

# **Deciding our future now, the choice is ours: Statement by Central Bank of Solomon Islands (CBSI) Governor, Denton Rarawa on the Launch of the 2009 CBSI Annual Report, Mendana Hotel, 13<sup>th</sup> May 2010**

## **Salutations**

Minister of Finance,  
Other Ministers,  
Representatives of the Diplomatic Corps,  
Senior Government officials,  
Central Bank Directors,  
Heads of Statutory Authorities,  
Commercial Bank Managers,  
Representatives of Non-Government Organizations,  
Representatives of the private sector,  
Representatives of the media,  
Ladies and gentlemen,

Good morning to you all and welcome to the launch of the 2009 Central Bank Annual Report.

This is my second annual report, and I would like to use this chance to comment on the current state of the Solomon Islands economy and how we in the Bank see the future. It is also an opportunity for me to account for the Banks actions and operations last year.

## **Introduction**

Last year, while launching the 2008 annual report in this same room, I described our situation then as that of a small boat adrift in the middle of a major storm. At that time we were unsure about the strength of the storm and how long it will last. Twelve months later, the storm has abated. We have faced its destructive fury but we have survived and emerged on the other side, battered and bruised but still afloat. I believe that experience has taught us many important lessons for the future. Now our boat needs repairs and a fresh lot of crew and captain to man the ship.

2010 is an important year for Solomon Islands. It is a year we have to make important choices. Because the choice we make will determine our future, not only in the next five years but the future of our children and grand children. I will return to this theme later on in my presentation.

But, first I would like to begin today by reviewing the year gone by outlining for you the Bank's impressions of how the global economic crisis unfolded in 2009 and how the Solomon Islands economy fared whilst navigating this storm.

## International Economy

In 2009 the world economy shrunk for the first time since the Great Depression. All across the globe production, trade, credit and confidence collapsed.

On average it was the industrialised nations who fared worst. The United States, where the financial collapse began, saw its economy contract two and a half percent, the Euro area declined by nearly four percent, whilst the Japanese economy shrunk by over five percent. The only major industrial nation not to enter recession in 2009 is our close neighbor Australia. Even there the year saw pain and hardship; as exports faltered and unemployment rose.

The developing and emerging nations of the world as a group continued to grow in 2009. The experiences of individual nations was however highly varied. Whilst some countries, especially in Asia, continued to grow at a rapid, although greatly reduced rate, others experienced deep slumps. China, our largest trading partner, expanded by over eight and a half percent in 2009 whilst the Russian economy shrunk by nine percent.

Only dramatic and unorthodox action from a large number of countries averted catastrophe and prevented global recession descending into global depression. Learning the lessons of the 1930s, governments around the world reacted swiftly with large spending packages. Central Bank lending rates plummeted toward zero whilst quantitative easing became mainstream monetary policy.

From the second quarter of the year these interventions began to yield results as a number of countries began to show the 'green shoots' of recovery. The global economy has since rebounded at a pace exceeding the expectations of many commentators.

The recovery however has been unbalanced and remains fragile. Whilst some nations have begun to grow again, others remain deep in recession. Even in countries where recovery has taken hold the threat of a 'double dip' recession persists. Unemployment rates remain high and the levels of sovereign debt that some governments have accumulated is a major risk to the recovery. It is hoped that the actions taken by the European Union and the IMF will avert a default by Greece and also prevent Portugal and Spain also falling into difficulties.

## Domestic Economy

Turning our attention to home, the global economic crisis has hit our country hard. The Bank estimates that the real GDP of Solomon Islands fell by 2% in 2009. This fall and the continued rise in our population meant that real GDP per capita, has fallen by around 5% last year. This represents a fall in the average incomes of people in this country.

This decline in GDP has been caused by falls in output from our key industries especially logging, fisheries and copra.

Exports of **round logs**, which for many years have supported our economic growth, collapsed in 2009, falling by 31%. This decline was caused by faltering demand from major overseas buyers of our logs. In particular, weaknesses in Asian housing markets strongly impacted negatively on demand for our logs.

One 'silver lining' has been the expansion of exports of plantation logs. Despite the effects of the global economic crisis, output in this sector increased across the year. With the sustainable nature of this product, it is hoped this industry can be successful and continue long after the exhaustion of natural forest stocks, which is predicted to occur in the not too distant future.

Total **fish catch** in the country declined by around 24% as international price falls and poor weather conditions affected production. This, along with the cessation of fishing activities by one major company, which now intends to concentrate on other activities, contributed to this poor performance in another of our key industries.

Our **copra producers** also suffered a poor year, with output declining by 37%. Falls in the price of copra combined with its high price elasticity of demand, decreasing yields due to the increasing senility of coconut palms, and continued problems with shipping, all contributed to this decline.

Of our major commodities only **cocoa** and **palm oil** made gains in 2009, but these gains were not sufficient to prevent the overall decline in production. Cocoa production increased 5%, as high international prices and the cocoa livelihood program helped boost production levels. The palm oil industry also continued with the impressive growth we have seen since its restart in 2006.

This year I am delighted to be able to comment on a range of smaller, upcoming commodities. The Bank has started collecting data from a range of commodities that are becoming important for incomes in rural areas. Of these, I can report that **coffee** grew by around 78% last year, **vanilla** production increased 7 fold and **kava**, which is now being exported regionally, increased in output by 55%.

Looking to the rest of the economy; **tourism** saw a promising year as arrivals rose by around 11%, despite global economic difficulties. Those arriving are also spending more money, boosting the local economy. A key driver of this has been the increasing competition in international aviation, which has brought improvements in service and lower fares. Internal transport links have also improved with increased reliability and comfort on domestic air routes and on passenger ships. The improving quality and expanded capacity of accommodation has also been a key contributor to growth in this industry.

The **telecommunication** industry also experienced growth in 2009. Prices have fallen and service coverage expanded as the incumbent provider prepared itself for the arrival of competition in mid 2010.

## **Balance of Payments**

The decline in commodity exports in 2009 did not only damage growth but also hit our trade imbalance. Poor export performance from the country's major foreign exchange earners was the key cause of the 19% fall in export receipts.

The country recorded a large trade deficit in 2009. The deficit in the services account however, improved across 2009 as net receipts from transportation and travel improved.

Even with the reduced deficits in services and larger positive inflows from secondary income, the increased deficit on primary income meant that the current account deficit again widened in 2009.

The overall balance of payments however showed a surplus of \$361million in 2009 as large capital and financial account inflows outweighed this loss from the current account.

## **Government Finances**

The decline in exports also had a strong impact on Government balances in 2009, cutting revenue and damaging cash flows. The Government responded with a rapid re-prioritisation to ensure the uninterrupted delivery of front line services and the continued operation of the machinery of government.

To achieve this, the Government issued a revised budget, in which many development projects were scaled back or deferred. Public sector recruitment in non-essential areas was frozen and reservations were placed on non-payroll expenditure, to help control Government costs. Measures were also taken to improve domestic revenue collection, especially through programs to reduce tax evasion.

These measures, combined with a \$79 million supplementary appropriation bill and, importantly, the continued support of the donor community, enabled the government to navigate the storm.

## **Foreign Reserves**

Moving onto the main business of the Bank; Solomon Islands' gross foreign reserves rose 64% across 2009, reaching a record high, of \$1,179 million, at year end. The main causes behind this rise were the one-off allocation of special drawing rights by the IMF to member countries, including Solomon Islands, and the continued support of the donor community. Currency revaluations, foreign direct investment inflows and tight monetary policy at the beginning of the year, also contributed to this rise.

The Bank has therefore found itself in a far more comfortable position at the end of 2009 than it had in the previous year, with reserve levels representing 6 months forward import cover, whilst at the close of 2008 this figure had been 2.5 months.

## **Inflation**

Inflation was a serious problem for Solomon Islands in 2008. Having risen to 23.5% in September 2008 it remained very high until the end of the year, finishing around 19.4%. In 2009 inflation has come under control and is now at a low and stable level, finishing the year at 1.3%.

Two major factors have contributed to this decline. The rapid falls in global inflation, in particular falls in oil prices, have been a key development. As prices fell across the world inflationary pressures in Solomon Islands also eased. Domestically, competition in the supply of rice and telecommunication services as well as the tight monetary policy pursued by the Bank at the end of 2008 all played a role in reducing inflation. Across the year as

inflation decreased and the economic conditions worsened the Central Bank loosened monetary policy, to help boost the economy and to stabilise inflation at low levels. The recent monetary policy stance adopted by the Bank for this year, outlines our current position, adopting a moderately accommodative monetary policy.

## **The Road Ahead**

Let me return to the theme of my presentation I noted earlier.

The road behind us was a perilous one; but we have followed it and emerged on the other side, bruised but far from beaten. So now we look to our future and find ourselves at the start of a new journey. And we need a new Captain and crew to lead us on our journey. This journey could take us down a number of paths and it is up to us to pick the right path. This year is a year of choices. The decision we take now will affect the route ahead and will shape our shared future. So the choices we make this year are very important and critical indeed.

The most obvious choice ahead for the people of Solomon Islands is the choice of our elected leaders. With the important choices and challenges ahead, when we go to the polls, it is vital we select the right men and women to lead this country forward.

The people of this country need and deserve leaders of integrity, courage and vision. Those new leaders chosen by the people must live up to expectations and repay the trust the people have placed in them. They must not fall into the traps of corruption and self service.

Economically, the storm of last year has eased. The Bank is predicting 5% growth in 2010. This prediction is based on strong growth from our non-logging commodity sector, the construction industry, fisheries and telecommunications.

There are however many threats to this projection. Positive shocks to this 5% growth could be provided by a greater resilience from the forestry sector than currently forecast. Downside risks to this forecast are a weaker than anticipated recovery for the global economy, or a return to high and unstable rates of inflation.

The medium to longer term outlook is also very uncertain. It is now that we must turn to face the future. We must confront our long term challenges, we must now choose the path for the future.

Our logging industry, for so long the crutch that has supported our economy, is in terminal decline. We must now find new sources of growth, We must look to the business leaders and entrepreneurs of this nation, as well as our political leaders, to lead us down a new path to growth.

In the process of making these choices, I think it is very important to get what I call the 'basics' right. These may seem unimportant but these are the foundations from which a successful economy can grow and prosper. Education is vital. We have a large and growing young population, and whilst we can not necessarily shape a future for our children, we can shape our children for the future. Education, and by this I do not just

mean academia but also equipping the next generation with relevant skills needed by our country such as mechanics, electricians, plumbers... Education is vital for our growth.

The basic utilities, water and electricity, must be improved. Neither rolling blackouts nor water problems are helpful to businesses, nor are they desirable for anyone. Imagine coming to work in the morning or going to bed at night without having a shower. It affects productivity at work. And when you return home, the clothes and plates and spoons are not washed because there is no water. And there was power outage during the day and the food in the fridge had gone bad so we have to buy new supplies for the week. These are not new issues and we experience them every day. But they have an economic dimension so we need to fix these problems.

Communications is another area that needs improvement, but also one in which improvements are occurring at some pace. 2009 saw pleasing developments in this sector and I hope 2010 will bring more. Then you won't have to listen to that irritating recorded message. "**subscriber cannot be connected at the moment**" on our mobile phones.

The list of basic institutions that we must sort goes on and on... The road network must be extended and crucially maintained. Inter-islands transport, in particular shipping, must be improved to spread growth throughout the islands, in this we hope the franchise shipping scheme will yield some benefits to people in isolated areas. Land rights must be improved to benefit communities around these islands. The list goes on and on...

But it is not just the institutions that must develop, we all have a role to play in pushing the country forward. From the agricultural sector we look to our coffee growers, our vanilla growers, our cocoa and honey producers, our copra farmers and our fishermen to drive our country forward. Though still small at this stage, these commodities are becoming important sources of income in rural communities.

Tourism presents us with an exciting opportunity to improve the living standards of our people. This path to growth however needs us all to work together. Growth will come not just through the building of hotels and improvements in airlines, not just through the running of boat trips and maintenance of attractions, but everyone working together. We must stop the throwing of rubbish in the streets, we must treat visitors with the kindness and friendliness that comes so naturally to our people. Our taxi and bus drivers must look presentable and charge reasonable fees. We must take pride in our country so that visitors can enjoy their time in our country.

The mining sector is another that will play a huge role in the years to come. We must ensure that the rents from our natural resources are used wisely and fairly to benefit all peoples of this nation and leave an enduring legacy for our children and theirs.

These are important choices and we have to make them now.

## **CBSI Operations**

Finally let me turn to the operations of the Central Bank in 2009.

Last year, the two objectives of the Bank's monetary policy stance, was to tackle inflation and to defend the foreign reserves of the country. I am pleased to report that both objectives have been met last year. Inflation has fallen, largely due to external factors but

we believe our monetary policy actions have contributed to low inflation. And our foreign reserves have grown in 2009 and are now around 6 months of import cover. So in terms of monetary policy we have achieved our objectives for 2009.

But against these successes, there were also disappointments. The Bank made a huge loss last year, largely due to recent changes in international requirements for the accounting treatment of the cost of printing notes and minting coins.

The global economic meltdown also severely impacted on the financial outcome of the Bank in 2009. Income earned from the Bank's overseas investment of reserves fell to \$14 million from \$39 million in 2008. On the other hand, operational expenses in 2009 rose by 64% to \$74.0 million. Of this, \$46.2 million (62%) represents the cost of printing and minting of currency notes and coins in 2009 and 2008. In previous years the cost of printing and minting of notes and coins were amortized over a period of time, however due to a change in accounting treatment under IFRS requirements, the full cost have been expensed in 2009 when currency consignments were received.

## **Conclusion**

Ladies and gentlemen, to conclude, let me return to the analogy of the boat I made in my opening remarks. We have emerged from the storm, bruised and battered but we have survived. And we have a lot of work to do to continue on our journey.

We need urgent repairs, a new Captain and fresh lot of crew. We have a role to play in the selection of the new team. We are all on the selection/recruitment panel and we do that when we cast our vote in few months time.

At that point in time we are making a choice. And it is important that we make the right choice. Because the future of our country and the future of our children and their children depend on the choice we make now.

Finally, let me end by acknowledging various institutions and people that have contributed to the production of the 2009 Annual Report. The Office of the Auditor General and our External Auditors, Deloitte of PNG for finalizing our accounts and my thanks to the financial institutions; government departments, statutory authorities, donors, non-governmental organizations, private sector and others, who have kindly provided both information for this report and time for our regular consultations with you. The analysis, interpretation and of course any errors remain our responsibility. I also acknowledge the invaluable advice and guidance by the CBSI Board Directors and my staff, who have untiringly worked on the report over the last several weeks.

With these few remarks, ladies and gentlemen, I have the pleasure in formally launching the 2009 CBSI Annual Report.

Thank you for listening and May **God Bless Solomon Islands**.

13<sup>th</sup> May 2010