

“Building resilience for a vibrant and prosperous future in Solomon Islands”, Remarks by CBSI Governor, Denton Rarawa at the launch of the Central Bank’s 2016 Annual Report at the Heritage Park Hotel, 19 May 2017

SALUTATION

Hon Prime Minister and Acting Minister of Finance & Treasury, Hon Manasseh Sogavare
Permanent Secretary, MOFT, Mr Harry Kuma;
Other Senior Government Officials;
Members of the Diplomatic Corp;
CBSI Board of Directors;
Heads of State Owned Enterprises;
CEO’s of Private Sector companies;
CEO’s of commercial banks;
Representatives of NGO’s, Churches, Media, Women & Youth groups;
Distinguished invited guests;
Ladies and gentlemen

INTRODUCTION

Let me thank you, especially our Prime Minister, for accepting our invitation to be with us this morning for the launch of the CBSI annual report for 2016. This is an important occasion for us to briefly inform the public about our country’s economic performance last year and also to account for Central Bank’s operations in the previous year.

This report is extra special as it marks the forty years of central banking in Solomon Islands. Over the past forty years, I believe our country has progressed on multiple fronts: economically, politically, and socially. The progress was however overshadowed by different challenges such as natural disasters; the Asian financial crisis; the global financial crisis; commodity price shocks; political instability; ethnic tension; rising demand for government services; and increased corruption.

What strikes me most is that, despite the many challenges and crises we have been through during the last forty years, our people, businesses houses, communities and government have displayed strong determination and resilience to bounce back from whatever difficult situation the country was in. All these experiences provide the motivation for my theme today i.e. **“Building resilience for a vibrant and prosperous future in Solomon Islands”**.

This theme is critically relevant now as the Solomon Islands is currently at a crossroad. I am aware of growing anxiety among the general populace over (1) exit of RAMSI in June 2017; (2) unsustainable levels of log harvesting; and (3) increasing demand for services from our people that is putting pressure on government finances. I will come back to this theme later on in my presentation.

MACROECONOMIC UPDATE AND PROJECTIONS

But first, let me provide an update on the state of the Solomon Islands economy in 2016.

State of the economy in 2016

Preliminary estimates from the CBSI showed the Solomon Islands economy grew by 3.5% in 2016, an improvement from the 2.9% growth in 2015. The positive outcome was driven by forestry and agriculture,

supported by construction, manufacturing, transportation, communication and services sectors. The construction sector benefited from public and private sector investments in large infrastructure projects and commercial buildings respectively.

Log production increased by seventeen percent against a year ago to 2.292 million cubic meters. This reflects re-entry into previously logged out areas, clear felling for alternative land use, and increase in plantation logs. Annual outputs for copra and palm oil bounced back in 2016, up by six percent and twelve percent respectively.

Labour market conditions slightly improved. Using SINPF membership as proxy, the number of contributors increased by one percent to 55,820 contributors. This is around 15 percent of the total labour force (both working and those between 15-64 years old looking for a job). However, the country needs to create more jobs for our growing population.

Headline inflation dropped from 2.9 percent in December 2015 to minus 2.8 percent. The downward trend was closely associated with the declining food and energy prices. However prices have shown an uptick in the first quarter of this year. We expect inflation to rise in the second half of the year.

Our foreign reserves position is more than sufficient to facilitate the trading needs of the country. It is equivalent to about ten months of imports of goods and services. The merchandise trade position of the country turned positive in 2016 due to increased exports and falling import payments (oil and machineries). While the overall current account position was still in deficit, it was offsetted by surpluses in the capital and financial accounts.

The value of the Solomon Islands dollar weakened slightly in 2016 in line with the performance of the currency basket vis-a-vis movements in the global foreign exchange markets. Movements in the exchange rate have negatively impacted the CBSI in the last few years as you will see in the Bank's financial statements later on. The Bank is treating this matter seriously as it is undermining the credibility and integrity of the Bank. So we are monitoring further developments in this area very closely and have secured technical assistance to address this issue in the second half of this year.

Money supply expanded by thirteen percent during the year to \$4,742 million following growth in credit to the private sector, increases in net foreign assets and government spending. Credit to the private sector rose by twelve percent year-on-year to \$2,192 million compared to sixteen percent growth in 2015. Major borrowing sectors were construction, distribution, tourism, forestry and personal.

Liquidity levels in the banking system accumulated further to \$1,330 million, an increase of eighteen percent year-on-year. This is more than sufficient to support the credit needs of the private sector.

Preliminary fiscal data showed the central government posted a deficit of \$457 million in 2016. The negative outcome was in line with the government's budget intentions. While revenue collection was lower than a year ago and against budget, expenditure dropped against budget but was higher than a year ago.

Short to Medium Term Outlook

The Solomon Islands economy is expected to grow by 3.4% on average in 2017-2019. This is based on the assumption that the logging sector would remain flat and taper off modestly in the short term.

The government had issued development bonds to partially fund its capital projects and buy shares in Solomon Telekom and SPOL. Even with the initial issuance, there is still policy space for the government to make further borrowing.

However, there are upside risks such as rising oil prices, geopolitical tensions, exchange rate volatilities, etc. It is important that we prepare this country to cushion or minimise any risks that could harm the economic welfare of our country. In other words, we need to build resilience to enable our country ride or withstand any external or internally induced shocks.

Let me turn to the CBSI operations and activities in 2016.

CBSI OPERATIONS

Ladies and gentlemen, as I alluded to earlier, the Bank marked forty years of central banking in our country last year. To mark the occasion, we organised a half day conference and the ‘Solomon Islands Money Day’ event. I would like to thank the financial institutions and the primary schools that participated in the celebrations.

So while we celebrated forty years of growth and development as an institution, the 2016 financial result was disappointing.

The Bank’s operations reported an overall **loss of \$42 million in 2016**. This was after taking into account unrealised foreign exchange revaluation losses of \$66 million, resulting from adverse exchange rate movements in the global foreign exchange market. Nearly half of this loss came from the BREXIT event in June 2016. On a positive note, however, if we exclude the revaluation losses, CBSI made an operating profit of \$24 million in 2016.

On Governance, the CBSI Board has two vacant positions that are yet to be filled. I am hopeful that this will be filled soon.

The Bank believes in training and upskilling of its work force and therefore continues to invest in its human resources.

In terms of our supervision of the domestic financial system, the financial system is stable, sound and prudently managed. The financial institutions are well capitalised and remained profitable. An interim banking license was issued to BRED Bank last year. Last month, the BRED Bank (Solomon Islands) was granted a full license to carry on banking businesses in the country. BRED should become fully operational within the next two months. BSP Finance (Solomon Limited) was also licensed to operate as a credit institution. These were positive developments in our efforts to broaden and deepen our financial system and encourage financial inclusion.

THEME: BUILDING RESILIENCE

Now let me come back to the theme of my talk this morning and that is: **‘Building resilience for a vibrant and prosperous future in Solomon Islands’**, a future that guarantees growth and prosperity in our country. Under this theme, I wish to comment on a few areas that I believe are important for us as a nation.

First of all, building resilience is critical for us because our country is ranked one of the most vulnerable and fragile countries in the World. But building resilience is not just about preparing for natural disasters or taking mitigation and adaptation measures to deal with the impacts of climate change.

The ‘resilience building’ I am talking about is much broader than simply preparing for natural disasters. It is multi-faceted, multi-dimensional and cross cutting in nature. It covers a lot of areas and therefore is a critical national issue that require the attention of all stakeholders. It is as much about planting mangroves to protect

our coastlines to tackling transfer pricing of the proceeds of our natural resources that is costing our country millions of dollars of foregone revenues. It is about enforcing our laws and regulations. It is about addressing our high population growth as much as tackling the rhinoceros beetle that is damaging our coconut trees or the giant African snail that is threatening our agriculture sector. It is about assisting and supporting our clients when they are down on their knees. It is about our communities allowing their land and resources for development.

In other words, building resilience is about nation building; about taking appropriate action now to ensure our country's future prosperity is guaranteed. I will try and pick up some of these issues.

Resilience in the export sector

Our export sector is dominated by round log exports which contributes more than seventy percent of our export earnings and is a major employing sector in the country. This heavy dependence on a single commodity leaves our country very vulnerable to what happens in this sector. We need to diversify our export base by encouraging both public and private sector investments in other productive sectors like agriculture, fisheries, tourism, and mining.

We are starting to see growth in the tourism sector but more needs to be done. We need to invest more in tourism infrastructure. We need to plant more hectares of cocoa, palm oil, coconut and other niche agricultural commodities to complete round log exports and build income resilience for farmers. So our land and resource owners need to allow their lands for development. Land disputes are a major challenge to building resilience in our country.

We need to invest and channel funds into small businesses so that they too can contribute to diversifying and broadening the economic base.

This is where a revived "DBSI" can play a role. If fully resourced and its governance requirements strengthened, DBSI is a potential vehicle for channelling public funds to promote local entrepreneurs and business growth.

External and Fiscal Buffers

Building external and fiscal buffers are critical components of resilience building. The need to maintain sufficient foreign reserves and fiscal reserves to accommodate unexpected macroeconomic shocks is critical. While we are comfortable with the current level of foreign reserves, our fiscal buffers have been drawn down in recent times and need to be regularly replenished. It is prudent that we have these 'self-insurance' facilities in place.

In addition to the need to have external and fiscal buffers in place, it is also critical to allow or provide for adequate policy space within our budget and public debt frameworks to enable us respond quickly to any natural or man-made shocks.

And we in the financial system have a role to play in building the resilience of our clients. As financial institutions we can be innovative and come up with 'client-friendly' policies such as debt relief through temporary grace periods or lower interest rates, especially for those clients who have been badly affected by shocks.

Enforcing our laws and regulations

Effective enforcement of our laws and regulations is a major weakness in our country and this is actually undermining our capacity to build our resilience. Our laws and regulations especially in the extractive sectors such as forestry and mining are simply being disregarded resulting in numerous legal cases before our courts

and huge loss of income through transfer pricing; income that could have been used to build resilience buffers in our country.

Reducing our population growth

One way of building resilience in our country is to reduce our population growth. Our population growth is like the 'elephant in the room'. Nobody is talking about it or wants to talk about it. I am aware past governments have tried to come up with a national population policy. I am not sure of the current status of that work. A fast and high growing population that demands more from the economy now means less will be preserved for the future. So we need to slow down the pace of our population growth as a means building resilience for the future.

Why Build Resilience?

Ladies and gentlemen, why should we build our resilience? The simple answer is that all of us want to see the living standards of all Solomon Islands citizens to improve and sustained at a higher level. It is critically important that all of us (including businesses, households, farmers/fishermen/tourist operators, government, and general economy) are able to bounce back quickly from any adverse shocks that hit our country. We are fortunate to have donors often come to our aid during our trying times. However, we cannot depend on donors forever. Their policies and focus can change and we must be prepared for that happening as well.

Investing in our own resilience therefore make sense. And there is no better time than now to start seriously considering these issues? Building our resilience now will guarantee our existence and prosperity in the future.

CONCLUSIONS

In concluding ladies and gentlemen, let me thank you all for coming this morning. Let me also thank the many government ministries and agencies, private sector companies, financial institutions and individuals who provided data and information used in this report. Without your support the completion of the report would not have been possible.

I would also like to thank the Auditor General and his contracted auditor, KPMG of Fiji for auditing the Banks 2016 financials and also to our printers for getting copies of the report out for this event this morning. And also let me thank the CBSI Board of Directors for their policy guidance, wisdom and commitment to the work of the Bank in 2016.

Finally, I would like to thank my hardworking officers for their contribution towards this report. Also let me specially mention Deputy Governor, Gane Simbe who ensured that the report went to print before he flew out to attend a major currency conference overseas.

With these few comments, ladies and gentlemen I now launch the 2016 CBSI Annual Report for public dissemination and consumption.

May God bless Solomon Islands!

Thank You

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