

G. Country Chapter: Solomon Islands

Table 25. Country Summary

Country	Solomon Islands
Prime Minister	Sir Allan Kemakeza replaced Mannaseh Sogevare as the Prime Minister following national elections in December 2001.
Head of State	Queen Elizabeth II represented by the Governor General, Sir John Ini Lapli.
Independence	July 7, 1978
Government	A Parliamentary Democracy with a single Legislative Assembly, it has its 50 seat parliament in Honiara. Each province is administered by its own elected Premier and provincial government.
Land area	Over 1.35 million sq km of sea and a land area of 29,785 sq km.
Population	470,861 (2004 est.). Population growth rate is 3.1% (2004 est.)
Cities	Capital: Honiara
Provinces	Nine provinces: Guadalcanal, Central, Western, Ysabel, Malaita, Makira, Temotu, Choiseul, and Rennell & Bellona.
Languages	English and Solomon Islands Pidgin, plus 87 listed indigenous languages and 30 dialects.
Natural Hazards	Typhoons, but rarely destructive; geologically active region with frequent earth tremors; and volcanic activity.
Natural Resources	Fish, forests, gold, bauxite, phosphates, lead, zinc, nickel.
Major Products:	Copra, marine products, and timber. Subsistence activities dominate the lives of 80 percent of Solomon Islanders.

1. Economic Overview

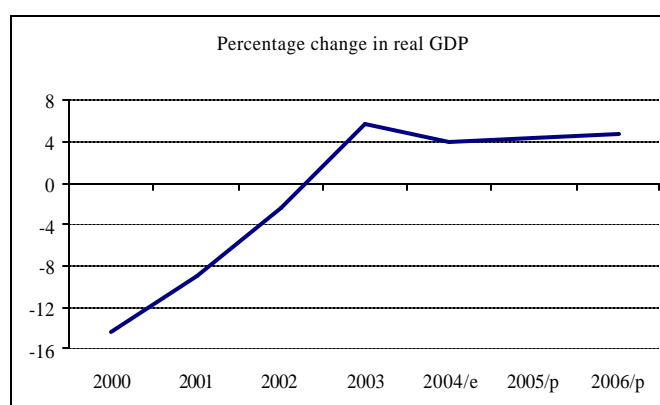
142. The Solomon Islands is the third largest archipelago in the South Pacific, comprising a scattered double chain of 992 islands, of which about one-third are populated. Beginning in late-1999, the Solomon Islands was plunged into political turmoil and civil strife due to ethnic tensions. As the security situation worsened, public administration deteriorated and by mid-2003 had reached a state of near-collapse. Intimidation and extortion of public servants by self-styled “constables,” as well as rampant corruption led to fiscal ruin. The general public was also subjected to this treatment. During this period the Solomon Islands fell into arrears with respect to all its external creditors, including the World Bank, and the Asian Development Bank.

143. In July 2003, an Australian-led regional intervention force, the Regional Assistance Mission to Solomon Islands (RAMSI) was deployed at the invitation of the Solomon Islands Government under the Facilitation of International Assistance Act (2003). Law and order was quickly restored and has been effectively maintained. In addition to the security force, RAMSI has the following components: (a) a police presence, expected to remain in place up to 10 years to maintain order and also rebuild the Solomon Islands police force; (b) technical assistance to support restoration of the budget process and more efficient and accountable public spending, and (c) development assistance to underpin peace and reconciliation. RAMSI-funded advisors and in-

line staff have been placed in the legal and judicial system and in economic and central agencies including the Ministry of Finance.

144. To date, RAMSI has enjoyed public support in the Solomon Islands because it has halted day-to-day violence, intimidation, and abuse of power. Improvements in security have boosted public confidence and reinvigorated formal business activity, particularly in Honiara. As a result of the restoration of law and order, real GDP growth rebounded sharply from an average of negative 8.6 percent over 2000-02 to 5.6 percent in 2003 (see Figure 11), supported by rising export levels, growth in primary production and construction activity. Over the near-term GDP growth is expected to remain buoyant, averaging around 4-5 percent a year during 2004-06.

Figure 11. Growth in Solomon Island's Real GDP during 2000-06.



145. As a result of the improvement in food supply and the stabilization of the nominal exchange rate, inflation has abated to single-digit levels from 10 percent in 2002-03 to an estimated 6 percent in 2004 and 2005.

146. The restoration of fiscal discipline was reflected in the estimated budget surplus of 10 percent of GDP in 2004, a turnaround from a deficit of similar magnitude in 2001-02. This outcome was mainly attributable to the significant improvement of tax collections aided by an amnesty on penalties, the cessation of payments to the ex-militants, a tightening of expenditure controls (particularly the wage bill), and significant grant based budgetary support from the major donors. Total public debt is expected to fall from 100 percent of GDP in 2003 to 87 percent of GDP in 2005.

147. The external position has improved sharply as reflected in the reversal of the current account deficit from an average of about 10 percent of GDP over 2000-02, to a surplus of 1.4 percent of GDP in 2003 and around 6 percent in 2004. As a result of a favorable trade balance, large inflows of foreign aid, and the depreciation of the domestic currency, international reserves have been rebuilt and are estimated to be equivalent to five months of imports of goods and services at end-2004.

148. Fishing, forestry, and agriculture are the principal productive sectors contributing to the Solomon Islands economy. In the fishing sector (9 percent of GDP in 2003) Solomon Taiyo Ltd.

(the only producer for export markets) resumed its operations at about 40 percent of capacity, after its suspension in mid-2000. Fish exports are estimated to be 17 percent of total exports in 2003-04.

149. The forestry sector (7 percent of GDP in 2003) was relatively unaffected by the 1999-2003 unrest. Timber exports accounted for almost 70 percent of total exports in 2003-04.

150. Although agriculture accounted for only 5 percent of GDP in 2003, its economic and social significance is far greater, as more than 80 percent of the population relies on subsistence agriculture for its livelihood. Cocoa represented about 6 percent of total exports in 2004 while copra represented around 3 percent. Overall, agriculture exports as a share of GDP are projected to grow at 3 percent in 2005-06.

2. Outlook

151. The current challenge for the government and donor partners is to successfully progress beyond the initial focus on stabilization, and implement policies and structural reforms to sustain the buoyant recovery in economic growth. RAMSI is now in the second phase of its mission which involves implementing reforms, particularly in the public sector and institutional and legal framework, as well as providing support to the provinces in the sectors of law and justice, financial management and rural service delivery.

152. In the immediate aftermath of the crisis some consideration was given to the adoption of a new constitution based on a federal system, with a significant number of political, financial and legal powers transferred to state governments. Much of the political impetus for this proposal derived from dissatisfaction with the poor reach of government services, especially beyond Honiara. Given major concerns about the availability of skilled administrators, lack of appropriate systems and the potential costs of setting up such a structure, these proposals require careful consideration. However, the underlying service delivery issues remain and need to be addressed.

153. Given the fragility of the economic recovery and looming uncertainties about future prospects, the government's approach to fiscal management has been to maintain the necessary flexibility. For the near term the government's strategy is to maintain a strong fiscal position by continuing to strengthen tax administration and widening the tax base, while working to strengthen public financial management and administrative capacity in the public sector. Considering the one-time nature of the recent revenue increase and the uncertainty about the level of external grants from major donors beyond 2004, tight controls on wages and cost reduction in non priority areas are vital priorities.

154. Besides implementing sector-specific policies to revitalize the main productive sectors, to rebuild infrastructure, and to improve health and education outcomes, structural reforms in the private sector are also vital. The environment supporting private activity could be improved to encourage investment and promote employment, particularly in potential growth sectors such as gold and mining, palm oil production, and tourism. Suitable policies to address the ongoing unsustainable pace of logging need to be designed and implemented. Private sector prospects have been boosted following the sale of the palm oil plantation in Guadalcanal to New Britain Oil Palm

Company which is expected to generate up to 7000 jobs once the rehabilitation commences. Investors from Malaysia, Australia, Papua New Guinea, Japan and Taiwan have also expressed interest in mining, fishing and fish-processing, and hotel projects. Some attention will need to be paid to land ownership issues in order to attract productive foreign investment.

3. Key Issues Shaping the World Bank's Involvement

155. Since becoming a World Bank member in 1978, the Solomon Islands has received eight IDA credits totaling US\$50 million, in the infrastructure, education, health, finance, and agriculture sectors.

156. Considering the strong presence of other partners in virtually all sectors of the economy, the challenge for the World Bank is to define an appropriate role in line with its comparative advantage, and to develop strategic partnerships with other stakeholders. The Solomon Islands exhibits many of the characteristics of a low-income country under stress (LICUS): weak government and institutions, recent conflict, coupled with high levels of poverty, arguing for a non-conventional approach to development support.

157. The aim of the World Bank Group's assistance program is therefore to identify selective entry points for supporting reforms and constituencies for change, capacity-building, tailored policy advice based on global experience and communications/outreach. The Solomon Islands program consists of analytical/advisory services and small grants, working with governments and, where appropriate, at the community level. A key emphasis is on coordination with other development partners to maximize leverage, particularly in key areas for MDG attainment.

158. The Bank's assistance program has been developed in consultation with the government and other development partners and is consistent with the government's own development priorities, articulated in the *National Economic Reform, Recovery and Development Plan* (NERRDP), 2003-2006.

159. It is expected that the Bank's program over 2005-08 will operate primarily in two broad areas which correspond to the first two pillars of the Bank Pacific regional strategy. First, the Bank will assist the government and other donors on public expenditure management issues to improve the delivery of basic services to communities and provide broader sector policy advice (e.g. public expenditure management, experience on the establishment of sectorwide approaches). Second, the Bank will target specific initiatives which seek to improve the climate for the private sector, such as reforms to the energy sector, telecommunications, financial sector management and foreign investment legislation.

160. Beyond these two focal areas the Bank will remain engaged and be prepared to respond flexibly. This would include, in particular, taking advantage of opportunities to contribute to long-term capacity building, tackling the underlying causes of instability and strengthening donor partnerships. In this context, the Bank will look to make a contribution to the productive sectors, recognizing that rural communities need to benefit directly from the recent stability in the Solomon Islands if the government and its development partners are to effectively address the underlying causes of conflict. The Bank is also considering the preparation of an application to

access the LICUS Trust Fund for the Solomon Islands, although further analysis and consultation is required to develop options for this.

161. Further details of the Bank's program to the Solomon Islands are outlined in Table 26. The Solomon Islands is eligible for IDA resources, expected to be grants under IDA14. The IDA14 allocation over FY2006-08 is expected to be SDR 5.3 million. This amount is indicative only. The actual amount will depend on (a) the country's own performance, (b) its performance relative to the performance of other IDA recipients, (c) the amount of overall resources available to IDA, and (d) the terms of financial assistance provided (grants versus loans). Subject to further discussions with the government, the allocation may be focused on rural development (agriculture/forestry), infrastructure (energy) or public expenditure management priorities.

Table 26. Summary of World Bank Assistance Program to the Solomon Islands

<i>Strategic Pillar & Focal Area</i>	<i>World Bank Activities</i>	<i>Expected Impacts</i>
<p>Strengthening government capabilities in service delivery.</p> <p>Improving the effectiveness of public expenditures in the social sectors.</p> <p>Improving the public expenditure management of infrastructural assets.</p> <p>Safeguarding service delivery by improving resilience to natural hazards.</p> <p>Improving the incentives for private sector growth and employment.</p>	<p>Improve health outcomes, particularly in rural areas - Health Sector Development Project (US\$4.0 million IDA Credit; approved 01/06/2000; closing 12/31/2006). . Health status in the Solomon Islands was affected by the ethnic tensions, the interruptions in services in Guadalcanal Province, and the sudden decline in government financing of the sector in 2000 and after. Important issues in the health sector include: (a) the need to consider moving to a sector-wide integrated expenditure and budget framework; (b) capacity building to create greater diversity in service provision and financing, and to reduce reliance on the government as the major provider, and (c) improved management, including the possibility of contracting out services or support functions and exploring new channels of funding to the community. The IDA-funded Solomon Islands Health Sector Development Project is helping to address some of these challenges through the strengthening of the reproductive health and malaria programs, testing new approaches and through improved planning, management and monitoring.</p> <p>Enhance access to and quality of education (TA). The government has launched a new education strategy and is developing a sector-wide approach to education planning and financing with support from NZAID and the EU. The Bank is providing selected policy inputs into this process, drawing on the lessons of such approaches elsewhere (including in the Pacific).</p> <p>Economic/Structural Reform (TA). The World Bank intends to work closely with other partners, in particular Australia and the ADB on economic analysis and advice, including in the areas of decentralization and intergovernmental fiscal relations. The World Bank will provide technical support to the Economic Reform Unit.</p>	<ul style="list-style-type: none"> • Greater access to improved health care services; improved health care supervision and management resulting in more effective allocation and utilization of resources • Development of an effective and comprehensive sector approach in the education sector. • Pragmatic advice provided to the Government based on international good practice.

<i>Strategic Pillar & Focal Area</i>	<i>World Bank Activities</i>	<i>Expected Impacts</i>
Reducing the costs of doing business.	<p>Improve energy supply (TA). The most recent estimate (1996) suggests that 15 percent of the total, and 5 percent of the rural population have access to electricity. The Solomon Islands Electricity Authority (SIEA) lacks management capacity and is facing a severe liquidity crisis, at least partly due to unpaid electricity accounts. Outside Honiara power supplies are almost entirely off-grid. However, there is considerable potential for development of renewable energy, particularly mini-hydro and solar power. The Bank is providing technical assistance for the financial restructuring of SEIA, regulatory reform and capacity building and to explore options to improve rural access and service delivery in remote areas. It is expected that this work will expand to include the water utility (Solomon Islands Water Authority).</p> <p>Reduce telecommunications costs and improve service (TA, initiated 02/12/2004). The availability of telecommunications services is low in absolute terms, particularly in rural and remote areas. Mobile and internet use are also comparably low. The market structure is monopolistic and the government's capacity to regulate the provider is limited. The Bank is providing technical assistance to the government to look at the ways to introduce a more competitive environment, thereby lowering costs and improving service quality and coverage.</p> <p>Promote rural income generation as the basis for stronger and more inclusive growth (TA). Acute rural poverty is a continuing concern in the Solomon Islands and a contributing factor to underlying social tensions. The challenge is to diversify and increase income-generating opportunities throughout the country so that local communities can begin to see more direct benefits from the restoration of law and order. The Bank is looking to work in partnership with key donors active in the sector, particularly the EU and AusAID to develop overall sector strategy and pilot projects for rural growth. The Bank will also maintain an interest in developments in the forestry sector to identify whether opportunities exist to strengthen the management and sustainability of forest exploitation. There are serious concerns that the current rate of logging is far greater than what can be sustained.</p>	<ul style="list-style-type: none"> • Introduction of comprehensive financial accounting processes; improved service provision. • Pilot approaches to rural energy supply. • Improved regulatory framework and telecommunications sector policy to foster competition. • Identification of sustainable income generating activities in rural areas.

<i>Strategic Pillar & Focal Area</i>	<i>World Bank Activities</i>	<i>Expected Impacts</i>
<p>Strengthening the management and sustainability of the resource-based sectors.</p> <p>Improving access to regional labor markets.</p>	<p>Financial sector recovery and development - Central Bank Capacity Building Project (TA, IDF Grant of US\$254,000; initiated December 2003) and National Provident Fund (TA). All financial institutions in the Solomon Islands were under stress due to the breakdown in fiscal discipline which resulted in government defaulting on its debts to both banks and non-bank financial institutions. While the private sector remains constrained by limited access to credit, near term efforts have focused on arrears repayments and financial reconstruction. The Bank has contributed to these efforts through technical assistance and policy support to the National Provident Fund and the Central Bank. The Bank has also mobilized an Institutional Development Fund (IDF) to help strengthen the Central Bank's capacity for effective economic and financial management.</p> <p>Remove impediments to foreign and domestic investment (TA). Prospects for foreign direct investment (FDI) are improving with recent progress in palm oil and gold (restoring facilities destroyed during the ethnic tensions), nickel and tourism development, but potential investors still face numerous administrative barriers. FIAS is providing assistance to the government for the preparation of a new foreign investment legislation and in the review of customs and related laws. A dialogue is underway on issues relating to improving the access to credit.</p>	<ul style="list-style-type: none"> • Enhanced effectiveness in the preparation of national accounts and key analysis. • Improved oversight of the banking and non-banking sectors • Development of comprehensive and effective legislation informed by international good practice.

4. Donor Coordination

162. Official development assistance to the Solomon Islands is substantial and has a major impact on budget planning and development. Aid flows have increased sharply since RAMSI's intervention: about US\$118 million for 2004 alone. This poses a challenge to government and partners alike in ensuring its productive use. The development budget is entirely composed of these donor funds, which are almost entirely grants. Projections of future support are not available but it is likely that the current levels will be maintained for the next 2-3 years.

163. Major donors (using 2004 aid flow data) are Australia (about 37 percent of donor funding), the European Union (about 14 percent); Japan (30 percent); New Zealand (about 5 percent); and Taiwan, China (about 10 percent). Donor support is concentrated in the social and governance sectors, notably, and income-generating activities and agriculture (2 percent) are significantly under-represented in donor programs.

164. Development partners are seeking to ensure their assistance is consistent with the priorities outlined in the NERRDP. The Department of National Reform and Planning is responsible for aid management; Australia is providing advisory assistance.

165. Table 27 describes the nature of the assistance provided by the Solomon Islands' other development partners.

Table 27. Activities of Other Development Partners

<i>Development partner</i>	<i>Primary activities</i>
ADB	Since 2003, ADB has reactivated one lending project in March 2004 (Post-Conflict Emergency Rehabilitation Project) whose objective is to help restore essential services, basic infrastructure, and community facilities affected by civil strife during the period 1999-2000. In view of the present debt situation, and in consideration of the availability of significant external grant funding, the decision has been taken not to pursue further lending in the short- to medium-term. Two nonlending products have been proposed for 2005 (Implementation of Interisland Transport Reforms, US\$500,000; Business Environment Reforms, US\$400,000; and Economic Development Report, US\$300,000). In 2006, 3 further nonlending activities are proposed: Ministry of Infrastructure Development Reform Program (US\$400,000); Private Sector Participation Program (US\$400,000); and, Secured Transactions Reforms (US\$700,000).
Australia	In 2004-05 Australia is providing an estimated total official development assistance to the Solomon Islands of A\$201.6 million reflecting its commitment to the RAMSI initiative (see above). Of this, around A\$93 million is provided under AusAID country program and the remainder by other agencies involved in RAMSI. In 2004-05, the priority will be for the governments of Solomon Islands, Australia and regional partners to consolidate and build on the gains made to date through RAMSI and Australia's bilateral development cooperation program. The focus will be on supporting Solomon Islands to implement a comprehensive reform agenda to improve the accountability and affordability of government. Priorities for reform are economic governance, rebuilding the machinery of government and strengthening the legal and judicial sector. Substantial support will be provided for continuing peace building, community development and health services programs.

<i>Development partner</i>	<i>Primary activities</i>
European Union	The Solomon Islands received an allocation of Euro 23 million under the 9 th EDF. The majority of this will be targeted to continuing a microprojects program. Other priorities include education and small business development in rural areas. The EU also has available STABEX funding (Euro 60 million) and is considering the potential for involvement in the forestry and rural development sectors. The EU budgetlines provided Euro 2.5 million for a marine conservation project shared with PNG and Indonesia.
Japan	In FY03 (April 1, 2003-March 31, 2004) Japan provided development assistance totaling US\$1.82 million comprising Grant financing (US\$0.73 million), TA (US\$1.09 million). Japan has no active lending operations in the Solomon Islands. TA activities are provided by experts in the field of water and waste water management.
New Zealand	NZAID provided the Solomon Islands with NZ\$16.14 million in bilateral aid (representing the largest single country allocation in its Pacific aid budget). Aid priorities include: education, the restoration of law and order, sustainable livelihoods and support to civil society. NZ\$12 million will be allocated to implement the Solomon Islands Education Strategic Plan (together with the EU) which aims to provide basic education for all children by 2015. Other initiatives include support of Honiara's Small Business Enterprise Center which to date has trained 3,800 potential and existing entrepreneurs.
Others	The following UN agencies have activities: FAO, ICAO, IFAD, ILO, IMO, ITU, UNCTAD, UNESCO, UPU, WHO, WMO, WtrO, UNEP, ITC, UNFPA, UNICEF, UNDP
