIs operated by the BPNG are the Central Securities Depository (CSD) and Securities Settlement System (SSS), both with limited functions.** The CSD, managed by the Domestic Financial Market Department, handles securities registry, foreign exchange market, and money market operations, focusing on Central Bank Bills (CBB) and government bonds (TBill, TBond, and Inscribed Stock) for monetary operation and fiscal measures. Currently, only primary markets are available, but plans are in place to develop secondary markets, with enhancements of the CSD expected by year-end. The SSS, managed by back office under the Corporate Secretary Group, supports primary market securities settlement, with fund settlement via KATS-RTGS enabling delivery versus payments mechanism. Although general risk management applies to both CSD and SSS, identification, adoption, and self-assessment against PFMI have not been conducted.

105. **The BPNG has been running a regulatory sandbox since 2020 and is in the early stages of exploring central bank digital currency (CBDC).** The sandbox aims to test general fintech innovations in a safe, controlled environment, fostering new social and economic opportunities. Four fintech firms have applied to participate in the sandbox, with one approved, two rejected, and one application in progress. The sandbox rules and procedures were developed iteratively. The BPNG is also keen to explore CBDC's potential to achieve financial inclusion and enhance payment system resilience and efficiency. It has held preliminary discussions with the central bank of Cambodia on project Bakong, and

<sup>19</sup> The importance of having comprehensive IT security guidelines for PSPs and PSOs, which align with international standards, the central bank's overall cyber resilience policy and strategy, and banking regulations, was tested when the largest bank experienced a technical issue during the migration of its core banking services. Upon migration, the new system failed to update customers' balances even after funds had been withdrawn from their accounts. Although the bank responded immediately to the incident, it took some time to resolve the issue. The unclear and uncertain resolution caused confusion among the affected customers. Comprehensive IT security guidelines covering a cyber resilience framework, governance, response and recovery plans, and specific cyber testing would guide both the PSP bank in identifying and mitigating risks related to its IT system and assist the regulator/supervisor in overseeing and ensuring effective incident management.

there is interest from a Japanese fintech firm for conducting a feasibility study.<sup>20</sup> A thorough understanding of CBDC's implications for monetary policy, financial stability, and payment systems is crucial for the BPNG to make informed decisions.

## Scope for future TA

106. **The BPNG should review and strengthen the legal basis of the NPS.** The primary legislation review should focus on incorporating provisions for cross-border payments and remittances to support economic initiatives. Additionally, provisions on legal proceedings that conflict with the general prosecutor's powers need alignment to minimize legal risks and avoid overburdening the central bank. Clarifying the e-money scheme is also necessary. The secondary legislation review should aim to provide comprehensive and clear guidance for NPS oversight and implementation/operations.

107. **The payment systems policy and oversight functions require strengthening.** The FSDD should gradually transfer the responsibility of formulating payment system policy to the PSOFD, while the PSOFD needs to increase capacity and expertise in this area. Immediate action is needed to fill the three vacant positions in the payment policy unit with competent individuals through rotation, external hiring, or a combination. Additionally, training on the PFMI for existing and new staff is essential, including in the IMF regional training institutes.

108. **The BPNG should develop a clear and comprehensive oversight framework, supported by a detailed assessment methodology.** The 2018 draft oversight framework should be updated, finalized, and issued. This framework should be completed with detailed identification of PFMI principles to be applied and provide a methodology to assess each principle. Strengthening coordination between payment systems, banking supervision, and the financial system development department is also crucial. This includes developing an integrated reporting process, inputs in the licensing process, market analysis discussions, and policy formulation. Enhanced coordination will mitigate confusion and reputation risks among PSP banks.

109. **The BPNG needs to enhance its IT risk supervisory capacity.** Hiring or identifying and training a pool of IT staff experienced in IT risk management and certified in IT audit is essential for effective supervision. This initiative should be implemented at the organizational level to support various supervision departments and ensure robust IT risk management across the board.

110. **The BPNG should formally adopt and apply the PFMI standards to SIPS, CSD, and SSS.** First, the BPNG should develop an FMI designation framework for SIPS. The criteria used for identifying SIPS should be consistent with the definition in PFMI. Designation of SIPS should follow immediately. Second, the BPNG should formally adopt PFMI for SIPS, CSD, and SSS. This should be done through directives, regulations, or guidelines that apply all the relevant principles to each system. Third, each

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<sup>20</sup> Project Bakong, launched by the National Bank of Cambodia in October 2020, is a blockchain-based national payment system designed to facilitate real-time transactions and financial inclusion. While Bakong leverages blockchain technology, it is distinct from a CBDC as it does not represent a digital version of the national currency issued by the central bank. For more information, see <https://bakong.nbc.gov.kh/en/>

operator of the systems should conduct self-assessments against PFMI. Lastly, the oversight unit should review the self-assessments and assess itself against the five authorities' responsibilities in the PFMI.<sup>21</sup>

111. **The payment licensing process could be strengthened.** The BPNG could develop an online licensing process to enhance efficiency, save resources, and mitigate risks associated with manual processing. The BPNG could also consider exercising its registration power under the NPS Act to leverage the licensing regime for less risky payment activities, schemes, or arrangements while maintaining financial stability and smooth payment system functioning.

112. **The IPT system could be enhanced to maximize its benefits to customers and the economy.** Onboarding more participants, particularly commercial banks, is essential. Comprehensive review and improvement of rules, procedures, and guidelines, including pricing policy influence, are necessary. Technical process improvements, such as separating IPT from the domestic debit card transaction processing platform, should also be considered.

113. **The BPNG should issue specific IT security guidelines for PSPs and PSOs and update them regularly.** These guidelines should cover cyber resilience requirements, including a cyber resilience framework, governance, response, recovery plans, and specific cyber testing with key service providers, aligning with CPMI-IOSCO Guidance on Cyber Resilience for FMI, banking regulations for PSP banks, and BPNG's cybersecurity policies and strategies is critical.

114. **KATS rules should explicitly outline disaster recovery plans and business continuity requirements for both operators and participants.** To increase transparency, a clear link between KATS rules issued by the PSOD and the business-as-usual disaster recovery arrangements by the Information & Communication Technology Department should be established, aligning with Principle 17 of the PFMI.

115. **Comprehensive prudential regulation for e-money providers should be gradually established.** The regulations should include detailed guidelines on fund safekeeping and segregation, incorporate robust risk management frameworks and policies addressing credit, market, operational, liquidity, and general business risks, ensure thorough oversight, and cover disclosure and transparency, data and privacy protection, and supervisory approaches. A reference to good practices published by IMF and CPMI/World Bank could also be made.

116. **The BPNG should review regulatory sandbox procedures to foster innovation and promote financial inclusion and increase its capacity and understanding on CBDC.** Sandbox procedures should be flexible to accommodate more innovation while ensuring robust testing to safeguard financial stability. In exploring CBDC, the BPNG should have a better understanding of CBDC's implications for monetary policy, financial stability, and payment systems, as well as its costs, risks, and benefits, to be able to make informed decisions.

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<sup>21</sup> Responsibility A to E of the PFMI, encompassing regulation, supervision, and oversight of an FMI, powers and resources, disclosure of policies, adoption of the PFMI, and cooperation with other authorities. See [https://www.bis.org/cpmi/publ/d101\\_es.pdf](https://www.bis.org/cpmi/publ/d101_es.pdf).

## H. Financial Statistics

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### Current situation

#### Financial Soundness Indicators

117. **The BPNG compiles and reports FSIs data to the IMF's Statistics Department (STA) for dissemination on the IMF's [FSIs data portal](#) on a quarterly basis.** These include 13 core and eight additional FSIs for deposit-takers (DTs), 11 for other financial corporations (OFCs) and two additional FSIs for real estate markets (Table 2). The latest disseminated FSI data refer to 2023Q4.

118. **The FSIs compiled are broadly in line with the IMF 2019 FSIs Guide methodology.** The 2022 IMF TA mission supported BPNG to implement the new methodology with recommendations for further improvement to source data. BPNG has addressed some of the recommendations and some are work-in-progress. Current FSI data coverage include DTs (excluding S&LSs) and OFCs (insurance companies and ASFs).

119. **The FSIs for DTs are compiled based on a cross border cross sector domestically incorporated (CBCSDI) consolidation basis, which is appropriate based on the structure of the banking sector.**<sup>22</sup> The 2019 FSIs Guide recommends using CBCSDI consolidation basis, but it also provides domestic location consolidation basis as an alternative method when resident DTs have no nonresident branches or subsidiaries or have ones that are so small that they do not materially affect the FSIs. The FSIs for DTs in PNG cover commercial banks, LFIs, and microfinance institutions. One bank in PNG has a resident non-deposit taker subsidiary (insurance company) and foreign deposit taking subsidiaries, therefore group data consolidation is applicable. However, the insurance subsidiary is not consolidated with the parent bank for FSI compilation purposes, in line with FSI Guide methodology.

120. **The current compilation of FSIs can be further improved to support financial sector stability analysis.** The areas for improvement include (1) implement last mission recommendation on the need for further institutional sector and financial instrument classification breakdowns for deposit takers and OFCs, (2) expand coverage of FSIs for DTs to include S&LSs, (3) collect and incorporate income and expense data for non-life insurance corporations in FSI compilation, (4) ensure reporting institutions comply with BPNG's reporting requirements for complete coverage of reporting population, (5) updating the FSIs metadata to accurately reflect the accounting and regulatory frameworks underlying FSIs data and any deviations from the 2019 FSIs Guide to better inform data users of the data and compilation practices, and (6) build technical capacity of staff working under FSI unit.

#### Monetary and Financial Statistics

121. **The BPNG reports monthly monetary statistics, using the IMF standardized report forms (SRFs) for the central bank, other depository corporations (ODCs) and OFCs, for dissemination by STA in the *International Financial Statistics (IFS)*.** The SRFs 1SR for the central bank, 2SR for ODCs

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<sup>22</sup> Coverage includes domestically incorporated, domestically controlled and foreign controlled, domestic and foreign branches and subsidiaries of DTs and domestic and foreign subsidiaries of financial non-DTs, excluding insurance companies and their foreign branches.

and 4SR for OFCs are compiled broadly based on the Monetary and Financial Statistics (MFS) *Manual and Compilation Guide* methodology in terms of classification of financial instruments, asset/liability valuation, and sectoring of institutional units. The implementation of SRFs for MFS compilation was supported by an STA TA mission in 2013.

122. **The institutional coverage for ODC include commercial banks, LFIs, S&LSs, and microfinance institutions.** On the other hand, OFCs' coverage includes insurance companies (life and non-life), pension funds, National Development Bank, fund managers, and investment managers. Data for the central bank and ODCs are reported monthly while data for OFCs are quarterly, using reporting templates which are fully aligned to the SRFs. Like for FSIs, full reporting compliance for MFS data, particularly OFCs, is lacking.

123. **The current compilation of MFS can be further improved to support financial sector stability analysis.** The areas for improvement include (i) clarifying the institutional arrangements in recording of IMF accounts between BPNG and the government of PNG, (ii) reviewing the mapping of BPNG chart of accounts to 1SR to ensure correct mapping of new accounts, (iii) reviewing the source data used for compiling OFC data, (iv) ensuring reporting institutions comply with BPNG's reporting requirements for complete coverage of ODCs, pension funds and insurance corporations, (v) BPNG initiating and implementing data sharing arrangements with the Office of Insurance Commissioner and Securities Commission, and (6) building technical capacity of staff working under MFS unit.

### International Investment Positions

124. **With support of IMF STA through the Capacity Development Office of Thailand, the BPNG started compiling quarterly balance of payments (BOP) based on the sixth edition of the Balance of Payments and International Investment Position Manual framework.** The main data source for the current account is the international transaction reporting system (ITRS) which requires to be revamped given its shortcomings. As recommended by the last TA mission, this is reconciled on a quarterly basis with the data from Customs Department obtained from the National Statistics Office. On the financial account the main data source is the ITRS since the private capital flow survey is yet to be conducted. The BOP data is disseminated on BPNG website and reported to the IMF on a quarterly basis. BPNG is still in the process of implementing some of the TA recommendations relating to BOP.

125. **Despite progress achieved in improving the BOP, more efforts are needed to compile and disseminate data on the international investment position (IIP).** For a start, the TA mission proposed the use of MFS data relating to non-resident sector to compile partial IIP. The production of IIP statistics, even though partial and preliminary, is key to improve and validate the quality of investment income and financial account transactions recorded in the BOP. Improvement of MFS data quality is therefore important given the many changes in the PNG economy (oil, mining, liquid natural gas and others) with more complex financial transactions, since the last MFS TA mission. BPNG is also in the process of conducting a pilot private capital flows survey which shall provide some estimates of assets and liabilities of the non-resident sector, useful for IIP compilation.

## Government Finance Statistics

126. **Budgetary Central Government (BCG) liabilities are compiled and reported to STA on annual basis.** However, compiling financial assets stocks and flows for BCG is a huge challenge, as cash accounting is still in use and the data are not in the integrated financial management information systems. The Treasury Department keep records of some of the financial instruments on spreadsheets and these are reported in the annual government public accounts, however there is always a delay with audits so there is a backlog in receiving these statements. There are major issues with determining the general government perimeter in PNG, so expanding coverage remains an issue but also a priority.

## Balance Sheet Approach

127. **The main data source for the balance sheet approach (BSA) matrix is MFS data presented in SRFs formats showing each financial instrument with counterpart sector and currency of denomination (domestic or foreign currency).** The SRFs enable developing from-whom-to-whom tables for stocks for inclusion in the BSA. In addition, information from the external sector and government sector statistics are also required for BSA compilation to supplement MFS data. The external sector statistics, in particular the international investment position (IIP), provides information on stocks of resident sectors with the rest of the world by instrument. Similarly, the government financial balance sheet (GFS) information presenting assets and liabilities of the general government or its subsectors by financial instrument and counterpart sector.

128. **A BSA matrix for PNG for end-2023 is provided in Table 4, based largely on MFS data.** This version of from-whom-to-whom framework presents total assets and liabilities for all the sectors by counterpart sector and by currency, enabling to trace who finances whom, by how much and in what currency. Note that by disaggregating total assets and liabilities, other BSA matrices can be produced for each financial instrument and for different maturity where data are available. PNG's GFS and IIP data are not available for 2023.

129. **After using MFS, IIP, and GFS data, the remaining data gaps in the BSA matrix can be filled with data on nonfinancial corporations and households.** However, collecting data on financial positions of nonfinancial corporations and households can be challenging, as they can only be obtained from national accounts-related data sources.

## Scope for future TA

130. **The authorities will benefit from further TA in macroeconomic statistics.** TA could assist with improving the compilation of MFS, FSIs and IIP to close the current data gaps in each of these areas. The BPNG officials, who are responsible for the statistics compilation, are also encouraged to attend training courses on MFS, FSIs, BOP/IIP, and GFS offered by the IMF. The detailed information relating to course curriculum and schedule are available on the webpage of the [IMF's Institute for Capacity Development](#).

## Financial Soundness Indicators

131. **TA could support the authorities in improving the FSI data quality.** TA can assist with (i) reviewing the quality of available source data and improving their sector and financial instrument

breakdowns for both DTs and OFCs in line with the recommendations made by the 2022 TA FSIs mission;<sup>23</sup> (ii) reviewing the definition and calculation of some important underlying series to ensure consistency with the *2019 FSIs Guide*, (iii) updating the FSIs metadata, and (iv) presenting the FSI compilation framework to FSI compilers as a hands-on training to improve staff technical capacity.

### Monetary and Financial Statistics

132. **A TA mission in 2013 supported expanding MFS coverage to include OFCs.** The mission reviewed available source data for CB, ODCs and OFCs (superannuation funds, insurance corporations, etc.), to assess their adequacy for the MFS compilation; assisted in setting up the report forms for OFCs based on the MFS Manual and Compilation Guide; and introduced the SRF 4SR for compiling MFS for OFCs. The mission also worked with the BPNG staff on expanding the ODCs coverage by including microfinance institutions and S&LSs.<sup>24</sup> However, coverage of OFCs data is not complete with partial reporting for general insurance corporations used in compiling the SRF 4SR for OFCs.

133. **TA could support BPNG to improve the quality of compiled MFS data.** TA in MFS could assist with (i) reviewing and improving source data for central bank 1SR data, (ii) reviewing source data for separate categories of institutions under ODCs (2SR) and OFCs (4SR), (iii) compiling the balance sheet approach matrix for PNG, and (iv) presenting the MFS compilation framework to MFS compilers as a hands-on training to improve staff technical capacity.

### International Investment Positions

134. **A TA mission on BOP was conducted in PNG in 2023.**<sup>25</sup> The mission assisted the BPNG authorities in strengthening source data to improve the coverage, periodicity, and timeliness of the BOP statistics, with emphasis on large current account transactions. The TA mission of December 2022 worked with ESS compilers to adopt the latest methodological standards Balance of Payments and International Investment Position Manual, sixth edition for its BOP estimates.

135. **Further TA could support the authorities to improve the BOP data quality and compile IIP.** The mission could assist BPNG to review /assist in the implementation of the last mission recommendations relating to (i) reconciliation of goods imports and goods exports with the National Statistics Office, (ii) implementation of the collection of data on personal transfers from BPNG's internal departments, (iii) surveys of the 30 largest entities for information on external transactions and positions, and (iv) production of preliminary IIP.

### Government Finance Statistics

136. **TA could support the authorities to improve the GFS data quality by supporting implementation of the recommendations of the last GFS TA mission.** A TA mission on GFS was

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<sup>23</sup> TA Report on Financial Soundness Indicators Mission (in-person) for Papua New Guinea (November 14–18, 2022).

<sup>24</sup> TA report on Monetary and Financial Statistics, TA Mission for Papua New Guinea (February 19– March 1, 2013).

<sup>25</sup> Report on External Sector Statistics TA Mission for Papua New Guinea (November 27 - December 8, 2023).

conducted in PNG in 2023<sup>26</sup>. The mission assisted the Department of Treasury in improving the compilation and dissemination of government finance statistics (GFS) and public sector debt statistics and assessed the progress in implementing past missions' recommendations.

### Balance Sheet Approach

137. **TA support to PNG in the above areas (MFS, FSI, IIP and GFS) will improve the quality of key data sources for compiling BSA.** As noted above the main data source, which is timely and mostly reliable, in compiling BSA is MFS data. BPNG would therefore benefit in working with MFS TA to address gaps in the identified areas of improvement as a matter of priority, to generate BSA on a regular basis. TA on other areas will facilitate availability of data which will supplement MFS data and close remaining data gaps in BSA compilation.

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<sup>26</sup> TA report on Government Finance Statistics, TA Mission for Papua New Guinea (August 2-15, 2023).

**Table 4. Papua New Guinea: 2023 Balance Sheet Approach Matrix**  
(in percent of GDP)

|                           | Government           |             | Central Bank |             | Other Depository Corporations |             | Other Financial Corporations |             | Nonfinancial Corporations |             | Households           |             | External     |             | Total  |             |  |  |
|---------------------------|----------------------|-------------|--------------|-------------|-------------------------------|-------------|------------------------------|-------------|---------------------------|-------------|----------------------|-------------|--------------|-------------|--------|-------------|--|--|
|                           | Assets               | Liabilities | Assets       | Liabilities | Assets                        | Liabilities | Assets                       | Liabilities | Assets                    | Liabilities | Assets               | Liabilities | Assets       | Liabilities | Assets | Liabilities |  |  |
| Government                |                      |             | Source: CB   |             | Source: ODCs                  |             | Source: OFCs                 |             | (GFS/MFS estimation)      |             | (GFS/MFS estimation) |             | Source: IIP  |             |        |             |  |  |
| Total                     |                      |             | 2            | 3           | 15                            | 6           | 8                            | 0           | ...                       | ...         | -                    | -           | -            | -           | 25     | 10          |  |  |
| In domestic currency      |                      |             | 2            | 3           | 15                            | 6           | 8                            | 0           | ...                       | ...         | -                    | -           | -            | -           | 25     | 10          |  |  |
| In foreign currency       |                      |             | -            | -           | -                             | 0           | 0                            | -           | -                         | -           | -                    | -           | -            | -           | 0      | 0           |  |  |
| Central Bank              | Source: CB           |             |              |             | Source: CB                    |             | Source: CB                   |             | Source: CB                |             | Source: CB           |             | Source: CB   |             |        |             |  |  |
| Total                     | 3                    | 2           |              |             | 9                             | 0           | 0                            | -           | 0                         | 0           | 2                    | 0           | 2            | 13          | 16     | 15          |  |  |
| In domestic currency      | 3                    | 2           |              |             | 9                             | 0           | 0                            | -           | 0                         | 0           | 2                    | 0           | 0            | 0           | 14     | 2           |  |  |
| In foreign currency       | -                    | -           |              |             | 0                             | -           | -                            | -           | -                         | -           | -                    | -           | 2            | 13          | 2      | 13          |  |  |
| Oth. Dep. Corporations    | Source: ODCs         |             | Source: CB   |             | Source: ODCs                  |             | Source: ODCs                 |             | Source: ODCs              |             | Source: ODCs         |             | Source: ODCs |             |        |             |  |  |
| Total                     | 63                   | 15          | 037          | 9           | 0                             | 1           | 3                            | 0           | 18                        | 11          | 12                   | 4           | 1            | 2           | 41     | 43          |  |  |
| In domestic currency      | 6                    | 15          | 0            | 9           | 0                             | 1           | 3                            | 0           | 17                        | 11          | 11                   | 4           | 0            | 1           | 39     | 41          |  |  |
| In foreign currency       | 0                    | -           | -            | 0           | 0                             | 0           | 0                            | -           | 1                         | 0           | 0                    | 0           | 1            | 2           | 1      | 2           |  |  |
| Oth. Fin Corporations     | Source: OFCs         |             | Source: CB   |             | Source: ODCs                  |             | Source: OFCs                 |             | Source: OFCs              |             | Source: OFCs         |             | Source: OFCs |             |        |             |  |  |
| Total                     | 0                    | 8           | -            | 0           | 0                             | 3           | 0                            | 0           | 0221                      | 2           | 17                   | 0           | 0            | 4           | 18     | 18          |  |  |
| In domestic currency      | 0                    | 8           | -            | 0           | 0                             | 3           | 0                            | 0           | 0                         | 2           | 17                   | 0           | 0            | 0           | 18     | 14          |  |  |
| In foreign currency       | -                    | 0           | -            | -           | -                             | 0           | 0                            | -           | -                         | 0           | -                    | 0           | 0            | 4           | 0      | 4           |  |  |
| Nonfinancial Corporations | (GFS/MFS estimation) |             | Source: CB   |             | Source: ODCs                  |             | Source: OFCs                 |             |                           |             | (No sectoral data)   |             | Source: IIP  |             |        |             |  |  |
| Total                     | ...                  | ...         | 0            | 0           | 11                            | 18          | 2                            | 0           |                           |             |                      |             | 13           | -           | 26     | 18          |  |  |
| In domestic currency      | ...                  | ...         | 0            | 0           | 11                            | 17          | 2                            | 0           |                           |             |                      |             | ...          | ...         | 13     | 17          |  |  |
| In foreign currency       | -                    | -           | -            | -           | 0                             | 1           | 0                            | -           |                           |             |                      |             | 13           | -           | 13     | 1           |  |  |
| Households                | (GFS/MFS estimation) |             | Source: CB   |             | Source: ODCs                  |             | Source: OFCs                 |             | (No sectoral data)        |             |                      |             | Source: IIP  |             |        |             |  |  |
| Total                     | -                    | -           | 0            | 2           | 4                             | 12          | 0                            | 17          |                           |             |                      |             | ...          | ...         | 5      | 31          |  |  |
| In domestic currency      | -                    | -           | 0            | 2           | 4                             | 11          | 0                            | 17          |                           |             |                      |             | ...          | ...         | 5      | 31          |  |  |
| In foreign currency       | -                    | -           | -            | -           | 0                             | 0           | 0                            | -           |                           |             |                      |             | ...          | ...         | 0      | 0           |  |  |
| External                  | Source: IIP          |             | Source: CB   |             | Source: ODCs                  |             | Source: OFCs                 |             | Source: IIP               |             | Source: IIP          |             |              |             |        |             |  |  |
| Total                     | -                    | -           | 13           | 2           | 2                             | 1           | 4                            | 0           | -                         | 13          | ...                  | ...         |              |             | 19     | 16          |  |  |
| In domestic currency      | -                    | -           | 0            | 0           | 1                             | 0           | 0                            | 0           | ...                       | ...         | ...                  | ...         |              |             | 1      | 0           |  |  |
| In foreign currency       | -                    | -           | 13           | 2           | 2                             | 1           | 4                            | 0           | -                         | 13          | ...                  | ...         |              |             | 18     | 15          |  |  |
| Total                     | 10                   | 25          | 15           | 16          | 42                            | 42          | 18                           | 18          | 18                        | 26          | 31                   | 5           | 16           | 19          | CHECK  | CHECK       |  |  |
| In domestic currency      | 10                   | 25          | 2            | 14          | 40                            | 40          | 14                           | 18          | 17                        | 13          | 31                   | 5           | 0            | 1           | 97     | 98          |  |  |
| In foreign currency       | 0                    | 0           | 13           | 2           | 2                             | 1           | 4                            | 0           | 1                         | 13          | 0                    | 0           | 15           | 18          | 34     | 34          |  |  |

Source: IMF Staff

## Annex 1. Papua New Guinea: FSSR Detailed TA Work Plan

| Strategic Objective 1. Strengthen an effective macroprudential policy framework |                                                                                                                                                   |          |
|---------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------|----------|
| Focus of TA                                                                     | Recommended actions                                                                                                                               | Timeline |
| Macroprudential policy framework is operational                                 | Adopt a communications strategy for financial stability (encompassing risks and policy measures)                                                  | ST       |
|                                                                                 | Develop a macroprudential policy strategy that outlines the policy toolkit                                                                        | MT       |
| Systemic risk monitoring framework implemented                                  | Finalize and publish a Financial Stability Report on a regular (annual) basis, considering expert review                                          | ST       |
|                                                                                 | Develop more systematic and structured systemic risk reporting for regular FSC review                                                             | ST       |
|                                                                                 | Develop the capacity to undertake stress testing by ensuring adequate models, data availability, and trained staff                                | MT       |
| Macroprudential policy tools used to mitigate specific systemic risks           | Complete designation process for domestically systemically important bank(s) and consider amending capital adequacy regulation for capital buffer | MT       |
|                                                                                 | Introduce the Basel III capital buffers framework                                                                                                 | LT       |

| Strategic Objective 2. Strengthen regulation and supervision of deposit-taking financial institutions |                                                                                                                                                                                                                                                                                                         |          |
|-------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------|
| Focus of TA                                                                                           | Recommended actions                                                                                                                                                                                                                                                                                     | Timeline |
| Legislation empowers supervisors with an adequate range of corrective measures                        | Amend the BFIA to broaden the range of corrective measures                                                                                                                                                                                                                                              | MT       |
| Prudential regulations on capital adequacy developed/strengthened                                     | Implement regulation on capital adequacy                                                                                                                                                                                                                                                                | ST       |
| Prudential regulations on risk management developed/strengthened                                      | Implement regulations on risk management, covering (i) credit risk management; (ii) market risk management; (iii) liquidity risk management; (iv) operational risk management; (v) management of interest rate risk in banking book; (vi) cyber security risk management; and (vii) IT risk management. | MT       |
| Prudential regulations on liquidity developed/strengthened                                            | Issue enhanced liquidity regulations in line with Basel III standard                                                                                                                                                                                                                                    | LT       |
| Supervisor monitor and supervise banking groups on consolidated basis                                 | Banks submit reports on a solo and consolidated basis                                                                                                                                                                                                                                                   | MT       |

|                                                                                     |                                                                                  |    |
|-------------------------------------------------------------------------------------|----------------------------------------------------------------------------------|----|
|                                                                                     | Supervisors assess banks' risks on a consolidated basis                          | MT |
| Quality and timeliness of regulatory data are adequate                              | Bank reports provide timely and relevant data for risk assessment                | MT |
| Supervisors have sufficient capacity to effectively implement supervisory processes | Supervisors are adequately trained to be able to implement supervisory processes | ST |

| Strategic Objective 3. Strengthen regulation and supervision of insurance companies and superannuation funds         |                                                                                                                                             |          |
|----------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------|----------|
| Focus of TA                                                                                                          | Recommended actions                                                                                                                         | Timeline |
| Prudential regulations for risk-based capital adequacy and risk management are developed/strengthened                | The regulations for life and general insurers are enhanced and harmonized                                                                   | ST       |
|                                                                                                                      | A risk-based capital regime with the adequate resilience calibration is in place                                                            | ST       |
| Effective risk-based supervision is in place and has been implemented                                                | The risk profiling tools are developed, and the supervisory stance is adjusted according to the level of riskiness of the supervised entity | MT       |
|                                                                                                                      | Stress test models are used, and risks are assessed under stressful conditions                                                              | LT       |
|                                                                                                                      | A group-wide supervision framework for insurance groups including the setup of colleges of supervisors where relevant is in place           | LT       |
| Supervisors have sufficient capacity to effectively implement risk-based supervision and other supervisory processes | The supervision structure allows for effective supervision                                                                                  | MT       |
|                                                                                                                      | Supervisors are adequately trained to effectively implement risk-based supervision and other supervisory processes                          | MT       |
| Effective supervision of superannuation funds is in place                                                            | Supervisory tools are developed to assess the probability of the investment strategy of superannuation funds to deliver the expected yield  | MT       |

| Strategic Objective 4. Strengthen the bank resolution regime     |                                                                                                                               |          |
|------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------|----------|
| Focus of TA                                                      | Recommended actions                                                                                                           | Timeline |
| Special resolution regime is introduced                          | Adopt amendments to the BFIA, CBA, Companies Act, and ICCA Act with regards to the development of a special resolution regime | MT       |
| Operational preparedness of the resolution authority is enhanced | Ensure adequate internal organizational structure and staffing of the resolution authority to discharge its responsibilities  | ST       |
|                                                                  | Develop recovery and resolution plans for the largest bank, including cross border aspects with foreign counterparts          | MT       |
|                                                                  | Develop and operationalize policies and procedures for the use of the various resolution instruments                          | MT       |

| Strategic Objective 5. Strengthen emergency liquidity assistance framework |                                                                                     |          |
|----------------------------------------------------------------------------|-------------------------------------------------------------------------------------|----------|
| Focus of TA                                                                | Recommended actions                                                                 | Timeline |
| Emergency liquidity assistance                                             | Adopt public instructions and internal procedures on emergency liquidity assistance | ST       |

| Strategic Objective 6. Strengthen crisis preparedness arrangements |                                                                                                                                                  |          |
|--------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------|----------|
| Focus of TA                                                        | Recommended actions                                                                                                                              | Timeline |
| Effective inter-agency coordination                                | Inaugurate the inter-agency Financial Sector Council with supporting charter and procedures                                                      | MT       |
|                                                                    | Sign the multilateral MoU with relevant foreign authorities on cross-border coordination on recovery, resolution planning, and crisis management | MT       |
| Crisis preparedness plan                                           | Formalize all crisis preparedness-related procedures into a financial crisis preparedness plan                                                   | LT       |

| Strategic Objective 7. Strengthen frameworks for oversight and operation of financial market infrastructures |                                                                                                                                |          |
|--------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------|----------|
| Focus of TA                                                                                                  | Recommended actions                                                                                                            | Timeline |
| Legal review of NPS law                                                                                      | Review the legal basis (legal framework and implementing regulations) of the NPS oversight and operations.                     | ST       |
|                                                                                                              | Strengthen the legal basis of the NPS.                                                                                         | MT       |
| Strengthening the oversight functions of payment systems                                                     | Develop a clear and comprehensive oversight framework, supported by a detailed assessment methodology, with reference to PFMI. | ST       |
|                                                                                                              | Train existing and new staff on PFMI.                                                                                          | ST       |
|                                                                                                              | Develop an integrated reporting process.                                                                                       | LT       |

|                                        |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |    |
|----------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----|
|                                        | Enhance IT risk supervisory capacity.                                                                                                                                                                                                                                                                                                                                                                                                                                                                | LT |
|                                        | Formally adopt and apply the PFMI standards to SIPS, CSD, and SSS.: <ul style="list-style-type: none"> <li>- Develop FMI designation framework for SIPS.</li> <li>- Draft regulation to designate SIPS.</li> <li>- Formally adopt PFMI for SIPS, CSD, and SSS.</li> <li>- Conduct self-assessments against PFMI (operators of KATS-RTGS, CSD, and SSS).</li> <li>- Review the self-assessments and assess oversight functions against the five authorities' responsibilities in the PFMI.</li> </ul> | MT |
|                                        | Draft specific IT security guidelines for PSPs and PSOs, covering cyber resilience requirements, including a cyber resilience framework, governance, response, recovery plans, and specific cyber testing with key service providers, aligning with CPMI-IOSCO Guidance on Cyber Resilience for FMI, banking regulations for PSP banks, and BPNG's cybersecurity policies and strategies.                                                                                                            | MT |
|                                        | Issue the IT security guidelines.                                                                                                                                                                                                                                                                                                                                                                                                                                                                    | MT |
|                                        | Update the IT security guidelines on regular basis.                                                                                                                                                                                                                                                                                                                                                                                                                                                  | LT |
| Strengthening the licensing process    | Develop an online licensing process to enhance efficiency, save resources, and mitigate risks associated with manual processing.                                                                                                                                                                                                                                                                                                                                                                     | LT |
| Enhancing operation of payment systems | <b>IPT</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                           |    |
|                                        | Onboard commercial banks to the systems.                                                                                                                                                                                                                                                                                                                                                                                                                                                             | ST |
|                                        | Onboard NBFIs and PSPs to the system.                                                                                                                                                                                                                                                                                                                                                                                                                                                                | MT |
|                                        | Review and improve rules, procedures, and guidelines, including pricing policy influence.                                                                                                                                                                                                                                                                                                                                                                                                            | MT |
|                                        | Improve technical process to increase speed, efficiency, and reliability of the system.                                                                                                                                                                                                                                                                                                                                                                                                              | MT |
|                                        | <b>KATS</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                          |    |
|                                        | Revise KATS rules to explicitly outline disaster recovery plans and business continuity requirements for both operator and participants and to make a clear link between KATS rules issued by the PSOD and the business-as-usual disaster recovery arrangements by the Information & Communication Technology Department.                                                                                                                                                                            | ST |
|                                        | Implement an alternative RTGS system that can settle time-critical transactions within the pre-defined recovery period should also be considered.                                                                                                                                                                                                                                                                                                                                                    | LT |

|                                       |                                                                                            |    |
|---------------------------------------|--------------------------------------------------------------------------------------------|----|
| E-money and mobile money              | Establish comprehensive prudential regulation for e-money providers                        | MT |
| Digital money and innovative payments | Review regulatory sandbox procedures to foster innovation and promote financial inclusion. | ST |
|                                       | Increase capacity and understanding on thinking through CBDC.                              | MT |

| Strategic Objective 8. Strengthen the compilation of accurate and timely financial statistics to support financial stability analysis |                                                                                                                                                                                                               |          |
|---------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------|
| Focus of TA                                                                                                                           | Recommended actions                                                                                                                                                                                           | Timeline |
| <b>Financial sector statistics</b>                                                                                                    |                                                                                                                                                                                                               |          |
| Improve quality of central bank MFS data including recording of Fund accounts.                                                        | Review the mapping of the central bank chart of accounts to SRF 1SR template for MFS compilation. Clarify the institutional arrangements in recording of IMF accounts between BPNG and the Government of PNG. | ST       |
| Improve quality of ODCs and OFCs data                                                                                                 | Training of BPNG MFS compilers and compilers from reporting institutions on the reporting requirements including underlying concepts and methods.                                                             | ST       |
|                                                                                                                                       | BPNG initiate and implement data sharing arrangements with the Office of Insurance Commissioner and Securities Commission.                                                                                    | MT       |
|                                                                                                                                       | Review reporting guidelines for ODCs and OFCs together with individual institutions source data for compliance and accuracy.                                                                                  | MT       |
| Compile Balance Sheet Approach matrix                                                                                                 | Train staff on use of MFS, IIP and GFS data to compile BSA and its use for policy analysis.                                                                                                                   | ST       |
| Improve the quality of FSI data                                                                                                       | Adopt the use of SRF data in DTs and OFCs for detailed sectoring of institutional units and breakdown of financial assets.<br>Expand FSI coverage to include S&LSs.                                           | ST       |
| <b>International Investment Position Statistics</b>                                                                                   |                                                                                                                                                                                                               |          |
| Improve compilation of balance of payment statistics and compile IIP                                                                  | Review and support the implementation of the last mission recommendation.                                                                                                                                     | ST       |
| <b>Government finance statistics</b>                                                                                                  |                                                                                                                                                                                                               |          |
| Lack of comprehensive government finance statistics (GFS) for the construction of BSA                                                 | Support the implementation of the recommendations of the last GFS TA mission and enhance efforts to compile financial assets.                                                                                 | ST       |