



INDEPENDENT STATE OF PAPUA NEW GUINEA

2009 BUDGET SPEECH

***“Promoting Sustained Economic Growth by
Empowering and Transforming the Rural
Economy”***

DELIVERED BY

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**On the occasion of the presentation of the
2009 National Budget**

Tuesday 18th November 2008



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INTRODUCTION

Mr. Speaker, I move that the Bill be read a second time.

It is a great honour for me to present to the Parliament the Government's 2009 National Budget. This is the Government's second budget since it was returned in the 2007 National Elections and the seventh successive budget under the Somare Government.

Mr Speaker, the 2009 Budget is being delivered amid very uncertain economic circumstances. The world has experienced the most severe financial crisis since the 1930's Great Depression. Across the world, major financial institutions have failed and stock markets have fallen dramatically. The global financial crisis is affecting economic growth prospects in both advanced and developing countries.

The extent of this crisis and the effects of the global downturn cannot be underestimated. Some of the largest and most developed economies have been affected – in the United States, in the United Kingdom, in Western Europe and in Australia.

Papua New Guinea is not immune from the fallout, with the commodity prices we receive for our exports and the fiscal outlook having deteriorated rapidly in recent months.

Given these developments, the Government is using the 2009 Budget to **promote sustained economic growth and to further empower and transform the rural economy.**

Mr Speaker, before I outline the state of the economy and the contents of the 2009 Budget, I would like to make some overarching points about the approach the Government has taken to framing this Budget.

Firstly, the Government's recently released *Medium-Term Fiscal Strategy 2008-12* provides a stable, responsible and prudent framework for the Government to ensure fiscal sustainability and promote macroeconomic stability over the medium term. The Government recognizes the importance of the Medium Term Fiscal Strategy in establishing and maintaining the country's economic credibility in the eyes of donors and the international and domestic communities in an uncertain economic environment.

Secondly, and with respect to the Government's strong programs and expenditure plans in 2009, the Government has sought to align planned expenditures with forecast revenues while continuing to pursue its ambitious development priorities for the nation.

Thirdly, in an uncertain economic environment the Government is mindful that commodity prices could continue to fall. In the short term, the Government will consider the ramifications if the revenue does not materialize in 2009 in order to avoid spending money that has not actually been received. Longer term, the Government seeks to use the 2009 Budget to insulate the economy from the current uncertainties and threats present in the global economy.

Mr Speaker, in summary, the Government's clear priority is to promote sustainable economic growth through empowering and transforming the rural economy. As a result, the Government has used the 2009 Budget to:

- Significantly expand the District Services Improvement Program in 2009, with planned funding being in addition to the substantial funding per district previously allocated in 2008.
- Undertake substantial investments in agriculture, infrastructure maintenance, improvement and development, in accordance with the Government's strategic plans and other priorities.

Mr. Speaker, I will now discuss the state of the economy and the contents of the 2009 Budget.

STATE OF THE ECONOMY

Mr Speaker, the global financial crisis has led to a significant deterioration of the global economic environment. The disruption of the credit markets, and subsequent collapse of global equity prices have damaged economic growth prospects across the world, with the US, Japan, European and some Asian economies either verging on, or entering recession. Significantly, the Chinese and Indian economies have also begun to slow considerably.

This slowdown has significantly reduced the prices for PNG's export commodities, with the prices of oil and copper falling by more than 50 per cent since the very high prices recorded in July 2008. This will have a major impact on the export values of PNG's commodities and our trade position. As a consequence, no

Additional Mineral Revenue collections are expected in 2009. The large falls in commodity prices have been accompanied by a significant increase in volatility, making it exceptionally difficult to estimate what commodity prices are likely to be in 2009, and increasing the uncertainty and risks around the revenue projections.

Mr Speaker, despite the deterioration in global economic conditions, growth prospects for the PNG economy remain favorable, with broad based growth expected to continue in 2009, albeit at more moderate rates than those recorded in 2007 and expected in 2008. As a result, non-mineral revenues are expected to continue to grow solidly in 2009.

In 2009, the real GDP growth is expected to be 6.2 per cent. This represents some moderation from the exceptionally high growth rates in 2007 and 2008 but if achieved, would represent a very high rate of growth on an international comparison basis. It reflects further expansion in the mobile phone sector, but at a slower pace; as well as a slow down – albeit at very high levels – of growth in construction activity, which is running up against capacity constraints, reducing the scope for further expansion in the industry. It also reflects two opposing trends in the mining and petroleum sectors, where a large fall in oil production due to the decline of existing oil fields, is expected to be offset by strong growth in the mining sector where a number of new mines are scheduled to commence production.

While the domestic economy is not expected to be significantly affected by the global downturn, there is a distinct risk that business and consumer confidence could weaken, which could reduce private sector activity. Combined with the effect of falls in commodity prices (both mineral and agricultural) and asset prices, this presents a major downside risk to the economic outlook.

The Agriculture, Forestry and Fisheries sector is expected to grow by a solid 4 per cent in 2009. The major driver of this growth is copra and copra oil, where increased production in Bougainville, an expansion in the number of export licenses and the revitalization of plantations is expected to provide a significant boost. Coffee, cocoa and palm oil are also expected to grow strongly.

The Petroleum sector is expected to decline by 7.3 per cent in 2009, as production from existing fields continues to decline as they continue to mature. The Mining and Quarrying sector is expected to grow significantly by 17.5 per cent. The expected increase is due to increased production levels in the major mines of Ok Tedi, Porgera and Lihir, as well as the progression of newer mines, such as Hidden Valley, Simberi and Sinivit into the production and ramp up phase.

In the non-mineral sector, the communication and construction sectors are expected to be the major drivers of growth. While the expansion in the mobile phone sector is expected to slow somewhat from the exceptional rates of growth experienced in 2007 and 2008, the subscriber base is still expected to increase, as the two operators expand operations throughout the country.

The construction sector is expected to continue to grow strongly due to increased donor funds and government spending through the District Services Improvement Program (DSIP) for rehabilitation and maintenance. Also, construction is supported by increased private sector investment including new projects in the construction phase like Ramu Nickel. The combination of low interest rates and strong domestic demand is also being translated into several new residential and commercial building projects.

Mr. Speaker, underlying this still strong but more moderate growth for 2009 is the assumption of continued fiscal discipline, political stability and prudent macroeconomic policies. However, there are also a number of risks, including further volatility and declines in commodity prices associated with deteriorating world economic growth prospects, unforeseen shutdowns in the mineral sector, the spread of the financial crisis into the PNG financial system, and the impact of large exchange rate fluctuations.

Inflation is expected to slow from the worryingly high rate of 10.6 per cent forecast for 2008 to 6.1 per cent in 2009. This is almost entirely due to a reduction of external inflationary pressures, due to the falls in world food and energy prices and the sharp appreciation of the Kina in the second half of 2008. The very volatile exchange rate environment presents significant risks for the competitiveness of our export and import competing sectors and has implications for inflation, depending on movements in the Kina against other major currencies.

We know that very strong domestic inflationary pressures still exist in the economy, with the strong and continued private sector expansion that is anticipated, relatively loose monetary conditions, increased Government expenditure and increased wage pressures. These will need to be monitored carefully, as the reduced inflationary pressures from the external side may only be temporary.

REVENUE IN 2009

Mr. Speaker, let me outline the revenue projections for 2009 which are contained in this Budget.

Revenue collections in 2009 are expected to be substantially lower than in the previous two years, because of lower mineral revenues and a fall in the Kina value of grants due to the appreciation of the Kina, particularly against the Australian dollar. Nonetheless, non-mineral revenue collections are expected to grow solidly in 2009 in-line with robust economic activity in the non-mineral sectors.

Total Revenue and Grants for 2009 is estimated at K6,666.4 million, substantially lower than estimated revenue and grants of K7,780.4 million in 2008. This is a downward revision from the 2009 BSP estimate of K7,341 million, mainly due to the decline in Mining and Petroleum Taxes and Dividend Withholding Taxes, as well as a fall in the Kina value of grants due to the sharp appreciation of the exchange rate.

Total revenue is projected to be K5,652.1 million in 2009, substantially lower than the expected 2008 collection of K6,595.5 million. This reflects a very large decline in mineral revenues due to lower commodity prices, the higher exchange rate and lower oil production, partly offset by increased non-mineral revenue collections attributed to higher wages, strong employment growth and larger profits.

Non-tax revenue is projected to rise due to the injection of K600.0 million of funds from the Gas Commercialization Equity Financing Trust Account.

Higher interest receipts are also expected from the large amounts of funds held in trust accounts. At the same time, the Departments of Treasury and Finance will be seeking more favorable interest rates on these funds.

Project grants are expected to be K974.3 million in 2009, lower than the 2009 Budget Strategy Paper estimate of K1,111.2 million. This downward revision reflects the significant appreciation of the Kina and lower infrastructure tax credits. This brings the 2009 Total Revenue and Grants estimate to K6,666.4 million.

BUDGET STRATEGY FOR 2009

Mr. Speaker, the 2009 Budget is framed by the Government's medium-term economic and development strategies: the *Medium-Term Fiscal Strategy (MTFS) 2008-2012*, the *Medium Term Development Strategy (MTDS) 2005-2010*, and the *Medium Term Debt Strategy*.

- The MTFS identifies the fiscal envelope, defining the funding available for ongoing (recurrent and development) expenditure, and the amount of Additional Mineral Revenue. In the 2009 Budget, there is no additional mineral revenue available for allocation, so the MTFS requires that ongoing expenditure in the recurrent budget equals total revenue.
- The MTDS identifies the priority areas for Government expenditure, and sets targets for that spending as a proportion of total expenditure. In 2009, the targets are 82.7 per cent for the Development Budget, and 55.5 per cent for the total Budget.

- The Debt Strategy seeks to minimize the cost of debt consistent with the Government's tolerance for financial risk. It recommends reducing debt to sustainable levels, reducing financial risk to prudent levels and developing the Government's inscribed stock, bill and loan markets.

Mr Speaker, the most significant consideration for Government has been that unlike recent budgets, no Additional Mineral Revenues are expected in 2009, due to substantially lower commodity prices, the appreciation of the Kina and lower oil production.

In light of this outlook, the Government's total planned recurrent and development expenditure will be K6,499.7 million in 2009.

Mr Speaker, the Government will fund these planned expenditures without increasing either domestic or foreign borrowings. The Government will instead fund its planned expenditure using tax revenues and K423 million funds that were previously set aside in the Gas Commercialization Equity Financing Trust Account that are no longer required for that purpose.

Mr Speaker, as a result, I can advise the Parliament that despite great economic turmoil and uncertainty, the Government's 2009 Budget is effectively balanced.

This achievement sends a clear signal to the domestic and international community about the importance the Government places on fiscal discipline and prudence to assist in insulating the economy from the current global financial turmoil.

EXPENDITURE PRIORITIES

Mr. Speaker, I would now like to discuss the Government's planned recurrent and development expenditure priorities in 2009 – priorities that seek to promote sustained economic growth and to further empower and transform the rural economy.

Recurrent Expenditure

Mr. Speaker, the Government's planned recurrent expenditure in 2009 is K3,904.5 million. This includes major funding in the following areas:

- Increased funding to individual agencies K291.4 million
- Maintaining education subsidies K143.0 million
- One-off Government expenditures K120.0 million
- Increased funding for road maintenance and upgrades K50.0 million
- Air Niugini Capital Injection K30.0 million
- LNG Project Support funding K20.0 million
- National Television Service K7.0 million

Increased funding to individual agencies

The Government has endorsed the recommendations of the Central Agencies Coordination Committee to increase the funding provided to a number of individual agencies to meet increased personnel and operating costs. Major increases are being provided to Provincial Governments and Provincial Treasuries (K119.6 million), Hospital Management Services (K46.1 million), Education (K14.7 million), Defence (K13.6 million), Internal Revenue Commission (K10.1 million), National Parliament (K8.3 million) and Transport (K6.2 million).

Maintaining Education subsidies

The 2009 Budget provides K143 million to subsidize school fees. This initiative builds on the generous funding provided to parents by the Government in the 2007 and 2008 Budgets. The Government's decision to continue this subsidy in 2009 will directly assist parents of school aged children and in doing so, encourage better educational outcomes for the children of this nation.

One-Off Government Expenditures

The 2009 Budget is providing additional funding for a series of important one-off Government expenditures including for the Civil Aviation Authority (K33 million), Oro Restoration Authority (K20 million), assistance to Milne Bay Provincial Government and the Western Highlands Provincial Government following the destruction of Provincial offices (K13 million), a contribution to the Motu-Koita Assembly (K10 million), Madang Marine Park (K10 million), the National Gaming Control Board (K5 million), Independence Scholarships (K5 million), Free Trade Zone (K5 million), the Office of Climate Change and Carbon Trading (K5 million), the National Border Authority (K4 million), Mirigini Haus (K4 million), the Women in Parliament initiative (K2.5 million), consultancy for a Nambawan Superannuation review (K2 million), Massim Cultural Foundation (K1 million) and funding for scoping work for a possible PNG team in the Australian National Rugby League (K0.5 million).

Increased funding for road maintenance and upgrades

The Government is allocating an additional K50 million for increased maintenance to the nation's priority roads as identified in the National Transport Development Plan. This increased funding will enable the Department of Works to undertake

additional routine and specific maintenance on over half of the PNG's 4,200 kilometers of priority roads.

Air Niugini Capital Injection

The Government will provide a K30 million capital injection to Air Niugini in 2009 to assist Air Niugini meet costs associated with refueling and other operational issues.

LNG Project Support Funding

The Government will provide K20 million in 2009 to meet the operating costs of the LNG Project Support office.

Establishment and operation of the National Television Service

The 2009 Budget includes K7 million for the continued rollout and ongoing operations of the recently established National Television Service.

Development Expenditure

Mr. Speaker, total GoPNG funding of the Development Budget in 2009 will be K1,620.9 million of which K1,385.9 million is from direct Government funding, K195 million from concessional loans and a K40 million infrastructure tax credit.

In the 2009 Budget, the Government has directed and reallocated additional funds to the development budget to pursue its ambitious development priorities. In doing so, the Government is seeking to promote sustained economic growth through empowering and transforming the rural economy and provide employment opportunities for our citizens.

The Government's concerted increase in development spending is also focussed on improving our crucial infrastructure. The provision of better infrastructure will also enhance our future economic growth potential.

The K1,385.9 million domestic funding for the Development Budget comprises the 2009 Budget Strategy Paper ceiling of K524.0 million, and a series of reallocations from the recurrent budget and new spending measures:

- District Services Improvement Program K356.0 million
- Transfer of National Agriculture Development Plan funds K100.0 million
- New MOA commitments K70.0 million
- Additional Provincial and Rural roads funding K66.0 million
- Wharves and Bridges funding K60.0 million
- Waigani office redevelopment K50.0 million
- National investments K43.0 million
- ADB Highlands Region Road Improvement Investment Program K38.0 million
- Prime Minister's Community College K30.0 million
- Rabaul assistance package K25.0 million
- Provincial Impact Projects K20.0 million
- National Stadium K20.0 million

Mr Speaker, as a result of the Government's contribution to the development budget, it is a massive 163 per cent higher than it was in 2008 – this represents a real achievement given the backdrop of the international financial crisis.

District Services Improvement Program

Mr Speaker, in recent years, the Government has made a substantial investment in our districts to directly improve the provision of services to all our citizens right across PNG.

In the 2007 Supplementary Budget, the Government allocated K4 million per district, or K356 million to the District Services Program. In the 2008 Budget, the Government allocated a further K6 million per district, or K534 million in total.

This funding has been used to help improve Transport, Health, Education, Water, Law and Justice and Agriculture programs and services in each of the nation's 89 districts.

Mr Speaker, in recognition of the importance the Government places on the District Services Improvement Program, I can announce today that the Government has decided to allocate a further K4 million per district, or a further K356 million funding in 2009 to the District Services Improvement Program.

This record level of funding will directly benefit our rural citizens and assist in revitalizing the most important services in each of the nation's 89 districts.

Transfer of National Agricultural Development Plan funding

The National Agricultural Development Plan is an important tool in meeting the Government's development priorities in a very important sector of the economy and society. In recognition of the priority the Government places on empowering and transforming the rural economy, the Government has decided to transfer the

existing K100 million funding from the recurrent budget to the development budget in 2009.

Of this K100 million funding, K80 million will go to funding the National Agriculture Development Plan itself while K20 million will be made available to the National Development Bank for providing credit facility to our rural farmers.

New MOA Commitments

Mr Speaker, the Government places a high priority on honoring its MOA commitments. In addition to the substantial allocations made in the 2008 Supplementary Budget, the Government is allocating a further K70 million in 2009 to honour MOA commitments with the Southern Highlands Province (K30 million), Gulf Province (K30 million) and New Ireland Province (K10 million).

Additional Provincial and Rural Roads funding

The 2009 Budget allocates an additional K66 million funding to invest in new roads and roads maintenance and upgrades to provincial and rural roads. The Government's substantial package comprises Transgogol – Amele Road in Madang Province (K15 million), Kerema – Malalawa Road in Gulf Province (K10 million), Kokopau – Tinputz Road in Bougainville (K5 million), Tambul – Tomba Road in Western Highlands Province (K7 million), Manus Provincial Road in Manus Province (K5 million) and the Kundiawa – Karimui Road (K20 million) and Kundiawa Town Roads (K4 million) in Simbu Province.

Wharves and Bridges funding

The 2009 Budget allocates K60 million additional funding for wharves and bridges projects. This includes K10 million for the Kimbe Wharf in West New Britain Province and K50 million for upgrades and maintenance of priority bridges across the country.

Waigani office redevelopment

The Government is allocating K50 million for the Waigani office redevelopment project. This project will provide urgently needed office accommodation in the government office precinct.

National Investments

Mr Speaker, the Government is using the 2009 Budget to invest K43 million in a series of projects that will further develop this nation and enhance its productive capacity. Funding will be provided in 2009 to invest in Growth Centres (K20 million), the Central City development (K10 million), Housing development (K8 million) and the Land Development Program (K5 million).

ADB Highlands Region Road Improvement Investment Program

In recognition of the importance the Government places on upgrading and enhancing road infrastructure under the Highlands Region Road Improvement Investment Program, the 2009 Budget includes an additional K38 million roads funding which will be funded through an ADB concessional loan (K30 million) and counterpart funding (K8 million).

Prime Minister's Community College

The Government is allocating K30 million in the 2009 Budget to fund the Prime Minister's Community College, an important initiative that seeks to enhance educational outcomes in this Nation.

Rabaul Assistance Package

The 2009 Budget allocates K25 million in recognition of priority development needs in Rabaul in East New Britain Province. This will enable funding for the Palmal - Lower Warangoi Road (K20 million), upgrading of Rabaul town drainage (K3 million) and the relocation of Matupit Islanders to Putput (K2 million).

Provincial Impact Projects

The Government is allocating K20 million, or K1 million per province, to fund a range of priority Provincial Impact Projects in 2009.

National Stadium

The 2009 Budget allocates K20 million to upgrade the National Stadium in Port Moresby in recognition of the importance the Government places on this important sporting and cultural asset.

MANAGING GOVERNMENT EXPENDITURE IN UNCERTAIN TIMES

Mr Speaker, the Government is mindful that in a rapidly changing economic environment, major uncertainties exist with the 2009 Budget. While the Government has been realistic with its economic assumptions and revenue forecasts, the Government recognizes that Government expenditure will need to

be closely monitored in 2009 and, if needed, may need to be adjusted as economic circumstances dictate.

This is very important as there is no safety buffer in the 2009 Budget for the Government to access in the event of further falls in commodity prices. If commodity prices continue to fall, expenditure plans may have to be reviewed and revised in line with changing circumstances. Going forward, the Government hopes that its substantial new development expenditure will help insulate the PNG economy from the impacts of the global downturn.

Mr Speaker, it is important to note that the Government also has substantial amounts in trust funds that were saved during the commodity boom period. These funds will be spent on infrastructure development over the next few years and should also help to shield the PNG economy from some of the worst impacts of the global downturn. In addition, the LNG project has now entered the Front End Engineering and Design stage and a decision will be made towards the end of 2009 about proceeding with the project. If this project proceeds, it will provide a substantial boost to economic growth and jobs in the PNG economy over the medium term.

Mr Speaker, while there is currently a lot of gloom and doom concerning the global financial crisis, the Government has grounds to be cautiously optimistic about the outlook for PNG over the medium term.

GROWING THE ECONOMY THROUGH SUSTAINED REFORMS

Mr Speaker, the Government also realizes that the economy can be strengthened through further economic reforms to the private and public sectors.

The Government is committed to promoting a competitive and dynamic private sector, and recognizes the benefits this brings to the economy through creating employment, higher incomes and stimulating economic growth.

In 2009, the Government will pursue opportunities for structural reform that encourage investment and promote a competitive private sector.

In recent years the country has enjoyed social and economic benefits from the introduction of competition in the telecommunications sector. In economic terms alone, the expansion of mobile phone services - from both Digicel and PNG Telikom - is estimated to have contributed around two and a half percentage points to GDP growth in the last couple of years.

Given the benefits of such competition, the Government welcomes the commencement of the new code sharing arrangement between Airlines of PNG and Pacific Blue Limited. The entry of an additional airline into PNG's aviation industry will continue to promote the benefits of competition, with potential reductions in the cost of fares and increased services for international travelers. This addition is expected to produce benefits for the tourism sector and will hopefully generate additional income earning opportunities for Papua New Guineans.

The Government also remains committed to implementing existing public sector reform programs and ensuring that their progress does not stall.

CONCLUSION

Mr. Speaker, let me conclude by emphasizing to the House that the economic circumstances we face are challenging and difficult times may lie ahead.

The Government is using the 2009 Budget to shield our economy and support its citizens **by promoting sustained economic growth and further empowering and transforming the rural economy.**

The Government has revised its revenue forecasts to reflect rapidly changing economic circumstances. The Government has also sought to align planned expenditures with forecast revenues while continuing to pursue its ambitious development priorities for PNG.

These measures send a clear signal about the importance of the Medium Term Fiscal Strategy in establishing and maintaining the country's economic credibility in the eyes of donors and the international and domestic communities in an uncertain economic environment.

The Government remains optimistic that through the adoption of prudent policies that promote macroeconomic stability and fiscal sustainability, the economic future of this country can be secured and our development priorities met.

Mr. Speaker, I now commend the Bill to the House.