**2014 Budget (preliminary Commentary on the PNG Budget tabled in Parliament on 19 Nov 2013)**

The 2014 Budget, tabled in Parliament on Tuesday, has provided few new surprises. It is basically a consolidation of the multi-year Budget launched by the new government commencing in 2013, but with some of the flaws addressed.

PNG has enjoyed a decade of economic growth, particularly robust since 2006, and yet the major concern of Papua New Guineans has been the dual nature of the economy and the limited spread of benefits and participation in this growth by much of the country's population, particularly in the country's remoter provinces and rural areas. The focus of the 2013, and now 2014 Budget has been to address the critical constraints to broader-based and sustainable economic and social development and participation, notably through increased expenditure on infrastructure, education, health, law and order , the districts and ostensibly agriculture and tackling corruption.

2013 was announced as the year of Implementation, entailing a major jump in expenditure on the key priorities (and a wide range of projects – some more meritorious than others - under the Alotau Accord) in order to make real headway in tackling years of declining public goods and services, and to partly offset the winding down of the PNGLNG construction phase, utilising deficit financing, and dependent upon future forecast increased revenue, notably from LNG and other extractive industries.

2013 should perhaps have been termed the year of <u>preparation</u> for implementation, as invariably with years of weak, and, in some institutions and provinces, declining capacity, planning and implementing major programmes or reforms was unachievable overnight, and governance, including oversight mechanisms deficient, particularly at the sub-national level. A major onus was placed (without much prior notie)upon development partners to facilitate the implementation process, and many hastened to adjust their ongoing programmes to support this need, albeit that many donor-funded programmes are themselves very unwieldy.

So, by October 2013, only about half the development budget was spent, partly owing to delays in fund release and implementation, whereas some allocations (often politically-favoured) were 'front-loaded' and some operational expenditure, including personal emoluments, continued to suffer from deficient restraint. The need for better coordination between implementation agencies, particularly at the sub national level was apparent, with greater local participation in planning and control over expenditure, if critical bottlenecks were to be overcome.

A commendable achievement in 2013 has been that, despite difficult global economic conditions and low commodity prices, which contributed to the kina's decline during the year, revenue remained surprisingly robust, with IRC and customs achieving strong revenue outcomes, partly from businesses and households hitherto sidestepping their tax obligations, even whilst mining and oil taxes were down.

So, with tougher economic conditions for the minerals and agricultural industries than had been experienced for several years, and circumstances particularly for middle and lower income households relatively tight, it was unsurprising that the 2014 Budget seeks to apply no new taxes, but does endeavour to further strengthen the hand of the revenue agencies in ensuring the State secure the taxes and duties to which it is entitled, pursuing those avoiding their responsibilities, including those fraudulently collecting GST from consumers, without passing it on to the State.

With its increased expenditure, reaching a record planned K15 billion, 2014 envisaged a deficit of K2.3 billion, funded from domestic and overseas borrowing. Debt to GDP is forecast to reach 35%, in itself a manageable level, albeit that the State also holds substantial additional off-budget liabilities (related to PNGLNG financing, superannuation funds etc). Once again it depends upon future revenue, notably from LNG, but despite the boost to GDP expected from the commencement of gas production during 2014, substantial revenue from this source is several years hence, and with the restrained global market conditions and less buoyant investment conditions facing PNG for the time being, it would be unwise to throw caution to the wind, and all expenditure needs to be carefully targeted to achieve positive benefits. There is continued commitment to launching the Sovereign Wealth Fund, albeit, barring some un-forecast bounce in commodity prices, there's unlikely to be much deposited into it, or invested by this fund for some years. Those of a more cautious disposition would tend to suggest that a lower, safer and less-costly Budget deficit might be preferable, enabling an earlier accumulation, investment and distribution from the SWF might be preferable, limiting public borrowing and possible squeezing out of the private sector.

With limited attention in the 2013 Budget to the limited implementation capacity, the Government seems now to better recognise this and focus upon remedial action, including specific allocations in each district for capacity building, and attention to minimum standards at each tier of sub-national administration. During 2013 and for the 2014 Budget allocations for major projects have been tightened, and hopefully the merging of the recurrent and development budgets and revived commitment to 'right-sizing' will ensure a better balance between constructing new infrastructure and restoring and maintaining the facilities already in place. Similarly with education the need for building on core capacity and standards have hopefully been taken on board, in parallel with meeting the demands for extra school intake and retention.

With the 2013 Budget overly optimistic on commodity prices and productive expenditure capacity, 2014's Budget is also perhaps overly optimistic on non-mining prospects, but does recognise the need for more serious support for the critical agriculture sector, albeit that the sector's institutions, notably its coordinating Department, remain weak and relatively unaccountable, and little able to implement initiatives, without overdue reform and support. There is some emphasis in the Budget to needed institutional reform and better governance and accountability by Departments and agencies, including through non-release of new funding until past expenditure has been properly acquitted, with penalties upon institution heads who fail to meet accountability criteria. This is needed, but whether it is achieved or the will really there, will be tested, with too much laxity in the past, particularly when political allies or pressures demand.

After several years of inflationary pressures, 2012 saw low inflation brought about partly by the kina's strengthening. 2013 has seen inflation remain relatively low, although perhaps higher than the Treasury's figures by year end, notably on the tail of the sliding kina. Higher inflation is forecast for 2014, albeit still at a manageable level (if not for lower income earners), although needing watching as the lower kina prevails and higher public spending on domestic goods and services occurs. As the year goes by the pressure on the kina may reverse and the need to maintain (downward) stability take precedence, avoiding further difficulties for agricultural export earners ( and import replacers), already facing other threats of disease (notably in cocoa) and other appreciating costs. Significant forthcoming adjustments to the minimum wage would clearly affect the agricultural formal sector, and should be offset with support for productivity gains, which will be critical for competitiveness and continued viability and employment generation.

Clearly, the effectiveness of currency support by the Central Bank is jeopardised by insecurity by investors, so greater assurance to existing and prospective international investors is needed to both discourage capital flight, but also to further invest , diversify the economy and generate the jobs, and investment in skills development, that the PNG labour force so needs. Emphasis should likewise be on value-adding, rather than processing per-se, although in many, but certainly not all cases they may coincide. At the end of the day both PNG and international investors, large or smaller scale, all need stability of investment conditions and the assurance that there's a reasonable prospect of making an adequate return, without being dispossessed or facing undue costs, including from inefficient markets, such as exorbitant monopoly charges from ill-performing utilities, or from inefficiency or malpractice by relevant government agencies, or substantially altered investment policies and rules

The 2014 Budget continues the bold stance set out for 2013, to make a substantial investment in PNG's physical and human capacity. It entails no great surprises, but does better recognise and seek to address constraints to implementation experienced in 2013. It recognises the over-costings in 2013 and the Ministers responsible for tabling the Budget acknowledged the need to reform the procurement systems, enhance oversight and rationalise institutions to avoid multiple entities, particularly at national level administering finances. But, as with corruption and the establishment of the planned anti-corruption commission (ICAC), effective outcomes with accountable government services, depend upon adequate financial and human resources, not spread too thinly across multiple institutions, and operational independence, and the readiness to resist the pressure to disburse jobs and other benefits to sustain support.

Each year the Budget is delivered with much good intent, but subsequently poorly implemented. As the Ministers highlighted with some frustration, it should not be their Budget, but the nation's Budget, with everyone pulling together to ensure it works. Valid point, but it is also essential that the watchdogs are adequately resourced, and particularly that civil society is made fully aware, right down to the local level, of the contents, its benefits and the processes of government, so that they can play their part in helping keeping (their) government officials and expenditure on track to meet their own needs and requirements, consistent with the Budget.

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