



SHADOW MINISTER FOR TREASURY & FINANCE

PO Parliament House

Waigani.NCD

m: +675 71111777

e: chairman@kdda.gov.pg

Sovereign Bond – Under-pricing a negotiation disaster

“The national government has cheaply sold off more of PNG’s resources with a deal good for international financiers and bad for PNG’s people. The massive under-pricing of the Sovereign Bond is like selling off more of PNG’s resources too cheaply. The resource on this occasion is future tax revenue from hard-working people in PNG through their income taxes and GST payments. And the biggest pain of repaying the \$US500 million in 10 years in 2028 is conveniently more than two elections away – so this government will try to run away from its irresponsibility in both the 2022 and 2027 elections” said Ian Ling-Stuckey, PNG’s Shadow Minister for Treasury and Finance.

“The Treasurer Charles Abel is boasting how the Sovereign Bond was massively over-subscribed. However, the 600% level of over-subscription simply says the buyers have got a bargain and the sellers, the people of PNG, have lost out. As a business person, if I put a property on the market and I immediately get more than six buyers at the offer price, I know for sure, I have under-priced the property. I would feel a fool for doing so. I would have essentially ripped myself off. In a very similar way, the people of PNG have just been ripped off with this huge loan called a sovereign bond-and the Treasurer has the audacity to boast about it! Big Maus Long?” said Mr Ling-Stuckey.

“A shameful element of the Treasurer’s press release is that he is caught out yet again, telling another fairytale! Fact, he states that the bond issue in part “will be used to retire high cost short term domestic debt“. There is no short term domestic debt more expensive than this new bond. He is simply lying! Short term debt, using PNG Treasury definitions, means 12 months or less. 182 day debt currently costs the government 4.73%. How is 4.73% “high cost” relative to the 8.375% being paid on this new bond? Even the most expensive short term domestic debt is less

than 8.375%. Somebody needs to go back to maths class in school" said Mr Ling-Stuckey.

"The coupon interest rate on 10 years US Government bonds is currently 2.88% - nearly a full 6 per cent lower than the PNG sovereign bond. Both bonds are for 10 years and will be repaid in US dollars (so having the same foreign exchange risk for investors). The difference of 6% for every year for 10 years means the total risk component of this loan is US300 million – or K1 billion (so 6% times 10 years times \$USD500 million at 0.30 exchange rate). This extraordinary amount of extra cost has two parts. The first part is the negotiation incompetence of the national government led by its Treasurer. We cannot be sure how much extra he has paid given the 600% over-subscription – let's say about a third at K350 million. The second component is the risk that investors think PNG won't repay its loans in 10 years time. One would have hoped that with PNG's strong repayment record and the strength of our exports and future potential over the next ten years that this risk would be much lower than K650 million. Why is this risk so high? Is it because PNG is regarded as a "junk bond" country by international rating agencies such as Moodys and S&P with ratings going backwards under Abel as Treasurer?" asked the Shadow Treasurer.

In a previous release, I indicated that even a nominal interest rate of 8 per cent would be too expensive, and the Treasurer has failed to deliver even an 8% outcome. On top of the 8.375% figure, there will be fees to pay – probably of around 1% - and a much more unknown foreign exchange risk. Using an independent source covering a long period, the Fitch ratings agency expects the Kina to depreciate against the US dollar by 3 per cent per annum. This is consistent with economic theory that the inflation rate in PNG is about 3% higher than in the US, so a depreciation is required each year just to stay competitive. On top of that, most commentators consider the Kina is currently over-valued at least until 2020. Overall, a more accurate figure for the true interest rate is likely to be over 15%. The true pain!

The Sovereign Bond has proven to be a good deal for foreign financiers. The 600% over-subscription confirms this. Most of the expensive bond will be used to pay off cheaper domestic debt. The likely interest cost will be over 15% after allowing for fees and foreign exchange losses. Better concessional loan sources were available if the right economic policies were in place. The Treasurer has done a bad deal for PNG and badly needs advice. The alternative government has the experience, initiative and credibility to help restructure the government and restructure its policies" said Mr Ling-Stuckey.

Hon.Ian Ling-Stuckey,CMG.MP
Shadow Minister for Treasury & Finance

30 September 2018

Treasurer Abel's statement boasting about the over-subscription, and the false claim re "high cost short term domestic debt".

INDEPENDENT STATE OF PAPUA NEW GUINEA

PRESS RELEASE FOR IMMEDIATE RELEASE

THE INDEPENDENT STATE OF PAPUA NEW GUINEA PRICES INAUGURAL 10 YEAR USD500 MILLION BOND, OVERSUBSCRIBED BY OVER 600 PERCENT

Port Moresby, September 28, 2018 – Papua New Guinea has raised a total of US \$500 million in a ten year inaugural sovereign bond issuance which concluded on Friday September 28, 2018.

Deputy Prime Minister and Treasurer, Hon. Charles Abel MP, has welcomed the successful outcome of the Bond issue that will be used to retire high cost short term domestic debt, convert short term debt to longer term, bring in foreign exchange and fund expenditure per the 2018 budget.

"The 10 year bond raised US\$500 million at 8.375%," the Deputy Prime Minister announced."

"The outstanding result was assisted by very strong international investor interest for this first time issuance, with hard offers in excess of US\$3.3 billion from 129 international banks and funds from Asia, Europe and the United States."

"The bond was priced at 8.375%, which was much better than expectations and is testament to the quality of the investor accounts."

"The result is also recognition of the investor support given to Papua New Guinea's credit story that has come from credible financial and economic management."



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Treasury Bills Auction Results

WEEK ENDING	14th Sept,2018						
AUCTION NUMBER	TB18/09/2-14						
AUCTION DATE	12th Sept 2018						
AMOUNT OFFERED ON AUCTION	K262.640 "MILLION"						

Terms	28	63	91	182	273	364	TOTAL
Weighted Average Yields of successful bids (%)	0.00	0.00	0.00	4.73	6.76	8.06	
Amount on offer Kina Million	0.000	0.000	0.000	20.640	100.000	142.000	262.640
Bids Received Kina Million	0.000	0.000	0.000	114.250	20.280	55.170	189.700
Successful Bids Kina Million	0.000	0.000	0.000	114.250	20.280	55.170	189.700
Overall Auction UNDER-SUBSCRIBED by	K0.000	K0.000	K0.000	K93.610	K79.720	K86.830	K72.940

<https://www.bankpng.gov.pg/financial-markets/domestic-money-and-bond-market-operations-and-development/treasury-bills/bills-weekly-auction-results/>

DEPUTY PRIME MINISTER, HON. CHARLES ABEL MP: SOVEREIGN BOND UPDATE

by PM_Admin | Sep 13, 2018 | Main, Media Releases, News | 0 comments



The Deputy PM and Treasurer, Charles Abel returned to Port Moresby today after leading the international roadshow to market PNGs inaugural (first ever) sovereign bond. The DPM and delegation covered Singapore, Hong Kong, London, New York, Boston and Los Angeles in 10 days. In a packed schedule arranged by global lead coordinator Credit Suisse and joint bookrunners Citibank the delegation presented to around 100 global banks and fund managers at 7 meetings per city.

"Our international partners have done a fantastic job in arranging meeting and providing advice. The interest has been really good with full meetings including all the major players. Everyone is interested in the PNG story. The market for emerging market or frontier market bonds has been rattled recently by the Turkey and Argentina economic problems but we believe PNG has a strong case regardless.

We are looking at a 5 year or 10 year benchmark minimum issue of USD500m. This is the minimum amount to qualify for the Emerging Market Bond Index and facilitate participation in the secondary market after issuance. Now that the roadshow is concluded we will field offers for amounts and pricing (interest rates) before making a final decision to sell the bonds. Of the potential proceeds, \$200m will go into operation and capital costs and \$300m will convert short term (less than 12 months) domestic debt into long term debt. This will better balance our loan book and bring in foreign exchange. PNG will be looking to establish its brand and yield curve in the international market for the future," said the DPM.

<http://www.pm.gov.pg/deputy-prime-minister-hon-charles-abel-mp-sovereign-bond-update/>

Debt-saddled Mongolia agrees \$5.5 bn IMF bailout



AFP February 20, 2017



Heavily dependent on copper exports, Mongolia's economy grew by 1.0 percent in 2016 (AFP Photo/MARK RALSTON)

Mongolia has reached an agreement with the International Monetary Fund on a \$5.5 billion bailout package, officials announced, as the debt-wracked country tries to stabilise its economy.

The landlocked north Asian nation has been hit hard by a more than 50 percent fall over the past five years in the price of copper, its main export.

Billions of dollars' worth of natural resources lie buried beneath Mongolia's sprawling steppes, but development has been delayed for years and slowing growth in its biggest customer China has hobbled the economy.

Mongolia's economy grew 1.0 percent in 2016, while its budget deficit exploded to 3.7 trillion tugrik (\$1.5 billion) according to its national statistics office.

The rescue package will include a \$440 million loan over the next three years, Koshiy Mathai, the IMF's Asia-Pacific deputy division chief, said in a statement issued Sunday.

The Asian Development Bank, World Bank, Japan and Korea are expected to provide another \$3 billion in support, while the People's Bank of China will extend its 15 billion yuan (\$2.2 billion) swap line for another three years.

The bailout package is intended to "restore economic stability and debt sustainability as well as to create the conditions for strong, sustainable, and inclusive growth, while protecting the most vulnerable citizens", Mathai said.

It will help the cash-strapped country make a \$580 million bond payment due in March.

The loan is subject to approval by the IMF's executive board, which is expected to consider it in March.

"Fiscal consolidation is a key priority, as loose fiscal policy in the past was a major driver of Mongolia's current economic difficulties and high debt," Mathai added.

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