

CHAPTER 2. 2009 BUDGET

2.1 OVERVIEW

Over recent years, the economy has benefited from strong economic conditions. However, over the last year, the global economy has weakened and has experienced the most severe financial crisis since the 1930s Great Depression. PNG will not be immune from any major global downturn in 2009.

In order to shield the economy from the worst of the impacts of this crisis, the 2009 Budget is designed to maintain confidence by being fiscally prudent and responsible given the circumstances, while providing for increased development expenditure to help support economic growth in rural areas.

The deteriorating global outlook is expected to lower domestic economic growth from 7.2 per cent in 2008 to 6.2 per cent in 2009. The key driver of this lower forecast is the significant fall in commodity prices.

Table 12: Key Economic Assumptions 2007 – 2009

	2007 Actual	2008 Estimate	2009 Projection
Real GDP Growth	6.5	7.2	6.2
Real Non-Mining GDP Growth	7.3	7.9	5.6
Inflation (year average)	0.9	10.6	6.1
Oil Price (USD/Barrel)	72.3	102.0	55.0
Copper Price (USD/Pound)	3.2	3.2	1.5
Gold Price (USD/ounce)	697.0	863.0	600.0
Interest Rates (Treasury Bills)	5.0	6.5	7.0

Source: Department of Treasury

The weaker international economic outlook and commodity prices in 2009 will have direct impact on forecast revenue, with total revenue and grants forecast to be K6,666.4 million, an K1,114.0 million, or 14.3 per cent, reduction from the 2008 estimate. Consistent with the MTFS framework and the need to promote macroeconomic stability and fiscal sustainability in these uncertain times, the Government has lowered its expenditure and net lending to be K6,676.7 million in 2009, K1,113.2 million, or 14.3 per cent lower than forecast in 2008. As a result, the 2009 Budget is effectively balanced, with a very small deficit of K10.3 million or 0.0 per cent of GDP.

Table 13: Budget Balance 2007 - 2009 (Kina Millions)

	2007 Actual	2008 Estimate	2009 Projection	Change
Total Revenue and Grants	7028.6	7780.4	6666.4	-1114.0
Total Expenditure and Net Lending	6552.4	7789.9	6676.7	-1113.2
Budget Balance	476.2	-9.5	-10.3	-0.8
Per cent of GDP	2.5%	0.0%	0.0%	

Source: Department of Treasury

2.2 FISCAL STRATEGY

The 2009 Budget has been framed against a background of the international financial crisis and rapidly slowing world economic growth. Despite the collapse in additional mineral revenue, the budget is expected to be balanced, however, there are major uncertainties surrounding the 2009 growth forecast and commodity price assumptions.

The 2009 Budget will be guided by the medium term frameworks which include the Medium Term Development Strategy (MTDS), Medium Term Debt Strategy (Debt Strategy) and the new Medium Term Fiscal Strategy 2008-2012 (MTFS).

The 2009 Budget is the first annual budget to be delivered since the Government's endorsement of its new MTFS. The MTFS has been designed to provide a stable, responsible and prudent framework for the Government to manage its fiscal resources and promote macroeconomic stability over the medium term.

The new MTFS is detailed in Chapter 9. Importantly, the MTFS contains three key fiscal rules to ensure macroeconomic stability, and four principles to guide the use of any additional revenue. These are set out in Box 3.

Box 3: Fiscal Rules & Principles in the MTFS (2008- 2012)

The MTFS will assist the Government in achieving the National Goals in the Constitution and the objectives of the MTDS. There are three key fiscal rules:

- Keep ongoing expenditure in line with normal revenues, which is defined as all non-mineral revenues plus mineral revenue equal to 4 per cent of GDP that can be reasonably expected to be collected if commodity prices fall to long-run levels;
- Use the additional mineral revenue to pre-fund public investment projects and repay debt and other liabilities, using a 70:30 split between the two uses as a guide; and
- Limit the actual amount of public investment expenditure sourced from the additional revenues in any given year to 4 per cent of GDP, in order to promote macroeconomic stability and avoid inflationary pressures.

The strategy lays out four principles to guide the allocation of additional mineral revenues. The use of these revenues should:

- benefit future generations;
- be flexible, in case the additional revenues do not materialize;
- be made while considering the impact on domestic and import demand; and
- be compared to and assessed against all other potential investment projects.

The strategy complies with the *Fiscal Responsibility Act (2006)*, which limits the Government to keep the level of public debt below the level at the beginning of the term. This limit on borrowing does not apply to investment projects by State-Owned Enterprises (SOEs) which are supposed to fund themselves, and investment projects with funding arrangements fully independent of the State.

In light of the forecast reduction in revenue arising from lower commodity prices, there will be no Additional Mineral Revenue in 2009. The Government will instead fund its planned expenditure using tax revenue and funds that were previously set aside in the Gas Project Equity Account.

Although inflation is expected to fall in 2009 from the uncomfortably high levels experienced in 2008, there are still strong inflationary pressures coming from within the domestic economy. Inflationary risks include:

- Higher government expenditure from the 2009 Budget and the recent 2008 Supplementary Budget and draw downs from trust accounts.
- Wage outcomes not supported by productivity, including potential outcomes arising from recommendations of the Minimum Wages Board.
- Ongoing growth in money supply and credit.
- Continued expansion in the private sector due to improved business confidence, relatively low interest rates and high profitability.

The Government remains committed to pursuing its development policies and the seven priority areas identified in the Medium Term Development Strategy (MTDS). This allows clear signals to be sent to donors and the public that PNG's development should be driven according to the Government's policy framework and development strategy – in line with the Government's goal of working towards economic independence and ***"Promoting Sustained Economic Growth by Empowering and Transforming the Rural Economy"***.

The 2009 Budget will continue to ensure a substantial allocation of the Government's own resources to these development priorities. However, the 2009 Budget has not met the MTDS priority spending targets, with 48.7 per cent of GoPNG expenditure in the recurrent and development Budgets going towards the MTDS priorities, compared to the target of 55.5 per cent; and 73.6 per cent of GoPNG funded Development expenditure, compared to the target of 82.7 per cent.

The 2009 Budget is based on the existing tax structure and does not propose any new taxes or tax increases.

2.3 REVENUE AND GRANTS

Total Revenue and Grants for 2009 are projected to be K6,666.4 million. This is K1,114.0 million below the revised 2008 estimate. The major factor behind this substantial downward revision is the large decline in the prices of PNG's major export commodities, partially offset by a one-off injection of funds from the Gas Equity Trust Account.

Table 14: Revenue and Grants 2007 – 2009 (Kina Millions)

	2007 Actual	2008 Estimate	2009 Projection	Change
Tax Revenue	5854.0	6116.2	4614.3	-1501.9
Non-Tax Revenue	433.0	479.3	1037.8	558.5
Infrastructure Tax Credits	20.6	73.7	40.0	-33.7
Project Support Grants	721.0	1111.2	974.3	-136.9
Total Revenue and Grants	7028.6	7780.4	6666.4	-1114.0

Source: Department of Treasury

2.3.1 Tax Revenue

Tax revenue is projected to decrease by a substantial K1,501.9 million or 24.6 per cent to K4,614.3 million in 2009, compared with the K6,116.2 million estimated for 2008.

Table 15: Tax Revenue 2007 – 2009 (Kina Millions)

	2007 Actual	2008 Estimate	2009 Projection	Change
Taxes on Income and Profits	4491.3	4659.1	3043.9	-1615.2
Dom. Taxes on Goods & Serv	958.5	1031.7	1114.2	82.5
Taxes on International Trade	404.2	425.4	456.2	30.8
Tax Revenue	5854.0	6116.2	4614.3	-1501.9

Source: Department of Treasury

The major decline is expected from Taxes on Income and Profits which is projected to fall by K1,615.2 million or 34.7 per cent. This is partly offset by the increased revenue from Domestic Taxes on Goods and Services and Taxes on International Trade, which are expected to increase by K82.5 million or 8.0 per cent, and K30.8 million or 7.2 per cent respectively.

Table 16: Taxes on Income and Profits 2007 – 2008 (Kina Millions)

	2007 Actual	2008 Estimate	2009 Projection	Change
Personal Income Tax	1006.9	1086.2	1195.1	108.9
Company Tax	723.7	778.2	877.3	99.1
Dividend Withholding Tax	199.3	196.8	144.2	-52.6
Mining and Petroleum Tax	2333.9	2392.2	626.5	-1765.7
Interest Withholding Taxes	19.3	21.1	19.1	-2.0
Other Direct Tax	111.2	93.1	85.8	-7.3
Gaming Tax	97.0	91.6	95.9	4.3
Taxes on Income and Profits	4491.3	4659.1	3043.9	-1615.2

Source: Department of Treasury

Taxes on Income and Profits are expected to be K3,043.9 million in 2009. This is K1,615.2 million lower than the revised estimate of K4,659.1 million for 2008. The decline is reflected in Mining and Petroleum Taxes which are estimated to fall by K1,765.7 million or 73.8 per cent. This reflects the substantial decline in commodity prices and appreciation of the exchange rate.

Personal Income Tax receipts are expected to increase by K108.9 million or 10.0 per cent to K1,195.1 million in 2009 compared with the estimate of K1,086.2 million in 2008. Corporate Income Tax receipts are estimated to increase by K99.1 million or 12.7 per cent to K877.3 million in 2009, compared with K778.2 million estimated for 2008. These increases reflect expected solid domestic economic conditions in 2009, with strong profit and employment growth.

Dividend Withholding Tax collections are expected to decrease by K52.6 million or 26.7 per cent to K144.2 million from the 2008 estimate of K196.8 million. The projected decrease reflects the lower expected dividend receipts from Ok Tedi in 2009 as a higher proportion of profits are expected to be retained for capital expenditure.

Interest Withholding Tax receipts are projected to decrease by K2.0 million or 9.5 per cent to K19.1 million in 2009 compared with K21.1 million estimated in 2008.

Other Direct Tax receipts are expected to decline by K7.3 million or 7.8 per cent to K85.8 million in 2009 in line with the full year impact of cuts to stamp duties announced in the 2008 Budget, which only began in March 2008. Gaming Tax is projected to increase by K4.3 million or 4.7 per cent to K95.9 million in 2009 compared with the K91.6 million estimated in 2008.

Table 17: Domestic Taxes on Goods & Services 2007–2009 (Kina Millions)

	2007 Actual	2008 Estimate	2009 Projection	Change
Excise	342.0	370.2	407.5	37.3
GST	557.5	646.1	703.0	56.9
Mining Levy	56.6	12.0	0.0	-12.0
Other Indirect	2.4	3.3	3.7	0.4
Domestic Taxes on Gds & Serv	958.5	1031.7	1114.2	82.5

Source: Department of Treasury

Domestic Taxes on Goods and Services are expected to increase by K82.5 million or 8.0 per cent in 2009 to K1,114.2 million compared with K1,031.7 million estimated in 2008.

Domestic excise collections are expected to increase by K37.3 million or 10.1 per cent to K407.5 million in 2009 compared with the estimate of K370.2 million in 2008. The National Government's share of Goods and Services Tax (GST) is expected to increase by K56.9 million or 8.8 per cent to K703 million in 2009 compared with the estimate of K646.1 million in 2008. This is due to increased economic activity. The Mining Levy has been phased out in 2008; hence no revenue is expected in 2009.

Table 18: Taxes on International Trade 2007 – 2009 (Kina Millions)

	2007 Actual	2008 Estimate	2009 Projection	Change
Import Duty	135.9	149.9	166.3	16.4
Export Duty	155.2	152.0	152.9	0.9
Excise Duty on Imports	113.1	123.5	137.0	13.5
Taxes on International Trade	404.2	425.4	456.2	30.8

Source: Department of Treasury

Collections from Taxes on International Trade are expected to increase by K30.8 million or 7.2 per cent in 2009 to K456.2 million compared with the 2008 estimate of K425.4 million. This is due to increased economic activity.

Import Duty receipts are expected to increase by K16.4 million or 10.9 per cent to K166.3 million in 2009 compared to the 2008 estimate of K149.9 million. Export Duty on logs is projected to increase by K0.9 million or 0.6 per cent to K152.9 million in 2009 compared with the 2008 estimate of K152.0 million. Excise Duty on Imports is projected to increase by K13.5 million or 10.9 per cent to K137.0 million in 2009 compared with an estimated K123.5 million in 2008.

2.3.2 Non-Tax Revenue

Table 19: Non Tax Revenue 2007 – 2009 (Kina Millions)

	2007 Actual	2008 Estimate	2009 Projection	Change
Property Income	312.7	376.5	322.9	-53.7
<i>Non-Mining Dividends</i>	87.0	140.0	195.0	55.0
<i>Mining & Petroleum</i>	225.7	236.5	127.9	-108.7
Injection from Trust Accounts	0.0	0.0	600.0	600.0
Interest & Fees from Lending	0.5	9.0	24.0	15.0
Other Non Tax Revenue	119.8	93.7	90.9	-2.8
Non Tax Revenue	433.0	479.3	1037.8	558.5

Source: Department of Treasury

Non-Tax Revenue receipts are projected to increase by K558.5 million or 116.5 per cent in 2009 to K1037.8 million compared with an estimated K479.3 million in 2008.

The large increase in Non-Tax Revenue is due to the injection of K600.0 million of funds from the Gas Equity Trust Account. This will be used to fund one-off expenditure in 2009.

Property Income is projected to decline by K53.7 million or 14.2 per cent to K322.9 million in 2009 compared with the 2008 estimate of K376.5 million. The decline in property income is due largely to a projected reduced dividend from the State's 15 per cent interest in the Ok Tedi mine, reflecting higher retained earnings for capital expenditures expected in 2009. The projection of K127.9 million in mining dividends is expected to come from the following: OTML K117.9 million and Petromin K10.0 million. The projection of K195.0 million in non-mining dividends is based on the expected receipt of dividends in 2009 from the Bank of Papua New Guinea (K70.0 million), National Fisheries Authority (K25.0 million) and the Independent Public Business Corporation (K100.0 million).

Interest and Fees from Lending is projected to increase by K15.0 million in 2009 to K24.0 million compared with the 2008 estimate of K9.0 million. This largely reflects higher expected interest revenue from the Government's trust accounts. Other Non-Tax Revenue, reflecting revenue from departments, is projected to decline by K2.8 million to K90.9 million in 2009 from the K93.7 million estimated for 2008.

2.3.3 Infrastructure Tax Credits

Infrastructure tax credits (ITC) are expected to decline from K73.7 million in 2008 to K40.0 million in 2009. This is a reduction of K33.7 million or 45.7 per cent and reflects reduced utilization of ITC as well as lower revenues, which ITC entitlements are based on.

2.3.4 Grants

Project Support Grants for 2009 are expected to decline by K136.9 million to K974.3 million from the estimated level of K1,111.2 million in 2008. The projected decrease reflects the appreciation of the Kina against major currencies, particularly against the Australian dollar.

Table 20: Grants by Source (Kina Millions)

	2008 Estimate	2009 Projection	Change	% Change
AusAID	833.6	699.3	-134.3	-16.1
JICA	212.8	139.6	-73.2	-34.4
European Union (EU)	29.8	19.2	-10.6	-35.6
New Zealand	51.9	48.4	-3.5	-6.8
China	33.7	21.4	-12.3	-36.4
United Nations (UN)	13.6	0.0	-13.6	-100.0
Others	31.6	40.0	8.4	26.4
Total Project Grants	1207.0	967.9	-239.1	-19.8

Source: Department of National Planning and Monitoring

2.4 EXPENDITURE

Total Expenditure and Net Lending is projected to be K6,676.7 million in 2009, which is K1,113.2 million or 14.3 per cent lower than the expected 2008 Budget outcome.

The total Recurrent Budget has been increased by K265.3 million or 7.3 per cent and the Development Budget has been increased by K720.5 million or 38.4 per cent in 2009.

Table 21: Total Expenditure and Net Lending 2007 – 2009 (Kina Millions)

	2007 Actual	2008 Estimate	2009 Projection	Change
Recurrent Expenditure	3498.0	3639.3	3904.5	265.3
Development Expenditure	1327.6	1874.6	2595.2	720.5
Reappropriation into Trust Account	0.0	0.0	177.0	177.0
Additional Priority Expenditure	1726.8	2276.0	0.0	-2276.0
Total Expenditure and NL	6552.4	7789.9	6676.7	1113.2

Source: Department of Treasury

2.4.1 Additions to recurrent expenditure

The 2009 Recurrent Budget provides for major increases to various key priority areas including individual Government agencies. Major funding increases include:

Increased funding to individual agencies

Increased funding will be provided to a number of individual agencies for specific projects and to meet increased personnel and operating costs. Major increases are being provided to Provincial Governments (K119.6 million), Hospital Management Services (K46.2 million), Education (K14.7 million), Internal Revenue Commission (K10.1 million), Transport (K6.2 million), Defence (K13.6 million), and the Office of Climate Change and Carbon Trading (K5 million).

One-Off Government Expenditures

The 2009 Budget is providing an additional K58 million to fund a series of important one-off Government expenditures including a contribution to the Motu-Koita Assembly (K10 million), assistance to Milne Bay Provincial Government and the Western Highlands Provincial

Government following the destruction of Provincial offices (K13 million), Madang Marine Park (K10 million), the National Gaming Control Board (K5 million), Independence Scholarships (K5 million), Free Trade Zone (K5 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).

Funding for specific road maintenance

K50 million will be provided for maintenance of 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 4,200 kilometers of priority roads.

Air Niugini Capital Injection

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

LNG Project Support Funding

To support the LNG Project, K20 million will be provided in 2009 to meet the operating costs of the LNG Project Support office.

Establishment & operation of the National Television Service

The 2009 Budget includes K7 million in addition to the K12 million provided in the 2008 Supplementary Budget for the continued rollout and ongoing operations of the recently established National Television Service.

Other major expenditures

Other major items announced in the 2009 Budget include new funding for the Civil Aviation Authority (K33.0 million), Oro Restoration Authority (K20 million) and National Border Authority (K4.0 million).

2.4.2 Recurrent Expenditure

Total recurrent expenditures are forecast to increase by K265.2 million (7.3 per cent) to K3,904.5 million in 2009 from K3,639.3 million in 2008.

Table 22: Recurrent Expenditure 2007 – 2009 (Kina Millions)

	2007 Actual	2008 Estimate	2009 Projection	Change
Personnel Emoluments	1456.3	1546.9	1603.5	56.6
Goods and Services	1387.1	1457.2	1601.2	144.0
ABG	50.0	54.2	57.0	2.8
Transfers to Statutory Institutions	238.6	226.8	253.9	27.1
Interest Payments and Fees	370.1	358.2	392.8	34.6
Net Lending to CSAs	-4.1	-4.0	-4.0	0.0
Total Recurrent Expenditure	3498.0	3639.3	3904.5	265.2

Source: Department of Treasury

2.4.2.1 Personnel Emoluments

Personnel Emoluments comprise salaries and allowances, wages, overtime, leave fares, superannuation contributions, superannuation pay outs, and contract gratuities. Personnel Emoluments for National Departments and Provincial Government, including Teachers' Salaries

are estimated to increased by K 56.6 million or by 3.7 per cent to K1,603.5 million in 2009 compared to K1,546.9 million in 2008.

There are several factors behind the increase in personnel emoluments in 2009. These include:

- The inclusion of award increases for health workers;
- Increased Teachers' salaries following the signing of a new MOA; and
- Position upgrades and increased allowances approved by SCMC.

Table 23: Personnel Emoluments 2007 – 2009 (Kina Millions)

	2007 Actual	2008 Estimate	2009 Projection	Change
National Departments	834.7	945.4	943.7	-1.7
Provincial Governments	621.6	601.5	659.8	58.3
<i>Staffing Grants</i>	183.6	171.0	198.7	27.7
<i>Teachers Salaries</i>	438.0	430.5	461.1	30.6
Total Personnel Emoluments	1456.3	1546.9	1603.5	56.6

Source: Department of Treasury

A summary of personnel emoluments at the National and Provincial level is provided in Table 23. The significant factor behind the overall increase in personnel emoluments in 2009 relates to the K58.3 million or 9.7 per cent increase being provided to Provincial Governments.

Table 24: Personnel Emoluments by Items 2007 – 2009 (Kina Millions)

	2007 Actual	2008 Estimate	2009 Projection	Change
Salaries	603.4	702.4	715.4	13.0
<i>Salaries and Allowances</i>	536.2	613.8	624.2	10.5
<i>Wages</i>	67.2	88.6	91.2	2.6
Superannuation	125.9	136.0	110.0	-26.0
Leave Fares	37.4	44.8	45.5	0.7
Contract Gratuity	3.6	5.0	6.1	1.1
Others 1/	64.4	57.2	66.7	9.5
Total Personnel Emoluments	834.7	945.4	943.7	-1.6

Source: Department of Treasury

1/ Includes overtime and contract officers' education benefit

A summary of the components of personnel emoluments is provided in Table 24. The increase in personnel emoluments has been driven by increased salaries and allowances (K10.5 million) and wages (K2.6 million). The decline in superannuation expenditure (K26.0 million) reflects the Government's decision to fund other spending priorities in 2009. This means that the Government is unlikely to be able to fully fund its employer superannuation contribution of 8.4 per cent of salary of Government employees from 2009 onwards.

2.4.2.2 Goods and Services

Total Goods and Services expenditure in 2009 is estimated to be K1,601.2 million. This is K144.0 million or 9.9 per cent higher than the revised estimate for 2008.

Table 25: Goods and Services 2007 – 2009 (Kina Millions)

	2007 Actual	2008 Estimate	2009 Projection	Change
National Departments	1263.7	1330.4	1420.8	90.4
Provincial Governments	123.4	126.8	180.4	53.6
Total Goods and Services	1387.1	1457.2	1601.2	144.0

Source: Department of Treasury

2.4.2.2.1 Goods and Services – National Departments

Total National Departments Goods and Services funding is estimated to be K1,420.8 million in 2009, which is K90.4 million or 11.2 per cent higher than the revised estimate for 2008.

Table 26: National Departments Goods and Services 2007 – 2009 (Kina Millions)

	2007 Actual	2008 Estimate	2009 Projection	Change
General Goods and Services	1050.8	1084.1	1207.4	123.3
Education Subsidies	148.9	143.0	143.0	0.0
Other Goods and Services	64.0	103.3	70.4	-32.9
<i>Pre-March 2003 Arrears</i>	<i>1.2</i>	<i>0.0</i>	<i>0.0</i>	<i>0.0</i>
<i>Structural Adjustments Program</i>	<i>6.8</i>	<i>51.3</i>	<i>18.4</i>	<i>-32.9</i>
<i>Court Orders</i>	<i>56.0</i>	<i>52.0</i>	<i>52.0</i>	<i>0.0</i>
Total Nat Depts Goods and Serv	1263.7	1330.4	1420.8	90.4

Source: Department of Treasury

General Goods and Services expenditure by National Departments is estimated to be K1,207.4 million in 2009, an increase of K123.3 million (or 11.4 per cent) compared with the revised estimate for 2008. The net increase is mainly due to increased allocations to various Departments including National Parliament, Internal Revenue Commission, Police, Education, Hospital Management Services and Works.

Education Subsidies are estimated to remain at K143.0 million for 2009.

Other Goods and Services expenditure in 2009 is estimated at K70.4 million, K32.9 million lower than the revised estimate for 2008. This is due mainly to lower than originally planned numbers of retrenchments which has resulted in a reduced provision for retrenchments and reduced Structural Adjustment Program expenditure.

No appropriation has been made for the pre-March 2003 Arrears as this will need to be addressed by individual departments who have incurred these arrears.

The Government continues to bear financial risks from the awarding of significant damages against the State. The 2009 Budget maintains an allocation of K52.0 million for payment of court orders.

Table 27: General Goods and Services by Item 2007 – 2009 (Kina Millions)

	2007 Actual	2008 Estimate	2009 Projection	Change
Operational Materials and Supplies 1/	95.3	112.6	122.9	10.4
Utilities	104.4	134.3	130.0	-4.3
Rental of Property	97.5	115.8	123.9	8.1
Grants to Individuals and NPO	158.3	72.0	79.6	7.7
Transport and Fuel	45.3	44.0	46.2	2.3
Travel and Subsistence	41.9	47.5	44.5	-3.0
Routine Maintenance	29.4	38.1	36.8	-1.3
Purchase of Vehicles	15.6	18.3	13.1	-5.2
Membership Fees/Contributions	6.5	9.0	9.7	0.7
Other 2/	669.5	738.9	814.1	75.2
Total Nat Depts Goods and Services	1263.7	1330.3	1420.8	90.5

Source: Department of Treasury

1/ Includes other operational expenses

2/ Other includes office furniture and equipments, training, administrative consultancy fees

Table 27 summarizes movements in General Goods and Services by item. Major increases are for Office Furniture and Equipment, Training, and Administrative Consultancy fees totaling K75.2 million; Operational Materials and Supplies of K10.4 million, Grants to Individuals and Non Profit Organizations (NPO) of K7.7 million and is offset by small decreases in Routine Maintenance of K1.3 million, Travel and Subsistence of K3.0 million, Utilities of K4.3 million and the Purchase of Vehicles of K5.2 million.

2.4.2.2.2 Goods and Services – Provincial Departments

Goods and services expenditure ceilings for Provinces have been determined on the basis of new funding arrangements for sub-national governments arising from the Review of Intergovernmental Financing Arrangements (RIGFA), which were passed by Parliament in July 2008.

Under the new system, the amount of goods and services funding provided to Provincial and Local-Level Governments, other than the National Capital District and Bougainville, is set at a specified percentage of Net National Revenue (NNR). The system is based on actual revenue data from the year two years before the Budget year (second preceding year), and legislation specifies the proportion of this NNR (or NNR rate) that should be provided. Due to the phased introduction of additional funding into the system, the NNR rate will increase from 5.12 per cent in 2009 to the ongoing rate of 6.57 per cent from 2013. The total pool of funding determined by applying the NNR rate to the second preceding year's NNR is known as the Equalisation Amount.

This “share of NNR” approach ensures that as “normal” revenues rise, funding to Provincial and Local-Level Governments also rises. Conversely, if revenues fall, the grants also reduce so that the system remains affordable. These new arrangements will lead to steady increases in funding for Provinces in 2009 and into the future.

Goods and Services expenditure ceilings for individual Provinces and Local Level Governments for the 2009 Budget were determined on the basis of the fiscal needs of each sub-national government. NEFC determines fiscal need using a ‘costs minus revenues’ formula, with additional available revenue being directed to those areas where the need is the greatest.

Under the new system, Provinces will no longer receive a derivation grant. However, two new grants will be provided:

- an Agriculture Function Grant for the goods and services costs associated with agriculture and other primary production, including fisheries and forestry; and
- an Other Service Delivery Function Grant for the goods and services costs associated with administering all of the functions assigned to Provinces which are not funded by a specific service delivery function grant. These include business development, community development, natural resource management and lands administration.

Table 28: Provincial Goods and Services Grants 2007 – 2009 (Kina Millions)

	2007 Actual	2008 Estimate	2009 Projection	Change
Unconditional Grants	16.1	15.5	24.3	8.8
<i>Administrative / Block</i>	16.1	15.5	24.3	8.8
Conditional Grants	66.9	69.2	125.3	56.0
<i>Health Function</i>	13.4	14.5	28.4	13.9
<i>Education Function</i>	21.6	21.7	31.6	9.9
<i>Transport Maintenance</i>	15.4	16.7	34.0	17.3
<i>Village Court Function</i>	2.2	2.2	2.2	0.0
<i>Derivation</i>	14.3	14.1	0.0	-14.1
<i>Agriculture Function</i>	-	-	14.1	14.1
<i>Other Service Delivery</i>	-	-	14.8	14.8
Other Grants for LLGs	40.4	42.0	45.6	3.7
<i>Urban LLG/Town & Urban Services</i>	3.0	11.1	11.9	0.8
<i>Rural LLG</i>	37.4	30.9	33.7	2.8
Total Provincial Goods and Serv	123.4	126.8	180.4	53.6

Source: Department of Treasury, NEFC

2.4.2.3 Transfers to Autonomous Bougainville Government

The 2008 Budget for the Autonomous Bougainville Government (ABG) established acceptable baselines for all the grants required under the *Organic Law on Peace Building in Bougainville*. Accordingly, the 2009 Budget funding for the ABG has been determined by indexing the 2008 grants as per the requirements of the Organic Law.

Table 29: Transfers to Bougainville 2007 – 2009 (Kina Millions)

	2007 Actual	2008 Estimate	2009 Projection	Change
Police Grant	2.1	2.2	2.3	0.1
Recurrent Grant	47.9	51.8	54.4	2.6
Conditional Grant	0.0	0.3	0.3	0.0
Total Recurrent Grant	50.0	54.2	57.0	2.8

Source: Department of Treasury

2.4.2.4 Transfers to Statutory Authorities

The Statutory Authorities' funding will be increased in 2009 by K27.2 million or 12.0 per cent to K253.9 million compared with the revised estimate for 2008.

Table 30: Transfers to Statutory Authorities 2007 – 2009 (Kina Millions)

	2007 Actual	2008 Estimate	2009 Projection	Change
Tertiary Institutions	76.3	84.5	91.0	6.5
<i>UPNG</i>	30.4	32.1	33.4	1.3
<i>University of Technology</i>	29.0	29.9	32.0	2.1
<i>University of Goroka</i>	11.1	11.6	12.4	0.8
<i>University of Vudal</i>	5.8	6.8	9.0	2.1
<i>Legal Training Institute</i>	1.0	1.3	1.5	0.2
<i>PNG Maritime College</i>	2.5	2.7	2.7	0.1
PNG Forest Authority	35.2	24.5	26.0	1.6
Civil Aviation Authority	11.5	12.2	9.6	-2.6
National Broadcasting Commission	13.1	13.8	20.3	6.5
Ombudsman Commission	11.0	11.1	14.0	2.9
Office of Auditor General	11.0	11.2	14.2	3.0
Tourism Promotion Authority	8.1	9.0	9.8	0.9
National AIDS Council	5.4	5.5	5.7	0.3
National Training Council	1.9	2.2	2.5	0.2
PNG Sports Foundation	4.4	2.8	3.2	0.4
Other 1/	57.0	50.0	57.5	7.5
Total Transfers to Stat Authorities	238.5	226.8	253.9	27.2

Source: Department of Treasury

1/ Comprises NRI, NEFC, National Narcotic Bureau, Institute of Medical Research, National Youth Commission, IPA, SBDC, NISIT, ICDC, National Museum Authority, National Housing Commission, National Cultural Commission, CCI, FPDA, NARI, NRA, ICCG, CLRC

Table 30 summarizes transfers to Statutory Authorities in 2009. Major funding increases will be provided to Tertiary Institutions (K6.5 million), National Broadcasting Commission (K6.5 million), Office of Auditor General (K3.0 million), Ombudsman Commission (K2.9 million) and the PNG Sport Foundation (K0.4 million) for participation in the Arafura Games in 2009.

More broadly, the Government's policy continues to be for Statutory Authorities to become self-funding over time, allowing the Government to focus resources on core functions and the MTDS priorities. However, progress in implementing the reforms in this area proposed by *Public Expenditure Rationalization Review* (PERR) program continues to be slow.

2.4.2.5 Interest and Other Fees

Total interest and other fees payments are projected to be K392.8 million in 2009, an increase of K34.6 million, or 9.7 per cent, from the revised estimate for 2008. The total payment is comprised of K304.0 million in domestic interest and fees outlays and K88.8 million in external interest and fees outlays.

Table 31: Interest and Other Fees 2007 – 2009 (Kina Millions)

	2007 Actual	2008 Estimate	2009 Projection	Change
Domestic Interest Outlays	252.1	275.3	304.0	28.7
<i>Treasury Bills</i>	51.2	64.6	73.7	9.1
<i>Inscribed Stock*</i>	202.2	206.8	223.5	16.7
<i>Other Domestic Debts</i>	-1.3	0.9	0.6	-0.3
<i>Agency Fees</i>	0.0	3.0	6.3	3.3
External Interest Outlays	117.9	82.9	88.8	5.9
<i>Interest</i>	117.9	82.1	70.6	-11.5
<i>Other Fees</i>	0	0.8	18.2	17.4
Total Interest & Other Fees	370.1	358.2	392.8	27.2

Source: Department of Treasury

* Premiums on Inscribed Stock are treated as a negative interest outlay.

Domestic interest and fees are forecast to rise by K22.0 million (or 7.8 per cent) in 2009 to K304.0 million. The increased payments reflect a moderate increase in Treasury Bill yields, increased interest expenses on Inscribed Stocks and the net replacement of external debt with domestic debt in order to reduce exchange rate risk.

External interest payments and other fees are projected to be K88.8 million in 2009, K5.9 million, or 7.1 per cent lower than the revised estimate for 2008, reflecting a moderate rise in the value of the Kina against major debt currencies. The large increase in Other Fees is due to a subscription fee to the IMF and World Bank as well as large fees for new loans from Finland and China.

2.4.3 Development Expenditure

The 2009 Budget provides for substantially increased funding to the Development Budget to pursue its development priorities. In doing so, the Government is seeking to promote sustained economic growth through empowering and transforming the rural economy and by providing employment opportunities for our citizens.

The Development Budget for 2009 is K2,595.2 million, which is K720.5 million or 38.4 per cent higher than the revised estimate for 2008. This reflects the Government's funding allocation in 2009 increasing by K857.5 million to K1,620.9 million for 2009, partially offset by a decline in funding from the Donor agencies due to the appreciation of the Kina, and a downward revision to the Infrastructure Tax Credits.

Table 32: Development Expenditure: By Source 2007–2009 (Kina Millions)

	2007 Actual	2008 Estimate	2009 Projection	Change
Government	607.5	763.4	1620.9	857.5
<i>Domestic Funding</i>	483.2	526.7	1385.9	859.2
<i>Infrastructure Tax Credit</i>	20.6	73.7	40.0	-33.7
<i>Loans</i>	102.8	163.0	195.0	32.0
Concessional	101.8	163.0	195.0	32.0
Commercial	1.0	0.0	0.0	0.0
Donor	721.0	1111.2	974.3	-136.9
<i>Project Grants</i>	721.0	1111.2	974.3	-136.9
Total Development Expenditure	1327.6	1874.6	2595.2	720.6

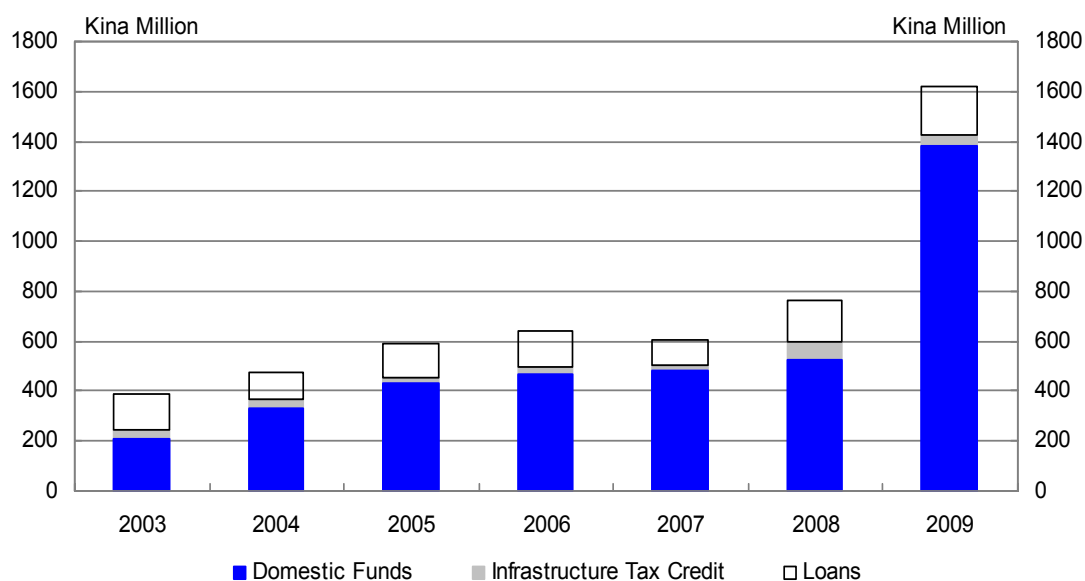
Source: Department of Treasury

The K1,385.9 million domestic funding for Development includes 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
• MOA Commitments	K70.0 million
• Wharves and Bridges Funding	K60.0 million
• Additional Provincial and Rural Roads funding	K66.0 million
• Waigani Office redevelopment	K50.0 million
• National investments	K43.0 million
• Rabaul assistance package	K25.0 million
• ADB Highlands Region Road Improvement Investments Program	K38.0 million
• Prime Minister's Community College	K30.0 million
• Provincial Impact Projects	K20.0 million
• National Stadium	K20.0 million

The additional spending over and above the budget will be closely monitored and measured in order to ensure that tangible benefits are achieved in line with the Government's objectives. Details of the 2009 Development Budget can be found in Chapters 6 and 7 of this Volume.

Figure 12: Government Contribution to Development Budget (Kina Millions)



Source: Department of Treasury

2.5 FINANCING

The 2009 Budget is expected to be a small deficit of K10.3 million, effectively a balance budget when measured against GDP. This reflects the impact of reduced revenues arising from the substantial fall in commodity prices and increased expenditure announced in the 2009 Budget.

Total new external borrowing of K195.0 million is expected to be undertaken in 2009, reflecting additional drawdowns on concessional loans.

External repayments (amortization) of existing loans of K224.6 million will more than offset new borrowing, resulting in a net external outflow of K60.6 million in 2009.

The net domestic funding required in 2009 to fund the outflows in external financing will be K70.9 million. This consists of K1,496.8 million in new borrowing and amortization of K1,425.9 million. No receipts from asset sales have been factored into financing of the 2009 Budget.