JANUARY 2025

BSP TREASURY & MARKETS MONTHLY MARKET PULSE

GLOBAL MARKETS

In 2024, US equities rose 25%, emerging markets gained 8.1%, and Japan performed well. Europe underperformed, and high yield bonds outperformed, while government bonds struggled. French political turmoil widened debt spreads.

COMMODITIES

Commodity markets were mixed in December, with coffee, cocoa, and natural gas rising due to supply concerns and cold weather. Precious metals and industrial metals declined, while crude oil traded in narrow ranges ahead of a delayed OPEC+ meeting.

FX MARKETS

In December 2024, FX turnover hit a record K5.5 billion, driven by end-of-year conversions from mining companies. Despite a reduction in BPNG's auction offering, demand remained strong, with outstanding orders cleared and new orders increasing.

MONEY MARKETS

Interest rates have likely peaked, with December's external funding helping the government repay its TAF and leave K1.0 billion for 2024 expenses. As funds are disbursed, market liquidity is expected to rise, easing financial sector tightness.

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GLOBAL MARKETS

Strong Year for Risk Assets in 2024

2024 was a strong year for risk assets, with developed market equities up 19.2%, driven by US growth. Emerging markets also performed well, with Chinese, Indian, and Taiwanese equities rising 8.1%. US mega-cap tech stocks led global growth stocks, while expectations for deregulation boosted global value stocks, which gained 12.3%. Commodities were held back by weak Chinese demand (5.4%), but gold surged 27.1%. Central banks began normalizing policy, while rising yields led to -1.7% returns for global investment-grade bonds.

US Economic Strength

US economic exceptionalism remained intact in 2024, with GDP growth averaging 2.6%. The S&P 500 delivered the strongest returns among global equity markets, up 25%. While AI-driven stocks led, broader economic momentum contributed to a broadening of earnings expectations that should continue into 2025.

European Weakness and Underperformance

Europe's economic performance weakened in 2024, particularly in manufacturing, hurt by high energy costs and lack of export demand. Political instability, especially in France and Germany, also weighed on markets. European equities lagged, returning just 8.1%, underperforming most other regions.

UK Economic Recovery

UK equities rose 9.5%, supported by a recovery and post-election optimism. However, larger-than-expected tax hikes in the autumn budget dampened sentiment and hurt business confidence.

Mixed Performance in Asia

China's economic challenges led to weak activity, but policy changes in September sparked a 19.8% rally in Chinese equities. Japan's recovery and reforms drove a 20.5% return, making it the second-best equity market.

Strong High Yield Bond Performance

High yield bonds were the top-performing fixed-income sector for the fourth year, up over 8%. European government bonds outperformed US Treasuries, which posted modest returns of 0.6%. Longer-duration bonds struggled due to rising yields.

Central Banks and Bond Market Outlook

Central banks began normalizing policy, but rate cuts were slower than expected. Global government bonds fell -3.1%, with UK Gilts and Japanese bonds underperforming. European bonds, especially Italian debt, performed better, with Italian bonds up 5.3%.

Political Turmoil in France

Political instability in France raised concerns over the country's debt, with French bond spreads widening relative to Germany and Spain, the first such widening since the global financial crisis.

FOREIGN EXCHANGE MARKETS

FX Market Turnover

In December 2024, foreign exchange (FX) turnover surged to a record K5.5 billion, surpassing the previous high of K5.4 billion set in September. This increase was driven by a 10% annual rise in market activity, particularly in the final quarter of the year. A key factor in the spike in turnover was the typical large end-of-year foreign currency conversions by major mining and resource companies, who tend to convert significant sums to meet their operational and financial needs. During this period, the Bank of Papua New Guinea (BPNG) adopted a more relaxed approach to FX auctions, offering only US$64 million in December, a sharp decline from the US$186 million offered the previous month. Despite the lower auction volume, the market saw a clearance of outstanding orders by the end of the month, followed by a gradual uptick in new FX orders, signaling continued demand for foreign currency as the year drew to a close.

PNG Kina Performance

The PNG Kina (PGK) ended the year at 0.2500 against the US dollar, reflecting an annual decline of 183 basis points or 6.82%. In December, the PGK/USD exchange rate fell by 17 points, maintaining an average weekly decline of 4 points.

AUD/USD Movement

The Australian dollar (AUD) experienced a significant drop in December, reaching two-year lows against the US dollar. This decline was driven by a combination of factors, including a shift in the US Federal Reserve's interest rate outlook and disappointing economic data both from the US and from Australia's major trading partner, China. The Federal Reserve's signals regarding future interest rate cuts dampened investor expectations, leading to a stronger US dollar and a weaker AUD. Additionally, the Caixin Manufacturing PMI survey showed that China's manufacturing sector slowed more than expected in December, which added downward pressure to the yuan and, by extension, affected other currencies tied to global trade, including the Australian dollar. Furthermore, Australia's domestic manufacturing sector showed signs of further contraction, with the latest data pointing to a worsening downturn. These factors combined to fuel the AUD's decline, pushing it to its lowest levels in two years and prompting markets to reassess their outlook for the Australian economy.

Australian Dollar Outlook

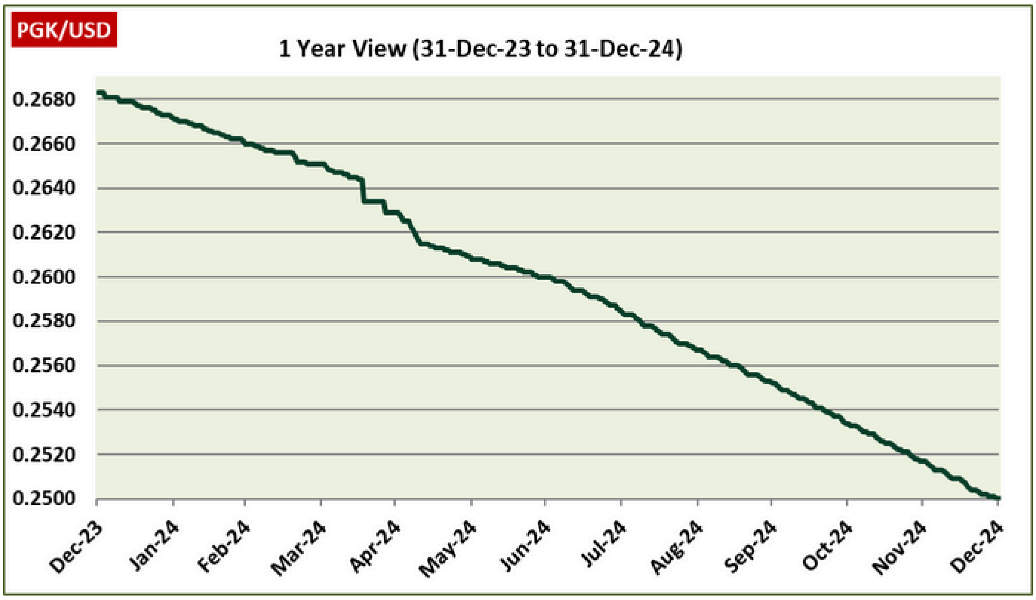
The Australian dollar fell around 9% in 2024, primarily due to the Reserve Bank of Australia's dovish stance in response to economic concerns. Market expectations now indicate a quarter-point rate cut in April, with some predicting a move as early as February.

PGK/AUD Exchange Rate

The PGK gained 4% against the Australian dollar in December, benefiting from the AUD's decline against the USD. The exchange rate started the month at 0.3864 and ended significantly stronger at 0.4022.

FOREIGN EXCHANGE MARKETS

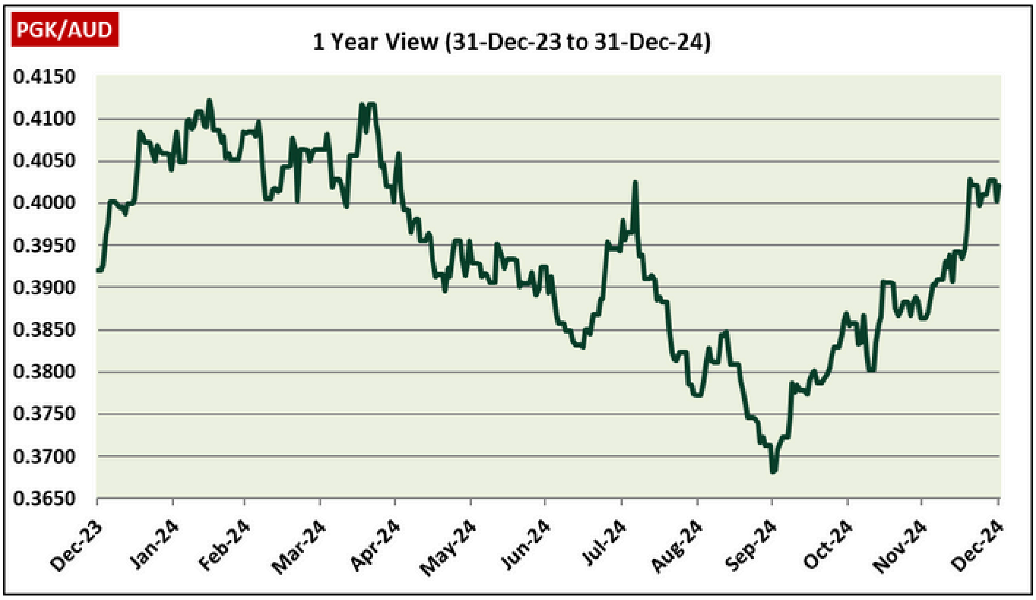
PGK/USD



PGK/USD

The PGK ended the year at 0.2500 against the US dollar, down 6.82% annually. In December, the PGK/USD rate dropped 17 points, with an average weekly decline of 4 points.

PGK/AUD



PGK/AUD

The PGK rose 4% against the Australian dollar in December, from 0.3864 to 0.4022, due to the AUD's decline against the USD. Risks for the AUD remain tied to fluctuations in iron ore and coal demand, as well as ongoing capital outflows to the US.

MONEY MARKETS

Interest Rates and External Funding

Interest rates in the domestic market have likely peaked, following a period of tightening. This shift in the interest rate environment coincided with the receipt of significant external funding in late December. The government received financial support from the International Monetary Fund (IMF), the Asian Development Bank (ADB), and the Australian government, which helped bolster its fiscal position. The infusion of these funds provided a crucial boost to the country's financial stability as it entered the final quarter of 2024.

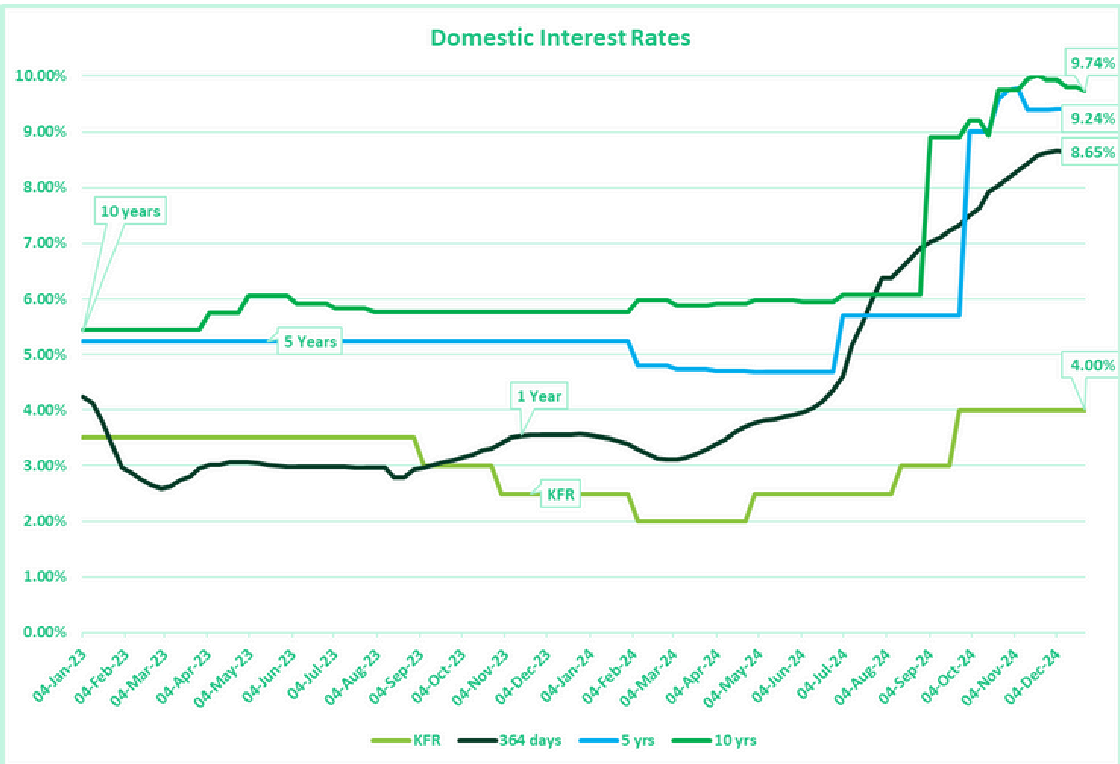
Government's Debt Repayment and Liquidity Outlook

Following the receipt of external assistance, the government used part of these funds to repay its Temporary Advance Facility (TAF) with the Bank of Papua New Guinea (BPNG). After settling the TAF, the government is expected to have approximately K1.0 billion remaining, which will be used to cover any outstanding expenses from the 2024 budget. This leftover amount ensures that the government has sufficient liquidity to address any short-term funding gaps as the fiscal year concludes.

Market Liquidity Expectations

As the government begins to disburse these funds, market liquidity is expected to increase in the coming weeks. The injection of capital into the economy will likely drive higher spending, particularly on projects and budgeted commitments that were delayed or postponed earlier in the year. This increase in government expenditure should help stimulate economic activity, leading to a more liquid market environment and potentially easing some of the tightness that had characterized the financial sector earlier in 2024.

Auction	Central Bank Bills					Treasury Bills			GIS	
Date	7	14	28	63	91	182	273	364	5 year	10 year
Previous	4.00		4.13			-	6.44	8.62	9.40	9.94
04-Dec-24	4.00						6.47	8.65	9.41	9.94
11-Dec-24	4.00					-	6.47	8.64	-	9.80
18-Dec-24	4.00					5.72	6.43	8.65	-	9.80
24-Dec-25	4.00					5.72	-	8.65	9.24	9.74
				-	-					
Movement	0.00	0.00	0.00	0.00	0.00	0.00	-0.01	0.03	-0.16	-0.20



COMMODITIES

December 2024 Commodity Price Recap

Commodity markets showed mixed trends in December. Coffee, cocoa, and natural gas continued their upward momentum, while precious metals, industrial metals, and grains saw declines. Cocoa remained strong due to ongoing production challenges in West Africa, while Arabica coffee surged over 33%, reaching a 47-year high amid concerns over Brazil's 2025 crop. Natural gas prices spiked, driven by colder-than-expected weather in the US and Europe, increasing demand. Conversely, precious metals, led by silver, fell as investors took profits following a strong 2024, compounded by a stronger US dollar and expectations of slower interest rate cuts. Industrial metals also weakened, while crude oil traded in narrow ranges ahead of a delayed OPEC+ meeting.

Market Background

December saw a continuation of key economic and political developments. The US presidential election led to a victory for Donald Trump, raising concerns about potential trade wars and fiscal strain from proposed policies, including tax cuts and infrastructure spending. Geopolitical tensions remained high, particularly with Russia, while the US dollar strengthened for the second consecutive month, closing at its strongest level in over two years according to the Bloomberg Dollar Index.

Natural Gas, Cocoa, and Coffee Surge

In the energy sector, natural gas prices hit fresh one-year highs due to higher power demand from colder weather and concerns about Russian gas flows to Europe. Cocoa extended its rally, up 240% for the year, driven by ongoing production issues in West Africa. Arabica coffee also surged, climbing 33% on fears regarding Brazil's 2025 crop, marking a 47-year high.

Precious Metals See Profit-Taking

Precious metals, especially silver, experienced declines as investors took profits following a stellar year. A stronger US dollar and robust economic data led to profit-taking, though the long-term outlook for gold remains positive, driven by global uncertainties, demand for safe-haven assets, and potential inflation risks linked to Trump's tariff policies.

Industrial Metals Mixed

Industrial metals showed mixed results, overall trending lower due to concerns over potential tariffs, particularly on Chinese imports. Copper fell over 5% amid worries about a slowdown in the energy transition and uncertainties around the Inflation Reduction Act (IRA). However, demand for copper, driven by electrification and the growth of EVs and energy industries in the US and China, is expected to rise in the longer term.

Crude Oil Stagnates

Crude oil markets remained relatively quiet in December, with WTI and Brent trading within their narrowest ranges since May. Prices were supported by rising refinery margins and ongoing geopolitical tensions, particularly the Russia–Ukraine conflict. However, concerns about oversupply in 2025, including potential OPEC+ production increases and robust output from non-OPEC countries, capped prices. Geopolitical risks, such as new sanctions on Iran and Venezuela, remained potential upside risks, though natural gas appeared to present a more significant opportunity due to rising global demand.

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