



VISION, MISSION, AND VALUE STATEMENTS

VISION

Solomon Islands to be amongst the top 4 low inflation and financially stable countries in the South Pacific region.

MISSION

Our mission is defined by Section 8 of the Central Bank of Solomon Islands Act 2012 in the following priorities:

- To achieve and maintain domestic price stability;
- To foster and maintain a stable financial system and
- To support the general economic policies of the Government.

VALUE

We are committed to uphold the following values:

- To provide quality economic analysis and assessment of the Solomon Islands economy to enable our stakeholders to make informed business judgements and decisions;
- To discharge our duties with integrity and honesty;
- To show excellence and professionalism in our work;
- To act with impartiality in the application of our decisions within the boundaries of the CBSI Act or any other laws we administer; and
- To exercise frugality in the management of the resources under our stewardship.

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24 April 2017

Hon. Snyder Rini, MP
Minister of Finance & Treasury
Ministry of Finance and Treasury
P O Box 26,
Honiara

Dear Minister,

Re: 2016 CBSI Annual Report

In line with Section 58(2) of the Central Bank of Solomon Islands (CBSI) Act 2012, I submit to you the 2016 CBSI Annual Report, along with the Audited Financial Statements.

Yours sincerely,



Denton Rarawa
Governor



GOVERNOR'S FOREWORD



The Governor, Denton Rarawa

40-years history of the Bank was the highlight of the presentations.

The second event was an open day that involved school children from six primary schools in Honiara adopted by the three commercial banks in the country. The children participated in various financial education and awareness activities such as speech competitions, quizzes, songs and dances. During the day, the children and members of the public visited the Central Bank and Ministry of Finance buildings as part of the awareness program.

Despite attaining 40 years of existence, the Bank's financial situation deteriorated in 2016. The Bank recorded a loss of \$42 million in 2016, largely wiping out the \$44 million profit recorded in 2015. This emanated from a \$66 million loss in foreign exchange revaluation. Excluding this amount, the Bank made an operational profit of \$24 million. The major exchange rate losses came from pound sterling in the aftermath of BREXIT. This led to a further deterioration in the Bank's balance sheet to a net liability position of \$11 million in 2016 from a net asset of \$13 million in the previous year.

The Central Bank's monetary policy stance in 2016 remained accommodative, aimed largely at maintaining price stability and enhancing financial deepening by addressing excess liquidity in the financial system.

Two former Directors returned to the Board in 2016. Businessmen, David Quan and Leslie Teama replaced outgoing Directors Lilly Lomulo and Loyley Ngira who completed their terms on

The Central Bank of Solomon Islands (CBSI) celebrated its 40th anniversary in June 2016, a major milestone in the history of the Bank.

The occasion was marked by two public events. The first was a public seminar where several prominent speakers including a former governor presented speeches on topics of national interest. A short video clip documenting the

the Board during the year.

Two vacant positions remain on the Board and hopefully both will be filled soon. At the same time three female managers left the Bank threatening the gender equality efforts especially in management positions in the Bank.

In terms of the performance of the Solomon Islands economy, 2016 had been a positive year. Economic output grew by an estimated 3.5% in 2016, the eighth consecutive growth in the economy since the global financial crisis. The increase in output was driven largely by growth in the forestry, agriculture, and services sectors. Favourable commodity prices and investment in infrastructure during the year also contributed to the growth in output.

Other macro indicators were also positive during the year. Inflation was at negative 2.8% at year-end, aided by lower food and energy prices, the foreign reserves were over 10 months of import cover, public debt remained low, while growths in money supply and private sector credit were up 13% and 12% respectively during the year.

The fiscal outturn in 2016 recorded a deficit equivalent to 5% of GDP. This came about as a result of lower performances across all revenue streams. Total revenue declined by 11% while expenditure, on the other hand, increased by 4% year-on-year.

BRED bank applied for a banking license in 2016. The Board considered the application and endorsed an interim license to allow BRED set up its operations in the country. The interim license will expire in May 2017 after which



Members of the CBSI Board Director waiting to board their plane after their meeting at Kirakira, Makira Ulawa Province in 1987. From L to R; Nestor, Late Solomon Ilala, Snyder Rini, Joseph Huta, Joses Tuhauku, Late John Rofeta and Tony Hughes. Missing are Late Mr. Kinika and Late Mr. Kelesi. CBSI celebrated its 40th Anniversary in June 21, 2016 and honoured the past members for their valuable contributions as board directors towards the development of central banking in Solomon Islands.

BRED can apply for a full banking license which can be considered for approval.

Outlook for 2017

The domestic economy is projected to grow at an average of 3.4% over the short to medium term. This expectation hinges on the assumptions that the fiscal expansion plans of the government continue over the medium term, pipeline infrastructure projects are progressing on schedule, donor support continues, and non-logging sectors expands to cushion any surprise declines from the logging sector. There are however, downside risks such as anticipated increases in energy prices, commodity price volatilities, and significant decline in logging output that could derail the projection.

Public debt is expected to rise in 2017 as the Government borrows to finance key projects like the Tina river hydro scheme and the submarine cable.

The expected RAMSI exit in June 2017, would have minimal impact on the economy because RAMSI's operations

are largely insulated from the domestic economy. At the same time, it is expected that most remaining RAMSI activities would be absorbed into existing bilateral arrangements with Australia and New Zealand.

I would like to thank the CBSI Board of Directors for their support, guidance and advice on policy matters throughout the year. Let me also thank all the many government agencies, state owned enterprises and private sector companies who provided the information used in this report. The analysis and interpretation of the data, of course is entirely the responsibility of the Bank.

Lastly, but certainly not the least, let me thank all my staff for all their contribution to the Bank during 2016. Without their support the Bank would not have come out of a very challenging year. I want to specially thank those staff involved in the compilation and production of this report for 2016.

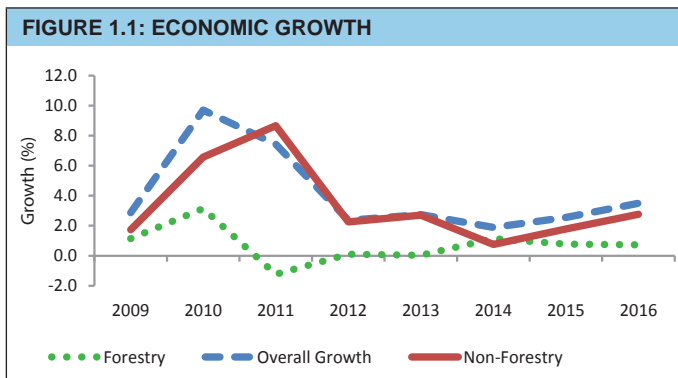
Thank you all.



Denton Rarawa
Governor

CHAPTER 1: OVERVIEW OF ECONOMIC DEVELOPMENTS IN 2016

The domestic economy is estimated to have grown by 3.5% in 2016, exceeding expectations for the year and was higher than the growth in 2015. This outcome was due to a sharp increase in logging activities, buoyant private sector activities fuelled by credit growth, fiscal stimulus particularly in building infrastructures, and favourable commodity prices. The external sector recorded a slight improvement against the previous year. Monetary aggregates continued to expand during the year, as a result of credit growth and fiscal injections combined with external inflows. The government recorded a fiscal deficit in 2016 on the back of high expenditure outlays as against a weaker than expected revenue performance.



Source: NSO & CBSI

INTERNATIONAL ECONOMY

According to the IMF World Economic Outlook in Jan 2017, the global economy was estimated to have grown by 3.1% in 2016 following the 3.2% growth in 2015. The overall growth benefited from positive developments both in the advanced economies category and emerging market and developing economies category. During 2016, world trade volumes expanded at the same pace as in the previous year at 2.6%.

The advanced economies grew by 1.6% in 2016 following a 2.1% growth a year ago. During the year, the US economy expanded by 1.6% following a strong rebound in economic activities in the second half of 2016. The euro area grew by 1.7% on the back of stronger than anticipated growth in Germany, France and Spain. United Kingdom performed higher than expected as demand continued to remain strong after the Brexit vote. Japan benefited from its accommodative monetary policy and exceeded expectations with a growth of 0.9%.

Growth in emerging market and developing economies stabilised at 4.1% as in 2015. The stable growth masked diverging growth in this country group. The Chinese economy was boosted by policy stimulus and remained as the major driver in this group with a growth of 6.7%. The other major drivers were India and ASEAN-5 economies, which recorded positive growths of 6.6% and 4.8% respectively.

The Australian and New Zealand economies, two of Solomon Islands closest trading partners, posted growths of 1.8% and 3.5% respectively in 2016. The growth in the former had been revised downward due to weaker than anticipated outcomes in the construction and mineral sectors. In contrast, growth for New Zealand was sustainably high on the back of positive demographic shifts, ongoing construction activities, tourism and an accommodative monetary policy.

The IMF projects the global economy to rise steadily in the medium term by 3.4% in 2017 and 3.6% in 2018. This resembles expectations that growths in the two major country groups (advanced economies, and emerging market and developing economies) would continue to rise in the next two years to respective growths of 2.0% and 4.8% by 2018. Policy stimulus in the US and Chinese economies are key considerations behind the medium term optimism. While the uptick in energy prices may harm oil importing countries, oil exporting countries have benefited so far and expected to contribute positively to overall growth.

Global inflation is expected to rise moderately in the medium term but still within policy targets. Inflation in the advanced economies is forecast to pick up from 0.7% in 2016 to 1.7% in 2017 and 1.9% in 2018. Inflation in emerging market and developing economies is expected to sustain at 4.5% in 2017 as in 2016 before easing marginally in 2018 to 4.4%. Inflation projections for Australia and New Zealand are envisaged to go up as well in 2017 to 2.1% and 1.6% respectively.

DOMESTIC ECONOMY

CBSI estimates showed that the domestic economy was more buoyant in 2016 than in 2015. Real GDP grew by 3.5% in 2016 as a result of a 3.3% growth in the primary sector combined with a 4.2% growth in the services sector. While mining and fishing activities remained subdued as in the previous year, overall economic activity was under-



SIPA's new \$190 million wharf was officially opened on 10th October, 2016. This Japan funded project will boost Solomon Islands international trade in goods. [Photo supplied by Solomon Star]



Solomon Sapphire is a new addition to NFD fishing fleet. The vessel is expected to commence fishing in 2017 in the international water outside of Solomon Islands EEZ and will increase the raw material supplied to the SolTuna Limited for fish processing and canning factory. Photo supplied by NFD/Cynthia Wickham.

pinned by forestry, agriculture, construction, manufacturing, transport, communication, and most service sectors. Donor support was also a major contributor to growth through the donor funded capital projects that were built across the country.

Labour market condition indicators showed slight improvements in 2016. Data from the Solomon Islands National Provident Fund (SINPF) pointed to a 1% year-on-year increase in the average number of contributors to 55,820 in 2016. The public sector workforce also trended upward with an annual growth of 3%. The continuation of donor supported initiatives such as the seasonal workers program and rapid employment program provided alternative jobs, though temporary, to locals.

The performance of the major commodities generally improved in 2016. The CBSI average annual production index reversed the downward trend in 2015 and increased 11% to 91 points. This reflected increase in round log volumes coupled with improved output from agricultural commodities. On a downside though, fisheries sector was low with fish catches below expectation. Fiscal revenue earned from international boats access fees fishing within the country's 200 Economic Exclusive Zone declined on a year to year basis.

Extraction of natural logs increased further in 2016 with exported log volumes rising by 17.4% year-on-year to 2,292 million cubic meters. The growth was attributed to re-entry into previously logged areas, clear felling for large projects such as bauxite mining, and increased volumes from plantation logs. The agriculture sector was also buoyant, owing largely to increases in palm oil output and to a lesser extent in copra and coconut oil. However, fisheries activities remained subdued.

The balance of payments (BOP) position although positive

in 2016 at \$77 million contracted from \$406 million a year ago. The lower year-on-year outturn came on the back of a current account deficit that worsened to \$426 million and a reduction in the positive capital and financial account position to \$581 million. On the current account, the sharp turnaround in net merchandise exports to positive position this year was outweighed by large deficits in services and primary income. Gross foreign reserves position of the country at end of year was \$4,402 million (excluding IMF subscription to \$4,210¹ million) and was adequate to cover 10.8 months of imports.

The exchange rate basket index² weakened slightly during the year by 30 basis points to 107.9. The bilateral exchange rate developments indicated that the Solomon Islands dollar (SBD) depreciated against the USD by 0.4% to \$7.95, driven by weakening local dollar towards year-end. However, the SBD gained against the Australian dollar (AUD), Great Britain pound, and New Zealand dollar.

Money supply rose steadily during the year by 14% to \$4,742 million, reflecting increased credit to private sector, external inflows and the withdrawal of government deposits. Excess liquidity rose, though at a slower pace than the previous year, by 18% to \$1,330 million. Credit growth slowed down by 5 percentage points to 12% to a stock of \$2,192 million by end year. The major drivers behind credit in 2016 were construction, personal, distribution, tourism, and forestry.

The government recorded fiscal deficit in 2016 at around 5% of GDP than a year ago. The negative outcome was consistent with the fiscal expansionary plans of the government. At the same time, revenue performance was weaker than the preceding year and even against budget.

1 This BOP reserve figure excludes the IMF subscription of \$192m, in accordance with the IMF's BPM6 definitions.
2 The basket is a trade weighted index to 100 with a base year of 2012.

Expenditure on the other hand exceeded the previous year by 4% to \$4,270 million. Meanwhile, the government debt stock increased to \$692.4 million during the year due to drawdowns of its loans from ADB and IDA.

Headline inflation further fell from 2.9% a year ago to minus 2.8% in December 2016. The fall matched the downward movements in both the imported and domestic components indices to minus 4.6% and 1.8% respectively. The deflation was driven by low food and energy prices. Core inflation also trended downward to minus 2.2% from 3.7% in December 2015. This implies a general decline across all non-food and non-energy items in the consumption basket.

ECONOMIC OUTLOOK

The CBSI projects the domestic economy to sustain growth at 3.6% in 2017. The positive assumptions were that logging sector would remain flat, non-logging sector continues to thrive on the back of projected increases in output and commodity prices, credit to private sectors to grow at trend rate, and fiscal expansion program is implemented as planned.

The balance of payments position is forecasted to moderate in the medium term. The current account deficit is anticipated to widen further as imports particularly for capital goods rises over the medium term. The deterioration is associated mainly with the assumption that energy prices trends up further together with planned implementation of large infrastructure and FDI projects in the medium term. With capital inflows expected to rise, the gross foreign reserves position of the country is forecast to remain high.

Inflation rate is ticking upward in early 2017 though still remaining below zero. While rising energy prices in late 2016 and in early 2017 are expected to continue and drive short term inflationary pressures, more imminent pres-



Construction work underway at Mataniko bridge, Central Honiara, will relieve the traffic chaos and reduce cost of doing business in the capital.

ures are seen coming from the domestic index. Over the medium term, inflation is expected to remain within the 3% - 5% range.

According to the 2017 Budget Outlook, the government projects another expansionary budget in 2017 with expenditure expected to rise to \$4,087 million against budgeted revenue of \$3,909 million. Of the total expenditure, capital outlay accounted for 29% while recurrent outlay 71%. As in previous years, the government is expecting sector budget support from donor partners. Revenue performance and budget support receipts from donors are critical funding mix for the successful execution of the 2017 budget. Like previous years, the government's priority focus remains on infrastructures and rural development.

However, there are risks to the medium term growth projections. Downside risks include higher than anticipated increase in energy prices which can drive production costs upward, and lead to a further deterioration in the country's trade position. A larger than expected financing gap in the 2017 budget due to revenue shortfalls can also have dampening effects on growth projection.

CHAPTER 2: GOVERNANCE AND ORGANISATION

CORPORATE GOVERNANCE

The governance and the organization of the CBSI are vested in the Board of Directors that are appointed under Sections 38 and 41 of the CBSI Act 2012. Board members are:

- (a) The Governor, as the chairperson
- (b) Deputy Governor;
- (c) The Permanent Secretary, Ministry of Finance & Treasury; and
- (d) Six non-executive directors.

The Board of Directors are charged with the formulation and supervision of the implementation of the CBSI policies; and supervision of the administration and operations of the Bank.

Directors for 2016 are Mr. Denton Rarawa, Governor and Chairperson; Mr. Gane Simbe, Deputy Governor and deputy Chairperson; the Permanent Secretary of the Ministry of Finance & Treasury (MoFT) Mr. Harry Kuma (ex-officio director). The six non-executive directors are Ms. Lilly Lomulo and Mr. Loyley Ngira, whose terms expired on 5th February 2016; and Mrs. Tele Bartlett and Mr. Primo Afeau who had their terms expired on 15th July 2016. Mr. John Usuramo and Sir Thomas Chan are serving current terms whilst Mr. David Quan and Mr. Leslie Teama filled in the two vacant board positions by year-end.

Board Meetings

The Board met eight (8) times during the year, two (2) more than the minimum of six (6) meetings required under the CBSI Act. There was no provincial meeting held in 2016.

Directors Name	Number of Meetings attended
Denton Rarawa	8 (out of 8)
Gane Simbe	7 (out of 7)
Harry Kuma	7 (out of 8)
John Usuramo	6 (out of 8)
Primo Afeau	3 (out of 3)
Sir Thomas Chan	2 (out of 8)
Mrs. Tele Bartlett	3 (out of 3)
David Quan	2 (out of 2)
Leslie Teama	1 (out of 2)

Board Businesses

In 2016 a total of 40 Board papers were submitted for Board deliberation, six (6) more than in 2015. Of the total, 19 papers were quarterly progress reports for noting; and 21 were policy papers for Board decisions. These policy papers included two bi-annual Monetary Policy Statements, the 2015 Annual Report and the 2015 Audited Financial Accounts, Investment Guideline for SINPF and

Credit Union, Fitness and Propriety Regulation regarding on Application to Establish Financial Institution, Rules of Procedures for Board, New \$20 Note, Compliance Policy, BRED Vanuatu Bank application, Amendment to staff Loan Policy, Empire Solomon's Bank application and the 2017 Business Plan and Budget.

Board Committees

There are three Committees that were set up to assist with the governance and management of the Bank. The Committees are; the Board Audit Committee, the Board Staff Remuneration Committee and the Board Disciplinary Appeal Committee.

Board Audit Committee

The Board Audit Committee was established at the end of 2010. The Committee has four members; three non-executive Directors, the Deputy Governor and the Manager of Internal Audit Unit who is Secretary to the Committee. One of the Non-Executive Directors is appointed by the committee members as the Chairperson of the Committee. The Chairman of the Board Audit Committee reports to the Board after each meeting. No meeting was held by the Board Audit Committee in 2016. The reason for this was because delay in the appointments of non-executive directors who are required to serve as chairperson and members to the Committee and therefor putting at risk the independent checks and balance for good governance practice. The Board Audit Committee provided feedback to the IMF on matters required to ensure the Bank meets the IMF Safeguard Assessment standards.

Board Staff Remuneration Committee

The Board Remuneration Committee was established in 2012 to consider and determine all aspects of the remuneration of Bank employees. The Committee is chaired by a non-executive Director, with two other non-executive Directors as members. The CBSI Legal & Compliance Officer is the Secretary to the Committee. No meetings were held in 2016.

Board Disciplinary Appeal Committee

The Board Disciplinary Appeal Committee (BDAC) is set up to review appeals by staff against any disciplinary actions that the Disciplinary Committee of the Bank may take against a staff. There are five members to the BDAC consisting of the Governor as the Chairman, one non-executive Board Director, two chief managers appointed by the Chair, one of whom must be from the department from which the staff is the subject of disciplinary action, and a member of the Staff Association. The Legal Officer and the Chief Manager of Human Resources & Corporate Services department are in attendance at meetings. There were no meetings held in 2016.

CENTRAL BANK OF SOLOMON ISLANDS BOARD OF DIRECTORS



DENTON RARAWA

Governor and Chairman of the Board

- Governor since August 2008;
- Chairman, Solomon Airlines Ltd;
- Chairman, National Financial Inclusion Taskforce (NFIT);
- Deputy Chairman, Solomon Islands Anti-Money Laundering Commission (AMLC);
- Vice Chairman, Solomon Islands National Trade & Development Council (NTDC);
- Vice Chairman, Alliance for Financial Inclusion (AFI) Committee on AFI Independence;
- Vice Chairman, Solomon Islands Football Federation (SIFF) Telekom S-League Board;
- Director, Investment Corporation of Solomon Islands (ICSI);

Previous positions held:

- Deputy Governor, CBSI;
- Chairman, Economic Association of Solomon Islands (EASI);
- Director, Solomon Islands Plantations Ltd (SIPL);
- Director, Solomon Printers Ltd (SPL)
- Director, Foreign Investment Board (FIB)



GANE SIMBE

Deputy Governor

- Appointed Deputy Governor, 18th September, 2008
- Member, CBSI Board Audit Committee
- Current Chairman, Pacific Islands Working Group on Financial Inclusion
- Director, SolTuna Limited

Previously held position:

- Manager Financial Institutions Department; CBSI;
- Manager Exchange Control (International Department), CBSI
- Assistant Manager, Currency & Banking Operations; CBSI
- Manager Administration, Solrice Limited



LESLIE TEAMA

Private Businessman

- Accountant - Ministry of Home Affairs and Provincial Government (Old Structure just after SI attained Independence)
- Treasurer and Head of Finance - Central Islands Provincial Government
- General Manager & CEO SINPF, 1989 to end of 1999 {10 years}
- Permanent Secretary, Ministry, of Finance, up until my retirement from public duties and formal employment in 2003
- Director - Mendana Hotel Limited, under the old Government shareholding Agency (GSA) ownership structure
- Director - National Bank of Solomon Islands (NBSI)
- Director - Bank of Hawaii (SI) Limited
- Director - Board Member SINPF
- Director - Board Member CBSI
- Director - Board member SOLTAL
- Director and Chairman of Board - Home Finance Corporation Limited



HARRY KUMA

Permanent Secretary - Ministry of Finance and Treasury

Previous positions held:

- Under Secretary - Ministry of Finance and Treasury
- Board Chairman - Solomon Telekom Company LTD



DAVID K.C. QUAN, MBE., MAICD., AFAM.

Chairman Solomon Islands Electricity Authority Board member

- Solomon Islands Chamber of Commerce & Industry
- Chairman -Solomon Islands Chinese Association
- Member - Rotary Club of Honiara
- Managing Director - Quan Chee Corporation Limited

PAST INVOLVEMENTS

- Managing Director -AVIS Solomon Islands
- Member -University of the South Pacific
- Solomon Islands Centre Advisory Committee
- Acting Chairman and Vice-chairman -Solomon Airlines Limited
- Chairman -Solomon Islands Chamber of Commerce & Industry



PRIMO AFEAU

Private Legal Practitioner

- Director, Solomon Airlines
- Trustee, Honiara Golf Club
- Chair, Committee of Prerogative of Mercy

Previously positions held:

- Attorney General of Solomon Islands
- Chairman, Anti-Money Laundering Commission
- Director, Transparency Solomon Islands



TELE BARTLETT

Managing Director, Liberty Holdings

- Board Member, Women in Business Association

Previous positions held:

- Teacher, Honiara Technical Institute



JOHN USURAMO

Campus Director,
USP Solomon Islands Campus

Previous positions held:

- Group Manager Student Administration Services
- Assistant Registrar, USP
- Personal Officer, SICHE



SIR THOMAS KO CHAN

Private businessman



BELLA SIMIHA

Chief Manager, Human Resource
& Corporate Services
Secretary to the Board since 2009



Governor Rarawa hands over CBSI staff donations to two representatives of the Fijian community in Honiara. This went towards the fundraising efforts to assist the victims of cyclone Winston which damaged parts of Fiji in March 2016

Community Relations

In 2016, the CBSI spent most of its donations budget assisting various community groups including schools, church organizations and sporting bodies as part of its corporate and community relationships.

Organization Structure

The functions of the Bank are organized under seven (7) main departments and three (3) smaller units as shown in the diagram below:

All the departments and units report directly to the Governors' office with support and collaborative efforts to achieving the Banks corporate mission. The exceptions

are the Internal Audit Unit which reports directly to the Board Audit Committee, and the Solomon Islands Financial Intelligent Unit (SIFIU) reporting directly to the Anti-Money Laundering Commission (AMLC) on the operational matters, but indirectly supervised daily under the Governor's office.

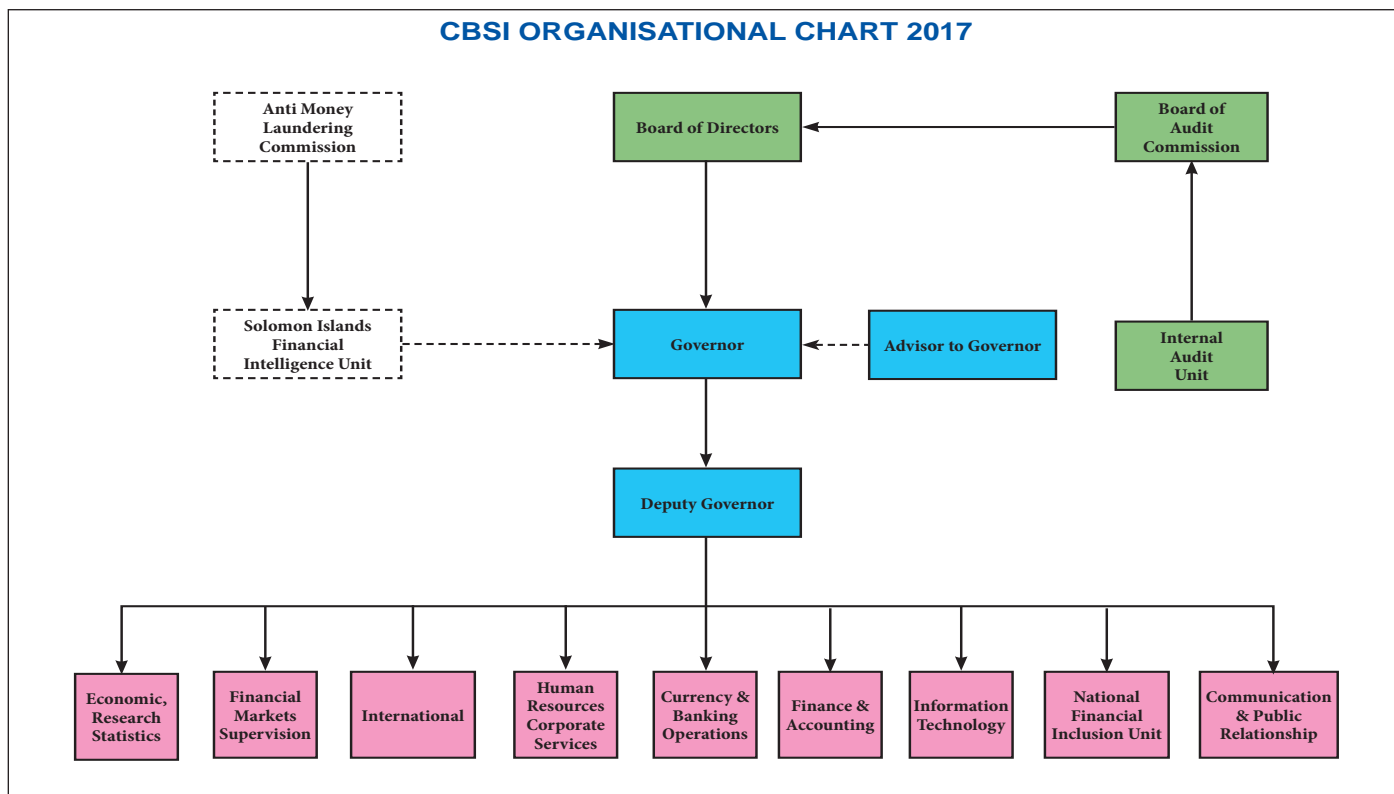
Staff Complement

At the end of 2016, the Bank staff complement totaled to 137 (inclusive of service staff). Around 89% of these positions were filled in 2016 while 11% remain vacant and pending recruitment this year, 2017. During the year, the Bank recruited nine (9) new officers for various positions within the Bank. Three (3) officers were promoted to Managers positions, while 1 officer was transferred to another department and seven officers were placed on job rotation within respective departments.

The management team comprised 16% of the total staff complement. In terms of gender composition, the Bank maintains the balance of 60% male and 40% female. Five (5) out of twenty-two (22) management positions are filled by females. The Bank promotes equal employment opportunity and encourages qualified females to apply when vacant positions are advertised.

Retirement and Resignations

The Bank farewell three (3) of its managers in 2016. Two (2) managers' voluntary took early retirement while one voluntary retired at the end of contract period. One officer got terminated for disciplinary reasons while another passed away after a short illness.





CBSI Staff group photo at their head office, Mud Alley St. At the end of 2016 the bank number of staff total to 137, including service staff.

Staff Training and Development

The Bank continued to encourage the training and development of its staff with continued support towards the learning culture in the bank. Its investment in the quality and caliber of its human capital is valued as a critical input to enhance productivity and boost morale towards achieving the Bank's mandate. As such the Board sets aside an annual training budget towards human capacity development.



CBSI staff prepare their group presentation on the topic "Understanding the CBSI Act 2012" during a workshop held at the Bank's Aruligo Recreational and Conference site in 2016. Understanding the provisions of various legislations that CBSI administers is required to help staff carry their work professionally.

Apart from its own budget, CBSI also received funding support from other bilateral partners particularly the International Monetary Fund (IMF), the Australian Prudential Regulation Authority (APRA), AusAid/DFAT, Alliance for Financial Inclusion (AFI), PFIP/UNDP; Commonwealth Secretariat, Pacific Financial Technical Assistance Centre (PFTAC) and the Asian Development Bank (ADB). These bilateral partners funded technical training for CBSI officers in monetary policy analysis, economic forecasting, banking and financial services supervision, financial inclusion and economic statistics.

Attending, participating and contributing to international conferences and seminar is part of CBSI human resource capital development. During the year the Bank sent 46 staff members overseas to take part in a number of im-

portant central-bank training programs. This excludes the official meetings that are attended by the Governor and the Deputy Governor and other senior staff. A handful of staff also attended important training programs that are offered locally and aimed at broadening knowledge and skills.

The Bank continued to assist staff pursue higher academic qualifications by providing full-time and part-time training sponsorship. Four officers were granted overseas study leave in 2016. Two (2) officers were on full Bank scholarships while two others were on partial sponsorship. Ten (10) other officers were supported to pursue part-time studies at the USP Honiara Campus.



Governor Denton Rarawa, of CBSI joins his fellow South Pacific governors in a panel discussion during the AFI Global Policy Forum held in Denarau Island, Fiji in 2016.

As at the year-end, one (1) officer graduated with a Bachelor of Commerce Degree, majoring in Management and Public Administration and International Business Marketing.

The Bank also supports the on-going learning culture within the Bank through on-the-job training by supervisors and managers, job rotation, online and distance correspondences, and the in-house trainings. Of the eight (8) scheduled in-house trainings conducted in 2016, an average of 27 participants attended each training.

CENTRAL BANK OF SOLOMON ISLANDS MANAGEMENT 2016

GOVERNORS OFFICE



DENTON RARAWA
Governor



GANE SIMBE
Deputy Governor



DR LUKE FORAU
Advisor to the Governor

CURRENCY & BANKING OPERATIONS DEPARTMENT



DANIEL HARIDI
Chief Manager



JOE VASUNI
Manager

INTERNATIONAL DEPARTMENT



ALI HOMELE
Chief Manager



DENSON DENNI
Manager



MICHAEL KIKIOLU
Chief Manager

ECONOMIC RESEARCH & STATISTICS DEPT.



ELIZABETH RAGIMANA
Manager (Till Sept, 2016)



DONALD KIRIAU
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NATIONAL FINANCIAL INCLUSION UNIT



CAROLINE KANOKO
Manager

HUMAN RESOURCE & CORPORATE SERVICES DEPARTMENT



BELLA SIMIHA
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ROSE SULU
Manager/ Human Resources



JOHN BOSCO
Manager/ Corporate Services

INFORMATION & TECHNOLOGY DEPARTMENT



EDWARD MANEDIKA
Chief Manager



MARLON HOUKARAWA
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JIMMY SENDERSLY
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FINANCIAL MARKET SUPERVISION DEPT.



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TREVOR MANEMAHAGA
Manager (Research)



LINDA FOLIA
Manager (Supervision)

FINANCE & ACCOUNTS DEPT.



EMMANUEL GELA
Chief Manager



SIMON RAMOIFAI
Manager

INTERNAL AUDIT UNIT



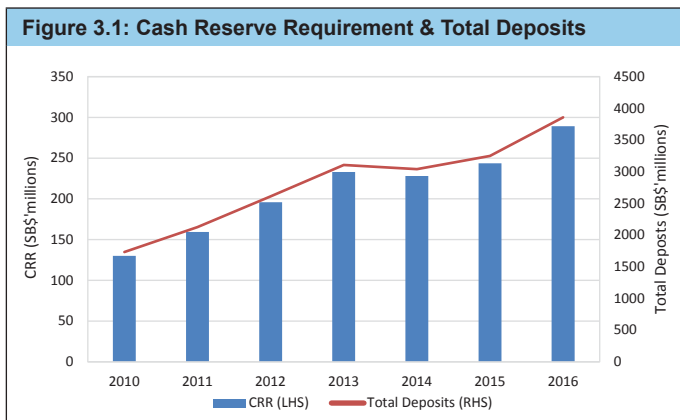
OLIVER KAROA
Manager

CHAPTER 3: MONETARY POLICY DEVELOPMENTS

To achieve its primary objective of price stability, the Central Bank of Solomon Islands monitored monetary policy developments during the course of the year. Its policy direction as set out in the bi-annual Monetary Policy Stance in March and September 2016 was to maintain an accommodative monetary policy stance for the year. This was primarily due to the persistently low inflation over the period and to support the government’s fiscal policy expansion.

In spite of limitations to effective monetary policy implementation due in part to the shallow nature of the country’s financial system, the Bank continued to develop and utilize its monetary policy tools. These have included direct policy instruments such as the cash reserve requirement (CRR), and indirect tools such as the Bokolo and Treasury Bills. In addition, exchange rate management was also an important policy instrument in view of the country’s exposure to external prices and shocks.

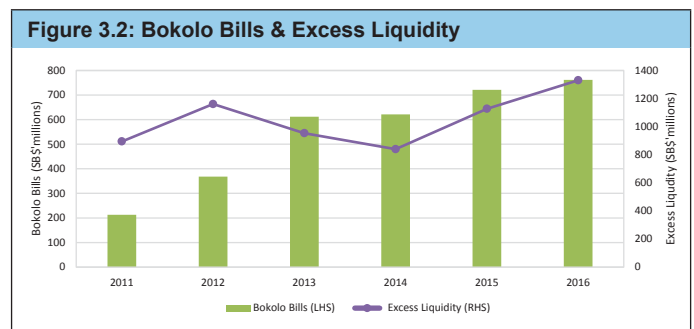
The Bank’s statutory CRR remained at 7.5% of total bank deposits in 2016. At the end of December, this represented \$289 million of deposits being withdrawn from the banking system; a 19% increase compared to the same period in 2015 and in line with the growth in total deposits. Moreover, to encourage lending in the private sector and in a bid to address excess liquidity, the CRR and call account deposits held with CBSI do not earn interest.



Source: CBSI

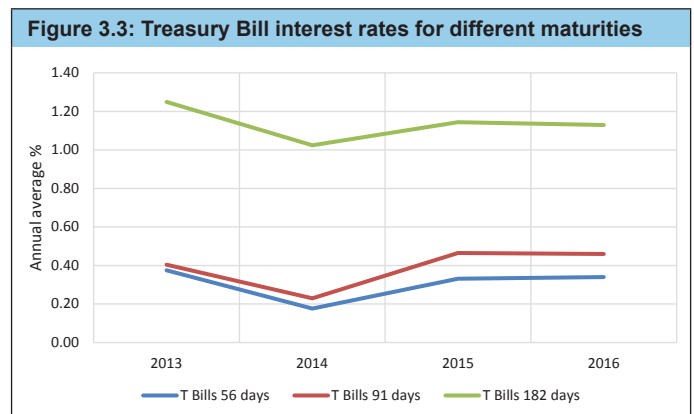
CBSI’s use of its Bokolo Bills to mop up excess liquidity continued to gain traction in the market. During the year, heightened excess liquidity and increased appetite saw the total volume of Bokolo Bills being auctioned rise from \$710 million in the period leading to July 2016 to \$750 million starting August 2016.

Moreover, there was over subscription in the Bokolo Bills auctions with an average \$966 million being bid in 2016 compared to \$707 million in 2015. However, the annual weighted average yield of the Bokolo Bills remained at 0.62% during the year.



Source: CBSI

Meanwhile, the Solomon Islands Government issued Treasury Bills was maintained at a stock of \$40 million in 2016. CBSI administers the Treasury Bill auctions on behalf of the Government, which has utilized it to finance their short-term liquidity requirements. Over-subscription was also evident during the year and was due to the relatively small volume of stock being auctioned. Compared to the previous year, the annual weighted interest rate of the 91-days Treasury Bills remained flat at 0.46%, while the 56-days Treasury bills rose by 10 basis points to 0.34%. The 182-days Treasury bills however declined by 10 basis points to 1.12%.



Source: CBSI

In spite of the various monetary policy instruments used, excess liquidity is still persistently high in the financial system. At end 2016, excess liquidity increased by 18% to \$1,330 million from \$1,127 million at end 2015. This came on the heels of a rise in foreign exchange inflows and fiscal injections by the Government. Nonetheless, CBSI will continue to monitor and review the level of excess liquidity to ensure that this does not trigger excessive inflationary pressures.

The exchange rate plays an important role in the country by facilitating external trade and is also a monetary policy transmission channel for imported prices. Notwithstanding minor operational changes, the Bank maintained its exchange rate policy of pegging the Solomon Islands dollar to an invoice-weighted basket of currencies in 2016.

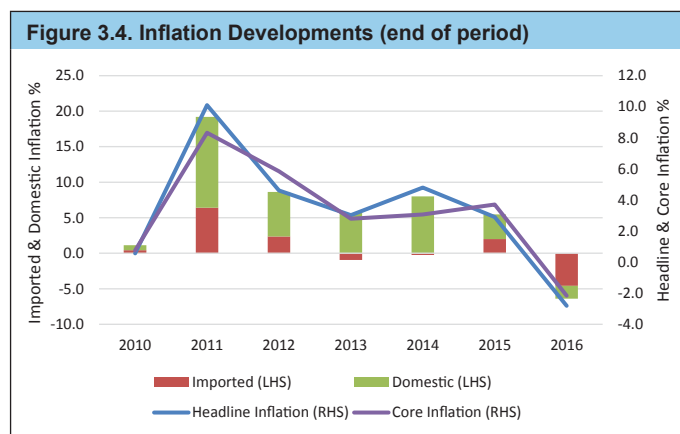
This has proved beneficial in minimizing volatility and fostered confidence in the market. During the year, the SBD depreciated against the Trade Weighted Index (TWI) by 30 basis points to 107.9 and reflected the mixed movements of the SBD against the key currencies. On an annual average basis, the SBD weakened against the United States Dollar but strengthened against the Australian and New Zealand Dollars.



Members of the CBSI Bokolo Bills Working Committee (BBWC) meets each week to decide on winning bids for Bokolo Bills (BB). CBSI issued \$750 million worth of BB to absorb access liquidity as part of its monetary policy

The Solomon Islands witnessed weak consumer prices in 2016. Driven by cheaper fuel and food prices, along with relative appreciation of the SBD against some of the key trading partners, headline inflation reached a deflation

level of minus 2.8% in December 2016, compared to 3.2% in December 2015. The downward pressure reflected the fall in both imported and domestic inflation. Core inflation also contracted implying that the downward move-



Source: CBSI

ment in prices also came from non-food and non-energy items during the year. Looking forward, oil and commodity prices have started to turn around in late 2016 and into early 2017. This would have some upward pressure on prices although within moderate levels for 2017. CBSI will closely monitor inflation price developments and may take necessary measures if required.

CHAPTER 4: CENTRAL BANKING OPERATIONS

ECONOMIC RESEARCH AND STATISTICS

The Economics, Research and Statistics Department (ERSD) comprises of six units namely the balance of payments, monetary, government finance, real sector, research and library. The key functions of the department include but not limited to compilation of macroeconomic statistics, publication of economic reports, formulation of the monetary policy stance and doing research work.

As in previous years, the ERSD conducted industry consultation meetings with most of the key stakeholders in Honiara, Gizo, Noro and Auki over a span of four weeks in January to February 2016. The invaluable responses from the industry consultations were used by CBSI to assess how the economy performed in 2015 and to project the medium term outlook of the country.

The Bank continued to receive Technical Assistance missions in 2016. In August 2016, an IMF/PFTAC sponsored Technical Assistance mission came to review the government finance statistics project. Mission recommendations were implemented but on a gradual basis throughout the year.

Building research capacity among local staff is an ongoing initiative which the Bank is committed to invest some bank resources. The ERSD staff had undertaken research and information papers for presentation at internally organised seminars and monetary policy committee discussions. A total of seven research and information papers were produced in 2016.

In June 2016, the CBSI joined a regional central banks sym-

posium that was organised by the Griffith University to forge collaborative research between the different institutions. The CBSI is committed to this arrangement and will work closely with Griffith University and other regional central banks in 2017.

The ODI fellowship scheme whereby ODI fellows joined CBSI on two years contract mutually came to an end in September 2016. This was after ten years of excellent collaboration between the two agencies. The CBSI is grateful to the ODI scheme for helping to build research capacity of local Bank staff. Nakubyana Mungomba, whose two-years contract lapsed in September 2016, was the latest ODI fellow to serve the CBSI under the scheme. The other ODI fellows before Nakubyana were William Baron, Thomas Coward, Patricia Salmon, and Kenneth Especkermann. The Bank might not be able to ODI again due to changes to the policy of the ODI fellowship body.

A major achievement in the library section was the scanning and archiving of old CBSI reports since 1976. Electronic copies of these old reports can now be accessed from the CBSI website (www.cbsi.com.sb).

COMMUNICATION AND PUBLIC RELATIONSHIPS

A new officer was recruited to support the growing responsibilities of Communication Unit, under the Governors' Office. This was carried out to meet the increasing demand of keeping the general public updated and informed with information about developments in the Solomon Islands economy and the policies of the Bank. As part of its endeavour to ensure timely information is available



Students from Burns Creek and Florence Young primary schools march during the 40th Anniversary and Solomon Money Smart Day, 27 June 2016. Financial education of students as future economic citizens of Solomon Islands, one of the goals of NFIS2.

and accessible to all, the Bank launched its new-look website in June 2016. Among other responsibilities, the new officer is also a full-time web administrator to the bank. In 2016, over 25,000 visits were conducted at the website, and Solomon Islands visitors were the majority from 200 countries that visited the site for information.

The Bank celebrated its 40th Anniversary which fell on 21 June. A conference was organized to mark the occasion with Minister of Finance Honourable Snyder Rini and first governor Mr. Tony Hughes among the main speakers. As part of the 40th Anniversary program, CBSI also hosted its public financial education program, the Money Smart Day. The focus of the second program was on financial education for school children and youth. Adopting the Global Money Week theme, "TAKE PART SAVE SMART" the three commercial banks, namely ANZ, BSP and POB adopted two primary schools each within Honiara, and assisted primary school students and teachers learn about banking services and financial education.

The Bank also participated in two provincial organized festivals in 2016. CBSI uses the opportunity to educate the public about work of Central Bank, proper handling of the currency notes and how to detect counterfeit notes. The festivals attended were the Yam Festival in South Malaita and the Kodili Festival in Isabel.



Group of visitors ask two staff of the Economic, Research & Statistic Department about the work of the department. This was during the CBSI open day which marked the 40th Anniversary celebration on 27th June 2016.

CBSI continued to maintain an on-going presence within mainstream media for coverage and informational purposes. This is part of the Banks' community and public relations agenda which includes the weekly radio program *Money Matters*; broadcast over the Solomon Islands Broadcasting Corporation and the Banks mandatory objective of covering the Solomon Islands economy through the Monthly Economic Bulletins, the Quarterly and Annual Reports and the biannual Monetary Policy Statements, including other operational and financial reports, amongst others. All this information had to be clear and accessible (on-line) to the general public for consumption.

In terms of community publications, CBSI's major general projects included the annual Money Smart Day magazine,

and the departmental pamphlets and brochures that are provided to the public in hard copies and soft copies.

2016 saw an increase in request for CBSI information which also included the publication of economic reports over the stakeholder-based Bloomberg website, mainly for overseas audience.

INTERNATIONAL AND EXCHANGE CONTROL

As part of its mandate the Bank is charged with administration of the Exchange Control Act, facilitating the banks official international payments and receipts on behalf of the government, management and investments of the country's official reserves and undertaking relevant market risk and compliance management researches in the international market for our purpose.

Exchange rate policy and Administration

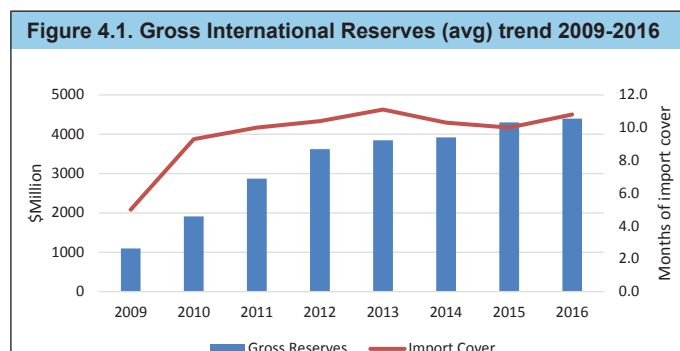
There was little change in the administration and determination of the Exchange rate policy during the year. The Solomon Island dollar is pegged to an invoice-weighted basket of major tradable currencies with minimal interventions. The policy intention is to ensure that our exchange rate policy contributes to domestic price stability and avoids volatility in the Solomon Island dollar and cross rates against major trading currencies.

During the year, the Trade Weighted Basket index appreciated from 107.6 at the start of the year to 107.2 at the end of the year.

In 2016, a slight turnaround in the global exchange rate behaviour resulted in mixed movements of SBD against USD. At the start of the year, the SBD weakened against the USD at an average of SBD8.14 per USD, later in the year it strengthened to around SBD7.90 to SBD8.00 per USD before settling at SBD 8.09 per USD at the end of December 2016. Overall, the local currency depreciated against the US dollar during the year.

Gross Foreign Reserves

The gross external reserves increased from \$4,295.7 million at start of year to \$4,401.8 million at end of year, an increase of 2.5%. The increase comprising mainly of foreign exchange deals in the domestic market between commer-



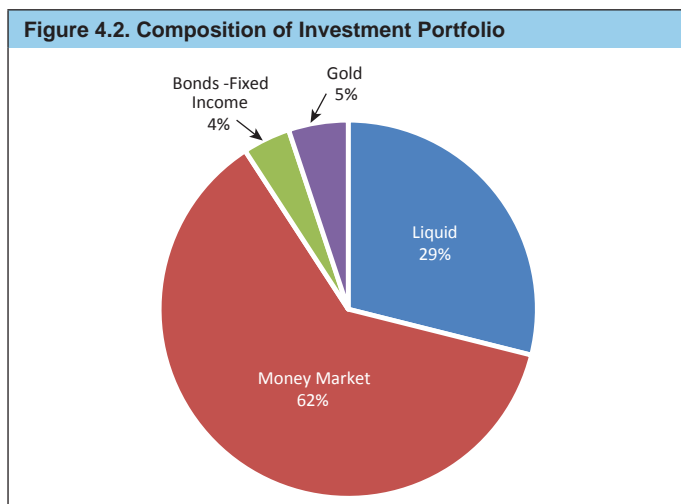
Source: CBSI

cial banks and CBSI more specifically log exports receipts, donor funding, SIG receipts and CBSI receipts. The level of gross reserve is equivalent to 10.6 months of import cover as at end Dec 2016.

Reserve management and Investments

Management of the international reserves is one of the functions of the Bank specified under CBSI act 2012. Section 17 of the CBSI Act 2012 provides that “the Central Bank shall conduct transactions in international reserves and shall manage such reserves consistent with international best practices in order to achieve its primary objectives of maintaining domestic price stability, with respect to its safety, liquidity and yield in that order of priority”.

Management and investment of gross foreign reserves throughout 2016 remained strong and in compliance with CBSI’s investment and reserve management policy guideline. The bank investment policy remained conservative



Source: CBSI

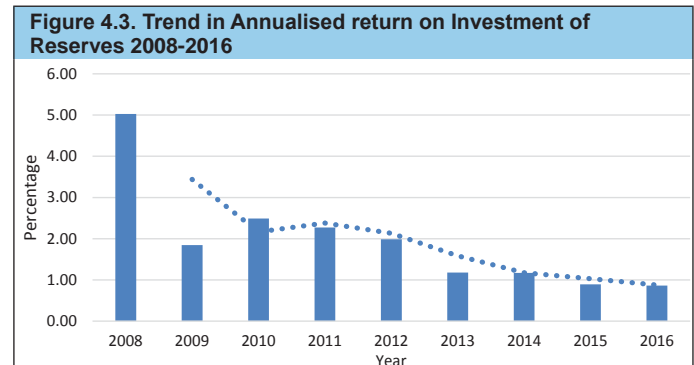
with its investment approaches prioritising safety, liquidity, and yield as paramount determinants of the investment portfolio mix. Figure 4.2. shows the composition of reserves investment portfolio in 2016.

Income from Foreign Reserves Investments

In 2016, uncertainties to global finance remain persistence, which impacted investments outcome. Accommodative monetary policies taken by major advanced economies continued to influence the interest rate market. As a result, deposit rates in the short term money markets and fixed long term instruments remain subdued all throughout 2016, resulting in lower income.

Deposit rates in EURO and JPY have remained negative, forcing the CBSI to recall all maturing deposits and real-locating to other prominent currencies. This exercise was necessary to reduce cost and negative income from both currencies, as a reserve safety objective became the immediate priority.

However, total interest earned on investments was \$41.1 million in 2016, an increase of 3.2% from the previous year. This was mainly driven by earnings from USD short term money market investments and AUD investment in fixed income securities and NCDS during the year.



Source: CBSI

The annualized rate of return measured in terms of interest earnings however, declined in December 2016 to 0.86% from 0.89% of December 2015.

Foreign Exchange Revaluation Gains and Losses

The volatility in the market in terms of exchange rate and interest rate continued to impact the CBSI’s unrealized currency revaluation in terms of Solomon Islands dollar. The Bank is required to hold long position in foreign currency to ensure the availability of the foreign exchange for trade.

In 2016, the Bank mitigated this risk through diversifying of the composition and share of each currency in its portfolio. However, the impact of Brexit and US election resulted in net unrealized loss of \$66.3 million due to losses on AUD and GBP revaluation (\$70 million in total) which the gains in other currencies were not sufficient to offset.

Mechanisms were put in place to ensure the effective management, control and safety of the reserves. This is reflected in the division of responsibilities within the international department. Three units - the front office, the middle office and the back office - handle the day-to-day management and investment of foreign reserves.

Middle Office Operations

The Middle Office main roles and responsibilities include identifying, analyzing and monitoring financial market risks, investment risks and operational risks and advise the management to take appropriate course of actions to mitigate these risks. The Middle Office reports directly to the Investment Advisory Committee (IAC) on any breach or non-compliance by the front and back office on rules and requirements stipulated in the approved Investment policy guidelines.

The Middle Office produces its quarterly compliance report on investment policy standards to the reserves management team (front office) and the Investment Advisory

Committee. Daily compliance checks on liquidity and internal controls and processes has also been incorporated lately as key fundamental functions to guide operational processes

The Back Office

The Back Office is responsible for settlements of Payments related to Investments and allocations of the reserves. It also maintains the records of all foreign currency accounts and the standard settlements instructions held by the Bank. It is also responsible to ensure that the accounts are reconciled each month. In addition to the settlement of payments for the Bank, the Back Office also facilitates both receipts and payments using the SWIFT payment transfer system (see Table 4.1) for both clients such as the Solomon Islands Government, commercial Banks and donors.

	2011	2012	2013	2014	2015	2016
Outgoing messages (Received)	1035	940	953	1039	1314	1301
Incoming Messages (sent)			1589	2279	3562	3804

Source: CBSI

In terms of the SWIFT operations, 1,301 outgoing messages were sent through the CBSI SWIFT system in 2016. A slight decrease of messaging. At the same time 3,804 messages were received, up by 9% increased from 2015.

Table 4.2 shows all receipts and payments transactions facilitated through the SWIFT during 2016 with the exception of foreign exchange deal data's between CBSI and the commercial banks. The total value of all receipts and payments transactions facilitated through SWIFT during 2016 recorded a decrease in receipts amounting to \$1,229 million. In terms of payments, a total of \$120 million was transacted during the year.

	2011	2012	2013	2014	2015	2016
CBSI Receipts/fx deals (\$M)	583.6	601.4	548.5	581.15	2329.6	1229.9
CBSI Payments/fx deals (\$M)	242.6	223.0	248.3	204.16	296.8	120.00

Source: CBSI

Exchange Control Administration

CBSI administers the Exchange Control Act and Regulations on behalf of the Government. The Exchange Control Act empowers the Bank to make regulations to confer powers, and impose duties and restrictions, in relation to foreign exchange, foreign exchange resources, and the protection of currency or public credit or revenue. The

primary goal for exchange control is to ensure that the country benefits from its resources and that all proceeds of goods and services exported are remitted back to the country.

Commercial banks are appointed authorised dealers under the Exchange Control Act and can process and facilitate trade transaction as per the specific requirements of the exchange control policy and regulation. All the three commercial banks in the country are appointed authorised dealers, they are ANZ Bank, Bank South Pacific and Pan Oceanic Bank.

Applications for Temporary Resident (TR) Status

Temporary Residential (TR) status is normally granted to non-residents, who intend to reside in Solomon Islands for a period of four years or less; or Solomon Islanders who are intending to reside overseas permanently. Non-residents working in the country on contractual basis can also be granted Temporary Residents status for Exchange control purposes. Non-residents who are granted temporary residence status are permitted to repatriate income earned in SI or brought in from abroad without limitation. In 2016, CBSI approved 202 temporary resident status permits, of which, 149 were new applicants and 53 were renewals.

	2013	2014	2015	2016
Newly Approved Temporary Resident applications	101	105	125	149
TR Applications Renewals	85	127	85	53
Total TR Approved	186	232	210	202

Source: CBSI

Non-resident Accounts

Individuals and Corporate Entities residing outside Solomon Islands who wish to open and hold bank accounts with a resident authorised dealer (commercial banks) in Solomon Islands requires CBSI approval. In 2016, CBSI approved 3 non-residents accounts, all of which were for corporate entities. There was no approval for individuals and CBSI declined 14 applications on the basis of non-compliance with requirements to open such account.

Foreign Currency Account (FCA) facility

The foreign currency account facility is basically designed to support exporters. However, over the years the Bank recognised the importance to expand the foreign exchange market and thus extended this facility on case by case basis to non-exporters. The operation of FCAs is a privilege and is strictly granted on merit. Individuals do not qualify to this facility for personal use. In 2016, CBSI approved 6 (six) new applications and renewed 13 expired accounts, all domiciled in USD. There was a significant drop in the

reported foreign exchange exposure from SBD1.1132 billion in 2015 to SBD434 million at the end of 2016. This drop was just a statistical bias for non-compliance by account holders to provide data on time and it is not an empirical result. To date there are 78 active foreign currency account holders approved by CBSI of which 75 FCA are held with local banks and 7 FCA held with banks outside the country.

Table 4.4: Number of approved foreign currency accounts held by exporters and non-exporters 2013-2016:

	2013	2014	2015	2016
Account holders/Entities	23	38	44	50
Qualified Exporters	10	10	12	13
Non –Exporters	13	28	32	37
Total number of accounts held	55	63	72	78
On-shore	46	57	65	71
Off-shore	9	6	7	7
Total value: (SBD\$ million)	896	934	1,132	434

Note: Some account holder hold more than one FC Account

Source: CBSI

Foreign exchange (FX) Restricted Classified Dealers

In 2016, the Bank promoted financial deepening by supporting foreign exchange market services expansion in the country. The bank issued 13 classified foreign exchange dealer's license during the year (See Table 4.5). Of the total licenses issued, nine were issued to eligible local companies seeking to operate as providers of Money Changer Services whilst four licenses were Money Transfer Services in the country. This foreign exchange licence is valid for 12 months and renewable thereafter.

Table 4.5: Number of approved Foreign Exchange Money Changer License 2013-2016

	2013	2014	2015	2016
Money Transfer services*	5	4	4	4
Money Changer Services	9	11	11	9
Total FX Classified Dealers	14	15	15	13

*As Western Union and Money Gram Agency and Sub-agents

Source: CBSI

In 2016, no new application was received and all license remained valid except for two money changers licenses that were revoked due to non-performance. Inward remittance receipts through Classified Money transfer agents slightly increased by 6.5% from previous year to SBD53.84 million and outbound remittance increased by 71.7% to SBD272.25 million. In terms of transactions by money changers, a total of SBD19.2 million equivalents of foreign currency notes were purchased and SBD28.08 million sold to the travelling public and commercial banks.

Private Sector Debt (Private Sector Offshore Borrowing)

Resident entities wishing to borrow funds abroad or creating debt in favour of non-residents require the authorization of the CBSI. Authorization by the CBSI is necessary for proper registration and monitoring of private sector debts and also as a prerequisite for any loan repayments in the future.

Of the twelve external loan applications received by CBSI during the year; eleven were authorized while one application was declined for falling short of the prudential requirements. The approved external loans were purposely to finance business expansion. The total foreign currency exposure of the authorized off-shore loans is equivalent to USD17.06 million or equivalent SBD133.3 million.

Table 4.6: number of private sector Overseas Borrowing Approved under Exchange control Requirement: 2012-2015

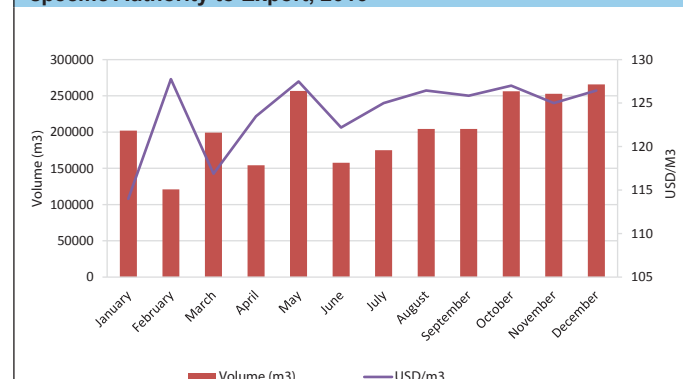
	2013	2014	2015	2016
Applications received & approved	12	14	10	11
Value in SBD(million)	106.8	327.0	216.9	133.3

Source: CBSI

Exports Administrations

The primary objective of export administration is to ensure that the country fully benefits from its resources through export of goods and services. The exchange control regulation requires that exported goods and services receive fair and reasonable market price and that export proceeds are fully remitted back and immediately sold to a commercial bank in the Solomon Islands within 3 months from the export date. There are two frameworks under which CBSI administers controls on exports (i) General authority and (ii) Specific Authority.

Figure 4.4. Volume and Average price of logs approved under specific Authority to Export, 2016



Source: CBSI

The export of all goods and services other than round log is administered by government agencies that issue export permits and do not require foreign exchange control authorization from the CBSI. However, exporters and government agencies are required to report to CBSI all the details pertaining to each export consignment of which

the CBSI's exchange control unit monitors to reconcile proceeds.

The export of round logs not covered under the general authority is directly administered by CBSI in collaboration with respective government agencies. This means that round logs must be granted 'Specific Authority' after receiving market price certification and forestry clearance from the Commissioner of Forestry.

Exports: - Administration of Specific Authority.

In 2016, CBSI issued 829 Specific Authorities to Export to round log exporters. This increased by 1.2% from the previous year (See Table 11), however the volume decreased by 2.6% to 2.612 cubic metres valued at approximately \$2,368 million.

	2013	2014	2015	2016
Total Applications approved (numbers)	846	848	819	829
Total Value of Exports-SA Approved SBD (Millions)	1,876	2,205	2,536	2,368
Volume of Exports- SA Approved (Million m3)	2.269	2.449	2.679	2.612

Source: CBSI

Imports payment administration: Applications above required CBSI limits.

CBSI continues to monitor transactions between residents and non-residents in terms of trade and service payments, capital and personal transfers. All applications for travel, personal transfers and sustenance above SBD 30,000 requires approval by the Bank. Furthermore, Trade and Services payments exceeding SBD 100,000 must be referred to CBSI for approval before the commercial banks can settle payments. Foreign exchange payment for amounts less than \$100,000 and \$30,000 respectively can be assessed and facilitated by the Authorised dealers (commercial banks) without CBSI approval.

Authorization of capital and financial account transactions such as capital transfers (dividends), loan repayment, equity proceeds, and property proceeds are not delegated to authorize dealers and must be referred to CBSI at all times.

During 2016, a total of 8,992 applications valued at \$5,258 million were referred to CBSI for authorization. This total figure includes all trade of merchandise comprising around 76%, service payments at 12%, capital transfers at 6% and personal transfer comprising 6% of the total payments. (See Table 12). Average value per application however has fallen from \$649,539 in 2015 to \$584,742 in 2016, indicating the strengthening of the Solomon Islands dollar compared to previous year.

Table 4.8: Number and value of foreign exchange applications approved by CBSI: 2013-2016

	2013	2014	2015	2016
Total Applications approved	6,439	7,503	8,135	8,992
Value of applications Approved SBD (Millions)	5,043	6,228	5,284	5,258

Source: CBSI

Share Transfer:

The purchase and sale of shares in companies registered in Solomon Islands by emigrating residents with non-residents or residents, require Exchange Control assessment and approval from the Central Bank.

This is to ensure proper legal transfer of valuable considerations to the new owners who may wish to remit capital funds, profits or dividends at a later date.

In 2016, the CBSI granted authority for 4 resident companies to register ownership in favour of non-resident entities. The Foreign Exchange Control approval was granted for the transfer of shares to one non-resident corporate entities and the issuance of additional shares to a non-resident individual entities. However, there are share transfers transactions that are non-compliant with this Exchange Control requirement and CBSI encourages all companies and individuals to comply with the legal requirement to avoid further complication regarding their share transfers.

FINANCIAL MARKET SUPERVISION

Financial Market Supervision Department (FMS) shoulders two core responsibilities. The first responsibility is assessment of new applications for license to establish bank and non-bank financial institutions in Solomon Islands while the second responsibility is prudential supervision of Financial Institutions (FIs) licensed under Central Bank of Solomon Islands Act, Financial Institutions Act, Insurance Act, National Provident Fund Act and Credit Union Act.

FMS executes its second responsibility using four-pronged approaches to supervision and these are: (i) offsite prudential supervision; (ii) onsite risk-based examination; (iii) relationship management; and (iv) financial market intelligence. This approach is aimed at ensuring Solomon Islands financial sector has sound and stable FIs and stable and healthy financial system. Having a stable financial system, intermediaries, markets and market infrastructures, is pertinent to maintaining orderly flow of financial services to Solomon Islands economy. Uninterrupted supply of financial services is important to supporting real sector activities and distribution of risks across the economy. An economy with strong financial system and diversified risk structure can better withstand economic shocks and maintain continuous supply of financial services than an economy with weak financial systems and less diversified risk structure.

Prudential Supervision

FMS conducted three risk-based onsite examinations and fifteen follow-up prudential reviews on the following FIs in 2016:

- Pan Oceanic Bank (POB);
- ANZ Bank (ANZ);
- Bank South Pacific (BSP);
- Tower Insurance Limited;
- Solomon Islands National Provident Fund (SINPF);
- Royal Solomon Islands Credit Union Limited (RSICUL)
- Credit Corporation (SI) Limited (CCSIL); and
- Solomon Islands Nurses Credit Union Limited (SINCUL).

Detailed findings and recommendations to mitigating risks identified during respective onsite examinations have all been communicated to concerned FIs for rectification during 2016. Most FIs examined, except credit unions, have instituted remedial steps to address risk areas identified and the matters have now been closed.

Relationship Management

FMS, in addition to prudential supervision, held 58 bilateral consultations with FIs. The consultations are aimed at enhancing operational and institutional understanding of FIs and to providing FIs direct channels for raising institution-specific issues to CBSI.

The department has also coordinated three bankers meeting for heads of FIs in 2016. The bankers meeting is a high level interactive forum where central bank officials and heads of FIs converge each quarter to discuss trends of macroeconomic aggregates and consolidated performances of banking sector and other generic issues currently affecting or likely to be affecting banking sector going forward.

Financial Stability Committee

FMS acts as secretariat to the Financial Stability Committee (FSC), one of the core committees within CBSI. FSC was set up to discuss financial sector issues and micro and macro-prudential policies and issues pertinent to financial sector stability and development. Three meetings were called in 2016 enabling the committee to endorse prudential guidelines, onsite examination reports and research papers. Prudential guidelines reviewed and approved in 2016 are Prudential Guideline 1 on Capital Adequacy, Prudential Guideline 2 on Asset Classification and Minimum Provisioning and Prudential Guideline 5 on Large Exposures while new prudential guidelines crafted and approved in 2016 are: (i) Standards for Insurance Brokers; (ii) Standards for Valuation of Unlisted Assets of SINPF; (iii) Standards for Agent Banking; (iv) Standards for Issuance of Commercial Paper; and (v) Standards for Con-

sumer Protection. These new guidelines are expected to improve and strengthen the risk management practices of FIs. Meanwhile, in terms of research, FMS has carried out an Insurance Market study to deepen supervisors' understanding of local insurance market, particularly from the supply and demand-side perspective. A nationwide insurance market survey was completed and findings to this research will be presented to FSC in 2017.

Legislations, Prudential Guidelines and Research Papers

FMS continues to push for review and upgrade of current legislations. As part of this process constant dialogue was held with the Ministry of Finance and Treasury (MoFT) across 2016 to fast-track review of Credit Union Act and SINPF Act. Close contact was also held with external consultants assisting FMS review the Financial Institutions Act and Insurance Act. Work on these two legislations is nearing completion and FMS is hopeful of submitting final policy papers to the Economic Reform Unit (ERU) to action in 2017. Finally, in terms of regulation, significant progress was made in 2016. The regulation on credit bureau was gazetted during the year and is now operational while the regulation on fitness of applicants of banking license was cleared by legal draftsman and is now with ERU to progress.

Licensing and Registration

Two new applications for license to operate banking business were received. One was from Bred Bank and the other was from Empire Solomon Bank. The former submitted its application for assessment in March and was granted an interim banking license in May after satisfying the assessment requirements. The latter submitted its application for assessment in October but unfortunately its application was unsuccessful.

Capacity Building, Workshops and Conferences

Training and capacity building are vital for financial sector supervisors for two reasons. Firstly, financial landscape is changing dramatically owing to changing market conditions and increasing globalization and, secondly, risks have become increasingly sophisticated and difficult to identify. Financial sector supervisors therefore need upskilling to enable them implement best international practices in financial sector regulation and supervision.

In 2016, FMS staff participated in various overseas seminars and workshops covering array of areas ranging from FI supervision and risk management and natural disasters to policy development and stress testing. One staff was sent on a 1-month attachment with Australian Prudential Regulatory Authority (APRA) in Sydney on research and policy development. His attachment was co-funded by APRA and CBSI.

In addition, FMS has also hosted one regional onsite examination and one internal workshop. The regional onsite examination was conducted on BSP with assistance from

APRA. APRA provided an advisor to support the onsite examination team comprising financial sector supervisors from Cook Islands, Papua New Guinea, Samoa, Timor Leste, Vanuatu and Solomon Islands. The internal workshop was conducted by the Pacific Financial Technical Assistance Center (PFTAC) on problematic credit unions for FMS staff.

Finally, as part of its contribution to capacity building, FMS management also conducted two internal workshops for FMS staff. The first workshop was on standardized ratings for FIs under CAMEL while the second workshop was on estimating credit loss function. Both trainings will continue in 2017. As part of its outreach program FMS had also conducted three refresher workshops for staff of commercial banks, credit unions and insurance companies in 2016.

FINANCE ACCOUNTS

Budget

In line with the requirement of the CBSI Act 2012 the Bank prepared its 2016 budget and was approved by the Board in November 2015. The budget totalled to an amount of \$96.8 million. This includes expense allocation of \$73.5 million for administration and operations, currency and monetary policy cost and \$23.3 million for Capital costs. Mid way through the year 2016 revision was made to the budget with a reduction to the total of \$93.5 million, which \$67.8 million for operation, currency and monetary policy cost and \$25.7 million for capital costs. The revision of the annual budget resulted from the changes experienced in the first half of the year and the remaining planned activities the Bank intended to deliver for the year 2016.

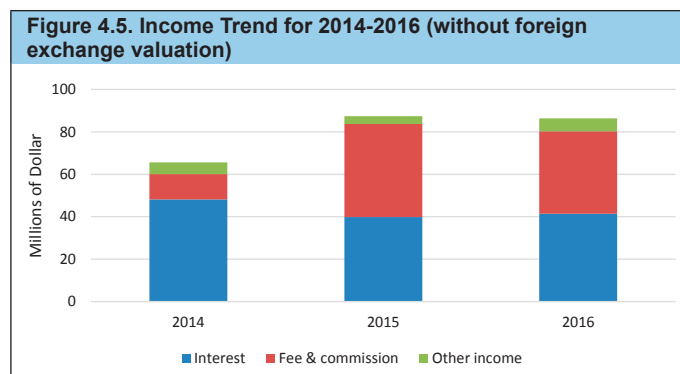
Accounting and Financial Reporting

Figure 4.5. compares the actual and budget for the financial year 2016. A more detailed analysis of the financial accounts is presented in the audited accounts for the year. In 2016 the Bank made an operating profit of \$24 million however with the inclusion of unrealized foreign currency loss movement of \$66.3 million, and the fair value movement in gold of \$17.9 million the Bank had a comprehensive net loss of \$24.6 million.

The statement of financial position had mixed movements in 2016. Total Assets increased by 3% from \$4.51 billion to \$4.67 billion, the increase largely came from the foreign currency assets. Similarly, liabilities of the Banks also increased by 4%, moving from \$4.49 billion to \$4.68 billion, this increase is also largely influenced by foreign currency liabilities. The equity position of Bank declined from \$13.2 million to a negative \$11.4 million, owing to the significant net unrealized foreign currency revaluation loss of \$66.3 million for the year.

The Bank continues to maintain its Accounts and Financial Reporting according to the International Financial Report Standard as required by the Central Bank of Solomon Islands Act 2012 and as a member of the international

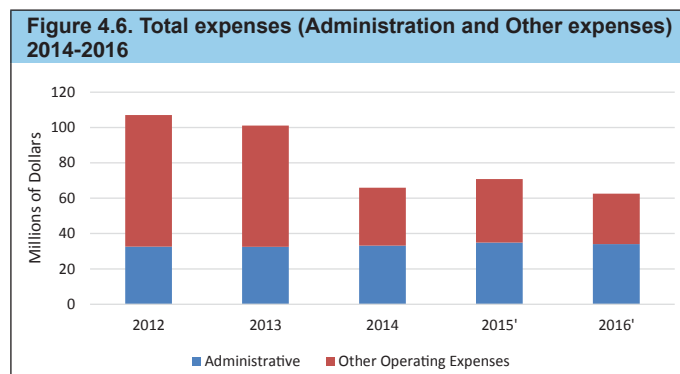
community.



Source: CBSI

External Audit

The external audit of the Bank for 2016 was provided by KPMG Fiji through the Office of the Auditor General. 2016 is the fourth year of a five-year contract for this engagement by KPMG. The audit engagement for 2016 began with a planning trip in November 2016, followed by a brief visit at 31st December to witness the currency stock take, and finally with the substantive on site field work conducted in 2017, for three weeks beginning 27th of February to the 17th of March 2017. The external auditor’s opinion on the financial statement of the Bank for the year 2016 is featured with the financial statements attached to this report.



Source: CBSI

Financial system

The Bank’s financial system project continued with implementation in 2016, with the old and new financial system operating parallel for the first six months. In June 2016, the old sun system was phased out and only used as an archive, and Technology One- One banking solution continued as the new financial system for the Bank. The new financial system enabled the Bank to streamline various financial processes through automation; Areas such as, procurement, settlement, receipting, payroll integration, fixed asset management as well as a flexible reporting tool in ExcelOne, which the Bank utilizes to report to its stakeholders.

Capital Projects

In 2016, the Bank improved and completed its conference and recreational facilities for staff welfare, at Aruligo. The facility was face-lifted with new security fencing, a leaf hut, and a permanent conference house. This new conference house is used for bank social events, meetings, conferencing and if not used, the bank can hire out to other organizations for their training or conference. However, priority is for the CBSI use.

In addition to the Aruligo project, the Bank also constructed a retainer wall to protect its property at Rifle Range, replaced aging generator for Skyline property, ordered new workstations for the Currency and Bank Operations Department, and reconfigured the third floor of the Head Quarter Building to accommodate additional staff. Also in 2016 the Bank completed its investment in the new financial system that now hosts the Bank's general ledger, payroll, budget and financial reports.

Bank's plan to start work on its Noro office was delayed pending completion of land titles for the site. At this time plan to extend the Head Quarter Building to its former office in Mud Alley Street is work in progress.

CURRENCY AND BANKING OPERATIONS

During the period under review, the Currency and Banking Operations department continued to discharge its function as mandated under section 9 (f) in conjunction with sections 18 to 25 and Part 6 of the Central Bank Act 2012, which provides the Bank the authority:

- To issue, regulate and manage the currency of the Solomon Islands;
- To promote a safe, sound and efficient payment system; and
- To act as banker, financial adviser and fiscal agent to the Government and to any other public bodies and organisations of Solomon Islands.

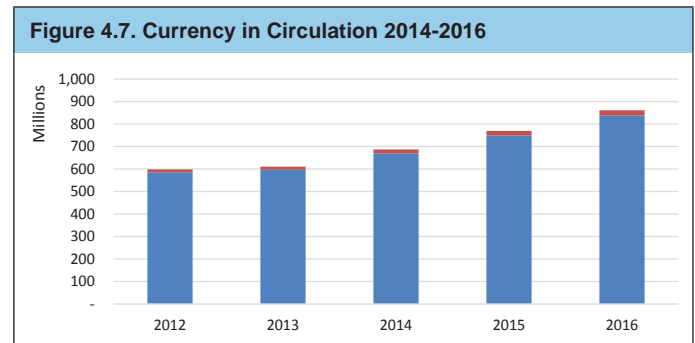
These specific authorities translated into key responsibilities that included currency stock control and management; issuing of notes to commercial banks for circulation; receiving of currency deposits from commercial banks and Solomon Islands government; sorting and destruction of unfit and soiled banknotes; and designing and ordering of new banknotes or coins. The department also engaged in social responsibilities such as advising and educating the public to care for notes and coins, and warning public about counterfeit notes. Outlined below are the activities performed by the Bank to implement this function.

Currency in Circulation stock

As at the end of 2016, the total value of currency notes and coins in circulation increased by 12.0% to \$861 million from \$769 million in the previous year. Currency notes accounted for 97% or \$837 million of the total circulation whilst coins made up 3% or \$24 million. Figure 4.7 below

shows the trend in the currency in circulation from 2012 to 2016.

The 100-dollar note represented 83 per cent of the notes in the hands of the public, reflecting its demand and popularity as the note for making payments and savings. Coins in circulation increased by 15% in 2016, but 2% less compared to the increase in 2015. Of the total coins in circulation \$2 makes half of the coins in circulation. This is followed by the \$1 at 29% and 50 cents at 13% and the balance shared between the two lower coin denominations, 20 cents and 10 cents respectively.



Source: CBSI

Volume of Counterfeit Notes impounded from circulation dropped

Only nine pieces of counterfeit notes were confiscated from circulation in 2016 which is almost 90% less than the 2015 record of 75 pieces. Of the total counterfeit notes impounded, six pieces were counterfeits of the old \$100 notes series, two pieces of the \$50 notes of which one piece was of the new series introduced in 2013, and a \$10 piece. The higher denominations are the most targeted notes by counterfeiters. The above graph shows a rising trend in counterfeit notes since 2010 to 2015. The introduction of the new series of \$100 notes in 2015 and the new \$50 notes in 2013 may be the cause of this positive reduction. However, the need to aggressively educate the public about the risks of circulating counterfeit notes is still a priority. The Bank uses the radio and print media throughout the year, as well as awareness programs to various schools and institutions around the country under the slogan 'Check, Look, Feel'. This is basically to encourage the general public to check for the security features, look for the watermark image and feel the raised print on their notes.

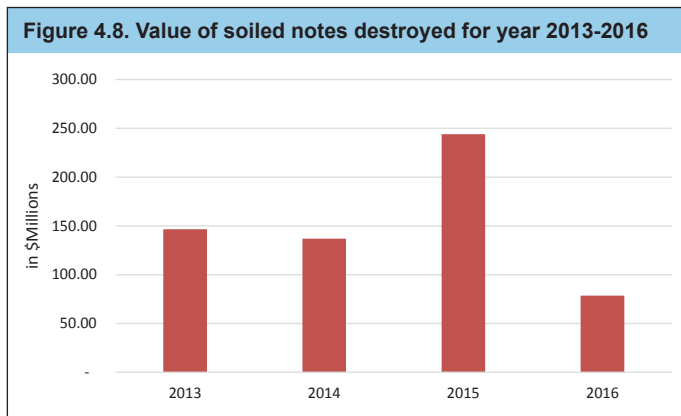
Note Processing

In 2016, \$78.68 million value of soiled notes was processed and destroyed compared to \$236.5 million in 2015. The reduction in the volumes of destroyed notes may not be the result of improved cash handling by the public but was due to the withdrawal and cancellation of volumes of the old \$100s and \$50s series of notes when the new \$50 and \$100 series were introduced in 2013 and 2015 respectively.

The high rate at which notes are returned from circulation is a concern for CBSI. It generally shows the poor handling of currency notes, despite the mass public aware-

ness on how to care for the currency notes.

De La Rue Cash Systems Engineers continued to provide maintenance and servicing support of our Cobra sorting and destruction machine as the Bank sees this as an important investment for the Bank that helps to improve efficiency and build local capacity in the Bank’s back-office cash operations.

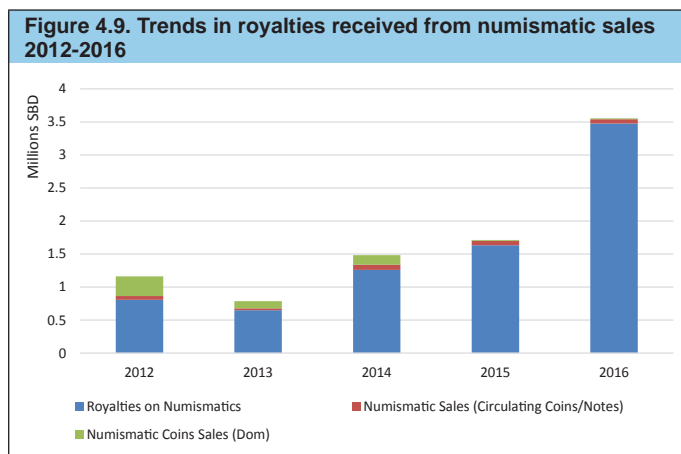


Source: CBSI

Numismatic items sales underpinned.

Total revenue earnings from both local and international sales of numismatic materials or collectibles more than doubled the total earnings in 2015 – an increase of 107% to \$3.6m in 2016 compared to \$1.7million in 2015. The increased revenue also exceeded the 2016 budget of \$2.25 million by \$1.3 million. This was attributed to various factors including increases in subscriptions to popular commemorative coin programs, successful marketing and sales of new products, increased number of new contracts signed in 2016, and the integrity of our coins that gave rise to increased demand for our coins amongst many collectors.

Sales in the domestic market, on the other hand, continued to dwindle basically because of the relatively small market for local collectibles. In terms of coin programs, almost 100 coin programs were approved during the year.



Source: CBSI

A large portion of the approved coin programs portrayed historical icons, landmarks and cultural heritage sites of significant value. Other designs portrayed important technological advancements and innovations in the transport and communications industries that also impacted on humanity generally. Some of the coins produced in 2016 were products of innovations involving state of the art technology which rendered them very unique in the market. The integrity of the coins continued to be the major determinant in approving the Bank’s participation in the coin programs.

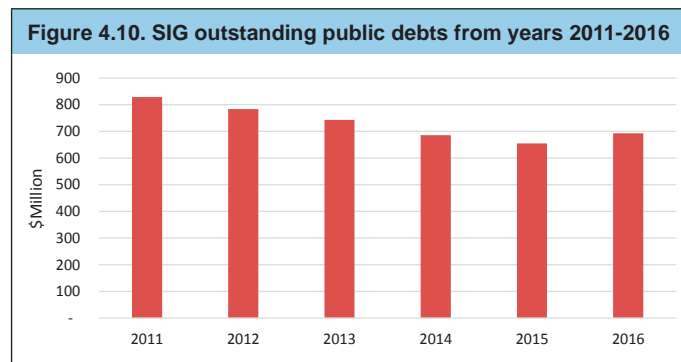
Bank continues to assist Government in the administration of the Government Debt Statistical Database

The CBSI Debt Unit (CDU) continues to act as the secondary site for Government’s external public debt database. Public debt data is kept on the CS-DRMS system while a portfolio analysis tool is maintained by the Government Debt Management Unit (DMU) for analysis of multicurrency loans.

As part of its activities, CDU performs monthly loan validations on the CS-DRMS, dispatches QEDs to the World Bank and uploads auction treasury bills results on the CS-SAS after each weekly auction. CDU also maintains the External Private Debt database. CDU also holds regular meetings with the DMU on administrative and technical issues including capacity development issues.

The external public debt profile is made up of thirty-five (35) active loans of which 29 are fully disbursed, 4 still disbursing and 2 are yet to be disbursed. The amount disbursed from July to December totalled to \$103.53 million. The Principal creditors includes the Asian Development Bank (ADB), International Development Association (IDA), European Union (EU); International Fund for Agriculture Development (IFAD) and Export Import Bank of Republic of China (EXIM). Figure 4.10 below, shows the outstanding balance of public external debt of Solomon Islands.

The Public Disbursed Outstanding debt (DOD) of the Solomon Islands at 31st December 2016 increased to \$692.43 million. The increase in the total stock was mainly due to exchange rate movement and disbursement of ADB and IDA Loans during the year. The DOD is anticipated to



Source: CBSI

increase in volume in to 2017 due to forecasted disbursements on the new loans that were contracted in 2014 and 2015 respectively.

Total external debt repayments in 2016 were \$60.66 million of which \$52.05 million was for Principal repayments and \$8.61 million for interest payments.

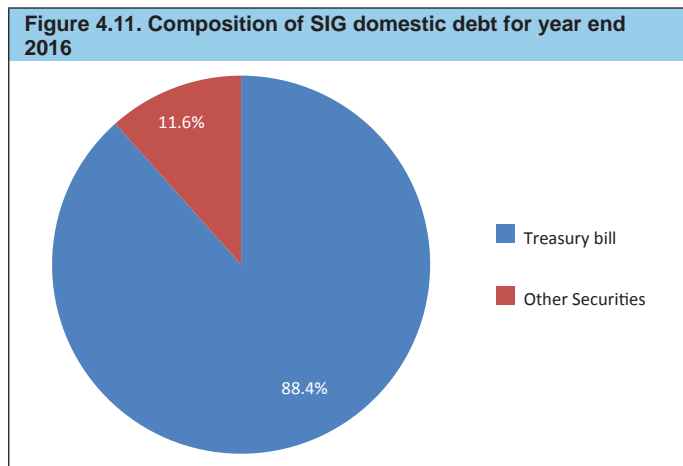
In terms of currency composition of the total official debt, the Special Drawing Rights (SDR) accounted for 85.24% of the total DOD or \$590.27.06 million followed by the United States Dollar with 13.55% or \$93.79 million, and the European Currency Units with 1.21% or \$8.36 million.

Government’s Domestic Securities Debts

Solomon Islands Government (SIG) domestic debt outstanding at the end of the year was \$42.58 million, a reduction of \$0.28 million compared to \$130.7 million in December 2015. The domestic debt outstanding balance comprised of \$37.64 million in Treasury Bills, and \$4.9 million in other SIG special securities. Debt service repayment during the year totalled \$0.34 million.

The major holders of domestic securities were the Solomon Islands National Provident Fund (SINPF) with 32.53%, Commercial Banks with 43.98%, CBSI with 11.80%, General Public with 10.36%, and other Creditors with 2.34%. The composition of the Government domestic debt is shown in figure 4.11 below.

The decline in the outstanding balances for both the external public debt and domestic debt reflected the governments continued commitment towards its debt service obligations.



Source: CBSI

BANKING SERVICES

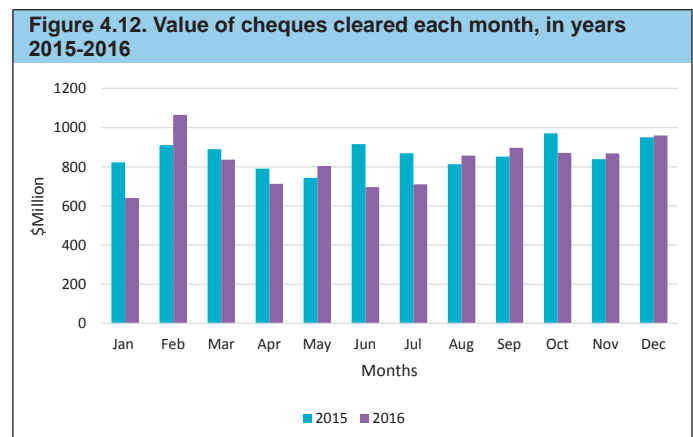
The Bank continued to deliver banking services to licensed financial institutions, the Solomon Islands Government (SIG) and other non-banking financial institutions as mandated in the CBSI Act 2012. These services include, but are not limited to, administering the local and foreign currency denominated accounts established with the Bank by SIG and its donor partners, facilitating domestic transfer

payments, providing general account enquiry services, daily monitoring of free liquidity of the commercial banks and the safe up keeping of e-registers and records for audit requirements.

Clearing House Activities

The CBSI supervises the daily clearing of cheques drawn on all the licensed commercial banks operating in the country. In 2016, the total value of cheques cleared amounted to \$9.9 billion with a monthly average value of \$827 million in cheques exchanged via the Clearing House. Compared to 2015, the total value of cheques cleared declined by 4% from \$10.4 billion to \$9.9 million in 2016.

On a monthly basis, the month of February registered the highest value of cheques cleared in the Clearing House as noted in the chart below. Overall, the decline in the total value of cheques could be attributed to the reforms in payment arrangements, which favours electronic transfers. However, all high value payments including payments in the securities market are still paid out in cheques.



Source: CBSI

Work slowly progressed on the establishment of a National Payments System.

In February 2016, the Cabinet agreed to have a new law on the National Payment System (NPS) and, approved that the Attorney Generals Chambers liaise with the Ministry of Finance and CBSI to draft the new law. Following the Cabinet decision, a MOU was signed with the International Financial Corporation (IFC) for the implementation of an automated clearing and settlement system in the country.

With the support of the Payments System Development Team in the World Bank Group together with IFC, a draft NPS legislation and a policy paper to support the drafting process was delivered.

The CBSI teamed up with the Economic Reform Unit in the Ministry of Finance and Treasury to carry out a country-wide consultation on the NPS Policy Note between September and November, 2016.

In the absence of a NPS legislation, however, the Central

Bank is given the power under Sections 26 and 27 of the CBSI Act 2012 to provide facilities, including intra-day credit, to oversee payment, clearing and securities settlement systems, and their participants, to ensure the safety, soundness and efficiency of the system.

The Central Bank recognises the need to have a Payment Systems Legislation that will support the reform of the national payment system and reduce risks, harmonize the provision of services, introduce oversight on the market and guarantee protection of the customers. In addition, the importance of secondary legislations to provide additional details in the area of Electronic Fund Transfers, Agents and Retail Payments after the NPS bill has been enacted.

CBSI continues to work closely with the World Bank and IFC payment experts which saw the success of the nationwide stakeholder consultation done in the 4th quarter of 2016. CBSI with the support of all stakeholders and the financial community is hoping for a more effective collaborative approach to ensure this project is achieved within the time frame.

SMALL BUSINESS FINANCE SCHEME

The CBSI administered Small Business Finance Scheme (SBFLS) came under review in 2016. The review was jointly conducted by the Ministry of Commerce, Industries, Labour and Immigration (MCILI) together with the Ministry of Finance and Treasury (MoFT) and CBSI. Consequently, a new arrangement materialised in the form of the Micro, Small and Medium Enterprises Business Loan Guarantee Scheme (MSME-BGLS), which came into existence in November 2016. A seed fund totalling \$2 million was deposited into the respective account for the guarantee scheme, established with CBSI.

In retrospect, no nominations for guarantees under the SBFLS was received from the participating banks in 2016 as was also the case in 2015. No guarantees were claimed from banks in 2016 as compared to a total of two (2) claims paid to ANZ in 2015 bringing YTD guarantees cancelled (as claims on the scheme) to thirteen (13) compared to eleven (11) at end 2014.

YTD loans approved under the scheme remained at sixty-four (64) with fifty-nine (59) nominations from ANZ Bank, BSP with three (3) and former Westpac bank with two (2).

In terms of YTD numbers, gross loan amount remains at SBD14.5 million as in 2015. As at end 2016, a sum total of \$1.2 million was paid to commercial banks for claims on the guaranteed amount – this represents 13 borrowers that defaulted on their loans.

On that same bearing, a total of \$3.7 million in guarantees was cancelled as the borrowers had repaid in full their loan obligations – this represents 46 borrowers who successfully paid off their loans.

Subsequently, only five (5) guarantees were outstanding at end 2016.

No change recorded in nominations by Provincial Location

No nominations were submitted by participating banks in the SBFLS to CBSI in 2015 and 2016. Issues such as limited access to banking services in the provincial towns and growth centres, lack of adequate and acceptable collateral, loan application processing costs, complex application and decision making processes are key issues SMEs highlighted during the review.

INFORMATION TECHNOLOGY

The Bank uses information technology to support its operational activities and corporate objectives. The information technology department shoulders the responsibility to improve, strengthen and maintain the information technology function of the bank. These include:

- Deploying of computers and software/systems within the departments to help them get their job done.
- Facilitating the workflow and information within the departments and to the clients of the bank.
- Securing the Bank's corporate electronic data and information.
- Enabling internet connections for officers to access information through internet services
- Allowing the Bank to disseminate economic information to stakeholders on timely manner for their use and to make informed decisions.

In 2016 the Bank focused on the following projects and activities:

- **Technology One Financial System Live Implementation:** This final phase of the project involved ceasing the parallel run of the old financial system and accepting the sole implementation of the new financial system. Configuration work and training for users on the Budget module were carried out. Receipt feature was also configured, tested and uses live and replace the manual receipting. Other features of the system will be progressively explored and tested as of next year.
- **Website Upgrade:** The Bank redesigned its website in-house with updated web software and improves its outlook and easy to administer and use. The upgrade allows the visitors to easily find and access the required information on the website. It is built on software platform that accommodates easy upgrades or maintenances in the future.
- **International Payment system upgrade:** The Bank carried out swift software applications upgrade on its SWIFT systems. These include upgrading to the current applications: SWIFT

Alliance Access/Entry 7.1.20, Browser 7.0.25, Alliance Web Platform 7.0.70, SWIFT Net Link 7.0.41 and SWIFT Alliance Gateway 7.0.41.

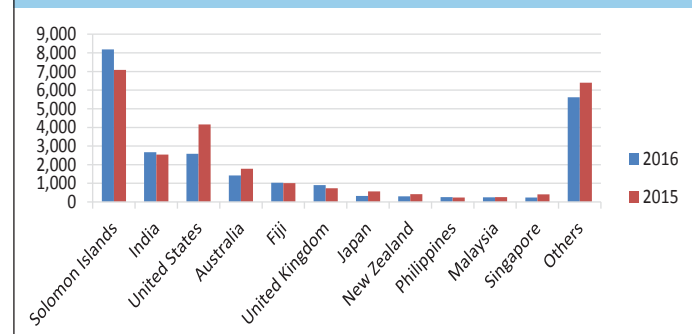
- **Paperless and Workflow:** The Bank also pursues the concept of minimising the use of paper and improving the workflow through introduction of the shared point system solution.
- **Currency Working Store system.** Focus on this system included monitoring the updated transactions and worked with users in maintaining and enhancing the reporting functions of the system. The users are using the system to maintain stock records of currency notes and coins which their balances are used to reconcile with the general ledger balances.
- **Exchange Control System:** Development of this outstanding system is work-in-progress with some activities carried out during the year included assessment of requirements, import features, monitoring and reconciliation, export and payments and prepared server environments for testing. The system if completed will improve the bank's recording, accessing and monitoring compliance with Foreign Exchange Control regulations on imports and exports transactions.
- **Maintaining Local Area Network (LAN) services:** These included resolving server issues on storage and processor, maintain operating system and server security updated patches, maintain LAN connections and access, as well as continue to monitor Anti-virus reports and ensuring no major threat are imminent.
- **Maintaining the Banks Software:** The Bank renewed its license software to maintain support by the supplier. This included the Bank's TechnologyOne Financial System, the statistical forecasting software Eview 9, the anti-virus software - Symantec Protection Enterprise Suite 4.1, the firewall - Smoothwall, the payroll system - Micropay Meridian, external mail - the Google Apps and Foreign Exchange trading system - Bloomberg. The Bank also maintains its current databases.
- **Maintaining the Bank's computer hardware items:** These involve repairing the faulty desktops, laptops and printers. The Bank replaced its aging hardware items with 10 desktops, 18 laptops, 12 Microsoft Surface Tablets and 5 printers including the 3 receipt printers.
- The Bank also provided support and maintenance services on its internet and emails.

Visitors to CBSI Website

In 2016, the total number of visits to the CBSI website reduced by 7% to 20,237 compared to 2015 visits of 25,597. Among visitors from all over 200 countries, Solomon Islands make the most visits to the CBSI website.

The Bank also provided new and updated information on its website for public to access and gather useful information about the Solomon Islands economy.

Figure 4.13. Number of visits by top countries to CBSI website 2015-2016



Source: CBSI

Disaster Recovery, Policies and Procedures

To improve and automate the manual backups of systems and data from the production servers at the main office and to restore the systems and data to the Contingency Servers at the Bank's temporary Disaster Recovery (DR) office, the Bank engaged Our Telekom and completed the installation of the Fibre Optic cabling and allow the bank to configure and setup connections between these two banks network sites.

The connection was available and live replication of data and virtual machines (systems) from the Production servers to the DR Servers started in the second half of the year. The testing of the systems and data at the DR office is planned to be carried out in 2017.

Work on drafting the department manual started in the year. The purpose of the manual is to define, develop, and document the information policies and procedures that support the goals and objectives of the bank.

INTERNAL AUDIT

The Internal Audit Unit (IAU/Unit) was able to recruit its second Internal Audit Assistant officer during the year - an internal transfer from the Finance and Accounts Department.

Though the Board Audit Committee (BAC) was not able to meet due to membership issue, the Unit had been functioning as normal and was able to review most of its 2016 possible high risk auditable areas.

The Unit was and will continue to ensure that management established Internal Control systems and processes, are not only working as expected but are robust in nature; that risks areas of potential risks that may potentially hinder the achievement of Bank objectives are appropriately and timely mitigated.

Table 4.9 Activities carried by the Internal Audit Unit in 2016	
Area of Assessment/ Review	Review Objective and Scope
Payroll Process and related activities	Compliance to External Regulatory Requirements <ul style="list-style-type: none"> • SINPF Act Requirements and the effective administration of staff contributions • IRD PAYE Employer obligations and the effective administration of staff fortnightly PAYE deductions
Subsidised Financial Assistants to Staff	Compliance to governing policies: <ul style="list-style-type: none"> • Security and safeguarding of Bank's Financial Resources. • Staff responsibilities and obligations • Effective administration of the schemes
General Ledger Reconciliations	Ensure quality of financial data/information had been stored and reported through Management and External Financial reporting <ul style="list-style-type: none"> • Accurate and timely reconciliation of all reconcilable Accounts (generally, all Assets and Liabilities in the Chart of Accounts) • Accurate and timely reversal or adjustment of any wrongly posted (reconciling item) transaction. • Effective supervision of all related reconciliation processes
IMF weekly/monthly Monetary Reports	As per IMF requirement - ensuring the integrity of the weekly/monthly Monetary report sent to the IMF by the Bank
Soiled Notes processing and Destruction	Assuring the Management that the Internal Controls (ICs) covering the safe keeping to the final shredding and burning of unfit currency notes are effective and robust.
Investment of External Reserve	Compliance assurance as per the approved Investment portfolios and placement limits in terms of currency and investment types
Management's influence over towards good governance and best accounting practices	To assure the Board through the Board Audit Committee (BAC) that, whilst the management is the primary custodian and implementer of policies, rules and procedures covering most staff and management benefits, the members of the management team do have high regard for good governance and best accounting practices. <ul style="list-style-type: none"> • Application, assessment and disbursement of managers' home, personal and vehicle loans. • Complete and accurate accounting for the Bank's Credit Cards disbursements • Compliance to applicable external legal requirements/provisions

CHAPTER 5: FINANCIAL INCLUSION



A CBSI officer points out to the interested members of the public the security features of Solomon Islands currency during the Kodili Festival held in Buala, Isabel Province. Educating the public to always be on guard against fake money and caring for our currency notes is part of CBSI's public education objectives during its participation in festivals held around the provinces.

In 2016, efforts in the financial inclusion activities continued to expand. The main highlight for financial inclusion during the year was the adoption of the second national financial inclusion strategy (NFIS2) 2016-2020 after being peer reviewed by the Alliance for Financial Inclusion (AFI's) working group – Financial Inclusion Strategy Peer Learning Group (FISPLG) – in Dar es Salaam, Tanzania. With the adoption of the strategy, financial inclusion has now been nationalized, as embedded in the definition of financial inclusion. In the context of Solomon Islands, financial inclusion is defined as “the process by which (i) appropriate and relevant financial products and services are sustainably provided by the formal and semi-formal financial intermediaries, (ii) governed by suitably tailored regulations and/or guidelines, (iii) at a fair, transparent and affordable cost, (iv) so that the disadvantaged, low-income segments of society can have access to and repeatedly use these financial products and services to enhance their financial competency and security, thereby improving their livelihoods”. The other highlight was the celebration of the Global Money Week (GMW), which coincided with the Central Bank’s 40th Anniversary. The theme of the GMW was ‘take part, save smart’.

	2011	2012	2013	2014	2015	2016
Commercial Banks	3	3	3	4	3	3
Agencies	7	7	7	7	7	7
Branches	13	13	12	14	14	15
ATMs	36	38	38	39	41	42
EFTPOS Terminals	175	224	306	346	400	310
EFTPOS Merchants			72	325	353	256
Mobile Banking Agents			0	105	164	192

Source: CBSI

In 2016 number of commercial banks licensed in the country remained the same as in previous year., The most notable improvement in financial services access is the increase in the mobile banking agents to 192 from 164 a year ago. Further, there was one additional ATMs installed bring the number of ATMs to 42 but, EFTPOS terminals numbers fell relative to 2015.



A CBSI staff helps two women to get information about financial services during the Kodili festival. Under the NFIS2, by 2020 the number of women who will be users of financial services is 150,000.

The National Financial Inclusion Strategy 2 (NFIS2)

The NFIS2 aims to have 300,000 new users of formal and semi-formal financial services and products by 2020 of which half (or 150,000 users) must be women. In order to reach this target, six broad objectives were identified. They are: (a) amplify the reach and quality of digital finance channels; (b) improve financial services delivery to the MSME sector; (c) include women, youth and rural adults as fully engaged participants in the national financial sector; (d) build financial resilience in households and communities; (e) build financial empowerment in ways that are relevant to daily life, motivating and actionable; and (f) execute NFIS2 through effective stakeholder coordination, responsive data and sound evidence.



Children from BSP adopted primary schools putting on their financial education fashions wears during the Solomon Money Smart Day in 27 2016.

These objectives are implemented through the establishment of four working groups; they are digital Financial Services working group (DFSWG); micro, small and medium entrepreneurs working group (SMEWG); consumer empowerment working group (CEWG); and inclusive insurance working group (IIWG). Consequently, implementation of the NFIS2 began during the year with the establishment of the first working group – the inclusive insurance working group. The remaining working groups will be established in 2017.

2016 Global Policy Forum

The Alliance for Financial Inclusion (AFI) eighth Global Policy Forum (GPF) was co-hosted by the Reserve Bank of Fiji, at Denarau in Nadi, Fiji from 7-9 September, 2016 with the theme “Building the Pillars of Sustainable Inclusion”. The forum brought together more than 500 senior policymakers, regulators, leaders from international organizations and the private sector around the globe. Eighth key areas of sustainable inclusion were the focus of the forum: they were green financial inclusion; SME financing; de-risking and re-risking; financial inclusion data; technology and innovation; consumer empowerment; and partnerships. The Solomon Islands delegation comprised the Central Bank of Solomon Islands, the Ministry of Commerce, Industries, Labour and Immigration (MCILI) and the Solomon Islands Women in Business (SIWIBA).



CBSI's custom king and queen promote Solomon Islands traditional monies and valuable as part of the AFI Global Financial Inclusion Forum held at Denarau, Fiji.

The final outcome of the forum was the production of an action plan called the 'Denarau Action Plan', which is AFI's commitment to Gender and women financial inclusion. One of the highlights for Solomon Islands in the forum was a commitment to assist the MCILI to provide an enabling and accommodating environment to improve financial service delivery to the Micro, Small, and Medium Enterprises (MSME). This commitment was made under the auspices of Maya Declaration. Another highlight was the participation of Solomon Islands in a cultural show during the forum.



Chung Wah and St. Nicholas students: POB adopted Primary Schools prepare to march to Art Gallery as part of CBSI's 40th Anniversary celebration 27 June 2016.



A Student reads an information pamphlet collected from CBSI stall during the Mala Mweimwei Yam Festival, in 2016

Microfinance Institution

The microfinance institution space is currently under-represented in the country. The South Pacific Business Development (SPBD) is the only microfinance institution operating in the country. Since inception, it has continued to assist women to improve their livelihood through saving and micro-credit. By the end of 2016, total savings account increased to 7,370 from 4,644 in 2015. In terms of the amount of loans disbursed in 2016 was \$25 million. In the first quarter in 2016, SPBD expanded its services to Western Province and established a branch in Munda.

Other Achievements

Other activities related to financial inclusion were also achieved during the year. For example, on 12 August a joint ANZ/Pacific Financial Inclusion Program (PFIP) coconut value Chain partnership, which was funded by the Australian Department of Foreign Affairs and Trade (DFAT), was launched. This project will see the expansion of digital finance to the agriculture value chain with the coconut farmers being the target as the starters of the value chain. This initiative will assist these farmers to access

to formal financial services, especially in saving, credit and payment services through ANZ's goMoney mobile banking platform.

Also during the year, a working group on inclusive insurance was established following a consultation workshop held on 20 February, 2016. This working group is the first of the four working groups that will implement the NFIS2. The inclusive insurance working group aimed at tapping the low income earners segment of the market. This segment is currently excluded from accessing financial services.

The second working group, Digital Financial Services, is scheduled to be established in the first quarter of 2017. A consultation workshop was conducted on 5 October, 2016. This working group will initially focus on digitizing government payments, mainly in the G2P and P2G space. Thereafter, an economy-wide focus on digitizing payments will follow suit.

Finally, financial inclusion activities in 2016 wind up with a launch of the Micro, Small and Medium Enterprises (MSME) guarantee loan scheme. The guarantee scheme



Raynold Moveni and Eddie Maek ask questions to members of Pacific Islands Regional Initiatives (PIRI) on lessons on how to introduce micro insurance to the poor during a PFIP & AFI organized workshop in Denarau, Nadi Fiji in 2016. According to Demand Side Survey carried out by PFIP, AFI and CBSI in 2015, it was revealed that 93% of the Solomon Islands population is uninsured. One of the objectives of NFIS2 is introduce affordable insurance to the people.

was a government initiative to support MSMEs in the country, and is facilitated by the Central Bank of Solomon Islands.

CHAPTER 6: COMBATING MONEY LAUNDERING AND FINANCIAL CRIMES

The Solomon Islands Financial Intelligence Unit (SIFIU) is established under the Money Laundering and Proceeds of Crime Amendment Act 2010 (MLPCAA 2010). The vision of the SIFIU is “Protecting Solomon Islands from Money Laundering”. The roles and functions of the SIFIU are provided under the MLPCAA 2010. SIFIU is one of the leading agencies in Solomon Islands that is primarily responsible for preventing and detecting money laundering and terrorist financing activities. The Unit maintains its four (4) seconded officers in 2016, three from the CBSI and one from the Ministry of Police, National Security and Correctional Services. In terms of operational functions; the SIFIU reports to the Anti-Money Laundering Commission (AMLC), established under section 11 (1) of the MLPCAA 2010. The Attorney General of Solomon Islands chairs the Commission.



Director of Solomon Islands Financial Intelligence Unit holds meeting with representative of reporting institutions on proper reporting of transaction required under the MLPCAA 2019 to protect Solomon Islands from money laundering and financial crimes.

The Solomon Islands Anti-money laundering regime has been carrying out its obligations to fight money laundering and terrorism financing activities seriously since its establishment in 2006. This is evident from the good ratings it received for the majority of the FATF core and key recommendations on the 2009 World Bank Mutual Evaluation report. Solomon Islands has also been given good and commendable ratings for its follow-up reports on the subsequent years after the 2009 mutual evaluation by the Asia Pacific Group (APG) on Money Laundering. We are hoping for even better ratings on our next Mutual Evaluation in 2018.

Money laundering and terrorism financing are rising activities in the world today. Solomon Islands therefore is not immune to these problems. In combating these unwanted practices, the country has put in place mechanisms and controls we are confident of capable to making our financial system safe from the misuse by criminals. The SIFIU is committed to carrying out its obligations to ensure Solomon Islands is protected from money laundering and terrorism financing activities.

Membership to International Anti Money Laundering Groups provides support to work of SIFIU

SIFIU is a member of the Asia Pacific Group (APG) on Money Laundering and also a member of the EGMONT Group. As a member of these international and regional organizations, the SIFIU and the AMLC are committed to performing their responsibilities to meet International AML/CFT standards and requirements. In addition, being members of these international bodies ensures that Solomon Islands remain in compliance with the best practices in combating money laundering and anti-terrorists financing.

Financing of SIFIU operations comes from the SI Government and the Central Bank of Solomon Islands

Funding for the operation of the SIFIU in 2016 came from the SI Government and the Central Bank of Solomon Islands, totalled up to \$989,540.72, of which \$709,800 from the Government and \$279,740.72 from the CBSI. The Government’s funding increased slightly in 2016 from \$676,000 in 2015 to \$ 709,800 in 2016, a 5% increase. The SIFIU expended \$970,718.72 of the total revenue on its operation in 2016. Apart from meeting the salaries and other benefits of two (2) of its officers, the CBSI also supported the Unit through subsidising some of its expenditure heads, such as medical benefits, leave entitlements, office equipment and IT services.

SIFIU maintained its relationships with reporting agencies through regular contacts

The SIFIU maintained close working relationships with the reporting agencies during the year. Quarterly meetings were held with the AML reporting officers from the three commercial banks in the country, ANZ, BSP and POB to discuss AML/CFT issues. It is encouraging to note that financial institutions in the country continue to play their part in ensuring the financial system of the country is free from money laundering and terrorism financing activities.

Advising Public Against Financial Scams

The SIFIU in 2016 was again involved in advising the public against “financial scams”. The Unit attended to numerous queries from the public during the year on false financial schemes and purported lottery wins. The Famous Family Charity Fund is still a much talked about subject in town. Victims of the scheme are still waiting for their promised returns. Numerous advices put out by the SIFIU and the CBSI through media, felled on deaf ears.

There is a rise in ATM card skimming in the Pacific region. There were reports of such crimes experienced in Samoa, Tonga and as well as in Fiji. SIFIU gave out a warning to the public through media press release during the year on this kind of financial crime, warning the public to take extra care when using ATM machines.



A staff from the SIFIU conducts a training session for bank officers and reporting institutions on the reporting requirements of the Solomon Islands Financial Intelligence Unit.

Numbers of suspicious transactions (STRs) received from the reporting agencies increased

The number of Suspicious Transaction Reports (STRs) received increased from 60 in 2015 to 72 in 2016 while the number of Case Disseminated Reports to law enforcement agencies decreased to eight (8), a 38% decrease. The reason behind the decrease in the case dissemination reports is because of the diversion of SIFIU's limited resources, staffing especially to the prioritized project for the year, the AML/CFT National Risk Assessment. The work on AML/CFT National Risk Assessment commences on the second half of the year.

SIFIU is confident, reporting agencies in the country now have good level of understanding on AML/CFT matters. This is evident in the increase in the number of reports they are now forwarding to the SIFIU. There is a significant increase in the number of Cash Transaction Reports reported in 2016, up by 121% from 51,058 reports in 2015 to 112,970 reports in 2016. There is also a significant increase in the number of Electronic Funds Transfer Reports reported in 2016, up by 75% from 14,402 reports in 2015 to 25,233 reports in 2016. There is however, a fall in the number of Border Currency Reports received in 2016, by 6% from 97 reports in 2015 down to 91 reports in 2016. We presume, the main reason for the drop is because people are now using the banking system more to transfer money as they become more aware of the AML/CFT requirements every Jurisdictions are required to roll out.

Table 6.1 below show the type and number of reports received by SIFIU in 2015.

Table 6.1 Type of Reports	Received		Disseminated	
	2016	2015	2016	2015
Suspicious Transaction Report (STR)	72	60	8	13
Cash Transaction Report (CTR)	112,970	51,058	0	0
Electronic Funds Transfer Report (EFTR)	25,233	14,402	0	0
Border Currency Report (BCR)	91	97	6	0

Source: CBSI/SIFIU

Meeting of the AMLC held during the year

During the year the AMLC met three (3) times. Attendance by members of the AML Commission was 75%. The AMLTEG was able to meet 4 times during the year with a 100% attendance by members. The AMLROs were only able to meet three (3) times during the year with the percentage turn-out of 75% by member institutions. For the Unit staff meetings, only six (6) meetings were held during the year with only 13% turn out rate. The lower turnout rate is due to the small size of the Unit where not all officers always present in the office as part of their job responsibilities involves undertaking other activities outside of office.

Table 6.2 below show the meeting types and number of meetings held in 2015.

Table 6.2 Meeting types and number of meetings				
Year	Meeting Type	Meetings Planned	Actual Meetings Held	Success Rate Percent (%)
2016	AMLC	4	3	75
	AMLTEG	4	4	100
	AMLRO	4	3	75
	Staff	48	6	13

Source: CBSI/SIFIU

Over Seas Trainings/Workshops and Meetings Attended

The Table below show the number of training courses and workshops attended by the SIFIU and supporting institutions in Solomon Islands.

Table 6.3 Show the Number of Workshops and Meetings attended in 2016		
Date	Particular of Training	Facilitator
04 – 08/04/2016	Implementing the International AML/CFT Standards	STI-IMF Training Institute
16 – 17/05/2016	Bali Process: Following the Money Forum	Australian Attorney Generals Office
05 – 09/09/2016	APG Plenary Meeting	Asia Pacific Group on Money Laundering (APG)
14 – 18/11/2016	AML/CFT Assessed Country Course	STI-IMF Training Institute
28 Nov – 1 Dec 2016	APG Typologies Workshop	APG – Jeddah, Saudi Arabia Attended by an AMLC Member

Source: CBSI/SIFIU

Local Training and Workshops

The unit also conducted workshops for local stakeholders in the country as well, as shown in Table below.

Table 6.4 show the number of workshops held for local stakeholders in 2016.				
Date	Particular of Training	Participants	Facilitator	No. of Participants
23/03/2016	Basic AML/CFT	Banks, Insurance Companies And Credit Institutions	FMSD SIFIU CBOD	27
26/05/2016	Roles & Functions of SIFIU	Institute of Solomon Islands Accountant Members	SIFIU	105
08/06/2016	Basic AML/CFT	Pan Oceanic Bank Staff	SIFIU	30
25- 27/07/2016	Scams/Pyramid Schemes	Members of the public who have attended the Yam Festival, Afio South Malaita	SIFIU CBOD	30
31/08/2016	Money Laundering & Terrorism Financing National Risk Assessment	Financial Institutions, LEAs, Cash Dealers and CBSI	NRA Technical Advisor	36
26 – 30/09/2016	Scams/Pyramid Schemes	Members of the public who have attended the Kodili Festival, Buala Isabel Province	SIFIU CBOD	40

Source: CBSI/SIFIU

CHAPTER 7: CALENDAR OF EVENTS 2016

• Month	• Events
• January	
• February	<ul style="list-style-type: none"> • Chief Manager Financial Market Supervision and Chief Manager International attended Portfolio Construction Class 2016 in Nadi, Fiji
• March	<ul style="list-style-type: none"> • Manager Internal Audit attended the 2016 South Pacific and Asia Conference of Internal Auditors - hosted by IIA - Australia in Brisbane. • CBSI received application from Bred Solomons to establish a bank in Solomon Islands • CBSI performed an onsite prudential examination of Royal Solomon Islands Police Credit Union Limited
• April	<ul style="list-style-type: none"> • Chief Manager Financial Market Supervision participated in an IMF-STI course on Macro-Financial Surveillance in Singapore • Senior Analyst Credit Union participated in Implementing the International AML/CFT workshop in Singapore • Advisor to the Governor's Office attended AFI's FISPLG work group meeting in Dar es salaam, Tanzania.
• May	<ul style="list-style-type: none"> • CBSI grants a 12-month Interim Banking License to Bred Solomons • Manager Financial Market Supervision participated in onsite examination of ANZ (Fiji) Bank in Suva, Fiji.
• June	<ul style="list-style-type: none"> • CBSI celebrated 40th Year Anniversary with the theme: Celebrate past success, harsh the future". • Global Money Day and Solomon Islands Money celebrated by National Financial Inclusion partners and six commercial banks adopted primary schools in Honiara on the theme, "Take Part Save Smart" to highlight the need for financial education in primary schools. • Chief Manager Financial Market Supervision attended annual meeting of Association of Financial Supervisors of Pacific Countries in Koror, Palau • Manager Applied Research, Policy and Regulation within Financial Market Supervision participated in regional seminar on Electronic Banking and Mobile Financial Services in Bangkok, Thailand • Advisor and Chief Manager Economics, Research, and Statistics attended the South Pacific Central Banking Symposium in Brisbane, hosted by Griffith University.
• July	<ul style="list-style-type: none"> • Deputy Governor & Chief Manager, Economics Research Statistics Department attended the 8th Australia Solomon Islands Business Forum in Brisbane, Australia. • Manager Financial Market Supervision and Analyst Insurance participated in prudential review of an insurance service provider in Dili, Timor Leste
• August	<ul style="list-style-type: none"> • Senior Research and Policy Development officer within Financial Market Supervision undertook one-month policy development internship with Australian Prudential Regulatory Authority in Sydney, Australia • CBSI, along with APRA and financial sector supervisors of Cook Islands, Papua New Guinea, Samoa, Timor Leste and Vanuatu performed an onsite examination of Bank South Pacific
• September	<ul style="list-style-type: none"> • Governor and Deputy Governor led a team of CBSI officers, a representative from the Ministry of Commerce Industries Labour & Immigration and a representative of SIWBA to attend the Alliance for Financial Inclusion (AFI) Global Policy Forum in Denarau, Fiji. • CBSI Board issued its midyear Monetary Policy stance choosing to remain with the accommodative stance. • SINTA Credit Union reviewed with Technical Assistance from PFTAC advisor. • Governor, Chief Manager Financial Market Supervision and Senior Analyst Banking attended annual Bank South Pacific College meeting in Port Moresby, Papua New Guinea • CBSI conducted an onsite examination on QBE Insurance
• October	<ul style="list-style-type: none"> • Deputy Governor attended NZ-OECD Global Symposium on Financial Education in Auckland, New Zealand. • CBSI receives banking license application from Expire Solomons Bank
• November	<ul style="list-style-type: none"> • Governor and Chief Manager Financial Market Supervision participated in forum on Strengthening Pension System in the Pacific in Suva, Fiji • Governor, Policy Adviser, and Chief Manager, Financial Market Supervision Department attended South Pacific Governors Conference in Delo, Temor Leste • Ministry of Commerce, Industries, Labour and Immigration and CBSI launched Micro, Small, Medium Enterprise Business Loan Scheme. • Manager Financial Market Supervision attended Maximizing the Power of Financial Access and Optimal Balance Between Financial Inclusion and Financial Stability in Bali • Manager International and Investment officer attended BIS Reserves management Workshop in Hong Kong, BIS Asia Region Office.
• December	<ul style="list-style-type: none"> • CBSI Board declined application from Empire Solomon Bank to establish banking business in Solomon Islands • Senior Analyst Insurance and Analyst Insurance within Financial Market Supervision attended a workshop on Risk Based Supervision, Risk Management and Disaster Insurance for SMEs and Agro-Business in Sydney, Australia • Senior Analyst Banking and Analyst Superannuation Fund within Financial Market Supervision participated in IMF-STA Workshop on Financial Soundness Indicators. • Chief Manager International attended Sixth IMF Roundtable of Official Asset Managers meeting in IMF Washington DC, USA and Brief Official Visit to Federal Reserve Bank in New York USA.



CENTRAL BANK OF SOLOMON ISLANDS

DIRECTORS' REPORT

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DIRECTORS' REPORT

The Directors present their report together with the financial statements of the Central Bank of the Solomon Islands ("the Bank") for the year ended 31 December 2016 and the auditors' report thereon.

DIRECTORS

The Directors in office during the financial year and at the date of this report were:

- Denton Rarawa (Chairman and Governor)
- Gane Simbe (Deputy Governor)
- Harry D Kuma (appointed 13 May 2015)
- Sir Thomas Ko Chan (appointed on 3 August 2015)
- Loyley Ngira (contract end on 5 February 2016)
- Lily Lomulo (contract end on 5 February 2016)
- John Usuramo (appointed on 18 December 2013)
- Tele Barttlet (contract end on 17 July 2016)
- Primo Afeau (contract end on 17 July 2016)
- David K C Quan (appointed on 17 August 2016)
- Leslie Teama (appointed on 17 August 2016)

STATE OF AFFAIRS

In the opinion of the Directors:

- there were no significant changes in the state of affairs of the Bank during the financial year under review not otherwise disclosed in this report or the financial statements;
- the accompanying statement of financial position gives a true and fair view of the state of affairs of the Bank as at 31 December 2016 and the accompanying statement of profit and loss and other comprehensive income, statement of changes in equity and statement of cash flows give a true and fair view of the results, of the Bank for the year then ended.

PRINCIPAL ACTIVITIES

The Bank's role as a central bank, as defined in the Central Bank of Solomon Islands Act, 2012 is:

- (a) to achieve and to maintain domestic price stability;
- (b) to foster and to maintain a stable financial system;
- (b) to support the general economic policies of the government.

RESULTS

The net loss of the Bank for the year ended 31 December 2016 was \$42.5m (2015: \$44.31m profit).

RESERVES

The Board approved the following transfers of reserves in the statement of profit and loss and other comprehensive income during the year:

- (\$66.35m) (2015: \$26.10m) to the foreign exchange revaluation reserve; and
- \$23.84m (2015: \$17.61m) to the general reserve.

PROVISIONS

There were no material movements in provisions during the year apart from the normal amounts set aside for such items as depreciation and employee entitlements.

GOING CONCERN

The Board believes that the Bank will continue to operate as a going concern.

ASSETS

The Directors took reasonable steps before the Bank's financial statements were made out to ascertain that the assets of the Bank were shown in the accounting records at a value equal to or below the value that would be expected to be realised in the ordinary course of business.

At the date of this report, the Directors were not aware of any circumstances which would render the values attributable to the assets in the financial statements misleading.

DIRECTORS' BENEFIT

No director of the Bank has, since the last financial year, received or become entitled to receive a benefit (other than a benefit included in the total amount of emoluments received or due and receivable by directors shown in the Bank's financial statements) by reason of a contract made with the Bank or a related corporation with the director or with a firm of which he is a member, or in a Bank in which he has a substantial financial interest.

UNUSUAL TRANSACTIONS

Apart from these matters and other matters specifically referred to in the financial statements, in the opinion of the Directors the results of the operations of the Bank during the financial year were not substantially affected by any item, transaction or event of a material unusual nature, nor has there arisen between the end of the financial year and the date of this report any item, transaction or event of a material unusual nature likely, in the opinion of the Directors, to affect substantially the results of the operations of the Bank in the current financial year.

EVENTS SUBSEQUENT TO BALANCE DATE

There has not arisen in the interval between the end of the financial year and the date of this report any item, transaction or event of a material and unusual nature likely, in the opinion of the directors of the Bank, to affect significantly the operations of the Bank, the results of those operations, or the state of affairs of the Bank, in future financial years.

OTHER CIRCUMSTANCES

At the date of this report, the Directors are not aware of any circumstances not otherwise dealt with in this report or financial statements which render amounts stated in the financial statements misleading.

Dated at Honiara this twentieth day of April 2016.

Signed in accordance with a resolution of the Board of Directors:



Denton Rarawa
Chairman of the Board and Governor



Harry Kuma
Director

STATEMENT BY DIRECTORS

In the opinion of the Directors:

- (a) the accompanying statement of profit and loss and other comprehensive income is drawn up so as to give a true and fair view of the results of the Bank for the year ended 31 December 2016;
- (b) the accompanying statement of financial position is drawn up so as to give a true and fair view of the state of affairs of the Bank as at 31 December 2016;
- (c) the accompanying statement of changes in equity is drawn up so as to give a true and fair view of the changes in equity of the Bank for the year ended 31 December 2016;
- (d) the accompanying statement of cash flows is drawn up so as to give a true and fair view of the cash flows of the Bank for the year ended 31 December 2016;
- (e) at the date of this statement there are reasonable grounds to believe the Bank will be able to pay its debts as and when they fall due;
- (f) all related party transactions have been adequately recorded in the books of the Bank, and
- (g) the financial statements have been properly prepared in accordance with International Financial Reporting Standards ("IFRS") and Central Bank Solomon Islands Act 2012 ("Act 2012").

For and on behalf of the Board of Directors by authority of a resolution of the Directors this 20th of April 2017.



Denton Rarawa
Chairman of the Board and Governor



Harry Kuma
Director

INDEPENDENT AUDITOR'S REPORT TO THE BOARD OF DIRECTORS OF CENTRAL BANK OF SOLOMON ISLANDS

SOLOMON ISLANDS OFFICE OF THE AUDITOR-GENERAL



Report on the financial Statements

Opinion

I have in joint consultation with the Board of Directors ("the Board") of the Bank pursuant to Section 60(1) of the *Central Bank of Solomon Islands Act 2012* contracted KPMG Fiji which is part of the KPMG International network to assist me to audit the accompanying financial statements of Central Bank of Solomon Islands ("the Bank"), which comprise the statements of financial position as at 31 December 2016, the statements of profit or loss and other comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising significant accounting policies and other explanatory information as set out in notes 1 to 27.

In my opinion, the accompanying financial statements give a true and fair view of the financial position of the Bank as at 31 December 2016, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS).

Emphasis of matter

As at 31 December 2016, the Bank's total assets amounted to \$4.666 billion. This was less than the sum of the Bank's total monetary liabilities and its unimpaired capital which total \$4.727 billion. These conditions have arisen from the Bank's large open position in foreign currency which is subject to foreign exchange rate movements.

Under section 56 of the *Central Bank of Solomon Islands Act 2012*, the Bank will be required to inform the Minister for Finance within 30 days of this report of the reasons for this shortfall and request a capital contribution to remedy the shortfall.

Without further modifying my opinion, I draw attention to Note 2 (b) in the financial statements which indicates that the bank had a deficiency in net assets of \$11.4 million as at 31 December 2016. These conditions indicate the existence of a material uncertainty which the Bank must address under Section 56 of the *Central Bank of Solomon Islands Act 2012* through a request to the Minister of Finance for capital contribution by the Government to remedy the deficit and maintain reputable going concern.

Basis for Opinion

I conducted the audit in accordance with International Standards on Auditing (ISAs). My responsibilities under those standards are further described in the *Auditors' Responsibilities for the Audit of the Financial Statements* section of my report. I am independent of the Bank in accordance to the ethical requirements that are relevant to my audit of the financial statements and I have fulfilled my other ethical responsibilities in accordance with these requirements. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management are responsible for the preparation and fair presentation of the financial statements in accordance with IFRS and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management are responsible for assessing the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Bank or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Bank's financial reporting process.

Auditors' Responsibilities for the Audit of the Financial Statements

My objective is to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with International Standards on Auditing (ISAs) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISAs, I exercise professional judgment and maintain professional skepticism throughout the audit. I also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Banks's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditors' report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify my opinion. My conclusion is based on the audit evidence obtained up to the date of my auditor's report.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

I communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that I identified during my audit.

Report on Other Legal and Regulatory Requirements

I have obtained all the information and explanations which, to the best of my knowledge and belief, were necessary for the purposes of my audit.

In my opinion:

- i) proper books of account have been kept by the Bank, sufficient to enable financial statements to be prepared, so far as it appears from my examination of those books; and
- ii) to the best of my knowledge and according to the information and explanations given to me the financial statements give the information required by the Central Bank of Solomon Islands Act 2012, in the manner so required.



PETER LOKAY
Auditor-General

Office of the Auditor-General
Honiara, Solomon Islands

28 April, 2016

**STATEMENT OF PROFIT AND LOSS AND OTHER COMPREHENSIVE INCOME
FOR THE YEAR ENDED 31 DECEMBER 2016**

	Note	2016 \$000	2015 \$000
Income			
Interest income	4(a)	41,444	39,844
Fees and commission income	4(b)	38,859	43,898
Other income	4(c)	6,153	4,695
Change in fair value of investment properties	10	-	600
Net unrealized foreign exchange revaluation gain		-	26,101
Total income		<u>86,456</u>	<u>115,138</u>
Expenses			
Interest expense	4(d)	5,058	12,463
Fees and commission expense		1,684	1,221
Administration expenses	4(e)	33,999	34,919
Other expenses	4(f)	21,873	22,227
Net unrealized foreign exchange revaluation loss		66,346	-
Total expenses		<u>128,960</u>	<u>70,830</u>
Net operating (loss)/profit		<u>(42,504)</u>	<u>44,308</u>
Other comprehensive losses			
Net change in fair value (available - for - sale financial assets)		-	14,626
Net change in revaluation (property, plant and equipment)		17,869	(26,890)
Total other comprehensive (loss)/income		<u>17,869</u>	<u>(12,264)</u>
Total comprehensive (loss)/ income		<u>(24,635)</u>	<u>32,044</u>


Chairperson and Governor


Director

This statement of profit and loss and other comprehensive income is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 44 to 62

**STATEMENT OF FINANCIAL POSITION
AS AT 31 DECEMBER 2016**

	Note	2016 \$000	2015 \$000
Foreign currency assets			
Cash at bank	20	1,048,532	781,517
Accrued interest		5,320	6,495
Held-to-maturity investments	5	2,859,056	3,094,483
Available-for-sale investments	6	225,460	206,921
International Monetary Fund	7	263,467	206,302
Total foreign currency assets		<u>4,401,835</u>	<u>4,295,718</u>
Local currency assets			
Cash on hand	20	202	196
Loans and advances	8	12,261	11,629
Currency inventory	9	36,116	36,623
Investment properties	10	13,262	13,262
Property, plant and equipment	12	149,644	150,180
Other assets	11	52,334	4,516
Total local currency assets		<u>263,819</u>	<u>216,406</u>
Total assets		<u>4,665,654</u>	<u>4,512,124</u>
Foreign currency liabilities			
International Monetary Fund	7	390,348	324,646
Demand deposits	13(a)	59,202	16,240
Total foreign currency liabilities		<u>449,550</u>	<u>340,886</u>
Local currency liabilities			
Demand deposits	13(b)	2,519,783	2,573,231
Currency in circulation	14	868,395	776,640
Fixed deposits	15	761,658	721,677
SIG monetary operations account	16	51,359	58,422
Employee entitlements	17	15,671	17,000
Other liabilities	18	10,628	11,025
Total local liabilities		<u>4,227,494</u>	<u>4,157,995</u>
Total liabilities		<u>4,677,044</u>	<u>4,498,881</u>
Net assets		<u>(11,392)</u>	<u>13,243</u>
Capital and reserves			
Paid up capital	21	50,000	50,000
General reserve	22(a)	77,021	53,179
Foreign exchange revaluation reserve	22(b)	(214,677)	(148,331)
Asset revaluation reserve	22(c)	104,318	104,318
Gold revaluation reserve	22(d)	(89,929)	(107,798)
Capital asset reserve	22(e)	61,875	61,875
Total (deficiency)/surplus in capital and reserves		<u>(11,392)</u>	<u>13,243</u>

Signed in accordance with the resolution of the Board of Directors:


Denton Rarawa
Chairperson of the Board and Governor


Harry Kuma
Director

This statement of profit and loss and other comprehensive income is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 44 to 62

STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 31 DECEMBER 2016

	Issued & paid up capital \$000	Gold revaluation reserve \$000	General reserve \$000	Foreign exchange assets revaluation reserve \$000	Asset revaluation reserve \$000	Capital assets reserve \$000	Total \$000
Balance as at 1 January 2015	50,000	(80,908)	35,572	(174,432)	89,092	61,875	(18,801)
Total comprehensive income for the year							
Profit (loss) for the year (Note 19)	-	-	17,607	26,101	600	-	44,308
<i>Other comprehensive income/(losses)</i>							
Fair value gains - gold	-	(26,890)	-	-	-	-	(26,890)
Fair value gains - Property, plant and equipment	-	-	-	-	14,626	-	14,626
Total other comprehensive income/(losses)	-	(26,890)	17,607	26,101	15,226	-	32,044
Balance as at 31 December 2015	50,000	(107,908)	53,179	(148,331)	104,318	61,875	13,243
Balance at 1 January 2016	50,000	(107,908)	53,179	(148,331)	104,318	61,875	13,243
Total comprehensive income for the year							
Profit (loss) for the year (Note 19)	-	-	23,842	(66,346)	-	-	(42,504)
<i>Other comprehensive income/(losses)</i>							
Fair value losses - gold	-	17,869	-	-	-	-	17,869
Fair value gain - Property, plant and equipment	-	-	-	-	-	-	-
Total comprehensive income/(losses)	-	17,869	23,842	(66,346)	-	-	(24,635)
Balance as at 31 December 2016	50,000	(89,929)	77,021	(214,677)	104,318	61,875	11,392

This statement of profit and loss and other comprehensive income is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 44 to 62

STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 31 DECEMBER 2016

	Note	2016 \$000	2015 \$000
Operating activities			
Interest received		42,666	38,500
Other income		45,013	48,494
Interest paid		(4,943)	(12,427)
Cash paid to suppliers and employees		(55,549)	(57,050)
Net movement in held to maturity investments		235,427	(209,933)
Net movement in International Monetary Fund accounts		33,759	(1,160)
Net movement in other receivables		(45,819)	38,990
Net movement in other payables		-	4,945
Cash flows used in operating activities		<u>250,554</u>	<u>(149,641)</u>
Investing activities			
Acquisition of property, plant and equipment		(4,803)	(2,777)
Proceeds from sale of premises, plant and equipment		-	99
Net movement in available-for-sale investments		(670)	(12,443)
Net movement in loan to government		(27)	63,950
Net movement in loans and advances to staff		(652)	(280)
Cash flows used in investing activities		<u>(6,152)</u>	<u>48,549</u>
Financing activities			
Net movement in currency in circulation		91,754	82,297
Net movement in demand deposits		(10,485)	96,270
Net movement in fixed deposits received		39,981	99,948
Solomon Islands government monetary operations		(7,063)	28,207
Net movement in International Monetary Fund credit facilities		(25,222)	(26,965)
Cash flows (used in)/from financing activities		<u>88,965</u>	<u>279,757</u>
Net effect of exchange rates		<u>(66,346)</u>	<u>26,101</u>
Net increase/(decrease) in cash		267,021	204,766
Cash and cash equivalents at the beginning of the financial year		<u>781,713</u>	<u>576,947</u>
Cash and cash equivalents at the end of the financial year	20	<u>1,048,734</u>	<u>781,713</u>

This statement of profit and loss and other comprehensive income is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 44 to 62

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2016

1. Principal activities and principal place of operations

The Central Bank of Solomon Islands ("the Bank") operates under the Central Bank of Solomon Islands Act, 2012. The Bank is an independent legal entity wholly owned by, and reporting to, the Government of the Solomon Islands. The Bank's primary objective as defined in the Central Bank of Solomon Islands Act, 2012, Section 8 is:

- (a) to achieve and to maintain domestic price stability;
- (b) to foster and to maintain a stable financial system;
- (c) to support the general economic policies of the government.

The Bank's principal place of operations is located at Mud Alley Street, Honiara, Solomon Islands.

The financial statements were authorised for issue by the Board of Directors on 20th April 2017.

2. Basis of preparation

(a) Statement of compliance

The financial statements of the Bank have been prepared in accordance with International Financial Reporting Standards ('IFRS') and the Central Bank of Solomon Islands Act, 2012, except where the Central Bank of Solomon Islands Act 2012, requires different treatment in which case the Central Bank of Solomon Islands Act, 2012 takes precedence.

The Bank will comply with the requirements of the Central Bank of Solomon Islands Act (Section 56) which requires that in the event that the value of its assets falls below the sum of its monetary liabilities and its unimpaired authorised capital, then –

- (a) The Board, with the advice of the external audit of the Bank, shall assess the situation and prepare a report on the causes and extent of the shortfall and assess the situation within a period of no more than 30 calendar days;
- (b) If the Board approves the report under paragraph (a), the Bank shall request the Minister of Finance for a capital contribution to be made by the Government to remedy the deficit; and
- (c) Upon receipt of this request the Government shall, within a period of no more than 30 calendar days, transfer to the Bank the necessary amount in currency or in negotiable debt instruments with a specified maturity issued at market-related interest rates prevailing in Solomon Islands.

As at 31 December 2016, the Bank's total assets amounted to \$4.67 billion. This was less than the sum of the Bank's total monetary liabilities and its unimpaired capital which totalled \$4.73 billion. The Bank had requested the Ministry of Finance for a capital contribution during the year to remedy the prior year deficit but the request had been repudiated. An emphasis of matter has been included in the audit report relating to this matter.

(b) Going concern basis of accounting

The financial statements have been prepared on a going concern basis, and as at 31 December 2016 the Bank had a deficiency in net assets of \$11.4 million.

The Bank's deficiency in net assets had implicate materiality on its going concern and requires reliable support of the Solomon Islands Government. These conditions indicate the existence of a material uncertainty which the Bank will address to maintain a reputable going concern.

The Board consider it appropriate to prepare these financial statements on a going concern basis and as provided for by section 56 of the Central Bank of Solomon Islands Act 2012 the Bank will again request through the Minister of Finance for capital contribution by the Government to remedy the deficit.

The financial statements do not include any adjustments relating to the recoverability or classification of recorded asset amounts and classification of liabilities that might be necessary should the Bank be unable to continue as a going concern.

(c) Basis of measurement

The financial statements have been prepared on the historical cost basis and do not take into account changes in money values except for the following material items in the statement of financial position.

- Available-for-sale financial assets are measured at fair value.
- Held to maturity financial assets are measured at amortised cost.
- Land and buildings classified as property, plant and equipment are measured at fair value.
- Investment properties are measured at fair value.

(d) Functional and presentation currency

The financial statements are presented in Solomon Islands dollars, which is the Bank's functional currency. All financial information presented in Solomon Islands dollars has been rounded to the nearest thousand except when otherwise indicated.

(e) Use of estimates and judgement

The preparation of the financial statements in conformity with IFRS requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revision to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2016

The estimates and assumptions that have a significant risk of causing material adjustment to the carrying amount of assets and liabilities within the next financial year are discussed in the following paragraphs;

Impairment of financial assets

A financial asset not carried at fair value through profit or loss is assessed at each reporting date to determine whether there is objective evidence that it is impaired. A financial asset is impaired if objective evidence indicates that a loss event has occurred after the initial recognition of the asset, and that the loss event had a negative effect on the estimated future cash flows of that asset that can be estimated reliably.

Objective evidence that financial assets are impaired can include default or delinquency by a debtor, restructuring of an amount due to the Bank on terms that the Bank would not consider otherwise, indications that a debtor or issuer will enter into bankruptcy, adverse changes in the payment status of borrowers or issuers in the Bank, economic conditions that correlate with defaults or the disappearance of an active market for a security.

3. Statement of significant accounting policies

The accounting policies set out below have been applied consistently to all periods presented in the financial statements.

(a) Foreign currency

Transactions in foreign currencies are translated into the functional currency of the Bank at the spot exchange rates at the date of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the spot exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between amortised cost in the functional currency at the beginning of the year, adjusted for effective interest and payments during the year, and the amortised cost in foreign currency translated at the spot exchange rate at the end of the year.

Non-monetary items that are measured based on historical cost in a foreign currency are translated using the spot exchange rate at the date of transaction.

Foreign currency differences arising on retranslation are recognised in profit or loss.

(b) Interest

Interest income and expense are recognised in profit or loss using the effective interest method. The effective interest rate is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial asset or liability (or, where appropriate, a shorter period) to the carrying amount of the financial asset or liability. When calculating the effective interest rate, the Bank estimates future cash flows considering all contractual terms of the financial instrument, but not future credit losses.

The calculation of the effective interest rate includes all transaction costs and fees paid or received that are an integral part of the effective interest rate. Transaction costs include incremental costs that are directly attributable to the acquisition or issue of a financial asset or liability.

Interest income and expense presented in the statement of profit and loss and other comprehensive income include:

- Interest on financial assets and financial liabilities measured at amortised cost calculated on an effective interest basis; and
- Interest on available-for-sale investments securities calculated on effective interest basis.

(c) Fees and commission

Fees and commission income and expense relate mainly to transaction and service fees, which are recognised as revenue when services are rendered or expensed as the services are received.

(d) Other income

Other income are brought to account on an accrual basis.

(e) Tax expense

The Bank is exempted from income tax under the Income Tax (Central Bank of Solomon Islands) (Exemption) Order of 21st June 1976 as provided for under Section 16 (2) of the Income Tax Act (CAP 123).

(f) Financial assets and financial liabilities

i. Recognition

The Bank initially recognises loans and advances, deposits and debt securities on the date that they are originated. All other financial assets and liabilities are recognised initially on the trade date, which is the date that the Bank becomes a party to the contractual provisions of the instrument.

A financial asset or financial liability is measured initially at fair value plus, for an item not at fair value through profit or loss, transaction costs that are directly attributable to its acquisition or issue.

ii. Classification

Financial assets

The Bank classifies its financial assets in one of the following categories:

- loans and advances;
- held to maturity;
- available-for-sale.

Financial liabilities

The Bank classifies its financial liabilities as measured at amortised cost.

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2016

iii. Derecognition

Financial assets

The Bank derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire, or it transfers the rights to receive the contractual cash flows in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred or in which the Bank neither transfers nor retains substantially all the risks and rewards of ownership and it does not retain control of the financial asset. Any interest in such transferred financial assets that qualify for derecognition that is created or retained by the Bank is recognised as a separate asset or liability. On derecognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset transferred), and the sum of (i) the consideration received (including any new asset obtained less any new liability assumed) and (ii) any cumulative gain or loss that had been recognised in other comprehensive income is recognised in profit or loss.

Financial liabilities

The Bank derecognises a financial liability when its contractual obligations are discharged, cancelled or expire.

iv. Amortised cost measurement

The amortised cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment.

v. Fair value measurement

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction on the measurement date.

The Bank measures the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded as active if quoted prices are readily and regularly available and present actual and regularly occurring market transactions on an arm's length basis.

Assets are measured at a bid price, while liabilities are measured at an asking price. Fair values reflect the credit risk of the instrument and include adjustments to take account of credit risk of the Bank.

(g) Cash and cash equivalents

Cash and cash equivalents include notes and coins held by the Bank, teller's cash, current accounts with a maturity of three months or less from the acquisition date and other short term highly liquid term deposits.

Cash and cash equivalents are carried at amortised costs in the statement of financial position.

(h) Held-to-maturity

Held-to-maturity investments are non-derivative assets with fixed or determinable payment and fixed maturity that the Bank has the positive intent and ability to hold to maturity. Held-to-maturity investments comprise of fixed term deposits, short term commercial papers and bonds.

Held-to-maturity investments are carried at amortised costs using the effective interest method less any impairment losses. A sale or reclassification of more than an insignificant amount of held-to-maturity investments prior to maturity would result in the reclassification of all held-to-maturity investments as available for sale, and would prevent the Bank from classifying investment securities as held to maturity for the current and the following two financial years.

(i) Available-for-sale

Available-for-sale investments are non-derivative investments that are designated as available-for-sale or are not classified as another category of financial assets. Available-for-sale investments comprise of gold holdings and are carried at fair value.

Fair value changes other than impairment losses are recognised in other comprehensive income and presented in the gold revaluation reserve in equity. When the investment is sold, the gain or loss accumulated in equity is reclassified to profit or loss. Impairment losses are recognised in profit or loss.

(j) Loans and advances

Loans and advances are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and that the Bank does not intend to sell immediately or in the near term. Loans and advances comprise of loans and advances to the Solomon Islands Government and staff loans.

Loans and advances are initially measured at fair value plus incremental direct transaction costs, and subsequently measured at their amortised costs using the effective interest method.

(k) Currency Inventory

Currency inventory are recognised in the statement of financial position at cost.

Currency inventory relates to notes and coins purchased for circulation. The amount expensed in profit or loss is based on the cost of notes and coins that are issued into circulation.

(l) Currency in circulation

Currency issued by the Bank represents a claim on the Bank in favour of the holder. Currency in circulation comprises notes and coins issued by the Bank and the liability for currency in circulation is recorded at face value in the statement of financial position.

(m) Property, plant and equipment

Recognition and measurement

Certain items of property, plant and equipment are initially measured at cost less accumulated depreciation and any accumulated

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2016

impairment losses. Land and buildings are initially recognised at cost less accumulated depreciation and subsequently revalued to fair value.

Costs includes expenditure that is directly attributable to the acquisition of the asset. Purchased software that is integral to the functionality of the related equipment is capitalised as part of that equipment.

Any gain or loss on disposal of property, plant and equipment (calculated as the difference between the net proceeds from disposal and the carrying amount of the asset at the time of disposal) is recognised within other income in profit or loss.

Subsequent costs

Subsequent expenditure is capitalised only when it is probable that the future economic benefits of the expenditure will flow to the Bank. Ongoing repairs and maintenance are expensed as incurred.

Depreciation

Items of property, plant and equipment are depreciated from the date they are available for use. Depreciation is charged on a straight line basis over the estimated useful lives of the assets. The rates of depreciation used are based on the following estimated useful lives:

Buildings	4 - 55 years
Computers	3 years
Furniture, plant and equipment	3 - 5 years
Motor vehicles	4 years

Periodic revaluation

The Board has determined that apart from land and buildings, the remaining fixed assets of the Bank are recorded at values approximating recoverable market values. With Board approval, a three year periodical revaluation of its land and buildings was first done in 2012 and recently done in 2015. This included a review of the asset classes, estimated useful lives and depreciation rates, and current market values where deemed appropriate. The basis of this valuation is the open market value, that is, the highest and best value the property would expect to be realised for, if put for sale on private treaty. The Board proposes to have such assets revaluation every three years. The next revaluation will be done in 2018.

(n) Investment property

Investment property, is property held either to earn rentals or for capital appreciation or for both. Investment property is initially measured at cost and subsequently at fair value with any change therein recognised in profit or loss. Costs include expenditure that is directly attributable to the acquisition of the investment property.

Any gain or loss on disposal of an investment property (calculated as the difference between the net proceeds from disposal and the carrying amount of the item) is recognised in profit or loss. When an investment property that was previously classified as property, plant and equipment is sold, any related amount included in the revaluation reserve is transferred to retained earnings.

When the use of the property changes such that it is reclassified as property, plant and equipment, its fair value at the date of the reclassification becomes its cost for subsequent accounting.

(o) Demand deposits

Demand deposits represent funds placed with the Bank by financial institutions and other organisations. Demand deposits are initially measured at fair value minus incremental direct transaction costs, and subsequently measured at their amortised cost using the effective interest method. These deposits are at call.

(p) Employee entitlements

Short-term employee benefits

Short-term employee benefits comprising of accrued wages and salaries, annual leave and entitlement to Solomon Islands National Provident Fund are measured on an undiscounted basis and are expensed as the related service is provided.

Liabilities recognised in respect of short-term employee benefits expected to be settled within 12 months, are measured at their nominal values using the remuneration rate expected to apply at the time of settlement.

Long-term employee benefits

Long-term employee benefits comprises of long service leave and early retirement benefit.

Liabilities recognised in respect of long-term employee benefits which are not expected to be settled within 12 months are measured at the present value of the estimated future cash outflows to be made resulting from employee's service provided to balance date, based on staff turnover history and is discounted using the rates attaching to the external bonds portfolio.

(q) Impairment

The carrying amounts of the Bank's assets are reviewed at balance date to determine whether there is any indication of impairment. If any such indication exists, the assets recoverable amount is estimated. An impairment loss is recognised whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. Impairment losses are recognised in profit or loss.

(r) Comparative figures

Where necessary, comparative figures have been changed to conform to changes in presentation in the current year.

(s) New standards and interpretations not yet adopted

IFRS 9 'Financial instruments', published in July 2014, replaces the existing guidance in IAS 39 'Financial Instruments: Recognition and Mea-

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2016

surement'. IFRS 9 includes revised guidance on the classification and measurement of financial instruments, including a new expected credit loss model for calculating impairment on financial assets, and the new general hedge accounting requirements. It also carries forward the guidance on recognition and de-recognition of financial instruments from IAS 39. The standard is effective for annual reporting periods beginning on or after 1 January 2018, with early adoption permitted.

IFRS 16 'Leases', removes the classification of leases as either operating leases or finance leases – for the lessee – effectively treating all leases as finance leases. Short-term leases (less than 12 months) and leases of low-value assets (such as personal computers) are exempt from the lease accounting requirements. There are also changes in accounting over the life of the lease. In particular, companies will now recognise a front-loaded pattern of expense for most leases, even when they pay constant annual rentals. Lessor accounting remains similar to current practice – i.e. lessors continue to classify leases as finance and operating leases. The standard is effective for annual reporting periods beginning on or after 1 January 2019, with early adoption permitted.

IFRS 15 Revenue from Contracts with Customers was issued in 2014 by IASB. The standard is not mandatorily effective for the Bank until 1 January 2018. IFRS 15 contains new requirements for the recognition of revenue and additional disclosures about revenue. It is expected that a significant proportion of the Bank's revenue will be outside the scope of IFRS 15.

	2016 \$000	2015 \$000
4. Income and expenses		
(a) Interest income		
Overseas investments	41,214	38,371
Local investments	230	1,473
	<u>41,444</u>	<u>39,844</u>
(b) Fees and commission income		
Foreign currency dealings	38,283	43,249
Local dealings	576	649
	<u>38,859</u>	<u>43,898</u>
(c) Other income		
Gain on disposal of fixed assets	1	99
Rent received	882	1,075
Sale of numismatic coins	78	80
Gains on foreign currency exchange	-	1,016
Royalties on numismatics	4,239	2,301
Others	953	124
	<u>6,153</u>	<u>4,695</u>
(d) Interest expense		
Foreign liabilities	66	57
Local liabilities	4,992	12,406
	<u>5,058</u>	<u>12,463</u>
(e) Administrative expenses		
Staff costs	23,516	25,012
Telecommunication	1,785	1,727
Utilities	2,101	1,801
Repairs and maintenance	3,021	2,304
Insurance	516	441
Consumables	424	430
Stationery, printing and postage	490	478
Consultancy	452	1,351
Other	1,694	1,375
	<u>33,999</u>	<u>34,919</u>

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2016

	2016	2015
	\$'000	\$'000
(f) Other expenses		
Board of directors remunerations and expenses	161	326
Currency expenses	11,569	14,952
Depreciation	5,339	5,335
Auditors remuneration	300	330
Other	4,504	1,284
	<u>21,873</u>	<u>22,227</u>
5. Held-to-maturity investments		
Fixed term deposits	2,680,828	2,828,000
Short term commercial paper	57,990	175,294
Bonds	120,238	91,189
	<u>2,859,056</u>	<u>3,094,483</u>
6 Available-for-sale investments		
Unallocated gold - at fair value	109,285	100,299
Gold bullion - at fair value	116,175	106,622
	<u>225,460</u>	<u>206,921</u>

7. International Monetary Fund

The Solomon Islands is a member of the International Monetary Fund (IMF) and the Central Bank of Solomon Islands has been designated as the Government of Solomon Islands' fiscal agency (through which the Government deals with the IMF) and as the depository for the IMF's holding in Solomon Islands dollars.

The Solomon Islands subscription to the IMF has been met by:

- (i) payment to the IMF out of the Central Bank's external assets which have been reimbursed by the Government of Solomon Islands by issue of non-interest bearing securities;
- (ii) the funding of accounts in favor of the IMF in the books of the Central Bank by the Government of Solomon Islands.
- (iii) The liabilities to the IMF include subscriptions which are maintained in the IMF No.1 and IMF No. 2 accounts, are disclosed together as capital subscription. The IMF maintains such balances in their accounts in both Special Drawing Rights (SDR) and Solomon Islands dollar equivalents; the Bank balances are maintained only in Solomon Islands dollars.

The standby credit facility with IMF commenced in 2010 with first disbursement received 23 June 2010. The final disbursement was transacted on the 1st December 2011.

The extended credit facility with IMF was approved and drawn down on 11th December 2012.

IMF related assets and liabilities

	2016	2015
	\$'000	\$'000
Foreign currency assets		
- Reserve tranche position	34,155	5,981
- Special drawing rights	37,944	93,243
- Currency subscription	191,368	107,078
	263,467	<u>206,302</u>
Foreign currency liabilities		
- Standby credit facility	73,069	101,753
- Special drawing rights allocation	109,918	107,714
- Extended credit facility	11,537	8,076

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2016

	2016	2015
	\$000	\$000
- Securities	190,895	102,388
- Capital subscription	4,929	4,715
	<u>390,348</u>	<u>324,646</u>

8. Loans and advances

Solomon Islands Government

Loans and advances	46	46
Development bonds	27	27
Treasury bills	10	30
Other securities	4,936	4,936
Amortising bonds	-	-
	<u>5,019</u>	<u>5,039</u>

Staff loans

Staff housing loans	5,780	5,039
Management car loans	512	453
Personal loans	950	1,044
	<u>7,242</u>	<u>6,590</u>
	<u>12,261</u>	<u>11,629</u>

9. Currency inventory

Notes	11,164	11,339
Coins	24,952	25,284
	<u>36,116</u>	<u>36,623</u>

10. Investment properties

Balance at beginning of financial year- at fair value	12,262	12,662
Add: Changes in fair value	-	600
Balance at end of financial year- at fair value	<u>13,262</u>	<u>13,262</u>

Investment property comprises of a commercial and a residential property that are leased to third parties. Each lease contains a lease period of 3 and 2 years respectively with annual rental subject to increase upon renewal indexed to the Honiara retail price index. Subsequent renewals are negotiated with the lessee.

When rent reviews or lease renewals have been pending with anticipated reversionary increases, all notices, when appropriate counter-notices, have been served validly and within the appropriate time.

Rental income from investment properties of \$881,845 (2015: \$1,075,000) has been recognised in other income.

Fair value hierarchy

The fair value of investment property and land and building (refer to note 12) was determined by an external, independent property valuer, having appropriate recognised professional qualifications and recent experience in the location and category of the property being valued. The independent valuer provides the fair value of the Bank's investment property portfolio on a regular basis.

The fair value of the Bank's investment property are categorised into Level 3 of the fair value hierarchy.

Valuation techniques and significant unobservable inputs

The following table shows the valuation technique used in measuring the fair value of investment properties, as well as significant unobservable inputs used.

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2016

Valuation technique	Significant unobservable inputs	Inter-relationship between key unobservable inputs and fair value measurement
Replacement cost method: where the improvements are valued using current replacement cost and an allowance for depreciation and obsolescence plus the freehold value of the land (notable sales of comparable vacant sites within Honiara are noted).	<ul style="list-style-type: none"> • Depreciation rate applied. • Locality of the property • Proximity to civic amenities • Topography/geographical feature of the land • Demand for the land 	The estimated fair value would increase (decrease if: <ul style="list-style-type: none"> • depreciation rate were lower (higher); • the property located in urban locality; • closer to civic amenities; • the higher the demand for the land.

2016
\$000

2015
\$000

11. Other assets

Commercial bank clearing	49,274	696
Others	3,060	3,820
	<u>52,334</u>	<u>4,516</u>

12. Property, plant and equipment

	Land & buildings \$000	Plant, equipment & furniture \$000	Motor vehicles \$000	Computer \$000	Work in progress \$000	Total \$000
<i>Cost/valuation</i>						
Balance at 1 January 2015	135,274	25,325	2,191	7,066	2,301	172,157
Transfer from Investment property	5,670	-	-	-	-	5,670
Acquisitions	-	162	237	570	1,808	2,777
Transfers	28	465	-	1,670	(2,163)	-
Disposals	-	(1,863)	(523)	(1,093)	-	(3,479)
Balance at 31 December 2015	140,972	24,089	1,905	8,213	1,946	177,125
Acquisitions	-	-	-	-	4,803	4,803
Transfers	-	643	-	1,194	(1,837)	-
Disposals	-	(122)	-	-	-	(122)
Balance at 31 December 2016	140,972	24,610	1,905	9,407	4,912	181,806
<i>Accumulated depreciation</i>						
Balance at 1 January 2015	6,039	20,583	1,524	5,895	-	34,041
Depreciation charge for the year	2,932	1,199	388	816	-	5,335
Disposals	(8,956)	(1,863)	(523)	(1,089)	-	(12,431)
Balance at 31 December 2015	15	19,919	1,389	5,622	-	26,945
Depreciation charge for the year	2,963	784	293	1,299	-	5,339
Disposals	-	(122)	-	-	-	(122)
Balance at 31 December 2016	2,978	20,581	1,682	6,921	-	32,162
<i>Carrying amount</i>						
At 1 January 2015	129,235	4,742	667	1,171	2,301	138,116
At 31 December 2015	140,957	4,170	516	2,591	1,946	150,180
At 31 December 2016	137,994	4,029	223	2,486	4,912	149,644

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2016

	2016	2015
	\$000	\$000
13. Demand deposits		
(a) Foreign currency demand deposits		
Demand deposits	59,240	16,240
Demand deposits include deposits from international organisations such as the Asian Development Bank (ADB), European Development Bank (EDB), International Fund for Agricultural Development (IFAD) and International Development Association		
	2016	2015
	\$000	\$000
(b) Local currency demand deposits		
Commercial banks	1,747,864	1,510,974
Solomon Islands Government	759,033	1,050,278
Other financial corporations	4,809	5,077
Other	8,077	6,902
	2,519,783	2,573,231
14. Currency in circulation		
Notes	837,146	748,548
Coins	31,249	28,092
	868,395	776,640
15. Fixed deposits		
Bokolo bills	761,658	721,677
Boko1o bills are short term discount securities issued and backed by the Central Bank of Solomon Islands. The instrument is used by the Bank for its monetary operations.		
	2016	2015
	\$000	\$000
16. SIG monetary operations account		
SIG monetary operations account	51,359	58,422
17. Employee entitlements		
Gratuity	1,080	1,096
Long service leave	631	1,404
Early retirement benefit	13,960	14,500
	15,671	17,000
18. Other liabilities		
Unpresented bank cheques	6,913	6,258
Other liabilities	3,715	4,767
	10,628	11,025
19. Determination of distributable profit		

Profits of the Bank are determined and dealt with in accordance with Section 54 and 55 of the Central Bank of Solomon Islands Act., 2012 as follows:

- a) Section 54(2)(a) states that unrealised revaluation gains shall be deducted from the net profits and shall not be available to be distributed but allocated to the respective unrealised revaluation reserve account;
- b) The realised gains from previous years shall be deducted from the appropriate revaluation reserve account and added to the distributable earnings as determined in section 54(2)(a).

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2016

	2016	2015
	\$000	\$000
<i>Net profit distribution according to CBSI Act 2012</i>		
Net operating loss	(42,504)	44,308
Add/(less) net unrealised foreign exchange loss/(gain)	66,346	(26,101)
(Less) changes in fair value in investment properties	-	(600)
Net (loss)/gain to be recorded in general reserve	<u>23,842</u>	<u>17,607</u>
Section 55(3) of the Central Bank of Solomon Islands Act, 2012 states that negative distributable earnings shall first be charged to the general reserve account and subsequently applied to authorised capital.		

	2016	2015
	\$000	\$000

20. Cash and cash equivalents

Cash and cash equivalents included in the statement of cash flows comprise of the following:

Cash on hand - local currency	202	196
Cash and cash equivalents- foreign currency	<u>1,048,532</u>	<u>781,517</u>
	<u>1,048,34</u>	<u>781,713</u>

21. Share capital

Section 6 (1) of the CBSI Act, states that the authorised and paid up capital of the bank shall be an amount equivalent to \$50 million dollars (2015: \$50 million). The capital is fully subscribed by the Government of Solomon Islands.

	2016	2015
	\$000	\$000
Balance at the beginning of the year	50,000	50,000
Transfer from General Reserve according to Section 6(1) of CBSI Act., 2012	-	-
Balance at the end of the year	<u>50,000</u>	<u>50,000</u>

22. Reserves

Under Section 53(2) of the CBSI Act., 2012, the Bank shall maintain the following reserves. Their purpose and method of operation are to be as follows:

- a) **General reserve**
The general reserve was established under Section 53(1) as a reserve for the purposes of covering losses sustained by the Bank.
- b) **Foreign exchange asset revaluation reserve**
Unrealised gains and losses on revaluation of foreign exchange balances are recognised in the profit and loss under other comprehensive income and are transferred to the foreign exchange asset revaluation reserve at the end of the accounting period.
- c) **Asset revaluation reserve**
The asset revaluation reserve reflects the impact of changes in the market value of property.
- d) **Gold revaluation reserve**
The unallocated and allocated gold is valued at current quoted market prices. Gold is accounted for as an available for sale financial asset. Unrealised gains and losses arising from revaluation are recognised in the gold revaluation reserve at the end of the accounting period.
- e) **Capital asset reserve**
The capital asset reserve is used to strengthen the Bank's equity position in relation to future major capital investment in buildings and equipment.

23 Financial risk and management policies

(a) Introduction and overview

The structure of the Bank's statement of financial position is primarily determined by the nature of its statutory functions. International Financial Reporting Standards (IFRS) 7 - (Financial Instrument Disclosures) requires disclosure of information relating to financial instruments, their significance, performance, accounting policy, terms and conditions, fair values and the Bank's policies for controlling risks and exposures relating to the financial instruments.

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2016

The Bank's risk management framework differs from the risk management framework for most other financial institutions. The main financial risks that the Bank faces include;

- Liquidity risk
- Credit risk
- Market risk
- Operational risk

This note presents information about the Bank's exposure to each of the above risks, the Bank's objectives, policies and procedures for measuring and managing risk.

Risk management framework

Like most central banks, the nature of the Bank's operations creates exposures to a range of operational and reputational risks. The Board of Directors has overall responsibility for the establishment and oversight of the Bank's risk management framework.

The Bank's management seeks to ensure that strong and effective risk management and control systems are in place for assessing, monitoring and managing risk exposure. The Board of Directors and management are responsible for managing and monitoring the business strategy, risks and performance of the Bank.

Internal Audit forms part of the Bank's risk management framework. This function reports to the Governor and the Board Audit Committee on internal audit and related issues. All areas in the Bank are subject to periodic internal audit review.

The Bank is subject to an annual audit by an external auditor. Auditing arrangements are overseen by an Audit Committee of the Board to monitor the financial reporting and audit functions within the Bank and the committee reviews the internal audit functions as well. The committee reports to the Board of Directors on its activities.

The overall risk management framework is designed to strongly encourage the sound and prudent management of the Bank's risk. The Bank seeks to ensure the risk management framework is consistent with financial market best practice.

The risk tables in this note are based on the Bank portfolio as reported in its statement of financial position.

(b) Liquidity risk

Liquidity risk is the risk that the Bank will encounter difficulty in meeting obligations associated with its financial liabilities that are settled by delivering cash or another financial asset.

Management of liquidity risk

To limit the liquidity risk, the Bank maintains an adequate level of reserves and taking into consideration the transaction demand on foreign exchange, ensures that an acceptable amount is maintained in current accounts at all times. The Bank invests in high quality instruments, including commercial paper and debt issued by Governments and Supranationals, all of which are easily converted to cash (refer to maturity analysis on liquidity).

The Central Bank of Solomon Islands Act (Section 56) requires that in the event that the value of its assets falls below the sum of its monetary liabilities and its unimpaired authorised capital, then –

- (a) The Board, with the advice of the external auditors of the Bank, shall assess the situation and prepare a report on the causes and extent of the shortfall and assess the situation within a period of no more than 30 calendar days;
- (b) If the Board approves the report under paragraph (a), the Bank shall request the Minister of Finance for a capital contribution to be made by the Government to remedy the deficit; and
- (c) Upon receipt of this request the Government shall, within a period of no more than 30 calendar days, transfer to the Bank the necessary amount in currency or in negotiable debt instruments with a specified maturity issued at market-related interest rates prevailing in Solomon Islands.

As at 31 December 2015, the Bank's total assets amounted to \$4.51 billion. This was less than the sum of the Bank's total monetary liabilities and its unimpaired capital which totalled \$4.55 billion.

Maturity analysis as at 31 December 2016

The maturity analysis noted below includes all financial assets and liabilities as at 31 December 2016.

	On Demand	0-3 Months	3-6 Months	6-12 Months	Over Year	Undefined	Total
	\$000	\$000	\$000	\$000	\$000	\$000	\$000
Foreign currency financial assets							
Money on demand	1,048,532	-	-	-	-	-	1,048,532
Fixed term deposit	-	1,929,862	743,184	17,606	-	-	6,690,652
Holding on special drawing rights	-	-	-	-	-	37,944	37944,243
Reserve tranche	-	-	-	-	-	34,155	34,155
Subscription	-	-	-	-	-	191,368	191,368
Gold investment	-	-	-	-	-	225,460	225,460
Bonds	-	31,828	655	61,666	35,044	-	129,193
Short term commercial paper	-	-	29,121	29,121	-	-	58,242

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2016

	On Demand \$000	0-3 Months \$000	3-6 Months \$000	6-12 Months \$000	Over Year \$000	Undefined \$000	Total \$000
	1,048,552	1,961,862	772,960	108,393	35,044	488,927	4,415,546
Local currency financial assets							
Cash on hand	202	-	-	-	-	-	202
Other receivables	-	49,215	59	-	-	-	49,274
Loans and advances	-	-	-	-	12,261	-	12,261
	202	49,215	59	-	12,261	-	61,737
Total Financial Assets	1,048,734	2,010,905	773,019	108,393	47,305	488,927	4,477,283
Foreign currency financial liabilities							
Demand deposits	59,202	-	-	-	-	-	59,202
IMF standby credit facility	-	-	-	-	-	73,069	73,069
IMF special drawing rights allocation	-	-	-	-	-	109,918	109,918
IMF extended credit facility	-	-	-	-	-	11,537	11,537
IW' securities	-	-	-	-	-	190,895	190,895
Capital subscription	-	-	-	-	-	4,929	4,929
	59,202	-	-	-	-	390,348	449,550
Local currency financial liabilities							
Demand deposits	2,519,784	-	-	-	-	-	2,519,784
Currency in circulation	-	-	-	-	-	868,395	776,640
SIG monetary operations account	-	51,359	-	-	-	-	58,422
Fixed deposits	-	750,771	11,258	-	-	-	721,677
Employee entitlements	-	-	-	-	15,670	-	17,000
Other liabilities	6,913	3,767	-	-	-	-	11,025
	2,526,697	805,474	11,258	-	15,670	868,395	4,227,493
Total Financial Liabilities	2,585,899	805,474	11,258	-	15,670	1,258,743	4,677,043
Net assets/(liabilities)	(1,537,165)	1,205,431	761,761	108,393	31,635	(769,816)	(199,761)

Maturity analysis as at 31 December 2015

The maturity analysis noted below includes all financial assets and liabilities as at 31 December 2015.

	On Demand \$000	0-3 Months \$000	3-6 Months \$000	6-12 Months \$000	Over Year \$000	Undefined \$000	Total \$000
Foreign currency financial assets							
Money on demand	781,517	-	-	-	-	-	781,517
Accrued interest	-	5,959	536	-	-	-	6,495
Fixed term deposit	-	2,083,482	744,518	-	-	-	2,828,000
Holding on special drawing rights	-	-	-	-	-	93,243	93,243
Reserve tranche	-	-	-	-	-	5,981	5,981
Subscription	-	-	-	-	-	107,078	107,078
Gold investment	-	-	-	-	-	206,921	206,921
Bonds	-	-	-	-	91,189	-	91,189
Short term	-	175,294	-	-	-	-	175,294
	781,517	2,364,735	745,054	-	91,189	413,223	4,295,718
Local currency financial assets							
Cash on hand	196	-	-	-	-	-	196
Other receivables	-	-	696	-	-	-	696
Loans and advances	-	-	-	-	11,629	-	11,629

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2016

	On Demand \$000	0-3 Months \$000	3-6 Months \$000	6-12 Months \$000	Over Year \$000	Undefined \$000	Total \$000
	196	-	696	-	11,629	-	12,521
Total Financial Assets	781,713	2,264,735	745,750	-	102,818	413,223	4,308,239
Foreign currency financial liabilities							
Demand deposits	16,240	-	-	-	-	-	16,240
IMF standby credit facility	-	-	-	-	-	101,753	101,753
IMF special drawing rights allocation	-	-	-	-	-	107,712	107,712
IMF extended credit facility	-	-	-	-	-	8,076	8,076
IW' securities	-	-	-	-	-	102,389	102,389
Capital subscription	-	-	-	-	-	4,716	4,716
	16,240	-	-	-	-	324,646	340,886
Local currency financial liabilities	2,573,231	-	-	-	-	-	2,573,231
Demand deposits	-	-	-	-	-	776,640	776,640
Currency in circulation	-	58,422	-	-	-	-	58,422
SIG monetary operations account	-	710,432	11,245	-	-	-	721,677
Fixed deposits	-	-	-	-	17,000	-	17,000
Employee entitlements	6,258	4,767	-	-	-	-	11,025
Other liabilities	2,579,489	773,621	11,245	-	17,000	776,640	4,157,995
	2,595,729	773,621	11,245	-	17,000	1,101,286	4,498,881
Total Financial Liabilities	(1,814,016)	1,491,114	734,505	-	85,818	(688,063)	(190,642)
Net assets/(liabilities)	(1,920,099)	1,711,232	430,021	31,195	161,393	(619,444)	(205,702)

(c) Credit risk

Credit risk is the risk of loss arising from a counter party to a financial contract failing to discharge its obligations.

Selection of a counter party is made based on their respective credit rating. Investment decisions are based on the credit rating of the particular issuer, country limits and counter party limits in place to control exposure risks.

The Bank uses Standard and Poor's, Moody's and Fitch credit ratings for assessing the credit risk of foreign counter parties. The credit ratings of counter parties are closely monitored and are updated as new market information is available. Foreign exchange limits per bank are imposed for all currency dealings.

Concentration of credit exposure

The Bank's significant end-of-year concentrations of credit exposure by portfolio type were as follows:

	2016 \$000	2015 \$000
Foreign currency assets		
Cash at Bank	1,048,532	781,517
Held to maturity investment	2,859,056	3,094,483
International monetary fund	263,467	206,302
Gold investment	225,460	206,921
	4,396,515	4,289,233
Local currency assets		
Loans and advances	12,261	11,629
	4,408,776	4,300,852

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2016

The Bank monitors credit risk by currency and sector. An analysis of concentrations of credit risk is shown below:

Concentration by currency	2016		2015	
	\$000	%	\$000	%
USD	2,436,841	56	2,293,297	53
AUD	986,192	23	841,733	20
EURO	129,059	3	214,842	5
SDR	263,468	6	206,302	5
NZD	232,219	5	267,494	6
SGD	154,076	3	155,461	4
STD	194,074	4	310,091	7
SBD	12,261	-	11,629	-
JPY	3	-	3	-
CNY	583			
Total financial assets	4,408,776	100	4,300,852	100
Concentration by sector				
Foreign currency assets				
Central banks	1,226,178	28	1,048,000	24
Commercial banks	2,906,870	66	3,034,921	71
International Monetary Fund	263,467	6	206,302	5
	4,408,776	100	4,289,223	100
Local currency assets				
Solomon Islands Government loan and advances	5,019	41	5,039	92
Staff loan and advances	7,590	57	6,590	8
	12,261	100	11,629	100
Total financial assets	4,408,776		4,300,852	

d) Market risk

Market risk is the risk that changes in market prices, such as interest rates and foreign exchange rates will affect the Bank's income or the value of its holding of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters while optimising the return on risk.

Interest rate risk management

The principal risk to which trading portfolios are exposed is the risk of loss from fluctuations in future cash flows or fair value of financial instruments because of a change in market interest rates. The Bank limits interest rate risk by modified duration targets. The duration of the portfolio is re-balanced regularly to maintain the targeted duration. Operations are largely money market focused.

At the reporting date the interest rate profile of the Bank's interest-bearing financial instruments was:

	2016	2015
	\$000	\$000
	Carrying amount	
Fixed rate instruments		
Cash at Bank (Financial assets)	575,273	581,341
Held-to-maturity investments (Financial assets)	2,859,056	3,094,483
Loans and advances (Financial assets)	12,261	11,629
Demand deposits (Financial liabilities)	-	(340,603)
SIG monetary operations account (Financial liabilities)	-	(37,923)
Fixed deposits (Financial liabilities)	(761,658)	(721,677)
	2,684,932	2,587,250
Variable rate instruments		
Cash at Bank (Financial assets)	267,896	192,180

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2016

International Monetary Fund (Financial assets)	37,944	92,243
International Monetary Fund (Financial liabilities)	(107,430)	(107,714)
	<u>198,410</u>	<u>177,709</u>

Fair value sensitivity analysis for fixed instruments

The Bank does not account for any fixed rate financial assets and liabilities at fair value through profit and loss. Therefore a change in interest rates at the reporting date would not affect the profit or loss.

Cash flow sensitivity analysis for variable rate instruments

A change of 100 basis points (bp) in interest rates at the reporting date would have increased (decreased) equity and the profit or loss by amounts shown below. This analysis assumes that all other variables, in particular foreign currency rates, remain constant.

	Profit or loss	
	100bp increase	100bp decrease
31 December 2016 Variable rate instruments	1,981	(1,984)
31 December 2015 Variable rate instruments	1,777	(1,777)

Foreign exchange risk management

Exchange rate risk relates to the risk of loss of foreign reserves arising from changes in the exchange rates against the Solomon Islands dollar. The Bank has adopted a currency risk management policy, which maintains the Solomon Islands dollar value of the foreign reserves and manages the fluctuations in the revaluation reserve account. While the effect of fluctuations in foreign exchange are recorded in profit or loss, foreign exchange fluctuations are not included as part of profit distribution but transferred to the revaluation reserve for monitoring purposes.

In accordance with the CBSI Act, 2012, the task of maintaining the safety and liquidity of foreign reserve assets, as well as the returns from reserves asset management, are achieved through diversification of investment by entering into transactions in international capital and money markets. Analysis of risks is the process of managing the currency reserves by comparing factual risk levels with set limits.

(e) Market risk

The Bank's exposure to foreign exchange risk, based on carrying amounts, was as follows:

2016 foreign currency risk

Foreign currency financial assets	USD \$000	NZD \$000	AUD \$000	EURO \$000	STG \$000	Others \$000	Total \$000
Money on demand	575,273	-	267,313	129,059	76,300	587	1,048,532
Fixed term deposit	1,636,108	232,219	540,650	-	117,773	154,076	2,680,826
Holding on special drawing rights	-	-	-	-	-	37,944	37,944
Reserve tranche	-	-	-	-	-	34,155	34,155
Subscription	-	-	-	-	-	191,368	191,368
Gold investment	225,460	-	-	-	-	-	225,460
Bonds	-	-	120,238	-	-	-	120,238
Short term commercial paper	-	-	57,990	-	-	-	57,990
Total	2,436,841	232,219	986,191	129,059	194,073	418,130	4,396,513
Foreign currency financial liability							
Demand deposits	59,202	-	-	-	-	-	59,202
IMF standby credit facility	-	-	-	-	-	73,069	73,069
IMF special drawing rights allocation	-	-	-	-	-	109,918	109,918
IMF extended credit facility	-	-	-	-	-	11,537	11,537
IMF securities	-	-	-	-	-	190,895	190,895
Capital subscription	-	-	-	-	-	4,929	4,929
Total	59,202	-	-	-	-	390,348	449,550
Net foreign currency asset	2,377,639	232,219	986,191	129,059	194,073	27,782	3,946,963

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2016

2015 foreign currency risk

Foreign currency financial assets	USD \$000	NZD \$000	AUD \$000	EURO \$000	STG \$000	Others \$000	Total \$000
Foreign currency financial assets							
Money on demand	581,342	-	41,067	151,112	7,993	3	781,517
Fixed term deposit	1,505,034	267,494	534,183	63,730	302,098	155,461	2,828,000
Holding on special drawing rights	-	-	-	-	-	93,243	93,243
Reserve tranche	-	-	-	-	-	5,981	5,981
Subscription	-	-	-	-	-	107,078	107,078
Gold investment	206,921	-	-	-	-	-	206,921
Bonds	-	-	91,189	-	-	-	91,189
Short term commercial paper	-	-	175,294	-	-	-	175,294
Total	2,293,297	267,494	841,733	214,842	310,091	361,766	4,289,223
Foreign currency financial liability							
Demand deposits	16,240	-	-	-	-	-	16,240
IMF standby credit facility	-	-	-	-	-	101,753	101,753
IMF Special drawing rights allocation	-	-	-	-	-	107,714	107,714
IMF extended credit facility	-	-	-	-	-	8,076	8,076
IMF securities	-	-	-	-	-	102,389	102,389
Capital subscription	-	-	-	-	-	4,716	4,716
Total	16,240	-	-	-	-	324,648	340,888
Net foreign currency asset	2,293,297	267,494	841,733	214,842	310,091	37,118	3,948,335

Concentration of foreign exchange

The Bank's net holdings of foreign exchange (excluding its holding of Special Drawing Rights) were distributed as follows as at 31 December 2016:

	2016		2015	
	\$000	%	\$000	%
USD	2,377,639	58	2,277,057	56
AUD	986,191	24	841,733	21
EURO	129,059	3	214,842	5
NZD	232,219	6	267,494	7
SGD	154,076	4	155,461	-
STG	194,073	5	310,091	4
JPY	3	-	3	8
CNY	583	-	-	-
	4,073,843	100	4,066,681	100

The following significant exchange rates were used at year end to convert foreign currency balances to the Solomon Island dollar equivalent.

Reporting date	spot rate	
	2016	2015
AUD	0.1717	0.1701
USD	0.1236	0.1240
NZD	0.1780	0.1810
STG	0.1010	0.0837
EURO	0.1182	0.1135
JPY	14.4836	14.940
SGD	0.1792	0.1753
SDR	0.0922	0.0920
CNY	0.8594	-

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2016

Sensitivity to foreign exchange rate risk	2016 \$M	2015 \$M
Impact of a:		
Change in profit/equity due to a 2 per cent appreciation in the reserves - weighted value of the Solomon Islands dollar	82	(78)
Change in profit/equity due to a 2 per cent depreciation in the reserves - weighted value of the Solomon Islands dollar	(78)	80

(e) Operational risk management

Operational risk is the risk of direct or indirect loss arising from a wide variety of causes associated with the Bank's processes, personnel, technology and infrastructure and from external factors other than liquidity, credit and market risks such as those arising from legal and regulatory requirements and generally accepted standards of corporate behaviour. Operational risk arises from all of the Bank's operations.

Managing operational risk in the Bank is an integral part of day-to-day operations and oversight. This includes adherence to Bank wide corporate policies. There is also an active internal audit function carried out on a quarterly basis.

Operating loss is the risk of loss from breakdown of internal controls. The Bank has established an internal audit function which will exercise monitoring and control over accounting policies and procedures, and the effective functioning of the system of internal controls at the Bank.

Operational risk relating to the activities of foreign currency reserves management is controlled by a number of internal instructions, and there is clear segregation of front office and back office activity. The latter is one of the mechanisms for managing operational risk.

24. Fair value of financial assets and liabilities

The fair value of an instrument is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arms length transaction. Quoted market values represent fair value when a financial instrument is traded in an organised and liquid market that is able to absorb a significant transaction without moving the price against the trader.

Valuation of financial instruments

The Bank measures fair values using the following fair value hierarchy that reflects the significance of the inputs used in making the measurements:

- Level 1: Quoted market price (unadjusted) in an active market for an identical instrument.
- Level 2: Valuation techniques based on observable inputs either directly (i.e. as prices) or indirectly (i.e. derived from prices). This category includes instruments valued using: quoted market prices in active market for similar instruments; quoted market prices for identical or similar instruments in markets that are considered less than active; or other valuation techniques where all significant inputs are directly or indirectly observable from market data.
- Level 3: Valuation techniques using significant unobservable inputs. This category includes all instruments where the valuation techniques include inputs not based on observable data and the unobservable inputs have a significant impact on the instrument's valuation. This category includes instruments that are valued based on quoted prices for similar instruments where significant unobservable adjustments or assumptions are required to reflect differences between the instruments.

If the inputs used to measure the fair value of an asset might be categorised in different levels of the fair value hierarchy, then the fair value measurement is categorised in its entirety in the same level of the fair value hierarchy as the lowest level input that is significant to the entire measurement.

The table below analyses financial instruments measured at fair value at the end of the reporting period

31 December 2016	Note	Level 1 \$000	Level 2 \$000	Level 3 \$000	Total \$000
<i>Investment securities</i>					
Available for sale financial assets (Gold)	6	225,460			225,460
Investment Property	10			13,262	13,262
31 December 2015	Note	Level 1 \$000	Level 2 \$000	Level 3 \$000	Total \$000
<i>Investment securities</i>					
Available for sale financial assets (Gold)	6	206,921			206,921
Investment Property	10			13,262	13,262
Property, Plant and equipment (only land & buildings)	12			140,957	140,957

Refer to note 10 and note 12 which shows a reconciliation from the opening balances to the closing balances for the Level 3 fair values above.

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2016

25. Related parties

The Bank has related party relationships with the Board of Directors, the Executive Management and the Solomon Islands Government.

The Board of Directors during the year were:

Denton Rarawa (Chairman and Governor)
 Gane Simbe (Deputy Governor)
 Harry D Kuma (appointed 13th May 2015)
 Sir Thomas Ko Chan (appointed on 3rd August 2015)
 Loyley Ngira (contract end on 5th February 2016)
 Lily Lomulo (contract end on 5th February 2016)
 John Usuramo (appointed on 18th December 2013)
 Tele Bartlett (contract end on 17th July 2016)
 Primo Afeau (contract end on 17th July 2016)
 David Quan (appointed on 17th August 2016)
 Leslie Teama (appointed on 17th August 2016)

Directors' fees and emoluments

Amounts paid to directors during the year are disclosed in Note 4 (f). No other emoluments were paid or are due to the directors at year end.

Related party disclosures requires the disclosure of information relating to aggregate compensation of key management personnel. The key management personnel of the Bank are members of the Bank Board and senior staff who have responsibility for planning, directing and controlling the activities of the Bank. Fees of the non-executive members of the Board are determined by the Minister of Finance. The contracts of the Governor and Deputy Governor are subject to mid-term review by the Minister of Finance and annually in accordance with Bank policy. The Board of Directors determines the remuneration of the Chief Managers.

During the year the following persons were the executives identified as key management personnel, with the greatest authority and responsibility for planning and controlling the activities of the Bank:

Denton Rarawa	Governor
Gane Simbe	Deputy Governor
Luke Forau	Advisor to Governors
Ali Homelo	Chief Manager International
Daniel Haridi	Chief Manager Currency and Banking Operations
Michael Kikiolo	Chief Manager Economics Research and Statistics
Bella Simiha	Chief Manager HR and Corporate Services
Emmanuel Gela	Chief Manager Finance and Accounts
Raynold Moveni	Chief Manager Financial Market Supervision
Edward Manedika	Chief Manager Information Technology

The remuneration of the Bank's key management personnel, included in 'personnel expenses' was as follows:

	2016 \$000	2015 \$000
Short-term employee benefits	2,647	2,568
Long-term benefits	1,120	785
	<u>3,767</u>	<u>3,353</u>

Short-term benefits include cash salary, and in the case of staff, annual leave, motor vehicle benefits, health benefits and the fringe benefits tax paid or payable on these benefits.

Long-term benefits include gratuity, long service leave and early retirement benefits.

As at 31 December 2016 loans by the Bank to key management personnel are as follows:

	2016 \$000	2015 \$000
Housing Loan	1,631	1,494
Personal Loan	59	62
Management Car Loan	180	126
	<u>1,870</u>	<u>1,682</u>

There were no other related party transactions with Board members; transactions with director-related entities which occurred in the normal course of the Bank's operations were conducted on the terms no more favorable than similar transactions with other employees or customers.

Transactions with the Solomon Islands Government

The transactions with the Solomon Islands Government include banking services, foreign exchange transactions, registry transactions and purchase of Government securities. During the year, the Bank received \$nil (2015: \$1.3m) of interest income relating to their investments in Government securities. The Bank also paid \$0.3 million (2015: \$8.3m) to the Government in accordance with Section 34 of the CBSI Act, 2012. The balance of the Bank's investment in Government securities at year end amounted to \$4.9 million (2015: \$4.9m).

26. Commitments and contingent liabilities

The Bank has guaranteed staff housing loans with the commercial banks to the sum of \$0.79 million as at 31 December 2016 (2015: \$0.79m). The guarantee scheme was no longer available to staff since 2011 and is valid for eligible staff until the date of cessation of employment with the Bank.

In 2007 the Solomon Islands Government introduced and provided \$10 million for the establishment of the Small Business Finance Guarantee Scheme to be administered by CBSI. As at 31 December 2016, a total of 5 (2015: 64) loans with a net guarantee of \$0.678m (2015: \$5.53m) million have been administered under the scheme.

27. Events subsequent to balance date

There has not been any matter or circumstance that has arisen since the end of the financial year that has significantly affected, or may significantly affect, the operations of the Bank, the results of those operations, or the state of affairs of the Bank in future financial years.



