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September 2007
IMF Country Report No. 07/304

Solomon Islands: 2007 Article IV Consultation—Staff Report; Staff Supplement; and Public Information Notice on the Executive Board Discussion

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the Article IV consultation with the Solomon Islands, the following documents have been released and are included in this package:

- The staff report for the 2007 Article IV consultation, prepared by a staff team of the IMF, following discussions that ended on May 22, 2007, with the officials of the Solomon Islands on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on June 29, 2007. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.

- A supplement on the IMF/World Bank debt sustainability analysis.

- A Public Information Notice (PIN) summarizing the views of the Executive Board as expressed during its July 16, 2007 discussion of the staff report that concluded the Article IV consultation.

The document listed below has been or will be separately released.

Tax Summary and Statistical Appendix Paper

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

To assist the IMF in evaluating the publication policy, reader comments are invited and may be sent by e-mail to publicationpolicy@imf.org.

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Washington, D.C.

INTERNATIONAL MONETARY FUND

SOLOMON ISLANDS

Staff Report for the 2007 Article IV Consultation

Prepared by the Staff Representatives for the 2007 Consultation
with the Solomon Islands

Approved by Steven Dunaway and Michael Hadjimichael

June 29, 2007

- **Time and place of consultation:** Honiara, May 11–22, 2007.
- **Team:** L. Papi (head), G. Fernandez, E. Sidgwick (all APD), and M. Pedroni (FIN). M. Stone (OED) attended the policy meetings.
- **Counterparts:** The team met with Minister of Finance Lilo, Governor Houenipwela of the Central Bank of the Solomon Islands (CBSI), senior government officials, donors, trade unions, and private sector representatives.
- **Past surveillance:** Executive Directors' comments at the conclusion of the last Article IV consultation on October 4, 2006 can be found at http://www.imf.org/external/np/sec/pn/2006/pn06122.htm.
- **Exchange system:** The Solomon Islands accepted the obligations of Article VIII, Sections 2(a), 3, and 4 in 1979 and now maintains an exchange system that is free of restrictions on payments and transfers for current international transactions. The exchange rate regime is a de facto peg to the U.S. dollar.
- **Publication:** As in past years, the authorities indicated that they intend to publish the Article IV documents.
- **Outreach:** The mission held a press conference.

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Executive Summary

Background and Challenges

The economy has been recovering since the civil conflict, but the country remains the poorest in the region and heavily dependent on logging and aid. Macroeconomic stability has been maintained and growth has averaged 6 percent since mid-2003, but per capita income remains the lowest in the region. In 2007, growth is expected to be 5½ percent, mostly reflecting an escalation in logging from an already unsustainable rate. The current account deficit is expected to widen sharply due to imports related to the gold mine, but strong aid flows and FDI should keep reserve cover at a comfortable level. The budget is too expansionary but projected to remain in surplus. Inflation is expected to ease to 7 percent.

The political situation remains fragile and medium-term challenges daunting. Political instability could resurface and donor relations have been strained but are improving. The logging stock is now estimated to decline sharply after 2009 and aid flows will likely slow. Absent higher nonlogging growth, living standards will stagnate.

Key Policy Issues

These challenges require a more integrated and forward-looking approach and immediate actions. Some progress has been made in structural reforms, but a well-prioritized country-led development strategy is needed and early actions should focus on:

- **Maintaining fiscal prudence and anchoring fiscal policy to a medium-term framework.** With the prospect of declining revenues and aid, and the need to increase priority spending while reducing debt, the authorities should: maintain their revenue efforts, continue refraining from borrowing until all debt indicators fall below the thresholds; save most of the likely revenue overperformance compared to the 2007 Budget; and adopt a medium-term budget framework that explicitly recognizes impending pressures. Early measures to improve the poor performance of state-owned enterprises and passage of the National Provident Fund bill are also necessary to mitigate the risks to the budget and strengthen governance.

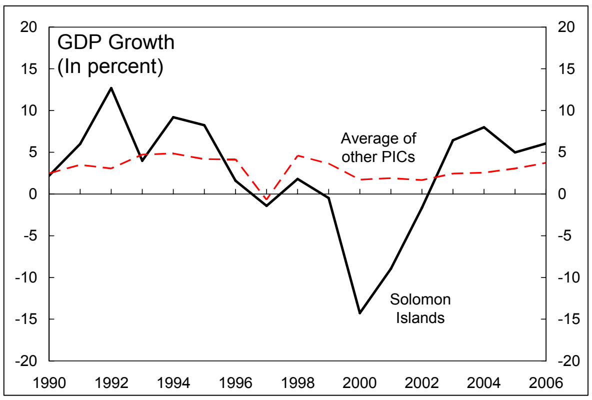
- **Easing the binding constraints to growth.** Measures should aim at reducing high business costs─expensive and unreliable utilities, weak transport infrastructure, and skilled labor shortages─and addressing poor governance stemming from opaque rules, unwarranted government discretion, and land tenure uncertainties.

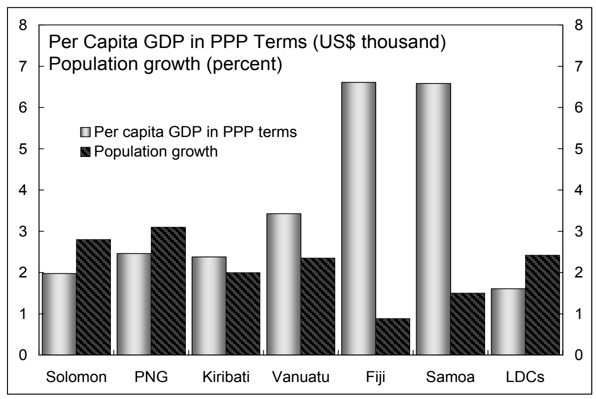
The current exchange rate policy is appropriate, but the CBSI should strengthen its monetary management and financial supervision. With strong inflows, the currency has been stabilized against the U.S. dollar but downward pressure should not be resisted. The CBSI should adopt a more forward-looking approach to countering inflation pressures if they materialize, and tighten prudential measures to ensure asset quality remains high.

The statistical data base hampers surveillance and should continue to be improved.

I. Background

1. **The economy has been recovering since the end of the civil conflict, but the Solomon Islands remains the poorest country in the region and relies heavily on logging and aid.** Since the intervention of the Regional Assistance Mission to the Solomon Islands (RAMSI) in mid-2003, growth has averaged 6 percent and financial stability has been maintained (Table 1). Nevertheless, with one of the fastest growing populations in the world, per capita income is the lowest in the region. Economic activity continues to rely on the unsustainable exploitation of the country's forests and large donor assistance. Social indicators are poor, and most MDGs are unlikely to be met (Annex V).





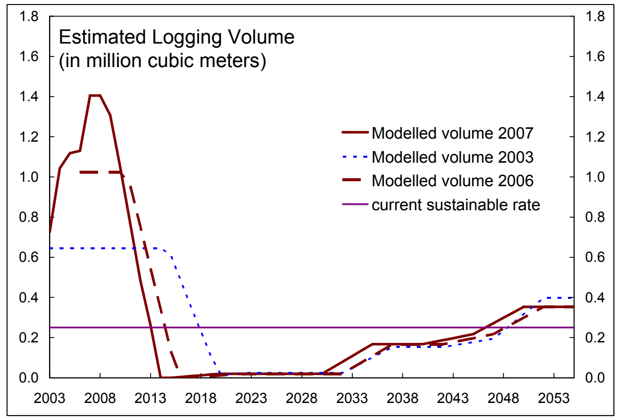
2. **After a rocky period following the 2006 elections, relations with donors have improved recently, but the political situation remains fragile.** The government survived a no-confidence vote last February and has taken steps to mend relations with donors. Aid flows have been largely unaffected, but tensions remain, and political instability could resurface given shifting political alliances.

3. **The government program focuses on rural development, but a comprehensive and well-articulated development and poverty reduction strategy has yet to be elaborated.** The government Policy Translation and Implementation Document emphasizes a bottom-up approach to development. At the same time, implementation of some donor-assisted sector strategies in education, health, transport, and agriculture are benefiting from improved capacity of some government departments. To bring order to these separate initiatives, recently there appears to be some renewed interest in reviving a national development strategy, which was shelved late last year contrary to Fund advice, after the change in government.

4. **The effectiveness of past surveillance has been mixed.** Progress has been made in simplifying foreign investment applications, developing transport infrastructure, reducing tax exemptions, and monitoring aid delivery. Nevertheless, reforms of state-owned enterprises (SOEs), the National Provident Fund (NPF), and the proposed liquidation of the troubled Development Bank of the Solomon Islands (DBSI) have fallen short of expectations. The

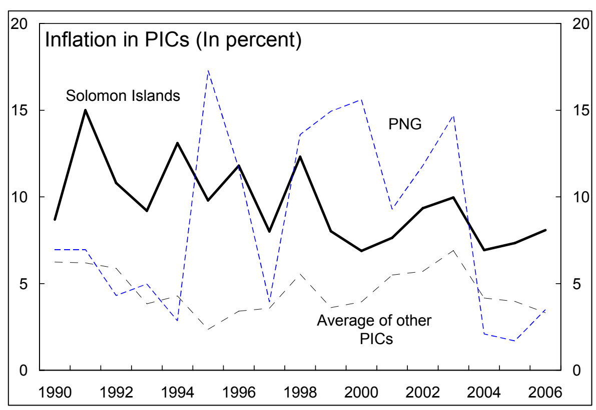
large civil service wage increases approved last October contradicted Fund advice. The backpedaling on the increase in the reference prices of logs, little follow-up to the Auditor General's Special Audits, and controversial government appointments have reinforced perceptions of uneven progress on governance.

5. **Longer-term challenges are daunting.** Based on a new government report, the fast-declining stock of logs is now estimated to run out in 2014, much earlier than previously anticipated. Activity in this sector accounts for 70 percent of exports, 15 percent of domestic government revenue, and 10 percent of GDP. Committed aid flows, currently about 35 percent of GDP, are also expected to decline.



II. Recent Economic Developments and Outlook

6. **Economic growth remained satisfactory in 2006.** Real GDP rose an estimated 6 percent: nonlogging growth accelerated to 6 percent, driven by fish, palm oil production, and services (Figure 1). Logging continued broadly at the same level as in 2005, over four times the sustainable rate. The current account deficit widened slightly to 26 percent of GDP, mainly reflecting higher fuel and investment-related imports (Table 2 and Figure 2).[1] Continued strong aid inflows and private FDI in the gold mine and the palm oil project kept international reserve cover at adequate levels. Brisk private credit growth persisted, but as credit to government again contracted reflecting an overall budget surplus, monetary growth moderated (Tables 3 and 4, Figures 3 and 4). Due to this and

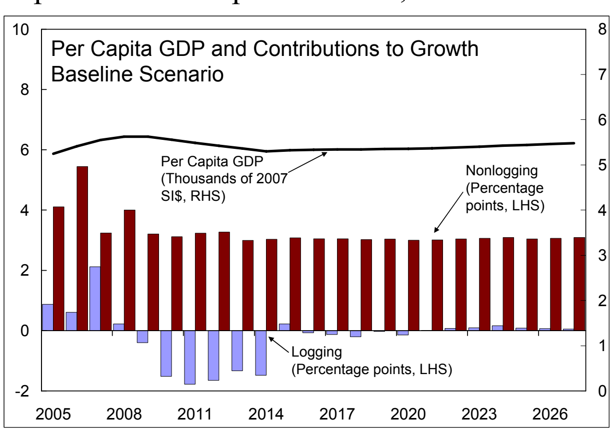


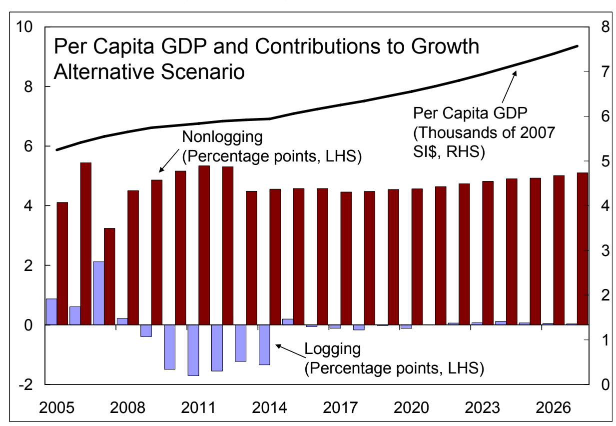
[1] New customs trade data, which have become available in 2006, show much higher imports than previously measured from foreign exchange transactions. Also, the new aid survey covering cash and noncash aid flows has revealed that aid flows have been significantly higher than previously estimated by staff.

receding oil prices, inflation decelerated to 7½ percent, but remains the highest among the Pacific Island Countries (PICs).

7. **Growth is expected to be about 5½ percent in 2007, mostly reflecting a further escalation in logging.** Logging has accelerated by over 50 percent year-on-year in January–April 2007 and shows no signs of abating given strong international demand, especially from China. However, nonlogging growth is expected to slow to 3½ percent, as fish and traditional crops are contracting, while palm oil will contribute about 1 percentage point to overall growth.[2] Despite much higher logging exports, the current account deficit is expected to widen to 40 percent of GDP due to imports related to the gold mine (17 percent of GDP). Nevertheless, continued strong aid flows and FDI are expected to keep reserve cover adequate (Table 5). Inflation is projected to ease to 7 percent.

8. **Absent an acceleration of key reforms, even the modest per capita income growth recently achieved is unlikely to be sustained over the medium term.** In the baseline scenario, which assumes RAMSI and donor support, an unchanged pace of reforms, and no new major projects, growth is projected to decline to 1½ percent by 2010 and average 3 percent in 2007–12 (nonlogging at about 3¾ percent), compared to population growth rate of almost 3 percent (Table 6). Although aid inflows—most of which are channeled outside the budget—are projected to fall by half, the effect on growth is likely to be limited because the decline will affect mostly technical assistance (representing over 60 percent of total) as capacity improves. Logging is projected to remain broadly at the current rate until 2009 and decline sharply thereafter. With project-related imports falling sharply once the rehabilitation of the gold mine is completed, the start of gold exports from 2008 and the planned expansion of palm oil production should help narrow the current account deficit considerably over the medium term, notwithstanding the decline of logging and diminishing aid flows. The reserve import cover is expected to fall, but remain above three months (Table 7).

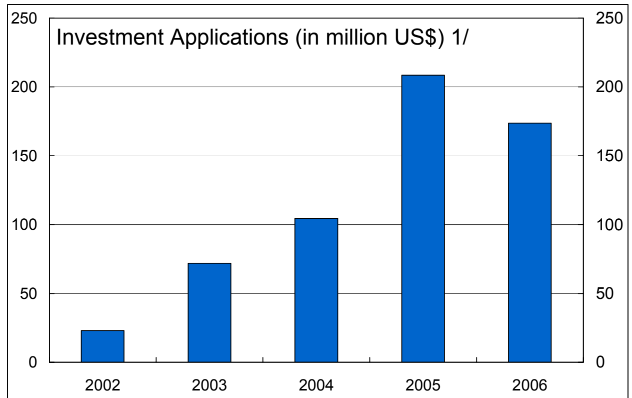




[2] The April tsunami is expected to have a negligible impact on growth. Logging remained unscathed; tourism is not a main growth source; and rebuilding activities could provide some stimulus.

9. **Risks to the baseline scenario remain tilted to the downside.** Potential risks stem mainly from: political instability, disruption to law and order, slippages in fiscal discipline, and interruptions in aid flows. Adverse shocks to commodity prices also remain a significant risk, given the highly-concentrated commodity export base.

10. **The staff's alternative scenario illustrates the improvements in living standards that could be achieved with targeted and concerted reform efforts.** Nonlogging growth could increase to about 5–6 percent with new investment projects taking place, and overall growth could average 4¼ percent, implying annual per capita income growth of about 1½ percent (Table 8). The current account deficit would narrow slightly more than in the baseline scenario, with stronger export growth partly offset by more imports. Higher fiscal revenue from expanding nonlogging activities and a comprehensive tax reform would create space for more government spending. Samoa and Mauritius provide clear examples of the growth benefits that can result from well-targeted reforms in small island economies. In the Solomon Islands, the rise in foreign investment applications since the new Investment Act came into force suggests that accelerating reforms along the lines discussed below could quickly translate into higher investment and growth.



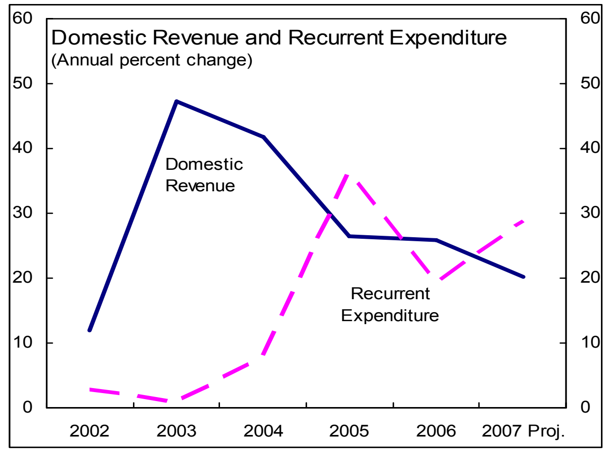
1/ The new Foreign Investment Act became effective in June 2006.

III. Policy Discussions

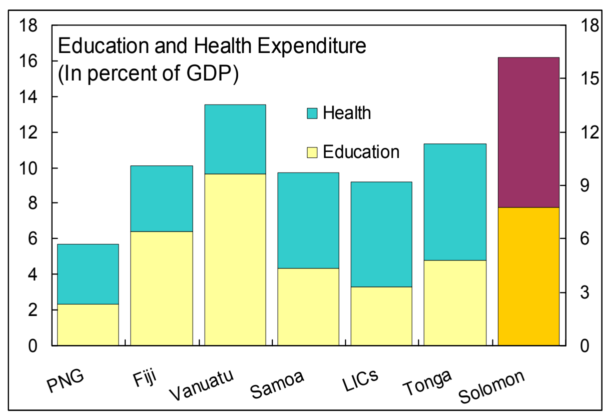
11. **The authorities are aware of the need to generate higher nonlogging growth, but an overarching development strategy is lacking.** Given the urgency of replacing logging, the authorities plan to facilitate investment in sectors that take advantage of the country's natural resources and low-cost labor, such as fishing, mining, palm oil, and tourism. They added that reforms to encourage more sustainable forestry management would become feasible once alternative growth sources have taken off. Yet, they recognized that there is still a need to adopt a country-led poverty reduction and growth (PRS) strategy that clearly identifies priorities, sequencing, implementable actions linked to budgets, and evaluation mechanisms.

12. **In the face of impending fiscal pressures and growth challenges, discussions centered on immediate policy priorities to facilitate faster sustainable development.** As the authorities broadly agreed with the medium-term outlook, the focus was on measures to: (i) maintain fiscal discipline and create additional fiscal space for priority spending within a medium-term framework; and (ii) make progress on implementing key structural reforms that would ease binding constraints to higher private sector-led growth.

A. Fiscal Policy and Debt



13. **The 2007 Budget outcome will likely be stronger than anticipated but appears too expansionary.** Compared to an estimated 4 percent of GDP surplus in 2006, the budget envisages an overall deficit of ¾ percent of GDP, although the staff projects a surplus of ½ percent because of higher logging revenue and investment underspending. The authorities have made commendable progress in lowering import duties, and reducing statutory and discretionary exemptions. Also, for the first time since 2003, reference prices of logs were raised. However, more than in previous years, revenue overperformance and investment underspending compared to the budget will be offset by higher spending on wages and goods and services. Current spending is projected to surge by 29 percent compared to a 20 percent increase in domestic revenue. This risks stoking inflation pressures and ignores looming medium-term challenges. The authorities argued that some expansion is warranted, especially in the social sectors and on wages, as the average civil service wage remains low.



14. **Over the medium term, budget pressures are bound to become severe.** They arise mainly from: (i) lower logging revenue while some major new projects have been granted generous tax concessions; (ii) rising recurrent costs of government and donor-funded investment projects; (iii) higher allocations for infrastructure; (iv) the need to eventually take over donor-funded recurrent spending; and (v) debt repayments and arrears settlement. Also, the authorities stated that, while spending on health and education is high by cross-country comparisons, there is pent-up demand for higher social spending.

15. **A medium-term budget framework would help manage fiscal pressures and ensure further progress toward debt sustainability.** Though declining, public sector debt remains uncomfortably high and contingent liabilities could rise (see below). With government deposits the only source of financing, and given debt repayments and the projected revenue path absent comprehensive tax reform, current expenditure would need to be reduced by some 3 percentage points of GDP, starting in 2008, to keep the primary domestic surplus at around ½ percent of GDP over the medium term and thereby reduce

debt.[3] The authorities agreed to avoid new borrowing for now and noted that the 2008 budget will be more forward-looking and prioritize expenditure better. However, they stated that spending cuts would be implemented only if revenues weaken. Staff cautioned that delaying the adjustment will make it more abrupt and possibly result in undue cuts in priority spending.

16. **Additional revenue efforts are planned.** While revenues have increased sharply, the effective import duty rate has declined to under 4 percent reflecting weak collection from customs, and reference prices of logs remain about 50 percent below international prices resulting in foregone annual revenue of around 3 percentage points of GDP. The authorities are upgrading systems and skills in customs to improve revenue collection. The Minister of Finance also committed to raising reference log prices by a further 20 percent by mid-year and adopting an automatic price adjustment mechanism to prevent future deviations from market prices. The registration of businesses is a welcome step toward a broad-based consumption tax which the authorities may introduce in the longer term.

17. **Strengthened expenditure control and efficiency are necessary to maintain financial stability and improve service delivery.** The rapid growth in spending over the last few years reflects the resumption of government operations after the conflict, but at around 33 percent of GDP current expenditures are significantly higher than in most LICs. Better expenditure allocation would create fiscal space for higher development spending as aid dependence is reduced, and on operations and maintenance as ongoing projects are completed. The authorities agreed that a system that links budget allocations to agencies' performance in achieving policy outcomes would be highly desirable.

18. **The high and rising civil service wage bill calls for tighter payroll control and improved service delivery.** The recent Special Audit Report on the Treasury Payroll has recommended critical measures including improving the monitoring of entry, exit, and attendance rates, and achieving closer coordination between Ministries, the Public Service and Teachers' Commissions, and the Treasury payroll. In addition, to improve incentives for better service delivery and move toward a leaner and more responsive civil service, the wage structure should be decompressed and preparations for the adoption of a performance-based remuneration system started. A census and functional review of the civil service would also set the stage for a comprehensive reform. The authorities agreed to tighten internal controls and practices related to the payroll, but emphasized that rebuilding a stronger middle-management is key to improving civil service performance.

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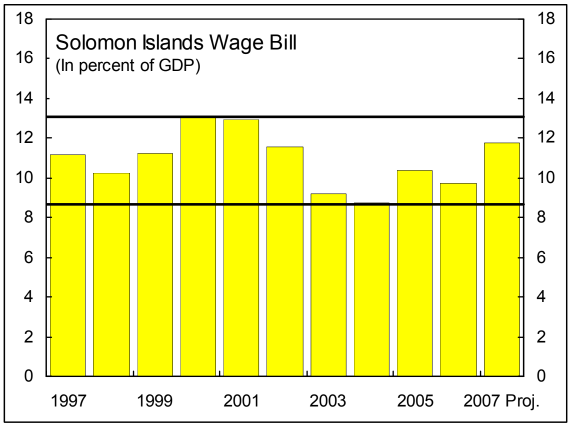
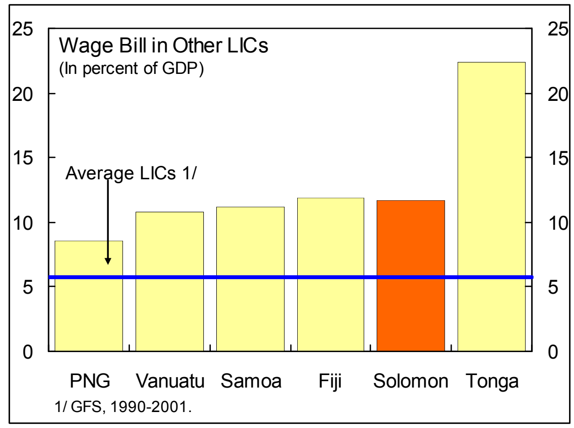
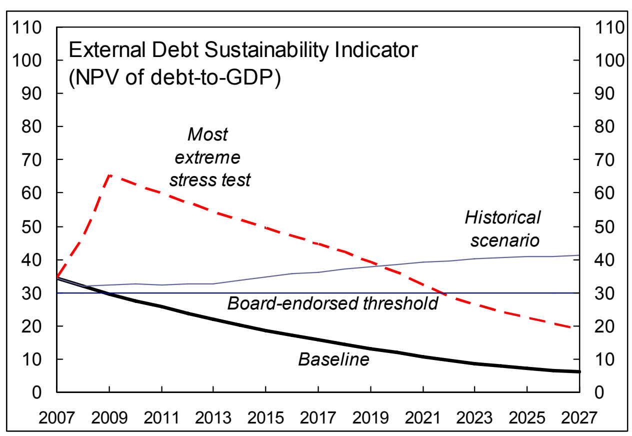
[3] This adjustment is larger-than-previously recommended due to the sharper projected decline in logging revenue, partially compensated by gold revenues.





19. **Budget preparation is improving, but public financial management could be strengthened.** The 2007 Budget contained more accurate information on aid flows and included some donor-funded health spending. For the 2008 Budget, the Expenditure Review sub-committee of the Cabinet (ERC) has been set up to agree early on key expenditure priorities, take into account recurrent costs of projects, and integrate more closely the recurrent and development budgets. The authorities are reviewing the revised Finance Instructions that would enhance expenditure control and accountability. Staff also considered that the appointment of an accountant-general is necessary to reinvigorate public financial management reform. These improvements, together with the adoption of a PRS and improved capacity, would also set the stage for the gradual integration of more aid into the budget.

20. **The authorities agreed that government debt remains high and vulnerable to shocks and maintained their commitment to further regularization.** Reflecting mainly the restructuring of debt owed to the central bank, total government debt fell to 73 percent of GDP in 2006, from 81 percent in 2005. However, the Net Present Value (NPV) of external debt to GDP ratio at 37 percent remained above the Board-endorsed threshold (Supplement I). The authorities hoped that additional relief would result from the review of the Honiara Club agreement soon to be concluded by one major creditor.[4] In the baseline scenario, assuming no new borrowing, all debt indicators



[4] The Honiara Club is a forum convened by the government in 2005 to seek debt relief from official creditors.

decline below thresholds in 2009. However, debt would rise sharply with even a temporary decline in export and GDP growth or a return of growth and the primary balance to historical levels. Moreover, most contingent liabilities (14 percent of GDP at end-2006) are likely to materialize and more could arise, given the SOEs' weak financial positions.

21. **The authorities did not share the staff's sense of urgency in tackling the SOEs' difficulties.** Several SOEs continue to incur arrears, depend on government support, provide poor services, and some have borrowed commercially. The bulk of identified contingent liabilities relate to the Solomon Islands Electricity Authority (SIEA) and the Water Authority (SIWA). However, the management contracts for the two utilities, recommended by the World Bank and long in the works, have yet to be tendered. Privatization plans for Solomon Airlines have been shelved. The authorities agreed that SOEs should operate on a more commercial basis and pointed to their plans to update accounts, introduce a new bill to improve governance, and increase private participation, but emphasized their social benefits. Staff cautioned that SOEs should not borrow until their finances have stabilized and suggested that the government should make any support more transparent and conditional on performance improvements. Steps toward the privatization of the marina and the fishing company are welcome, provided transparent tender procedures are used. Finally, the authorities could not commit to the liquidation of the DBSI, even though several commercially-based schemes to extend access to financial services in rural areas are being implemented.[5]

22. **The NPF's profitability is improving, but the government attaches low priority to the new bill.** After successful asset recovery and restructuring, the NPF's nonperforming assets are estimated to have declined to below 10 percent, and its net operational income to assets ratio rose to 4 percent in 2006 from 1½ percent in 2005. The NPF is also increasing its investments abroad, which should boost returns without undue risks, provided the newly-approved guidelines are applied conservatively. However, the government's proposal that the NPF acquire the Solomon Islands Home Finance Limited (SIHFL) could have an adverse effect if a significant share of SIHFL's assets are impaired. The authorities explained that SIHFL would become a subsidiary to which the existing NPF's housing loans would be transferred and would be managed at arms' length, allowing the NPF to concentrate on generating higher returns for its contributors. Staff countered that passage of the NPF bill is needed to clarify the NPF's objectives, improve governance, and ensure investment decisions are commercially based, but the authorities commented that political support for the bill is weak.

[5] A rural and small businesses credit scheme is administered by commercial banks and the government's guarantee is capped. Also, the government is providing capital transfers for additional mobile banks and ATMs.

B. Structural Reforms

23. **The authorities noted advances on several fronts of the reform agenda, while staff stressed that a sharper focus on the binding constraints to growth could yield higher payoffs.** Although some progress on structural reforms has been achieved, capacity constraints, entrenched vested interests, and infrequent parliamentary sessions have contributed to delays (Table 9). Staff encouraged the authorities to better target reforms, as tackling many problems simultaneously can lead to poor sequencing and prioritization, and further burden weak implementation capacity.

24. **Staff analysis suggests that low investment returns pose critical obstacles to growth**. Low social returns stem mainly from high costs of doing business—in particular, costly and unreliable utilities, weak transport infrastructure, and shortages of skilled labor (Box 1). The low share of returns that accrues to private investors appears related to governance issues, including opaque rules, perceptions that the government can exercise discretion and renege on previous commitments, and uncertainties surrounding land tenure. Lack of financing does not seem to be a binding constraint given the excess liquidity in the banking system and strong aid inflows.

25. **Improving utilities, transportation, and the predictability of the investment environment are critical elements in fostering private sector growth.** The authorities agreed with the need to improve the operations of SIEA and SIWA, but the timeframe for the management contracts remains unclear. Attempts to introduce competition in the telecommunications sector have led to reduced telephone costs, but legal procedures have stalled the process. The road network is being upgraded with the Asian Development Bank's assistance, but airline and shipping services remain unreliable. Staff also underscored the importance of maintaining clearly-defined and transparent rules, minimizing the use of negotiated tax agreements and exemptions for individual investors, and improving the commercial dispute resolution system. The authorities pointed to improvements in the business environment with the new Investment Act and streamlined work and residency permits procedures, and also noted their plans to eliminate provincial business licenses and modernize the Companies' Act. They added that land tenure problems cut across all sectors, but reforms will take time.

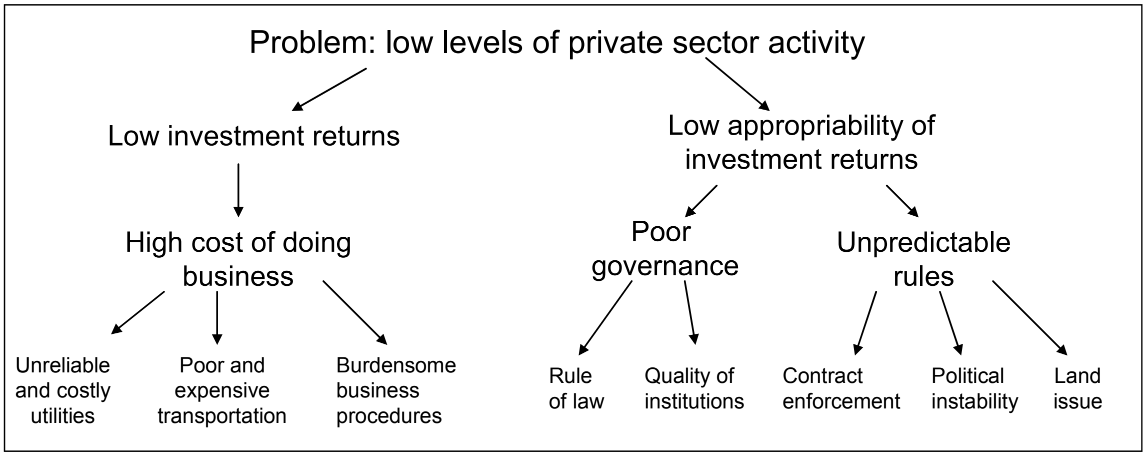
C. Exchange Rate and Monetary Policies

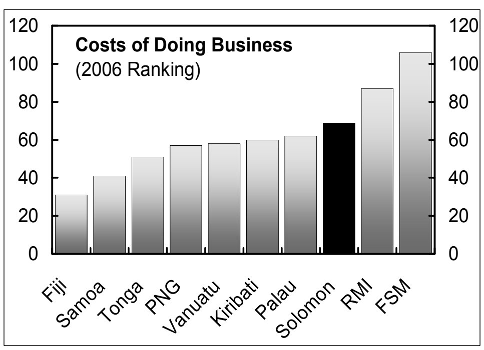
26. **Competitiveness appears adequate, but wage increases could erode it.** The real effective exchange rate (REER) appreciated slightly in 2005–06 and export shares increased somewhat. Despite a decline in 2006, growth in nonlogging export volumes has been robust in recent years and is expected to increase with the start of gold exports in 2008 and continued expansion of palm oil production, contributing to over half of the decline in the current account deficit over the medium term. Furthermore, the recent high volatility of nonlogging exports does not appear related to competitiveness. Nevertheless, the profitability

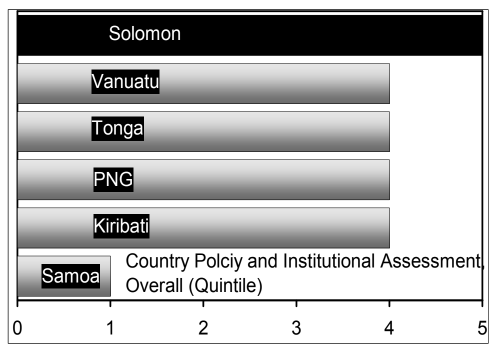
Box 1. Identifying Binding Constraints to Growth

The Solomon Islands face certain unavoidable impediments to growth as a result of remoteness and sparse population, but other constraints could be addressed through structural reforms.

The Hausmann, Rodrik, and Velasco diagnostic framework[6] is used to identify which among the following general constraints are binding: (i) inadequate returns to investment; (ii) low private sector share of investment returns (appropriability); and (iii) inadequate access to finance. It then asks which factors lead to these problems. In the Solomon Islands, poor investment returns and low appropriability seem the most relevant constraints as evidenced by high business costs and poor governance and predictability of government rules.







Business Costs

The Solomon Islands ranks 69th out of 175 countries in the World Bank's (WB) cost of doing business indicators, one of the highest in the region. The Asian Development Bank (AsDB) and WB reports and interviews with firms point to lack of infrastructure, expensive and unreliable transport, high electricity and communications costs, land issues, a burdensome regulatory system, and scarce skilled labor as major problems. For instance, high electricity costs have a large impact on the gold mine's investment decisions and both the gold mine and the palm oil company are seeking alternative power-generating options since the state-owned

[6] Hausmann, Rodrik, and Velasco (2005), "Growth Diagnostics," Harvard University, Cambridge, Massachusetts.

electricity company cannot provide service to most parts of the country. Indicators show that electricity, internet, and telephone charges are expensive relative to comparator countries. Business start-up costs are also high.

Selected Indicators of Business Costs

	Electricity Rates (2005)	Cost of Telephone Calls to the U.S. (US$/minute, 2004)	Price Basket for Internet (US$/month, 2003)	Access to Electricity (percent of population, 1999-02)
Vanuatu	0.2163	1.56-2.00	46.70	25
Micronesia	0.1933	…	…	…
Kiribati	0.2350	2.42-3.03	…	…
Tonga	0.1816	0.75-0.80	45.45	85
Samoa	0.1800	1.74	42.97	60
American Samoa	0.1642	…	…	…
Kosrae FSM	0.1583	…	…	…
Solomon Islands	**0.1701**	**1.65-2.96**	**91.15**	**10**
Marshall Islands	0.1467	2.00	20.00	100
Fiji	0.0857	1.46	31.74	60
Palau	0.1067	1.15-1.5		60
Papua New Guinea	0.0596	…	20.00	…
Carribbean Islands 1/			21.29	95.3

Sources: ADB and WB reports, and World Development Indicators.
1/ Includes data, where available, for Dominica, Grenada, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, and Antigua and Barbuda.

Low Private Appropriability

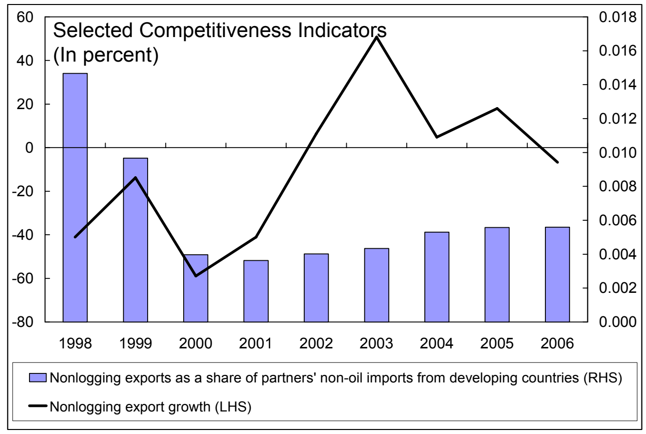
The findings of the AsDB's private sector assessment report corroborate the widely-held view that corruption is endemic. The country is at the lowest quintile on the WB's Country Policy and Institutional Assessment ranking and scores the lowest in the region in the Kauffman Rule of Law Index. Low private returns are also associated with poor contract enforcement and uncertainties surrounding land tenure, given that more than 80 percent of the land is customarily-owned. A WB survey of contract enforcement ranks the Solomon Islands 102nd out of 175 countries.

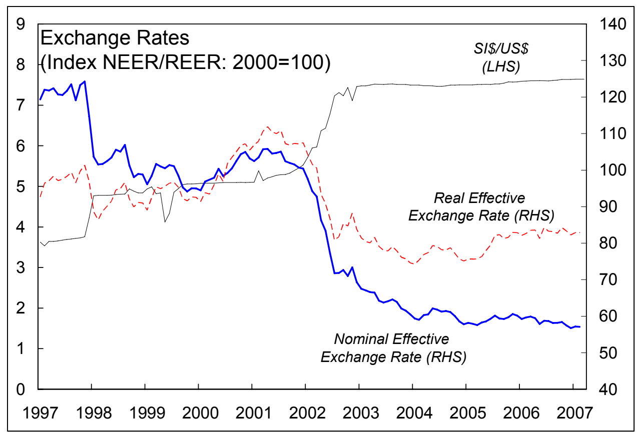
Selected Indicators of Business Costs and Governance Constraints

	Starting a Business-- (cost in percent of income per capita)	Dealing with Licenses (cost in percent of income per capita)	Enforcing Contracts (rank out of 175)	Kauffman's Rule of Law Index (from -2.5 to 2.5) 1/
New Zealand	0.2	27.2	15	1.93
Australia	1.8	13.8	7	1.83
Palau	4.9	6.8	151	0.77
Mauritius	8	13.7	109	0.82
Seychelles	9.1	51.3	73	-0.03
Tonga	10.3	174.6	126	0.18
Marshall Islands	18.1	37.6	103	-0.22
Fiji	25.8	41.7	86	-0.09
Papua New Guinea	28.2	110	88	-0.76
Samoa	45.5	105.1	54	0.84
Kiribati	50	545.2	136	0.36
Solomon Islands	**68.9**	**501.1**	**102**	**-1.01**
Micronesia	135.9	21.3	139	0.44

Source: World Bank--Doing Business Data , 2006.
1/ Minus 2.5 is the lowest and 2.5 the highest score.

of labor-intensive projects—such as the palm oil plantation—would be threatened if a recent proposal by a Minister to quintuple the minimum wage (not adjusted since 1996) resulted in substantial wage increases.

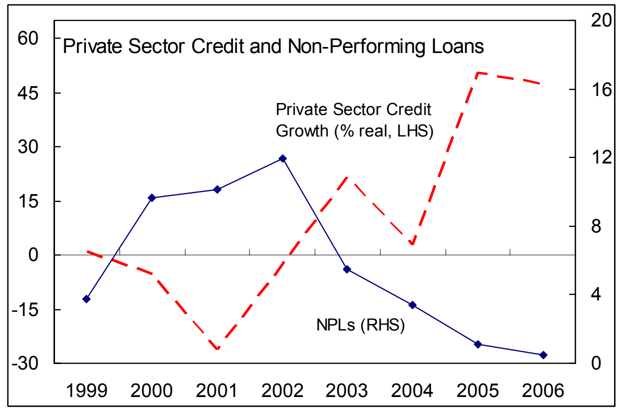




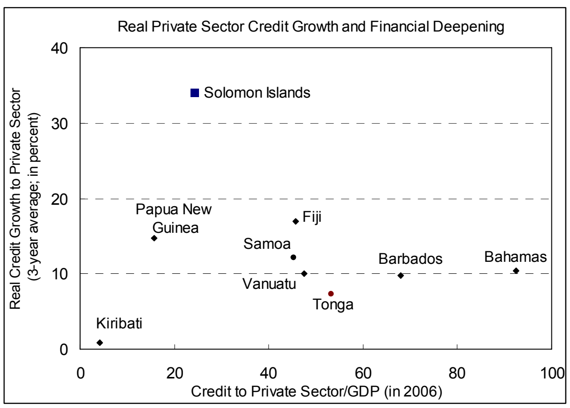
27. **The staff continued to support the current exchange rate policy.** Amid strong aid and FDI inflows, the CBSI has stabilized the value of the SI dollar against the U.S. dollar. As projects financed by these inflows are implemented, reserves should be allowed to decline. Should downward pressure on the exchange rate materialize from other sources, the exchange rate should be allowed to adjust since the current policy framework could not support a pegged exchange rate. The staff added that domestic policy slippages should be countered with financial tightening.

28. **The CBSI remains committed to counter inflationary pressures if they resurface.** Inflation has moderated, but could be rekindled by wage increases, donor spending, and rapid credit expansion, especially given supply constraints. The CBSI indicated that measures would be introduced if inflation exceeds 10 percent for three consecutive months or if reserves come under pressure. The staff recommended a more forward-looking approach by taking action as soon as the inflation outlook deteriorates. The planned offshore investments of the NPF and the CBSI’s remunerated standing deposit facilities would help absorb excess liquidity and strengthen monetary management. If action is needed before the standing deposit facilities are introduced, the CBSI would have to resort to raising reserve requirements or introducing credit ceilings. Developing additional market-based instruments as the treasury bill market evolves would also be desirable.

29. **The CBSI considered that risks related to rapid credit growth are contained.** Credit to the private sector has nearly doubled since 2005, driven by loans to personal, forestry, and distribution sectors, but financial intermediation remains low by regional standards. Moreover, banks’ credit appraisals appear cautious, most lending is collateralized, and capital adequacy ratios are above the 10 percent prudential norm. However, the CBSI



should require loans to be classified as nonperforming after 90 days and end the current practice of allowing banks discretion when they deem the collateral sufficient to recover the loan. Data on house prices and rents should be collected, as real estate loans are the fastest growing segment of the loan portfolio. To reduce concentration risks, the CBSI could consider applying the single customer exposure limit to the capital of local bank branches and allowing a transition period as adjustments would be necessary.[7] A simple credit registry would also enhance credit assessments.



Financial Soundness Indicators

(In percent)

	2002	2003	2004	2005	2006	2007Q1
Risk weighted capital ratio	28.2	26.9	27.0	24.1	16.5	17.1
NPLs/Total Gross Loans	11.9	5.5	3.4	1.1	0.5	0.5
Return on assets	4.7	5.7	5.0	4.2	4.8	5.5
Return on equity	24.2	32.6	31.9	26.5	32.3	42.1
Liquid assets/Total assets	16.5	18.6	33.6	31.2	24.5	21.0

Source: CBSI.

D. Statistical Issues

30. **Some measures are being taken to address serious deficiencies in statistics, which hamper surveillance.** The National Statistics Office has recently published a Household Income and Expenditure Survey which will be used to rebase GDP and calculate a national consumer price index (Annex VI). However, SOEs' accounts are still lacking, monitoring of the MDGs is weak, and balance of payments statistics are poor.

IV. Staff Appraisal

31. **Macroeconomic stability will likely be sustained in the near term, but political uncertainty and an acceleration in logging have heightened the economy's vulnerability.** With RAMSI and donor engagement, financial stability should continue, but the tensions of

[7] With the recent foreign acquisition of the National Bank of the Solomon Islands, all banks are branches of nonresident banks. Currently, the single customer exposure limit applies to the capital of the parent bank.

the past year have highlighted that even the fragile stability achieved so far cannot be taken for granted. Also, the recent escalation in logging has brought forward the exhaustion of the natural forest and intensified the urgency of generating alternative sources of growth to prevent living standards from falling.

32. **Medium-term challenges require a more integrated and forward-looking approach to economic reform and immediate action.** Progress on structural reforms is welcome, but limited. The country needs a medium-term national development strategy that can serve as the umbrella framework for all programs and projects, which should achieve enhanced policy and aid effectiveness. Also, pressures on the budget in the medium term are almost certain to intensify due to lower logging revenues and aid inflows and higher infrastructure and maintenance spending. Now is a propitious time to accelerate reforms, given the degree of macroeconomic stability achieved and the current favorable international backdrop.

33. **A medium-term budget framework that explicitly recognizes future pressures and financing constraints and continues to make progress toward debt sustainability is urgently needed.** Public sector debt remains at high risk of distress. The NPV of external debt to GDP is projected to fall below the Board-endorsed threshold only in 2009 and several shocks could interrupt the declining trend of recent years. Hence, the government should sustain its efforts to regularize debt and uphold its policy of no new borrowing at least until all debt indicators fall below the thresholds.

34. **With the 2007 Budget too expansionary, the likely overperformance on revenue should be saved and current expenditure kept strictly within budget.** Saving a large share of the overperformance would ease the transition until new sources of revenue come on stream when logging falls, or could be used to reduce debt or cushion shocks. This policy would also contribute to contain inflation pressures.

35. **Adjusting the reference prices of logs could provide a powerful signal of the government's commitment to additional revenue reform.** This year's increase is welcome, but reference log prices should be raised further without delay and an automatic price adjustment mechanism introduced. Strides taken in broadening the tax base are commendable and preparations for introducing a VAT should continue. The results obtained by the inland revenue suggest that better administration can raise revenue substantially, something that has yet to happen on the customs side.

36. **Enhanced expenditure control, composition, and efficiency should be key elements of the fiscal strategy.** Recent increases in current expenditure cannot be sustained and will have to be partly reversed over the medium term. The wage bill is high and continues to rise, while domestically-financed investment spending remains low. Not only should generalized wage increases be avoided and future increases linked to skills and performance to boost service delivery, but tighter payroll controls should be implemented

immediately. The setting up of the ERC sub-committee should help improve expenditure prioritization and implementation of investment projects. Strengthening public financial management remains at the core of ensuring efficient and accountable use of public funds.

37. **Vigorously pursuing SOE reform and strengthening the NPF are crucial to minimize future contingent liabilities to the budget and strengthen governance.** The implementation of the SIEA and SIWA management contracts would provide a convincing signal of the authorities' commitment, and consideration should be given to the commercialization of Solomon Airlines. As recommended in previous consultations, the DBSI should be liquidated. Passage of the NPF bill is required to enhance governance, which holds the key to raising profitability. Even before the bill is passed, the authorities should continue to work toward increasing the risk-adjusted returns on the NPF's assets by ensuring investment decisions follow purely commercial criteria.

38. **Reforms focused on removing binding constraints to growth are likely to attain higher payoffs**. Lowering the costs and improving service delivery of the utilities, together with continuing to upgrade transport infrastructure, would raise investment returns. Maintaining a level playing field would give investors greater certainty that they can recoup a higher share of their investment returns.

39. **The level of competitiveness appears adequate and the present exchange rate policy remains appropriate.** Despite a slight appreciation of the REER in 2005–06, nonlogging export growth is expected to accelerate in the next few years with increasing palm oil production and gold coming on stream. However, substantial increases in the minimum wage would be detrimental. Stabilizing the exchange rate as inflows continue to be strong remains advisable, but should downward pressure on the exchange rate materialize, the value of the currency should adjust.

40. **The CBSI is gearing up to be in a position to take measures quickly if inflation picks up.** Although inflation has moderated, demand pressures could reignite it. The planned introduction of standing deposits facilities to absorb the structural excess liquidity in the system would increase the CBSI's monetary control and enable it to take quick action if the inflation outlook deteriorates.

41. **Banks appear generally sound, but prudential measures should be tightened.** Despite the rapid increase in bank credit, financial intermediation is still low and banks appear to take a conservative approach to lending. Nevertheless, to ensure that asset quality remains high, the CBSI should intensify its surveillance, tighten loan classification, consider redefining the single customer exposure limit, and support the introduction of a credit registry.

42. **The statistical database should continue to be improved.** Despite some progress, the coverage and quality of the data are barely adequate for surveillance. Priority should be

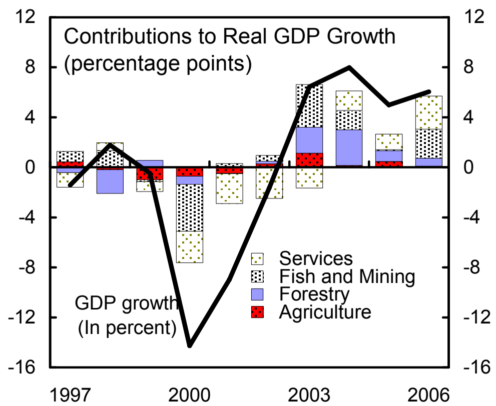
given to the new GDP statistics, SOEs' accounts, monitoring the MDGs, and balance of payments statistics.

43. It is proposed that the next Article IV consultation be held on the 12-month cycle.

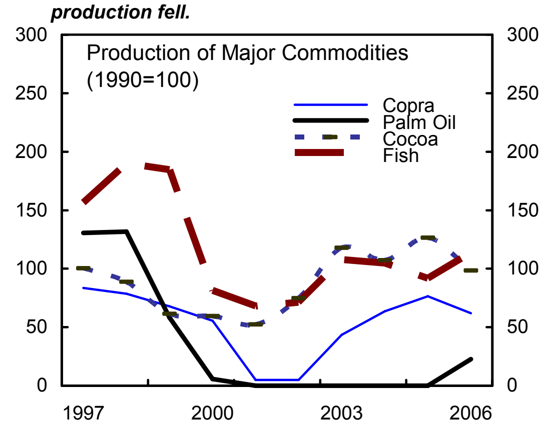
Figure 1. Solomon Islands: Production and Price Developments, 1986–2007 1/

Growth continued to be robust and inflation eased in 2006, but per capita income is still two-thirds of its pre-conflict level.

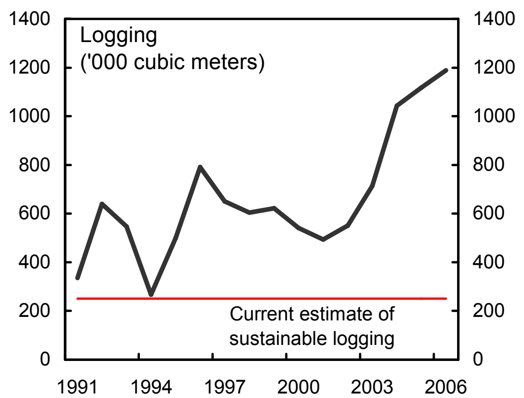
Fish and services were the main drivers of GDP growth in 2006.



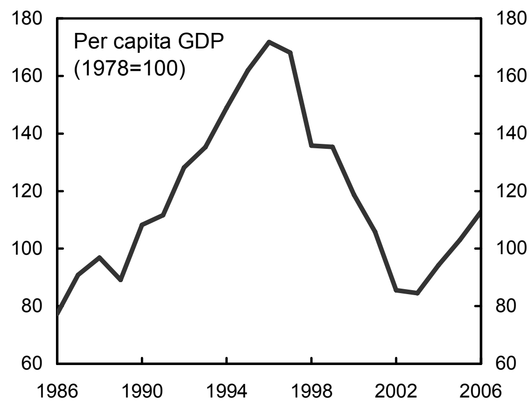
Palm oil production resumed and fish catch recovered in 2006, but cocoa and copra production fell.



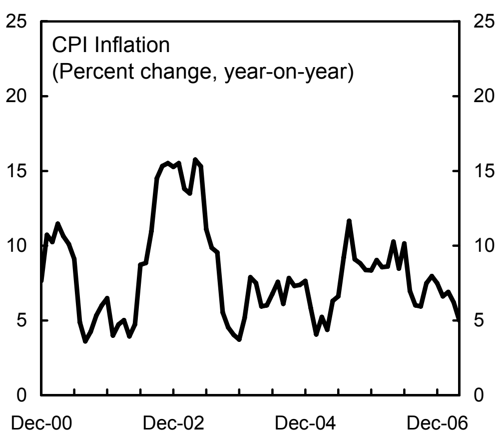
After rising markedly in 2004, logging continued to increase in 2005-06 and has accelerated in 2007.



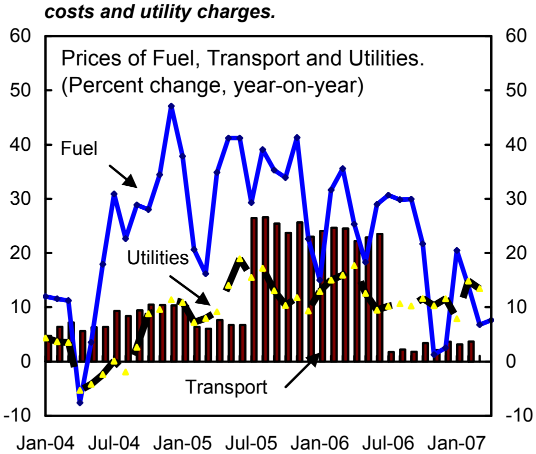
Per capita income continued to recover, but is still about two-thirds of its pre-conflict level.



Inflation moderated in 2006...



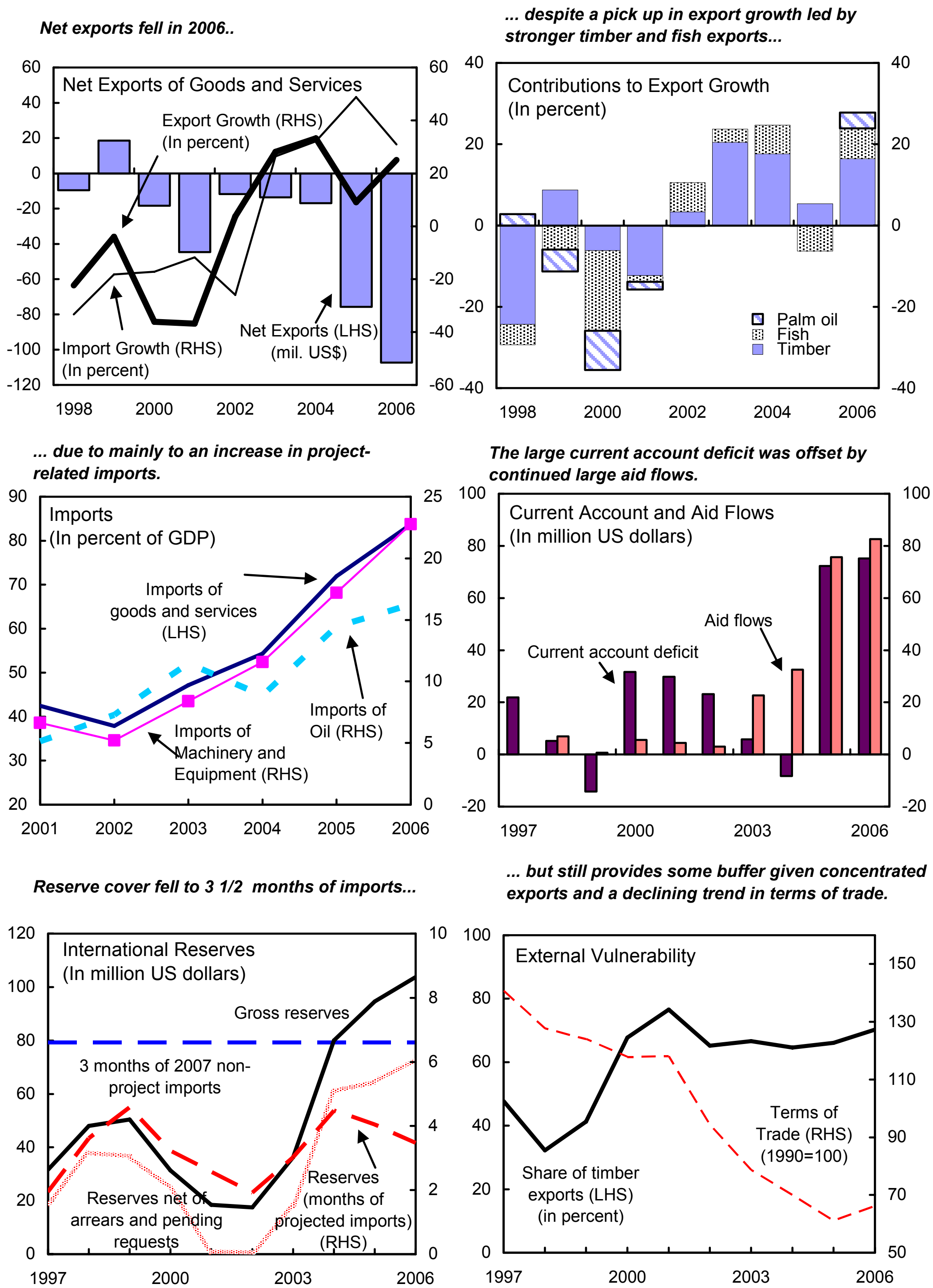
...as declining fuel prices led to lower transport costs and utility charges.



Sources: Data provided by the authorities, WEO and IFS databases; and Fund staff estimates.
1/ 2006 GDP is an estimate.

Figure 2. Solomon Islands: External Sector Developments, 1997–2006 1/

The large current account deficit continued to be more than offset by strong aid inflows.

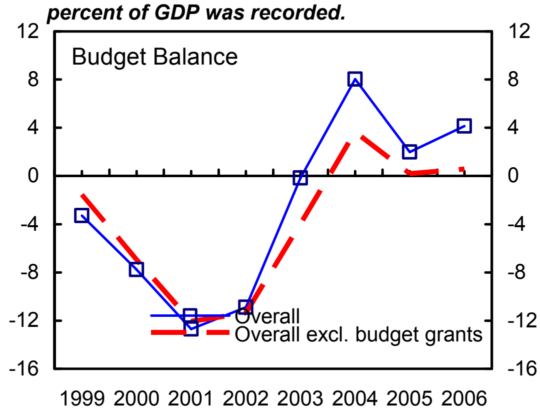


Sources: Data provided by the authorities, WEO and IFS databases; and Fund staff estimates.
1/ Prior to 2002, import figures reflect foreign exchange transactions data. From 2002 onwards, import figures are based on customs data. From 2005 onwards, aid flows are based on more accurate estimates from the authorities.

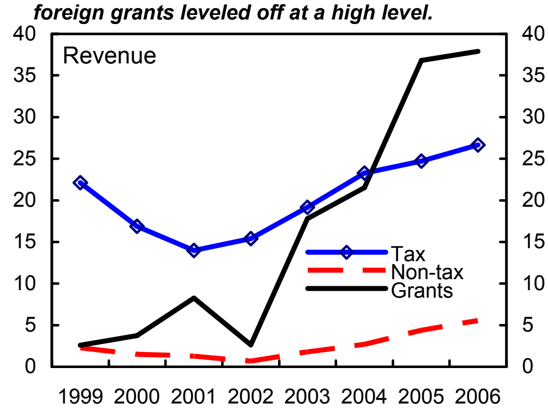
Figure 3. Solomon Islands: Fiscal Developments, 1999–2006 1/
(In percent of GDP)

The central government's budget was contractionary in 2006.

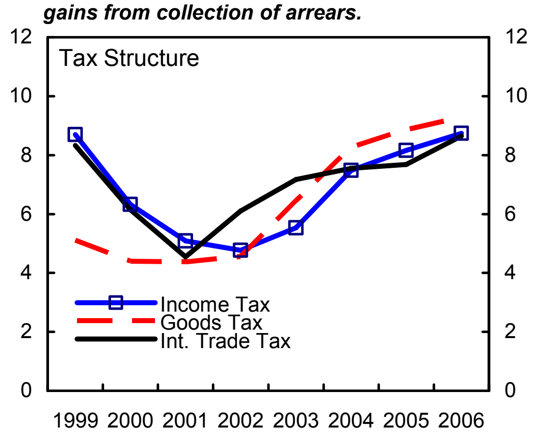
In 2006, an overall budget surplus of over 4 percent of GDP was recorded.



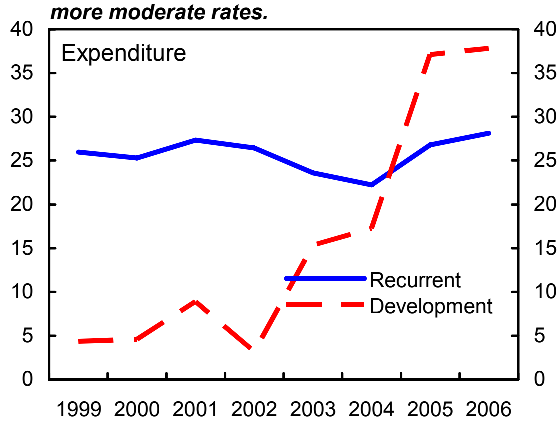
The domestic revenue effort was maintained; foreign grants leveled off at a high level.



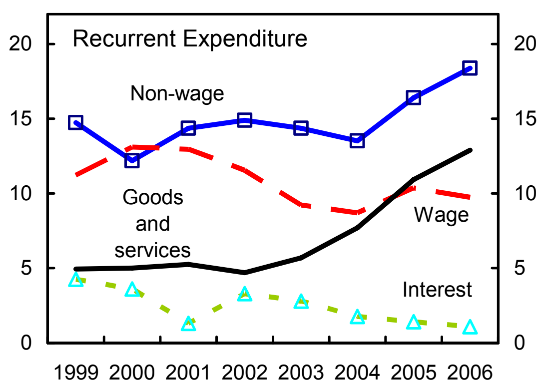
Tax revenues were boosted by a decline in log exemptions, improved compliance, and one-off gains from collection of arrears.



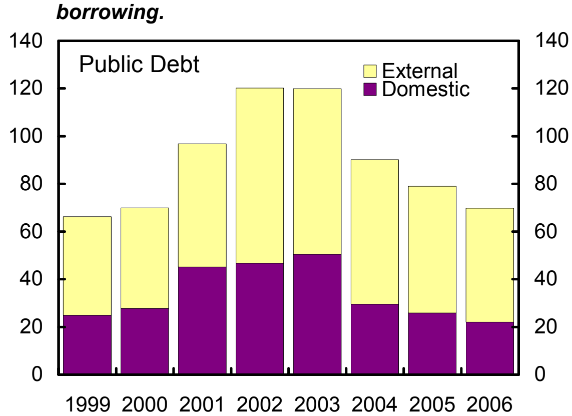
Following recent sharp increases, both recurrent and development spending grew at more moderate rates.



The rise in recurrent outlays was driven by non-wage spending, but the wage bill will surge in 2007.



Public debt continued to fall due to growth, payment of arrears, debt forgiveness, and no new borrowing.

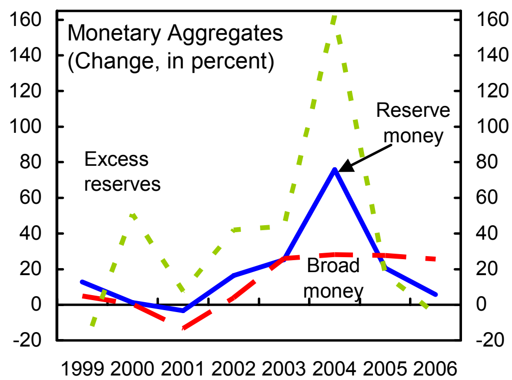


Sources: Data provided by the authorities and Fund staff estimates.
1/ 2006 data are partly estimated by Fund staff.

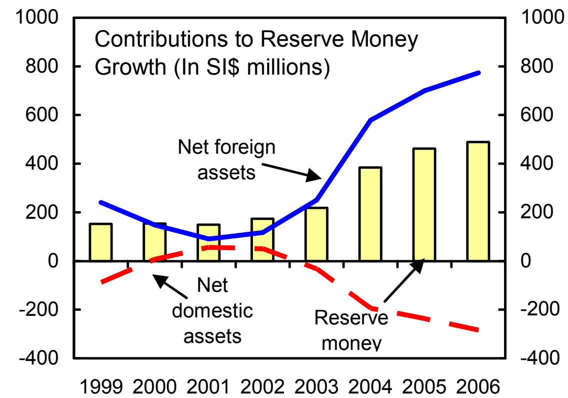
Figure 4. Solomon Islands: Monetary Sector Developments, 1999–2007

Growth in private sector credit remained high, while the banking sector's claims on government fell and excess liquidity declined slightly. The sector remains generally sound but loan risk exposure is rising.

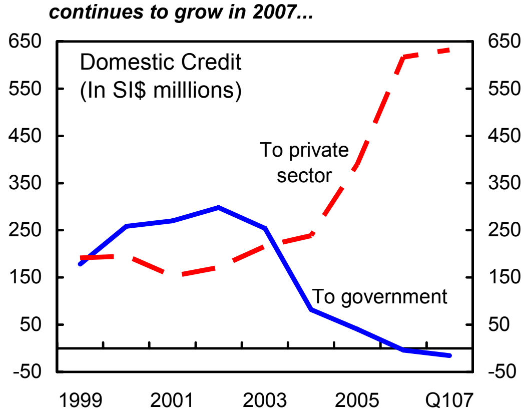
Monetary growth continued to decelerate in 2006...



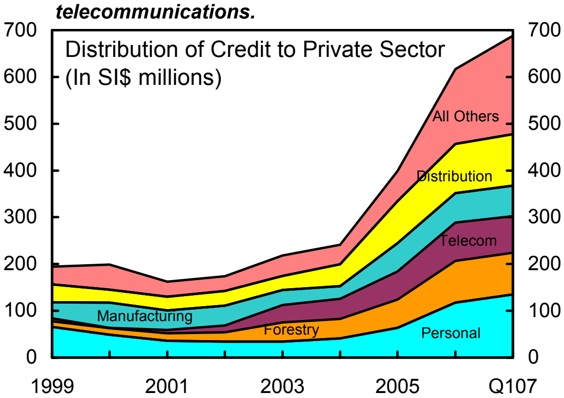
...reflecting a moderation in NFA growth, and a continued decline in NDA.



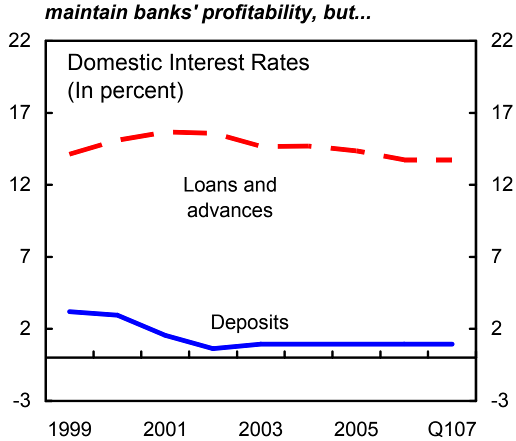
Net credit to the government fell, while private sector credit growth remained high and continues to grow in 2007...



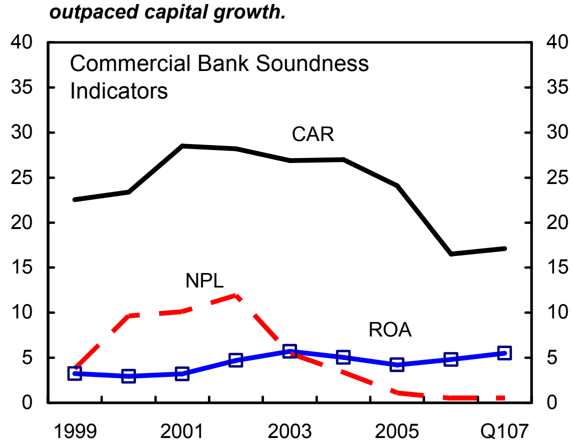
...driven by rapid expansion of personal loans as well as loans for forestry, distribution, and telecommunications.



Persistently large interest margins helped maintain banks' profitability, but...



...capital adequacy ratios fell as asset growth (loans) outpaced capital growth.



Sources: Data provided by the authorities and Fund staff estimates.

Table 1. Solomon Islands: Selected Economic Indicators, 2002–07

Nominal GDP (2006): US$336 million
Population (2006): 494,959
GDP per capita (2006): US$678
Quota: SDR 10.4 million

	2002	2003	2004	2005	2006 Est.	2007 Proj.
Growth and prices (percentage change)						
Real GDP	-1.6	6.4	8.0	5.0	6.1	5.4
Of which : Nonlogging	-1.9	4.6	5.5	4.5	6.0	3.6
CPI (period average)	9.3	10.0	6.9	7.3	8.1	6.3
CPI (end of period)	15.3	3.7	7.6	8.4	7.5	7.0
Per capita GDP (in US$)	514	508	566	619	678	709
Central government operations (percent of GDP)						
Total revenue and grants	18.7	38.8	47.5	65.9	70.1	69.0
Recurrent revenue	16.1	20.9	26.0	29.1	32.2	35.0
Grants	2.6	17.8	21.5	36.8	37.9	34.0
Total expenditure 1/	29.6	38.9	39.5	63.9	66.0	68.5
Recurrent expenditure	26.4	23.6	22.2	26.8	28.1	32.8
Development expenditure	3.2	15.4	17.2	37.1	37.8	35.7
Recurrent balance 2/	-9.9	1.2	8.1	4.1	6.8	4.4
Overall balance 3/	-10.9	-0.2	8.0	2.0	4.1	0.5
Foreign financing (net)	3.8	0.2	-0.9	2.6	0.9	0.2
Domestic financing (net)	-2.9	-9.2	-6.6	-2.1	-1.8	-0.8
Other	8.9	9.8	-2.3	-2.3	0.1	0.1
Stock of expenditure arrears (in percent of GDP, end of period) 4/	12.0	14.7	7.8	3.6	2.8	2.6
Central government debt (percent of GDP) 5/	113.3	120.4	90.2	81.3	72.8	66.7
Domestic	46.7	50.9	29.8	24.4	18.9	16.3
External	66.6	69.5	60.4	56.9	53.9	50.4
External debt (in US$ millions, end of period)	151.6	160.8	160.3	169.5	180.7	181.9
External debt service to exports of GNFS (accrual basis)	10.3	9.3	5.9	7.2	4.3	4.3
Monetary and credit (percentage change, end-year data)						
Net foreign assets	30.2	101.8	118.8	22.0	8.1	15.2
Net domestic assets	-4.8	-9.0	-64.4	63.2	108.2	24.9
Net domestic credit	11.0	-2.9	-34.7	37.6	37.7	26.3
Credit to private sector	12.2	26.1	10.5	63.1	62.5	23.2
Broad money	4.0	26.0	28.2	27.7	25.7	18.0
Interest rate (3-month t/bill rate, average) 6/	8.3	5.8	6.0	4.5	3.5	3.4
Balance of payments (US$ millions, unless otherwise indicated)						
Exports, f.o.b	57.8	74.2	96.7	102.5	120.4	146.2
Imports, c.i.f.	-69.1	-93.8	-121.4	-185.1	-250.6	-291.7
Current account	-23.2	-5.7	8.3	-72.3	-88.9	-144.4
(Percent of GDP)	-10.2	-2.5	3.1	-24.2	-26.5	-40.0
Capital account	6.3	21.1	28.1	82.5	94.6	152.6
Overall balance (accrual)	-16.9	15.3	36.4	10.3	5.7	8.2
Gross official reserves (US$ millions, end of period)	17.5	36.3	80.0	94.6	103.8	113.0
(in months of next year's imports of GNFS)	1.9	3.0	4.5	4.0	3.5	3.9
Exchange rate (SI$/US$, end of period) 6/	7.46	7.49	7.51	7.58	7.62	7.65
Real effective exchange rate (period average, 2000=100)	90.1	78.5	77.1	79.5	83.5	83.5
Nominal effective exchange rate (period average, 2000=100)	80.1	64.4	60.3	59.1	58.5	...

Sources: Data provided by the authorities; and Fund staff estimates.

1/ Expenditures are presented on an accrual basis.
2/ Includes recurrent budget grant support.
3/ Calculated from above-the-line data.
4/ Includes interest arrears.
5/ Includes arrears.
6/ As of May 30, 2007.

Table 2. Solomon Islands: Balance of Payments, 2002–07 1/

(In millions of U.S. dollars)

	2002	2003	2004	2005	2006 Est.	2007 Proj.
Current account balance	-23.2	-5.7	8.3	-72.3	-88.9	-144.4
Current account balance (excl. net pub. sec. transfers)	-29.8	-14.9	-1.4	-72.4	-89.9	-145.5
Trade balance	-11.3	-19.6	-24.7	-82.6	-130.2	-145.5
Merchandise exports, f.o.b.	57.8	74.2	96.7	102.5	120.4	146.2
Of which: Logging	37.7	49.5	62.6	67.7	84.6	108.4
Fish	10.5	12.4	17.6	11.5	19.2	18.3
Palm Oil	0.0	0.0	0.0	0.0	4.0	8.0
Merchandise imports, c.i.f.	69.1	93.8	121.4	185.1	250.6	291.7
Of which: Petroleum	16.6	26.6	23.5	43.1	54.4	55.2
Services and income (net)	-6.3	0.5	9.1	7.0	25.4	-13.1
Nonfactor services (net)	-0.4	6.0	7.7	6.8	23.0	-12.3
Exports	16.7	21.2	30.4	36.3	53.1	54.5
Imports	17.1	15.3	22.7	29.4	30.2	66.8
Net factor income from abroad	-5.9	-5.5	1.4	0.1	2.5	-0.8
Credit	2.7	3.5	8.5	8.5	11.4	12.7
Of which: Interest	0.5	0.7	2.5	3.1	4.4	5.5
Debit	8.6	9.0	7.1	8.3	9.0	13.4
Of which: Interest	4.4	5.2	3.2	2.5	2.1	3.0
Net current transfers	-5.5	13.4	23.9	3.4	15.9	14.1
Private sector	-12.1	4.2	14.2	3.2	14.9	13.0
Receipts	15.9	18.4	37.1	35.0	50.1	53.8
Payments	28.1	14.2	22.9	31.8	35.2	40.8
Public sector	6.6	9.2	9.7	0.2	1.0	1.1
Receipts	7.3	14.3	11.6	5.3	7.1	7.2
Of which: Unidentified grants	0.0	0.0	0.0	0.0	0.0	0.0
Payments	0.7	5.2	1.9	5.1	6.1	6.1
Capital account balance	6.3	21.1	28.1	82.5	94.6	152.6
Government sector	5.8	22.2	28.6	77.2	86.5	90.3
Medium- and long-term lending	2.7	-0.6	-4.0	-1.5	-0.1	0.3
Inflows	6.0	3.1	0.3	6.0	5.3	5.9
Amortization	3.3	3.6	4.3	7.5	5.4	5.6
Net Investment flow (projects)	3.1	22.7	32.5	78.7	86.6	90.0
Inflows	0.0	10.0	20.0	104.4	118.1	114.7
Outflows	0.0	0.0	0.0	25.7	31.5	24.7
Private sector	0.5	-1.1	-0.4	5.3	8.1	62.3
Investment activities (incl. FDI)	1.0	-0.1	0.3	7.4	5.9	33.8
Medium- and long-term lending	0.0	-0.7	-0.5	-1.7	7.0	41.7
Inflows	0.5	0.0	0.0	0.4	7.3	43.7
Amortization	0.5	0.8	0.5	2.1	0.3	2.0
Other flows	-0.5	-0.3	-0.3	-0.4	-4.8	-13.2
Overall balance (accrual)	-16.9	15.3	36.4	10.3	5.7	8.2
Commercial bank holdings (increase)	1.4	2.0	2.2	0.5	0.5	0.5
Errors, omissions, and valuation	14.1	2.3	5.8	-2.3	2.1	0.0
Exceptional financing	3.1	3.2	3.7	7.1	1.9	1.0
Interest arrears	4.1	3.1	2.3	-3.2	0.8	0.8
Amortization arrears	3.3	1.5	1.4	1.0	-0.2	0.0
Pending import requests	-4.3	-2.4	-1.5	-0.1	0.0	0.0
Debt forgiveness	0.0	1.0	1.5	9.4	1.3	0.2
Restructured arrears	0	0.0	0.0	0.0	0	0
Overall balance (cash)	-1.0	18.8	43.7	14.6	9.2	9.3
Memorandum items:						
Gross official reserves	17.5	36.3	80.0	94.6	103.8	113.0
(in months of next year's imports of GNFS)	1.9	3.0	4.5	4.0	3.5	3.9
(in months of next year's nonproject imports)	2.3	3.4	5.4	4.7	3.9	4.3
Net international reserves (NIR)	15.8	33.4	77.0	92.4	101.5	110.8
NIR excl. pending import requests and external arrears	0.6	17.9	61.0	64.6	73.1	81.6
(in months of next year's imports of GNFS)	0.1	1.5	3.4	2.8	2.4	2.8
External arrears (interest plus principal)	11.1	13.8	15.8	27.8	28.4	29.2
Exports GNFS–Value Growth	3.7	28.1	33.2	9.1	25.1	15.7
Exports GNFS–Volume Growth	-1.6	36.7	33.0	10.4	4.5	13.6
Logging Exports–Value Growth	4.4	31.4	26.4	8.3	24.8	28.2
Nonlogging Exports–Value Growth	82.5	22.8	38.3	1.5	3.2	5.4
Imports GNFS–Value Growth	-25.9	26.5	32.1	48.8	30.9	27.7
Imports GNFS–Volume Growth	-25.1	16.4	19.1	36.3	21.7	23.4
Current account (including transfers)/GDP	-10.2	-2.5	3.1	-24.2	-26.5	-40.0
Current account (excluding transfers)/GDP	-13.1	-6.4	-0.5	-24.3	-26.8	-40.3
Terms of trade (index: 1990=100)	94.4	78.7	69.9	61.1	66.2	66.5

Sources: Data provided by the authorities; and Fund staff estimates.

1/ Import figures from 2002 onwards are now based on customs data and net investment flow projects of the government from 2005 are based on more accurate estimates of aid flows from the authorities.

Table 3. Solomon Islands: Central Government Operations, 2002–07

(In percent of GDP)

	2002	2003	2004	2005	2006		2007	
					Budget	Est.	Budget	Proj.
Total revenue and grants	18.7	38.8	47.5	65.9	43.9	70.1	71.7	69.0
Total revenue	16.1	20.9	26.0	29.1	26.9	32.2	31.4	35.0
Tax revenue	15.4	19.1	23.3	24.7	23.6	26.7	27.1	30.8
Income and profits	4.8	5.5	7.5	8.2	7.4	8.7	8.6	8.8
Goods and services	4.6	6.4	8.3	8.9	8.9	9.3	9.1	10.9
International trade and transactions	6.1	7.2	7.6	7.7	7.2	8.6	9.4	11.1
Tax on logging	...	3.2	3.2	3.8	3.6	5.0	6.0	7.7
Other revenue	0.7	1.8	2.7	4.4	3.3	5.6	4.3	4.2
Stamp duty	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Licenses and fees	0.2	0.1	0.3	0.2	0.2	0.2	0.2	0.2
Miscellaneous revenue	0.3	1.4	2.2	3.9	2.9	5.1	3.8	3.8
Grants	2.6	17.8	21.5	36.8	17.0	37.9	40.3	34.0
Development grants 1/	2.2	14.0	17.1	35.0	15.2	35.2	38.1	31.8
Recurrent budget grants	0.5	3.8	4.4	1.8	1.8	2.7	2.2	2.2
Expenditure 2/	29.6	38.9	39.5	63.9	46.8	66.0	72.5	68.5
Recurrent expenditure	26.4	23.6	22.2	26.8	28.9	28.1	29.6	32.8
Compensation of employees	11.5	9.2	8.7	10.4	8.8	9.7	11.6	11.7
Goods and services	4.7	5.7	7.7	10.9	15.5	12.9	14.1	16.4
Of which: Recurrent costs of development spending 3/	--	--	--	--		--	--	1.7
Interest	3.3	2.8	1.8	1.4	1.2	1.1	1.3	1.3
Grants to provinces	0.9	2.0	2.5	1.5	2.4	2.4	2.2	2.2
Other 4/	5.8	3.7	1.4	2.6	1.0	2.0	0.4	1.2
Development expenditure	3.2	15.4	17.2	37.1	18.0	37.8	42.9	35.7
Grant financed	2.2	14.0	17.1	35.0	15.2	35.2	38.1	31.8
Concessional loan financed	1.0	1.3	0.1	2.0	1.0	1.6	1.6	1.6
Domestically financed	0.0	0.0	0.0	0.1	1.8	1.1	3.2	2.3
Recurrent balance (above the line) 5/	-9.9	1.2	8.1	4.1	-0.2	6.8	4.0	4.4
Primary domestic balance (above the line) 6/	-7.1	0.2	4.6	3.6	-2.7	4.1	-0.1	1.2
Overall balance (above the line)	-10.9	-0.2	8.0	2.0	-2.9	4.1	-0.8	0.5
Discrepancy (neg. are net expenditures)	1.2	-0.6	1.8	0.4	0.0	3.2	0.0	0.0
Overall balance (below the line)	-9.7	-0.8	9.9	2.4	-2.9	0.9	-0.8	0.5
Financing	9.7	0.8	-9.9	-2.4	2.9	-0.9	0.8	-0.5
Foreign (net)	3.8	0.2	-0.9	2.6	...	0.9	…	0.2
Disbursements	5.4	1.3	0.1	2.0	...	1.6	…	1.6
Amortization (accrual)	1.6	1.6	1.6	2.5	...	1.6	…	1.5
Debt forgiveness	0.0	0.4	0.6	3.2	...	0.9	…	0.1
Domestic bank and nonbank (net)	-2.9	-9.2	-6.6	-2.1	...	-1.7	…	-0.8
Banking system (accrual)	-1.0	-9.0	-8.6	-1.8	...	-1.6	…	-0.6
Central bank	2.4	-3.8	-5.7	-2.8	...	0.0	…	-0.3
Commercial banks	-3.5	-5.2	-2.8	0.9	...	-1.6	…	-0.3
Nonbank (accrual)	-1.9	-0.2	1.9	-0.2	...	-0.1	…	-0.2
National Provident Fund	-1.2	0.0	1.6	-0.2	...	-0.1	…	-0.2
Other	-0.7	-0.2	0.3	0.0	...	0.0	…	0.0
Privatization receipts	0.0	0.0	0.0	0.0	...	0.3	…	0.0
Increase in expenditure arrears 7/	3.7	4.1	-5.1	-3.3	...	-0.4	…	0.1
Principal debt arrears	5.2	5.7	-9.9	0.3	...	-0.1	…	0.0
External	1.9	0.1	0.5	0.3	...	-0.1	…	0.0
Domestic	3.4	5.6	-10.4	0.0	...	0.0	…	0.0
Restructured Bonds	0.0	0.0	12.7	0.0	...	0.0	…	0.0

Sources: Data provided by the authorities; and Fund staff estimates.

1/ Development grants and grant-financed development spending are currently administered by donors, and hence are not under the direct control of the government. They exclude police and military spending, but include noncash grants. Data on aid flows are now being captured more accurately, and they indicate much higher levels than previously estimated.
2/ On an accrual basis.
3/ Recurrent costs of projects and from taking over recurrent costs currently funded by donor grants.
4/ Includes transfers for realized contingent liabilities in 2005, 2006, and 2007.
5/ Domestic revenue and recurrent grant budget support minus recurrent expenditure.
6/ Domestic revenue minus noninterest recurrent expenditure and domestically-financed development spending.
7/ Includes interest arrears.

Table 4. Solomon Islands: Summary Accounts of the Banking System, 2002-07

	2002	2003	2004	2005	2006 Est.	2007 Proj.
I. Central Bank	(In millions of S.I. dollars, end of period)					
Net foreign assets	117.5	250.4	578.2	699.7	773.1	890.4
Net domestic assets	49.8	-26.6	-194.6	-237.2	-284.2	-358.1
Credit to the government (net)	159.5	93.6	-20.5	-82.5	-81.9	-90.2
Claims	186.3	185.4	185.6	196.9	161.7	156.3
Deposits	-26.8	-91.9	-206.1	-279.4	-243.5	-246.5
Other items (net)	-109.8	-120.2	-174.0	-154.6	-202.3	-267.9
Reserve money	167.3	223.8	383.6	462.6	488.9	532.3
Currency outside DMBs	84.8	102.7	123.2	153.0	177.6	211.6
II. Monetary survey						
Net foreign assets	132.2	266.9	583.9	712.5	770.1	887.4
Net domestic assets	283.6	261.3	93.2	152.0	316.6	395.1
Domestic credit	471.4	457.8	299.1	411.5	566.7	715.7
Government (net)	298.3	253.8	81.8	40.6	-4.2	-20.2
Claims	336.9	355.7	335.6	342.9	295.0	282.5
Deposits	-38.6	-101.9	-253.8	-302.3	-299.2	-302.7
Credit to rest of NFPS	1.8	-12.0	-21.3	-18.3	-61.4	-43.3
Private sector	171.3	216.0	238.6	389.1	632.3	779.3
Other items (net)	-187.8	-196.5	-205.9	-259.4	-250.2	-321
Broad Money (M2)	415.8	528.2	677.0	864.6	1086.6	1282.4
Narrow money	247.1	335.9	427.2	538.7	704.5	831.5
Quasi money	168.7	192.3	249.8	325.8	382.1	451.0
	(Annual percentage change, end of period)					
Reserve money	12.0	30.4	75.9	20.6	5.7	8.9
Net foreign assets	30.2	101.8	118.8	22.0	8.1	15.2
Net domestic assets	-6.0	-7.9	-64.4	63.2	108.2	24.8
Net domestic credit	11.0	-2.9	-34.7	37.6	37.7	26.3
Of which: Private sector	-20.7	26.1	10.5	63.1	62.5	23.2
Broad money (M2)	3.1	27.0	28.2	27.7	25.7	18.0
Memorandum items:						
Velocity of broad money (marketed output)	2.5	2.2	2.0	1.8	1.6	1.5
Money multiplier	2.5	2.4	1.8	1.9	2.2	2.4
Excess liquidity to deposits ratio	17.9	19.6	39.5	36.0	26.8	22.5
Net international reserves (in millions of US$	15.8	33.4	77.0	92.4	101.5	110.8
Private sector credit growth in real terms	-2.7	21.5	2.6	50.5	51.2	15.2
Government credit (net) growth in real terms	-4.2	-18.0	-70.1	-54.2	-109.6	-350.8

Sources: Data provided by the Central Bank of Solomon Islands; and Fund staff estimates.

Table 5. Solomon Islands: Indicators of External Vulnerability, 2002–07

	2002	2003	2004	2005	2006 Est.	2007 Proj.
Financial indicators						
Government sector debt (in percent of GDP)	113.3	120.4	90.2	81.3	72.8	66.7
Broad money (percent change, 12-month basis)	4.0	26.0	28.2	27.7	25.7	18.0
Private sector credit (percent change, 12 month basis)	12.2	26.1	10.5	63.1	62.5	23.2
3 month T-bill yield (in percent, nominal) 3/	8.3	5.8	6.0	4.5	3.5	3.4
3 month T-bill yield (in percent, real) 3/	-0.9	-3.7	-0.9	-2.7	-4.3	…
External indicators						
Merch. Exports (percent change, 12-month basis in US$)	22.6	28.4	30.4	5.9	17.5	21.4
Of which : nonlogging exports	82.5	22.8	38.3	1.5	3.2	5.4
Merch. Imports (percent change, 12-month basis in US$)	-19.0	35.7	29.4	52.4	35.4	16.4
Terms of trade (percent change, 12 month basis)	-20.1	-16.6	-11.2	-12.6	8.3	0.5
Current account balance (in percent of GDP)	-10.2	-2.5	3.1	-24.2	-26.5	-40.0
Capital account balance (in percent of GDP)	2.8	9.1	10.6	27.7	28.2	42.3
Gross official reserves (in US$ millions)	17.5	36.3	80.0	94.6	103.8	113.0
Central Bank short-term foreign liabilities (in US$ millions)	1.7	2.9	3.0	2.3	2.3	2.3
Central Bank foreign currency exposure (in US$)	15.8	33.4	77.0	92.4	101.5	110.8
Short term foreign assets of the financial sector (in US$)	...	...	...	...	...	...
Short term foreign liabilities of the financial sector (in US$)	...	...	...	...	...	...
Foreign currency exposure of the financial sector (in US$ millions) 1/	2.0	2.2	0.8	1.7	-0.4	-0.4
Official reserves (in months of next year's imports of GNFS)	1.9	3.0	4.5	4.0	3.5	3.9
Gross international reserves to broad money	0.3	0.5	0.9	0.8	0.7	0.7
Total external public sector debt (in percent of GDP) 2/	66.6	69.5	60.4	56.9	53.9	50.4
Total external debt to exports of GNFS	203.5	168.5	126.1	122.2	104.1	90.6
External interest payments to exports of GNFS	4.1	2.8	2.0	4.1	0.8	1.1
External amortization payments to exports of GNFS	0.8	3.6	2.3	4.7	3.2	2.8
Exchange rate (SI$/US$, period average)	6.75	7.51	7.48	7.53	7.61	…
Exchange rate (SI$/US$, end of period) 3/	7.46	7.49	7.51	7.58	7.62	7.65
REER appreciation (+) (period average)	-17.1	-12.9	-1.8	3.1	5.1	…

Sources: Data provided by the authorities; and Fund staff estimates.

1/ Net foreign assets of commercial banks.
2/ Includes arrears.
3/ 2007 column reflects data as of end-May.

Table 6. Solomon Islands: Medium-Term Baseline Scenario, 2005-12

	2005	2006	2007	2008	2009	2010	2011	2012
		Est.			Projection			
Growth and prices (percentage change)								
Real GDP	5.0	6.1	5.4	4.2	2.8	1.6	1.5	1.6
Of which : Nonlogging	4.5	6.0	3.6	4.5	3.6	3.5	3.5	3.5
CPI (period average)	7.3	8.1	6.3	7.3	6.6	6.2	5.5	5.0
CPI (end of period)	8.4	7.5	7.0	6.7	6.5	6.0	5.0	5.0
Nominal GDP (millions of US$)	298	336	361	381	399	416	434	453
Per capita GDP (in US$)	619	678	709	728	742	752	763	776
Per capita GDP in 2007 prices (in US$)	697	711	729	739	739	730	721	713
Central government operations (percent of GDP)								
Total revenue	65.9	70.1	69.0	65.9	59.6	51.7	50.3	49.0
Recurrent revenue	29.1	32.2	35.0	34.8	34.4	33.6	32.9	32.3
Grants 1/	36.8	37.9	34.0	31.0	25.2	18.1	17.4	16.7
Total expenditure 2/	63.9	66.0	68.5	64.6	58.4	50.5	49.0	47.6
Recurrent expenditure	26.8	28.1	32.8	33.0	32.3	31.4	30.4	29.6
Development expenditure 1/	37.1	37.8	35.7	31.7	26.1	19.2	18.6	18.0
Recurrent balance 3/	4.1	6.8	4.4	3.8	3.9	4.0	4.2	4.3
Primary domestic balance 4/	3.6	4.1	1.2	0.5	0.4	0.4	0.5	0.5
Overall balance 5/	2.0	4.1	0.5	1.3	1.2	1.2	1.3	1.4
Foreign financing (net)	2.6	0.9	0.2	-1.5	-1.8	-1.6	-1.6	-1.5
Domestic financing (net)	-2.1	-1.7	-0.8	0.0	0.3	0.1	0.0	-0.2
Other	-2.3	-0.1	0.1	0.2	0.3	0.2	0.2	0.2
Central government debt (percent of GDP) 6/	81.3	72.8	66.7	60.5	55.1	50.5	46.1	41.9
Monetary and credit (percentage change, end-year data)								
Net foreign assets	22.0	8.1	15.2	-5.7	3.2	-1.6	-10.7	-6.1
Net domestic assets	63.2	108.2	24.8	46.1	17.3	20.2	26.1	16.7
Net domestic credit	37.6	37.7	26.3	18.8	13.8	12.1	11.6	10.4
Credit to private sector	63.1	62.5	23.2	16.2	11.1	9.6	9.4	8.3
Broad money	27.7	25.7	18.0	10.3	8.9	8.0	7.3	7.0
Interest rate (3-month t/bill rate, average) 7/	3.5	3.5	3.4	...	...	...	...	...
Balance of payments								
Exports (GNFS; percentage change)	9.1	25.1	15.7	17.4	5.5	0.5	0.1	0.7
Imports (GNFS; percentage change)	48.8	30.9	27.7	-2.7	-10.4	-5.3	2.2	-0.9
Current account	-72.3	-88.9	-144.4	-104.6	-55.5	-36.8	-42.1	-37.2
(percent of GDP)	-24.2	-26.5	-40.0	-27.5	-13.9	-8.8	-9.7	-8.2
Capital account	82.5	94.6	152.6	93.4	53.9	31.1	29.1	29.4
Overall balance (accrual)	10.3	5.7	8.2	-11.2	-1.6	-5.7	-13.0	-7.8
Gross official reserves (US$ millions, end of period)	94.6	103.8	113.0	102.7	101.9	97.2	85.1	78.2
(in months of next year's imports of GNFS)	4.0	3.5	3.9	3.9	4.1	3.9	3.4	3.1
Exchange rate (SI$/US$, end of period) 7/	7.58	7.62	7.65	...	...	...	...	...
Real effective exchange rate (period average, 2000=100)	79.5	83.5	83.5	83.5	83.5	83.5	83.5	83.5
Nominal effective exchange rate (period average, 2000=100)	59.1	58.5	...	...	...	...	...	...

Sources: Data provided by the authorities; and Fund staff estimates.

1/ Estimated by staff as currently only limited data exist. Development grants and grant-financed development spending are currently administered by donors, and hence are not under the direct control of the government. They exclude police and military spending, but include TA.
2/ Expenditures are presented on an accrual basis.
3/ Includes recurrent budget grant support.
4/ Domestic revenue minus noninterest recurrent expenditure and domestically-financed development spending.
5/ Calculated from above-the-line data.
6/ Includes interest arrears.
7/ 2007 column reflects data for end-May 2007.

Table 7. Solomon Islands: Medium-Term Baseline Scenario–Balance of Payments, 2005–12 1/

(In millions of U.S. dollars)

	2005	2006	2007	2008	2009	2010	2011	2012
		Est.			Proj.			
Current account balance	-72.3	-88.9	-144.4	-104.6	-55.5	-36.8	-42.1	-37.2
Current account balance (excl. net pub. sec. transfers)	-72.4	-89.9	-145.5	-105.7	-56.6	-37.8	-43.2	-38.3
Trade balance	-82.6	-130.2	-145.5	-118.3	-86.1	-69.2	-75.4	-71.3
Merchandise exports, f.o.b.	102.5	120.4	146.2	179.3	191.2	191.3	190.3	190.8
Of which: Logging	67.7	84.6	108.4	113.3	109.2	93.1	74.0	56.0
Fish	11.5	19.2	18.3	18.6	18.7	19.2	19.5	19.8
Minerals (mainly gold)	0.2	0.8	0.8	24.7	37.7	52.0	68.4	84.9
Palm Oil	0.0	4.0	8.0	11.4	14.0	15.1	16.2	17.4
Merchandise imports, c.i.f.	185.1	250.6	291.7	297.6	277.3	260.5	265.7	262.1
Of which: Petroleum	43.1	54.4	55.2	68.2	70.8	68.8	69.2	71.2
Services and income (net)	7.0	25.4	-13.1	-1.2	15.1	16.4	16.6	16.7
Nonfactor services (net)	6.8	23.0	-12.3	5.1	22.3	23.2	23.2	23.5
Net factor income from abroad	0.1	2.5	-0.8	-6.3	-7.2	-6.8	-6.7	-6.8
Net current transfers	3.4	15.9	14.1	14.8	15.5	16.1	16.7	17.4
Private sector	3.2	14.9	13.0	13.8	14.4	15.0	15.7	16.4
Public sector	0.2	1.0	1.1	1.1	1.1	1.1	1.1	1.1
Capital account balance	82.5	94.6	152.6	93.4	53.9	31.1	29.1	29.4
Government sector	77.2	86.5	90.3	76.0	64.0	45.4	45.1	45.4
Medium- and long-term lending	-1.5	-0.1	0.3	-5.7	-7.3	-6.6	-6.9	-6.6
Inflows	6.0	5.3	5.9	0.0	0.0	0.0	0.0	0.0
Amortization	7.5	5.4	5.6	5.7	7.3	6.6	6.9	6.6
Investment flow (projects)	78.7	86.6	90.0	81.7	71.3	52.0	52.0	52.0
Inflows	104.4	118.1	114.7	110.9	93.4	68.1	68.1	68.1
Outflows	25.7	31.5	24.7	29.3	22.1	16.1	16.1	16.1
Private sector	5.3	8.1	62.3	17.4	-10.1	-14.3	-16.1	-16.1
Investment activities (incl. FDI)	7.4	5.9	33.8	18.8	6.1	3.8	3.9	3.9
Medium- and long-term lending	-1.7	7.0	41.7	9.0	-10.9	-12.8	-14.6	-14.6
Inflows	0.4	7.3	43.7	19.1	0.0	0.0	0.0	0.0
Amortization	2.1	0.3	2.0	10.1	10.9	12.8	14.6	14.6
Other flows	-0.4	-4.8	-13.2	-10.3	-5.3	-5.3	-5.3	-5.3
Overall balance (accrual)	10.3	5.7	8.2	-11.2	-1.6	-5.7	-13.0	-7.8
Commercial bank holdings (increase)	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5
Errors, omissions, and valuation	-2.3	2.1	0.0	0.0	0.0	0.0	0.0	0.0
Exceptional financing	7.1	1.9	1.0	0.8	0.9	0.9	0.9	1.0
Interest arrears	-3.2	0.8	0.8	0.8	0.9	0.9	0.9	1.0
Amortization arrears	1.0	-0.2	0.0	0.0	0.0	0.0	0.0	0.0
Pending import requests	-0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Debt forgiveness	9.4	1.3	0.2	0	0	0	0	0
Overall balance (cash)	14.6	9.2	9.3	-10.3	-0.8	-4.8	-12.1	-6.9
Memorandum items:								
Gross official reserves	94.6	103.8	113.0	102.7	101.9	97.2	85.1	78.2
(In months of next year's imports of GNFS)	4.0	3.5	3.9	3.9	4.1	3.9	3.4	3.1
(In months of next year's nonproject imports)	4.7	3.9	4.3	4.4	4.5	4.2	3.7	3.3
NIR (excl. pending import requests and external arrears)	64.6	73.1	81.6	70.4	68.8	63.1	50.1	42.2
(In months of next year's imports of GNFS)	2.8	2.4	2.8	2.7	2.8	2.5	2.0	1.7
External arrears (interest plus principal)	27.8	28.4	29.2	30.0	30.9	31.8	32.7	33.7
Exports GNFS–Value Growth	9.1	25.1	15.7	17.4	5.5	0.5	0.1	0.7
Exports GNFS–Volume Growth	10.4	4.5	13.6	17.2	5.9	0.4	0.0	0.7
Logging Exports–Value Growth	8.3	24.8	28.2	4.5	-3.6	-14.8	-20.5	-24.3
Nonlogging Exports–Value Growth	1.5	3.2	5.4	74.8	24.3	19.7	18.5	15.8
Imports GNFS–Value Growth	48.8	30.9	27.7	-2.7	-10.4	-5.3	2.2	-0.9
Imports GNFS–Volume Growth	36.3	21.7	23.4	-0.5	-8.6	-4.7	2.8	-0.3
Current account (including transfers)/GDP	-24.2	-26.5	-40.0	-27.5	-13.9	-8.8	-9.7	-8.2
Current account (excluding transfers(/GDP	-24.3	-26.8	-40.3	-27.8	-14.2	-9.1	-10.0	-8.4

Sources: Data provided by the authorities; and Fund staff estimates.

1/ Import figures from 2002 onwards are now based on customs data and net investment flow projects of the government from 2005 are based on more accurate estimates of aid flows from the authorities.

Table 8. Solomon Islands: Medium-Term Alternative Scenario, 2005–12

	2005	2006	2007	2008	2009	2010	2011	2012
		Est.			Projection			
Growth and prices (percentage change)								
Real GDP	5.0	6.1	5.4	4.7	4.5	3.7	3.6	3.8
Of which : Nonlogging	4.5	6.0	3.6	5.1	5.5	5.7	5.8	5.7
CPI (period average)	7.3	8.1	6.3	7.3	6.6	6.2	5.5	5.0
CPI (end of period)	8.4	7.5	7.0	6.7	6.5	6.0	5.0	5.0
Nominal GDP (millions of US$)	298	336	361	382	406	430	455	483
Per capita GDP (in US$)	619	678	709	731	755	777	801	826
Per capita GDP in 2007 prices (in US$)	697	711	729	743	755	761	767	774
Central government operations (percent of GDP)								
Total revenue	65.9	70.1	69.0	66.3	60.0	55.5	54.3	53.3
Recurrent revenue	29.1	32.2	35.0	35.4	35.2	35.2	35.1	35.1
Grants 1/	36.8	37.9	34.0	30.9	24.8	20.4	19.2	18.1
Total expenditure 2/	63.9	66.0	68.5	65.0	58.8	54.3	53.0	51.9
Recurrent expenditure	26.8	28.1	32.8	33.4	33.0	32.7	32.3	32.1
Development expenditure 1/	37.1	37.8	35.7	31.5	25.8	21.6	20.7	19.8
Recurrent balance 3/	4.1	6.8	4.4	3.8	4.0	4.1	4.4	4.5
Primary domestic balance 4/	3.6	4.1	1.2	0.5	0.4	0.4	0.5	0.5
Overall balance 5/	2.0	4.1	0.5	1.3	1.2	1.2	1.3	1.3
Foreign financing (net)	2.6	0.9	0.2	-1.5	-1.8	-1.5	-1.5	-1.4
Domestic financing (net)	-2.1	-1.7	-0.8	-0.1	0.3	0.1	0.0	-0.2
Other	-2.3	-0.1	0.1	0.2	0.2	0.2	0.2	0.2
Central government debt (percent of GDP) 6/	81.3	72.8	66.7	60.3	54.1	48.8	43.9	39.3
Monetary and credit (percentage change, end-year data)								
Net foreign assets	22.0	8.1	15.2	6.1	13.3	16.6	9.8	14.4
Net domestic assets	63.2	108.2	24.8	24.5	5.1	-4.5	6.6	-6.2
Net domestic credit	37.6	37.7	26.3	20.0	15.6	13.1	12.0	11.0
Credit to private sector	63.1	62.5	23.2	17.4	12.7	10.7	10.0	9.1
Broad money	27.7	25.7	18.0	11.7	10.5	9.7	8.9	8.7
Interest rate (3-month t/bill rate, average) 7/	3.5	3.5	3.4	...	...	...	...	...
Balance of payments								
Exports (GNFS; percentage change)	9.1	25.1	15.7	18.1	7.6	4.7	6.4	6.5
Imports (GNFS; percentage change)	48.8	30.9	27.7	-3.0	-8.4	-1.6	7.4	4.0
Current account	-72.3	-88.9	-144.4	-102.2	-54.7	-36.2	-40.5	-34.2
(percent of GDP)	-24.2	-26.5	-40.0	-26.7	-13.5	-8.4	-8.9	-7.1
Capital account	82.5	94.6	152.6	103.4	63.9	51.0	49.6	50.6
Overall balance (accrual)	10.3	5.7	8.2	1.3	9.2	14.7	9.0	16.4
Gross official reserves (US$ millions, end of period)	94.6	103.8	113.0	115.2	125.2	140.8	150.8	168.2
(in months of next year's imports of GNFS)	4.0	3.5	3.9	4.3	4.8	5.0	5.2	5.5
Exchange rate (SI$/US$, end of period) 7/	7.58	7.62	7.65	...	...	...	...	...
Real effective exchange rate (period average, 2000=100)	79.5	83.5	83.5	83.5	83.5	83.5	83.5	83.5
Nominal effective exchange rate (period average, 2000=100)	59.1	58.5	...	...	...	...	...	...

Sources: Data provided by the authorities; and Fund staff estimates.

1/ Estimated by staff as currently only limited data exist. Development grants and grant-financed development spending are currently administered by donors, and hence are not under the direct control of the government. They exclude police and military spending, but include TA.
2/ Expenditures are presented on an accrual basis.
3/ Includes recurrent budget grant support.
4/ Domestic revenue minus noninterest recurrent expenditure and domestically-financed development spending.
5/ Calculated from above-the-line data.
6/ Includes interest arrears.
7/ 2007 column reflects data for end-May 2007.

Table 9. Solomon Islands: Structural Reforms Status as of end-May 2007

Area	Specific Reform	Assisting Institution/Donor	Status
National Development Plan	Policy Framework Document		Issued in May 2006.
	Policy Translation and Implementation Document		Issued in August 2006.
	Successor Plan		Stalled, but recent efforts to revive preparations are starting.
Tax reform	Income Tax Amendments (PAYE)	LEG	Passed by Parliament December 2005.
	Income tax, goods tax, and import duty exemption guidelines		Issued June 2006.
	Value Added Tax Act, Revenue Administration Act, and Customs Act Redrafting	PFTAC/LEG	Business Revenue Reform Steering Committee set up and draft plan prepared.
	Tax Incentives Review	FIAS	Discussion paper submitted to authorities.
	Increase in reference price of logs (to assess export duty)		11 percent increase effective January 2007; additional 21 percent increase scheduled on July 1, 2007.
Public Sector Financial Management	Review of Public Finance and Audit Act	PFTAC	Revised Finance Instructions submitted to authorities.
	Solomon Islands Government Accounting Service (SIGAS)		Being revamped, but progress slow.
	Local Purchase Orders		Introduced 2006.
State Enterprise Reform	SOE Reform and Private Sector Participation	ADB	Ongoing TA to improve SOE ownership, accountability, and performance. Cabinet papers on recommended reforms and SOE Bill drafted and submitted to the authorities. Plans for privatization of the Sasape Marina and Soltai Fishing and Processing companies under consideration.
	Electricity Authority (SIEA)	World Bank (WB)	Financial restructuring plan

Area	Specific Reform	Assisting Institution/Donor	Status
	Restructuring	AusAid	(FRP) report finalized and government has agreed to a performance-based management contract, but it is yet to be implemented. Implementation requires SIWA's FRP.
	SIWA Restructuring	WB	FRP prepared but recommendations yet to be adopted. Government has agreed to performance-based management contract, but it is not yet implemented (see SIEA).
	Solomon Airlines & civil aviation regulation	ADB/WB/AusAid/ RAMSI	Privatization strategy document submitted to authorities in December 2005, but shelved. Civilian Aviation bill drafted in H2 2006, and Civilian Aviation Plan being prepared. Introduction of some competition in 2006 has reduced air fares.
Business Environment	Foreign Investment Act	FIAS	Approved by Parliament December 16, 2005, effective June 26, 2006.
	Administrative Barriers (licensing; immigration and labor permits)	FIAS	Improvements to processing of labor and immigration permits introduced in August 2006. Provincial business licenses under review.
	Investment Promotion Strategy	FIAS	Planning stage.
	Business Law Reform	ADB	Companies Act review completed in December 2006 and new Act being prepared. Cabinet paper drafted as of February 2007, but not approved.
Infrastructure	National Transport Plan (NTP) and National Transport Fund (NTF)	ADB/AusAid/NZAid	Cabinet approved NTP and NTF in September 2006, but NTF yet to be established.
	Barriers to efficient shipping	ADB	TA completed in December 2006. Shipping strategy expected to be finalized in 2007, including review of nonviable shipping routes.

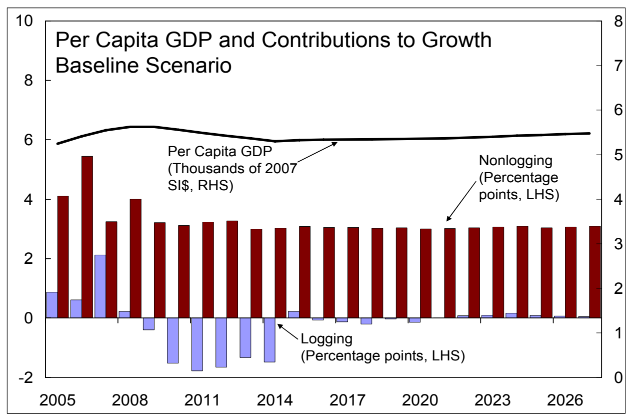
Area	Specific Reform	Assisting Institution/Donor	Status
			Import duties on shipping reduced in June 2005.
	Rehabilitation of Roads and Bridges	ADB/AusAid/NZAid	Repair work to be completed by September 2007. Construction for new road improvement project and infrastructure damaged by the tsunami to start in 2008.
	Strengthening of Ministry of Infrastructure	ADB	TA completed in December 2006. Final report expected in 2007.
	Review of the telecommunication monopoly	WB	Cabinet approved competition in the telecommunication sector in September 2006. Negotiations on Telekom's contract started in Q4 2006 but have been interrupted by court challenges.
Health and Education	Health Sector-Wide Approach (SWAp)	AusAid/WB	Diagnosis and public expenditure review completed. WB Health Swap project approval expected in Q4 2007.
	Education SWAp	EU/NZAID/WB	Ongoing. Bank co-financed a study to support a National Skills Training Plan presented to Government in December 2006. National Education Action Plan (2007-2009) drafted and expected to be adopted soon.
Financial Sector	DBSI		CBSI court-appointed management mandate extended to end-June 2007; almost all depositors were repaid. Government decision on next steps pending.
	NPF	WB	New NPF Bill submitted to government, but issue dormant.
	Financial Intelligence Unit	LEG/AusAid	MOU signed to provide funding for three years. FIU officer started work. LEG to provide follow-up TA on AML/CFT surveillance

Area	Specific Reform	Assisting Institution/Donor	Status
	Secured Transactions Reform Credit guarantee scheme and extension of commercial financial services to rural areas	ADB	Initial report submitted to authorities. TA planned for second half of 2007. Credit guarantee scheme for rural and small businesses has been designed by CBSI with seed funding included in the 2007 Budget (scheme should not result in any new Government liabilities or guarantees). Also, more mobile banks and ATMs to be deployed in rural areas in late 2007.
Rural Development	Agriculture and Rural Development Strategy (ARDS)	AusAid/EU/WB/Japan	Strategy paper launched in April 2007. New Rural Development Project to implement the ARDS to be presented to the WB Board in August 2007.
Governance	Institutions Strengthening Program Machinery of government Introduction of a single ballot box	RAMSI RAMSI	Ongoing. Ongoing. Legislation approved in July 2005.
Insurance	Revision of the Insurance Act Resolution of troubled insurance company (SMI)	MCM MCM	Initial review of the Act to check compliance with international standards completed. SMI under the jurisdiction of the court for liquidation, and SMI's license revoked.
Statistics	See Annex VI	See Annex VI	See Annex VI
Trade	Integrated Framework	WTO/UNDP	Application submitted February 2006. Technical review completed.
Land Reform	Tribes and Customary Land Titles Act		Consultations on draft legislation started.

APPENDIX I. SOLOMON ISLANDS: JOINT FUND-BANK DEBT SUSTAINABILITY ANALYSIS (DSA)

Under the medium-term baseline scenario, living standards would fail to rise, and the debt remains at high risk of distress.[1] *Assuming macroeconomic stability, but an unchanged reform pace, growth would average 3 percent. Logging would start detracting significantly from growth from 2010 after its recent acceleration brought forward the exhaustion of the natural forest. Although the debt situation has continued to improve, historical scenarios and several stress tests—even some temporary ones—still lead to a significant rise in the debt burden and cause several indicators to rise above thresholds.*

Appendix Box 2. Medium-Term Baseline Scenario



Under the medium-term baseline scenario, real GDP growth is projected at an average of 2.8 percent, barely matching the population growth. This scenario assumes RAMSI and donor support, an unchanged pace of reforms, and that the two large projects that have recently started (the palm oil plantation and the gold mine) will continue, but no major new nonlogging activities would commence. Based on a new government report, logging is projected to continue at over 5 times the sustainable rate in 2007-2009, given continued strong expected demand from China and favorable international prices, after which it drops dramatically and detracts significantly from growth until the natural forests are exhausted in 2014. After 2014, logging is expected to contribute only marginally to growth, mainly from plantations. Nonlogging growth is projected at an average of 3¾ percent in the medium term, and is expected to stabilize at about 3 percent in the long run. Inflation is projected to ease but would remain at around 5 percent. The real effective exchange rate is assumed to be constant. Despite the decline in logging exports, the current account deficit is expected to narrow rapidly as import growth declines given lower official development assistance (ODA) and investment inflows, and as the gold mine starts production in 2008, but would remain at about 8 percent of GDP. The reserve cover is projected to fall, but would remain adequate at above 3 months of imports. The budget position would need to maintain a small surplus due to financing constraints and the desire to avoid abrupt fiscal retrenchment, and to reduce the high public debt.

Risks to the baseline are tilted to the downside. Potential risks stem mainly from: the country's history of political instability, disruption to law and order, slippages in fiscal discipline, donors leaving and interruptions in aid flows, and adverse exogenous shocks, such as to the terms of trade, given the highly-concentrated export base. Also, growth and exports have been highly volatile.

[1] Data on private external, state enterprise, and provincial government debt are not available. Therefore, the analysis is limited to central government debt data.

Progress has been achieved in regularizing the debt situation. The Honiara Club initiative led to a short-term moratorium on principal payments and the forgiveness of interest payments during the moratorium (0.2 percent of GDP) from one creditor, which expires in 2007, as well as the possibility of debt forgiveness and arrears settlement after an ongoing review.[2] This analysis, however, does not assume debt forgiveness, but incorporates the impact of the short-term moratorium and related interest forgiveness. Successful negotiations with an external commercial creditor achieved debt relief amounting to ½ percent of GDP in July 2006. In February 2006, agreement was also reached on debt owed to the Central Bank of the Solomon Islands (CBSI): 25 percent of interest arrears amounting to 0.4 percent of GDP was settled, the rest was forgiven (1.3 percent of GDP), and outstanding advances were converted into long-term bonds carrying a 2¼ percent interest rate. The stock of arrears to suppliers also fell by about 1 percentage point of GDP to 1.2 percent of GDP in 2006. These developments helped bring down total public debt to 73 percent of GDP at end-2006, from 81 percent of GDP in 2005.

Debt Sustainability in the Baseline Scenario

Results of the baseline external debt sustainability analysis are mixed (Appendix Table 10).[3] At end-2006, the NPV of external debt to GDP at 37 percent was higher than its Board-endorsed threshold, but is expected to fall below it by 2009. This relies critically on the assumption that the government's current policy of incurring no new debt will continue.[4] All other indicators, including the ratios of the NPV of debt to exports and revenue, and debt service ratios were below their thresholds, and are expected to decline over time. Although the starting point of the NPV of external debt to GDP is about the same as earlier projected for 2006, indicators decline at a slower pace over the medium term due mainly to the lower projected GDP and the faster decline in logging revenue.

Albeit declining, the overall central government debt remains high (Appendix Table 12). At end-2006, central government domestic debt including arrears stood at 19 percent of

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[2] The Honiara Club is a multilateral forum convened by the government in October 2005 to seek debt relief from its official creditors. Four creditors participated in the Honiara Club, namely, the Export Finance and Insurance Corporation (EFIC), the European Commission, the European Investment Bank, and the International Fund for Agricultural Development.

[3] This analysis assumes that the government remains current on all obligations from June 2007, and that all debts in arrears are treated as a current short-term obligation with NPV equal to its face value. Existing external arrears are assumed to continue growing with accrued interest.

[4] The thresholds (see Appendix Table 10) apply to countries with weak policies and institutions, and are discussed in *Operational Framework for Debt Sustainability Analysis in Low Income Countries—Further Considerations*. Albeit improving, the Solomon Islands' 3-year average CPIA at 2.5 remains the lowest among the Pacific Island Countries.

GDP, from its 2003 peak of 51 percent. In 2007, this is expected to decline further to 16.3 percent of GDP, partly reflecting the settlement of most remaining informal arrears and the continuing repayment of existing debt as scheduled. Nevertheless, total central government debt would still be 42 percent of GDP in 2012, and the NPV of public sector debt to revenue ratio stays above 100 percent until 2011.

Risks to the debt dynamics

Historical scenarios and even some *temporary* stress tests demonstrate the country's vulnerable debt position (Appendix Tables 11 and 13).

- *External Debt:* Key variables at their historical averages set the NPV of external debt to exports on a rising path as historical averages for real GDP and export growth are close to zero, and the 10-year average of non-debt creating flows is significantly below recent levels. The export shock (bound test B2) is the most extreme stress test for the NPV of debt to export and NPV of debt service to export ratios due to the high volatility of exports. Even a temporary decline in export growth to its historical average increases the NPV of debt to exports to twice its threshold. The most extreme stress test for the NPV of debt to GDP ratio is the temporary reversion to historical averages, minus one half a standard deviation, of real GDP growth, export growth, the U.S. dollar GDP deflator, and net non-debt creating flows (bound test B4). If all recognized contingent liabilities are realized (14 percent of GDP), the NPV of external debt to GDP would exceed 30 percent of GDP until 2015.

- *Public Debt:* Lower GDP growth, even temporarily, and a return of growth and the primary balance to their historical averages causes the NPV of public debt to GDP and revenue ratios to rise dramatically. The most extreme stress test, which assumes a temporary decline in GDP growth to its historical average less one standard deviation, almost triples the current level of the NPV of public debt to revenue ratio.

These tests seem especially relevant given the country's volatile economic and political history, poor credit history, and mixed progress in key areas of the reform agenda.

These results are indicative given major uncertainties surrounding important variables. Macroeconomic variables (especially GDP) are subject to large measurement errors. ODA plans are uncertain and contingent liabilities are likely to increase as the SOEs' financial situation remains poor.

The authorities should sustain their efforts to regularize debt and uphold the policy of no new borrowing at least until all indicators fall below the thresholds. In view of impending fiscal pressures from declining logging revenues and aid, and the need to sustain progress towards debt sustainability, the authorities should maintain fiscal prudence, continue to work towards clearing all arrears, retain the policy of no new borrowing, and anchor fiscal policy to a medium-term framework. Vigorously pursuing SOE reform and strengthening the National Provident Fund will also be necessary to minimize future contingent liabilities to the budget.

Appendix Table 10. Solomon Islands: External Debt Sustainability Framework, Baseline Scenario, 2006–27 1/
(In percent of GDP, unless otherwise indicated)

	Actual			Estimate	Projections												
	2006	Historical Average 5/	Standard Deviation 5/	2007	2008	2009	2010	2011	2012	2007-12 Average	2013	2014	2015	2016	2017	2027	20013-27 Average	Board Endorsed Threshold 6/
External debt (nominal) 1/	53.9			50.4	46.5	42.8	39.6	36.6	33.8		31.1	28.6	26.2	24.0	21.9	9.2		
Of which : public and publicly guaranteed (PPG)	53.9			50.4	46.5	42.8	39.6	36.6	33.8		31.1	28.6	26.2	24.0	21.9	9.2		
Change in external debt	-3.0			-3.5	-3.9	-3.7	-3.1	-3.0	-2.8		-2.7	-2.5	-2.4	-2.2	-2.1	-0.4		
Identified net debt-creating flows	-5.8			6.9	1.5	-5.2	-3.8	-2.3	-3.3		-3.2	-5.2	-4.3	-4.9	-3.0	-1.9		
Noninterest current account deficit	26.1	7.1	10.9	39.4	26.9	13.4	8.4	9.3	7.9		9.7	6.8	7.4	5.8	6.2	2.5		
Deficit in balance of goods and services	32.0			43.7	29.7	16.0	11.1	12.1	10.6		12.4	9.6	10.3	8.8	9.4	5.8		
Exports	51.7			55.6	61.9	62.3	60.1	57.7	55.7		52.4	48.4	47.8	46.7	45.5	30.6		
Imports	83.7			99.4	91.6	78.3	71.2	69.8	66.2		64.8	58.0	58.1	55.5	54.9	36.4		
Net current transfers (negative = inflow)	-4.7	-2.0	4.1	-3.9	-3.9	-3.9	-3.9	-3.9	-3.9		-3.8	-3.8	-3.8	-3.8	-3.8	-3.8		
Other current account flows (negative = net inflow)	-1.1			-0.4	1.1	1.3	1.2	1.1	1.2		1.1	1.1	0.9	0.8	0.7	0.5		
Net FDI and other nondebt-creating flows (negative = inflow)	-26.1	-8.3	10.9	-30.7	-24.2	-18.1	-12.2	-11.7	-11.2		-12.8	-12.0	-11.2	-10.4	-9.0	-4.3		
Endogenous debt dynamics 2/	-5.7			-1.9	-1.3	-0.5	0.0	0.1	0.0		0.0	0.0	-0.5	-0.3	-0.3	-0.1		
Contribution from nominal interest rate	0.6			0.8	0.8	0.7	0.7	0.6	0.6		0.5	0.5	0.4	0.4	0.4	0.2		
Contribution from real GDP growth	-3.1			-2.7	-2.0	-1.3	-0.7	-0.6	-0.6		-0.5	-0.4	-0.9	-0.7	-0.7	-0.3		
Contribution from price and exchange rate changes	-3.3			…	…	…	…	…	…		…	…	…	…	…	…		
Residual (3-4) 3/	2.8			-10.4	-5.4	1.5	0.6	-0.7	0.5		0.5	2.7	1.9	2.6	1.0	1.5		
Of which : exceptional financing	-0.6			-0.3	-0.2	-0.2	-0.2	-0.2	-0.2		-0.2	-0.2	-0.2	-0.2	-0.2	-0.1		
NPV of external debt	36.7			34.3	32.0	29.6	27.7	25.7	23.9		22.1	20.4	18.8	17.2	15.8	6.4		
In percent of exports	71.0			61.7	51.7	47.5	46.0	44.5	42.9		42.2	42.1	39.2	36.9	34.7	20.8		
NPV of PPG external debt	36.7			34.3	32.0	29.6	27.7	25.7	23.9		22.1	20.4	18.8	17.2	15.8	6.4		30
In percent of exports	71.0			61.7	51.7	47.5	46.0	44.5	42.9		42.2	42.1	39.2	36.9	34.7	20.8		100
In percent of revenue (excluding grants)	126.3			106.6	101.9	85.0	80.5	76.5	72.7		68.4	65.4	62.4	57.4	53.0	23.1		200
Debt service-to-exports ratio (in percent)	4.0			3.9	3.3	3.8	3.4	3.5	3.3		3.3	3.3	3.0	2.9	2.7	0.8		
PPG debt service-to-exports ratio (in percent)	4.0			**3.9**	**3.3**	**3.8**	3.4	3.5	3.3		3.3	3.3	3.0	2.9	2.7	0.8		15
PPG debt service-to-revenue ratio (in percent)	8.0			**7.2**	**6.8**	**7.0**	6.2	6.2	5.8		5.6	5.3	5.0	4.7	4.4	0.9		25
Noninterest current account deficit that stabilizes debt ratio	29.1			42.9	30.8	17.2	11.5	12.3	10.7		12.4	9.3	9.8	8.1	8.3	2.9		
Key macroeconomic assumptions																		
Real GDP growth (in percent)	6.1	0.2	7.1	5.4	4.2	2.8	1.6	1.5	1.6	2.8	1.6	1.5	3.3	2.9	2.9	3.1	2.8	
GDP deflator in US dollar terms (change in percent)	6.1	-0.2	9.0	2.0	1.3	1.9	2.6	2.8	2.8	2.2	2.9	3.0	2.0	2.2	2.3	2.0	2.6	
Effective interest rate (percent) 4/	1.3	2.1	0.9	1.7	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.8	1.7	
Growth of exports of G&NFS (US dollar terms, in percent)	25.1	0.5	28.7	15.7	17.4	5.5	0.5	0.1	0.7	6.7	-1.6	-3.2	4.1	2.8	2.6	2.8	1.4	
Growth of imports of G&NFS (US dollar terms, in percent)	30.9	6.2	31.6	27.7	-2.7	-10.4	-5.2	2.2	-0.8	1.8	2.2	-6.3	5.5	0.5	4.0	3.2	1.4	
Grant element of new public sector borrowing (in percent)	...	...	...	54.8	...	...	...	...	...	54.8	...	...	...	...	...	...	...	
Memorandum item:																		
Nominal GDP (billions of US dollars)	0.336			0.361	0.381	0.399	0.416	0.434	0.453		0.474	0.495	0.522	0.549	0.578	1.007		

Sources: Data provided by the authorities; and Fund staff estimates.

1/ Refers to central government debt only due to data availability. This table assumes the government's current policy of not incurring new debt. The DSA exercise was conducted jointly with the World Bank.
2/ Derived as [r - g - r(1+g)]/(1+g+r+gr) times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, and r = growth rate of GDP deflator in U.S. dollar terms.
3/ Includes exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets; identified net debt-creating flows and valuation adjustments. For projections also includes contribution from price and exchange rate changes. For 2007, about half was contributed by the difference between the current account deficit and net FDI inflows due mainly to the large imports and foreign borrowing related to the gold mine rehabilitation.
4/ Current-year interest payments divided by previous period debt stock.
5/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.
6/ These thresholds apply to countries with weak policies and institutions and are discussed in *Operational Framework for Debt Sustainability Analysis in Low-Income Countries--Further Considerations* .

Appendix Table 11. Solomon Islands: Sensitivity Analyses for Key Indicators of Public and Publicly Guaranteed External Debt, 2007–27 1/
(In percent)

	Estimate	Projections						
	2007	2008	2009	2010	2011	2012	2017	2027
NPV of debt-to-GDP ratio								
Baseline	34	32	30	28	26	24	16	6
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2008–27 2/	34	32	32	33	32	33	36	41
A2. Realization of all recognized contingent liabilities as external debt in 2008 3/	34	44	42	40	38	36	28	18
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2008–09 4/	34	36	36	34	31	29	18	9
B2. Export value growth at historical average minus one standard deviation in 2008–09 5/	34	42	55	53	51	49	40	17
B3. US dollar GDP deflator at historical average minus one standard deviation in 2008–09	34	36	37	34	32	29	19	14
B4. Net non-debt creating flows at historical average minus one standard deviation in 2008-09 6/	34	47	56	54	52	50	41	18
B5. Combination of B1-B4 using one-half standard deviation shocks	34	46	65	62	60	57	45	19
B6. One-time 30 percent nominal depreciation relative to the baseline in 2008 7/	34	45	42	39	36	33	21	13
NPV of debt-to-exports ratio								
Baseline	62	52	48	46	45	43	35	21
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2008–27 2/	62	52	52	54	56	58	79	133
A2. Realization of all recognized contingent liabilities as external debt in 2008 3/	62	71	67	66	66	65	62	59
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2008–09 4/	62	58	58	56	54	52	40	30
B2. Export value growth at historical average minus one standard deviation in 2008–09 5/	62	108	199	198	198	198	195	126
B3. US dollar GDP deflator at historical average minus one standard deviation in 2008–09	62	57	59	57	55	53	41	46
B4. Net non-debt creating flows at historical average minus one standard deviation in 2008–09 6/	62	76	90	90	90	90	89	57
B5. Combination of B1-B4 using one-half standard deviation shocks	62	86	125	124	124	123	118	75
B6. One-time 30 percent nominal depreciation relative to the baseline in 2008 7/	62	73	67	65	62	60	46	42
Debt service ratio								
Baseline	3.9	3.3	3.8	3.4	3.5	3.3	2.7	0.8
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2008–27 2/	3.8	3.4	4.0	3.9	4.2	4.2	4.8	5.9
A2. Realization of all recognized contingent liabilities as external debt in 2008 3/	3.8	3.2	4.6	4.2	4.3	4.1	3.7	1.6
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2008–09 4/	3.8	3.6	4.5	4.2	4.3	4.0	3.4	0.8
B2. Export value growth at historical average minus one standard deviation in 2008–09 5/	3.8	5.1	8.9	9.2	9.4	8.9	7.9	9.0
B3. US dollar GDP deflator at historical average minus one standard deviation in 2008–09	3.8	3.2	3.7	3.4	3.4	3.3	2.8	1.4
B4. Net non-debt creating flows at historical average minus one standard deviation in 2008–09 6/	3.8	3.2	4.1	4.1	4.2	4.0	3.5	4.1
B5. Combination of B1–B4 using one-half standard deviation shocks	3.8	4.2	6.1	6.2	6.3	6.0	5.3	5.2
B6. One-time 30 percent nominal depreciation relative to the baseline in 2008 7/	3.8	3.2	3.7	3.4	3.4	3.3	2.8	1.4
Memorandum item:								
Grant element assumed on residual financing (i.e., financing required above baseline)	55	55	55	55	55	55	55	55

Sources: Data provided by the authorities; and Fund staff estimates.

1/ The DSA exercise was conducted jointly with the World Bank.
2/ Variables include real GDP growth, growth of GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.
3/ Liabilities realized and add to arrears from the beginning of 2008, attracting an interest rate equal to 2008 six month libor.
4/ Ratios calculated using baseline export-to-GDP, since GDP and exports are driven by the same primary commodities.
5/ Exports values are assumed to remain permanently at the lower level, but the current account as a share of GDP is assumed to return to its baseline level after the shock (implicitly assuming an offsetting adjustment in import levels).
6/ Includes official and private transfers and FDI.
7/ Depreciation is defined as percentage decline in dollar/local currency rate, such that it never exceeds 100 percent.

Appendix Table 12. Solomon Islands: Public Sector Debt Sustainability Framework, Baseline Scenario, 2004-27 1/ 2/

(In percent of GDP, unless otherwise indicated)

	Actual					Estimate	Projections								
	2004	2005	2006	Historical Average 7/	Standard Deviation 7/	2007	2008	2009	2010	2011	2012	2007-12 Average	2017	2027	2013-27 Average
Public sector debt 2/	90.2	81.3	72.8			66.7	60.5	55.1	50.5	46.1	41.9		25.8	10.0	
Of which: foreign-currency denominated	60.4	56.9	53.9			50.4	46.5	42.8	39.6	36.6	33.8		21.9	9.2	
Change in public sector debt	-30.5	-9.2	-7.5			-6.3	-6.3	-5.6	-4.8	-4.4	-4.2		-2.6	-0.5	
Identified debt-creating flows	-22.9	-15.0	-14.8			-3.5	-5.9	-4.5	-3.9	-3.8	-3.5		-2.2	-0.4	
Primary deficit	-9.8	-3.4	-5.2	0.0	6.3	-0.5	-2.4	-2.2	-2.1	-2.2	-2.1	-1.9	-1.4	-0.2	
Revenue and grants	47.5	65.9	70.1			71.7	65.9	59.6	51.7	50.2	48.9		39.6	32.3	
Of which: grants	21.5	36.8	37.9			40.3	31.0	25.2	18.1	17.4	16.6		10.1	4.8	
Primary (noninterest) expenditure	37.7	62.5	64.9			71.2	63.5	57.4	49.6	48.1	46.8		38.2	32.1	
Automatic debt dynamics	-13.1	-8.5	-8.4			-3.0	-3.5	-2.3	-1.8	-1.7	-1.4		-0.7	-0.2	
Contribution from interest rate/growth differential	-11.5	-6.5	-6.5			-4.2	-3.4	-2.3	-1.5	-1.2	-1.1		-0.6	-0.2	
Of which: contribution from average real interest rate	-2.6	-2.2	-1.9			-0.5	-0.7	-0.6	-0.6	-0.5	-0.4		0.2	0.1	
Of which: contribution from real GDP growth	-8.9	-4.3	-4.6			-3.7	-2.7	-1.7	-0.9	-0.7	-0.7		-0.8	-0.3	
Contribution from real exchange rate depreciation	-1.7	-2.0	-1.8			1.2	-0.1	0.0	-0.4	-0.5	-0.3		...	...	
Other identified debt-creating flows	0.0	-3.2	-1.2			0.0	0.0	0.0	0.0	0.0	0.0		-0.2	0.0	
Privatization receipts (negative)	0.0	0.0	-0.3			0.0	0.0	0.0	0.0	0.0	0.0		-0.2	0.0	
Recognition of implicit or contingent liabilities 3/	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Debt relief (HIPC and other)	0.0	-3.2	-0.9			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Residual, including asset changes	-7.6	5.9	7.3			-2.8	-0.4	-1.1	-0.8	-0.6	-0.7		-0.4	-0.1	
NPV of public sector debt	73.9	65.7	56.1			50.8	46.1	41.8	38.2	34.9	31.6		19.6	7.2	
Of which: Foreign-currency denominated	44.4	41.9	36.7			34.3	32.0	29.6	27.7	25.7	23.9		15.8	6.4	
Of which: External	44.4	41.9	36.7			34.3	32.0	29.6	27.7	25.7	23.9		15.8	6.4	
NPV of contingent liabilities (not included in public sector debt) 3/	…	...	13.5			12.3	11.1	10.2	9.4	8.8	8.2		5.7	2.7	
Gross financing need 4/	-8.0	2.0	-2.0			2.3	0.0	-0.1	-0.1	-0.2	-0.1		-0.1	0.2	
NPV of public sector debt-to-revenue ratio (in percent) 5/	284.3	226.1	174.1			161.9	132.3	121.7	113.8	106.1	98.0		66.6	26.2	
Of which: External	170.7	143.9	114.0			109.3	91.8	86.2	82.4	78.2	73.9		53.5	23.2	
Debt service-to-revenue ratio (in percent) 5/ 6/	6.8	14.7	6.9			6.1	4.5	4.1	3.9	4.0	4.3		2.7	0.7	
Primary deficit that stabilizes the debt-to-GDP ratio	20.7	5.8	2.3			5.8	4.0	3.4	2.7	2.3	2.1		1.3	0.3	
Key macroeconomic and fiscal assumptions															
Real GDP growth (in percent)	8.0	5.0	6.1	0.0	7.1	5.4	4.2	2.8	1.6	1.5	1.6	2.8	2.9	3.1	2.8
Average nominal interest rate on forex debt (in percent)	2.0	1.6	1.3	2.3	1.2	1.7	1.7	1.7	1.7	1.7	1.6	1.7	0.0	0.0	0.4
Average real interest rate on domestic currency debt (in percent)	-4.3	-5.1	-4.7	-2.0	5.0	-2.3	-3.8	-3.6	-3.9	-3.4	-3.0	-3.3	5.9	17.5	8.8
Real exchange rate depreciation (in percent, + indicates depreciation)	-2.6	-3.5	-3.5	3.9	12.2	2.3	...	...	...	...	...	...	...	...	...
Inflation rate (GDP deflator, in percent)	5.8	7.7	7.2	6.5	2.1	4.9	6.3	6.0	6.3	5.8	5.3	5.8	4.7	4.5	4.7
Growth of real primary spending (deflated by GDP deflator, in percent)	3.0	24.5	15.4	6.0	12.4	17.7	13.7	2.8	1.0	0.4	0.9	6.1	4.3	4.0	2.8
Grant element of new external borrowing (in percent)	...	...	...	...	...	54.8	...	...	...	...	...	54.8	...	...	...

Sources: Data provided by the authorities; and Fund staff estimates.

1/ The DSA exercise was conducted jointly with the World Bank.
2/ Gross central government debt, including informal arrears. Foreign currency denominated debt converted using end-of-period exchange rate.
3/ Current estimate of recognized contingent liabilities. Remaining contingent liabilities are estimated at 14.3 percent of GDP.
4/ Gross financing need is defined as the primary deficit plus debt service plus the stock of short-term debt at the end of the last period.
5/ Revenues excluding grants.
6/ Debt service is defined as the sum of interest and amortization of medium- and long-term debt.
7/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

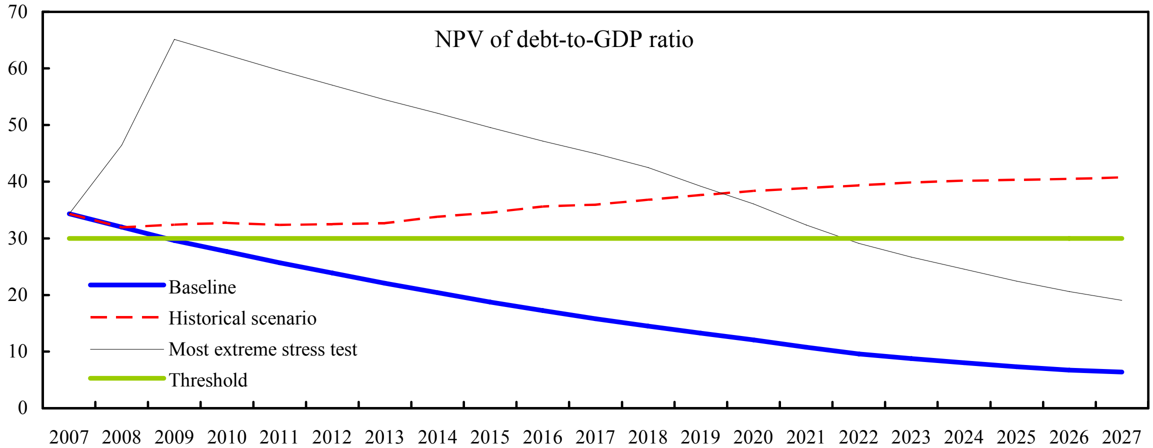
Appendix Table 13. Solomon Islands: Sensitivity Analysis for Key Indicators of Public Debt, 2007–27 1/

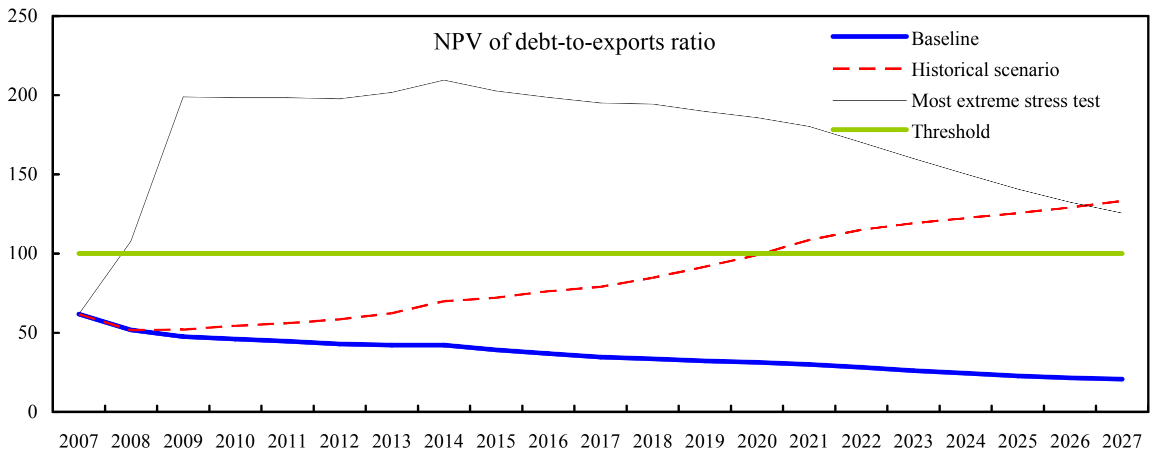
	Estimate	Projections						
	2007	2008	2009	2010	2011	2012	2017	2027
NPV of Debt-to-GDP Ratio								
Baseline	51	46	42	38	35	32	20	7
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	51	50	49	48	47	46	47	48
A2. Primary balance is unchanged from historical average	51	48	46	44	43	41	37	28
A3. Permanently lower GDP growth 2/	51	47	45	43	42	42	49	107
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviation in 2008-2009	51	56	64	67	70	73	90	123
B2. Primary balance is at historical average minus one standard deviation in 2008-2009	51	54	57	54	50	47	35	18
B3. Combination of B1-B2 using one half standard deviation shocks	51	55	59	52	46	41	19	6
B4. One-time 30 percent real depreciation in 2008	51	62	57	53	50	46	32	13
B5. 10 percent of GDP increase in other debt-creating flows in 2008	51	55	51	47	44	41	28	13
NPV of Debt-to-Revenue Ratio 3/								
Baseline	162	132	122	114	106	98	67	26
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	162	144	143	143	144	144	158	174
A2. Primary balance is unchanged from historical average	162	138	134	132	130	128	125	102
A3. Permanently lower GDP growth 2/	162	136	130	128	128	129	167	388
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviation in 2008-2009	162	160	186	199	212	226	304	447
B2. Primary balance is at historical average minus one standard deviation in 2008-2009	162	155	167	160	153	146	117	66
B3. Combination of B1-B2 using one half standard deviation shocks	162	158	171	156	141	126	65	240
B4. One-time 30 percent real depreciation in 2008	162	177	167	159	152	144	110	48
B5. 10 percent of GDP increase in other debt-creating flows in 2008	162	159	148	141	134	126	96	47
Debt Service-to-Revenue Ratio 3/								
Baseline	6.1	4.5	4.1	3.9	4.0	4.3	2.7	0.7
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	6.1	4.7	4.8	5.0	5.4	6.2	6.5	13.5
A2. Primary balance is unchanged from historical average	6.1	4.5	4.5	4.6	4.9	5.5	5.2	7.9
A3. Permanently lower GDP growth 2/	6.1	4.6	4.4	4.4	4.7	5.5	6.6	21.6
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviation in 2008-2009	6.1	5.0	5.8	6.8	7.9	9.3	12.2	31.9
B2. Primary balance is at historical average minus one standard deviation in 2008-2009	6.1	4.5	5.4	6.4	6.2	6.4	4.9	6.0
B3. Combination of B1-B2 using one half standard deviation shocks	6.1	4.8	5.7	6.2	5.7	5.8	2.8	8.9
B4. One-time 30 percent real depreciation in 2008	6.1	5.0	5.1	4.9	5.0	5.3	3.0	1.4
B5. 10 percent of GDP increase in other debt-creating flows in 2008	6.1	4.5	5.6	5.2	5.2	5.6	4.0	3.8

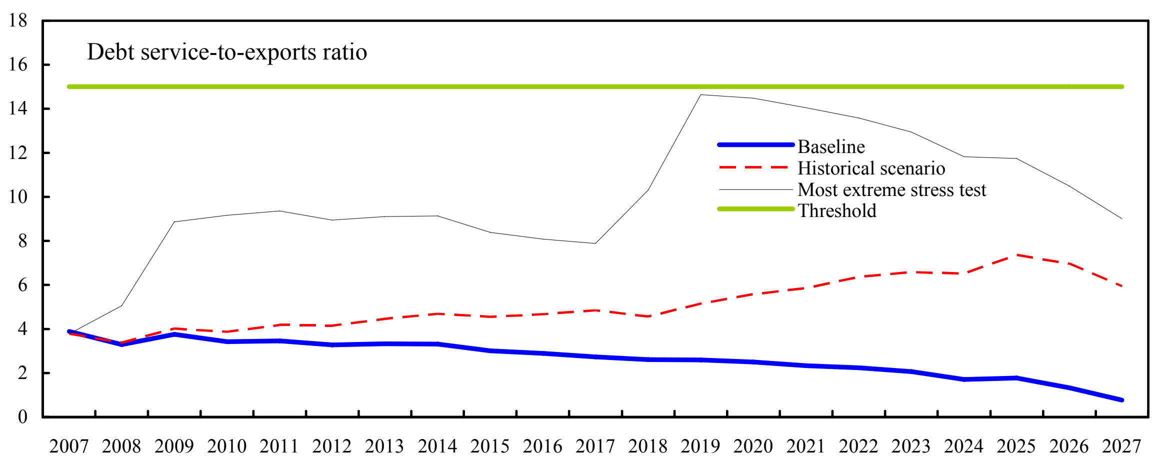
Sources: Data provided by the authorities; and Fund staff estimates.

1/ The DSA exercise was conducted jointly with the World Bank.
2/ Assumes that real GDP growth is at baseline minus one standard deviation divided by the square root of 20 (i.e., the length of the projection period).
3/ Revenues exclude grants.

Appendix Figure 5. Solomon Islands: Indicators of Public and Publicly Guaranteed External Debt Under Alternative Scenarios, 2007–27
(In percent)

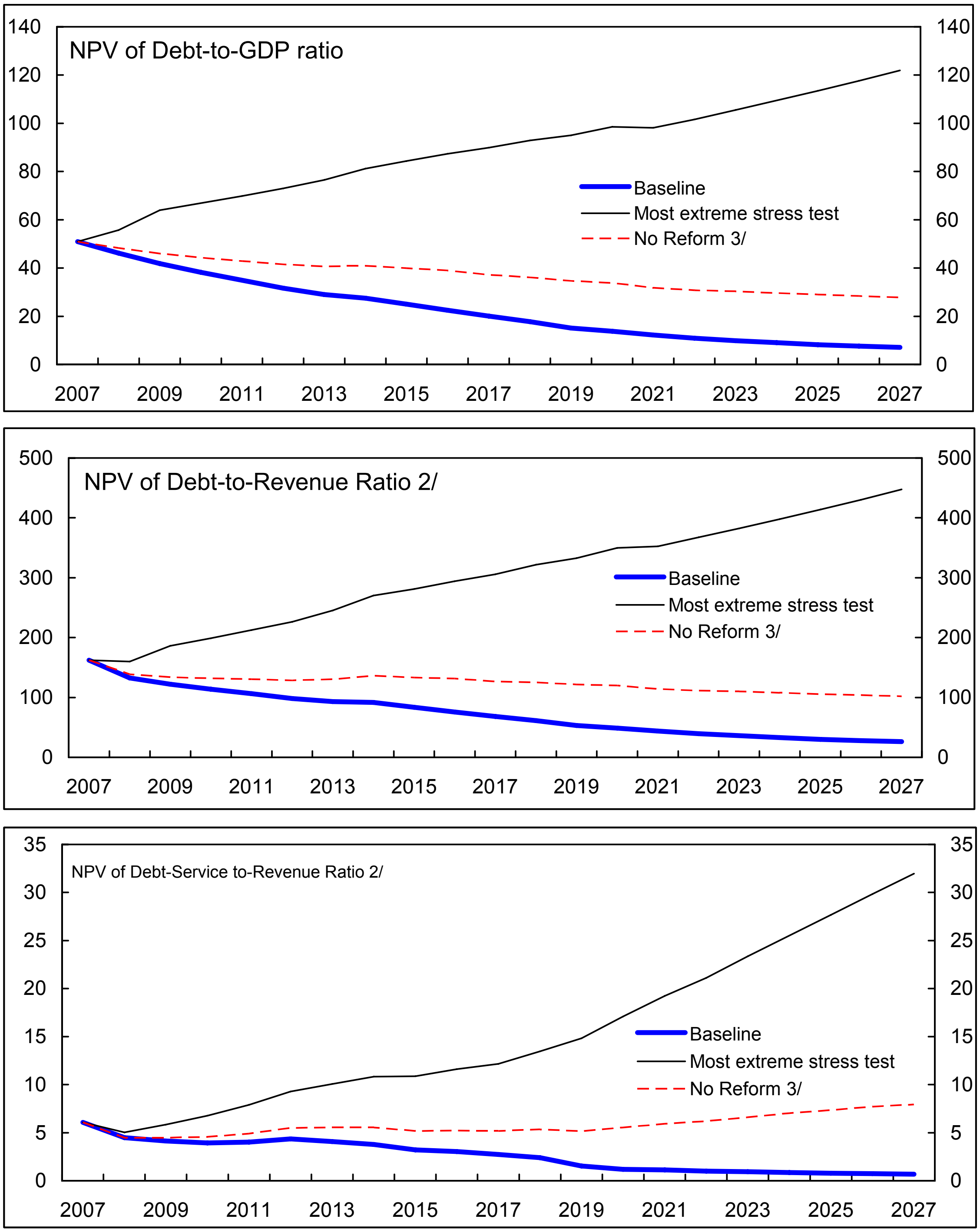






Source: Staff projections and simulations.

Appendix Figure 6. Solomon Islands: Indicators of Public Debt
Under Alternative Scenarios, 2007–27 1/
(In percent)



Sources: Staff projections and simulations.
1/ Most extreme stress test is test that yields highest ratio in 2017.
2/ Revenue includes grants.
3/ Primary balance remains at historical average.

INTERNATIONAL MONETARY FUND

SOLOMON ISLANDS

Staff Report for the 2007 Article IV Consultation—Informational Annex

Prepared by Staff Representatives for the 2007 Consultation with Solomon Islands

(In consultation with Other Departments)

June 29, 2007

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I. SOLOMON ISLANDS—FUND RELATIONS
(As of April 30, 2007)

I. Membership Status: Joined September 22, 1978; Article VIII

II. General Resources Account:

	SDR Million	Percent Quota
Quota	10.40	100.00
Fund holdings of currency	9.85	94.73
Reserve position in the Fund	0.55	5.29

III. SDR Department:

	SDR Million	Percent Allocation
Net cumulative allocation	0.65	100.00
Holdings	0.01	1.12

IV. Outstanding Purchases and Loans: None

V. Latest Financial Arrangements:

Type	Approval Date	Expiration Date	Amount Approved (SDR Mission)	Amount Drawn (SDR Million)
Stand-by	6/22/1983	6/21/1984	2.40	0.96

VI. Projected Payments to Fund:
(SDR Million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2007	2008	2009	2010	2011
Charges/Interest	0.02	0.03	0.03	0.03	0.03
Total	0.02	0.03	0.03	0.03	0.03

VII. Implementation of HIPC Initiative: Not applicable.

VIII. Implementation of MDRI Assistance: Not applicable.

IX. Exchange Rate Arrangements:

Since November 2000, the exchange rate for the Solomon Islands (SI) dollar has been based on an undisclosed trade-weighted basket of the currencies of the Solomon Islands' major trading partners, with the U.S. dollar as the intervention currency. During 2002, as pressures on external reserves intensified, the Central Bank of Solomon Islands (CBSI) accelerated the rate of currency depreciation, leading to a gradual real depreciation of the SI dollar. Since December 2002, the CBSI has kept the exchange rate broadly stable against the U.S. dollar, although there is no public commitment to continue to do so. The Solomon Islands now maintains an exchange system that is free of restrictions on the making of payments and transfers for current international transactions.

X. Last Article IV Consultation:

The 2006 Article IV Consultation discussions were held in Honiara during June 8–June 20, 2006. The staff report (IMF Country Report No. 06/362, August 30, 2006) was considered by the Executive Board and the consultation concluded on October 4, 2006.

XI. Technical Assistance:

Date	Department	Purpose	Duration
Short-term			
January 14, 1998	PFTAC	Statistics	2 weeks
February 3, 1998	PFTAC	Tax administration	1 week
May 4, 1998	PFTAC	Tax administration	4 weeks
June 7, 1998	PFTAC	Banking supervision	2 weeks
June 30, 1998	PFTAC	Balance of payments statistics	2 weeks
November 28, 1998	PFTAC	Public financial management	1 week
February 9, 1999	PFTAC	Banking supervision	1 week
September, 1999	MAE	Treasury bill auctions and monetary operations	8 weeks
October 3, 2000	MAE	Advisor to CBSI	2 weeks
May 2001	PFTAC	Banking supervision	1 week
October 2002	PFTAC	Banking Supervision	10 days
January 2003	PFTAC	Statistics	1 week
February 2004	PFTAC	Statistics	2 weeks
May 2004	PFTAC	Tax and customs administration	2 weeks
September 2004	MFD	AML/CFT	1 week
January 2005	PFTAC	Financial reporting system	2 weeks
February 2005	PFTAC	Financial supervision of insurance	2 weeks
April 2005	PFTAC	Financial supervision	2 weeks
May 2005	MFD	Financial supervision of insurance	2 weeks
May 2005	PFTAC	Tax policy and administration	2 weeks
August 2005	MFD	Reserve management	2 weeks
August 2005	MFD	Financial supervision of insurance	4 weeks
August 2005	PFTAC	Statistics	2 weeks
September 2005	PFTAC	AML/CFT	2 weeks
October 2005	LEG	AML/CFT	4 days
October 2005	MFD	Financial supervision of insurance	4 weeks
November 2005	STA	Monetary and Financial Statistics	3 weeks
January 2006	PFTAC	Tax policy	2 weeks
January 2006	LEG	Tax policy	2 weeks
February 2006	PFTAC	AML/CFT	2 days
February 2006	MFD	Financial supervision of insurance	4 weeks
February 2006	PFTAC	Statistics	2 weeks
April 2006	PFTAC	Statistics	2 weeks
April 2006	MFD	Central Bank Accounting	3 weeks
May 2006	PFTAC	Public Financial Management	2 weeks

June 2006	MFD	Central Bank Accounting	2 weeks
August 2006	PFTAC	Public Accounting Procedures	4 days
August 2006	PFTAC	Public Expenditure Management	3 weeks
October 2006	MCM	TA program monitoring	2 weeks
October 2006	MCM	Financial sector supervision	3 weeks
October 2006	MCM	Reserve Management	3 weeks
October 2006	PFTAC	Budget and Public Expenditure Mgt	1 week
December 2006	PFTAC	Business Revenue Reform	1 ½ weeks
February 2007	PFTAC	Balance of Payments Statistics	3 weeks
February 2007	PFTAC	National Income Accounts	3 weeks
March 2007	MCM	Accounting	2 weeks
July 2007	STA	Monetary and Financial Statistics	2 weeks
Long-term			
June 1995–June 1999;	MAE	Advisor to CBSI Governor	Five years extended in October 1999 through 2000
January 2001–present	MFD	Peripatetic Advisor to CBSI Governor	Ten six-week missions
August 2006-present	PFTAC	Public Financial Management	12 weeks in five months

XII. Resident Representative: None

II. SOLOMON ISLANDS—SUPPORT FROM THE PACIFIC FINANCIAL TECHNICAL ASSISTANCE CENTER[1]

(As of June 1, 2007)

Tax Administration and Policy

A mission in May 2004 designed plans to modernize and enhance the efficiency of the Customs and Tax Divisions. A further mission in May 2005 reviewed the current system, outlined a detailed strategy for the implementation of tax reforms over the next few years, and assessed the required technical assistance to support this strategy. The authorities released a tax reform proposal in conformity with PFTAC's advice. A mission in February 2006 assisted the government further with a detailed implementation plan, including discussions on the policy and design issues in relation to the VAT, income tax, and revenue administration. With assistance from LEG, draft legislation was prepared for the VAT and Revenue Administration Acts. In December 2006, a mission assisted the authorities in the preparation of a high-level design and project plan for the implementation of the Business Revenue Reform, and a follow-up visit took place in early May 2007. However, the government's revenue policy remains to be finalized.

Public Financial Management

In May 2006, the PFTAC adviser undertook a review of the *Public Finance and Audit Act (PFAA; 1978),* the *Financial Instructions (FI; 1978)* and the *Stores Instructions (1976;* SIs). The mission agreed with the authorities that the more immediate need was for a process redesign of the key accounting operations, linked to a significant redraft of the FI. In August 2006, a mission recommended measures to improve accounting operations and installed two consultants to redraft the FI. A final report was sent to the authorities in January 2007.

Financial Sector Regulation and Supervision

In September 2004, an advisor visited the CBSI to advise on the implementation of an anti-money laundering regime. A peripatetic advisor visited in January 2005 to assist with improving the CBSI's bank supervision department's database. In April 2005, the PFTAC advisor worked with an MCM expert to provide assistance in dealing with a failed insurance company and developing a supervisory framework for insurance companies, provided advice on the oversight of the National Provident Fund, developed supervisory guidelines on

[1] The Pacific Financial Technical Assistance Centre (PFTAC) in Suva, Fiji, is a regional technical assistance institution operated by the IMF with financial support of the Asian Development Bank, Australia, Japan, Korea, and New Zealand. The Center's aim is to build skills and institutional capacity for effective economic and financial management that can be sustained at the national level. Member countries are: Cook Islands, Federated States of Micronesia, Fiji, Kiribati, Marshall Islands, Nauru, Niue, Palau, Papua New Guinea, Samoa, Solomon Islands, Tokelau, Tonga, Tuvalu, and Vanuatu.

AML/CFT activities in financial institutions, and prepared a project document for the establishment of the Financial Intelligence Unit (FIU). In September 2005, the PFTAC advisor assisted CBSI staff in conducting an AML/CFT on-site examination of a domestic bank. CBSI staff also attended a seminar on monetary policy in shallow markets arranged by PFTAC/MFD in March 2005. In February 2006, the advisor participated in an AML/CFT awareness training seminar conducted by the CBSI. In November 2006, the CBSI hosted the annual meeting of the Association of the Financial Supervisors of Pacific Countries.

Economic and Financial Statistics

During 2003, the National Statistics Office (NSO) restarted activity, with the production of the Honiara CPI. A joint PFTAC/Secretariat of the Pacific Community mission in February 2004 devised a recovery plan, and AusAID and NZAID provided funding for equipment and a long-term advisor (a former PNG deputy statistician) to help build capacity and also to coordinate the Household Income and Expenditure Survey (HIES). The CBSI compiles balance of payments and GDP data and CBSI staff attended a regional training course on balance of payments statistics arranged by PFTAC in April 2005. Missions in August 2005 and February 2006 reviewed current methodologies for balance of payments and national accounts statistics and suggested some short-term improvements to their compilation. Assistance was also provided on a prototype government finance statistics system. In September 2006, the NSO released the findings of the 2005/06 HIES. Over the February–March 2007 period, PFTAC experts assisted the authorities in improving the compilation of balance of payments statistics and revising the GDP data.

Contact person: Susan Adams, Project Coordinator, sadams@imf.org.

III. Solomon Islands—Relations with the World Bank Group

(As of June 2007)

Since becoming a Bank member in June 1978, the Solomon Islands has received eight IDA credits totaling US$50 million in the infrastructure, education, health, finance, and agriculture sectors. Following the repayment of all outstanding arrears in September 2003, the Solomon Islands came out of nonaccrual status, and country relations have normalized. The Solomon Islands is eligible for an IDA 14 allocation of SDR 7.3 million (indicative only) over FY 2006–08. The IDA allocation for FY 07 is SDR 5.2 million.

The Bank's assistance to the Solomon Islands is motivated by the need for re-engagement in a low capacity post-conflict country, while recognizing the abundance of donor funds. The assistance program is guided by the government's own development priorities articulated in the *National Economic Reform, Recovery, and Development Plan* (2003–06), and the Bank's broader *Pacific Regional Strategy* which has a focus on: (i) strengthening government capabilities, and (ii) improving incentives for the private sector. The Bank's involvement in the Solomon Islands is in the following areas:

Strengthening Government Capabilities

- **Health Sector:** The government has initiated preparatory steps to move toward a sector-wide approach (SWAp) in the health sector, consistent with the direction that AusAID, as main donor to the sector, is also moving as indicated in the recent AusAID's White Paper on development aid. IDA is exploring options for its engagement to strengthen the health sector, including technical assistance, sector policy analysis and advice, and IDA grant funding (US$2 million), if there is a financing gap in the health program.

- **Education SWAp:** The Bank has co-financed a study to support the development of a National Skills Training Plan. The government has indicated interest in joining the Education for All Fast Track Initiative (FTI) and the process to prepare the Ministry of Education for participation has begun. It is hoped that with technical assistance, a costed sector strategy will be developed by late 2007 and formal FTI participation would begin in 2008. Any funding that the Bank provides for FTI activities would become part of the ongoing SWAp, which is currently financed only by the EU and NZAID.

- **Energy Supply:** The Bank is supporting the government's decision to implement a structural reform program in the electricity sector in order to improve electricity supplies, reduce their dependence on diesel-fired electricity generation, and provide affordable rural electricity systems. The government has determined that the best way to improve the performance of the Solomon Islands Electricity Authority (SIEA) is to contract out SIEA's management for five years through a performance based management contract. The management contract will provide the skills necessary to improve SIEA's commercial management as well as providing SIEA with the specialist expertise it requires to implement a proposed rural electrification program and a program to convert the outer islands diesel systems to bio-diesel. A management contract will also allow local managers to receive the training they require to resume full control of SIEA by the end of the contract. The procurement process has commenced with the appointment of a procurement advisor to the government funded by AusAid. The management contract is expected to commence by end-2007. The Bank has also included the Solomon Islands in a regional renewable energy project to be financed by the GEF.

- **Water Sector:** The Bank has prepared a Financial Restructuring Plan (FRP) for the Solomon Islands Water Authority (SIWA). The report provides the government and SIWA Board with an overview of SIWA's financial position and recommends that the management contract for the SIEA be extended to cover SIWA.

- **Rural Growth:** The Bank has completed the Agriculture and Rural Development Strategy (ARDS) which has been disseminated within the country. In parallel, the Bank has also started the preparation of the Solomon Islands Rural Development Project (RDP), which would be co-financed by the EU and AusAID, and implements the main recommendations of the ARDS.

Improving Incentives for the Private Sector

- **Telecommunications Sector:** The Bank is providing technical assistance to the government to examine ways to improve the competitiveness of the sector to reduce telecommunication costs and improve the service quality and coverage. Specifically, the Bank has provided technical assistance to the government to: (i) assess the telecommunication sector and offer the government strategic options for reform; (ii) prepare and implement a new telecommunication code; and (iii) provide the government with options to change the license granted to Solomon Telekom. The Bank will continue to assist the government to pass a modern telecommunications code (a good draft has been produced) to prepare for competition in the sector and good sector regulation. The Bank is ready to assist the government to manage the transition from a monopoly to competition if the management of Solomon Telekom is willing to renegotiate the exclusive license.

- **Foreign and Domestic Investment:** The Foreign Investment Advisory Service (FIAS) has provided assistance to the government for the preparation of new foreign investment legislation and is assisting with a review of investment incentives and administrative barriers to business.

Solomon Islands: IDA Lending Operations (as of June 12, 2007)

	Disbursed (USD million)	Undisbursed (USD million)
Health Sector Development Project	3.77	0.78

IV. Solomon Islands—Relations with the Asian Development Bank
(As of June 2007)

Since joining AsDB in 1973, Solomon Islands has received 16 loans amounting to $79.3 million, and 58 technical assistance (TA) projects amounting to $13.85 million. In 2006, AsDB also approved an Asian Development Fund (ADF) grant in the amount of $350,000. The last AsDB loan—Post-Conflict Emergency Rehabilitation Project (PCERP)—was approved in 2000. Solomon Islands is eligible for the Asian Development Fund (ADF) grants available to countries that are very poor, heavily indebted, or in a post-conflict situation. The 2005–06 ADF allocation for Solomon Islands succeeded in catalyzing substantial bilateral grant cofinancing for the improvement of rural roads.

AsDB's country assistance strategy seeks to achieve rapid, pro-poor, private sector-led economic growth, and focuses on improving transportation infrastructure and services and the enabling business environment. Capacity development and the promotion of good governance are priorities. AsDB assistance is provided entirely on a grant basis and, in line with government policy, no new lending to the country will be provided until public finances stabilize. The Country Strategy and Program Update 2007–09 can be found at www.adb.org/Documents/CSPs/SOL/2006.

AsDB has committed substantial support to the country in response to a strong earthquake and consequent tsunami on April 2, 2007, which caused significant damage in Choiseul and Western Provinces. AsDB supports the recovery and rehabilitation of the affected areas through disaster risk management advisory support to the Government, and assistance for the rehabilitation of damaged infrastructure to be accommodated within existing projects and a proposed ADF grant funded emergency project.

AsDB currently has five ongoing TA projects in the areas of institutional strengthening of the Ministry of Infrastructure and Development, inter-island transportation, state-owned enterprise reform and private sector participation, companies law, trustee law, companies registration, and secured transactions reform. AsDB's ongoing PCERP loan helps rehabilitate roads and bridges on Guadalcanal and Malaita that were damaged during the conflict. The Solomon Islands Road Improvement Project, approved in 2006 as an ADF grant with significant bilateral grant cofinancing, helps rehabilitate roads and bridges throughout the country to improve rural residents' access to markets and economic and social services, promote private sector-led development, foster market formation, and facilitate domestic and international trade and income and employment opportunities.

AsDB's Pacific Liaison and Coordination Office in Sydney is responsible for country programming, project implementation and administration, supported by the Pacific Operations Division in Manila.

Loans, Approvals, and Disbursements, 1999–2006

(In millions of U.S. dollars)

	1999	2000	2001	2002	2003	2004	2005	2006
Loan approvals	--	10.00	--	--	--	--	--	--
Loan disbursements	0.32	0.45	0.01	0.00	0.23	0.86	2.76	4.09
Cumulative loan amount approved (as of end-of-year)	69.31	79.31	79.31	79.31	79.31	79.31	79.31	79.31
Cumulative net effective loans (as of end-of-year)	64.65	54.30	64.05	64.83	65.87	66.31	79.31	79.31
Cumulative disbursements (as of end-of-year)	53.61	54.07	54.07	54.07	54.30	55.16	57.91	62.00

Contact person: Winfried Wicklein, Country Team Leader for Solomon Islands, AsDB Sydney (wwicklein@adb.org).

V. Solomon Islands—Poverty and Human Development Indicators

Social indicators of poverty and human development remain low in the Solomon Islands. The country ranks 128 out of 177 countries in the 2006 United Nations Human Development Index, below all Pacific island countries, except Papua New Guinea. There are few recent poverty statistics, but anecdotal evidence suggests poverty remains high. However, the more extreme forms of poverty, such as malnourishment, have remained limited due to an abundant resource base, assured access to customary land tenure, and resilient social networks. This advantage is under pressure from a population growth rate that, at about 3 percent a year, is among the highest in the world.[2]

Results of the 2005–06 HIES indicate that majority of the population do not have access to basic services such as electricity and water. For example, 86 percent of the population uses open fire for cooking, 80 percent relies on kerosene lamps as primary source of energy, and 78 percent does not have water piped into their household.

Nonetheless, the Solomon Islands has achieved some progress in improving living conditions since independence despite falling per capita incomes. Prior to the civil conflict in 1999, sizable health and education expenditures (at 3–5 percent of GDP each) and high per capita aid inflows had helped underpin these improvements. Providing widespread and quality education to the very young population (45 percent under age 15) is a challenge. The primary education enrollment ratio is about 95 percent, although primary education is not compulsory. The enrollment ratio is only 30 percent in secondary education. Concerning health, malaria is rampant, with the highest rate of infection in the world outside of sub-Saharan Africa, and a third of the rural population lacks access to safe water.

The paucity of data makes an assessment of human development trends since 1999 difficult, but anecdotal evidence suggests that pro-poor services delivery is improving. The positive trend was likely either halted or reversed during the civil conflict. While the conflict sharply reduced agricultural production for market (due to the lack of security and transport services), this has recovered since mid-2003 and service delivery has been enhanced.

The aggregate social indicators mask large differences between urban and rural areas. The two main problems in the rural sector are the lack of essential public services such as health and education, and cash income due to difficulties in market access for rural products. While the urban areas have better social services and average incomes are higher, the urban poor face difficulties in securing employment and land for residence.

[2] The 2005–06 HIES estimates the average population growth rate at 4.4 percent, but the authorities are disputing this.

The government has committed to monitor progress towards the Millennium Development Goals (MDGs). Achieving the MDGs by 2015 is still possible, but remains a major challenge. Progress in some areas, such as reducing malaria incidence, maternal mortality, and ensuring environmental sustainability, has so far been inadequate.

Table V.1. Solomon Islands: Millennium Development Goals Progress

	1990	2000	Latest Data 2003–05	Target 2015
Goal 1: Eradicate Extreme Poverty and Hunger				
Prevalence of child malnutrition (percent of children under 5)	21	21	…	11
Goal 2: Achieve Universal Primary Education				
Net enrollment ratio in primary education	83	74	80	100
Goal 3: Promote Gender Equality				
Ratio of girls to boys in primary school (percent)	86	92	97	100
Ratio of girls to boys in secondary school (percent)	63	78	81	100
Proportion of seats held by women in national parliament (percent)	0	2	0	…
Goal 4: Reduce Child Mortality				
Under 5 mortality rate (per 1,000)	63	60	56	12
Infant mortality rate (per 1,000 live births)	38	36	34	25
Goal 5: Improve Maternal Health				
Maternal mortality ratio (per 100,000 live births)	…	130	142	…
Births attended by skilled health staff (percent of total)	…	85	87	…
Goal 6: Combat HIV/AIDS, Malaria and Other Diseases				
Incidence of tuberculosis (per 100,000 people)	134	73	59	…
Incidence of malaria (per 100,000 people)	45,000	15,172	19,600	less than 8,000
Goal 7: Ensure Environmental Sustainability				
Forest area (percent of total land area)	99	91	78	…
Nationally protected areas (percent of total land area)	…	0	0.3	…
CO2 emissions (metric tons per capita)	0.5	0.4	0.4	…
Access to an improved water source (percent of population)	…	71	70	100
Access to improved sanitation (percent of population)	…	30	31	…
Goal 8: Develop a Global Partnership for Development				
Fixed line and mobile telephones (per 1,000 people)	15	21	17	…
Personal computers (per 1,000 people)	…	38	43	…

Sources: World Bank, World Development Indicators; and World Bank Human Development Indicators.

Table V.2. Solomon Islands: Social Indicators

	Latest Single Year				Same Region/Income Group	
	1970–75	1980–85	1990–95	1996–2005	East Asia & Pacific	Low-Income
POPULATION						
Total population, mid-year (thousands)	193	300	364	477	1,870	2,353
Growth rate	3.6	3.4	2.6	2.5	0.8	2.0
Urban population (percent of population)	9.1	12.4	15.0	16.8	40.6	30.6
Total fertility rate (births per woman)	7.1	6.2	5.0	4.1	2.0	4.0
INCOME						
GNI per capita (US$)	290	530	880	590	1,627	580
Consumer price index (2000=100)	8	20	64	139	127	128
Food price index (1995=100)	...	33	...	158	...	...
SOCIAL INDICATORS						
Public expenditure						
Health (percent of GDP)	...	...	…	5.0	1.9	1.5
Education (percent of GDP)	5.3	4.5	3.8	3.8	2.3	3.0
Social security and welfare (percent of GDP)	...	...		... ...	...	...
Net primary school enrollment rate						
(Percent of age group)						
Total	...	...	83	80	…	79
Male	...	...	89	80	…	…
Female	...	...	77	79	…	…
Access to an improved water source						
(Percent of population)						
Total	...	...	…	70	79	75
Urban	...	...	…	94	92	88
Rural	...	...	…	65	70	70
Immunization rate 1/						
(Percent 12-23 months)						
Measles	...	...	68	72	82	63
DPT	...	46	69	80	87	67
Child malnutrition (percent under 5 years)	21	...	…	21	15	39
Life expectancy at birth						
(Years)						
Total	57	62	61	63	70	59
Male	56	61	60	62	68	58
Female	58	63	62	63	72	60
Mortality						
Infant (per 1,000 live births)	71	43	37	34	29	80
Under 5 (per 1,000 live births)	99	56	63	56	37	122
Adult (15-59)						
Male (per 1,000 population)	...	...	...	261	169	298
Female (per 1,000 population)	...	...	...	237	111	244
Maternal (modeled, per 100,000 live births)	...	...	...	142	117	681
Births attended by skilled health staff (percent)	...	...	85	85	86	41.0

Source: World Bank, 2006 World Development Indicators.
1/ Immunization refers to children aged 12-23 months who received vaccinations before one year of age.

VI. Solomon Islands—Statistical Issues

The economic and financial database is poor, which significantly hampers surveillance, particularly for the real, fiscal, and external sectors. Although the National Statistics Office (NSO) is being rebuilt, the central bank (CBSI) continues to publish highly summarized monetary and price data in its *Monthly Economic Bulletin* and data on all sectors in its *Quarterly Review* and *Annual Report*. There is a Solomon Islands page in *IFS,* but significant updating delays occur, particularly for the balance of payments (BOP), government finance, and national accounts statistics.

Real Sector Statistics

As the NSO has not produced national accounts data since 1994, the task of preparing GDP estimates was taken over by the CBSI. GDP estimates are severely hampered by data availability and quality, and rely on limited sources (primarily commodity exports and employment estimates). Data on production of major export commodities are reported monthly. No breakdown of GDP by expenditure categories exists. A survey of business activities for 2003 covering 1,434 businesses was published by the NSO in August 2006, including employment and financial data for NSO-registered private and government business enterprises. The 2004 business survey is still being finalized.

A 2005–06 Household Income and Expenditure Survey (HIES) completed in September 2006 should help strengthen estimation of GDP. A PFTAC advisor in February 2007 rebased the GDP to 2004 and recalculated the GDP series, but major weaknesses in measuring GDP, primarily the shortage of informal sector data, severely limit the accuracy of GDP estimates, which the authorities have not yet adopted.

The NSO resumed production of the CPI (which currently covers only Honiara, the capital) in August 2003, but the weights are outdated. Using the HIES results, the weights of the Honiara price index are scheduled to be revised in 2007, and eventually, a national CPI measure will be estimated. Limited data on total employment can be obtained from the National Provident Fund. Wage data are not compiled.

Monetary and Financial Statistics (MFS)

The CBSI publishes monthly MFS in summary form and provides more detailed data in its quarterly and annual reports. Monetary statistics had been reported every two months to STA, but now reporting has fallen behind. A November 2005 expert mission, during a PFTAC monetary statistics workshop held in Fiji, reviewed the compilation procedures and provided training and a work plan for the CBSI to comply with the methodology of the *Monetary and Financial Statistics Manual* and to report data using the standardized report forms (SRFs). However, limited progress has been made on the mission's recommendations due to the high turnover rate of the CBSI's monetary statistics team. A PFTAC mission scheduled for July 2007 will assess the progress in the implementation of the 2005 mission's recommendations, introduce the SRFs, and develop an integrated monetary database that will meet the data needs of the CBSI and the Fund.

Government Finance Statistics (GFS)

The Ministry of Finance (MOF) started monthly press releases on budget outturns in August 2003. However, its expenditure and financing data are not consistent with the *GFSM 2001* methodology, and historical data seems unreliable given the breakdown of accounting mechanisms and large expenditure arrears during the conflict. The NSO has developed a prototype GFS system, but problems exist in the coverage of the general government. In particular, data for provincial governments are unavailable and ongoing audits of state enterprises have yet to be completed. The authorities started collecting disbursement information on donors' grants in 2006. The introduction of the Commonwealth Secretariat Debt Recording and Management System (CS-DRMS) database in the CBSI and MOF in March 2005 has improved the quality of official debt data, but coordination problems remain. The MOF does not report annual or subannual GFSM 2001-based data for the *Government Finance Statistics Yearbook* (*GFSY*) and the *International Financial Statistics* (*IFS*), respectively.

External Sector Statistics

The CBSI estimates partial quarterly BOP data based on cash foreign exchange transactions (FET) reported through the banking system, which are available with a three-month lag. These data are deficient in detail and coverage. A February 2006 PFTAC mission noted a significant deterioration in the net errors and omission item. In addition, "other items" in several categories have increased significantly, indicating a deterioration of data quality. Surveys of enterprises on service and financial flows are conducted to collect supplementary information, but the response rates are very low. The NSO started publishing merchandise trade data in 2005 but there are still coverage issues. A mission from New Zealand in February 2006 began to install PCTrade software in the Customs Department to facilitate the NSO's use of Customs data to prepare trade statistics. A February 2007 PFTAC mission assisted the authorities in further improving compilation of the BOP and international investment position statistics. The key recommendations were: (i) improve the balance of payments report forms, (ii) maintain regular contact with the most important respondents, (iii) improve coverage and classification in the foreign exchange transactions system, and (iv) further develop the international investment position, including integrating it with other external sector statistics.

Remedial Measures

The NSO is gradually resuming data collection and publication responsibilities, but its effectiveness continues to be hampered by weak technological skills among its staff and low survey response rates. A PFTAC GDDS mission in February 2004 concluded that rebuilding the statistical system will require extensive technical assistance and external funding. Following its recommendations, a new government statistician was appointed in 2004 and a long-term social statistics advisor (18 months)—funded by AusAid and NZAid—took up his post in April 2005. In addition, the NSO and CBSI supported the February 2007 PFTAC mission's advice to engage an economic statistics advisor to further strengthen compilation. The CBSI is planning to host a STA/PFTAC mission in July 2007 to further develop the monetary statistics.

Preparations for a Demographic and Health Survey started in mid-2006. The Ministry of Tourism, in coordination with NSO, has started a project to measure tourism spending. A population census is planned for late 2009, with preparations expected to commence in 2007. The NSO has requested PFTAC's assistance to enhance the GFS, and the Secretariat of the Pacific Community's (SPC) assistance to rebase the CPI.

The February 2006 PFTAC mission identified a number of statistical issues that require attention, including: (i) ensuring that compilation methodologies are applied consistently for GDP and BOP data; and (ii) collecting prices for additional items in the CPI, particularly on diesel fuel and telecommunications products. In the area of the BOP, there is a need to: (i) increase the response rate to enterprise surveys to reduce reliance on FET records; (ii) investigate alternative data to supplement FET data, including the use of official transfers data from the government's financial accounts; and (iii) review the Customs merchandise data.

TABLE VI. 1. SOLOMON ISLANDS—COMMON INDICATORS REQUIRED FOR SURVEILLANCE

(As of June 22, 2007)

	Date of Latest Observation	Date Received[8]	Frequency of Data[9]	Frequency of Reporting[9]	Frequency of Publication[9]
Exchange Rates	May 2007	May 2007	D	M	M
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	May 2007	May 2007	W	M	M
Reserve/Base Money	December 2006	February 2007	M	M	M
Broad Money	December 2006	February 2007	M	M	M
Central Bank Balance Sheet	December 2006	February 2007	M	M	M
Consolidated Balance Sheet of the Banking System	December 2006	February 2007	M	M	M
Interest Rates[2]	April 2007	April 2007	W	M	M
Consumer Price Index	April 2007	May 2007	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[3]–Central Government	December 2006	May 2007	A	A	A
Revenue, Expenditure, Balance and Composition of Financing[3]–General Government[4]	NA	NA	NA	NA	NA
Stocks of Central Government and Central Government-Guaranteed Debt[5]	December 2006	May 2007	A	A	A
External Current Account Balance[6]	March 2007	May 2007	Q	Q	Q
Exports and Imports of Goods and Services[6]	March 2007	May 2007	Q	Q	Q
GDP[7]	December 2006	May 2007	A	A	A
Gross External Debt[10]	December 2006	March 2007	A	A	Upon Request

[1] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[2] Both market-based and officially-determined, including discount rates, money market rates, rates on Treasury bills, notes and bonds.
[3] Foreign, domestic bank, and domestic non-bank financing.
[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.
[5] Including currency and maturity composition.
[6] Detailed BOP data derived from FET through the banking system and trade data from the Customs and Excise Division are available on a quarterly basis with a 3-month and 5-month lag, respectively.
[7] The most recent official data are for 1994, but the central bank has produced real production estimates through 2006.
[8] Includes data received following specific requests by Fund staff.
[9] Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Annually (A); and Not Available (NA).
[10] Data on private sector debt is not available.

INTERNATIONAL MONETARY FUND
Public Information Notice
EXTERNAL RELATIONS DEPARTMENT

Public Information Notice (PIN) No. 07/110
FOR IMMEDIATE RELEASE
September 7, 2007

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Executive Board Concludes 2007 Article IV Consultation with the Solomon Islands

On July 16, 2007, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with the Solomon Islands.[1]

Background

The economy has been recovering since the end of the civil conflict and the intervention of the Regional Assistance Mission to the Solomon Islands (RAMSI) in mid-2003, but the country remains poor and relies heavily on logging and aid. Over the last four years, economic growth has averaged 6 percent—although logging is occurring at an unsustainable rate—and financial stability has been maintained. Large amounts of donor assistance and the restart of two large projects (gold mine and palm oil plantation) have helped sustain economic activity.

Real GDP growth rose to an estimated 6 percent in 2006, driven by fish, palm oil production, and services, but is expected to ease to 5½ percent in 2007, as a further escalation in logging—now running at around five-times the sustainable rate—will be likely offset by lower growth of fish and traditional crops. The April 2007 tsunami is not expected to have a significant impact on growth. The current account deficit, which widened slightly to 26 percent of GDP in 2006, mainly reflecting higher fuel and investment-related imports, is expected to increase to 40 percent of GDP in 2007 due to imports related to the refurbishment of the gold mine

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities.

(17 percent). Nevertheless, continued strong aid flows and foreign direct investment are expected to keep reserves adequate.

A sizeable overall budget surplus in 2006 helped slow overall monetary growth, as the resulting contraction in credit to government partly offset continued strong growth in banking sector credit to the private sector. This moderation in monetary growth, combined with receding oil prices, helped inflation decelerate to 7½ percent from 8½ percent at end-2005. In 2007, despite a higher revenue effort, the overall budget surplus is projected to decline to ½ percent of GDP, reflecting sharply higher spending on wages and goods and services. Thus, while private sector credit growth is expected to moderate and oil prices stabilize, inflation is projected to ease only slightly, to 7 percent by end-year.

With the natural forest expected to be depleted within the next few years, structural reforms are necessary to generate higher sustainable growth, raise living standards, and reduce the economy's vulnerability to shocks. However, progress in this area has been mixed. Import duties were lowered; statutory and discretionary tax exemptions were reduced; reference prices of logs were raised for the first time since 2003; work permit and immigration procedures were streamlined; and, with the help of donors, sectoral strategies are being implemented in health, education, transport, and agriculture. The road network is improving. Against this, little progress has been made in easing other critical constraints to higher sustainable growth; namely, in restructuring the utilities, which continue to provide unreliable and costly services and threaten the budget, and in strengthening governance, which continues to be adversely affected by opaque rules, the perception that government exercises excessive discretion, and uncertain land tenure arrangements.

Executive Board Assessment

Executive Directors welcomed the Solomon Islands' favorable near-term growth prospects, and the authorities' success in maintaining macroeconomic stability since the end of the civil tensions, and the support of the Regional Assistance Mission to the Solomon Islands. Directors supported the authorities' intention to adopt a medium-term national development strategy, which once implemented, could help them better cope with the significant challenges ahead. These include improving the outlook for employment, poverty reduction, and growth, against the backdrop of rapid depletion of the natural forests due to intensive logging. In that connection, Directors encouraged the authorities to implement their planned structural reforms to generate alternative sources of growth in the context of a poverty reduction strategy framework.

Directors commended the recent strengthening of the revenue effort, especially in reducing tax exemptions and improving tax administration and collection in the Inland Revenue Division, and the simplification of the import duty structure. They encouraged the authorities to save most of this year's expected revenue overperformance. They looked forward to the introduction of an automatic adjustment mechanism for the reference prices of logs used in calculating export duties, and to further progress on a comprehensive tax reform. Directors welcomed proposals to strengthen the budget process and called for efforts to rein in current expenditure in order to make room for higher spending on high-priority maintenance and infrastructure investments.

This should include tighter payroll controls, linking future civil service wage increases to productivity improvements, and strengthening public financial management.

Looking ahead, Directors encouraged the authorities to adopt a medium-term fiscal framework to help anchor fiscal policy in the face of impending revenue pressures, assist with the prioritization of spending, and support the attainment of debt sustainability. They recommended that the authorities refrain from new borrowing until the sustainability of public debt is well secured.

Directors supported the central bank's commitment to restrain inflation and its readiness to tighten reserve requirements if inflation accelerates. They considered that the introduction of a standing deposit facility would help absorb some of the excess liquidity and increase the central bank's control over monetary aggregates. Looking ahead, Directors recommended that the authorities develop a more forward-looking and proactive approach to monetary policy, and supported Fund assistance to develop inflation forecasting capability. Directors agreed that the banking system appears generally sound, but the continued growth in bank credit calls for intensified supervision and tightened loan classification.

Directors observed that although the current account deficit is fully financed by aid inflows and foreign direct investment, close monitoring is called for in view of the large swings in the deficit. Export competitiveness appears adequate, but Directors cautioned that a large minimum wage increase—in excess of productivity increases—could weaken labor-intensive exports and rekindle inflation. Directors supported the current exchange rate policy of stabilizing the exchange rate against the U.S. dollar, in the light of strong inflows and adequate competitiveness. However, Directors recommended that the exchange rate be allowed to adjust downward, if needed, in response to market pressures.

Directors considered that the restructuring of state-owned enterprises, liquidation of the Development Bank of Solomon Islands, and durable strengthening of the National Provident Fund will be critical to minimize future contingent liabilities and improve public sector governance. They encouraged the authorities to implement without further delay the management contracts for the electricity and water utilities, which should lower costs and improve service delivery. Continued efforts to improve basic infrastructure should lead to a better return on investments over the medium term. Directors welcomed recent improvements in the investment and business environment, and looked forward to further progress, including the promotion of further governance enhancements.

Directors welcomed recent improvements in the statistical database, and recommended continued efforts to address weaknesses that complicate the effectiveness of surveillance and policymaking.

Public Information Notices (PINs) form part of the IMF's efforts to promote transparency of the IMF's views and analysis of economic developments and policies. With the consent of the country (or countries) concerned, PINs are issued after Executive Board discussions of Article IV consultations with member countries, of its surveillance of developments at the regional level, of post-program monitoring, and of ex post assessments of member countries with longer-term program engagements. PINs are also issued after Executive Board discussions of general policy matters, unless otherwise decided by the Executive Board in a particular case. The staff report (use the free Adobe Acrobat Reader to view this pdf file) for the 2007 Article IV Consultation with Solomon Islands is also available.

Solomon Islands: Selected Economic Indicators, 2002–07

	2002	2003	2004	2005	2006 Est.	2007 Proj.
Growth and prices (percentage change)						
Real GDP	-1.6	6.4	8.0	5.0	6.1	5.4
Of which: Nonlogging	-1.9	4.6	5.5	4.5	6.0	3.6
CPI (period average)	9.3	10.0	6.9	7.3	8.1	6.3
CPI (end of period)	15.3	3.7	7.6	8.4	7.5	7.0
Per capita GDP (in US$)	514	508	566	619	678	709
Central government operations (percent of GDP)						
Total revenue and grants	18.7	38.8	47.5	65.9	70.1	69.0
Recurrent revenue	16.1	20.9	26.0	29.1	32.2	35.0
Grants	2.6	17.8	21.5	36.8	37.9	34.0
Total expenditure 1/	29.6	38.9	39.5	63.9	66.0	68.5
Recurrent expenditure	26.4	23.6	22.2	26.8	28.1	32.8
Development expenditure	3.2	15.4	17.2	37.1	37.8	35.7
Recurrent balance 2/	-9.9	1.2	8.1	4.1	6.8	4.4
Overall balance 3/	-10.9	-0.2	8.0	2.0	4.1	0.5
Foreign financing (net)	3.8	0.2	-0.9	2.6	0.9	0.2
Domestic financing (net)	-2.9	-9.2	-6.6	-2.1	-1.8	-0.8
Other	8.9	9.8	-2.3	-2.3	0.1	0.1
Stock of expenditure arrears (in percent of GDP, end of period) 4/	12.0	14.7	7.8	3.6	2.8	2.6
Central government debt (percent of GDP) 5/	113.3	120.4	90.2	81.3	72.8	66.7
Domestic	46.7	50.9	29.8	24.4	18.9	16.3
External	66.6	69.5	60.4	56.9	53.9	50.4
External debt (in US$ millions, end of period)	151.6	160.8	160.3	169.5	180.7	181.9
External debt service to exports of GNFS (accrual basis)	10.3	9.3	5.9	7.2	4.3	4.3
Monetary and credit (percentage change, end-year data)						
Net foreign assets	30.2	101.8	118.8	22.0	8.1	15.2
Net domestic assets	-4.8	-9.0	-64.4	63.2	108.2	24.9
Net domestic credit	11.0	-2.9	-34.7	37.6	37.7	26.3
Credit to private sector	12.2	26.1	10.5	63.1	62.5	23.2
Broad money	4.0	26.0	28.2	27.7	25.7	18.0
Interest rate (3-month t/bill rate, average) 6/	8.3	5.8	6.0	4.5	3.5	3.4
Balance of payments (US$ millions, unless otherwise indicated)						
Exports, f.o.b	57.8	74.2	96.7	102.5	120.4	146.2
Imports, c.i.f.	-69.1	-93.8	-121.4	-185.1	-250.6	-291.7
Current account	-23.2	-5.7	8.3	-72.3	-88.9	-144.4
(percent of GDP)	-10.2	-2.5	3.1	-24.2	-26.5	-40.0
Capital account	6.3	21.1	28.1	82.5	94.6	152.6
Overall balance (accrual)	-16.9	15.3	36.4	10.3	5.7	8.2
Gross official reserves (US$ millions, end of period)	17.5	36.3	80.0	94.6	103.8	113.0
(in months of next year's imports of GNFS)	1.9	3.0	4.5	4.0	3.5	3.9
Exchange rate (SI$/US$, end of period) 6/	7.46	7.49	7.51	7.58	7.62	7.65
Real effective exchange rate (period average, 2000=100)	90.1	78.5	77.1	79.5	83.5	...
Nominal effective exchange rate (period average, 2000=100)	80.1	64.4	60.3	59.1	58.5	...

Sources: Data provided by the authorities; and IMF staff estimates.
1/ Expenditures are presented on an accrual basis.
2/ Includes recurrent budget grant support.
3/ Calculated from above-the-line data.
4/ Includes interest arrears.
5/ Includes arrears.
6/ As of May 30, 2007.