Overview of the Banks Functions and Operations

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A central bank cannot achieve its multiple objectives without the support of other government policy measures or what is commonly called Fiscal Policy. Economic activity, which is a measure of the total expenditures of households, businesses and government for consumption and investment, is influenced by both monetary and fiscal policies and must work in tandem. A policy action taken by a central bank or government to achieve a particular objective may conflict with another stated objective, hence underscoring the need for consultation on and synchronization of policy objectives, targets and instruments.

For example, Government deficit spending designed to stimulate employment may lead to increased household expenditure and higher prices for goods. Further, government's borrowing to finance a deficit may cause interest rates to rise. If this were to happen, some local investment projects may be delayed or permanently shelved. Alternatively, if a central bank increased the supply of money to bring about a decline in interest rates in order to promote local investment, this may have adverse balance of payments consequences arising from an increase in capital imports and/or a flight of short-term capital to earn higher interest rates overseas.

Monetary policy aims, by and large, to control the money stock. The factors which influence the money stock are:

- Issue of notes and coins by a central bank;
- Variations in government's cash holdings and deposits with a central bank and/or commercial banks;
- Changes in loans and advances to government and/or in holdings of treasury bills and other government securities by a central bank and/or commercial banks;
- Changes in the foreign exchange reserves of a country;
- Variations in the statutory cash reserve requirement and the liquid assets ratio;
- Changes in a central bank's discount rate, also referred to as the Bank rate; and □ Adjustments in commercial banks' desired level of excess reserves.

In order to achieve its objectives which, include, among other things, the development of a sound credit and banking system, a central bank must be equipped with special powers and policy instruments to effectively influence the factors which affect the money stock:

1. The Central Bank as Currency Authority
2. The Central Bank as Banker and Advisor to the Government
3. The Central Bank as Banker to the Commercial Banks
4. The Central Bank as Manager of the External Reserves

The Central Bank as Currency Authority

The Central Bank has sole authority for the issue of notes and coins in Solomon Islands. The unit of currency is a dollar which is divided into one hundred cents.

The value of the SBD$ is determined from a currency basket comprised of the currencies of the five main trading partners, ie. USD$, AUD$, NZD$, Pound Sterling and the Japanese Yen. The weight assigned to each currency reflects its importance in trade with Solomon Islands. These weights are reviewed annually by the Bank. No change can be made to the weights without the prior approval of the Minister of Finance.

The Bank calculates the value of the SBD$ each day against the intervention currency which is currently the US dollar. The Bank has been empowered to make discretionary changes to the calculated rate, within certain specified limits, so as to make it consistent with current policy objectives. The Bank is also required to provide weekly records to the Minister of Finance on the actual rates and movements during the week.

SI dollar notes of various denominations issued by the Bank are legal tender in Solomon Islands at their face value for the payment of any amount.

The Bank from time to time arranges for the printing of notes and minting of coins for its stock and for issue to the public. Old notes returning to the Bank from circulation are reissued if they are in good condition. The Bank also redeems notes of one denomination into another; notes into coins or coins into notes.

The denomination of notes in circulation are $100, $50, $20, $10, $5, and $2; and coins, in denomination of $2, $1, 50 cents, 20 cents and 10 cents. The total value of currency in circulation for 2019 increased by 0.9% to 955.3 million from $947.2 million on 2018 compared to 2.5% increase in the previous year. Of the total currency in circulation, currency notes accounts for 97.0% ($922.8 million) while coins hold the remaining 3.0% ($32.5 million). *CBSI 2019 Annual Report*

The Central Bank has issued commemorative $100 gold coins; and silver coins in denominations of $10 and $5. These coins are legal tender but they do not circulate. The Bank has also commemorated major events such as the Pacific War, the Battle for Guadalcanal, Pacific Navigators, and other events through the issuance of commemorative coins which are of interest to coin collectors.

In next week’s article, we will look at the role of Central Bank as Banker and Advisor to the Government.