

Luke Forau: 2023 Annual Report Launch

Statement by Mr Luke Forau, Governor of the Central Bank of Solomon Islands, at the Launch of the 2023 CBSI Annual Report, Honiara, 22 April 2024.

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- Permanent Secretary of Finance and Treasury;
- Heads of Financial Institutions;
- Representatives of the Diplomatic Corps;
- Senior Government officials;
- Central Bank Board of Directors;
- Heads of Statutory Authorities;
- Representatives of Non-Governmental Organizations;
- Representatives of the Private Sector;
- Representatives of the Media;
- Distinguished Guests;
- Ladies and gentlemen

Good morning!

It gives me great pleasure to warmly welcome you all this morning to the launch of the Central Bank's 2023 Annual Report. Thank you for accepting our invitation and for honoring us with your presence today.

This morning, I will provide you a brief assessment on the economic performance of our country in 2023, and offer some insights into future prospects in 2024 and beyond. Then I'd like to focus on something that I think is relevant for the next government to take on board for a possible path for the economy to prosper.

I will then finish off by highlighting some key operations of the Bank last year, as a way of informing the public about what we do, as a means of being transparent and accountable for our actions.

As you are aware, last week the country had a national general election to elect members of parliament for the 12th Parliament.

As I speak, counting of some ballot boxes is still continuing. We offer our hearty congratulations to the successful candidates.

The next important one is the formation of the executive government.

With that in mind, I'd like to underscore that our economy is at the crossroad; the road to economic prosperity is not going to be easy. Despite rebounding from the recession caused by the pandemic, the country's current economic environment remains precarious.

Against this background, my theme for this year is: **"The Time is Now: Taking Bold Action to Level Up Growth in Solomon Islands"**.

Today, the global landscape has changed from what it was in the pre-COVID19 era, and we must adapt accordingly, or risk lagging behind. Now is the time to take critical action to realize our growth potential, 'levelling up' the quality and inclusiveness of our economic growth in the midst of uncertainties. There is no better time than now to seriously address the country's dire economic situation. This is an opportune time to start anew.

We can do that by unlocking the power of our people (human resource), laying the foundations for a labour-market expansion that would enable us to look at our demographic boom not as a burden, but as an opportunity. I will return to this later – but first, let me briefly reflect on the performance of our economy over the past year.

Economic Update

Growth

In 2023, global growth slowed to 3.2 percent from 3.5% in 2022, in the wake of considerable monetary tightening by major central banks, the winding down of COVID related fiscal support in many large economies and an overall climate of geopolitical uncertainty.

On the domestic front, the Solomon Islands economy returned to normalcy, growing by an estimated 4 percent year-on-year according to CBSI estimates. This favourable outcome was driven by a four-fold expansion in mining activity, greater output of key agricultural commodities such as copra and cocoa, a rebound in logging exports, and higher manufacturing outturns, which collectively outweighed a weak performance in fishing and palm oil production. Also, many businesses in Honiara were negatively affected by several months of power supply disruption between May and August.

The hosting of the 17th Pacific Games in November 2023, which CBSI celebrated through the issuance of a commemorative \$10 note, was the source of important revenue windfalls for the services sector, benefitting primarily the hospitality industry, transport, telecommunications, and wholesale and retail industries, thanks to a surge in visitor arrivals in the final quarter of the year.

It must be noted though, that the benefits brought by the Pacific Games came at high opportunity costs, as the funneling of funds towards the event led to substantial resource diversion away from other productive sectors.

Labour Conditions

In terms of employment, labour market conditions improved last year, in line with the increased economic growth recorded. Job vacancy advertisements surged, and the number of 'active' and 'slow-active' contributors to the Solomon Islands National Provident Fund rose by 3 percent to more than 57,000 members. Public Service employment also increased, from 19,800 to slightly above 20,000, and this is mainly due to recruitment in the education sector.

Inflation

Following high inflation in the beginning of the year, the Central Bank was able to bring down inflation to a level that is within the Bank's desirable range. By December 2023, the headline inflation was recorded at 3.5%. This reflected the CBSI's prudent management of the monetary and exchange rate policy, combined with easing global oil prices.

External conditions

External conditions improved as well during the year: both the trade-balance and current-account deficits narrowed, due to a rise in exports, inward remittances and donor inflows. This, combined with a buoyant capital and financial account, led to a surplus in the overall balance of payments position of \$218 million. As a result, gross foreign reserves rose by 6 percent to \$5.8 billion, sufficient to cover 11.8 months of imports. This is well above our minimum threshold of 6 months of import cover.

Fiscal

On the fiscal front, the Government's financial conditions deteriorated markedly last year. The deficit more than doubled to 7 percent of GDP (or \$950 million) from the 3 percent of GDP registered in 2022. Some financing of the deficit came largely from borrowing. As a result, the Central Government's debt stock – domestic and external – reached 21 percent of GDP at the end of the year, compared to 16 percent of GDP one year prior.

The worsening fiscal balance is attributable to a noticeable rise in spending, geared towards the hosting of the Pacific Games and the preparation for the recent synchronized elections at the same time, as revenue collection declined during the year [\[1\]](#).

Monetary

Due to the sizeable fiscal expansion and improved external-sector performance, all monetary aggregates (M0, M1, M3) expanded in 2023. Broad money (M3), in particular, rose by 6 percent to \$6.2 billion. Private-sector credit, an important measure of financial development in the country, grew by 5 percent, supported by the narrowing of the interest margin between lending and deposits rates to 8.3 percent.

This may be an indication of improving efficiency in the banking sector, and will hopefully usher in an era of increasing affordability of financing for our people. Meanwhile, the banking sector continued to accumulate liquidity, which once again rose by 6 percent on an annual basis to \$2.6 billion in December 2023. While excess liquidity remains high, it is deemed of limited inflationary risk, given the supply-side nature of inflation in the country.

Growth Outlook

Turning to the outlook for the year, 2024, the Central Bank projects the post-Pacific-Games Solomon Islands' economy to grow by 2.9 percent in 2024 and 2.5% in 2025. This growth projection is anticipated to come from a rebound in fishing and palm oil production, further expansion in the mining sector – with an expected increase in nickel

exports – and continued infrastructure support by development partners. Modest growth is also expected across all other sectors.

In the medium term, growth is projected to average around 2.5 percent. This is expected to be triggered by the staggered implementation of planned development projects and the continued prospects for global growth, as logging is forecasted to decline.

In spite of this positive growth outlook, the state of our economy remains fragile and susceptible to shocks. The key underlying fundamentals of the economy remain unaddressed; this include but not limited to narrow economic base, high unemployment, narrow tax base, continuous fiscal deficit, low production, low demand, shallow market, shallow financial system, and weak monetary policy transmission mechanism.

In addition, domestic challenges still remain, such as rising costs of doing business, inefficient process of accessing to land for investment, and an inefficient domestic infrastructure including inadequate transportation system, coupled with limited access to finance, and limited fiscal space which are further threatened by climate change risk.

As the largest employer, the largest consumer, the largest contributor to national savings/investments, government action has a larger impact on the economy. It is one of the two pillars of the economy, the other one being the private sector. As such, it is crucial that management of fiscal operations is done to spur economic growth and improve the livelihoods of our people.

That said, the fiscal outlook for 2024 entails a deficit of 4% of GDP, with a total budget of \$4.2 billion. I want to stressed that fiscal discipline and effective management of the budget is crucial for the delivery of the budget. Until now, we are uncertain of the incoming government's plans, but any further fiscal expansion would severely strain the fiscal space and put the government in a very tight and strenuous debt situation. With limited financial resources, policy priorities have to be realistic and targeted.

Theme

Let me now return to the theme of my address today: **The Time Is Now: Taking Bold Action to Level Up Growth in Solomon Islands.**

Ladies and gentlemen, we must act now!

As I alluded to earlier, the country is at the crossroad. We urgently need major economic reform program if the economy were to prosper in the medium to long term. In the short term, the government needs to implement the budget and address the "lower hanging fruits" for example, review the legislations that need to be reviewed.

The ultimate goal of any economic reform program must be to grow the economy. There is no way around this, we must grow the economy in order to support and meet the ever-growing needs of the population. The reform program must be specific, targeted and measurable.

The incoming government is in a better position to initiate this reform. Again, the reforms must aim at growing the economy. For me, a minimum average growth rate of 5% would be an acceptable rate of growth for such a developing economy as Solomon Islands.

We have a fast-growing population, with a population rate of growth higher than the average economic growth rate. This is dangerously not good and is a serious concern. We need to grow the economy faster than the growth of the population.

That said, let me highlight few areas that I think requires immediate attention of the incoming government in order to grow the economy.

First, support and facilitate the export sector. Solomon Islands seriously needs to focus on increasing the export volume. Often times we hear exporters complaining about them not meeting the demand of their buyers. The government must support the exporting companies by providing appropriate incentives in order for them to increase their volume. This support should include the whole supply chain starting from the farmer (if it's an agricultural commodity) right up to the exporter. Moreover, the government needs to listen to the exporters, they know best. Important to note that the agriculture sector hasn't reach its potential output yet. Therefore, large investments are needed in the agricultural sector.

At the same time, it's about time that we start focusing on adding value to our exports by down streaming our primary commodities. Again, this requires reasonable incentives from the government. The country hasn't had any large investment in the secondary production since the establishments of Soltuna cannery and Palm Oil. We must seriously focus on investing in this sector to help boost our GDP.

When the export sector booms, our foreign exchange earnings also increase – good for the country!

High exports can also cause the local currency to strengthen.

Second, the government needs to seriously institute appropriate governance mechanisms in the management of the extractive industry. Apart from minimizing the destruction to the environment, there is a need to strengthen the governance of the economic returns (revenue) obtained from the extractive industry. This ensures that the investor, government and landowners receive a fair share of the economic return from the resource. Doing so, it would also entail striking a balance between respecting traditional forms of land ownership and enabling economic development through large-scale infrastructure and commercial projects.

Furthermore, having in place good governance structures on these extractive resources ensures the financial returns are saved and invested to benefit both the current and future generations.

And if I may add, it is an opportune time for the government to explore the possibility of establishing a Sovereign Wealth Fund or similar vehicles, to accumulate buffers and use it during the *rainy days*. This fund can be reinvested to earn interest.

Third, we must make good use of the most precious resource at our disposal: our people. Given current demographic trends, we are at the point of entering a period of demographic dividend, in which the working-age population continues to expand relative to the economically-inactive age groups, and is increasingly able to finance both the education of our children and the caring for our elderly.

This demographic gift is however easily squandered: only in the presence of appropriate employment opportunities for our youths will we be able to fully reap the rewards of our medium-term demographic destiny. The risks, as we know, are high, for example, an under-employed youth is a restless one. As our population continues to increase, we are also faced with the prospect of rising tides of rural-to-urban migration, which could easily overstretch the infrastructure in our urban centres, as currently experienced, and drain our rural communities of vitality and economic opportunities.

The question of how best to leverage and employ our abundant labour must therefore be paramount in our minds, and more especially the government needs to come up with a policy to engage and cater for the working-age population as we chart a path forward.

In this regard, I'd like to thank the Australian and New Zealand Governments for providing additional employment opportunities to our working-age population through the Seasonal Workers Scheme, the Pacific Australia Labour Mobility (PALM) scheme and the Recognized Seasonal Employment (RSE). This has acted as a stopgap measure to absorb excess domestic labour, while also benefitting our country through rising remittances^[2] and productivity spill-overs. The country is happy to supply up to 100,000 workers for both Australia and New Zealand.

However, it is imperative that any sustainable growth strategy for our country must rely on the expansion of domestic economic opportunities. Hence, the need for economic reforms. And to do that, again it's important that the government provide a conducive environment for businesses to thrive and attract genuine investors, at the same time expand economic sectors to broaden the economic base in order to provide more employment for the working-age population.

CBSI stands ready to support the Government of the day in this regard by ensuring that macroeconomic conditions in Solomon Islands are conducive to growth and stability.

Ladies and gentlemen, during our consultation with the stakeholders in the private sector, two factors routinely emerged as major constraints to growth and employment: (i) a shortage of skilled labour, and (ii) the unreliability and inefficiency of domestic infrastructure.

The former is of particular importance for all of us in strategic terms. Growth will not magically materialize from a rising number of working-age people in our country; rather, it will depend crucially on the skill level of that workforce, and on their ability to find suitable employment. It is therefore essential that our education system keep up with rising domestic demand for skilled labour, and that our healthcare system ensures the health and well-being of our people. We believe the Government can contribute to this by continuing to step up its efforts at promoting a healthy life-style, strengthening the fight against NCDs and ensuring that every individual has access to a healthy and affordable diet.

For the infrastructure, the Private-sector actors are calling on the Government to step up investment in infrastructure and its maintenance, ensuring also that it is climate resilient, in order to forge more reliable domestic supply chains and facilitate intra- and inter-island movement and trade. Better infrastructure would also place Solomon Islands more firmly onto the global tourism map.

In terms of financial infrastructure, CBSI is committed to providing an ever more enabling environment for financial development, and to actively champion financial inclusion as we inch ever closer to reaching that 'last mile'. Recent technological advances, especially in the fintech space, have brought us closer to that goal than ever before, thanks to increasingly agile payment infrastructures and savings devices.

As some of you may be aware, that CBSI recently launched the go-live Solomon Islands Automated Transfer System known as the SOLATS, which is a real time gross settlement (RTGS) payment system. You may have recently experienced that payment transfers are now instant.

CBSI aims to ensure every resident of Solomon Islands is finally able to access the financial services they require and deserve at their finger-tips. We will also redouble our efforts to improve access to credit, the lifeblood of investment. This is of vital importance for our SMEs – the backbone of our economy – and our new start-ups, our disruptors and innovators, who often require special care and incubation in the earliest stages of operation.

Ladies and gentlemen, all these things cannot be done without the ceasing effort of everyone. It needs the support of all stakeholders, including the government, the private sector, non-state actors, NGOs, development partners, and all individuals. We all have a role to play in this.

CBSI Operations

Let me now close by briefly reflecting on the Bank's operations last year.

The Bank recorded a net operating profit of \$199.4 million, reversing the \$12.8 million loss incurred in 2022. Of the total profit, \$129 million is in the form of unrealized revaluation gains and \$70 million is operational profit. Overall, CBSI's net equity position improved significantly, rising by 64% to \$531 million. Total assets stood at \$6.60 billion at the end of 2023, the majority (90%) are foreign reserves, which we aim to maintain at a comfortable level to support the country's international trading and transaction requirements.

In terms of governance, the Bank was able to leverage the oversight and expertise of its full nine-member Board of Directors. Last year, the Board endorsed the Bank's Strategic Plan 2024-2027, which charts CBSI's direction for the next four years; in it, we aligned our shared vision of CBSI as "*A Modern Central Bank Empowering Development of Solomon Islands*" with the key mandates stipulated in the CBSI Act.

The Bank currently has a dedicated workforce of 165 staff, up from 148 in 2022. We strive to be an equal-opportunities employer, with females comprising 41 percent of the workforce. We also continued to actively encourage capacity-development and

wellbeing programmes for our staff, with the goal of enhancing skills, enriching knowledge, and promoting overall staff health throughout the year.

The Bank has also made good progress reviewing the laws that govern its roles and contribution to the development of the country. In October, the National Parliament approved an amendment of the CBSI Act 2012, following extensive consultations in Honiara and the Provinces. We also made progress towards the implementation of the National Payment System, with the establishment of a dedicated Department to spearhead its implementation. The Bank further progressed policy papers to review the Money Laundering and Proceeds of Crime (Amendment) Act, the Financial Institutions (Amendment) Act, the Insurance Act, and the Exchange Control Act. These documents have now been rendered to the Ministry of Finance and Treasury for Cabinet approval.

Conclusion

Finally, let me acknowledge the many contributors to this report: the Government, the businesses houses, the development partners, the NGOs, and everyone that have contributed directly and indirectly to our work. Thanks to our external auditors, Ernst and Young, contracted through the Office of the Accountant General, for the timely auditing of our accounts.

I thank the Board for providing the oversight role and my staff at the Central Bank for the continued team work and professionalism displayed.

With that, ladies and gentlemen, I now have the pleasure to commend the 2023 CBSI Annual Report for your reading.

Thank you, and May God Bless you all.