

INDEPENDENT STATE OF PAPUA NEW GUINEA

2008

SUPPLEMENTARY BUDGET SPEECH

DELIVERED BY

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Minister for Treasury and Finance

On the occasion of the presentation of the 2008 Supplementary Budget

Tuesday 23rd September 2008



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**2008 Supplementary Budget Speech
“Enhancing Growth”**

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INTRODUCTION

Mr. Speaker and Honourable Members of Parliament, I am very pleased and honoured to present to this House the 2008 Supplementary Budget.

This is a record fourth successive supplementary budget for Papua New Guinea and is my second as Minister for Treasury and Finance.

Mr. Speaker, the Government is committed to improving service delivery to our people. The supplementary budget presents yet another opportunity to achieve this. However, the Government remains mindful of the significant domestic and international economic challenges the country faces.

Mr. Speaker, in order to move the country towards a better future, the Government has adopted the new Medium Term Fiscal Strategy (MTFS) 2008-2012, which is guided by very important principles for allocating additional mineral revenue.

Mr. Speaker, it is appropriate that prudent fiscal management is based in the context of the prevailing economic environment, hence I would like to discuss the state of the economy before going on to outlining the main themes and initiatives of the 2008 Supplementary Budget.

THE 2008 STATE OF THE ECONOMY

Mr. Speaker, the economy is in its sixth successive year of growth.

The 2008 Mid Year Economic and Fiscal Outlook (MYEFO) Report revised the expected economic growth in 2008 up to 7.3 per cent from 6.6 per cent forecast in the 2008 Budget.

This revision was due to higher than projected growth in the communication and agricultural sectors, as well as a broad based increase in economic activity in other non-mining sectors. The mining and quarrying sector is also expected to expand, largely due to higher production from Ok Tedi.

Given the positive outlook for economic growth in 2008, the Government is using the 2008 Supplementary Budget to invest in infrastructure, pay down debt and improve service delivery.

Going forward, the economy is facing significant domestic and international economic challenges, including a heightened inflationary environment, an extremely uncertain international economic environment, falling and volatile commodity prices from very high levels and a significant appreciation in the exchange rate.

In light of this uncertain economic outlook, the Government is developing the 2009 Budget responsibly in order to promote macroeconomic stability and prudent fiscal management. A detailed rundown on economic developments and the outlook will be provided in the 2009 Budget in mid November this year.

THE GOVERNMENT'S FISCAL POSITION

Mr Speaker, there has been a significant improvement to the Government's fiscal and debt position due to good fiscal and macroeconomic management. The budget has been in surplus in recent years, which provided opportunity for the Government's total debt to be reduced to 34.1 per cent of GDP in 2007, and is moving towards a sustainable path in the medium term.

Beginning in 2008, the Government's expenditure decisions will be guided by the principles of the MTFS 2008-2012. As a starting point, a 70:30 rule will apply in the

allocation of windfall revenue: 70 per cent will be used to pre-fund future one-off additional public investments and 30 per cent to be used for public debt repayment.

Consistent with this Strategy, the Government will be maintaining recurrent expenditure at sustainable levels and the windfall revenue to be used to provide for the benefits of the future generation by comparing against competing investment proposals and on funding one-off infrastructure and repaying public debt with some consideration on the impact this will have on inflation.

Mr. Speaker, political stability and the Government's commitment to prudent fiscal policy and debt reduction including opening up of key economic sectors for competition will also continue to play a key role in increasing confidence among our international partners and domestic private sector businesses.

Mr. Speaker, the impact of this has been very positive for Papua New Guinea. The reduction of public debt will continue to increase macroeconomic stability and investor confidence, and will help to reduce interest rates, which in turn will cause reduction on the Government's interest expense on loans. This will free up more funds to be used on MTDS priorities.

Expected Fiscal Developments in 2008

Mr. Speaker, I would now like to report on the Government's expected fiscal performance for 2008.

Revenue Estimates

Mr. Speaker, the 2008 MYEFO forecast that there would be K1,414.6 million additional funds available in 2008 from the 2008 Budget forecast released in November last year.

The bulk of this, about K1.1 billion, was mainly due to an upward revision to Mining and Petroleum Taxes (MPT) due to higher commodity prices (especially the doubling of oil prices) since the 2008 Budget. The remainder was due to higher economic growth and inflation.

However, since the MYEFO estimates were published, there have been a number of significant developments affecting the revenue available for allocation in the 2008 Supplementary Budget. These developments include large falls in both the price and production of our major export commodities, particularly oil, coupled with the appreciation of the Kina against the US dollar, lower MPT arrears collection and lower dividend payment from Ok Tedi.

These developments have resulted in the amount of additional funds available for allocation in the 2008 Supplementary Budget being revised downward to K850 million.

Allocating Additional Revenue

Mr. Speaker, in order to derive optimum returns from our scarce resources, we have considered and taken into account the following factors in formulating the 2008 Supplementary Budget:

- the potential threat and uncertainty which remains in the revenue forecasts over the rest of 2008 due to the commodity price falls experienced over recent weeks, which may continue;
- the need to continue with prudent fiscal management and budget discipline;
- the large amounts already appropriated for spending in 2008 and all the funds that are currently available to be spent in trust funds because of the significant lead time it takes to prepare and implement quality spending plans including capacity constraints;
- the economy running at full capacity and any additional fiscal stimulus to the economy needs to be undertaken in ways that will minimise the impact on domestic demand, inflation and therefore interest rates;
- equity considerations for future generations as well as the entire population because most of the additional revenue to be allocated is derived from the sale of non-renewable natural resources of PNG for which they are equally entitled to benefit from; and

- the need to strike a good balance in relation to the great development needs in PNG, combined with the need to improve service delivery right across the country, weighted against the desire to reduce Government debt to a more sustainable level, together with addressing other Government liabilities that are growing more strongly.

Mr. Speaker, the Government’s consideration of these factors in the 2008 Supplementary Budget is important in ensuring that the extra revenues are used productively. The Budget also aims to further strengthen the Government’s overall financial position and address both the pressing development needs of the country and to reduce the Government’s public debt and other liabilities.

THE 2008 SUPPLEMENTARY BUDGET

Mr. Speaker, the 2008 Supplementary Budget allocates K850 million in four key areas:

1. Public Debt and Other Liabilities	K285.0 million
2. Transport Infrastructure (roads, airports, wharves and jetties)	K250.5 million
3. NEC Approved Expenditures	K127.4 million
4. Other Spending Priorities	K187.1 million

Mr. Speaker, I now turn to the details of the 2008 Supplementary Budget.

Repayment of Public Debt and Other Liabilities

Mr. Speaker, in a high inflationary environment, the new MTF5 calls for more than 30% of the additional mineral revenue to be allocated to the repayment of public debt and other liabilities. As a consequence of the fiscal discipline shown by the Government, PNG’s public debt level has halved when expressed as a percentage of GDP over the last five years, falling to 34.1 per cent at the end of 2007. The Government’s strong fiscal position this year provides a further opportunity to reduce these obligations even further, hence K285 million is allocated for this purpose in the 2008 Supplementary Budget.

Mr. Speaker, the Government is also mindful that the unfunded superannuation liability has increased sharply over 2007 and 2008 as super funds have experienced extraordinary returns including significant new numbers of Government employees that are entitled to receive superannuation contributions paid for by the Government have come to light.

While the Departments of Treasury and Finance are working with Nambawan Super to determine better estimates of the Government's unfunded superannuation liability, the quantum could be roughly around 12% of GDP. The Government's persistent endeavours to repay its debt and other liabilities has and will continue to result in significant benefits such as improving investor confidence, interest savings and reduced exchange rate risks. This has and will continue to free up resources to allocate to other priority expenditure areas on a recurrent basis. The repayment of public debt and other liabilities is the most prudent fiscal policy approach the Government could take in the current circumstances of strong economic growth and high inflation.

Reducing the Government's Liabilities with Nambawan Superfund

Mr. Speaker, the State has previously allocated K400 million to reduce its unfunded superannuation liabilities with Nambawan Super. However, Nambawan Super has earned an extraordinary high rate of return on its invested funds in 2007 and looks likely to enjoy another very high return in 2008. Nevertheless, the Government's unfunded liability owed to Nambawan Super is now well over K400 million less than what it would have been if these funds had not been repaid.

Funds repaid to Nambawan Super provide more funds for investment in PNG by Nambawan Super. While this helps to strengthen private sector investment in the economy, the Government also needs to be mindful of demand management within the economy, with the economy growing strongly and inflation being too high. Balancing both the high rates of return recently experienced by Nambawan Super and demand management issues, K40 million is allocated to Nambawan Super in the 2008 Supplementary Budget.

Outstanding MOA Commitments

Mr. Speaker, the State is required to honour its commitments to the resource project provinces. The 2008 Supplementary Budget provides a real opportunity to the Government to honour these commitments especially leading up to developing the PNG LNG Project for which PNG is expected realise huge revenue flows for years to come.

To honour some of these commitments, K195 million is allocated in the 2008 Supplementary Budget. Of the K195 million, K100 million is for Southern Highlands Province and K60 million for Gulf Province. K20 million is allocated for outstanding commitments endorsed by the Expenditure Implementation Committee, K10 million for the Gobe-Samberigi Road and K2.5 million each for Hela and Jiwaka.

Repayment of Public Debt

Mr. Speaker, with K195 million allocated to outstanding MOA commitments, and K40 million for the repayment of unfunded superannuation liabilities to Nambawan Super out of a minimum of K285 million allocated to debt and liability repayment, the balance of K50 million is allocated for public debt repayment in the 2008 Supplementary Budget.

Pre-funding of Public Investment Programs

Mr. Speaker, with K285 million allocated to debt and liability repayment, K565 million remains to be allocated in this supplementary budget.

The major emphasis for funding in this supplementary budget is placed on funding maintenance and construction of transport infrastructure including roads, bridges, wharves, jetties and airports. This is consistent with the National Transport Development Plan (2006 – 2010) and the Government's broader Medium Term Development Strategy (2005 – 2010).

Funding for Transport Infrastructure Development

Mr. Speaker, the amount of funding made available for transport infrastructure development in this supplementary budget is considered after taking into account the substantial funds that are already available in trust, and in recurrent and development budgets.

In this context, the 2008 Budget appropriation of K195.6 million for National Infrastructure Development Program (NIDP) is reallocated for maintenance and rehabilitation of five of the 16 highest priority roads under the National Transport Development Plan (2006 – 2010) separately. An amount of K82.6 million is allocated for funding the maintenance of the Highlands Highway, while the remaining K113 million has been distributed to fund the other four very high priority road projects. The Sepik Highway is allocated with K53 million while Koroba-Kopiago-Mendi Road, Buluminsky Highway, and New Britain Highway are allocated K20 million each. All of this represents new funding available for roads.

Mr. Speaker, the 2008 Supplementary Budget will part fund the remaining 11 of the 16 priority road projects that are identified in the National Transport Development Plan and some other major roads that are also in great need. It is envisaged that additional funding for national priority roads will be considered in the 2009 Budget. Hence, K90 million is provided in this supplementary budget for the following roads:

1. Porgera-Togoba Road	K 20 million
2. West Coast Road	K 10 million
3. Baiyer Road	K 10 million
4. Hiritano Highway	K 10 million
5. Coastal Highway	K 10 million
6. Kokoda Road	K 5 million
7. Wau Highway	K 5 million
8. Buka Highway	K 5 million
9. Magi Highway	K 5 million
10. Ramu Highway	K 5 million
11. Northern Highway	K 5 million

In addition to funding of these roads, the 2008 Supplementary Budget further allocates K64 million or K4 million to each of the following 16 rural town roads:

1. Ialibu-Pangia Road	K4.0 million
2. Mt Hagen Road	K4.0 million
3. Wabag Road	K4.0 million
4. Minj Road	K4.0 million
5. Madang Road	K4.0 million
6. Lumi Road	K4.0 million
7. Wau-Bulolo Road	K4.0 million
8. Bogia Road	K4.0 million
9. Korere Road	K4.0 million
10. Vanimo Road	K4.0 million
11. South Coast Road	K4.0 million
12. Kompiam Road	K4.0 million
13. East Sepik Rural Roads	K4.0 million
14. Angoram Road	K4.0 million
15. Agaun Road	K4.0 million
16. Kelerakwa Road	K4.0 million

Mr. Speaker, apart from funding construction and maintenance of road infrastructures, this supplementary budget also allocates K96.5 million to fund the following sea and air transport infrastructures:

1. Existing Lae port	K21.5 million
2. Other ports, wharves, jetties	K20.0 million
3. Airport upgrades	K20.0 million
4. National and Rural Bridges	K35.0 million

Funding of NEC Approved Expenditures

Mr. Speaker, I reiterate that the Government will not allocate additional mineral revenues to fund ongoing expenditures, simply because they are not sustainable in the absence of a commodity price boom. It is appropriate instead to have ongoing expenditures screened properly, scrutinised and considered in the context of the 2009 Budget, which will be handed down in November.

The following NEC approvals totalling K127.4 million granted earlier this year are funded in this supplementary budget:

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| 1. Pre-fund on-lending to Air Niugini for purchase of a new aircraft. | K 70.0 million |
| 2. National Television Service set-up by National Broadcasting Commission, for equipment & installation costs for 6 sites under phase 1 of the project. | K 12.0 million |
| 3. Outstanding land settlements. | K 12.0 million |
| 4. Set up of the Office of Climate Change. | K 3.8 million |
| 5. Payment of housing allowance for Attorney General's staff. | K 2.6 million |
| 6. Funding for the Commission of Inquiry into Finance. | K10.0 million |
| 7. Outstanding National Disaster Office verified liabilities for Oro Disaster. | K 6.5 million |
| 8. Feasibility studies for a road from Kisenepou in the Southern Highlands Province to Toweï in the Gulf Province, linking the current construction of Gobe-Samberigi road. | K 5.0 million |
| 9. National Planning Technical Advisory Team | K5.0 million |
| 10. Bouganville Office | K0.5 million |

Other Spending Priorities

Mr. Speaker, a total of K167.1 million is allocated on other spending priorities in the 2008 Supplementary Budget in the following manner:

1. National Border Authority	K40.0 million
2. Construction of 4 regional provincial treasury offices and other District Administration Offices to complete the district treasury roll out program	K26.0 million
3. Outstanding liabilities for Yomoki Ltd of K1.3 million and New Guinea Fisheries of K80, 000 for food supplies	K1.38 million
4. Refurbishment and maintenance of the air-conditioning system and acquisition and installation of new generator set for the National Museum	K1.4 million
5. Outstanding liabilities for the 2008 LLG elections and the 2007 National Elections National Elections	K12.9 million
6. Land acquisitions by the State - for State schools	K 1.74 million
7. Government Funding for Integrated Financial Management System	K 5.85 million
8. Replenishment of the Secretary's advance	K12.63 million
9. PNG National Games	K 2.3 million
10. Church Run Hospital Partnership (PPP)	K14 million
11. Additional funding for Government House	K1.6 million
12. Additional funding for National Parliament	K6.0 million
13. Public Accounts Committee	K1.3 million
14. Mirigini House Renovation	K3.0 million
15. Prime Minister's overseas and domestic commitments	K5.0 million
16. Court Orders	K20.0 million
17. PNG Canberra Office – Purchase of Residence	K12.0 million
18. Public Service Housing	K 10.0 million
19. Waigani Office Re-development	K 10,0 million

CONCLUSION

Mr. Speaker, let me conclude by emphasising the key messages.

The economy continues to grow strongly and the Government's fiscal position has improved significantly. This creates yet another opportunity for the Government to improve the lives of our people. To achieve this, the Government is doing the sensible thing by making sure that extra funds are spent in an effective and fiscally sustainable manner for the benefit of the entire population. However, we need to ensure that the expenditure allocations in this supplementary budget do not add to further inflationary pressures in the currently high inflationary environment. We have also sought to insulate the recurrent budget from the effects of any possible downturn in international commodity prices, as we have seen recently for our major export commodities.

Mr. Speaker, the 2008 Supplementary Budget is set within the Government's medium term strategies, which serve as the basis for allocating more funds to the development priorities of the Government. Consistent with this, additional funding is provided in this supplementary budget for Public Investment Programs, in particular the provision of transport infrastructure projects. This is in addition to the significant funding already provided in the previous budgets for this purpose. This clearly demonstrates the Somare-Temu Government's commitment to develop and improve the infrastructure needs of our people. We now need to see our Government departments and agencies follow through with appropriate spending plans and effective implementation of the projects.

Mr. Speaker, it is with great pleasure that I commend the Appropriation Bill for the 2008 Supplementary Budget to the House.