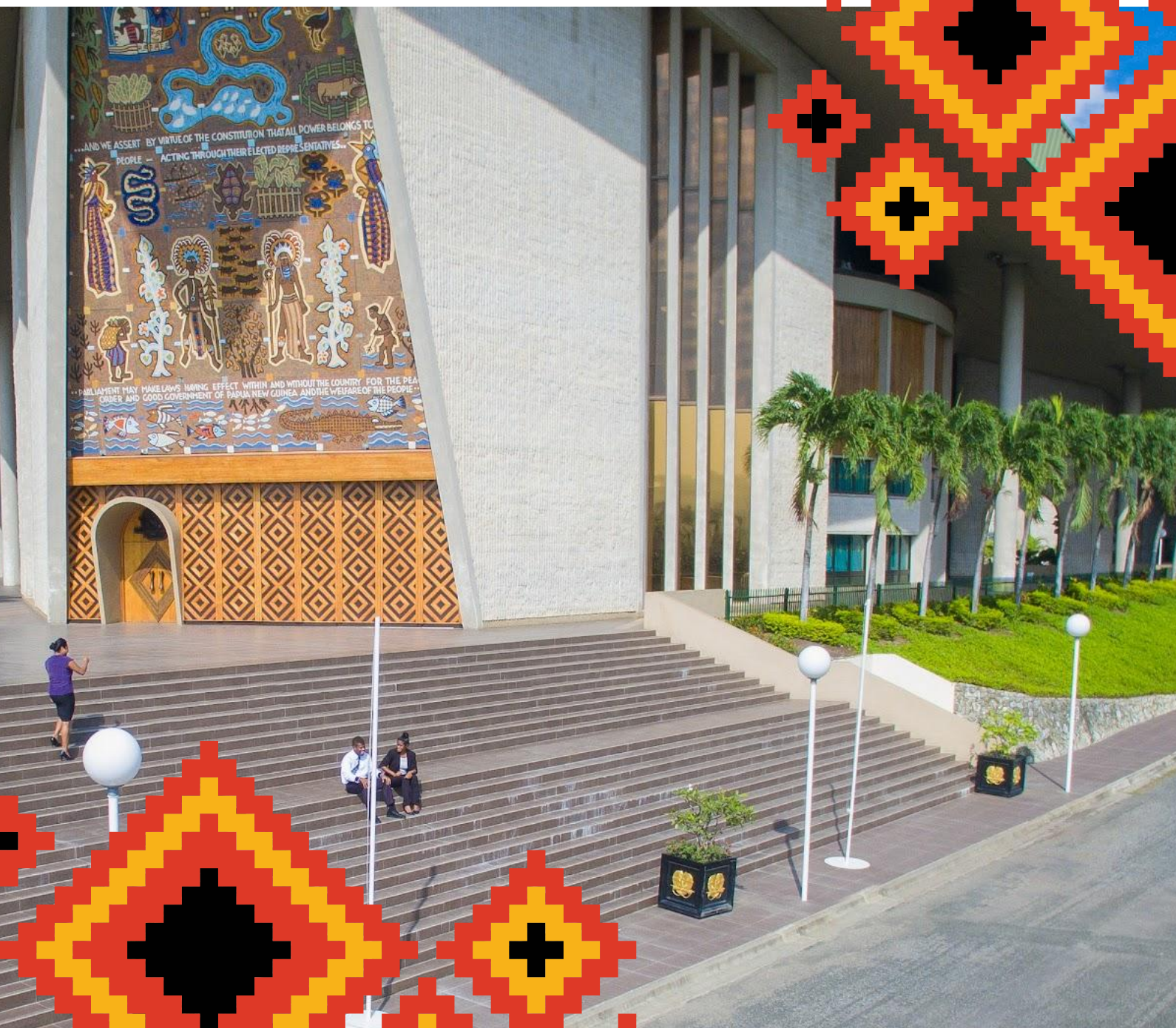


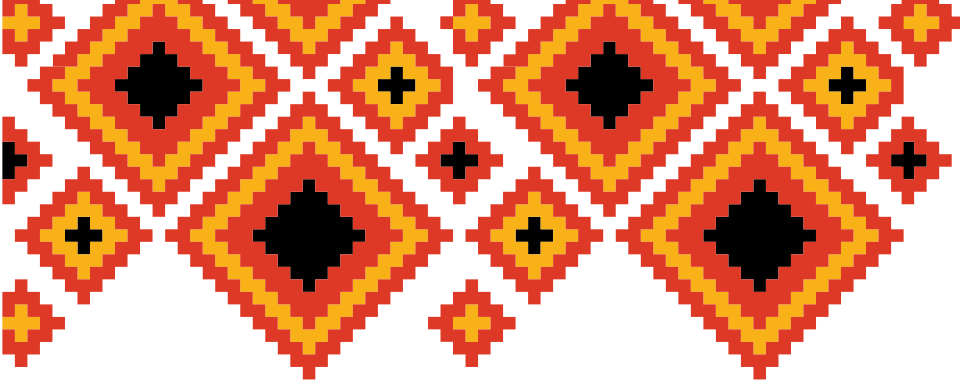
# Staying the course?

## PwC's 2023 Budget insights



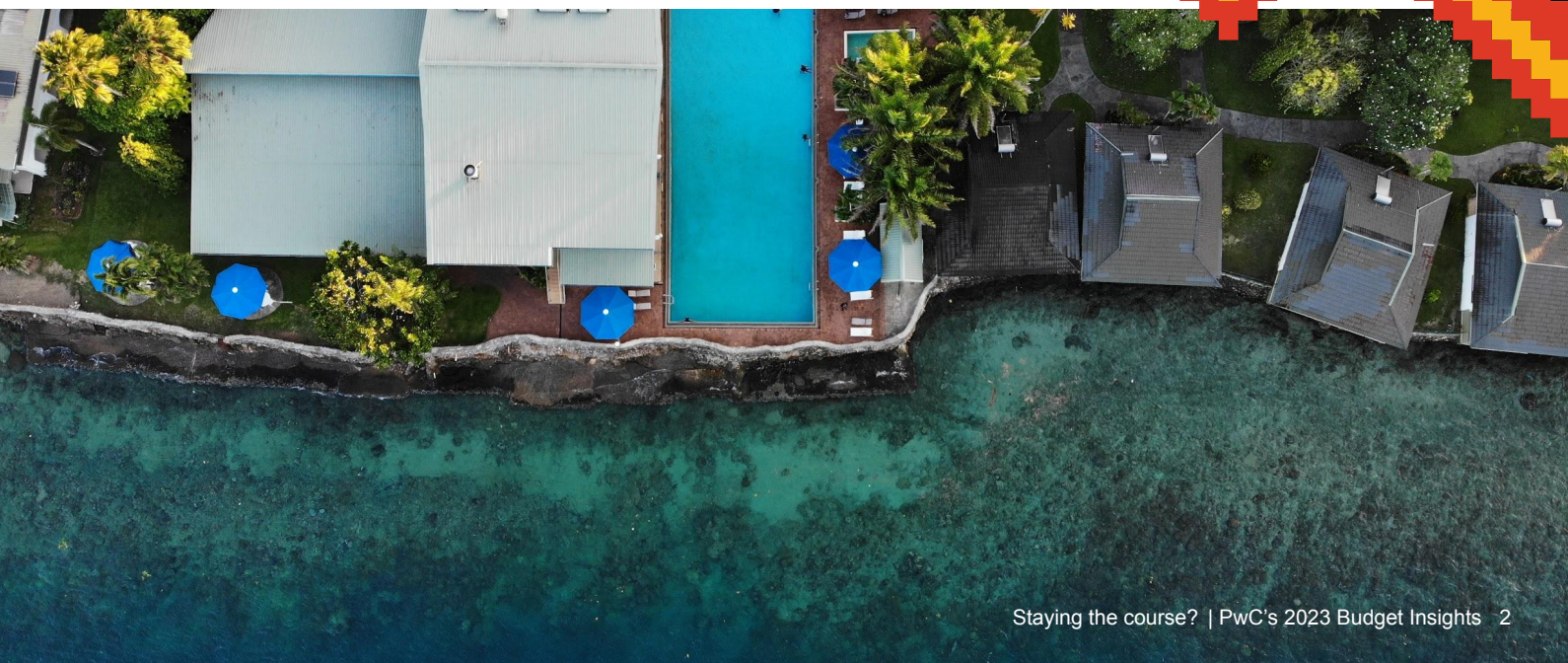
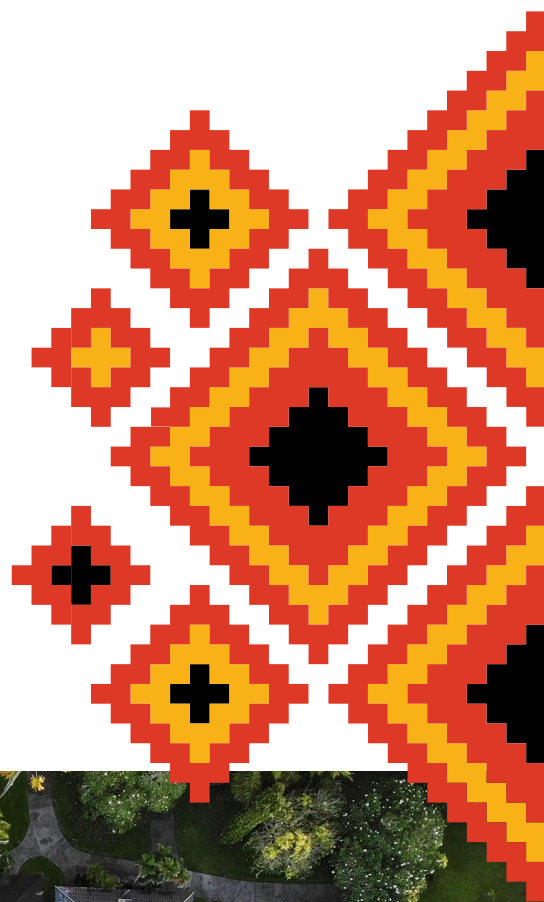
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# Introduction

## **Growth is now comfortably above 2019 levels (pre-pandemic)**

Papua New Guinea (PNG) has navigated the pandemic well. GDP growth in 2022 has improved, following weak growth over the past 3 years. GDP is now expected to be above 2019 levels in 2022. In 2023 the PNG economy is expected to grow by 4.5 per cent in real terms.

Government spending has provided a buffer to the COVID-19 impacts on the economy and has helped mitigate health impacts on households. As a result, debt has increased, as has been the case in most economies including PNG's neighbours during the pandemic. Looking forward, the Government has committed the 2022 and 2023 budgets to the difficult task of returning PNG to a stronger fiscal position. This will take time, but fiscal consolidation is required to strengthen debt sustainability and rebuild additional resilience into the PNG budget as an insurance policy against future shocks.

## **Revenue projections have improved**

By 2023 the budget deficit is forecast to decline by an additional K1 billion reflecting stronger than anticipated revenue growth, in part this reflects that some difficult decisions were made to support revenue growth.

Taxes have been increased in this budget for the banking sector, through a banking company income tax rate increase to 45 per cent, this will be applied to all commercial banks.

## **But budget repair remains a necessary part of the fiscal strategy**

The fiscal repair task is sensibly spread out over the coming 12 year period. This is commensurate with the scale of the task. The Government is to be commended for its commitment to delivering a return to annual surpluses by 2027. This budget shows the Government is on track to achieve this goal.

This ongoing commitment to rebuilding fiscal flexibility was demonstrated in the MYEFO update where all new spending was very deliberately offset by cuts in the capital budget to retain the same deficit as projected in the 2022 Budget. The 2023 Budget is following along the same path and has reported improved performance on the budget deficit.

Strict fiscal discipline will bring its own rewards. International organisations supporting PNG to transition from COVID will provide PNG with maximum access to concessional loans. This is important, because access to concessional loans allows the Government to retire the most expensive debt early.



**1** Spend the money we have more wisely

**2** Raise the revenues more fairly

**3** Finance the debt more cheaply

**4** Leverage friendly international support more intelligently

**5** Focus on growth in the agriculture, forestry and fishing sector, SMEs and the informal economy

**6** Distribute resource benefits more equitably

**7** Stimulate non-resource growth back to at least 5% annually

**8** Comprehensive Government state owned enterprise (SOE) reform program for cheaper energy, internet and water

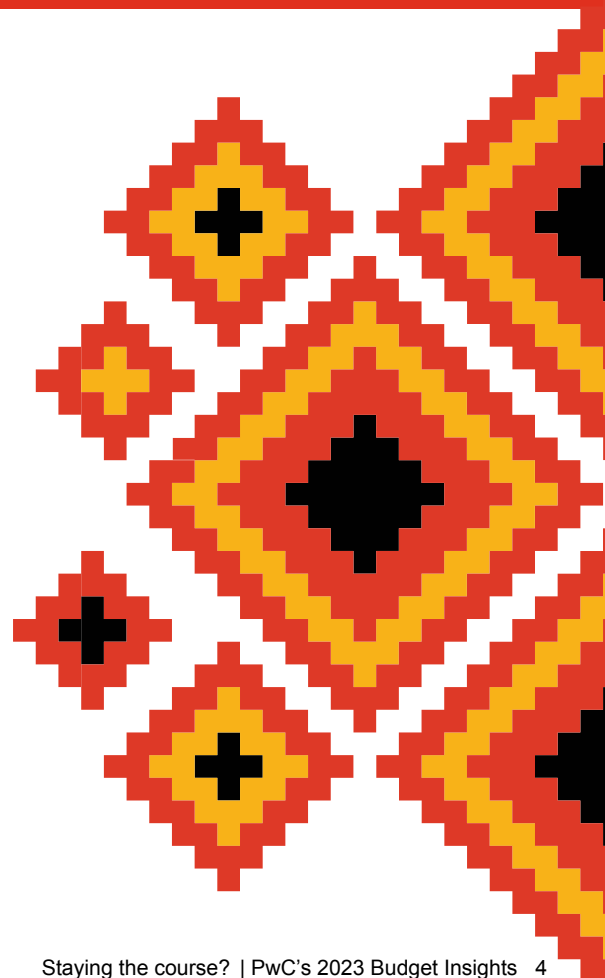
**9** Getting foreign exchange flowing more freely

**10** Create at least 10,000 jobs annually

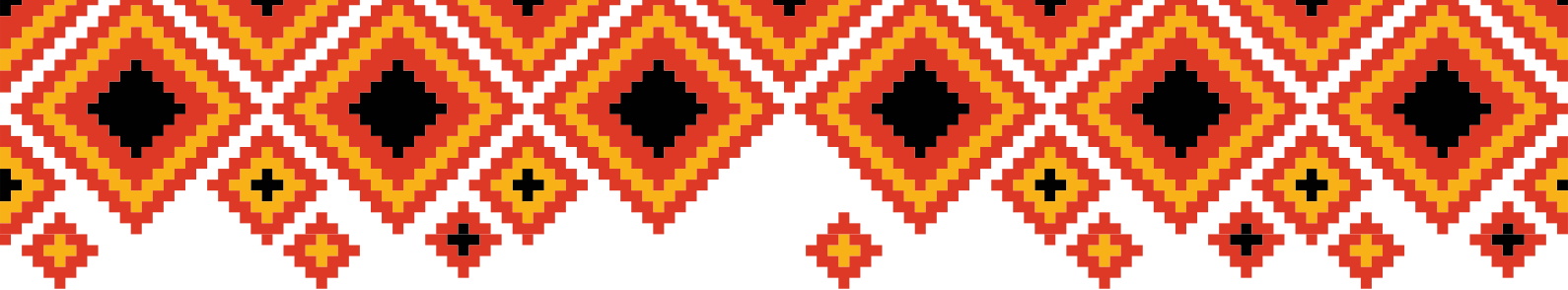
### Box 1 - The 2023 Budget will continue to be built around the following ten principles.

Lowering the deficit by around 7 per cent of GDP from 2021 levels is also needed to meet the requirements of the Fiscal Responsibility Act, which specifies that debt should be maintained at no more than 40 per cent of GDP over the long term. Government Gross Debt is expected to have peaked at 52.2 per cent of GDP in 2021, and is projected by the IMF to ease to around 44 percent of GDP by 2027.

The 2023 Budget outlines the following budget strategy objectives: the budget repair programme which, consistent with the 2022 Budget, is to provide the platform for fiscal consolidation whilst at the same time continuing to support economic growth and community services through strategic human and capital formation, expanding the tax base, and improving the delivery of essential services.







The 2023 Budget also outlines four core objectives to support PNG's development strategy, over the medium term. These objectives are designed to improve governance. The objectives will also arrest the erosion in social and economic development enablers, and improve the strategic positioning of government policy to their human development targets.

The objective are:

1. Strong economy
2. Connect PNG
3. Going Rural
4. Good Governance

### **War in Ukraine is pushing up key commodity prices**

The war in Ukraine, and the resultant supply shocks, created a global energy crisis and also put significant pressure on global food prices, grains in particular. For PNG this has pushed up commodity prices, for oil and gas in particular, which has driven higher revenue for PNG. However, this has also driven up global inflation. Inflation in Australia is expected to peak at around 8 per cent in 2022. Australia is a major source of imports for PNG, higher inflation in Australia will put pressure on imported prices for PNG.

### **And cost of living pressure**

Persistent price pressure is shaping up as the next challenge for the PNG economy to manage. Temporary relief was delivered in MYEFO to assist households with the initial price shock. However, as price levels are likely to remain elevated this is not sustainable over the medium term, the government has recognised this.

Inflation is expected to average 6.2 per cent in 2022. Imported inflation is a challenge. Australian headline inflation is expected to peak at around 8 per cent in December 2022. As Australia is PNG's largest source of imports, imported inflation is expected to drive up prices in PNG in 2023.

### **The government has intervened to ease cost of living pressure**

In response to domestic and imported price pressures, PNG's supplementary budget (post MYEFO) added a further package of K177m to extend the fuel tax reductions (removal of fuel excise and a GST exemption) to December 2022 and to lift the tax free threshold to K20,000 from 1 November 2022 for two months.

A package of temporary measures in response to higher cost of living prices for households flowing from the war in Ukraine was implemented during 2022. The package consisted of:

- removal of the fuel excise and GST on fuel products for 6 months;
- raising the income tax threshold from K12,500 to K17,500 from 1 June 2022 to the end of the year;
- paying for school project fees; and
- purchasing staple food items for sale to the public at fixed prices

The package was expected to cost K611m (0.6 per cent of GDP) in 2022.

In the 2023 budget K590m was considered as appropriate to further ease cost of living pressures for households in 2023.

The household assistance package consists of K280 million in income tax cuts for 2023 through the temporary lifting of the tax free threshold, K150 million on cuts to excise taxes on fuel for the first six months of 2023, and K160 million to fund school project fees.





**The PNG Kina has appreciated broadly in-line with the \$US, and is now overvalued**

The PNG Kina has strengthened against major trading partner currencies in 2022, in part reflecting the appreciation of the \$US and management of the Kina by the Bank of PNG (BPNG). While the Kina is recognised as floating, in practice it is a stabilised currency managed by the BPNG.

**A controlled depreciation by the BPNG over 2023 would ease FX availability**

The PNG Treasury and the IMF agree the Kina is overvalued. Estimates are that the over valuation is around 2.4 per cent in real terms (IMF estimate in mid-2022). BPNG will need to manage foreign exchange, with a view to reducing shortages in supply for 2023 and beyond.



## Growing the economy

PNG's GDP growth is expected to be 4.6 per cent in real terms in 2022, and a further 4.0 per cent in 2023, before stabilising at around 3¼ per cent from 2024 and carrying this growth into the medium term.

- The non-resource economy is expected to grow by 4.5 per cent in 2022, 4.6 per cent in 2023 then by around 5 per cent over the medium term.
- The resources sector was underpinned by favourable conditions in the mining and quarrying sector with growth of 13.5 per cent recorded for in 2022, while oil and gas is expected to record growth of 1.4 per cent.



**Table 1: Key economic indicators (real sector statistics)**

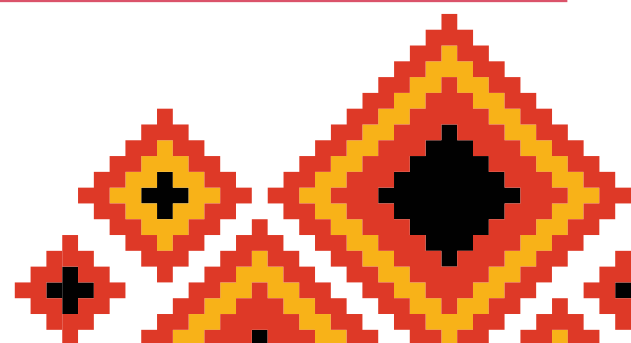
	2022 Budget 2022	MYEFO 2022 2022	2023 Budget 2022	2023 Budget 2023
Nominal GDP (Million)	K101.6	K110,302	K107,807	K113,108
Real GDP (%)	4.2	4.7	4.6	4.0
Non - resource (%)	3.5	4.4	4.5	4.6
Resource (%)	9.9	5.7	4.8	2.0
Inflation (%)	5.6	6.2	6.6	5.7

**Table 2: Key fiscal indicators (nominal statistics)**

	2022 Budget 2022	MYEFO 2022 2022	2023 Budget 2022	2023 Budget 2023
Deficit (K,mil)	5,984.7	-5,984.7	-5984.5	-4,984.9
Deficit % GDP	-5.9	-5.4	-5.6	-4.4
Revenue (K,mil)	16,190.2	17,389.0	17,389.1	19,582.0
Expenses (K,mil)	20,174.8	23,373.6	23,373.6	24,566.9
Gross debt (K,mil)	52,765.2	52,765.2	54,157.7	59,142.611
Debt % GDP	51.9	47.8	51.5	52.3
Interest costs (K,mil)	2,324.4	2,324.4	2,324.4	2,511.0

In this paper we briefly consider:

- how the international outlook has evolved (chapter 1)
- the PNG Government's revised fiscal position (chapter 2)
- specific tax changes set out in the Budget (chapter 3)
- observations for 2022 and beyond (chapter 4).



# 1. The PNG Economy

In this chapter we discuss the global economic environment (section 1.1) and then consider the updated domestic economic outlook as presented in the 2023 Budget (section 1.2).

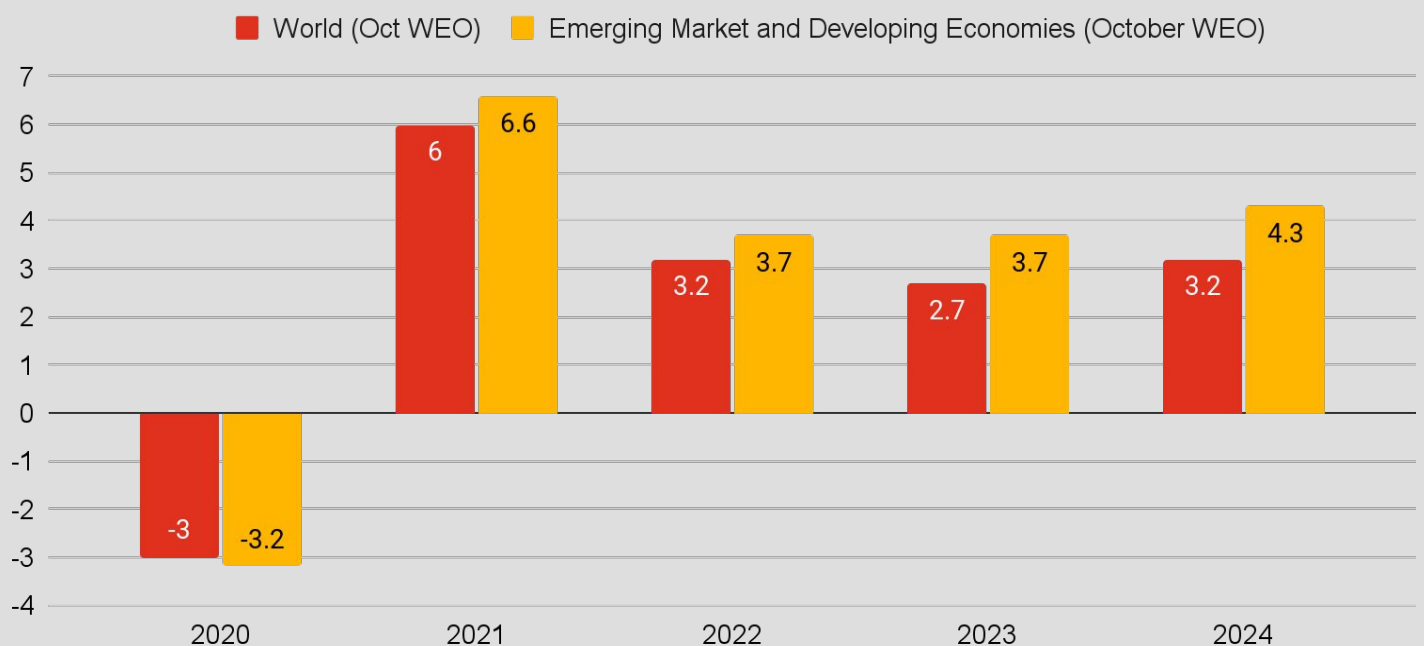
## 1.1 The global economic environment

The world has entered a challenging and more volatile period. The relief as international economies recovered from the pandemic was short lived. The global economy now faces three powerful forces: War in Ukraine, significant inflation pressures that are broadly based, and a sharp slowdown in China. In addition, climate and ecological changes are impacting a number of regions across the globe.

Figure 1 shows the recovery from the pandemic in 2021, and more moderate world growth and emerging and developing economies growth projected from 2022. The IMF notes that 'persistent and broadening inflation pressures have triggered a rapid and synchronized tightening of monetary conditions, alongside a powerful appreciation of the US dollar against most other currencies'.



Figure 1: IMF World GDP and Emerging market and developing economies GDP (%)



Source: IMF WEO October



Russia's war in Ukraine has heightened geo-political tensions and is destabilising the global economy. Gas prices in Europe have increased fourfold since 2021. The conflict has also disrupted food prices, the impact on staples for lower income households is significant. Inflation is expected to peak in 2022, but will remain elevated for longer than expected declining to 4.1 per cent by 2024.

Tighter monetary policy and financial conditions will slowly work through the global economy over the next 12 months gradually putting downward pressure on demand and reducing inflationary pressure.

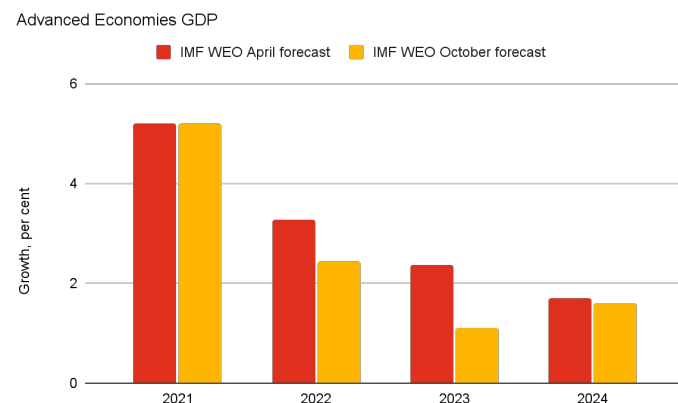
The global environment is creating significant challenges for emerging and developing economies. The sharp appreciation of the \$US adds significant domestic price pressures and creates cost of living pressure for households.

Capital flows have not recovered to pre-pandemic levels, and many developing economies are in or close to debt distress. Downside risks to the global economic outlook remain elevated while policy tradeoffs to address the cost of living crisis have become incredibly challenging for many countries.

The IMF notes that 'the risk of monetary, fiscal or financial policy miscalibration has risen sharply as a time when the world economy remains historically fragile and financial markets are showing signs of stress'.

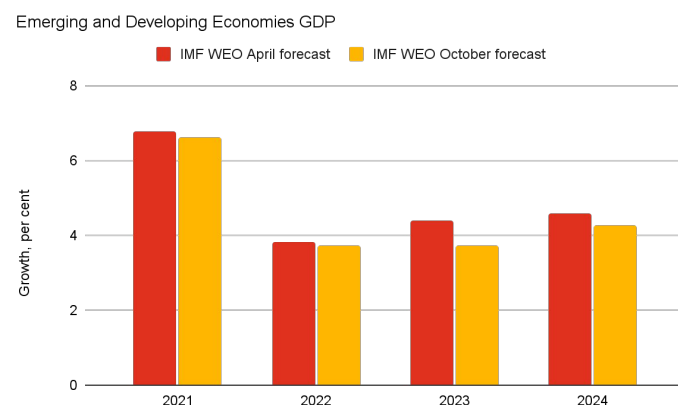
Since the April WEO advanced economy growth has been downgraded by 0.8 percentage points in 2022, and 1.3 percentage points in 2023. Emerging market and developing economies have been downgraded by 0.8 percentage points over 2022 and 2023 (see Figure 2 and Figure 3).

**Figure 2: IMF downgrades growth for Advanced Economies, GDP (%)**



Source: IMF WEO, April - October

**Figure 3: The IMF downgrades growth for Emerging and Developing Economies, GDP (%)**



Source: IMF WEO, April - October



1.2 The domestic economy

From lingering pandemic effects, to managing the fallout from the war in Ukraine, the PNG economy has weathered the challenges of the last three years well. Like its neighbours PNG is now in the process of managing the debt related to the additional pandemic expenditure and managing the inflation impacts on households.

The inflation impacts from the war in Ukraine and higher global inflation are also having significant impacts on the cost of living for every day PNG households. These are shaping up as the key challenges for the PNG Government in 2023.

The PNG Government has a Budget Repair and Reconstruction Plan

The PNG economy recorded modest growth of 0.1 per cent in 2021 (see Figure 4). The 2022 Budget estimates that the PNG economy will grow by around 4.6 per cent in 2022. Growth is then expected to moderate to 4.0 per cent in 2023.

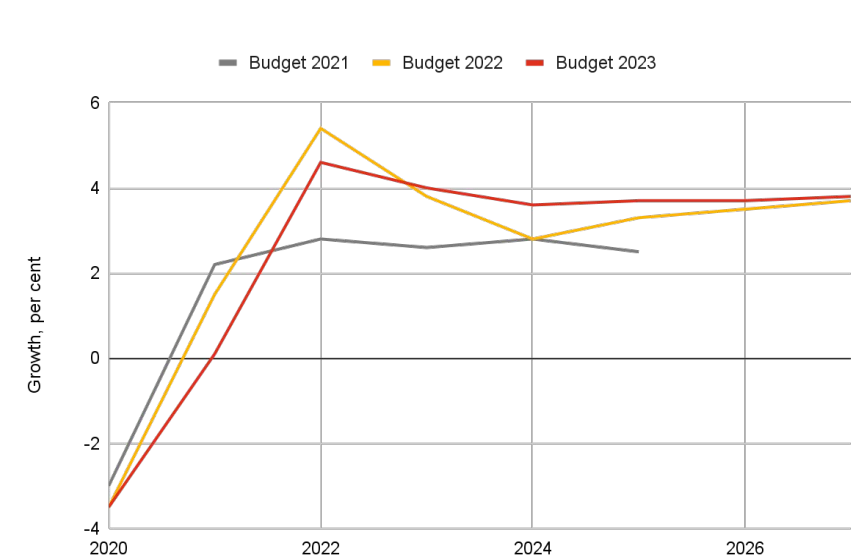
Domestic economic growth

The PNG economy recorded modest growth of 0.1 per cent in 2021 (see Figure 4). The 2023 Budget estimates that the PNG economy will grow by around 4.6 per cent in 2022. Growth is then expected to moderate to 4.0 per cent in 2023. From 2024 growth is expected to average around 4¾ per cent over the medium term. This is slightly above the IMF estimates and assumes that the government's plans to increase human capital formation, and improve the delivery of essential services will yield a growth dividend in the medium term.

The IMF projects that medium term growth will settle at around 3 per cent (medium term growth is the estimate for the productive capacity of the current structure of the PNG economy).



Figure 4: PNG Real GDP (%) growth, Budget 2021, Budget 2022, Budget 2023



Source: Budget 2020, 2021 & 2022

The PNG forecasts are broadly in line with the IMF forecasts in the near term, changes largely reflect updated data relative to what was available to the IMF in May 2022 (see Figure 5). The IMF Article IV projections also provide a sense of the current medium term capacity of the non-resource economy to generate growth. The PNG budget presents a slightly stronger picture for medium term growth reflecting an assumption that human capital development and spending on essential services will boost medium term potential growth to be above the IMF estimates.



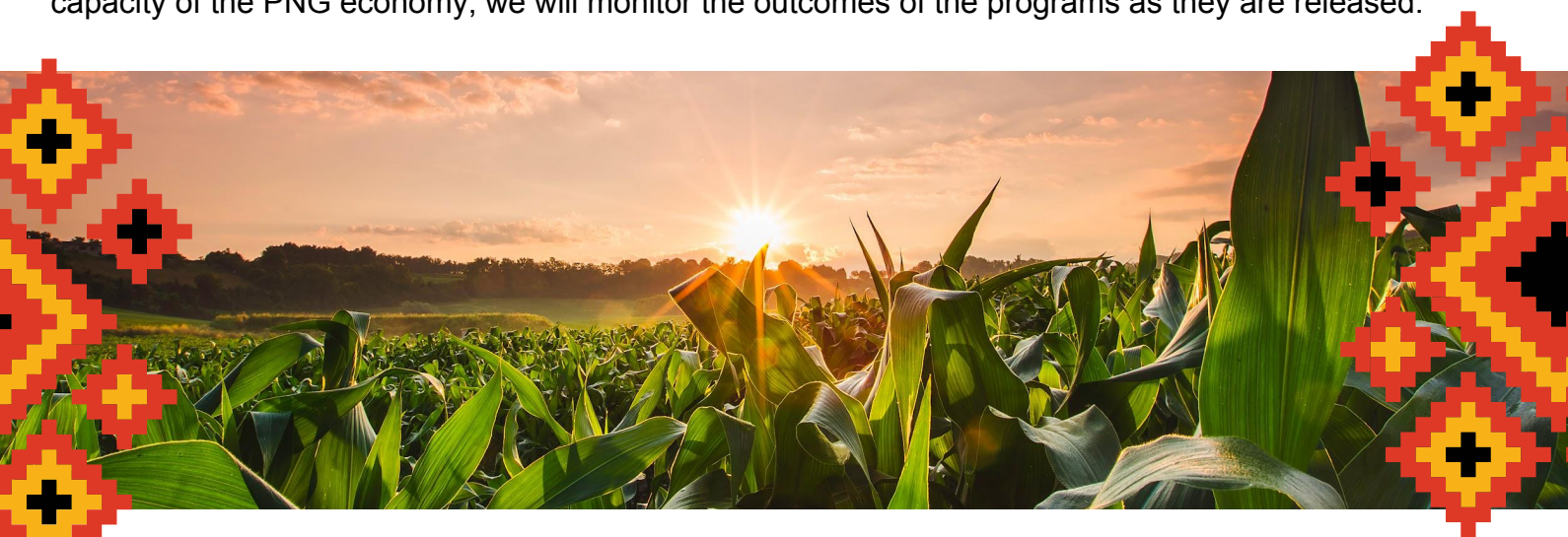
The IMF estimates of the medium term projections for the resources and the non-resources sectors of the PNG economy are important. They provide a sense of the speed limits for growth. In the resources sector for example, the medium term projections do not incorporate estimates of future or new resource projects, or their output. So resources sector GDP growth declines to near zero from 2024, this is updated as new information on growth in output and investment becomes available.

The non-resource sector is projected to grow by around 4 per cent a year in the medium term, while GDP growth is expected to grow by around 3 per cent. Growth in the non-resources sector is critical if the PNG Budget is to meet the aspirational targets to raise revenue and reduce debt.

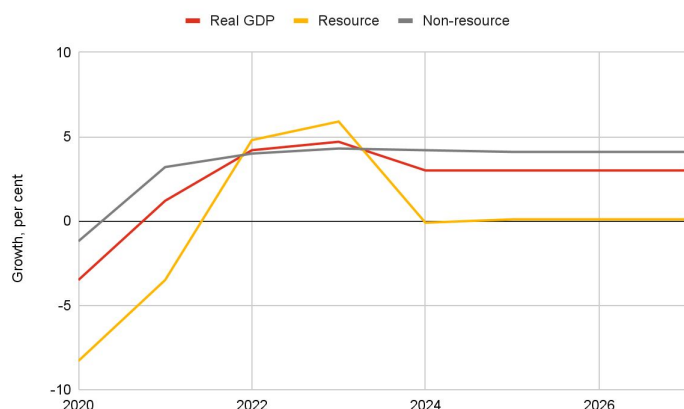
Growth in GDP and the non-resources economy (see Figure 6) are expected to improve solidly in 2022. Data from the BPNG liaison program indicates that sales increased solidly in the March quarter 2022 (up by 7.6 per cent, nominal) although this was lower than sales estimates for December 2021 which increased by 19.1 per cent. However, excluding the sales declined in March by 1.9 per cent.

However, the outbreak of the war in Ukraine has raised concerns of a slowdown in growth in the non-resource economy as prices have risen sharply for households. The Government's household assistance program was designed to buffer the impact of sharp increases in fuel and other consumer staples. The 2023 Budget provides an extension to this program of assistance in 2023.

Beyond 2022 activity in the economy is expected to return to a more modest growth path in line with potential in the economy. The PNG Budget's 10 point plan is designed to improve the productive capacity of the PNG economy; we will monitor the outcomes of the programs as they are released.



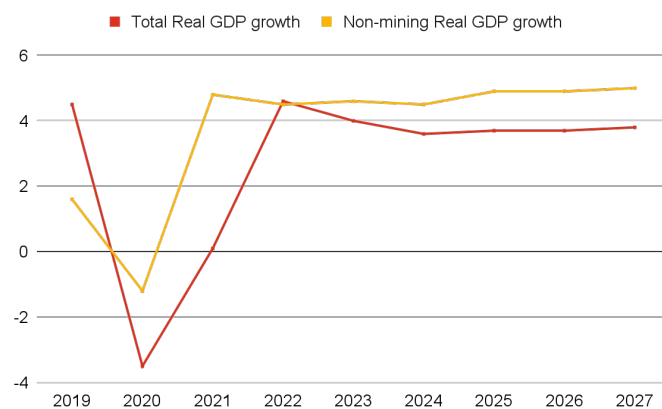
**Figure 5: IMF forecasts real GDP 2020- 2024**



Source: IMF Article IV 2022, GDP components of growth

Note: The IMF (and the PNG Budget) hold levels of productive capacity in the resources sector constant in the medium term..

**Figure 6: Real GDP growth in the non-mining sector and the total economy (%)**

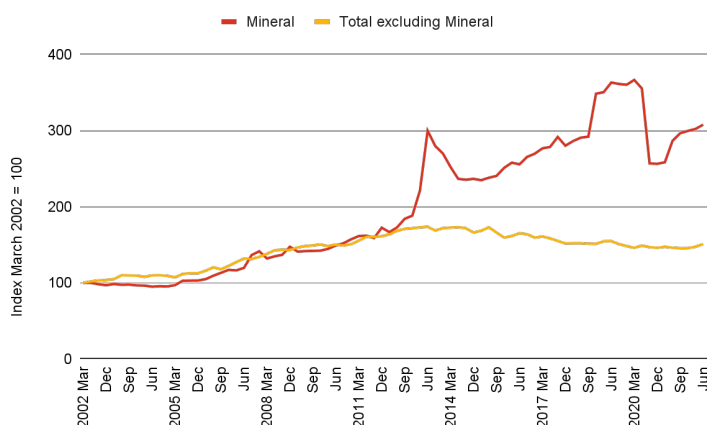


Source: Budget 2022

## Employment

The Bank of PNG's quarterly employment survey, as shown in Figure 7, clearly indicates the significant hit to employment in the minerals sector in the most recent data from COVID-19. As documented in last year's MYEFO, this contraction was triggered by a 'significant reduction in the Ok Tedi Mine production due to COVID-19 impact and a fire at a mill in December 2020, the delayed operation of Porgera mine and the unexpected closure of Simberi mine'. The latest data (March quarter 2022) shows employment in the minerals sector has started to come back on line and is now just above 2019 employment levels. Total employment excluding Minerals employment is held down by slower growth in a number of sectors (see Figure 9).

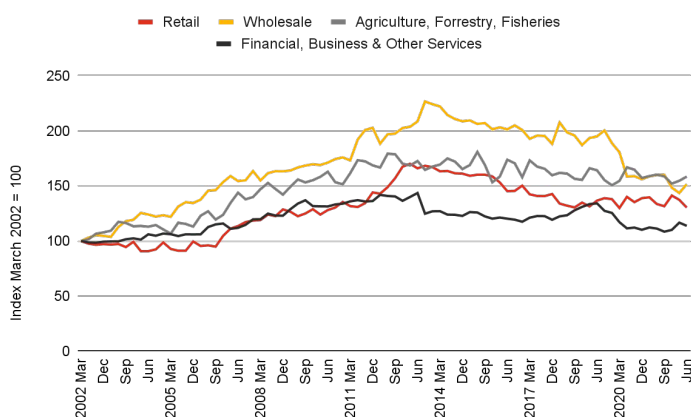
**Figure 7: Employment index (March 2002 = 100)**



Source: BPNG Employment Index 2022

Treasury (2021), Mid-Year Economic and Fiscal Outlook (MYEFO) Report, p.4

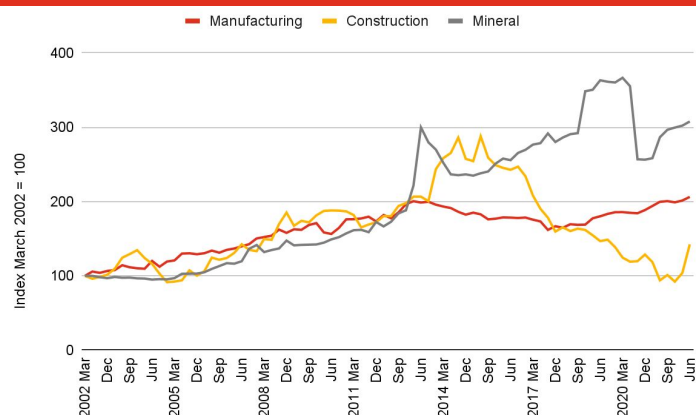
**Figure 9: Employment index (March 2002 = 100)**



Note: March Qtr 2022 data is provisional  
Source: Bank of PNG

The PNG 2023 Budget notes that total employment in the formal private sector improved in 2022 due to fresh recruitment in both mineral and non-mineral sectors as business operations and activities ramped up to meet production targets (to cater for post-COVID demand). According to BPNG's provisional employment statistics for June quarter of 2022, total employment increased by 3.7 per cent through the year from June 2021 to June 2022 driven by an increase in the mineral sector by 7.4 per cent and non mineral sector by 3.2 per cent.

**Figure 8: Employment index (March 2002 = 100)**



Note: March Qtr 2022 data is provisional  
Source: Bank of PNG

Figure 8 indicates the sectors of the economy that have been supporting employment growth in 2022. The Construction sector has seen employment improve recently; Manufacturing has shown a solid increase in employment since around 2018, and the Mining sector has seen employment levels return to be just above 2019 levels.

Figure 9 shows the sectors of the economy that have retained largely stable employment levels, Finance, Business and Other Services, Retail, Agriculture, Forestry and Fisheries. The Wholesale sector has seen employment decline since mid-2019 and levels have not yet recovered.



## Inflation

Inflation pressures have increased in PNG in 2022, reaching 5.9 percent over the year to the March quarter 2022. This reflected both higher headline inflation and strong growth in the underlying measures of inflation (Trimmed Mean CPI Index of inflation) see Figure 10.

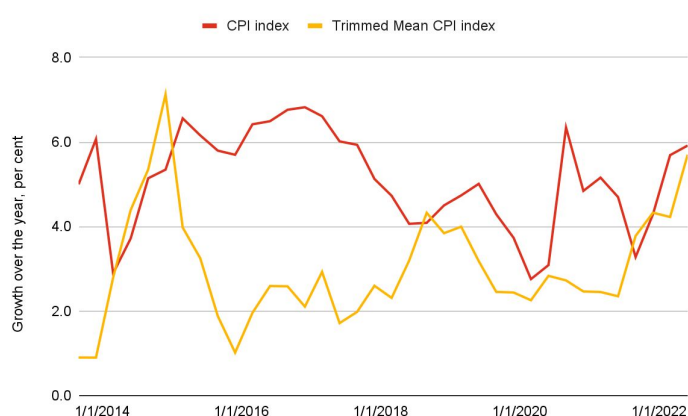
The PNG 2023 Budget notes that inflation is projected to average at 5.7 per cent in 2023 as inflationary pressure is expected to subside (see Figure 11).

Internationally, slower growth in inflation will reflect monetary policy tightening by central banks, and a potential global recession, which may also reduce inflationary pressures for imported goods entering PNG. The projected fall in the global oil price is also expected to also put downward pressure on prices of goods and services.

Domestically, the Government's extension of the fiscal relief measures for another six months in 2023 will continue to mitigate the impact of higher fuel prices on domestic inflation.

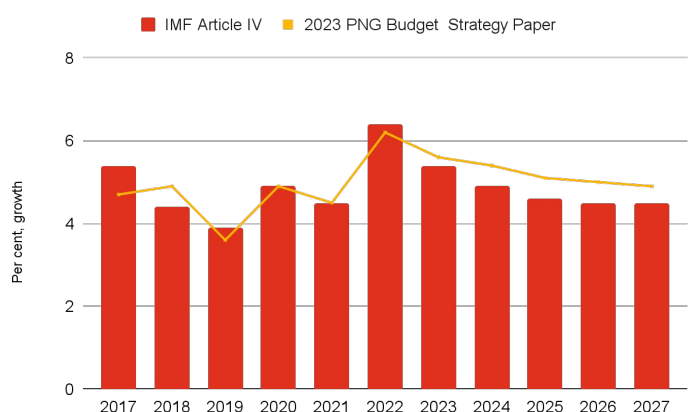
Over the medium term, inflation is projected to average around 5.2 per cent in line with the Government's macroeconomic stability objective.

**Figure 10: Inflation CPI, Index and Trimmed Mean, growth over the year, per cent**



Source: Bank of PNG

**Figure 11: PNG inflation projections**



Source: Budget 2022, IMF, IHS Markit

COVID-19 related disruptions have increased freight costs and transit times in both the global shipping and airfreight industries. Freight costs have eased in 2022 but they remain elevated and will continue to remain above average well into 2023.



## Foreign exchange

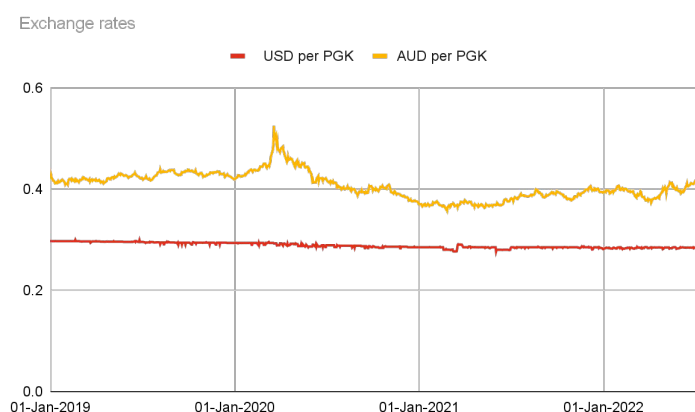
By and large, the Kina should move broadly in line with major trading partners' currencies (Australia, New Zealand, Japan, etc).

However, over 2022 and in previous years (see Figure 12) we have seen:

A flat USD/PKG relationship as the Bank of PNG intervened in the foreign exchange market.

Appreciation of the Kina against the Australian dollar. This reflects cross-currency movements; as the US dollar appreciated against the Australian dollar, so the Kina appreciated against the Australian dollar given the flat Kina/USD relationship

Figure 12: Exchange rates for the Kina (PGK)

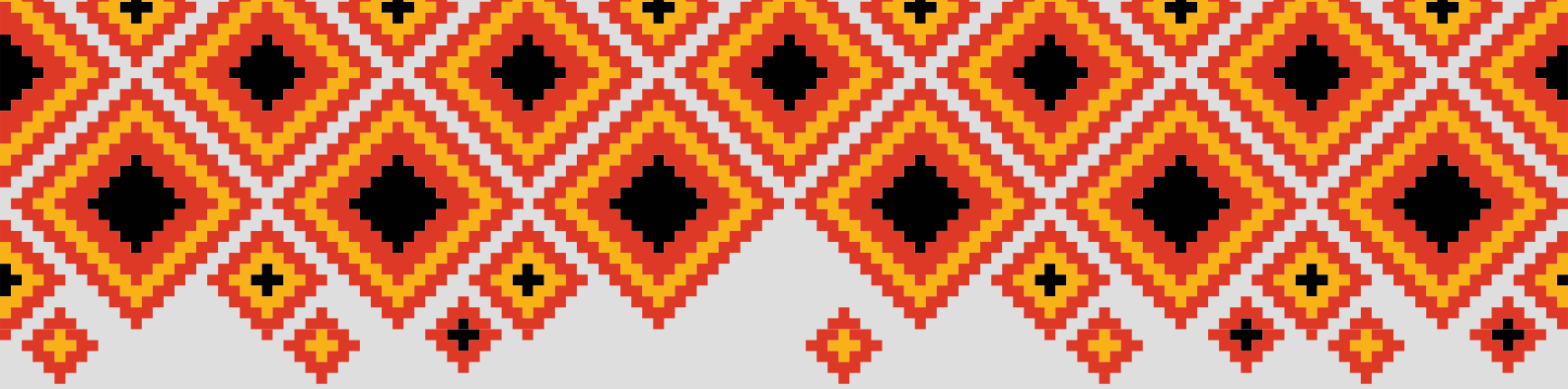


Source: Reserve Bank of Australia, [Exchange rates.org](https://www.rba.gov.au/exchange-rates/)

As the BPNG maintains the trading range, currency availability, and 'getting foreign exchange flowing more freely' remains one of PNG's key challenges.

To cope with the shortages of foreign reserves, over the past six years, there has been rationing of reserves being made available to the broader PNG economy. The rationing policy has focused on allowing for priority imports such as food, and has created significant backlogs in import funding and arrears on foreign payments by firms. Profit repatriation by any firms outside the extractive sectors is also significantly restricted, frustrating established foreign investors, and deterring new potential investors.





We have previously commented that the measures under last year's Budget would both assist and harm the availability of foreign exchange as:



access to external financing will provide an injection into foreign exchange reserves that will facilitate the easing of the foreign exchange imbalance, but



the fiscal deficit financing under a quantitative easing (QE) program run by BPNG will have the opposite impact on FX reserves.

Indeed, the previous years budget papers note that 'legacy issues such as foreign exchange shortages will continue to be impediments towards the improved growth of the business environment in the non-mineral sector'.

The Budget reflects that the FX shortage has remained unresolved since 2014 and that this continues to weigh on economic activity, particularly in the non-resource sectors. If these issues persist into 2023, there is a risk that economic growth projections will not be achieved, impacting business sentiment, income, employment and service delivery.

It will be important for the Treasurer to continue to advocate for greater FX convertibility to reduce the risk that growth estimates are not met as non-resource growth is critical to driving stronger revenue growth in the medium term to get the budget back to surplus.







## 2. The Government's Fiscal Position

Table 3: Key fiscal indicators\

	2022 Budget 2022	MYEFO 2022 2022	2023 Budget 2022	2023 Budget 2023
Revenue (K,mill)	16,190.2	17,389.0	17,389.1	19,582.0
Expenses (K,mill)	20,174.8	23,373.6	23,373.6	24,566.9
Deficit (K,mill)	5,984.7	-5,984.7	-5984.5	-4,984.9
Deficit % GDP	-5.9	-5.4	-5.6	-4.4
Gross debt (K,mill)	52,765.2	52,765.2	54,157.7	59,142.6
Debt % GDP	51.9	47.8	51.5	52.3
Interest costs (K,mill)	2,324.4	2,324.4	2,324.4	2,511.0



**Table 4: 2023 Budget Revenue Details (Kina, million)**

	2021 Actual	2022 Supp. Budget	2023 Budget	2024 Proj.	2025 Proj.	2026 Proj.	2027 Proj.
<b>Total Revenues and Grants</b>	<b>13,860.4</b>	<b>17,389.1</b>	<b>19,582</b>	<b>20,498.8</b>	<b>22,226.8</b>	<b>25,123.7</b>	<b>28,368.7</b>
Total Revenue (as % of GDP)	15	16.1	17.3	16.9	17.1	18.1	19.5
<b>Taxes</b>	<b>11,129.4</b>	<b>13,831.5</b>	<b>14,899.6</b>	<b>15,813.6</b>	<b>17,196.6</b>	<b>19,414.9</b>	<b>21,940</b>
Taxes on income, profits, and capital gains	6,356.1	8,841.9	8,935	8,899.9	9,008.8	9,677.4	10,816.3
Taxes on payroll and workforce	0.80	-	-	-	-	-	-
Taxes on goods and services	3,993.7	4,130.2	5,015.3	5,888.1	6,796	7,622.3	8,613.9
Taxes on International trade and transactions	778.8	859.4	949.4	1,025.6	1,391.9	2,115.2	2,509.9
<b>Grant</b>	<b>2,088</b>	<b>1,824.9</b>	<b>2,024.9</b>	<b>2,074.9</b>	<b>2,124.9</b>	<b>2,175.2</b>	<b>2,224.9</b>
<b>Other Revenue (Non-Tax)</b>	<b>643</b>	<b>1,732.7</b>	<b>2,657.4</b>	<b>2,610.2</b>	<b>2,905.2</b>	<b>3,533.6</b>	<b>4,203.8</b>
<b>Total Revenue (excluding grants)</b>	<b>11,772.4</b>	<b>15,564.2</b>	<b>17,557</b>	<b>18,423.8</b>	<b>20,101.9</b>	<b>22,948.5</b>	<b>26,143.8</b>

## 2.1 Revenue

An objective of successive governments has been to raise the level of taxes collected to better enable PNG to invest in physical and human capital to advance development goals.

The 2023 Budget projects tax revenue to grow to be K19.6 billion or 17.3 per cent of GDP in 2023. Revenue is projected to slowly increase at a faster rate than economic growth to be around K28.4 billion or 19.5 per cent of GDP by 2027.

Table 4 indicates that PNG's tax revenue is expected to increase by 7.7 per cent amounting to K14,899.6 million (13.2 per cent of GDP) in 2023 on the back of the anticipation of global commodity price moderation and dissipation of pent-up global demand. The non-tax revenue is expected to increase strongly by 53.4 per cent to K2,657.4 million (2.3 per cent of GDP). Consequently, Total Revenue and Grants is projected to increase by K2,192.9 million or 12.6 per cent to K19,582.0 million (17.3 per cent of GDP).



## 2.2 Expenditure

The 2023 Budget projects expenditure to grow to be K24.6 billion or 21.7 per cent of GDP in 2023 (see Table 5). Expenditure is projected to grow slightly slower than the pace of economic growth to be around K28.2 billion or 19.4 per cent of GDP by 2027. This in essence is the central plank of this Government's fiscal strategy, containing expenditure growth while growing the revenue pie.

Total expenditure for 2023 is set at K24,567.0 million, consisting of K21,386.0 million in GoPNG-funded expenditure and K3,180.9 million in expenditure supported by development partners, which comprises of K2,025.0 million in donor grants and K1,156.0 million in concessional loans. The 2023 expenditure target is K1,180.7 million or 5.0 per cent higher than the 2022 Supplementary Budget estimate, and 10.8 per cent higher than the original 2022 Budget estimate.

**Table 5: 2023 Budget Expenditure Details (Kina, million)**

	2021 Actual	2022 Supp. Budget	2023 Budget	2024 Proj.	2025 Proj.	2026 Proj.	2027 Proj.
<b>Total Expenditure</b>	<b>20,131</b>	<b>23,374</b>	<b>24,567</b>	<b>24,468</b>	<b>25,689</b>	<b>26,898</b>	<b>28,262</b>
% of GDP	21.8	21.7	21.7	20.2	19.8	19.4	19.4
<b>GoPNG Expenditure</b>	<b>18,268</b>	<b>21,799</b>	<b>22,542</b>	<b>22,393</b>	<b>23,564</b>	<b>24,723</b>	<b>26,037</b>
% of GDP	19.8	20.2	19.9	18.5	18.2	17.8	17.9
<b>Operational Component (PE and G&amp;S)</b>	<b>10,575</b>	<b>12,064</b>	<b>12,260</b>	<b>12,780</b>	<b>13,641</b>	<b>14,549</b>	<b>15,498</b>
% of Total Expenditure	52.5	51.6	49.9	52.2	53.1	54.1	54.8
<b>Interest Payment</b>	<b>2,255</b>	<b>2,324</b>	<b>2,511</b>	<b>2,615</b>	<b>2,692</b>	<b>2,711</b>	<b>2,691</b>
% of Total Expenditure	11.2	9.9	10.2	10.7	10.5	10.1	9.5
<b>Capital Investment Component</b>	<b>7,301</b>	<b>8,985</b>	<b>9,796</b>	<b>9,072</b>	<b>9,356</b>	<b>9,637</b>	<b>10,073</b>
<b>Total Expenditure (excluding GoPNG Expenditure)</b>	<b>20,131</b>	<b>23,374</b>	<b>24,567</b>	<b>24,468</b>	<b>25,689</b>	<b>26,898</b>	<b>28,262</b>

Source: Department of Treasury



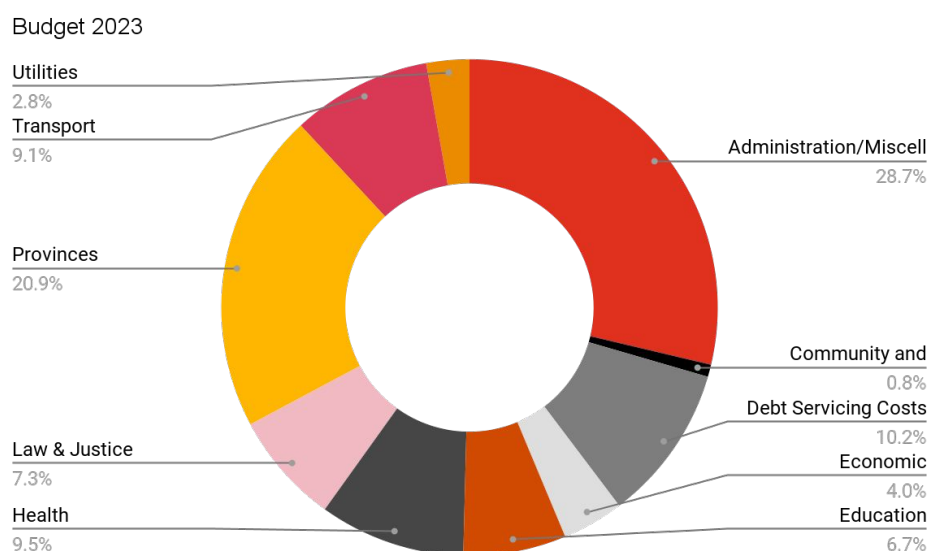
Table 6 and figure 13, show expenditure as a share of the total budget it is important to note that debt servicing costs are now around 10 per cent of the budget, significantly larger than spending on education and spending on Health. To meet development goals this needs to reverse. The Government is aware of this and is currently in the process of attempting to achieve better outcomes. The Budget is an important document that allows us to check in on how the government's achievements stack up against the objectives. Progressively, the table below should show lower debt interest costs and higher spending on education and health as this will increase the productive capacity of the economy and PNGs people.

**Table 6: Expenditure by sector as a % of the total budget**

	Budget 2019	Budget 2020	Budget 2021	Budget 2022	Budget 2023
Administration/Miscellaneous	25.2	21.5	27.3	30.2	28.7
Community and Culture	0.9	0.7	0.5	0.7	0.8
Debt Services	12.3	12.5	12.0	10.8	10.2
Economic	4.6	4.8	3.4	4.4	4.0
Education	8.5	9.0	5.6	6.6	6.7
Health	9.6	10.4	8.9	11.9	9.5
Law & Justice	8	9.7	6.5	6.5	7.3
Provinces	19	23.7	20.1	19.8	20.9
Transport	8	6.4	11.0	6.7	9.1
Utilities	3.8	1.2	2	2.3	2.8

Source: Budget 2019-2022

**Figure 13: Expenditure in 2023 by sector as a % of total expenditure (net of Debt Servicing)**



Source: Budget 2022

## 2.3 Debt

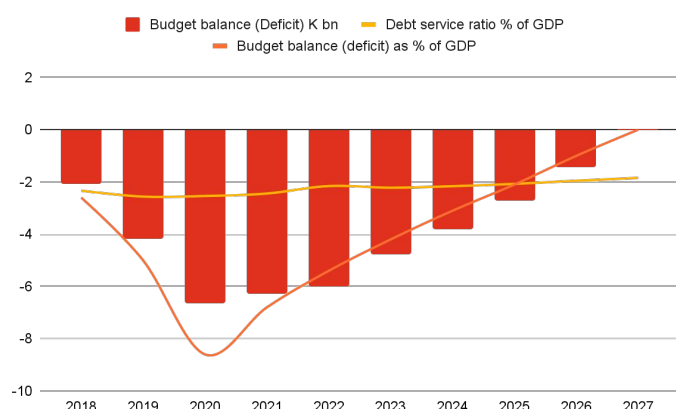
Cost of debt has decreased in recent years as the Government has focused on meeting requirements for concessional loan agreements, this has helped to bring down the costs of domestic borrowing with a falling yield curve at longer end maturities.

In 2023, with total revenue of K19,582 million and total expenditure of K24,566.9 million, the resulting fiscal deficit is K 4984.9 million (or 4.4% of GDP).

Figure 14 shows the path of projected deficits in millions of Kina and as a percentage of GDP. We have also included the debt servicing ratio as a per cent of GDP (averaging a little over 2 per cent of GDP in 2023, before declining to a little under 2 per cent of GDP by 2027).

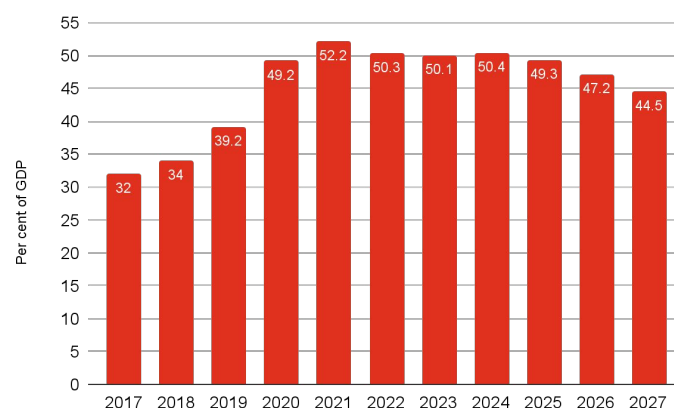
This is an ambitious path of debt and deficit reduction (see Figure 15). However, the Government has to date stuck to its plans and has in fact achieved stronger declines in deficits than it previously projected. In part this reflects stronger commodity prices and revenues, however, the Government has still out performed its previous projections and should be commended..

**Figure 14: Net borrowing (Kina, million and % of GDP)**



Source: Budget 2023

**Figure 15: Debt as a percentage of GDP 2023 Budget**



Note: 2020 are actuals and 2021 refers to the supplementary budget  
Source: Budget 2022

Importantly, the goal to reduce debt will over time reduce the burden of interest costs as a share of the nominal economy. A lower interest rate, through refinancing with multilateral organisations, is also helping the Government to lower debt servicing costs (see Figure 16).

**Figure 16: Debt servicing costs**

	2020	2021	2022	2023	2024	2025	2026	2027
Debt servicing (Kina million)	2064.4	2270.8	2,324.0	2511.0	2615.0	2692.0	2711.0	2691.0
Debt servicing as a % of total expenditure	11.5%	11.6%	10.5%	10.2%	10.6 %	10.5%	10.1%	9.5%

Note: 2020 refers to the 2020 Supplementary Budget  
Source: Budget 2023





## 3. Taxation Developments and Amendments

The 2023 Budget continues to be framed in the context of the Medium Term Fiscal Strategy, and with the ongoing goal of strengthening revenue collection to support the overall goals of deficit reduction. The goal of a surplus by 2027 will rely on revenue collection increasing at a higher rate than expenditure. In broad terms for 2023, the Treasurer is aiming at allowing growth in the expenditure side of the budget at approximately 10% (against the 2022 budget), and matching this with almost 20% growth in revenue (against the 2022 budget). However, with the final revenue outcomes for 2022 expected to exceed the 2022 budget, the growth from the supplementary budget is anticipated as a more modest 7.7%. Further it should be acknowledged that the most significant growth in the current budget comes from non-tax revenues, rather than tax collections alone. The budget appropriation for IRC and Customs does not significantly increase, so the basic expectation will be that the revenue collection agencies will need to 'do more with the same'.

### **Legislative changes**

There are limited tax changes introduced as part of this year's budget. The most significant represent part of the government's commitment to address cost of living pressures and identifying some relief for private households in particular.

### **Cost of living pressures**

These changes have targeted the tax free thresholds for salary and wages tax. During 2022 the government implemented a temporary increase in the tax free threshold from PGK12,500 per annum to PGK17,500 per annum. The current budget further extends this relief, with a temporary increase through to PGK20,000. This change is scheduled to end on 31 December 2023, and presumably to revert to the basic threshold of PGK12,500 at that time. The Treasurer highlighted that this measure will benefit approximately 170,000 individuals in formal employment. The measure comes with an estimated cost of PGK280M.

Another cost of living measure is the extension of a current temporary measure eliminating excise duties on fuel products (diesel, petrol and zoom) for a further six months from 1 January 2023. This measure was originally introduced for six months in 2022 and has already been extended for two months through to 31 December 2022. The measure eliminates the fuel excise except for a number of listed entities. The measure is estimated to cost the budget PGK150M for 2023. The corresponding temporary removal of GST from fuel products for households that was part of the 2022 measures has not been extended, but will expire on 31 December. GST will therefore apply normally to fuel products in 2023.

### **Tax on the banking sector**

The most significant revenue raising measure within the tax system is the introduction of an increased corporate income tax rate for commercial banks. Rather than the normal tax rate of 30%, a tax rate of 45% will now be imposed on the four commercial banks operating in PNG. This measure is scheduled to take effect through updating the Income Tax, Dividend (Withholding) Tax and Interest (Withholding) Tax Rates Act. from 1 January 2023. Clearly this is a very targeted measure and is expected to raise additional revenue of PGK 50M.

The budget has now repealed the Market Concentration Levy and the Additional Company Tax introduced last year will no longer apply.



### Export duties

In support of the government's undertakings with respect to moving to more downstream processing for the forestry sector and banning the export of round logs, the export duty on unprocessed logs has been further increased by 20%. The expected revenue from this measure is set to be contributed to the UN Biodiversity and Climate Trust Fund for PNG, rather than going into consolidated revenue.

### Customs and excise

Within the scope of sin taxes, the government has looked again at the excise duties for certain types of mixed drinks with high alcohol contents. From 1 January the excise has been increased almost five-fold.

There are also a significant number of changes to the schedules associated with the Customs Tariff Act. These are amendments to more than 350 tariff classification codes to bring the act in line with the latest update of the Harmonised System. The existing act was aligned with the Harmonised Schedule as of 2017, but has now been updated to a 2022 version of the standardised tariff codes. The expectation is for these amendments to be revenue neutral.

### Income Tax Act reform

The rewritten Income Tax Act was not in the Bills presented to Parliament.

The Treasury had advised in consultation that the effective date of the new Tax Act would be 1 January 2024, but that the Act would be introduced to Parliament for passage with the 2023 National Budget. There is no commentary or explanation provided on why this did not occur, and timing of the future legislative passage is unknown.

### The importance of non-tax revenue.

The key to deficit reduction in this year's budget is ensuring that revenue is growing faster than expenditure in 2023. Revenue is made up generally of tax, non-tax and grant revenue.

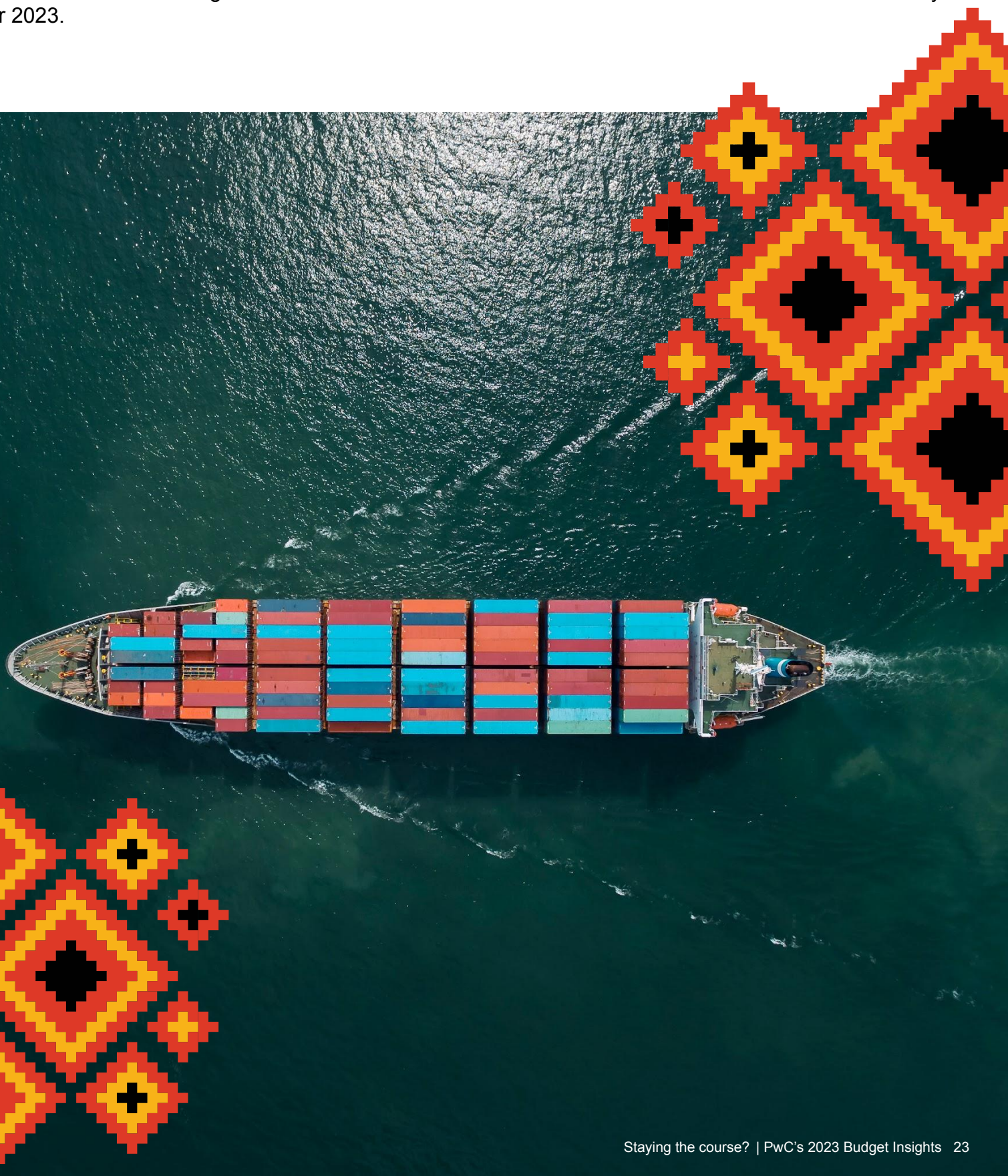
Grant funding continues to be an important element of financing, and the level of support from foreign governments remains relatively steady year on year. Grants are generally supporting specific programs that are spread throughout different areas of the budget. The primary development partners providing grant funding (in order of magnitude) are Australia, UN, ADB, EU, Japan and China.

However, non-tax revenue is becoming proportionately more important in 2023 with a relatively significant increase expected. There are two key features that support this increase. The primary tool is the introduction of the Non Tax Revenue Administration Bill (NTA). This piece of legislation is a replacement for the Public Money Management Regularisation Act which was originally introduced in 2016 but later found to be unconstitutional. The intent of the NTA is to essentially sweep surplus funds from statutory authorities through to consolidated revenue. The agencies are then funded from allocations out from the centre. The sweep does not apply to State Owned Entities. The revenue impact for 2023 from implementing this legislation is indicated as PGK550M, which represents a significant proportion of the anticipated growth in revenue.



The second substantial contributor to non tax revenue are dividends from State Owned Entities and in particular from Kumul Petroleum Holdings Limited and Ok Tedi Mining Limited. These are key entities operating in the mining and gas sectors. The anticipated increase in funding for the 2023 budget arising from SOE dividends exceeds PGK1 Billion. The mechanism by which this increase has been achieved is through an expectation that significantly higher dividends will be declared by the entities. For OTML, there is a further assumption that 85% of the total dividends to be declared will be directly routed to consolidated revenue, rather than to its shareholders.

While the economic estimates being used for the budget take into account future strong commodity prices, including significant estimated dividends from operated and non-operated projects in the resource sector into budgeted non-tax revenue is noted as one of the risks to macroeconomic stability for 2023.







## 4. Observations for 2023 and beyond

Papua New Guinea (PNG) has navigated the pandemic well. The government has committed in the 2023 Budget to maintain its focus on growing the economy, reducing debt burdens and improving fiscal flexibility and will continue to invest in core programs to improve the wellbeing of the PNG people and to improve the productive potential of the economy.

Expanding the PNG revenue base is clearly an important part of the Government's plan to return the budget to surplus, however, it will be important to balance the need to grow the economy with the need to broaden the revenue base. This will be an important balancing act.

This is the first budget following the election and it is important to see the Government remains committed to growth and budget repair despite challenging conditions. Revenues have increased reflecting tight global markets for a number of PNG's resource exports. A portion of this windfall has helped to reduce deficits and to ease cost of living pressure on households.

Inflation pressure from the war in Ukraine created significant cost of living pressures for households. The Government's household assistance package is helping to ease the impact on households and this is also easing (if temporarily) inflation in PNG. And there is likely to be further flow through of imported inflation in early 2023 as prices in Australia remain elevated. Australia is a key source of imports for PNG.

Expenditure efficiency and governance issues have been identified as important issues for this term of government. The budget papers have specifically identified the need to address challenges with the governance around public expenditure. Widespread failures and non-compliance by agencies with respect to providing quarterly expenditure reports, lack of project monitoring and non-payment of obligations are all under increased scrutiny. With the need to maintain budget discipline throughout the government's 13 year plan to eliminate debt, this focus is certainly warranted. The challenge will continue to be on implementing the monitoring and evaluation mechanisms already in place and newly proposed.

Performance of SOEs is also under renewed scrutiny. The government set out a plan for reform and improvement of State Owned Entities from 2020-2022 supported by an ADB funded project. The reforms targeted strengthening the requirements around financial reporting and ensuring skills based board appointments. With an increasing reliance of the budget on dividends from SOE's the success of the reform program and the management of SOEs will become even more critical, although the documented shortfalls in expected against delivered dividends in the years from 2019-2022 are significant.





The PNG Budget commentary has been prepared to provide an overview of the general issues raised in the 2023 Budget. It does not cover exhaustively the subjects discussed. When specific issues occur in practice it is necessary to refer to the laws and regulations and to obtain appropriate professional advice.

While every care has been taken in the preparation of this publication, no warranty is given as to the correctness of the information it contains and no liability is accepted for any statement or opinion, nor for any error or omission.



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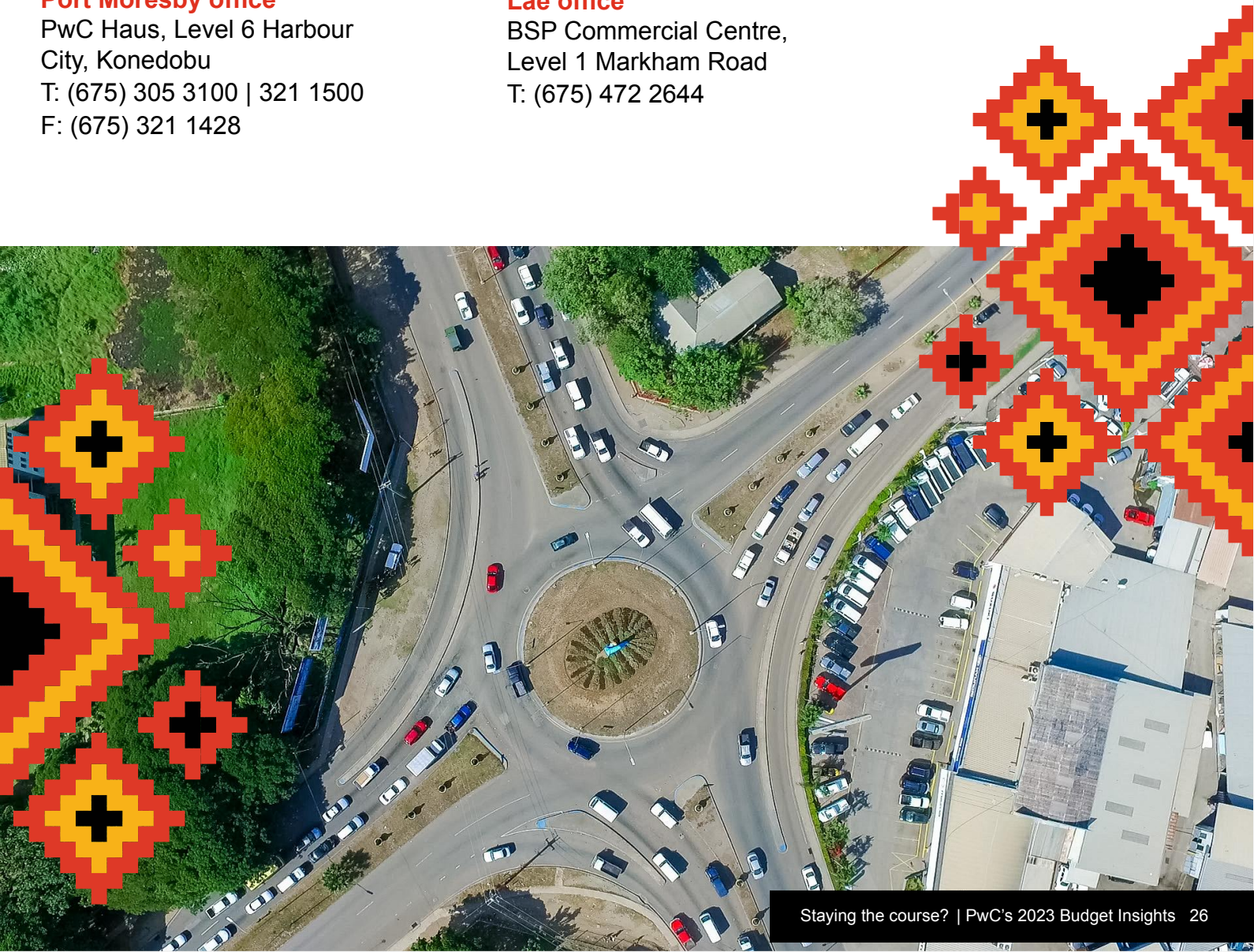
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