



THE INDEPENDENT STATE OF PAPUA NEW GUINEA

**2011
SUPPLEMENTARY NATIONAL BUDGET SPEECH**

“Sharing the benefits of economic growth with our people”

DELIVERED BY

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**On the Occasion of the Presentation of the 2011 Supplementary National
Budget to National Parliament**

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Hon. Don Polye, MP
Minister for Treasury and Finance

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1. INTRODUCTION

Mr. Speaker,

It is a great honour for me to present to this honourable House, the O'Neill-Namah Government's first Budget, the 2011 Supplementary National Budget.

Mr Speaker, the 2011 Mid Year Economic and Fiscal Outlook Report estimated a budget surplus of K606.8 million for 2011. The surplus reflects two factors. Firstly, higher than expected tax revenue largely due to higher Personal Income Tax resulting from stronger employment and wages growth in the economy. Secondly, higher than expected Mining and Petroleum Taxes flowing on from stronger commodity prices compared to the 2011 Budget assumptions and slightly higher taxes on international trade.

Further, due to the technical delays in the implementation of certain projects under the 2011 Development Budget, a total of K116 million has been identified for re-appropriation under the 2011 Supplementary Budget.

Mr Speaker, after years of non payment of dividends, finally Independent Public Business Corporation (IPBC) will be paying a dividend of K27 million to the State. This is supported by another dividend payment of K22 million from the Bank of Papua New Guinea. Mr Speaker, a further K10 million identified as excess revenue from the Work Permit Trust Account will be flowing in to support this Supplementary Budget.

Hence, Mr Speaker, there is potentially the capacity for additional spending of a total of K781.8 million. This allows this Government to fund a number of its key expenditure priorities, including tuition free education up to grade 10 and 75 percent tuition subsidy for grades 11 and 12, improving public infrastructure and roads, improving health services for our people, and improving law and order. Funds have also been allocated to a number of high priority expenditure pressures neglected by the previous Government, including funding for the 2015 Pacific Games, funding to support the PNG LNG project, and the costs of a major court case lost by the previous Government.

Mr. Speaker, unlike the previous Government, the O'Neill-Namah Government won't just talk about transforming the rural economy, it will deliver improvements in the rural economy by ensuring funding is allocated to the right areas, by being transparent and accountable in the expenditure of public funds, and by weeding out corruption in the system. Providing funding alone is not enough - it is just as critical to implement projects properly and ensure services are delivered on the ground. With this sentiment in mind, the theme for this Supplementary Budget is **“sharing the benefits of economic growth with our people”**.

Mr Speaker, this is a Supplementary Budget of hope.

This is a Supplementary Budget for the future families of Papua New Guinea.

This is a Supplementary Budget for our children.

This is a Supplementary Budget that says thank you to the people of Papua New Guinea who have worked hard for so long without partaking in the benefits of the much trumpeted economic growth and prosperity.

Importantly, Mr Speaker, the Supplementary Budget is prudent and responsible Budget. It will maintain a balanced budget position so all our development partners in all sectors of the economy can be confident of a stable investment climate.

Mr Speaker, the 2011 Supplementary Budget reverse declines under the previous Government in the proportion of funding allocated to the key Medium Term Development Plan (MTDP) sectors of education, health, transport infrastructure, and law and order. Adequate funding of these key MTDP sectors is critical to future development of our nation, and to sharing the benefits of economic growth and prosperity among our people.

Mr Speaker, let me first provide a brief update on the State of the Economy and then discuss the details of the 2011 Supplementary Budget.

2. STATE OF THE ECONOMY

Mr. Speaker, the 2011 Supplementary Budget is being delivered in the midst of an uncertain global economy and a strong and vibrant domestic economy.

Mr Speaker, the Papua New Guinea economy is expected to grow by a very strong 9.3 per cent in 2011, significantly higher than the 2011 Budget forecast of 8 per cent. This is driven by higher levels of economic activity in the non-mining sector and the construction sector of the PNG LNG project. If this expectation eventuates, the economic output in Papua New Guinea will have expanded for more than a decade, representing the longest period of uninterrupted economic growth in our country's history.

Mr Speaker, the prices of Papua New Guinea's major export commodities continued to climb, following strong demand from emerging and developing economies and supply shocks. The prices of Papua New Guinea's major mineral exports of gold, copper and oil have risen above the 2011 Budget forecasts, and are expected to remain at elevated levels through the remainder of 2011. As a result, the oil price assumption used to prepare the Mid Year Economic and Fiscal Outlook report rose by over 20 per cent, and the gold and copper price assumptions rose by around 25 per cent, compared to the price assumptions used in the 2011 Budget. This has resulted in higher than projected Government mineral revenue in 2011.

Mr Speaker, economic overheating is now a concern in Papua New Guinea. Annual inflation is now forecast to be 9 per cent in 2011, an upward revision to 2011 Budget forecast of 8.2 per cent. This is largely due to the high level of economic growth, a continuing shortage of skilled labour and land which pushes up wages and rental prices, and higher food and fuel prices from high global demand. Furthermore, there is a concern that official inflation figures are under-estimating the true extent of inflationary pressures in the economy.

Mr. Speaker, in summary the domestic economic outlook is positive but not without risks. The risks include volatile and falling commodity prices from the projected high levels, negative domestic factors like landowner issues, bad weather, mine disruptions and a heightened inflationary environment.

On the global front, although the global economic recovery is expected to continue in the remainder of 2011, significant downside risks remain. These include European sovereign debt concerns, fiscal and financial imbalances in other advanced economies and the effect of the Japanese earthquake and Tsunami on industrial production. Emerging and developing economies are growing strongly, although economic overheating is increasingly a concern.

Considering these risks, the Government is mindful of the need to promote macroeconomic stability and to provide prudent fiscal management. The 2011 Supplementary Budget has been structured with these objectives in mind.

Mr. Speaker, I will now discuss the 2011 Supplementary Budget Strategy in detail.

3. SUPPLEMENTARY BUDGET STRATEGY

Mr Speaker, the 2011 Supplementary Budget is framed against the Government's medium term policy framework. This includes the Medium Term Fiscal Strategy, the Medium Term Debt Strategy, the Fiscal Responsibility Act 2006 and the Medium Term Development Plan or MTDP. These frameworks support economic and fiscal stability in Papua New Guinea, which are essential ingredients for employment growth and economic development.

Mr. Speaker, consistent with the Government's policy frameworks and the 2011 Budget Strategy, the 2011 Supplementary Budget will be a balanced budget. Proposed expenditure is equal to projected revenue. This is a responsible Budget, which takes into consideration the high level of activity in the domestic economy, capacity constraints in the private sector and the risks evident with commodity prices being very volatile.

Mr Speaker, with strong growth in the domestic economy and investment, inflation has gained momentum. The economy is facing significant capacity constraints, particularly in accessing skilled labour. In this environment, additional Government spending risks driving inflation up further without adding to the overall level of economic activity or development. To avoid very high rates of inflation, coordinated and better management of fiscal and monetary policies are necessary. In this regard, allocating funds to areas that will not add further fiscal stimulus immediately is considered most appropriate at this time.

Mr Speaker, in this regard, the 2011 Supplementary Budget will use trust accounts to pre-fund critical development expenditure programs outlined in the MTDP such as Education, Health, Infrastructure and Law and order, and other commitments such as the 2015 Pacific Games. Major development expenditure programs include the National Health Plan and the Tuition Free Education Policy. Therefore, providing some funding upfront in the supplementary budget will ease pressure on forward years' budgets, in particular, the 2012 National Budget.

4. REVENUE

Mr. Speaker, I will first outline the revenue projections for the 2011 Supplementary Budget.

Total Revenue and Grants for 2011 are now estimated at K9,935 million, which is K606.8 million higher than the 2011 Budget estimate. This reflects an upward revision to Tax Revenue of K498.1 million and an upward revision to Non-Tax Revenue of K108.7 million since the 2011 Budget.

Mr Speaker, the upward revision to Tax revenue in 2011 by K498.1 million primarily reflects higher receipts of Personal Income Taxes and Mining and Petroleum Taxes. This reflects higher employment and wages, and stronger commodity prices in international markets.

Mr Speaker, Non-Tax revenue collections are projected to be higher than the 2011 Budget estimate by K108.7 million, due to higher Mining and Petroleum Dividend income. This reflects higher mineral prices and an expected one-off dividend from a major project.

Mr Speaker, IPBC have not paid consistent dividends under the former Government. For this reason, the profits of State Owned Enterprises were not shared consistently with our people. I am happy to announce that IPBC will be paying a dividend of K27 million to be shared with our people.

The Bank of Papua New Guinea has also put its hand up to provide a further K22 million in dividends to support key programs under the Supplementary Budget.

Mr Speaker, excess revenues sitting idle in the Work Permit Trust Account of the amount of K10 million have also been identified to support critical programs under this Supplementary Budget.

5. REAPPROPRIATIONS

Mr Speaker, a further K116 million has been identified for re-appropriation from the 2011 Development Budget. Due to the technical delays in the implementation of these projects, these amounts have been identified for reappropriation to other critical areas. The K116 million has been taken from the following projects;

- National ID Cards K30 million;
- Cuban Doctors (MDG 4 & 5 special intervention) K25 million;
- Economic Corridor (PRAEC) K17 million;
- PR for Promotion of Government's Policy Initiatives K15 million;

- NHC – Housing Development Program K15 million;
- Public Sector Housing K10 million; and
- Pacific Medical Centre K4 million.

Mr Speaker, if these funds are not used by the end of the year, they will lapse in accordance with the requirements of the Public Finances (Management) Act, hence it is only prudent to reallocate these funds to areas that are in critical need.

6. EXPENDITURE

Mr. Speaker, I would now like to discuss the 2011 Supplementary Budget expenditure priorities.

Mr Speaker, priority has been given to aligning Recurrent and Development Budget funding with the MTDP enablers, including:

- Unlocking land for economic development;
- Establishing quality national transport corridors that connect rural populations to markets and services;
- Higher and technical education to redress the severe skills shortage within PNG's labour force;
- Universal access to quality primary and secondary education;
- The provision of key utilities of electricity, clean water and sanitation and communications;
- Improving health outcomes; and
- Improving law and order.

Mr Speaker, the MTDP was designed to refocus Government priorities from those contained in the 2006-2010 Medium Term Development Strategy (MTDS). Under this plan, there was a steady decline in the share of the Development Budget going to the key MTDP enablers such as Education (Primary, Secondary and Higher), Health, Land, Infrastructure (Transport and Utilities) and Law and Justice and Transport. It is critical that this Government ensures the funding for key MTDP

enablers do not decline further but increase over the medium term. The 2011 Supplementary Budget will begin to reverse this trend.

Mr Speaker, while additional funds have been identified, the outstanding expenditure pressures far exceed the resource envelope identified. Major expenditure pressures are the development priorities outlined in the MTDP, including tuition free education, the National Health Plan and transport infrastructure. Expenditure pressures also include critical commitments which were not funded by the previous Government, such as the 2015 Pacific Games, commitments to support the PNG LNG project, and outstanding court settlements. It is impossible to fund all known expenditure pressures without running a very high budget deficit which would be damaging and imprudent.

Hence, Mr Speaker, the Government has had to make some difficult but right choices, and have given priority in this Supplementary Budget to key MTDP development priorities, in particular, tuition free education, and other critical programs.

7. 2011 SUPPLEMENTARY NATIONAL BUDGET ALLOCATIONS

Mr Speaker, I now turn to the details of the Supplementary Budget. The K781.8 million of expenditure in the Supplementary Budget is allocated to the following areas:

- Education K305 million;
- Health K109.5 million;
- Infrastructure K230.8 million;
- Law and Order K20 million;
- Agriculture Sector K22 million; and
- Other Contractual Obligations K94.5 million

Education

Mr Speaker, the current Government has prioritized Education as the key to a sustained and inclusive economic growth and development for Papua New Guinea. The private sector is desperately short of skilled workers, while at the same time so many Papua New Guineans look for work. Education is critical if we are to develop a well trained and highly skilled workforce to meet the needs of the modern economy, and so that more Papua New Guineans can enjoy the benefits of employment. Education is critical to giving the opportunity to ordinary Papua New Guineans to participate in the modern economy.

In the 2011 Supplementary Budget, the Government has allocated a total of K305 million to this sector. The K305 million is comprised of K300 million to pre-fund Tuition Free Education and K5 million for the University of Papua New Guinea. The K5 million allocated to the University of Papua New Guinea includes K2 million for rehabilitation of the Michael Somare Library, K2 million for the computer laboratory and K1 million for electronic research facilities or e-library.

Mr Speaker, the total funding for tuition free education is estimated at K970 million in 2012. This amount includes tuition free and subsidies for 2013 that need to be prefunded in 2012. Of the K970 million, the 2011 Supplementary Budget will prefund K300 million for the tuition free education for 2012 to ensure that funds are available on 1 January 2012, so that money can be paid to schools before the commencement of the school year. Such action will reduce the total funding for 2012 to K670 million. This will facilitate the smooth rollout of the tuition free education policy.

Mr Speaker, the K970 million is only for tuition free education (including boarding fees) from elementary to grade 10 and 75 percent tuition subsidies for Grades 11 and 12 and vocational education. However, it does not include the cost for additional teachers and related infrastructure such as classrooms and teacher housing.

Health

Mr Speaker, the level and quality of rural health services have diminished over the term of the last Government as a result of lack of maintenance of health infrastructure, particularly the aid posts, due to a lack of adequate funding and the remoteness of our rural communities. At present, the rural health service is either completely non-existent or, for the lucky few, some services are provided by Non-Government Organizations, such as the church. There is a significant need to address this issue as majority of the population of Papua New Guinea live in the rural communities, and commuting to major centres for health services often adds enormous hardship to our rural population. This is consistent with the goal of the National Health Development Plan which aims to strengthen primary health care and improve service delivery to the rural majority and urban disadvantaged.

To address this issue, the 2011 Supplementary Budget allocates K109.5 million to the Health Sector. This is comprise of K72 million for District Rural Health Centres, K21 million for provincial hospital maintenance and equipment and K10 million for the State-Church health partnership.

Mr Speaker, to complement allocations to rural health services, the balance of K6.5 million is allocated to Port Moresby General Hospital for medical equipment to improve the health service provided to the growing urban population in the nation's capital.

Infrastructure

Mr Speaker, while significant amounts of funds have been allocated to improving transport infrastructure across the country, a lot remains to be done. The increased domestic economic activity and insufficient public investment is resulting in capacity limitations in critical infrastructure, particularly at entry points such as airports and wharves. The 2011 Supplementary Budget proposes to provide an additional K230.8 million to infrastructure, including its commitment to the Infrastructure pertaining to the 2015 Pacific Games and to undertake extension and maintenance work on the National Parliament House.

The K230.8 million is comprised of:

- Rural District Roads K72 million;
- Provincial Roads K50 million;
- Port Moresby Roads K30 million;
- Nat. Parliament Extension & Maint. K25 million;
- Pacific Games K20 million;
- ADB Loan (1709) Counterpart funding K15 million;
- Goilala Highway K6 million;
- Malalaua – Kaintiba Highway K6 million;
- Nadzab Airport Road Maintenance K5 million; and
- Papua New Guinea Air Service Ltd K1.8 million;

Mr Speaker, the allocation of K72 million in the 2011 Supplementary Budget for Rural District Roads shows the O'Neill-Namah Government is committed to improving service delivery to the 80 percent of the people of Papua New Guinea who live in the districts and rural areas.

Mr Speaker, with the spinoff effects of high economic activities from the LNG and high agriculture commodity prices, many provincial economies are also booming. To support and facilitate economic activity in the provinces, the Government has allocated K50 million for the provincial roads and an additional K30 million to Port Moresby Roads. The K30 million to Port Moresby roads is in addition to the K70 million previously allocated in the 2010 Supplementary Budget to ease the traffic congestion currently being experienced in the nation's capital.

Mr Speaker, the ADB Loan (1709) Counterpart funding for Highlands Highway was under appropriated in the 2011 Budget, as a result road projects under this facility are at serious risk of discontinuation in 2011, unless the counterpart funding is made available. Given the importance of these road projects, the Government is allocating K15 million in the Supplementary budget to address this shortfall in the 2011 Budget.

Mr Speaker, K6 million each has been allocated to Goilala Highway for maintenance and upgrade and a feasibility study for the Malalaua-Kantiba Highway, respectively.

An amount of K1.8 million is allocated to Papua New Guinea Air Services Limited (PNGASL) to support the air transport sector to expand services to areas not serviced by larger airlines. With the massive increase in flying activity (both planes and helicopters), not only in the petroleum and mineral areas but throughout Papua New Guinea, there is an urgent need for PNGASL to increase its capacity to provide the travelling public with a safe and efficient communication and air navigation services. This funding will support PNGASL's efforts to upgrade air traffic management system and new investment in reliable communication that is critical to aviation safety.

Mr Speaker, Papua New Guinea has been nominated to host the 2015 Pacific Games. The total cost of preparation and hosting the game is estimated at K1.2 billion. Unfortunately, the previous Government has failed to fund a single toea towards the Pacific Games, and time is fast running out to complete the required construction and refurbishment. To ensure the cost of the games remains affordable, the focus will be on upgrading existing facilities instead of building a new stadium. The games will include new accommodation built around tertiary institutions such as the University of Papua New Guinea, which will leave a legacy to our tertiary education institutions after the games. Hence to commence preparations and to ease pressure on future budgets, K20 million has been allocated to the 2015 Pacific Games.

Mr Speaker, K25 million has been provided to National Parliament. Of this K25 million, K15 million is for the maintenance of this honourable house and to expand the facilities to cater for additional members of Parliament given the two new provinces and new seats for women and the balance of K10 million for the shortfall in the recurrent appropriation for National Parliament in 2011.

Law and Order

Mr Speaker, the Law and Justice Sector is one of the 7 enablers under the MTDP. The O'Neill-Namah Government is committed to improving law and order to ensure a safe and just society. A total of K20 million been allocated to Law and Order sector. The K20 million is for maintaining institutional houses of the disciplinary forces, mainly the Police, Defence and the CIS. Gordons Police Barracks has been allocated K10 million while Defence Barracks and CIS Barracks have each been given K5 million for maintenance.

Agriculture Sector

Mr Speaker, this Government recognizes the importance of agriculture sector and its significant role in a sustained and inclusive economic growth and development for Papua New Guinea, particularly in rural population. The majority of our rural population are subsistence farmers, whose livelihood depend heavily on agriculture for food and income generation. This Government recognizes that in order to address some of Papua New Guinea's poor socioeconomic indicators, it should allocate adequate funding for agriculture, and for this reason, it is allocating a total of K22 million in the 2011 Supplementary Budget to address some the challenges that are being faced in this sector.

The K22 million is allocated to:

- Agricultural Initiatives K10 million;
- Air Freight subsidy support for agric. Produce K 5 million;
- Counterpart funding for small agric development program K3 million; and
- NARI Drought preparedness program K4 million.

Contractual Obligations & Other Commitments

Mr Speaker, the 2011 Supplementary Budget allocates K94.5 million for other contractual obligations and commitments, most of which are outstanding and cannot

be avoided. Allocating funds to clear these obligations now will free up resources in the future to be allocated to other priority areas.

Mr Speaker, the K94.5 million includes:

- Ministerial PNG LNG Commitments K40 million;
- Coastal Vessels Program K17 million;
- Autonomous Bougainville Government K15 million;
- District Markets Program K8.5 million;
- Outstanding legal settlement – Downer K5 million;
- Petroleum MOAs Review K5 million;
- Financial Audit & Legal Advice K2 million; and
- Air Services Investigation K2 million.

Mr Speaker, PNG LNG related commitments arising from the UBSA, LBBSA and relevant NEC decisions amount to just over K3 billion. The Government has commenced paying some of these commitments in the 2010 Supplementary Budget and the 2011 National Budget, but more needs to be done. Of those amounts that have been funded, some amounts have been reallocated by the Department of National Planning and Monitoring (including the feasibility studies, business development grants and infrastructure development grants). The K120 million appropriated in 2011 for Infrastructure Development Grant is yet to be released to the Trust Account. This is because the guidelines for the use of these funds are yet to be completed.

Mr Speaker, this Government is committed to see the PNG LNG Project proceed smoothly. Hence the 2011 Supplementary Budget allocates K40 million to Ministerial Commitments made as part of the Umbrella Benefit Sharing Agreement.

Mr Speaker, of the amounts allocated to LNG commitments already, the Government will ensure they are applied as intended and agreed following proper procedures as set out in the Public Finances (Management) Act and the various agreements.

Mr Speaker, the coastal vessel program is an important modality of transportation for marine or coastal region of Papua New Guinea, particularly for remote and isolated islands. The Government recognizes that its fair share of rural community live in these remote regions and therefore bringing essential services to them and/or providing access to market is crucial to improving their livelihood hence a total of K17 million has been allocated to this program.

Mr Speaker, the K15 million allocated to Autonomous Bougainville Government is to honor Government's commitment to the Autonomous Bougainville Government's peace and restoration program. It is a development grant to ABG which is part of the Peace Agreement. The previous Government neglected to fund this commitment, in the 2011 Budget. However, the new Government will honour this commitment by providing funding in the 2011 Supplementary Budget.

Mr Speaker, this Government recognizes the importance and benefits for the rural population to fully participate in economic activities which is crucial to sustained income generation vital to poverty alleviation and improved living standards, hence a provision of K8.5 million for district markets is made in the Supplementary Budget through the district market program.

Mr Speaker, while significant funds have been allocated and paid to beneficiaries of Petroleum Memoranda of Agreements (MoAs), there are some who still claim to be legitimate stakeholders and have not received any payments. A total of K5 million is allocated to review MOAs in relation to Kutubu, Gobe and Moran Projects and establish whether all legitimate beneficiaries have been covered.

Mr Speaker, A total of K103.4 million has been paid in outstanding legal costs owing to Downer Construction. However, K11.2 million was retained as tax components by the Internal Revenue Commission (IRC) and therefore Downer Construction has again billed the State for this shortfall. K10.7 million was paid recently and the current K5 million allocated under the 2011 Supplementary Budget is to cater for the balance including the tax components and exchange rate differences.

Mr Speaker, this Government is about transparency and accountability hence, K2 million each have been allocated to financial audit and legal advice and air service investigation into recent misapplication of funds.

8. CONCLUSION

Mr. Speaker, in conclusion, the 2011 Supplementary Budget is being delivered amid strong economic growth with inflationary pressures high. However, critical development needs remain, and rather than being reactive, the O'Neill-Namah Government is responding proactively to fund the highest priority areas.

Mr Speaker, the 2011 Supplementary Budget is fiscally responsible. It is focused on the policy-priorities of the nation as reflected in the MTDP. Spending is being shifted to important policy-driven development priority areas to invest in the development of our nation, and to share the benefits and opportunities of economic growth with ordinary Papua New Guineans, our people.

Mr Speaker, I commend the 2011 Supplementary Budget to the Honourable Members and the people of Papua New Guinea.