

Investor Notes – 1 December 2024

Impact of 2025 National Budget Changes to Taxation of Banks - BSP

- **The Papua New Guinea 2025 National Budget was presented in Parliament on 29 November 2024.**

- **Somewhat unexpectedly, there are further changes to the taxation of commercial banks**

- **We explore the impact on BSP**

- The 2025 National Budget was introduced in the National Parliament on 29 November 2024 by the Treasurer, Hon. Ian Ling-Stuckey, MP.
- Among the new measures introduced in the 2025 budget were further changes to the taxation of commercial banks in Papua New Guinea.
- This is an industry which has seen extraordinary instability in taxation in recent years as the government has grappled with how to extract the appropriate rent from the industry as a whole and its dominant player, BSP Financial Group (*'BSP'*), in particular.
- The original attempt at a two-tiered banking taxation system involved the introduction of the K190 million Dominant Player Levy in 2021 (for the 2022 fiscal year) which was squarely and explicitly aimed at BSP. After challenging the constitutionality of this amendment and levy, BSP eventually settled with the IRC for K95 million – being half of the levy originally paid in 2022 – and the levy was repealed.
- The levy was replaced by a flat 45% corporate income tax rate to be applied on all commercial banks operating in Papua New Guinea. This was introduced in 2022 for the 2023 fiscal year.
- The 45% tax rate has now been reduced – and replaced – with another two-tiered system of taxation for commercial banks.

The latest amendments to bank taxes

Back to a two-tiered structure

The Corporate Income Tax (*CIT*) rate of commercial banks operating in Papua New Guinea will be progressively reduced over the next 10-years to 35% from the current 45%.

The reduction will be effected through a two-tiered structure:

- Tier 1 = the first K300 million of Taxable Income for a commercial bank
- Tier 2 = Taxable income above K300 million.

Tier 1:

For 2025, the first K300 million of taxable income will be taxed at a rate of 40%.

For 2026 and future fiscal years, the first K300 million of taxable income will be taxed at a rate of 35%.

Tier 2:

In 2025, taxable income of a commercial bank in excess of K300 million will be taxed at a rate of 44%.

The tax rates applicable to amounts above that level will then drop by 1% per annum from 43% in 2026, through to 35% in 2034.

The Impact on BSP

We estimate the 10-year cumulative positive impact of the changes in the CIT for commercial banking operations in Papua New Guinea on the operations of BSP to be **between K1.072 billion and K1.437 billion** with an estimated NPV of **between K430 – 700 million**:

BSP: Cumulative NPAT impact 2025-2034						
K'Millions						
Growth in Earnings	5%	6%	7%	8%	9%	10%
Tax Savings	1,072	1,136	1,205	1,277	1,355	1,437

K'Millions PV	
Low	430.70
High	700.15

Using Cost of Capital estimates of between 15-18% and Taxable Income Growth of 5-10% per annum.

We estimate the impact of this, when present valued and calculated on a per BSP share basis to be **between K0.922 and K1.499 per share**. This is value derived by BSP shareholders exclusively from the changes in the CIT rates for commercial banking operations in Papua New Guinea in the FY2025 National Budget.

BSP: PGK/Share Impact of 2025 Tax Change				
PGK per Share				
Cost of Capital	18%	17%	16%	15%
Growth in Earnings				
5%	0.922	0.982	1.049	1.124
6%	0.972	1.037	1.109	1.189
7%	1.026	1.095	1.173	1.259
8%	1.083	1.158	1.241	1.334
9%	1.143	1.224	1.313	1.414
10%	1.208	1.294	1.391	1.499



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The above findings must be read in light of the rest of our report and are based on high-level estimates and prepared for illustration purposes only. A number of factors assumed to remain unchanged in the development of the above estimates may in fact change – and significantly so.

Covering our Proverbial

Please read our Investor Notes in light of the following:

- JMP Securities Limited is deeply committed to the development of capital markets in Papua New Guinea and furthering the participation of Papua New Guinean investors in these markets.
- We are also committed to assisting the investing public, including by providing information and analysis that is relevant to local and international capital markets.
- In doing so, we will from time to time provide forward estimates and comments or statements about the possible future performance of markets or securities.
- These statements, estimates and forecasts will at all times be subject to significant risk and uncertainty. They will be based on the best information available to us and we cannot guarantee that all data or information pertinent to the estimates have been seen by us or factored into our analysis.
- Nothing in our Investor Notes should be read as a recommendation or inducement to trade or refrain from trading.
- For the most part, we provide estimates or numerical examples for the purposes of illustrating the 'order-of-magnitude' of a factor or event, not specific or detailed forecasts.
- Our aim is to allow investors and interested readers to use our Investor Notes as yet another data point as they make up their own mind as to the impact of factors and developments on securities markets in Papua New Guinea.

Diving a little deeper

Significant positive development for BSP

Our analysis is premised on:

- FY2023 and FY2024 YTD financial performance of BSP
- Assumption that PNG Banking Ops will continue to be about 80% of the Taxable Income of BSP in the foreseeable future
- Changes to valuation of Deferred Tax Assets on BSP balance sheet will be taken to P&L in each year rather than in one hit upfront.
- Changes to DTAs offset 55% of the reduction in taxes for each period

- We estimate the 10-year cumulative improvement in NPAT for BSP from the current changes to the PNG CIT rate to be between and K1.07 and K1.44 billion.
- This is based on the following forecast parameters:

K'Millions			
5% PBT Growth	Low	1,072	Cumulative reduction in Tax
10% PBT Growth	High	1,437	Payable 2025 - 2034

- The above estimated cumulative impact is based on projected Profit Before Taxation for BSP for FY2024 of K1.7 billion and applying either a 5% or a 10% annual growth rate during the period from 2025 through 2034.
- We have used 5 and 10% growth rates for illustration purposes only and do at this stage not provide specific forecasts. Our point is to illustrate the order of magnitude of the impact rather than the absolute best estimate thereof.
- We have further assumed that 80% of PBT for BSP will continue to be derived from PNG Banking Operations over the forecast period and that changes to the tax rate will result in periodic (as opposed to one-off) changes to the valuation of deferred tax assets on the BSP balance sheet. These are assumed to reduce the periodic NPAT by 55% of the relevant period's increase in NPAT from the change in the tax rate.

High Case

15% Cost of Capital and 10% Growth in PBT

	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034	Cumulative 2025-2034
	K'Millions											
BSP Financial Group - Taxable Income	1,700	1,870	2,057	2,263	2,489	2,738	3,012	3,313	3,644	4,009	4,409	29,803
% of Taxable Income from PNG Bank	80%	80%	80%	80%	80%	80%	80%	80%	80%	80%	80%	
PNG Bank PBT	1,360	1,496	1,646	1,810	1,991	2,190	2,409	2,650	2,915	3,207	3,527	23,842
Tax on First K300m - Band 1	45%	40%	35%	35%	35%	35%	35%	35%	35%	35%	35%	
Tax on Excess - Band 2	45%	44%	43%	42%	41%	40%	39%	38%	37%	36%	35%	
Prima Facie Tax @ 45%	612	673	741	815	896	986	1,084	1,193	1,312	1,443	1,587	10,729
Tax under new regime	612	646	684	739	798	861	928	998	1,073	1,151	1,235	9,113
Prima Facie Reduction in Tax Payable	-	27	57	75	98	125	157	195	239	292	353	1,616
Change in deferred tax balances (P&L Im	(15)	(16)	(10)	(12)	(15)	(18)	(21)	(25)	(29)	(34)	-	(179)
Net Impact on Statutory NPAT	-	10	47	63	83	107	136	170	210	258	353	1,437
Present Value Factor @ Ke of 15%	-	0.93	0.81	0.71	0.61	0.53	0.46	0.40	0.35	0.30	0.27	
Present Value of Tax Savings at 15%	-	9.78	37.95	44.43	50.81	56.99	62.90	68.51	73.76	78.64	93.51	577
Terminal value at 15%											137.70	138
Present Value of Tax Savings at 15%	700.15											
Valuation impact per share (PGK)	1.499											



- We estimate that the Present Value of the changes in the CIT rates for PNG commercial banking operations to have a Net Present Value of K700.15 million to BSP shareholders if we assume a Cost of Capital of 15% and an annualized 10% growth in Taxable Income during the period from 2025 – 2034.
- This amounts to K1.499 per issued Ordinary Share.
- Our forecast assumes all other variables remain unchanged.

This is not a Trade
Recommendation

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Low Case

18% Cost of Capital and 5% Growth in PBT

	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034	Cumulative 2025-2034
	K'Millions											
BSP Financial Group - Taxable Income	1,700	1,785	1,874	1,968	2,066	2,170	2,278	2,392	2,512	2,637	2,769	22,452
% of Taxable Income from PNG Bank	80%	80%	80%	80%	80%	80%	80%	80%	80%	80%	80%	
PNG Bank PBT	1,360	1,428	1,499	1,574	1,653	1,736	1,823	1,914	2,009	2,110	2,215	17,961
Tax on First K300m - Band 1	45%	40%	35%	35%	35%	35%	35%	35%	35%	35%	35%	
Tax on Excess - Band 2	45%	44%	43%	42%	41%	40%	39%	38%	37%	36%	35%	
Prima Facie Tax @ 45%	612	643	675	708	744	781	820	861	904	949	997	8,083
Tax under new regime	612	616	621	640	660	679	699	718	737	757	775	6,903
Prima Facie Reduction in Tax Payable	-	26	54	68	84	102	121	143	167	193	222	1,180
Change in deferred tax balances (P&L Im)	(14)	(15)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(16)	-	(107)
Net Impact on Statutory NPAT	-	11	46	59	74	91	109	130	152	177	222	1,072
Present Value Factor @ Ke of 18%	-	0.92	0.78	0.66	0.56	0.47	0.40	0.34	0.29	0.24	0.21	
Present Value of Tax Savings at 18%	-	10.16	36.01	39.33	41.69	43.22	44.05	44.29	44.03	43.38	45.98	392
Terminal value at 18%											53.02	53
Present Value of Tax Savings at 18%		430.70										
Valuation impact per share (PGK)		0.922										



- We estimate that the Present Value of the changes in the CIT rates for PNG commercial banking operations to have a Net Present Value of K430.70 million to BSP shareholders if we assume a Cost of Capital of 18% and an annualized 5% growth in Taxable Income during the period from 2025 – 2034.
- This amounts to K0.922 per issued Ordinary Share.
- Our forecast assumes all other variables remain unchanged.

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- Our advisors can assist you in gaining an understanding of local market conditions and assist you in formulating and executing investment strategies in both equities and fixed interest markets.
- All investments involve risk and we encourage all clients develop a detailed understanding of your own personal financial and life circumstances, formulate clear investment objectives and work with your advisors to develop an actionable investment plan that takes each of these factors into account.

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