



Kundu

March 2020



Foreword

As KPMG is the only professional services firm in PNG with dedicated in-house specialists in all of the following areas: internal audit/risk, visa migration, corporate finance, management consulting, IT advisory, fraud investigation as well as tax and assurance, we are well placed to provide a truly multi-disciplined approach to business advisory. We hope you enjoy our regular KPMG Kundu.

KPMG PNG – business as usual

We would like to reassure our clients and the PNG business community that all of our partners, leadership, management and staff are on the ground in PNG and working on a business as usual basis. We are of course taking the necessary health and safety precautions to safeguard our staff during these uncertain times. We also have a business continuity plan in place which will enable us to work remotely within PNG if the need ever arises. Please reach out for new business enquiries.

State owned enterprise reform in PNG by Wayne Osterberg, Director, Advisory Services

There is a strong focus in PNG currently on the reform of the State Owned Enterprises (SOEs). The Government, with the backing of the Asian Development Bank and other multi-lateral agencies, has a determined approach to reform the SOEs, to reduce their fiscal drag on the economy and provide a platform for growth generally, given that the SoE's are integral to the infrastructure and logistics of the nation. This is not a new initiative but economic imperatives are underpinning the renewed focus.

What are the SOEs? These include PNG Power, PNG Ports, Air Niugini, Water PNG, Eda Ranu, Telikom, Motor Vehicle Insurance Ltd, National Development Bank and others. Their holding company is Kumul Consolidated Holdings which holds all government owned commercial assets in trust and manages them to improve commercial performance and underpin economic development.



PNG is not alone in seeking to reform their SOEs – many emerging and developing countries have undertaken reforms since the 1980s and more recently, and closer to home, since the Asian financial crisis of 1997. The experiences have met with mixed success and have followed variations on several themes but the starting point has invariably been corporatisation. This has already happened in PNG. The ADB

has identified that “the SOE reform effort is based on the premise that any commercial enterprise, whether public or private, functions most efficiently when it seeks to maximise profits, operates in a competitive market, is accountable to shareholders and for the use of resources, and reports in accordance with established and accepted financial standards.” An additional premise is that the SOEs manager should have the requisite autonomy and capacity and motivation to respond to market signals.

Successful SOE reform therefore starts with an appropriate legislative framework which provides for the independence of the entities and a regulatory framework which allows competition and appropriate industry oversight. Improved corporate governance, which reduces or removes political interference from the board of directors, has been found to be key to successful reform including having independent board members who bring a diversity of skills and experience. At the heart of board oversight is the quality of information and reporting systems, underpinned by good management information systems and accounting and finance teams.

SOE reforms have often resulted in full or partial privatisation of the respective entities. This process has been met with mixed public popularity which goes to the heart of the Government’s dilemma between balancing the need for the entities that are often integral to the economy, to operating commercially and still providing the requisite services to its nation’s citizens in an affordable manner.

The ADB has identified that there is mounting evidence that privatisation – partial or full – does improve financial and operational performance even though there is often a lag between the short term restructuring pain and the flow on benefits to the public in terms of improved service, and the government, in terms of reduced fiscal drag and increased tax revenues.

Privatisation can take many forms but all require investors or partners of one form or another – equity, debt or technical - and most often a combination of all three. In order to bring in such partners, any process of SOE reform in PNG will need to focus on three critical areas.

- Firstly, and most significantly, corporate governance reform to ensure no political interference in the boards of the entities and the inclusion of strong independent skills. This gives investors comfort that the entity will be allowed to operate effectively.
- Secondly, the entities require strategic technical partners to provide the relevant industry specific skills and experience that give investors comfort that the entity can meet the unique technical requirements of the specific business.
- Thirdly, operational improvements to ensure good accounting and information systems are in place to provide investors comfort that there is effective management of the entities.

These are the minimum requirements to make SOEs investible, which are, at the end of the day, no less stringent than any public company which operates commercially and seeks to offer its shareholders a requisite return on their investment.

Practical advice on the implications of COVID-19 for PNG private, mid-market and emerging businesses.

The recent outbreak of novel coronavirus (COVID-19) has introduced many new challenges to our communities and businesses.

Below is practical advice to help emerging, private and mid-market businesses navigate some of the difficulties they may currently be facing.

Key takeaways:

- Caring for your people's physical and mental wellbeing should be at the core of all actions taken during the COVID-19 outbreak.
- Cash flows and business plans should be managed through assessing supplier and customer status, optimising cash flows and managing loans and funding needs.
- The PNG Government is expected to shortly release a number of economic stimulus measures to help the local economy, following their scheduled meetings with financial institutions and superannuation funds.
- Timely and efficient communication plans for all stakeholders should be implemented.

Caring for and retaining your team

As we navigate these unsettling times, your people's physical and mental well-being should be at the core of your business considerations. While some difficult times may be ahead for many businesses, decisions should be made with compassion towards the people that may be affected.

It is important for all businesses to take steps to protect their team's immediate health. Consider your company's current travel policies and adjust them to reflect the current expert guidance. We know that this is a fast evolving situation so continue to review these guidelines as the advice changes. Restricting face-to-face meetings and considering if those meetings can be held virtually instead is also recommended.

There may be a need for a back-up plan to protect staff that may be impacted either through illness, or the need to protect vulnerable people in their households. A back-up plan could include contingencies for more automation, remote-working arrangements, or other flexible resourcing capabilities to backfill for personnel constraints. Set expectations with your staff and ask them to be prepared to work more agilely across different roles within their teams. With the use of internal and external technology your company can aid collaboration and the ability to work seamlessly from remote locations.

Managing cash flow and business plans

The careful management of cash flows and business plans is important during this period.

Understanding your supplier and customer positions will help you identify risks and opportunities – a simple phone call can help you gain a clearer forward picture. Adjusting your go-to-market strategy to an online sales channel will help your business to continue reaching a market whose movements may be restricted.

Internally, create two new teams to specifically address your business' response communications, and supply chain assessment and risk management. Communication of accurate information should be open and consistent between your key stakeholders. Continued conversations with them will allow you to maintain stakeholder confidence and inform customers who may be impacted by your evolving business response. Your supply chain assessment and risk management teams should be focused on identifying upcoming exposure – ask them to review contracts with key customers and suppliers to understand the liability in the event of supply shortages.

There are some immediate actions that can be taken to manage cash flows. In the short term you should follow up on any customer payments due, particularly from larger corporates, and seek extended credit terms with suppliers. Now is the time to revise cash flows, working capital management and inventory forecasts alongside your new supply and demand predictions to help understand how financial stability may be impacted, also consider this impact in relation to, and restrictions in, access to funding. Have a conversation with your banker to clarify expectations, understand your current loans, including bank covenants, and repayment obligations. They may also be able to help you understand the options if there is a need to raise additional debt or equity.

Communication plans and stakeholder engagement

It is important to keep communications during a crisis timely and efficient. Proactively engaging stakeholders and raising awareness of the changing situation will assist your organisation to effectively navigate new and developing challenges. Your messages to key stakeholders should convey ability, humanity and integrity to ensure confidence and understanding regarding your organisations' actions and responses.

Speaking to your banker today about your current debt obligations, the impact of COVID-19 on your cash flows and what additional assistance you may need in the short to medium term can assist in creating longer term plans. Your insurance policies, including coverage and claims processes, are also important to understand. If your company is listed, address your continuous disclosure and financial reporting obligations moving forward.

If your business is part of a distressed sector, including retail, travel and education, consider talking to a corporate restructuring adviser who can assist in a number of ways. They will be able to help prepare an urgent financial assessment focusing on short-term liquidity, work with you to develop available levers to reduce costs and improve cash flow and create a strategy for managing stakeholders and reporting to financiers and major creditors.

The current global pandemic landscape is challenging for us all. During time of such uncertainty naturally our attention turns to our families at home – but our work families – our employees, peers, colleagues and business leaders – may also need assistance during this time.

The PNG Government, banks and other corporates are aware that these times are difficult and that private, mid-market and emerging businesses have specific business needs.

We are seeking to support our clients and business by bringing together all of the available and reliable guidance KPMG has access to. As the situation evolves, we will continue to bring you further updates on how to face these difficult times during the COVID-19 crisis.

BPNG policy response to COVID-19

Bank of Papua New Guinea has announced a range of policy measures aimed at maintaining monetary and financial stability and at providing liquidity to businesses and individuals at a reasonable cost during this time. These measures will take effect immediately and include:

- A reduction in the Kina Facility Rate (KFR) from 5% to 3%. BPNG have also directed the banks to reduce their respective Indicator Lending Rates.
- A reduction in the Cash Reserves Requirement from 10% to 7% to provide additional liquidity to the banking system.
- The intention to buyback Government securities (either Treasury Bills or Government Inscribed Stock) in an open market quantitative easing programme to provide liquidity to holders of these instruments. This programme is offered for a three-month period and includes flexibility around full or partial redemptions.
- Encouraging interbank borrowing and lending among commercial banks by increasing the margin on Central Bank borrowing and lending to commercial banks by 25 basis points to 100 basis points on both sides of the KFR.
- Continuing to provide the Intra Day Liquidity Facility to commercial banks to support the efficient clearing of payment transactions. This facility can be accessed on demand at prevailing limits.
- New purchases under the Tap Facility will cease throughout the fourteen day SOE period until further notice.
- Authorised Foreign Exchange Dealers have been directed to give priority to retailers and wholesalers of medical drugs, medical and pharmaceutical companies and the import of Covid 19 related products. BPNG will also make foreign currency directly available to the Department of Health for Covid 19 related purchases overseas.
- Prudential requirements will be relaxed to cover the three months' loan repayment holiday, namely the Prudential Standards relating to asset quality, capital adequacy and loan loss provisioning.

BPNG have committed to supplying adequate currency to commercial banks on a daily basis – this includes the cash distributions centres and the Lae currency processing facility. BPNG has also said that the operation of the kina automated transfer system and the retail electronic payment systems will continue as normal.

IRC and IPA reactions to COVID 19

During the current State of Emergency, effective from 24 March for fourteen days, only essential staff of Government bodies are working at this time. In terms of the IRC essential personnel include those in Processing and Payments, Recovery and the GST refund team while non-essential staff have been sent home. This has meant that some scheduled IRC audits have been postponed for the time being. The IRC are encouraging electronic payments and lodgements rather than face to face interactions. There have been no confirmations as yet of reliefs for taxpayers during this time although we have asked that IRC consider measures such as extended due dates and waivers of penalties to assist stressed businesses.

Meanwhile the IPA have closed their offices and lodgement counters and have encouraged companies to avail of their online lodgements site. Again, there is no indication of penalty reliefs at this time.

Treasury announcements on COVID-19

We are expecting some announcements from Treasury in relation to COVID-19 measures on 1 April 2020. We will keep you informed in due course.

Postponement of Income Tax Act rewrite

We understand Treasury intend to postpone the submission deadline for the Income Tax rewrite. We are awaiting details of the extended deadline for submissions.