Information, Ownership, Transparency, Implementation and the 2009 Budget

Part 1.

The 2009 National Budget is now passed. That was a brief Parliamentary Session! MPs don't seem to be overdoing it lately, and now won't meet again until next March. Perhaps, there's a reticence, considering delays in receiving salaries and Parliament's apparent financial problems. MPs and PAC seem surprisingly tolerant of the Speaker.

The Budget is the people's money plan. The Treasury, unlike other public agencies, has been doing a sound job over recent years in improving transparency, placing details of the Budget and progressive expenditure on their website, and making it more accessible. Next February the global Open Budget Initiative (OBI) report will be released, showing how PNG ranks in managing its Budget process compared with other countries. Many developing countries have made great strides in recent years to make their Budget and expenditure more accountable to their own population, right to the local level.

As we all know, public infrastructure and basic services are totally unsatisfactory in PNG, and a disgrace for a country with strong revenue over many decades (notably from natural resource extraction). We also recognise, from audits, inquiries, Public Accounts Committee reports and direct experience, that massive abuse of public funds is occurring, undermining the delivery of goods and services, with government machinery widely dysfunctional. The sound objectives in the Budget and our Medium Terms plans, therefore, often bear little relationship with actual implementation and outcomes. Large amounts are spent and remain in Trust Funds annually, with little achieved on the ground. Commendable fraud investigations have been undertaken and charges applied in 2008, notably in Mendi, but high level fraud, like the K40 million+ allegedly siphoned off to Singapore, has triggered merely denials or silence, rather than outrage and probes by government.

Effective implementation requires greater public awareness and ownership of the Budget itself, combined with mechanisms to safeguard public resources from abuse, and more functional arrangements for investment and service delivery, such as transparent Public-Private Partnerships (with reputable companies, churches and NGOs) and use of genuinely independent boards and audit committees.

What will undermine improved performance and accountability is the tendency by government towards secretiveness. The Treasury Minister's banning of the Post Courier from the Budget press-lockup undermines needed Budget awareness and ownership, whilst aspects of the proposed Amendment to the Organic Law on the Ombudsman apparently weaken needed accountability of political leaders.

The print media is a key mechanism for providing the public with details on how their money will be spent. So, if the Minister disliked premature leakage, he should have been eager for all media to receive and disseminate the real version. His treatment of the public's Budget as his own private matter is disappointing, but reminiscent of his effort, as former Forest Minister, to restrict public dialogue on forest policy. Fortunately, the current Forest Minister (and management) seem readier to acknowledge long-standing forest governance problems in PNG and to consult over how to address them. Several independent reports and a recent major Supreme Court decision have highlighted how PNG’s forestry policy and laws have been widely abused, including in securing new concessions through backdoor arrangements, and failing to manage projects on a sustainable basis. Recognition of problems is the essential first step to resolving them, and forestry (as with other industries) should play a significant constructive role in PNG's rural economy, both from sustainable production as well as conservation (including carbon retention)

Operating companies in any industry are correct in stating that they should not be blamed entirely for poor industry standards. Some companies worldwide maintain high standards of their own accord (partly because of a long term commitment to that resource or market), but others have shorter time horizons and are prepared to use all means to minimise costs and maximise returns. If PNG allows poor standards and fails to manage its resources in its own interest less scrupulous companies feel little responsibility. If the PNG authorities send a clear message that high standards are required and corrupt practices not tolerated (amongst government staff or investors), and demonstrates high penalties for malpractice (and practical benefits for good conduct), most miscreant companies will invariably change their ways (or not come), providing wide benefits to PNG, although to the detriment of some leaders and their offshore accounts and property! PNG should certainly join and seriously adhere to such international mechanisms as FLEGGT and the Extractive Industries Transparency Initiative (EITI) and ensure that operating companies, whether in mining, forestry, fisheries (or other industries) meet international best practise (this also benefits the industry, by encouraging resource sustainability and that the reputation of good operators are no longer tarnished universally by the bad).

The proposed Amendment to the Ombudsman Commission legislation provides some benefits, but undermines some valuable current functions of the Leadership Code, notably over protecting public offices from abuse. With corruption severely undermining the functions of the public sector, from the highest to the lowest levels (despite the solid yet inadequate efforts of many dedicated leaders and public servants), it is crucial that there are both dynamic mechanisms to intervene and prevent abuse and protect key public offices and institutions, and also firm deterrents, notably though effective application of the Criminal Code. A core function of the Leadership Code is to protect public offices, through prompt dismissal of offenders, where necessary, without the Criminal Code’s level of onus of proof. Dismissal or the small fines under the Leadership Code do not provide a fitting punishment, if a serious offences have been committed. It is not double-dipping, therefore, to strategically safeguard the public office from abuse under the Leadership Code, whilst subsequently imposing a penalty that fits the crime under the Criminal Code, following a full investigation and referral by the police (which the police have long been remiss in doing).

It’s hard for the public or private sector or even other agencies to obtain any information on government processes, laws and programmes. In the past there were valuable yearbooks produced by the Office of Information, and annual directories listing Departmental structures and office holders and their contacts; these were immensely useful, especially for those in the provinces. Statistics were obtained and released promptly, and contributed to planning. Preparation for the 2010 National Census should now be well advanced, with comparable village mapping undertaken and an advisory group operational with NSO. This is not the case. Now, despite modern ICT, few agencies even have websites, let alone providing updated information; (Treasury, Bank of PNG and TPA are some agencies which do). The government's newsheet (Gavaman Sivarai) dishes out often obsolete press statements and promotion, without providing valuable community information; it could be made much more useful.

For 2009 government must shift focus from seeking to control, whilst reluctantly sharing information, to open dialogue, performance standards and service-orientation, whilst facilitating private sector opportunities (progressively removing unnecessary bottlenecks) to diversify and continue to grow the economy, despite the recent global economic and commodity downturn.

Part 2.

2009 Budget Commentary

PNG's been enjoying strong economic performance over the past 3 years, with growth estimated by Treasury at 6.2% for 2007 and 7.2% in 2008; a significant margin over the 2.7% population growth rate, with investment and employment expansion in all sectors, and increased government revenue and allocations for priority expenditure, although growth remains imbalanced towards enclave sectors and a few towns.

This growth has been enabled partly by some reforms (notably from the Morauta Government pre-2002), which facilitated stable political conditions and monetary management, combined with subsequent sound fiscal and debt management (including through medium term fiscal and debt strategies and the 2006 *Fiscal Responsibility Act).*

The main driving force, however, has been the recent spurt in commodity prices, driven especially by the burgeoning demand from China and India. It should be noted that whilst the government since 2002 shelved or moved slowly with market reforms, its few modest reforms, notably opening up mobile phone competition in mid-2007 have contributed to the growth in 2007 and 2008, (with mobile telephony estimated by Treasury at providing 2% of the 7.2% growth for 2008)
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There was a widely expressed notion that economic cycles were something of the past, with few listening to the few economic soothsayers warning of an impending financial crisis (based upon the US) with likely wider economic repercussions

When the financial crisis and economic downturn struck US, W. Europe and Japan, some still believed PNG was immune, driven by continued strong Chinese/Indian growth.

Even a few weeks back the Treasury Minister was still cocooned, and he and his Department head provided highly contrary forecasts!

China and India are currently expected to still register growth of at least 7-8%, driving continued, though more modest, demand for raw materials from PNG, supported by the Chinese Government's announced major economic support plan.

PNG remains a dual economy, partly driven by commodities, with the other half still subsistence-based, gaining few benefits from development, but remaining relatively immune to market swings and troughs.

The global financial crisis resulted from lack of transparency in financial markets; excessive leveraging, verging upon blindness, with repackaging of risky (over-exposed) loans into overrated securities (SIVs etc), leading to the collapse of the money market, with no-one knowing other financial institutions' level of exposure. Markets can be restored over time (to more modest and sustainable levels) through mandatory disclosure, restoring banks' balance sheets (with interim Government interventions), return to basic financial prudence and understanding of products and exposure (including by bosses and regulators), and slashing financial incentives towards excessive risks or cheating.

PNG will be caught by the global cold, but it is crucial that it maintains monetary and fiscal stability, and sustains adequate bank liquidity (including when Government Trust Funds are drawn down during 2009/10) and demonstrates prudence with whom it trades and reliability in honouring its own contracts. PNG needs to ensure it builds/retains a reputation of credibility in this uncertain market (including new markets like carbon trading). Public institutions should avoid additional international borrowing, except on concessional terms, especially entailing mortgaging public resources.

The commodities which PNG exports have taken a thrashing of late, both minerals/oil but also most agricultural products (including vegetable oils, now substitutes for mineral oil); it is probably unrealistic to forecast such positive continued growth from these agricultural products, especially copra/coconut oil, as envisaged in the Budget (Minister's speech); with 50% price falls for some crops, and some (like tea) not even finding a market, unless there's a strong price recovery and excellent growing conditions, agricultural growth is likely to be limited in 2009/10, if at all (smallholder producers reverting to meeting basic expenses, or meeting a 'target income').

There's a saying that commodities always return to their long term trend. Some, including oil, remain above the level say 5 years ago, so maybe there's some further downside, but at current levels for many products, so long as prices don't fall further, they should still provide better returns than hitherto. For oil and gas producers there are grounds for optimism that the longer term price trend will be firm, with continued global demand and growing purchasing power, especially in emerging economies, combined with declining supplies.

The massive hike in commodity prices was not good for the world economy, and despite windfall revenues, such price fluctuations are not really good for PNG, encouraging distortions and exaggerated expectations, inflation, currency appreciation and other aspects of the 'Dutch disease'.

So how is PNG set to weather the storm, now buffeting the global economy and especially commodities? The 2009 Budget was written and edited hurriedly in the face of rapidly evolving and unpredictable global market conditions. It remains largely fiscally conservative, although agriculture maybe optimistic, with large potential risks. For 2009, at least, there are accumulated funds to fall back upon, if necessary.

Positives economic and Budgetary aspects include: -

- public debt level is now down to about 29% of GDP (from 75% in the early 2000s), thanks largely to GDP growth, but some steady repayments. The actual debt should probably have been reduced further, as an investment for tighter times in future, reducing future foreign debt service obligations. This is an effective way at stabilisation, without setting up new investment vehicles (like multiple trust funds)
- total external debt (at the end of 2007) – public and private – is 41% of GDP, or K6.9 billion, down from 79.5 % in 2001 (K8.3 billion), (further reduced in recent weeks by the stronger kina)
- record foreign exchange reserves – K 6.5 billion in mid-2008 or 9.3 months of import cover (13.5 months non-mining)
- debt composition improved (lower cost, more domestic and less forex risk)
- interest rates remain low, though recently higher (and perhaps could be higher to restrain overheating and undue inflation, and avoid negative gearing, although we also need to restrain currency appreciation)
- Several years of positive current account balances (estimated at 8.7% of GDP for 2008) have shored us up. From 2009 the trade surplus will be severely reduced, especially with high imports for new mines, with several years of current account deficit from 2009 forecast, drawing down on capital and financial accounts.
- Reduced global inflationary pressure (as commodity prices, especially oil and some foods, fall) and with the appreciation of the Kina to Aust Dollar, though the latter undermines competitiveness for PNG's exports and import replacement
- On the fiscal side, PNG has built up strong fund accumulations, usable for the rainier days ahead ; K2.5 billion unused in Trust Funds and K2.2 billion yet to be released from the 2005-2008 Supplementary Budgets, including about K840 mill unused from the 2008 DSIP (K10 million per District); with the slow drawdown of these 'windfall funds' there will be K3.7 billion (notably in Trust funds, or being deposited into them) to continue funding priorities over the next couple of years, whilst restraining undue inflationary effects; (The K2.2 billion includes K600 million, hitherto allocated for gas equity, to be transferred to fund 2009 and subsequent Budget initiatives, including an additional K4 mill per District under DSIP)
- the Economy has a good head of steam, partly driven by new externally-funded investment (e.g. mines) but substantially self-generating (including new construction) using domestic finance (from banks little exposed to the international crisis, through a strong deposit base, at least whilst the Trust Funds remain substantial, despite negative real interest rates!)
- improved financing (equalisation) is provided for Provinces from 2009 to meet basic infrastructure and service needs, using NEFC recommendations of

minimum costs, but there's limited capacity building to implement, including the DSIP

- whilst lower oil prices weaken PNG's revenue and trade balance, they clearly benefit households and most businesses (other than producers, including, part substitute producers, e.g. vegetable oils/biofuels). As a main driver of inflation, lower prices help restore international demand and recovery (combined with greater transparency in the financial markets and clearing out the backlog of bad debt)
- Government has (tentatively) awoken to the need to embrace the private sector to generate more sustainable growth, hence:-
  - competition in mobile phones, has been directly impacting investment and economic activity, and indirectly improving opportunities for trade and economic activity right into rural areas (where transport infrastructure exists). In Feb 2009 under Phase 2, competition need to be extended to all ICT (internet, international gateways, VSAT etc, dropping continued impediments)
  - PPP policy introduced to improve service delivery (through long term investment and contractual arrangements), though privatisation remains frozen
  - improved Foreign Employment legislation applicable from January 2009 , whilst the Department has improved operations (although other critical business impediments, including Migration, DPM etc., remain entrenched, with little effort to address most of them)
  - the Lands Act amendment could improve land administration, but only really if organisational changes occur

Bad aspects:

- little progress pursued in recent years with public sector reform (notably the Right Sizing Committee recommendations), needed to make service delivery better focused and sustainable; far too much goes to National Departments and administration, regardless of priorities or capacity, with little progress with retrenchments, safeguarding operational funding, and incessant growth in public service costs. The latest salary increase is meant to be performance linked...is this for real, considering current generally low performance?
- In recent years conservative prices have been used in the Budget, but this year some (e.g. agriculture) may prove optimistic. We're in uncharted water. Its very difficult to predict trends, except that they're likely to return to longer term averages, but already prices of oil and some agricultural crops are below the 2009. The Budget is optimistic over agriculture's potential, but new mine development and construction and other ongoing projects should maintain the momentum
- cash crop agriculture maybe hard pressed to meet Budget forecasts (although there are some good prospects there if the kina can remain competitive (i.e. restrained), but it requires focused attention on addressing wide ranging sector constraints, especially infrastructure and access to markets and law and order problems, but also threats on our doorstep now, such as cocoa pod borer which could devastate production if left to sweep through without adequate attention to upgrading farming standards; there will invariably be winners and losers (and, hopefully, even in a global downturn everyone will want their cup of coffee and chocolate!)
- the risks include banks (largely overseas) not issuing Letters of Credit (notably to importers) in a declining or volatile market and buyers trying to renege on existing

contracts when prices have slumped, since contracts were signed. This is already happening overseas with oil palm and other crops, and could undermine trade and shipping;

- NADP has largely been a wasted opportunity, so far. Grants have been made to individuals and businesses without clearly applied criteria or quality checks. Why should one group secure a large subsidy and not another, undermining a level playing field, those borrowing, whilst encouraging corruption; for example, K17 million for 6,000 head of cattle indeed, or nearly K3,000 per head of unremarkable cattle! We need to be much more prudent with (limited) investment funds.
- large sums are allocated to recognised non-performing mechanisms, e.g. to administer District grants. Critical funding is required for restoring District infrastructure and services, more realistically effective mechanisms should be used.
- There's been little progress addressing corruption and accountability issues, so wastage is little restrained, although DSIP safeguards are markedly tighter.
- IPBC has mortgaged and probably lost publicly-owned Oil Search shares in a deal to acquire an equity stake in LNG. IPBC's function is caretaking and divesting State equity, through transparent mechanisms, not being a vehicle for acquisitions. Revenue to the State from dividends through IPBC, and from fisheries licences through FIA, requires tighter rules and transparency.
- opportunities are being missed for divesting equity, whilst simultaneously improving competitive services. Instead, the State continues committing additional public funds to investing in SOEs, like Telikom and Air NG (k70 million for new aircraft and K30 mill capital injection), and undermining viability of Singapore flights by also servicing nearby KL; The SOEs no doubt need additional capital but that should entail private equity investment and more commercially experienced boards, driven by commercial opportunities and stimuli
- the 2009 Budget has lost focus, unduly sidestepping MTDS priorities, and funding a mishmash of low priority, or ill-considered projects; for example it would be better to invest in upgrading NBC radio stations to reach across the nation, rather than a new TV station; It is appealing to improve choice and (programme quality) through competition and a State service-provider, but will NBC have the resources to either achieve quality and sustain it, or just run another service of limited quality, spreading limited capacity and diminishing funds further?
- There are large arbitrary allocations to selective authorities, e.g. Motu-Koita (K10 million, probably justified from years of being sidelined) and Provinces which have burnt their HQs (K13 million rewards apiece?), and projects like Madang marine park (which, if needed, should entail private investment, – K15 million in Trust and now another K10 million)), Community colleges (surely better used to support existing rundown schools/technical and vocational schools). We should dump the extravagant Central City (a field day for unproductive consultants, like that housing project Mr Conrad induced POSF into!), a new executive jet (K40 mill), Konebada petroleum park (K50mil - should entail private capital), and ICT policy shouldn't cost K20 mill to formulate!....these expenditures invariably prove excessive or a complete waste, like the past industrial centres. What are “National Investments” (K43 million), and why always such large extra allocations, e.g. Defence increase (k13.6 mill), K20 mill for the long term plan, K20 million for LNG support office? Is there no recognition of tighter future revenue?
- Why then the failure to honour superannuation commitments from 2009?

- Continued excessive out of court settlements are budgeted; let's minimise these ill-judged or hastily made decisions (e.g. on dismissals) exposing the State to challenges. Sometimes this has involved appointing unsuitable persons to top position, realising this but then skipping processes in the dash to remove them; all at great cost to the State (I.e. the public)!
- MWB **–** the cost of living has certainly increased substantially (especially for low income and informal sector earners) although some costs should level off and even decline now. An adjustment to the minimum wage is needed but the process should be more dynamic, through negotiation between the players using the National Tripartite Council, rather than the unwieldy periodic Minimum Wages Board process. It must recognise capacity to pay, and that most formal sector employers are currently paying well above the minimum, whilst parts of the rural sector have limited capacity when prices are low (although generally providing housing and some other benefits). Attention should be focused towards various local and foreign-owned businesses currently ignoring even the current minimum (and IPA rules) but have the capacity to pay. Proper/impartial enforcement is necessary, as with tax application, where many significant businesses never contribute. Many jobs, however, will be lost if an arbitrary and unrealistic minimum wage determination is set, and it's better to give people the option of formal employment even on a basic, but affordable wage, than no job and dependency upon marginal IS employment. Flexibility is required as some companies and businesses can afford to pay more, whilst other productive industries (NOT extractive industries), especially in remote locations genuinely cannot.

In conclusion: -

The 2009 Budget was hastily prepared, during rapidly changing global economic and market conditions, with an inevitable but unpredictable impact on PNG's economy and fiscal scenario.

- during the period of high commodity prices, PNG is fortunate to have accumulated substantial reserves and savings (partly resulting from its own implementation incapacity), which should sustain steady public expenditure for the next two years, when credit and investment conditions should also remain sound, so long as the macro-economic conditions do not deteriorate, or exchange rate appreciate.
- many realised that these were windfall revenues, but hoped they would last, but this bonus encouraged loss of focus (living in dreamland), overlooking priorities whilst still throwing tens of millions on low priority extravagant projects.
- Government has largely failed, therefore, to take advantage of the opportunity and strive for needed reform of the public sector, whilst progressing wider economic reforms at a snail's pace. These reforms are essential for the economy to be diversified, growth to be sustainable and priority objectives to be achieved right out in rural areas (notably Millennium Development goals and MTDS priorities). The biggest reform has been the first step in 2007 toward ICT competition, which has highlighted wide economic (and some social) benefits, replicable in other industries (including through potential full competition in all ICT from February 2009).
- the needed reforms include seriously addressing poor governance and corruption, which currently undermine service delivery severely and waste tens of millions of kina annually

- the overruns in 2008 include public sector emoluments (demonstrating the failure of years of botched public sector reform) and over-expenditure outside MTDS priorities
- LNG is the central focus of government, and a market stimulus (including for real estate and rentals). It is perceived as the panacea for PNG's future economy (which it isn't) and revenue (which it maybe), but it could be a major liability if adequate safeguards from the Dutch Disease are not applied early. If it proceeds, it will have a big impact, though not nearly as big as some envisage, as most components and employment are sourced overseas, and transfers return overseas. Treasury estimates it could raise GDP by 25-30% in peak years (well below the ACIL-Tasman figures) or average 9% of GNI till 2047 (i.e. excluding transfers overseas).
- If proceeding the project(s) should export LNG from 2013, although making a significant impact on economic activity (and the balance of payments) hitherto. In the meantime new mine developments and ongoing (largely domestically-financed) construction will sustain economic activity, although mineral and agricultural prices and hence earnings and (agricultural) production may remain depressed.
- We simply cannot depend unduly upon LNG benefits, to the detriment of the wider economy. The 2009 Budget focus is upon rural development. That is reflected in some actions, including the changes to provincial and local government financing, but, unless sound and transparent planning, implementation and monitoring of the DSIP, NADP and other rural infrastructure development (and improved law an order conditions) occur the benefits to the rural areas will be limited and sporadic, if at all.

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