

Monetary Policy Stance 2009

In response to the international environment, domestic economic conditions and in line with the Central Bank of the Solomon Islands Act the Bank will follow the following priorities in 2009:

1. The Bank will act to reduce and stabilize the level of inflation
2. The Bank will act to protect and preserve the level of official foreign reserves
3. The Bank will act to ensure the stability and robustness of the financial system

Reducing and stabilizing the level of inflation

During 2008 the price level rose at a rate felt by the Bank to be unacceptably high. In response to this the Bank tightened its monetary policy. The subsequent fall in international prices has acted to lower the rate of inflation in the Solomon Islands economy yet it still remains above a level the bank would deem conducive to stability and long run growth in the economy. At present core inflation in the economy is decreasing and it is believed that the upturn in headline inflation is a transitory reaction to the flooding experienced in the Islands. It is the opinion of the Bank however that to loosen monetary policy due to this declining trend would be premature with the rate of headline and core inflation above 17%. The Bank will continue to monitor the price level and will intervene where necessary to benefit the economy.

Protecting the level of official foreign reserves

The current level of reserves is below the Bank's desired level of sufficient to cover the predicted next three months of imports. As the rate of reserves is already below target the desire of the Bank must strive to bring it above this level. In the worst scenario we must act to prevent a further dwindling of the reserves. To achieve this goal the Bank proposes to keep monetary policy tight. It is hoped that this can prevent a hemorrhaging of reserves. If this were to prove unsuccessful then the Bank may have to consider pursuing different courses of action in the future. The Bank is proposing a level of reserves equivalent to 2 months import cover at which point more extreme measures may be required. In the longer term the bank will hope to work with the government to develop and implement structural reforms in the economy that may help to rebalance the current trade deficit.

Ensuring the stability and Robustness of the financial system

The global financial system was severely tested in 2008 and some of the procedures in place to supervise and regulate financial systems around the world were found severely wanting. Whilst the financial system of the Solomon Islands is secure and has not fallen prey to the problems of other markets, especially more complex ones, it seems an appropriate juncture to review our procedures in this field and to reinforce any area we feel weak. In 2009 therefore the bank intends to further improve the system currently in place. Revised prudential guidelines will be completed and enforced governing capital adequacy, asset quality, liquidity management, large credit exposures and external audit requirements. A new prudential guideline has been formulated for foreign currency open positions. By strengthening prudential guidelines, bank reporting standards and by increasing the range and detail of analysis conducted on this data the Bank hopes to ensure the continued stability of the financial system of the Solomon Islands.