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More on debt: Focus on PNG

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It is budget season for Pacific island countries (PICs).

For Fiji, Papua New Guinea (PNG), Solomon Islands and Vanuatu, the fiscal year is the same as the calendar year: January to December. For the other two major countries, Samoa and Tonga, fiscal year differs from the calendar year. It is from July to June.

While PNG's 2014 budget will be presented to the parliament on November 19, Vanuatu's 2014 budget presentation would be in early December.

Fiji's 2014 budget was unveiled last week. It laid emphasis on free education for all students from primary to secondary school levels and loan and scholarship assistance for all tertiary students. The budget allocation for education is $64.5 million and wage increases are a close $93 million.

Expected fall in Fiji's debt ratio

Despite these sizeable provisions, the net deficit, which is the difference between revenue and expenditure is estimated to be small compared to past years. The reasons behind the modest budget deficit are based on two optimistic expectations: higher growth of the economy in 2013 and 2014 and increase in revenue.

The growth rate for 2013 has been revised upwards to 3.6 percent from the earlier forecasted rate of 3.2 percent; and the growth rate predicted for 2014 was also raised to 3 percent from the previous forecast of 2.5 percent.

Tax revenue is directly related to rise in national income. The estimated revenue receipts are naturally expected to be high at $2.722 billion. Since the total expenditure is $2.883 billion, the estimated net deficit is $161 million. The estimated 2014 deficit, as a percentage of the forecasted GDP of $8.283 billion, is 1.9 percent. This is less than the revised deficit of 3.5 percent for 2013.

According to latest clarifications by Permanent Secretary, Ministry of Finance, borrowing would be restricted to financing the capital expenditure. As a result, public debt is expected to decrease to 48.3 percent of GDP in 2014 from the estimated 49.3 percent in 2013.

UNCTAD on Debt

Bringing down the debt ratio is very much of current interest.

At the 9th United Nations Conference on Trade and Development (UNCTAD)-sponsored Debt Management Conference held this week in Geneva, UNCTAD Secretary General Mukhisa Kituyi revealed that debt stocks of developing countries had increased by more than 10 percent per annum since the 2009 world economic downturn. However, in 2012 they expanded by 12 percent. Significant growth had enabled them to reduce the average ratio of total debt to GDP from 28 percent in 2001 to 21 percent in 2011. It worsened in 2012 to reach 22 percent of GDP.

Dr. Kituyi noted that stagnation of advanced economies had caused a "sharp contraction of export growth" in developing countries. He cautioned that "high levels of unemployment and a corresponding need for social services had increased government expenses and budget deficits would lead to further rise in budget levels."

Expectations have been raised high by Fiji's 2014 budget on all fronts. The revenue gathering machinery has to work hard. The spending ministries have to prudently devote their increased resource allocations for the purposes they are meant. The goals are clear: the targeted, small deficit and debt ratios.

PNG's economy

The PNG economy is at crossroads.

Its US$19 billion liquefied natural gas (LNG) project is almost complete. Capital inflows are decreasing. Added to this, there has been a rising demand for foreign exchange from manufacturers, wholesalers/retailers and services sectors, and for consumer and capital imports, besides for increased government spending. Consequently, PNG's floating currency, the kina has depreciated considerably. That has raised concerns on inflation front, since prices of critical food imports have gone up.

To halt further depreciation of the kina, the central bank sold US$847 million. Consequently, reserves have declined from US$4.0 billion to US$3.0 billion.

Although depreciation of the kina should help promoting exports, rise in export earnings has been slow. Exports of both coffee and cocoa have decreased during last four quarters. A World Bank report says "the low volumes combined with lower prices reduced the Kina value of coffee and copra exports by almost two-thirds, and cocoa exports by 40 per cent, despite the support to kina receipts from the currency's depreciation".

However, Standard & Poor's ratings agency has rated PNG as stable. The foreign and local currency long-term ratings stand at 'B+', and the short-term ratings at 'B'.

High hopes are pinned on LNG project. According to World Bank, government expects a 26 percent rise in nominal GDP when LNG production starts by mid 2014.The debt ratio would fall below 30 percent of GDP.

In the meanwhile, the challenges remain.

The government has to ensure that 2014 budget has to be fiscally responsible. Any expansionary budget to meet the shortfall in aggregate demand due to the winding down of LNG project would only aggravate the deteriorating current account balance. It would further contribute to inflation.

PNG's Prime Minister O'Neill assured the nation that the budget deficit would be reduced, from the current 7 percent of GDP to less than 6 per cent of GDP. If that happens, the debt ratio would not rise very high. The current ratio is 30 percent of GDP.

Anyway, the government hands are tied. It has to observe the limit imposed by the Medium Term Debt Strategy adopted by the parliament. The limit is 35 percent of GDP in 2013 and 2014.