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Report No: PGD421

INTERNATIONAL DEVELOPMENT ASSOCIATION

PROGRAM DOCUMENT FOR A

PROPOSED GRANT

IN THE AMOUNT OF SDR15.4 MILLION (EQUIVALENT TO US$20 MILLION)

COMPRISING

A DEVELOPMENT POLICY GRANT OF SDR11.5 MILLION (US$15 MILLION EQUIVALENT)
AND
A DEVELOPMENT POLICY GRANT WITH A CATASTROPHE DEFERRED DRAWDOWN OPTION OF SDR3.9 MILLION (US$5 MILLION EQUIVALENT)

TO

SOLOMON ISLANDS

FOR THE

FIRST SOLOMON ISLANDS RESILIENCE DEVELOPMENT POLICY OPERATION WITH A CATASTROPHE DEFERRED DRAWDOWN OPTION

NOVEMBER 1, 2023

Macroecononomics, Trade and Investment Global Practice
Urban, Resilience and Land Global Practice
East Asia and Pacific Region

Public Disclosure Authorized

Solomon Islands

GOVERNMENT FISCAL YEAR

January 1 – December 31

CURRENCY EQUIVALENTS

(Exchange Rate Effective as of September 30, 2023)

Currency Unit

US$1.00 = SI 8.37

SDR 1 = USD$1.31

ABBREVIATIONS AND ACRONYMS

ADB	Asian Development Bank
Cat DDO	Catastrophe Deferred Drawdown Option
CBSI	Central Bank of Solomon Islands
CCA	Climate Change Adaptation
CCP	Climate Change Policy
CDF	Contingency Disaster Risk Facility
CPF	Country Partnership Framework
CIT	Corporate Income Tax
CRW	Crises Response Window
DA	Dedicated Foreign Currency Bank Account
DPO	Development Policy Operation
DPG	Development Policy Grant
DSA	Debt Sustainability Analysis
FCV	Fragility, Conflict and Violence
FDI	Foreign Direct Investment
IAU	Investment Analysis Unit
IDA	International Development Association
IFC	International Finance Corporation
IHR	International Health Regulations
IMF	International Monetary Fund
IPCCC	International Panel on Climate Change
IRD	Inland Revenue Division
JPRG	Joint Policy Reform Group
LPI	Logistics Performance Index
MMERE	Ministry of Mines, Energy and Rural Electrification
MSME	Micro, Small and Medium Enterprise
MTDP	Medium-Term Development Plan
NBC	National Building Code
NDC	National Disaster Council
NDMO	National Disaster Management Office
NDRMP	National Disaster Risk Management Plan
NDS	National Development Strategy
NHSP	National Health Strategic Plan
NHEC	National Emergency Health Council
NTF	National Transport Fund
OAG	Office of the Auditor General
PAAC	Project Analysis and Assessment Committee
PAYE	Pay-as-you-earn
PCDF	Provincial Capacity Development Fund
PPAs	Performance and Policy Actions
PV	Present Value
SIEA	Solomon Islands Electricity Authority
SIPA	Solomon Islands Ports Authority
SIWA	Solomon Islands Water Authority
SIG	Solomon Islands Government
SOE	State-Owned Enterprises
SME	Small- and Medium-sized Enterprises
SDR	Special Drawing Rights

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SOLOMON ISLANDS

The First Solomon Islands Resilience DPO with a Catastrophe Deferred Drawdown Option

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SUMMARY OF PROPOSED FINANCING AND PROGRAM

BASIC INFORMATION

Operation ID	Programmatic	If programmatic, position in series
P178676	Yes	1st in a series of 2

Proposed Development Objective(s)

The proposed series of two operations supports the Solomon Islands Government in its efforts to improve fiscal management, private sector development, and climate and disaster resilience.

Organizations

Borrower:	Solomon Islands
Implementing Agency:	Ministry of Finance and Treasury

PROJECT FINANCING DATA (US$, Millions)

Maximizing Finance for Development

Is this an MFD-Enabling Project (MFD-EP)?	No
Is this project Private Capital Enabling (PCE)?	No

SUMMARY

Total Financing	**20.00**

DETAILS

World Bank Group Financing

International Development Association (IDA)	20.00
IDA Grant	20.00

IDA Resources (US$, Millions)

	Credit Amount	Grant Amount	SML Amount	Guarantee Amount	Total Amount
National Performance-Based Allocations (PBA)	0.00	18.75	0.00	0.00	18.75
Crisis Response Window (CRW)	0.00	1.25	0.00	0.00	1.25
Total	**0.00**	**20.00**	**0.00**	**0.00**	**20.00**

PRACTICE AREA(S)

Practice Area (Lead)

Macroeconomics, Trade and Investment

Contributing Practice Areas

Urban, Resilience and Land

CLIMATE

Climate Change and Disaster Screening

Yes, it has been screened and the results are discussed in the Operation Document

OVERALL RISK RATING

Overall Risk	Substantial

RESULTS

Indicator Name	Baseline	Target
1. Non-logging domestic revenue (as percent of GDP)	20.4 percent (2022-2023 average)	22.4 percent (2026-2027 average)
2. Nickel royalty per dry tonne (in constant US$)	US$ 1.2 (2023)	US$ 3 (2027)
3. Percentage of externally financed project proposals analyzed following PIM Appraisal Guidelines	0 (2023)	100 (2027)
4(a) Commercial electricity tariff differential relative to structural peers in the region (Kiribati, Samoa, and Vanuatu, US$/KWh) 4(b) share of renewable energy in the energy mix (excl. Tina River)	(a) 0.3 (2021) (b) 2 percent (2023)	(a) 0.2 (2027) (b) 5 percent (2027)
5(a) Domestic credit to private sector (as share of GDP) 5(b) Loans granted to women (as a percent of total)	(a) 32.1 percent (2021-2022 average) (b) 12 percent (2022)	(a) 35 percent (2026-2027 average) (b) 17 percent (2027)
6. The number of foreign enterprises registered in Solomon Islands	63 (2022)	75 (2027)
7. Development applications screened against the climate and disaster risk ordinances developed in at least 2 provincial government areas.	0 percent (2023)	100 percent (2027)
8. Share of permit applications assessed for compliance with the building regulations and code (percent of total)	0 percent (2023)	100 percent (2027)
9. Number of public health emergency preparedness and response drills conducted at provincial level, incorporating gender-based violence survivors.	0 (2023)	9 (2024-2027)

IDA PROGRAM DOCUMENT FOR A PROPOSED GRANT FOR SOLOMON ISLANDS

1. INTRODUCTION AND COUNTRY CONTEXT

1. **The proposed Development Policy Operation (DPO) has three objectives and pillars designed to improve: (i) fiscal management, (ii) private sector development, and (iii) climate and disaster resilience.** The operation is the first in a programmatic series of two with a Development Policy Grant (DPG) of US$15 million combined with a Disaster Risk Management (DRM) DPG with a Catastrophe Deferred Drawdown Option (Cat DDO) of US$5 million.[1]

2. **Solomon Islands is a remote archipelago that faces a unique set of development challenges.** The population of 721,000 people is dispersed over 90 inhabited islands, stretching across 1.6 million square kilometers of ocean. Such geographical dispersion, combined with remoteness to international markets, shapes the development challenges. Classified as a fragile, conflict and violence (FCV) affected country, its stretched capacity in government combined with institutional fragility pose a continuous threat to sustainable development. These constraints make the design and implementation of public policy challenging, resulting in large development gaps and persistent fiscal challenges. The need for economic diversification is urgent given over-reliance on a declining logging sector. Attempts to find new sources of economic growth, however, are constrained by several impediments, including an unfavorable business environment.

3. **Solomon Islands is the second most vulnerable country affected by climate change and natural hazards, according to the World Risk Index.** Over the past 30 years there have been seven major disasters, resulting in loss of life and severe adverse economic impacts. In the next 50 years, the country is expected to incur an average annual loss of 5 percent of GDP due to earthquakes and tropical cyclones. Climate change is adversely affecting the country through increased temperatures, intensity of rainfall, storm surge, tropical cyclones, and sea level rise. These trends are expected to exacerbate, making climate change a critical development challenge for the country.

4. **The COVID-19 pandemic tested the ability and resilience to respond to health crises while maintaining the provision of routine health services.** Due to a lack of health emergency preparedness and response, the already fragile health system was overwhelmed during the peak period of virus transmission. One of the lessons learnt from the COVID-19 pandemic is the need for better policies and governance mechanisms when health-related disasters occur.

5. **Poverty was reduced in the last decade, but the impact of COVID-19 has likely reversed that trend.** According to the latest household survey (HIES 2012/2013), around 61 percent of the population was living below the lower-middle income poverty line (USD 3.65 in 2017 PPP terms). An ongoing poverty analysis shows large reductions in multidimensional poverty over the period 2009-2019, driven by broad-based growth. However, the impact of COVID-19, the 2021 civil unrest and the accompanying economic contraction have arguably reversed that trend.

6. **The proposed operation supports the government to improve fiscal management, private sector development, disaster risk and climate change management.** Pillar 1 aims to support fiscal management by reforming the tax system, improving the fiscal regime of the extractives sector, and improving public investment management (PIM). Pillar 2 serves to foster private sector growth by reducing energy costs, diversifying the energy mix, and enhancing private sector credit. Finally, pillar 3 aims to enhance resilience to climate change, natural disasters and health emergencies through policy and regulatory reforms.

7. **The proposed operation is fully aligned with the World Bank's focus on domestic resource mobilization and private sector development.** With prior actions on taxation, credit reporting, and foreign investment, the operation is expected to catalyze domestic resources and address key barriers to private sector investment. Furthermore, it is closely

[1] This operation is fully aligned with GCRF's pillar 4 to strengthen policies, institutions, and investments for rebuilding better. The US$5 million DRM DPG will be financed with US$1.25 million (25 percent) from the Country Allocation, US$1.25 million (25 percent) from the Crisis Response Window, and the remaining US$2.5 million (50 percent) from IDA's general resources.

aligned with the IDA20 Themes on Governance and Institutions, Jobs and Economic Transformation, and Climate Change. The DPO series also aligns well with the IDA20 Special Theme on Fragility, Conflict and Violence (FCV).

8. **Solomon Islands is preparing to host the 2023 Pacific Games and general elections are scheduled in 2024.** In November 2023, Solomon Islands will organize the South Pacific Games. Furthermore, the term of the current Parliament will end in December 2023 with general elections planned in April 2024. Nevertheless, the direction of reform is unlikely to change given the broad political consensus for the key reforms supported by this operation, broad donor support for the reforms, and continuity in the public administration implementing critical steps following political endorsement of reforms. Solomon Islands also has a soundtrack record in reform implementation, including programmatic DPOs.[2]

9. **The macroeconomic policy framework is considered adequate for the purposes of the proposed operation.** Following several years of declining economic activity, growth is expected to average 2.7 percent over the medium term driven by large infrastructure investments, services sector growth, and new investment in the mining and fishing sectors. The fiscal deficit is projected on a declining trend from 4.2 percent of GDP in 2023 to 3.3 percent of GDP in 2026 owing to tax policy reform, economic recovery and unwinding of COVID-19 fiscal support. Public debt is sustainable, and the risk of both public and external debt distress is moderate. The monetary policy stance has started to tighten responding to inflationary pressures. International reserves are projected to decline to 7 months of imports but remain within the reserve adequacy range over the medium term. The financial sector remains relatively stable, with well-capitalized banks and comfortable liquidity levels. Subdued global economic conditions, climate shocks, low levels of cash buffers, and social instability pose downside risks. On the upside, increased participation in regional labor mobility programs may bring additional economic benefits.

2. MACROECONOMIC POLICY FRAMEWORK

2.1. RECENT ECONOMIC DEVELOPMENTS

10. **The post-COVID19 recovery has been dampened by a series of adverse shocks.** Three days of civil unrest in November 2021, the outbreak of COVID-19 in early 2022, and the spike in global food and fuel prices have resulted in three consecutive years of negative growth between 2020-2022. Activity in all sectors remained weak in 2022, while a decline in logging and agriculture production contributed to the economic contraction, partly explained by lower demand for exports. After the full removal of COVID-19 restrictions in July 2022, tourism showed some signs of recovery with increasing arrivals, while the reopening of the Gold Ridge mine contributed to economic activity. Despite weak growth, inflation accelerated sharply, from deflation in 2021 to inflation of 5.5 percent in 2022, driven by higher global fuel and food prices, supply chain disruptions and the civil unrest (Table 1).

11. **The current account deficit more than doubled compared to 2021, reaching 13.3 percent of GDP in 2022.** The decline in exports of logging and agricultural products were only partly offset by a modest increase in tourism and mining receipts and higher export prices. Conversely, higher import prices for food and energy have also significantly contributed to the widening current account deficit. As a result, foreign reserves fell from 11.5 months of imports in 2021 to 9.5 months of imports by the end of 2022. The increase in the current account deficit has been financed through external concessional borrowing and FDI inflows.

12. **Stagnating revenue collection and increasing development expenditures resulted in a widening fiscal deficit, from 3.6 percent of GDP in 2021 to 4.1 percent of GDP in 2022.** Total revenues and grants expanded slightly to reach 32.6 percent of GDP in 2022, supported by revenue collection as well as development grants. The government managed to contain expenditure growth, despite facing substantial spending demands. Expenditure increased from 34.8 percent of GDP in 2021 to 36.8 percent in 2022, explained mostly by the increase in development expenditure on the Pacific Games and to a lesser extent recurrent expenditure. The increase in expenditure has been contained by the delayed passing of

[2] All Solomon Islands DPOs that have been evaluated by IEG are rated as moderately satisfactory or above.

the 2022 Budget combined with late disbursement of budget support grants. A draw-down of government deposits helped finance the deficit.

13. **Public debt increased to 16.9 percent of GDP in 2022, up from 13.5 percent of GDP in 2020.** This was due a rising primary fiscal deficit and lagging nominal GDP growth. As part of the COVID-19 response, the government issued domestic development bonds during 2020-22, close to doubling the stock of Development Bonds from SI$360 million at the end of 2020 to SI$650 million at the end of 2021, as the Central Bank of Solomon Islands (CBSI) tripled its purchase of development bonds in the secondary market[3]. Domestic payment arrears accumulated in 2021 (to 0.8 percent of GDP), but the government started clearing the arrears in the second half of 2022 to decline to 0.5 percent of GDP, financed by donor support and domestic borrowing.

Table 1. Key Macroeconomic Indicators

	2020	2021	2022	2023	2024	2025	2026
Real Economy	Annual percent change and sectoral contribution to growth						
Real GDP growth	-3.4	-0.6	-4.1	1.9	2.8	3.1	3.0
Agriculture	-1.2	-0.3	-3.6	0.0	0.4	0.5	0.5
Industry	-0.6	0.4	0.0	0.8	1.0	1.0	0.9
Services	-1.6	-0.7	-0.5	1.1	1.4	1.6	1.6
Consumer prices (period averages)	3.0	-0.1	5.5	4.7	3.7	3.3	3.3
Public sector finances*	Percent of GDP, unless otherwise indicated						
Revenues and grants	33.4	31.2	32.6	28.8	30.8	31.4	31.3
Expenditure	36.0	34.8	36.8	33.0	35.3	34.8	34.6
Overall fiscal balance	-2.5	-3.6	-4.1	-4.2	-4.5	-3.4	-3.3
Foreign financing (net)	1.4	1.1	2.1	0.1	2.4	2.3	0.8
Domestic financing (net)	1.0	2.6	0.6	4.1	2.9	2.1	3.2
Public debt	13.5	15.4	16.9	20.1	23.5	25.6	27.2
of which external debt	9.9	9.5	11.2	13.8	14.9	15.9	15.4
Balance of Payments	Percent of GDP, unless otherwise indicated						
Current Account Balance	-1.6	-5.1	-13.3	-12.7	-10.2	-9.8	-7.9
Exports	27.9	26.8	24.4	29.5	27.2	25.8	25.0
Imports	36.2	40.1	45.4	48.0	44.4	42.4	39.6
Overall balance (BoP)	4.8	2.5	-0.4	-5.0	-1.6	-2.5	-0.8
Gross official foreign reserves (US$, million)	660.6	694.5	641.0	560.7	541.7	498.9	485.5
In months of next years' imports	12.8	11.5	9.5	8.4	8.0	7.4	7.0
Memorandum items:							
Nominal GDP (US$, million)	1,536	1,545	1,596	1,691	1,808	1,921	2,039
SIG Deposit Account and others (% of GDP)	1.0	0.9	1.8	1.7	1.6	1.5	1.4
Credit to private sector (annual % change)	0.3	-0.4	0.8	2.0	3.5	5.0	5.0
Exchange rate (SI$/US$, period average)	8.2	8.0	8.2	.	.	.	.

Note: *Central Government Operations. Source: World Bank, IMF, SIG.

14. **Despite inflationary pressures, the Central Bank of Solomon Islands maintained an accommodative monetary policy[4] throughout 2022 to support the recovery.** After a deflationary period in 2021 reflecting subdued domestic activity, inflation more than doubled from 4.3 percent in June 2022 to 9.1 percent in December 2022 reflecting higher import prices and the incipient economic recovery. In response to rising inflationary pressures, CBSI tightened its monetary policy stance in March 2023, and raised the cash reserves ratio from 5 percent to 6 percent. The Central Bank continued to manage the exchange rate as a peg against a basket of currencies, which overall remains an appropriate anchor. However,

[3] CBSI does not expect further government bond purchases, although it did not rule out a possibility of taking measures to stabilize the market under exceptional circumstances (IMF Article IV May 2023). The 2023 amendment of the CBSI Act allows CBSI to buy and sell treasury bills in the primary market for monetary policy purposes. Complementary provisions are, however, needed to ensure that such primary market purchases are only used in exceptional cases, under key safeguards that specify clear conditions (e.g., declaration of public emergency) and relevant restrictions (e.g., terms of purchase and repayment).

[4] The Central Bank uses the exchange rate and cash reserves as main monetary policy tools, not interest rates. There is no target inflation rate. Given weak transmission channels, only a limited impact is expected from monetary policy actions.

the exchange rate is overvalued, highlighting the need to review the currency basket. The credibility of the basket exchange rate regime is preserved by maintaining an adequate level of gross official reserves.

15. **The financial system has shown relative stability during recent adverse shocks.** Banks have been well capitalized, with comfortable liquidity levels. Non-performing loans (NPLs) in the banking sector, while still high relative to peers, declined from 11.8 percent in 2020Q2 to 10.9 percent in 2022Q2. Profitability indicators have also been improving compared to lows during the pandemic. Private sector credit (supported by reforms under PA5/IT5) started to recover in 2022Q3 to reach 31.9 percent of GDP in 2022, following almost two years of standstill. Vulnerabilities stem from further asset quality worsening, weak risk-based supervision capacity and gaps in early intervention, bank resolution, crisis preparedness and the financial safety net. Structural constraints create high costs of financial intermediation reflected in high deposit and lending rate spreads (9.3 percent lending rate compared to 0.47 percent deposit rate in May 2023).

Table 2. Selected Fiscal Indicators

	2020	2021	2022	2023	2024	2025	2026
	Percent of GDP, unless otherwise indicated						
Total revenue and grants	33.4	31.2	32.6	28.8	30.8	31.4	31.3
Total revenue	24.6	22.6	23.0	23.1	24.3	25.0	24.8
Tax revenue	21.1	19.5	20.6	20.1	20.6	21.3	21.2
Income and profits	7.3	7.8	7.5	6.6	7.2	7.4	7.4
Goods and services	4.8	4.0	5.2	5.6	6.6	6.6	6.6
International trade and transactions	8.6	7.2	7.5	7.3	6.4	6.9	6.7
Of which: Tax on logging	3.8	3.2	2.7	2.4	2.1	1.9	1.8
Other revenue	3.5	3.1	2.3	3.1	3.7	3.7	3.7
Of which: Mining revenue	0.0	0.0	0.1	0.1	0.2	0.3	0.3
Grants	8.8	8.7	9.7	5.7	6.6	6.4	6.4
Budget support grants	4.3	2.9	2.6	2.9	.	.	.
ADB	0.6	0	0.3	0	.	.	.
China	0	0.7	0.2	0.2	.	.	.
DFAT	1.0	0.4	1.1	1.1	.	.	.
EU	0.5	0	0.2	0.2	.	.	.
MFAT	0.9	0.8	0.2	0.3	.	.	.
Saudi Arabia	0	0	0	0.3	.	.	.
Taiwan, China	0.6	0	0	0	.	.	.
World Bank	0.8	1.0	0.7	0.9	.	.	.
Expenditure	36.0	34.8	36.8	33.0	35.3	34.8	34.6
Of which Pacific Games spending	0.9	1.6	0.8	2.6	0	0	0
Of which election spending	0.1	0.1	0.2	1.5	.	0	0
Recurrent expenditure	27.7	26.1	26.4	23.0	22.6	22.7	22.9
Compensation of employees	11.6	11.5	11.6	11.3	11.1	10.9	10.9
Interest payments	0.2	0.2	0.3	0.5	0.5	0.6	0.7
Other recurrent expenditure	15.9	14.3	14.5	9.7	11.1	11.2	11.2
Development expenditure	8.3	8.8	10.3	10.1	12.7	12.0	11.7
Of which: Constituency Development Funds	1.9	2.7	2.6	2.4	2.6	2.5	2.3
Current balance	-3.1	-3.5	-3.5	0.2	1.6	2.3	2.0
Primary balance	-2.3	-3.4	-3.8	-3.7	-4.0	-2.7	-2.6
Overall balance	-2.5	-3.6	-4.1	-4.2	-4.5	-3.4	-3.3

Source: World Bank, IMF, SIG.

2.2. MACROECONOMIC OUTLOOK AND DEBT SUSTAINABILITY

16. **The economy is expected to recover in the medium term, with an average growth rate of 2.7 percent over the period 2023-2026.** The economy is projected to recover in 2023 with 1.9 percent growth, boosted by the 2023 Pacific Games and several large infrastructure projects in the energy and transport sectors. The latter are expected to have a larger contribution to medium-term growth than the Pacific Games infrastructure, which requires repurposing for

productive, post-Games use.[5] The services sector is expected to support growth in the medium term, followed by construction and increased mining activity. An uptick in the labor mobility program is expected to also contribute to economic activity through the remittance channel. Conversely, the projected decrease in logging activity will dampen growth in the primary sector. In the longer term, tourism, still in a nascent stage of development, as well as mining and agriculture, have the potential to become more significant growth drivers.

17. **Inflation is projected to average 3.8 percent during 2023-2026.** Inflation is expected to ease to 4.7 percent in 2023 (from 5.5 percent in 2022) amid cooling energy and food prices and to moderate afterwards. However, the forecasted inflation rate of 3.8 percent remains well above the average inflation rate of 2.7 percent over the past five years (2018-2022), reflecting potential inflationary pressures from the implementation of large-scale infrastructure projects that may create excess demand for certain goods and services.

18. **The current account deficit is projected to remain substantial, averaging 10.1 percent of GDP over the period of 2023–2026.** This is primarily driven by high import demand related to infrastructure investments and a projected decline in logging exports. However, gradual improvement is expected over the medium term with the current account deficit projected to decrease from 12.7 percent of GDP in 2023 to 7.9 percent by 2026. The trade deficit is also projected to improve in the medium term but remains substantial due to limited export growth and high import demand. Furthermore, over the medium-term, official grants (on and off budget) are projected to decline and average around 6.3 percent of GDP (from 8.7 percent in 2021), while FDI inflows are projected to increase steadily, supported by investment reforms included in this operation (Table 4). Official foreign reserves are expected to decline to 7 months of imports by 2026, which is still within the upper reserve adequacy range of 3 to 7.5 months assessed by the IMF.

19. **Large-scale investments for the 2023 Pacific Games combined with expenditures for the preparation of the 2024 elections add to existing spending pressures.** At 4.1 percent of GDP in 2023, SIG spending related to these two priority events have supported the incipient recovery and could contribute to boosting medium-term growth in Solomon Islands, they have also been contributing to domestic financing challenges. As domestic borrowing and budget support loans fell below expectations, the government reduced recurrent and capital spending by an estimated 4.5 percent of GDP in 2023. Recurrent expenditures are limited to essentials – payroll, utilities, health and education – while capital expenditures are restricted to the Pacific Games and the Constituency Development Funds, thereby deferring regular productive public investment. Low cash buffers and lack of financing increase the risk of payment delays and the build-up of arrears. Budget support grants from development partners such as Australia, New Zealand, Saudi Arabia, the European Union and China have contributed to easing financing pressures (Table 2).

20. **The fiscal deficit is projected to decline over the medium term**. After reaching 4.2 percent of GDP in 2023, the fiscal deficit is projected to decline over the medium term, reaching 3.3 percent of GDP in 2026. This partly reflects declining recurrent expenditure and the normalization of development grants after the pandemic and post-Pacific Games. Revenue and grants are expected to stabilize at around 30.6 percent of GDP (2023-2026), below the pre-pandemic period or 35.2 percent of GDP (2018-19), explained by lower revenue from logging and other international trade taxes, and lower donor grants.

21. **Revenue is projected to stabilize at 30.6 percent of GDP in the medium term.** Domestic revenue is expected to improve in the medium term following weak performance in 2021 and 2022, driven by economic recovery and policy reforms (e.g., the passage of Tax Administration Bill). The new VAT Bill, supported by this program, can help consolidate the fragmented tax system and generate additional revenues over the medium term. Fiscal reforms in the mining sector, supported by this program, is expected to boost mining revenue collection. The improvement in domestic revenue is projected to partly offset declining revenue from international trade and transactions (including tax on logging) and grants.

[5] The total budget for the 2023 Pacific Games is estimated at 17 percent of GDP, of which 11 percent of GDP in infrastructure spending. The Games are mostly funded through off-budget grants by bilateral donors, channeled through the National Hosting Authority (NHA) and the Games Organizing Committee (GOC). Maintaining the Games infrastructure is estimated at a yearly 0.5 percent of GDP, which is currently unfunded. Ongoing Public Investment Management (PIM) reforms – including policy actions in the proposed operation – are expected to improve PIM practices, including maintenance spending.

22. **Public spending is expected to consolidate and stabilize at 34.4 percent of GDP over the medium term (2023-2026), in line with pre-COVID averages.** While the implementation of large infrastructure projects, the organization of the 2023 Pacific Games and the preparations for the 2024 general elections resulted in increased spending, the government also reduced recurrent and capital expenditures by an estimated 4.5 percent of GDP in 2023. Over the medium term, recurrent expenditure is projected to stabilize around 22.8 percent of GDP, in line with pre-COVID averages but lower than 26.4 percent of GDP in 2022. Conversely, development expenditure is expected to increase to 11.6 percent of GDP over 2023-2026, up from 8.3 percent in 2020, and in line with sustained needs to investment. Reforms to improve Solomon Islands' public investment management (PIM) systems, including through PA3/IT3, will be crucial to improve practices throughout the whole PIM cycle.[6] In turn, such reforms could boost the sustainability of public investment, fiscal multipliers and their contribution of development expenditures to long-term growth.

Table 3. Public Debt

	2018	2019	2020	2021
		Percent of total		
Multilateral Creditor	**69.0**	**69.0**	**65.4**	**48.8**
ADB	36.8	36.2	36.4	27.1
IDA	28.6	29.5	26.6	20.0
Other multilateral	3.7	3.3	2.5	1.8
Bilateral Creditor	**6.8**	**5.6**	**3.5**	**11.5**
China Exim Bank	6.8	5.6	3.5	2.2
JICA	0.0	0.0	0.0	9.3
Government Securities	**23.7**	**24.9**	**30.8**	**39.4**
Short Term	5.9	8.2	6.0	4.9
Medium and long term	17.7	16.8	24.8	34.5
Total Central Government Debt	**100.0**	**100.0**	**100.0**	**100.0**

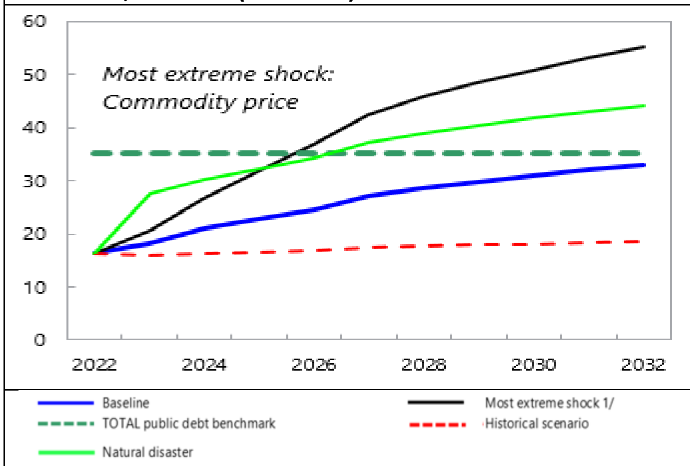
Source: World Bank, IMF, SIG (2023 DSA)

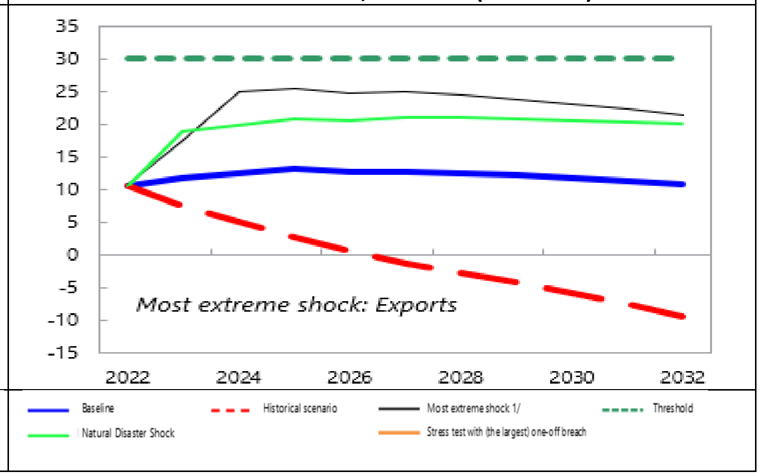
23. **Solomon Islands remains at a moderate risk of debt distress.** An update of the March 2023 Bank-Fund Joint Debt Sustainability Analysis (DSA) concludes that the risk of debt distress is moderate with substantive space to absorb shocks. The majority of public debt is external loans that are contracted at highly concessional terms (Table 3). All external debt indicators remain below the relevant indicative thresholds under the baseline scenario but breach the threshold of the present value (PV) of the external debt-to-exports ratio under an export shock scenario (Figure 1). The PV of the public debt-to-GDP ratio remains below the indicative threshold under the baseline scenario but breaches the threshold under various alternative scenarios including a commodity price shock. A tailored natural disaster shock of a similar scale to the largest historical shock would also cause a significant deterioration in the debt trajectory. While the DSA suggests that there is substantial space to absorb shocks, Solomon Islands faces significant fiscal liquidity challenges stemming from the current low level of government cash balance and rising fiscal risks, including lack of maintenance spending on infrastructure projects. Those projects include large-scale investments to host the 2023 Pacific Games as well as a cell phone tower expansion project. A sizable shift to domestic financing projected in the medium term could bring about risks in debt management.

[6] As highlighted in the 2022 World Bank Public Expenditure Review (PER), total public maintenance spending in Solomon Islands has been falling well short of international benchmarks: in 2019, these represented around 0.8 percent of an assumed replacement value of the public capital stock – well short of the 'gold standard' maintenance spending rate of between 2–5 percent.

Figure 1. Debt Sustainability Analysis

Figure 1.1 Indicators of Public Debt Under Baseline Scenarios, 2022–32 (% of GDP)	Figure 1.2 Indicators of Public and Publicly Guaranteed External Debt Under Baseline Scenarios, 2022–32 (% of GDP)





Source: World Bank and IMF staff estimates.

24. **Solomon Islands completed the FY22 and FY23 Sustainable Development Finance Policy (SDFP) Performance and Policy Actions (PPAs).** In FY22, it enhanced fiscal sustainability by simplifying taxpayer processes and providing the legal basis for the use of e-tax through the Cabinet submission of the Tax Administration Bill. The government also improved debt management by strengthening the governing framework of the domestic debt market, through issuing Operational Guidelines for domestic government bonds. FY23 PPAs included the approval of the VAT Bill – a prior action in this operation – and adherence to a zero ceiling for non-concessional external borrowing (NCB).

Table 4. Sources and Uses of External Financing

	2020	2021	2022	2023	2024	2025	2026
Financing requirements	**30.7**	**83.7**	**217.3**	**220.4**	**190.1**	**196.5**	**169.1**
Current account deficit	25.1	78.3	212.1	214.9	183.9	187.8	161.1
Short term debt amortizations	0	0	0	0	0	0.0	0.0
Long term debt amortizations	5.6	5.4	5.2	5.5	6.2	8.7	8.1
Financing sources	**226**	**218.4**	**233.3**	**76.9**	**131.3**	**112.3**	**150.1**
FDI	5.7	23.1	39.5	41.9	44.1	46.6	49.2
Portfolio investment (net)	-1.5	-6.1	-3.9	-4.2	-4.4	-4.7	-5
Capital grants	62.3	65.7	137.6	73.2	73.2	74.3	76.7
Debt disbursements	86.4	97.4	65.7	51.2	46.9	44.6	44.6
Change in reserves	44.3	38.3	-5.6	-80.3	-19	-42.8	-13.5
IMF credit (net)	28.8	0	0	-4.9	-9.5	-5.7	-1.9
Net errors and omissions	-195.3	-134.7	-16	143.5	58.8	84.2	19

Source: World Bank, IMF, SIG.

25. **Macroeconomic risks are tilted to the downside.** Subdued global economic conditions may reduce demand for commodity exports, in particular demand for logs, with negative impacts on growth, the current account balance, as well as government finances. The country relies largely on capital transfers to finance sustained current account deficits, which increases external vulnerability. Solomon Islands faces significant fiscal liquidity challenges[7] stemming from the current low level of the government cash balance and rising fiscal risks including aid dependency, lack of maintenance spending on infrastructure projects and the build-up of domestic arrears. Solomon Islands remains highly susceptible to climate-

[7] Debt servicing is prioritized and regularly replenished through a debt servicing account. Liquidity shortages arise due to cash management challenges but to address the issue, the government is taking steps towards improving cash forecasting.

related risks. These risks can have far-reaching consequences, including damage to infrastructure and disruption of key economic sectors such as agriculture and fishing. The 2024 general elections increase the risk of political instability and social unrest, accompanied by economic uncertainty. On the upside, the pace of recovery in the tourism sector and increased participation in regional labor mobility programs may bring economic benefits, while the acceleration in infrastructure investment could spur a stronger recovery. Against this background, rebuilding cash buffers and managing fiscal risk becomes even more important given limited fiscal space.

26. **The macroeconomic policy framework is considered adequate for the purposes of the proposed operation.** Following several years of declining economic activity, growth is expected to average 2.7 percent over the medium term driven by large infrastructure investments, services sector growth, and new investment in the mining and fishing sectors. The fiscal deficit is projected on a declining trend from 4.2 percent of GDP in 2023 to 3.3 percent of GDP in 2026 owing to tax policy reform, economic recovery and unwinding of COVID-19 fiscal support. Public debt is sustainable, and the risk of both public and external debt distress is moderate. The monetary policy stance has started to tighten responding to inflationary pressures. International reserves are projected to decline to 7 months of imports but remain within the reserve adequacy range over the medium term. The financial sector remains relatively stable, with well-capitalized banks and comfortable liquidity levels. Subdued global economic conditions, climate shocks, low levels of cash buffers, and social instability pose downside risks. On the upside, increased participation in regional labor mobility programs may bring additional economic benefits.

2.3. IMF RELATIONS

27. **Solomon Islands does not have an ongoing program with the IMF.** The last Article IV Consultation was concluded in May 2023. The Press Release indicated that the economy is recovering from the multiple shocks, supported by the 2023 Pacific Games and the reopening of the borders. The IMF recommended to make progress with the tax reforms, including the approval of the VAT Bill, enhance public investment management, address structural bottlenecks to growth, and improve the fiscal regime of the mining sector, all reform areas supported by this operation. Concessional external financing is deemed necessary to rebuild cash balances and ensure fiscal sustainability.

3. GOVERNMENT PROGRAM

28. **Solomon Islands' development objectives are articulated under the National Development Strategy (NDS) 2016-2035.** The NDS is structured around five national development objectives, namely i) sustained and inclusive economic growth; ii) poverty alleviated across the whole of Solomon Islands; iii) all Solomon Islanders have access to quality health and education; iv) resilient and environmentally sustainable development with effective disaster risk management, response, and recovery; and v) a unified nation with effective governance. The NDS is translated into five-year rolling plans, consisting of prioritized and costed activities which are subject to a monitoring and evaluation framework.

29. **The National Disaster Council (NDC) Act, the National Climate Change Policy (NCCP) and the National Disaster Risk Management Plan (NDRMP) form the policy framework for climate and disaster resilience.** The NDC Act 1989 legislates the disaster management governance arrangements, including the establishment of a National Disaster Council. It also establishes the National Disaster Management Office (NDMO) as the secretariat to the NDC. The NDC Act requires the establishment and maintenance of disaster plans and disaster management committees at the national, provincial, and local levels. SIG is currently undertaking key policy reforms to strengthen its focus on climate and disaster resilience and health emergencies, including a revision of the NCCP (2012-2017), a new National Building Code (NBC) and a Building Standards Bill, all supported by this operation. SIG has also embarked on reforms under the provincial governments' performance-based grants mechanism (Provincial Capacity Development Fund) to mainstream risk into investment planning activities, infrastructure designs and prioritize climate change adaptation measures and strengthen disaster preparedness.

4. PROPOSED OPERATION

4.1. LINK TO GOVERNMENT PROGRAM AND OPERATION DESCRIPTION

30. **The proposed series supports the government's objective to improve fiscal management, support private sector development, enhance resilience to climate change, natural disasters and health emergencies.** Pillar 1 aims to support fiscal management by reforming the tax system, improving the fiscal regime of the extractives sector and a better management of public investments. This is aligned with the government's policy to implement tax reforms for revenue mobilization. Pillar 2 serves to improve the business environment by reducing energy costs, enhancing private sector credit and foreign investment, aligned with the government's policy statement to create and promote more opportunities for business. Finally, pillar 3 is aligned with the government's objective to enhance resilience to climate, natural disasters and health emergencies by updating the climate change policy, increasing resilience of buildings and improving the institutional and regulatory framework for health emergencies.

31. **The proposed operation will strengthen SIG's capacity to respond to natural disasters and health emergencies.** Annually, SIG appropriates a contingency fund under the National Disaster Council Disaster Relief Fund and Contingency Warrants for unforeseen circumstances including natural disasters and health emergencies. Additional funds can also be released from the government's Consolidated Fund during a State of Public Emergency. However, the country is expected to incur an average annual direct loss of over US$20 million due to natural disasters and climate change (PCRAFI 2012). To meet budget shortfalls during emergencies, SIG has opted onto the ADB policy-based Contingency Disaster Risk Facility (CDF). The proposed Cat DDO would complement and expand on these existing disaster risk financing options.

32. **Joint policy dialogue and lessons from previous DPOs/Cat DDOs informed the design of this operation.** The proposed prior actions are largely drawn from the joint Policy Reform Matrix (PRM) of the Joint Policy Reform Group (JPRG). The JPRG is a budget support forum led by SIG, including the ADB, Australian, New Zealand and Japanese governments, the European Union, and the World Bank as members. The 3-year PRM was designed in March 2023 with the World Bank as the lead technical agency and was endorsed by Cabinet in May 2023. Policy actions grounded in robust analytical work and complementary technical assistance were employed as key design principles of the PRM. IEG evaluations and the World Bank's Good Practice Note for DPO design emphasize these principles.

33. **Drawdown triggers.** The Constitution and the NDC Act of 1989 have been reviewed to ensure that proposed drawdown trigger is relevant and appropriate across the statute book available to SIG in times of a disaster, including the coverage needed for public health emergencies.

34. **Proposed Cat DDO drawdown trigger.** No withdrawal shall be made of the Single Withdrawal Tranche unless the Association is satisfied, based on evidence satisfactory to it that, in order to respond to a Natural Disaster:[8] (a) a state of public emergency has been declared by the Recipient's Governor-General in accordance with the manner prescribed in Section 16 of the Recipient's Constitution;[9] or (b) a state of disaster or emergency has been declared by the authorized official of the Recipient in accordance with Section 12 of the National Disaster Council Act 1989.

35. **The key features of the Cat DDO are:**

a) Drawdown period and renewal: The drawdown period for the Cat DDO will be three years and the Cat DDO may be renewed once, for a maximum of six years in total. The adequacy of the macroeconomic framework and satisfactory implementation of the DRM Program will be considered as pre-conditions for renewal.

b) Funding sources: The Cat DDO resources of this operations will be funded through the Solomon Islands' IDA Country Allocation envelope. Of the amount requested, 25 percent will be funded from the IDA Country

[8] Natural Disaster means an imminent or occurring emergency situation, caused by: (i) a cyclone, flood, earthquake, landslide, volcanic eruption, tsunami, drought, or other similar event; or (ii) an epidemic, pandemic, or other public health emergency, that requires the Recipient to promptly mobilize its capacity and/or financial resources, but excluding an emergency situation caused by human induced hazard.

[9] Section 16 of the Constitution can also be used to declare a State of Public Emergency for public health emergencies.

Allocation, with a further 25 percent covered using IDA Crisis Response Window resources: and the remainder of up to 50 percent will be financed by the International Development Assistance (IDA) general resources.

36. **This program is aligned with the goals of the Paris Climate Agreement.** First, the reform program is consistent with the country's climate strategies as well as the resilient and environmentally sustainable development objectives under the NDS. The operation directly supports the mitigation actions related to increasing affordability and accessibility to electricity, including developing renewable energy projects (PA4) and promoting private sector investment and participation in renewables (PA6). On adaptation, PA3, PA7, and PA8 directly support efforts to build climate and disaster resilience. Second, from a mitigation perspective, prior actions PA1, PA2, PA5, PA6 and PA7 are not expected to lead to a significant increase in GHG emissions nor are they expected to introduce persistent barriers to Solomon Islands' transition to low-GHG emissions development pathways. PA3, PA4 and PA8 were further assessed from a mitigation perspective to ensure that potential risks are mitigated by the country's institutional mechanisms. They are not expected to reinforce significant and persistent barriers to transition to the country's low-GHG emissions development pathways. Therefore, all prior actions are aligned with the mitigation goals of the Paris Agreement. Third, in terms of adaptation and resilience dimensions, it is unlikely that climate hazards will impact the contribution of the prior actions to the development objectives. Further, PA3, PA7, and PA8 directly contribute to building Solomon Islands' adaptation and resilience to climate change. Therefore, all prior actions are aligned with the adaptation and resilience goals of the Paris Agreement.

37. **Monitoring policy actions and reforms would occur throughout the three-year term of the operation.** Parallel Technical Assistance will support such monitoring. Ongoing engagement with SIG and the preparation of DPO2 will also support the monitoring, maintain the integrated policy dialogue across the three pillars and leverage support from other development partners.

4.2. PRIOR ACTIONS, RESULTS AND ANALYTICAL UNDERPINNINGS

Pillar 1: Improving Fiscal Management

38. **The objective of Pillar 1 is to improve fiscal management by (i) enhancing the productivity of the tax system, (ii) increasing revenue collection in the mining sector, and (iii) strengthening public investment management.**

Increasing VAT Revenue Collection

Prior Action #1 for DPO1	Indicative Trigger #1 for DPO2
To improve revenue collection, the Recipient has submitted to Parliament the Value Added Tax (VAT) Bill, which taxes goods and services at a standard rate of 15 percent and zero-rates all exports.	To improve revenue collection, the Recipient, through its Cabinet, has approved amended Regulations to introduce new fees and charges for non-tax revenues in Fisheries, Lands, and Commerce and Home Affairs.

39. **The tax system in Solomon Islands is highly fragmented and overly complex, with multiple indirect taxes charged on goods and services.** Indirect taxes that are charged on goods and services include goods tax, sales tax, excise duty, accommodation levy, and stamp duty. There is also fragmentation in terms of the tax bases and applicable rules. As a result, tax productivity on goods and services is low compared to regional peers.[10] Furthermore, a narrow tax base that targets large businesses and excludes many services creates inequity and distortion in taxation of different economic activities. Finally, by imposing a high burden on business inputs, the current tax system discourages specialization and puts exporters at a competitive disadvantage compared to countries with a fully refundable input Value-Added Tax (VAT).

40. **To address inefficiencies in taxation, Cabinet has submitted the VAT Bill to Parliament, which will increase revenue collection and stimulate economic growth (prior action #1).** Recognizing the need to strengthen its tax system, SIG is engaging in a systematic reform of both tax policy and administration. Currently, SIG aims to introduce a VAT (after

[10] Tax productivity – measured as the ratio of tax revenue over household consumption – fell below 10 percent in 2019, lower than most regional peers.

which it will engage in income taxation reform). The VAT Bill proposes a standard rate of 15 percent, a registration threshold of SI$ 2,000,000,[11] with medical, educational, and financial services and bus and taxi fares are exempted. The introduction of VAT is expected to increase revenue collection and promote economic growth by enhancing tax productivity and ensuring export businesses are internationally competitive (by zero-rating exports). VAT is estimated to increase overall tax revenue by 0.7 percent of GDP in the medium (World Bank PER, 2022). In the medium term, the introduction of VAT is expected to have positive poverty and social impacts. With the enactment of the Bill, redundant Tax Acts will be repealed.

41. **As an indicative trigger (#1), the DPO proposes Cabinet approval of amended Regulations in non-tax revenue. Non-tax revenue represents around 13 percent of domestic revenue (3 percent of GDP).** However, many fees and charges are outdated and do not reflect the true cost of government service delivery. Therefore, the government initiated a review of non-tax revenue in Fisheries, Lands, and Commerce and Home Affairs. Each ministry will undergo an in-depth assessment, including a review of the main fees and charges. Following the review, relevant Regulations will be amended to introduce new fees and charges, which is expected to increase non-tax revenue.

42. **The results indicator will measure non-logging revenues, capturing both tax and non-tax revenue reforms.** The introduction of VAT and the revision of fees and charges are expected to increase domestic revenue and improve fiscal management. To capture the impact of these reforms, the results indicator will measure growth in non-logging domestic revenue – relative to GDP and averaged over 2 years, with a target value of 22.4 percent in 2026-2027 (these developments are reflected in the fiscal tables).

Increasing Revenue Collection in the Mining Sector

Prior Action #2 for DPO1	Indicative Trigger #2 for DPO2
To increase revenue collection in the mining sector, the Recipient, through its Minister of Mines, Energy and Rural Electrification, has made the Mine and Minerals (Nickel) (Royalty) Regulations 2023 to determine the nickel royalty based on the contained metal in the ore.	To increase revenue collection in the mining sector, the Recipient, through its Minister of Mines, Energy and Rural Electrification, has issued a Ministerial Order to (i) undertake a third-party review of the fiscal terms of any new mining contracts and (ii) publish the third-party review along with the fiscal terms of the mining contract on the Mining Portal.

43. **The mining sector in Solomon Islands is experiencing a revival, but the governance framework needs improvement, including the fiscal regime.** After the closure of the Gold Ridge mine in 2014, mining activity came to a standstill, contributing less than 0.5 percent of GDP. However, in the second half of 2022, gold production from Gold Ridge restarted. Furthermore, the country contains several sites with nickel deposits, estimated at 180 million tons of nickel mineralization (0.7-1% Ni), which is valued at US$ 43 billion (2,500 percent of GDP). Nickel ranks higher in exportable metal value than gold and bauxite, making it the most precious mineral in the country. For a sustainable mining sector to flourish, however, important governance challenges need to be addressed, including land use and regulatory capacity at central and provincial levels. To do so, SIG is revising its Mining legislation, supported by a World Bank project. Additionally, the government is also reforming the fiscal regime of the mining sector,[12] with support from the IMF.

44. **As a DPO prior action (#2), the government has introduced a nickel royalty on a contained metals basis.** The Mining Act indicates that the royalties rate – set at 3 percent – is imposed on the gross value of minerals. Prior to the reform, nickel royalties were based on a set price per tonne exported. However, the authorities have changed approach

[11] Initially, a lower threshold was envisioned. However, due to capacity constraints in government and complexities in overhauling the tax system, the authorities raised the threshold. Once the implementation is completed and teething issues resolved, the government will gradually bring down the threshold. VAT implementation is supported by a team of five ADB-funded, in-country experts, while the JPRG forum will act as an instrument for continued policy dialogue on the main VAT parameters.

[12] The fiscal regime for extractive mining in Solomon Islands consists mainly of royalties, export duties, profit-based taxes, and mining tenement fees. It is embedded in 3 Acts: the Solomon Islands Mines and Minerals Act (MMA, 1990), the Income Tax Act (ITA), and the Customs and Excise Act. The MMA provides the legal framework for mining in Solomon Islands, including royalties and tenement fees. The ITA regulates Corporate Income Tax (CIT) and Additional Profits Tax (APT), applied to positive net revenue and cash flows of mining companies, respectively. The Customs and Excise Act specifies export duties paid on mineral resources.

and determine the royalty based on the value of the metal contained in the shipment. This approach has several advantages. First, nickel royalties are expected to more than double using this valuation method. Second, it ensures that royalties move transparently with changes in nickel metal markets. Third, it simplifies the information requirements and reduces the administrative burden on government. Finally, this approach would allow to also to tax the by-product cobalt, if it is present in sufficient quantities.

45. **As an indicative trigger (#2), the government will conduct and publish the findings of a third-party review of the fiscal terms for new mining contracts.** In the past, mining investors have been able to secure favorable fiscal terms for their mining projects. For instance, for a nickel mine, the investor was able to obtain a CIT holiday for the initial 4-year life of the mine, despite an internal rate of return of 156 percent. Limited capacity in government and pervasive information asymmetries explain these suboptimal outcomes. A detailed fiscal regime analysis by a third-party expert (the IMF), however, could help in scrutinizing investor assumptions and elucidate the implications of different fiscal regime choices. A detailed Terms of Reference will be developed to ensure a high-quality review and stimulate a close collaboration between the Ministry of Mines and the Ministry Finance. Such analysis is expected to strengthen the government's bargaining power, result in better fiscal terms, increased revenue and benefit in the national interest. The third-party review will be published on the Mining Portal of the Ministry of Mines, together with the fiscal parameters of new mining contracts, increasing accountability.

46. **The results indicator measures growth in revenue collection from nickel mining.** The new valuation method and the fiscal review are expected to increase nickel revenue. The results indicator measures the nickel royalty per dry tonne, which for 2023 is estimated at US$ 1.2 when based on a set price per dry tonne. With the reforms implemented, the nickel royalties are expected to increase to US$ 3 per dry tonne.

<u>*Strengthening Public Investment Management*</u>

Prior Action #3 for DPO1	Indicative Trigger #3 for DPO2
To strengthen public investment management, the Recipient, through its Ministry of Finance and Treasury, has issued a Ministerial Order which establishes a framework for managing externally financed public investments, including climate change impacts as one of the guiding principles.	To strengthen public investment management, the Recipient, through its Ministry of Finance and Treasury, has issued the Public Investment Management Guidelines that govern the appraisal, selection, implementation, and monitoring of externally financed public investment projects.

47. **Addressing the large infrastructure gap in Solomon Islands requires a sound Public Investment Management (PIM) system, which currently faces many weaknesses.** Inadequate investment is germane to many of Solomon Islands' growth and development challenges. Chronic underinvestment materializes in several ways, including the small and declining capital stock plus severe shortages of essential infrastructure. For instance, only 15 percent of the road network is in fair-to-good condition. The inherent risks of natural disasters[13], likely to worsen with climate change, present a further challenge by hastening the degradation and destruction of public assets. The government is addressing the investment gap with a large, externally financed public investment pipeline, estimated at more than 80 percent of GDP over the 2022-2027 period. Managing these investments requires a sound PIM system, which is currently lacking. For instance, investment plans are only weakly integrated with project selection and budgeting processes. Effective appraisal is constrained by a range of structural limitations, including the absence of a proper appraisal process. Finally, the country lacks an effective institutional framework for analyzing and addressing maintenance needs (World Bank PER, 2022).

48. **DPO prior action (#3), the Ministry of Finance and Treasury has approved a climate-resilient public investment framework and a PIM Steering Committee.** To improve the PIM system, the Minister of Finance and Treasury has issued a Ministerial Order to establish a new framework for regulating for externally financed projects, which comprise more

[13] Data shows that most past disasters in Solomon Islands are climate induced. With climate change, the frequency and severity of these disasters will continue to increase in the future.

than 90 percent of total public investment. The framework promotes climate-resilient public investment for sustainable economic growth and poverty reduction.[14] The Ministerial Order outlines the main institutional elements of the new framework, i.e., a PIM Policy, PIM Guidelines and Manual, a PIM Chapter in an amended PFM Act, and includes a roadmap for the introduction of the different elements. Additionally, the Ministerial Order establishes a PIM Steering Committee (PIMSC), which will provide executive oversight on the PIM reform agenda. Once fully implemented, the new framework is expected to address many of the current PIM weaknesses by improving appraisal, selection and project implementation and maintenance.

49. **As an indicative trigger (#3), the DPO proposes the issuance of Public Investment Management Guidelines to govern externally financed public investment projects.** The PIM Guidelines will provide a procedural framework to govern the different stages of the PIM cycle, i.e., proposal, appraisal, selection, implementation, and monitoring and evaluation. The Guidelines will include detailed appraisal and selection criteria – including a focus on climate resilience, an assessment of the funding source, and procedural documentation such as project appraisal and life-cycle cost analysis templates.

50. **The results indicator will measure compliance with the new PIM Guidelines.** Currently, the appraisal of externally financed public investments is limited to a debt sustainability analysis by the Debt Management Advisory Committee (DMAC). With the new PIM Guidelines, the appraisal process will be significantly expanded, including an economic analysis and a climate-resilience assessment, following detailed procedures. By 2027, the target is that all externally financed project proposals are appraised following the PIM Guidelines.

Pillar 2: Creating the Enabling Environment for Private Sector Development

51. **The objective of Pillar 2 is to create the enabling environment for private sector development by (i) reducing electricity tariffs and diversifying the energy mix, (ii) strengthening credit information systems and boosting access to credit, and (iii) promoting private investment.**

Reducing Electricity Tariffs and Diversifying the Energy Mix

Prior Action #4 for DPO1	Indicative Trigger #4 for DPO2
To reduce electricity tariffs and diversify the energy mix, the Recipient has submitted to Parliament the Electricity (Amendment) Bill which amends: (i) the mechanism for setting the rates and scales of electricity tariffs, and (ii) the definition of installation to allow for the inclusion of renewable energy generation equipment.	a) To reduce electricity tariffs and diversify the energy mix, the Recipient, through its Cabinet, has submitted to Parliament the Energy Sector Bill which *inter alia* removes barriers to private sector participation in the energy sector and establishes an energy regulator. b) To reduce electricity tariffs and diversify the energy mix, the Recipient, through the Minister Mines, Energy and Rural Electrification has revised the Electricity Tariff Regulations.

52. **Electricity tariffs in Solomon Islands are among the highest in the world, posing substantial challenges to private sector development**. With an average tariff of 0.7 US$ per kilowatt-hour (kWh) in 2021, electricity prices were over four times the global average (0.165 US$/kWh) and more than double the regional average (0.3 US$/kWh). Low access to grid connected electricity, near total reliance on imported diesel fuel for power generation, high cost of generation, and low on-grid renewable energy penetration are among the factors that contribute to high electricity tariffs.[15] Solomon Islands Electricity Authority (SIEA) is responsible for the electric power generation, transmission, and distribution to all urban centers. Electricity tariffs are set on the recommendation of SIEA (with the approval of the Minister of Mines, Energy and Rural Electrification). High energy prices contribute to the already high costs of doing business in Solomon Islands, eroding

[14] The PIM Framework aims to improve the efficiency of externally financed public investments by having climate resilience as one of the guiding principles. This will be achieved by ensuring that the PIM Policy and Guidelines do not compromise the well-being of the present and future generations and take into account climate change impacts (PIM Framework, p. 4). While still to be developed, the Guidelines are expected to include a hazard and risk information section and a costing rubric to assess the maintenance costs needed to reduce the impacts of climate change and natural disasters.
[15] Renewable energy contribution in the electricity grid is 2 percent in Solomon Islands. The Tina River Hydropower Project (15 MW) will provide an estimated 68 percent of the share of renewable energy on the Honiara Grid when the hydropower facility is commissioned. Through a World Bank-funded additional 2 MW of grid connected solar will be commissioned by mid-2024.

margins, and reducing competitiveness, especially for small and medium-sized enterprises (SMEs). Reforms to transition to a cost-reflective tariff and move towards independent regulation in the energy sector would help to promote private sector development.

53. **The Government is prioritizing electricity sector reforms through an amendment of the Electricity Act (Prior Action #4).** First, the amendment adjusts the definition of installation to include any electricity generation equipment. As such, it clarifies the regulatory ambiguity on the development and installation of renewable energy generation to support the expansion of renewable energy in Solomon Islands.[16] Second, at the request of Cabinet, the amendment would allow the Minister of Mines, Energy and Rural Electrification (MMERE) to set the tariff on recommendation of the Director of Energy, after the Director consults with relevant stakeholders. The amendment thus promotes greater independence and transparency in the tariff setting process as a first step toward independent regulation in the energy sector.

54. **Continued reforms to restructure the electricity sector through a new Energy Sector Bill and the revised 2016 Electricity Tariff Regulations (Indicative Trigger #4) are required to further lower electricity tariffs.** These reforms will repeal the existing Electricity Act, remove the upfront barriers to private sector participation in the energy sector and create the legal basis to establish an energy regulator. The regulator would allow for an independent review of electricity price setting, to ensure that decisions on electricity tariffs and participation in the market for generation and distribution of electricity are transparent and promote the interests of consumers. The revised Electricity Tariff Regulations could introduce a new mechanism for electricity tariff setting for both base tariffs and tariff adjustments, which would be under the mandate of the regulator.[17] These sector reforms combined with least cost planning, the promotion of cost efficient renewable energy generation and a diversification of the energy mix would contribute to reducing electricity tariffs.

55. **The supported reforms are expected to reduce electricity prices and facilitate the expansion of renewables in the energy mix while easing binding constraints to private sector development**. The amendment of the Electricity Act combined with sustained reforms under the Energy Sector Bill and the Electricity Tariff Regulations are expected boost the independence and transparency of tariffs setting, encourage private sector investment in the sector, and increase the share of renewables in the energy mix. Further, these reforms are expected to create market opportunities for private sector investments in renewable energy generation, create new green jobs, and reduce Solomon Islands' dependency on fossil fuels. Lower energy prices would reduce the costs of doing business, improving margins and competitiveness. The first results indicator measures the decline in the electricity tariff differential relative to structural peers in the region - Kiribati, Samoa, and Vanuatu - from US$ 0.3/kWh in 2021 to US$ 0.2/kWh in 2027. The second results indicator measures the increase in the share of renewables in the energy mix (excluding Tina River), from 2 percent in 2022 to 5 percent in 2027.

Strengthening Credit Information Systems and Boosting Credit Access

Prior Action #5 for DPO1	**Indicative Trigger #5 for DPO2**
To increase access to credit, the Recipient has submitted to Parliament the Central Bank of Solomon Islands (Amendment) Bill 2023 ("CBSI Bill"), which permits the use of credit information for the purpose of improving the quality of bank credit and non-bank credits (CBSI Bill Clause 16).	To increase access to credit, the Recipient, through its Cabinet, has approved an amendment to the 2016 Credit Reporting Regulations which *inter alia* implements comprehensive credit reporting.

56. **Access to financial services and credit are major challenges for both individuals and firms in Solomon Islands while the gender gap is much higher than for most peers in the region.** The gender gap in financial services remains at 15 percent which is much higher than most peer countries in the region and the global average of 8.3 percent.[18] Three out of four adults do not have access to a bank account, compared to only one out of three in Fiji. Women are

[16] The amendment of the Act would also delete the definition of 'prime mover', i.e., a machine supplying mechanical electricity to a generator.
[17] The revision of the 2016 Electricity Tarif Regulations would need to be preceded by a cost-of-service study.
[18] PoWER Women's and Girl's Access and Agency Assessment: Solomon Islands, 2020.

disproportionately affected: only 20 percent of women have access to a bank account compared to 32 percent for men. Similarly, banks have more men than women clients with a gender gap of ten percent in active users, nine percent in active depositors and 35 percent in formal credit. Women in Solomon Islands are more likely than men to turn to informal financial services (e.g., informal savings clubs) to meet their financial needs (88 percent of which are women). Women are also less likely to have access to land titles needed as collateral for credit. In addition, at only 32 percent of GDP, private sector credit has been stagnating and is one of the lowest amongst Pacific Island economies. The current credit information ecosystem contributes to these outcomes among others because the credit information currently collected and used is based on negative credit events only (e.g., missed payments and defaults). Negative credit reporting can make it difficult for lenders to make informed decisions about borrowers' creditworthiness and could result in some being unfairly excluded from credit, in addition to creating distortions in pricing and misallocation of loans.

57. **The Government is committed to boosting financial inclusion through the improvement of the credit infrastructure and a transition to comprehensive credit reporting.** As a first step, the amendment of Section 29 of the Central Bank Act removed the restriction limiting the use of the credit reporting from bank-only credit to include other forms of credit (Prior Action #5). Without the amendment, only banks would be able to access CBSI data, which in turn would put non-bank lenders at increased risk as banks will reject the poorer quality borrowers. Further, non-bank institutions will most likely be customers of the banks so their borrowing facilities could also be at risk of being a loss for the banks due to their customers not repaying. The amendment is a necessary first step to support the key roles and functions of CBSI as a supervisor and licensor and update the credit regulations framework to enable the introduction of comprehensive credit reporting.

58. **The amendment of the 2016 Credit Reporting Regulations would support the implementation of comprehensive credit reporting (Indicate Trigger #5).** The transition from negative to comprehensive credit reporting will enable financial institutions to make more efficient and accurate credit decisions and expand access to credit. The updated regulations would allow CBSI to mandate the contribution of negative and positive data from financial institutions and nonregulated lenders to voluntarily provide similar credit data.[19][20] It would allow for the collection, processing and sharing of alternative credit data such payment history data (with the consent of the borrower) and include a wider membership catchment such as banks, non-bank lenders, major retailers, microfinance institutions, insurance, and utility companies. The amended Regulations existing would be expanded to allow for an applicant to apply for a license to operate a Credit Bureau and for CBSI to subsequently deal with such an application.[21] In addition, the amendment would also provide rules of reciprocity, mechanisms for self-enquiry and dispute resolution, free annual credit reports, and penalties for gross negligence. These reforms are informed by IFC technical assistance and support the Government's National Financial Inclusion Strategy (2021-2025) to increase financial inclusion and deepening by building financial capability, expanding access to financial services, and enhancing the financial infrastructure.

59. **The introduction of comprehensive credit reporting is expected to improve access to credit through more accurate credit decisions, reduction in default risks, lower interest rates, and improvements in regulatory oversight.** Comprehensive credit reporting will help financial institutions make more efficient and accurate credit decisions, at lower costs, which could expand access to credit for individuals and businesses that have previously been excluded. Through IFC's Comprehensive Credit Reporting Project, authorities at CBSI have already commenced training, undertaking a field trip to Cambodia. By providing lenders with a more complete and clearer picture of borrowers' credit history, financial health, and behavior, it could help to reduce the risk of default and improve the overall quality of loan portfolios. Through a more accurate assessments of risks, comprehensive credit reporting may be able to lower interest rates to borrowers

[19] Repayment history, credit limits, address changes and utility payments.

[20] The proposed legislative and regulatory environment will provide robust protections for data security and data privacy. Sensitive credit information will only be able to be shared with a borrower's consent and used only for proper purposes. Lenders may only access information with consent and only as part of a credit application, for revision of an already existing facility or for other approved purposes. Credit information is maintained on secure servers, hosted in safe and secure places, supported by business continuity processes and procedures. Central Bank audits credit bureau activities and compliance with confidentiality requirements.

[21] Preceding the amendment, the existing credit bureau operator, Credit and Data Bureau (Solomon Islands) Ltd (CDBSI), has not applied for a license to operate.

with good credit histories, which could help make credit more affordable and accessible. The result indicator tracks the increase in domestic credit to private sector from the 2021-2022 average of 32.1 percent of GDP to an average of 35 percent of GDP in 2026-2027[22].

60. **The supported reforms boost financial inclusion and are expected to have a disproportionately positive impact on female borrowers.** While financial institutions will save on costs spent on reviewing loan applicants, the availability of more comprehensive data is expected to decrease the credit gap for previously excluded individuals as well as MSMEs. Given that women in Solomon Islands are less likely to have access to a bank account and land titles needed as collateral and for developing a credit history, the transition to comprehensive credit reporting would help women build a "reputational collateral" to include a broader range of financial behaviors and making it easier to establish creditworthiness based on a wider set of factors (e.g., payment history – including borrowing histories of women lending from informal sources such as saving groups or utility payments data). Comprehensive credit reporting could also address some of the gender biases inherent to negative credit reporting systems (income disparities, breaks in income due to caregiving responsibilities etc.). The impact on access to finance for the underserved, especially for women, could be significant. Evidence from the introduction of comprehensive credit reporting in Cambodia shows an increase of 25 percent and 24 percent in the value of first-time loans to women and to self-employed, respectively. The results indicator tracks the increase in the share of loans granted to women as percent of total from 12 percent (2022) to 17 percent (2027).

Promoting Private Investment

Prior Action #6 for DPO1	Indicative Trigger #6 for DPO2
To promote private investment, the Recipient, through its Cabinet, has approved the Solomon Islands Investment Policy and Promotion Strategy, which sets out a framework for streamlining the process of doing business, protecting investors, simplifying investment admission and establishment, and establishing a new Investment Promotion Authority.	To promote private investment, the Recipient, through its Cabinet, has submitted to Parliament an amendment to the Foreign Investment Act, which *inter alia* introduces greater transparency and predictability for investment by modernizing arbitration laws, establishing an investor grievance mechanism, and promoting regulatory independence.

61. **Private sector development in Solomon Islands has been hindered by under-investment due to a complex regulatory environment coupled with a lack of coherent requirements and limited protections for foreign investors**. During the last decade, FDI inflows averaged at 2.2 percent of GDP, less than half of the average for Pacific Island Small States at 4.8 percent of GDP. There are significant untapped investment opportunities in sectors such as tourism, agriculture, and fisheries. Although in terms of ownership restrictions on foreign capital Solomon Islands is one of the most open countries to FDI, below potential outcomes point to the fact that additional reforms are needed for boosting private investment and attracting FDI. As highlighted in the 2016-2035 National Development Strategy, reforms to improve business and investment climate could play a pivotal role in fostering investment and economic growth. Benefits would translate through multiple channels including employment creation, knowledge and technology transfers, increased productivity, private sector growth, and export competitiveness.

62. **To address these challenges, the Government has prepared the Solomon Islands Investment Policy and Promotion Strategy (SIIPPS) which is intended to facilitate an increase in sustainable private investment, both domestic and foreign.[23]** The SIPPS addresses some of the key regulatory and business environment constraints that investors face as well as improves marketing, investor entry and aftercare services. The investment policy part of the SIIPPS includes specific measures easing registration and entry requirements, improving flexibility for land ownership and in financial procedures, fast-tracking utilities reform, removing restrictions and opening up investments in alternative and renewable

[22] Following the launch of a comprehensive credit reporting system in Fiji in 2019, credit to private sector increased from 101 percent of GDP in 2019 to 134 percent in 2021, to then decline to 119 percent in 2022.

[23] In Solomon Islands, an approved Policy is the first step in the legislative reform process. That is, without a Cabinet-approved Policy, the executive cannot engage in any further legislative reform.

energy[24], liberalizing agricultural and other sector-specific policies, and establishing a competition policy. The investment promotion component outlines an investment promotion strategy as well as the establishment of a new Investment Promotion Authority (IPA)[25]. The investment promotion strategy targets marketing of specific industries and activities including through improvements in the regulatory environment, provides investors services to facilitate the establishment of new investment, and aftercare support aimed to retain established investments and encourage reinvestment.

63. **The Solomon Islands Investment Policy and Promotion Strategy prioritizes a number of policy reforms to improve inward investment.** Central to these reforms is an amendment to the Foreign Investment Act (FIA) of 2005 (Indicative Trigger #6). A formal review of the act will begin with the adoption of the SIIPPS and will focus on investment entry and establishment, investor protection and dispute resolution. Amendments to the FIA, and other acts and regulations, will be drafted and submitted to Cabinet for review in 2024. The World Bank is providing technical assistance to the government with the amendments.

64. **Streamlined investment procedures, greater market access, and improved investor services will encourage local and foreign entrepreneurs to enter the market and expand their businesses.** The supported reforms to open market access to FDI, simplify investment admission and establishment and strengthen investment protection and promotion are expected to attract more foreign investors to Solomon Islands, leading to an inflow of capital, technology, and knowledge, thereby contributing to economic growth and development. They also complement IFC's Solomon Islands Tourism Investment Facilitation program aimed at spurring private investment in the country's tourism sector. The results indicator tracks the increase in the number of foreign enterprises registered in Solomon Islands and targets a 20 percent increase from 2022, equivalent to 75 enterprises by 2027.

Pillar 3: Improving Resilience to Climate Change, Natural Disasters and Health Emergencies

65. **The objective of Pillar 3 is to improve resilience to climate change, natural disasters and health emergencies by (i) enhancing the policy framework for climate change adaptation and mitigation, (ii) improving the resilience of buildings; and (iii) strengthening public health emergency preparedness, response and recovery.**

Enhancing the Framework for Climate Adaptation and Mitigation

Prior Action #7 for DPO1	Indicative Trigger #7 for DPO2
To enhance climate resilience, the Recipient, through its Cabinet, has approved the National Climate Change Policy (2023-2032) which *inter alia* sets directives to address climate change through adaptation and risk reduction measures.	To enhance climate resilience, the Recipient, through its Cabinet, has submitted to Parliament the Climate Change Bill which *inter alia* provides the legal mandate to the Ministry of Environment, Climate Change, Disaster Management and Meteorology to coordinate, monitor, and report on progress of climate activities.

66. **The National Climate Change Policy (NCCP) 2012-2017 is the overarching policy framework for managing climate change, but it is outdated.** The Policy sets the foundational framework for addressing climate change and disaster risk reduction in Solomon Islands. However, the NCCP is outdated and many provisions articulating the governance arrangements need revision. Furthermore, global warming has accelerated at a faster pace than projected in the past decade and the exacerbating impacts of climate-induced disasters are already felt across the economy.[26] Therefore, the

[24] SIIPPS sets out to explicitly remove restrictions and open up investments in alternative and renewable energy which combined with reforms under PA4 could boost both domestic and foreign investment in these previously untapped sectors and support the expansion of renewable energy coverage. Further, SIIPPS provisions to promote sustainable investment support NDS sustainability objectives for the development of environmentally sound and sustainable practices, principles and regulations for natural resources management to minimize environmental degradation and promote biodiversity conservation.

[25] Considering 124 countries, Harding and Javorcik (2011) show that IPAs targeting sectors explicitly "receive more investment in the post-targeting period, relative to the pre-targeting period and non-targeted sectors" especially when information asymmetries exist. In addition, the study found that a dollar spent on investment promotion increases FDI inflows by $189, and that a new job created costs just $78 in investment promotion.

[26] The Inter-government Panel on Climate Change Committee reported that global warming has surpassed the 1.5ºC level earlier than projected in the period 2010-2020 and that the trend cannot be reversed until after 2050.

Policy needs to be revised to account for new climate projections and include strategies to build adaptive capacities to deal with increased extreme weather events.

67. **The revised NCCP 2023-2032 (Prior Action #7) updates and modernizes the climate change framework for Solomon Islands.** It defines climate change as the biggest single threat to livelihoods, environment, economy and overall wellbeing of people. Building on the NCCP 2012-2017, the updated NCCP introduces new strategies that are critical for tackling climate change, including (i) establishing new institutional mechanisms to coordinate and monitor climate change actions; (ii) developing climate vulnerability assessment and adaptation investment prioritization tools, taking into account nature-based solutions; (iii) developing a new Climate Change legislation, and (iv) accessing to climate financing resources. These directives embodied a fundamental shift towards a whole of society/stakeholder approach to climate change action as well as aim to establish a clear legal mandate to coordinate stakeholders' efforts to optimize the impacts of climate change programs. This shift is critical to strengthen the overall resilience framework and it continues to promote an integrated approach to climate change and disaster risk management.

68. **The Climate Change Bill (Indicative Trigger #7) will strengthen the legal framework to implement and coordinate climate change activities.** The Bill will provide the mandate to the Ministry of Environment, Climate Change, Disaster Management and Meteorology (MECDM) to lead climate change action, and provide the regulatory framework for the directives articulated in the Policy. The NCCP Policy framework will be guided by analytical work and will inform SIG's actions on climate mitigation and adaptation. This work will contribute towards the development objectives articulated in the NDS 2016-2035 as well as its medium-term strategies such as resilient and environmentally sustainable development with effective disaster risk management.

69. **The results indicator ensures all development applications are screened against the climate and disaster risk ordinances developed in at least two provincial government areas.** With support from MECDM, two of the nine Provincial Governments will develop and establish the Ordinances that will delineate disaster-prone areas, where development should not be allowed. In addition, the ordinances will be aligned with the Building Code to ensure that any buildings meet the new resilience standards. It will complement ongoing efforts by MECDM and Ministry of Provincial Government Institutional Strengthening, with of the World Bank funded Integrated Economic Development and Community Resilience Project (IEDCR P173688), to risk-inform investment planning and prioritization of climate adaptation measures implemented under the provincial capacity development performance-based grants. It will also complement the PIM framework supported under PA3.

Improving the Resilience of Buildings

Prior Action #8 for DPO1	Indicative Trigger #8 for DPO2
To improve climate and disaster resilience of infrastructure, the Recipient, through its Cabinet, has approved for submission to Parliament: (i) the National Building Standards Bill 2023; and (ii) the National Building Code, which improve the national building standards and ensure construction methods comply with climate change and disaster resilience measures.	To improve climate and disaster resilience of infrastructure, the Recipient, through the Ministry of Infrastructure Development, has established an operational Building Approval Authority to assess all new public and private building applications against the new National Building Code 2023.

70. **Enforceable building codes are lacking in Solomon Islands, leading to increased risk and liability.** During disasters, safe buildings are fundamental to protecting lives and livelihoods. As natural disasters continue with exacerbating impacts from climate change , the housing/building stock is expected to suffer greater losses without reform, with an average annual loss estimated at 9 percent of GDP (UNESCAP, 2020). Furthermore, in the absence of an enforceable building code, approval of new building applications and issuance of permits has been left entirely at the discretion of respective officers at Ministry of Infrastructure and Development (MID), with no proper due diligence process resulting in unsafe construction practices and substandard building designs.

71. **SIG is committed to addressing the above development challenges through a new National Building Code (NBC) and Building Standards Bill 2023 (Prior Action #8).** This is a critical reform that will establish standards and enforcement mechanisms to improve the resilience of both public buildings and private dwellings against tropical cyclones and seismic/earthquakes, two high risk hazards for the housing stock in the country. The NBC establishes the minimum construction standards and the Bill provides the regulatory framework needed to administer and enforce the NBC. It also establishes a proper due diligence process for reviewing new building applications. The NBC applies acceptable performance standards for structural sufficiency, fire safety, health, and amenity, as well as measures for disaster risk reduction and climate change adaptation, including measures to address wind and seismic parameters. New buildings on customary land and single story buildings less than 40sq.meter are exempted from the NBC requirements to minimize cost increase for low income and vulnerable households. The increased construction cost for buildings bigger than 40 sq. meter and buildings on leased land is expected to be offset by gains resulting from the resilience standards applied[27]. The NBC and Bill have incorporated amendments recommended by the Cabinet to ensure the implementing agency sits with MID, and the NBC will come into effect once the Bill is passed by Parliament and enacted.

72. **The approval of the Building Standards Bill paves the way for the establishment of a dedicated and operational Building Approval Authority (BAA) to assess new building applications and enforcing the NBC (Indicative Trigger #8).** By passing the legislation, the new BAA will have the power to approve and reject new building applications based on the building specifications outlined in the NBC and other construction parameters established. To fully operationalize the BAA, a Chief Building Inspector will be appointed to supervise inspections and to manage the appointed authorized officers. The BAA will be established with operational work plan and annual budget, a physical office space and technical support from development partners, including the World Bank to build capacities. The BAA will coordinate with local authorities to implement and enforce the Code in their respective jurisdictions.

73. **The results indicator measures the degree to which permit applications are assessed for compliance with the NBC for new public buildings and private dwellings.** By 2027, the target is to have all building applications assessed against the NBC in 2 local government areas.

Strengthening Public Health Emergency Preparedness, Response, and Recovery

Indicative Trigger #9 for DPO2
To improve public health emergency preparedness, the Recipient, through its Cabinet, has submitted to Parliament a revised Public Health Emergency Bill to (i) strengthen the governance arrangements; and (ii) improve the regulatory framework for prevention, control and response measures of public health emergencies.

74. **The lack of a clear legal framework for overseeing public health emergencies in Solomon Islands is putting livelihoods at risk.** When COVID-19 broke out, SIG declared a State of Public Emergency under the Solomon Islands Constitution. However, one of the main lessons learned during the COVID-19 pandemic was that a specific regulatory framework was needed to prevent, control, and respond to public health emergencies and reduce loss of life. Furthermore, with climate change, public health emergencies and zoonotic disease outbreaks are likely to increase (World Bank, 2018). The pandemic also exacerbated other social issues, including gender-based violence (GBV), which is highly prevalent in the country[28]. The associated stress, insecurities and restriction of women's mobility and access to employment and care/support services during the pandemic increased women's vulnerability to GBV.

75. **To strengthen the institutional framework for health emergency preparedness and response, the government is developing a Public Health Emergency Bill (Indicative Trigger #9).** The Bill directly addresses the shortcomings of the current framework of public health emergencies by: (i) providing a legal provision for the declaration of a public health

[27] Based on analytical studies, every US$1 spent on infrastructure disaster-resilience saves US$4 in reconstruction cost (United Nations Office for Disaster Risk Reduction)
[28] A Study in 2009 reported 64 percent of women aged 15-49 have reported physical and/or sexual abuse by a partner (Solomon Islands, Ministry of Women, Youth, Children and Family Affairs, 2009)

emergency; (ii) establishing the regulatory and coordination mechanisms needed for detection, prevention, and response; and (iii) mitigating the social, health and economic effects of public health emergencies. The Bill was approved by Cabinet and went through a reading before the Bills and Legislation Committee (BLC). The BLC suggested to further strengthen the regulatory framework and with support of WHO, the government is revising the Bill for final submission to Parliament.

76. **Public health emergency preparedness and response drills, conducted at the provincial level, will serve as the results indicator.** Health emergency drills will be conducted with key response agencies, key stakeholders and non-government organizations who will mainstream the drill exercises in their public health emergency, climate/health resilience and gender-based violence programs and plans. The target is to have all (9) provinces conduct one drill by 2027.

4.3. LINK TO CPF, OTHER BANK OPERATIONS AND THE WBG STRATEGY

77. **The proposed operation is aligned with the priorities laid out under the Country Partnership Framework.** The World Bank Group's Country Partnership Framework for Solomon Islands is structured around three focus areas, namely i) strengthening the foundations of well-being; ii) promoting inclusive and sustainable growth; and iii) managing uneven development. The program development objectives (PDO) of the DPO series – improving fiscal management, improving the enabling environment for private sector growth, and improving climate and disaster resilience – are fully aligned with focus areas of the CPF. The PDO is expected to support Solomon Islands' transition to more sustainable growth and thereby contribute towards the World Bank's mission to end extreme poverty and boost shared prosperity on a livable planet.

78. **The proposed operation aligns closely with broader World Bank Group engagements, including the World Bank's Climate Change Action Plan.** These comprise World Bank projects in the mining, energy, and health sector, IFC's priority to strengthen the country's financial sector, and ongoing analytical engagements, and private sector development. Furthermore, the proposed operation complements the Bank's engagement through the IDA Sustainable Development Financing Policy (SDFP). The approval of the VAT Bill – prior action # 1 – constitutes a Performance and Policy Action (PPA) for FY23. Pillar 3 is aligned with the World Bank Group's Climate Change Action Plan. The Plan notes that climate action is fundamental to alleviating poverty and promoting shared prosperity.

79. **This series has been screened for potential short-and long-term climate and disaster risks.** The screening suggests an overall moderate risk for the project outcome. However, with prior actions on climate resilient public investment management, climate policy, building resilience, and health emergencies, the proposed series is expected to enhance the overarching policy and institutional framework of SIG to manage climate and disaster risks and health emergencies preparedness.

4.4. CONSULTATIONS AND COLLABORATION WITH DEVELOPMENT PARTNERS

80. **SIG has adequate processes in place for public consultations, and these processes have helped shape the design of the DPO reforms**. The SIG Handbook for Legislative Drafting indicates the requirement to conduct consultations when drafting legislation. As such, the VAT Bill has undergone various consultations from an early stage – including provincial consultations and interactions with the private sector – to shape the high-level design as well as the detailed provisions of the Bill (rate, threshold, exemptions). Similarly, the Public Health Emergency Bill, the Electricity Act Amendment, the CBSI Act Amendment and the Building Standards Bill underwent various consultations, the former including scrutiny by the Bills and Legislation Committee. Also, the other policy actions supported by the operation were subject to feedback from various stakeholders, including public sector agencies and development partners.

81. **The DPO series complements and leverages the support of other development partners as well as the Bank's own interventions.** In keeping with the established practice in the region, the specific areas for World Bank support have been identified in close coordination with other development partners under the Joint Policy Reform Group (JPRG). The JPRG is a mechanism for joint budget support dialogue chaired by the Ministry of Finance which has the ADB, Australia, the European Union, Japan, New Zealand, and the World Bank as members. The Bank has been the lead technical agency for the development of the latest joint policy reform matrix (PRM), covering the period 2023-2025. The PRM priorities a

set of critical and government-owned reforms that are implementable over the medium-term. The policy actions included in the PRM are focused around four strategic areas – domestic resource mobilization, public financial management, good governance, economic growth – and are supported by the different members of the JPRG as well as other development partners (IMF, IFC).

5. OTHER DESIGN AND APPRAISAL ISSUES

5.1. POVERTY AND SOCIAL IMPACT

82. **The reforms under the first pillar to improve fiscal management could have positive poverty and social impacts in the medium and long run, conditional on allocating increased revenues into services and investments benefiting the poor.** The replacement of indirect taxes with the new VAT (PA1), the introduction of a nickel royalty (PA2), and the climate-resilient framework for the appraisal of externally financed public investments (PA3) are expected to improve the government's revenue collection and strengthen the effectiveness of public investments. These reforms could translate into improved allocations to social assistance programs and access to basic infrastructure and services, with potentially significant pro-poor benefits in the medium and long run.

83. **The introduction of VAT is expected to have a negligible impact on the poor.** Estimating the net impact of introducing VAT and repealing the current system of goods and service taxes is complicated given the complexity of the tax system and binding data limitations. However, the effective VAT rate for low-income households is expected to be around 3 percent as a large share of their consumption basket is self-produced.[29] Such a tax rate is not significantly different from the current effective tax rate for the poor. Furthermore, a review of 31 low- and middle-income economies indicates that the introduction of consumption taxes is progressive in countries with a large informal sector (like Solomon Islands). Regional experience also suggests that the introduction of the VAT may be progressive. For instance, a recent Fiji Commitment to Equity (CEQ) analysis finds that Fiji's VAT is mildly progressive. Finally, the introduction of VAT in Solomon Islands is expected to increase tax revenue by 0.7 percent of GDP. The reform under PA1 could have positive impacts in the medium term if such increased revenue is directed toward providing services benefiting poorer households.

84. **The reforms under the second pillar should benefit poor people and vulnerable groups.** The decline in electricity tariffs supported by PA4 will benefit all electricity users, including lower-income households. While lower-income households are less likely to be connected to electricity, the decline in tariffs could contribute to improving their welfare. Reforms to introduce comprehensive credit reporting (PA5) would allow financial institutions to make more efficient and accurate credit decisions at a lower cost and is expected to decrease the credit gap for previously excluded individuals and MSMEs. This will result in improved credit allocation at a reduced cost to borrowers, thus increasing financial inclusion, especially for previously underserved such as the poor and vulnerable as well as women[30]. Reforms to improve investment climate (PA6), will boost long-term growth and productivity, with a likely positive poverty and social impacts.

85. **The reforms under the third pillar are expected to have a positive impact on the poor by enhancing resilience against climate and disaster shocks.** Because the poor tend to be disproportionally vulnerable to climatic events and natural disasters, the reforms to update the National Climate Change Policy (PA7) will eventually boost the capacity of the poor to cope with shocks. The National Building Code (PA8) has been designed to minimize its impact on the poor and vulnerable where appropriate.[31] Too stringent building regulations could increase construction costs, limit housing supply, and thereby increase housing prices, further inducing the construction of informal housing in hazardous areas.

[29] Financial, medical, educational and transport services are exempted VAT supplies. The government did consider exempting rice but based on advice by the Health Ministry decided not to given its limited nutritious value. As such the government aims to incentivize the consumption of local substitutes such as yam.
[30] Evidence from the introduction of comprehensive credit reporting in Cambodia shows an increase of 25 percent and 24 percent in the value of first-time loans to women and to self-employed, respectively.
[31] Poor households in informal settlements, especially prevalent in the Honiara area, are not expected to be impacted by the new Building Code. Under the NBC, self-recovery practices can be implemented following a disaster, and upgrading existing capacity is considered a "minor repair" that does not require a permit approval. Furthermore, NBC minimizes the impact of potential cost increases on new private dwelling construction for poor and vulnerable households. Private dwellings on customary land and single-story houses constructed with traditional or mixed traditional-commercial materials not exceeding 40m2 are exempt from the NBC.

5.2. ENVIRONMENTAL, FORESTS, AND OTHER NATURAL RESOURCE ASPECTS

86. **The reforms supported are not expected to have any significant negative impacts on Solomon Islands' environment.** The prior actions to improve fiscal management, strengthening private sector development and framework for climate, natural hazards and health emergencies are not likely to have any significant environmental impacts. For instance, the PIM Guidelines will inform decision making during the appraisal and selection stage of new investments to ensure they are environmentally friendly. The reform under the Electricity (Amendment) Bill to allow for the installation of solar power generation systems will help reduce green-house gas emissions to protect ecosystems. The NCCP promotes environment safeguards measures and nature-based solutions which will contribute to protection of the environment. The incorporation of climate resilience and environmentally friendly practices in the designs of new buildings and construction practices will help reduce negative environmental impacts.

87. **Solomon Islands has a framework in place to safeguard the environment, but interagency coordination strengthening is needed.** The overarching environment management framework is set out under multiple legislations, most notably the Environment Act of 1998. The legislative framework cuts across multiple sectoral agencies' mandates including MECDM, who has the overall mandate for environmental management. With this broad environmental framework, inter-agency coordination is critical for effective implementation. However, while SIG receives technical assistance from development partners, there is a need to strengthen the overall environmental protection framework.

5.3. PFM, DISBURSEMENT AND AUDITING ASPECTS

88. **Overall, the fiduciary risks associated with this operation are substantial.** Significant weaknesses in SIG's core PFM functions contribute to a substantial overall risk. The 2022 IMF Article IV consultation highlighted the need to strengthen fiscal governance and greater transparency through fiscal reforms and priorities such as finalizing the regulations under the PFM Act and ensuring that budget allocations are aligned with development priorities. The external audit function remains weak, with limited scrutiny and follow-up on audit findings. Public investment management is also weak and lacks a proper appraisal process. The most recent PEFA was completed in 2012 and no PFM roadmap is in place. However, many of these challenges are being addressed through government-led reforms and donor supported interventions, including the implementation of a new FMIS (which has generated immediate gains). Budget regulations are being drafted and an IDA funded project to build capacity in the external audit function is currently under preparation.

89. **The 2013 PFM Act provides a strong legal framework for PFM functions, but key subsidiary regulations are yet to be fully developed.** The Act sets out the responsibilities of the Minister of Finance and public officers in managing public funds; establishes an Internal Audit Office; sets rules on the use of Special Funds; sets out requirements for the budget preparation and approval process; restricts the use of virements and contingency warrants; places restrictions on government borrowing, including prohibiting borrowing except for high-priority development projects; gives the Minister power to set procurement rules; and sets requirements on the preparation of public accounts. The PFM law is designed to have subsidiary regulations for each of these functions, but there has been limited progress to put these in place. Only regulations for internal audit, debt management and procurement are currently in place. The procurement regulations enshrine value for money, competition, transparency, and equity as principles of public procurement and provide detailed guidance on procurement practices and responsibilities. For detailed guidance on the other PFM functions, SIG is still operating based on the 2010 Financial Instructions. These Instructions were applied under the previous Public Finance and Audit Act 1978 and remain effective under the PFM Act 2013's transition arrangements, until new regulations are made. The external audit function is also still governed by the Public Finance and Audit Act. However, the Office of the Auditor General (OAG) is currently working on an OAG Policy to strengthen the legislative framework in audit.

90. **There is a significant lag in published audited financial statements for the general government, and these routinely receive disclaimer opinions**. The most recent audit was completed in 2020 for the 2017 public accounts, which were submitted to the OAG in June 2019. The accounts received a disclaimer audit opinion, with the Auditor-General

citing inadequate recordkeeping, weak internal controls and instances of non-compliance with the reporting requirements of the PFM Act and International Public Sector Accounting Standards (IPSAS). The audits for 2012-2015 also received disclaimer opinions. The situation is reportedly improving, especially after a long-running vacancy in the key Accountant-General position was filled in 2018 with support from the New Zealand Government. Furthermore, a World Bank project is in the pipeline to build capacity in the audit function, which is expected to improve scrutiny of public accounts.

91. **The budget is published at the time of initial presentation to Parliament and is available through the MoFT website and in hardcopy from the ministry.** Budget documentation includes a comprehensive presentation of recent economic developments and the outlook, revenue and expenditure trends, policy priorities, and spending performance and activities of all ministries. Within-year fiscal performance is reported monthly through the central bank's regular publications, which are available on its website.

92. **The CBSI annual report, audited and unqualified financial statements and the report of the independent auditor for the 2022 financial year have been published**. The auditor's report contained an emphasis on the reporting framework and the treatment of gold reserves and its variances with IFRS 9 "Financial Instruments", which do not impact on the adequacy of the foreign exchange environment for the use of DPO resources. The CBSI has an established foreign exchange revaluation reserve for the unrealized gains and losses on revaluation of foreign exchange balances. Under the CBSI Act, the CBSI maintains the safety and liquidity of foreign reserves and the returns from reserve asset management, which is achieved through diversification of investments. According to the 2022 annual report, the strategic asset allocation of foreign reserves remains a key part of foreign reserve management. The composition and allocation of foreign reserves holdings by major currencies (USD, AUD, NZD, JPY, GBP) are determined according to the reserve management policy. A minimal amount of EUR, SGD, and Chinese Renminbi is maintained as support of the government's external obligations as well as for investment purposes. CBSI also holds the IMF Special Drawing Rights and IMF Standby Credit Facility.

93. **An IMF Safeguards Assessment was conducted in 2022 and deemed the foreign exchange control environment of the CBSI to be generally adequate but noted weaknesses in the internal control environment.** The Safeguards Assessment analyzed the governance arrangements, internal and external audit, the legal structure, financial reporting, and internal controls of CBSI. While the conclusions regarding the CBSI's foreign currency management environment are generally adequate, the assessment highlights the need to improve controls and alignment of the reserve management framework with leading practices. The assessment further noted that the internal audit function does not provide assurance on the effectiveness of internal controls due to capacity constraints. A 2021 IMF Article IV report noted the need to increase transparency by publishing the composition of the basket of currencies by a regular revision of the basket. The IMF is supporting CBSI to help improve compliance with best practice safeguard standards.

94. **Nevertheless, to mitigate risks of weaknesses in the internal control environment at CBSI, the World Bank requires the measures detailed below:**

a) **Dedicated Foreign Currency Bank Account (DA):** Once the operation becomes effective, implementation of the program is satisfactory and the macroeconomic framework remains adequate, at the request of the Recipient, the proceeds will be deposited by IDA into a DA at the CBSI which forms part of the country's foreign exchange reserves, and the Recipient will promptly deposit an equivalent amount in its local currency budget accounting system. As a due diligence measure, within 30 days of receipt the Recipient will provide a written confirmation to IDA that the amount has been transferred to a local currency account available to finance budgeted expenditures. Therefore, the Recipient shall ensure that upon each deposit of an amount of the IDA financing into the DA, an equivalent amount is accounted for in the Recipient's budget management system, in a manner acceptable to the Bank. The proceeds of the operation would not be used to finance expenditures excluded under the General Conditions for IDA Financing: Development Policy Financing (2018) dated December 14, 2018 (last revised on July 15, 2023) ("General Conditions"). If, after being deposited in a government account, the proceeds of the operation are used for ineligible purposes as defined in the General Conditions, IDA will require the Recipient to refund the amount directly to IDA. Any such amounts refunded to IDA shall be cancelled.

b) **Reporting and Auditing**: Through CBSI, the Recipient will report the deposit of IDA funds into the DA and movement of funds from the DA to its local currency account, ensure that all withdrawals are for eligible expenditures, confirm that the IDA proceeds were received into an account of the government that is part of the country's foreign exchange reserves and that an equivalent amount has been accounted for in the country's budget management system (normally within 30 days after disbursement), and submit a report on receipts and disbursements for the DA. IDA may request the Recipient to submit an audited report of the DA.

95. **The operation will follow IDA's disbursement procedures for DPGs.** Once the operation becomes effective and at the request of the Recipient, the proceeds will be disbursed in compliance with the stipulated release conditions. Disbursement will not be linked to any specific purchases and no procurement requirements will have to be satisfied.

96. **Cat DDO Disbursement.** The funds for the partial or full disbursement of the US$5 million equivalent Cat DDO will be made available after the drawdown conditions are met, as defined in paragraph 36 *"Proposed Cat DDO drawdown trigger"* and in accordance with the Financing Agreement**.** At the request of the Recipient, and with the IDA being satisfied that SIG has declared an eligible state of emergency, the proceeds of the Cat DDO will be deposited by IDA into the Dedicated Foreign Currency Bank Account at the CBSI to finance budgeted expenditures.

5.4. MONITORING, EVALUATION AND ACCOUNTABILITY

97. **Monitoring of the operation will be conducted jointly between the MoFT and donors, under the JPRG.** The MoFT Financial and Economic Development Unit (FEDU) has adequate capacity and is the main office responsible for monitoring the program and all associated outcome indicators. FEDU will provide quarterly reports to the World Bank and other JPRG budget support partners on implementation progress against established timetables and agreed performance indicators. This will be done as part of the established reporting process under the JPRG. The overall reform effort will be reviewed by the Government in close coordination with the World Bank's in-country office and regular joint-donor dialogue to ensure continued implementation of the program within an adequate macroeconomic policy framework.

98. **Grievance Redress.** Communities and individuals who believe that they are adversely affected by specific country policies supported as prior actions or tranche release conditions under a World Bank Development Policy Operation may submit complaints to the responsible country authorities, appropriate local/national grievance redress mechanisms, or the WB's Grievance Redress Service (GRS). The GRS ensures that complaints received are promptly reviewed in order to address pertinent concerns. Affected communities and individuals may submit their complaint to the WB's independent Inspection Panel which determines whether harm occurred, or could occur, as a result of WB non-compliance with its policies and procedures. Complaints may be submitted at any time after concerns have been brought directly to the World Bank's attention, and Bank Management has been given an opportunity to respond. For information on how to submit complaints to the World Bank's corporate Grievance Redress Service (GRS), please visit http://www.worldbank.org/GRS. For information on how to submit complaints to the Bank's Accountability Mechanism, please visit https://accountability.worldbank.org.

6. SUMMARY OF RISKS AND MITIGATION

99. **The overall risk level for the proposed operation is substantial.** Despite the mitigation measures detailed below, there remains substantial overall risk for the achievement of development outcomes. Three risk categories, namely political and governance, institutional capacity for implementation and fiduciary pose a risk to sustained results to DPO reform areas. Residual macroeconomic risk is rated as moderate, but rests on the assumption of a timely DPO disbursement. A delayed disbursement, however, may aggravate the government's cash management challenges, lead to further cuts in recurrent spending, which would undermine service delivery and increase the risk of social instability.

100. **Political and governance risks are substantial, reflecting the possibility for political instability due to the general elections scheduled to take place in April 2024**. The current Parliament's term will end in December 2023, and the

formation of a new government could cause delays in the pace of reform implementation. There is a risk that the Building Standards Bill undergo changes before adoption. The elections could increase the risk of political instability and social unrest, accompanied by economic uncertainty associated with cuts in spending. Nevertheless, the direction of reform is unlikely to change given the broad political consensus for the key reforms supported by this operation, donor support for the reforms, and continuity in the public administration, following political endorsement of reforms. Solomon Islands also has a sound track record in reform implementation, including programmatic DPOs. As a mitigation measure, the proposed reforms are largely drawn from the joint Policy Reform Matrix of the Joint Policy Reform Group, a budget support forum led by the Government. The 3-year PRM was designed in March 2023 and endorsed by Cabinet in May 2023, demonstrating Government commitment. Further, the proposed reforms underwent substantial consultation and are also well aligned with the SIG's medium- and long-term development objectives.

101. **Risks related to institutional capacity for implementation are high, exacerbated by the prioritization of the upcoming Pacific Games and the 2024 general elections.** Governance challenges related to thin administrative and technical capacity, and information failures may pose challenges for the implementation of the proposed reforms. The Pacific Games and upcoming general elections are expected to further strain human resource constraints, posing challenges to government resources and administrative focus. At the program level, delays in lowering the VAT registration (PA#1) threshold in a timely manner could risk the achievement of these reforms' development objectives, mitigated by strong follow-up through the JPRG mechanism. The risk of limited institutional capacity is being mitigated by close and ongoing dialogue with SIG, focusing on a select number of reforms, and ensuring alignment between those policy actions and government priorities. The risk of limited capacity is also mitigated through continued technical assistance from the World Bank (Annex 6) and various development partners to support the implementation of the policy actions. The technical support provided will also focus measures to mitigate risk of over-reliance on donor support and strengthening ownership. This includes building technical capacity across the sectors and putting in place coordination and collaboration mechanisms to optimize the financial resources available.

102. **Fiduciary risks are substantial**. Weak financial management, lack of internal controls, and inadequate systems for financial reporting and auditing of procurement systems are among the main sources of fiduciary risks in Solomon Islands, even after mitigation measures. The procurement process is characterized by weak oversight, limited competition, and a lack of transparency, which increases the risk of fraud and corruption. As mitigation measures, the new Public Procurement Regulations under the PFM Act supported by the previous Second Solomon Islands Transition to Sustainable Growth DPO, introduced binding rules to promote integrity, transparency, and efficiency in procurement, but these measures will take time to be fully implemented and internalized. There is a risk that domestic payment arrears will accumulate, against a background of increased non-performing loans.

Table 5: Summary Risk Ratings

Risk Categories	Rating
1. Political and Governance	Substantial
2. Macroeconomic	Moderate
3. Sector Strategies and Policies	Moderate
4. Technical Design of Project or Program	Moderate
5. Institutional Capacity for Implementation and Sustainability	High
6. Fiduciary	Substantial
7. Environment and Social	Moderate
8. Stakeholders	Moderate
9. Other	
Overall	Substantial

ANNEX 1: POLICY AND RESULTS MATRIX

Prior Actions and Triggers		Results		
Prior Actions under DPF 1	**Triggers for DPF 2**	**Indicator Name**	**Baseline**	**Target**
Pillar 1: Improving Fiscal Management				
Prior Action #1. To improve revenue collection, the Recipient has submitted to Parliament the Value Added Tax (VAT) Bill, which taxes goods and services at a standard rate of 15 percent and zero-rates all exports.	**(Indicative) Trigger #1.** To improve revenue collection, the Recipient, through its Cabinet, has approved amended Regulations to introduce new fees and charges for non-tax revenues in Fisheries, Lands, and Commerce and Home Affairs.	**Results Indicator #1**: non-logging domestic revenue (as percent of GDP)	20.4 percent (2022-2023 average)	22.4 percent (2026-2027 average)
Prior Action #2. To increase revenue collection in the mining sector, the Recipient, through its Minister of Mines, Energy and Rural Electrification, has made the Mine and Minerals (Nickel) (Royalty) Regulations 2023 to determine the nickel royalty based on the contained metal in the ore.	**(Indicative) Trigger #2.** To increase revenue collection in the mining sector, the Recipient, through its Minister of Mines, Energy and Rural Electrification, has issued a Ministerial Order to: (i) undertake a third-party review of the fiscal terms of new mining contract and (ii) publish the third-party reviews along with the fiscal terms of the mining contract on the Mining Portal.	**Results Indicator #2:** nickel royalty per dry tonne (in constant US$)	US$ 1.2 (2023)	US$ 3 (2027)
Prior Action #3. To strengthen public investment management, the Recipient, through its Ministry of Finance and Treasury, has issued a Ministerial Order which establishes a framework for managing externally financed public investments, including climate change impacts as one of the guiding principles.	**(Indicative) Trigger #3.** To strengthen public investment management, the Recipient, through its Ministry of Finance and Treasury, has issued the Public Investment Management Guidelines that govern the appraisal, selection, implementation, and monitoring of externally financed public investment projects.	**Results Indicator #3:** percentage of externally financed project proposals analyzed following PIM Appraisal Guidelines	0 (2023)	100 (2027)
Pillar 2: Creating the Enabling Environment for Private Sector Development				

Prior Actions and Triggers		Results		
Prior Action #4. To reduce electricity tariffs and diversify the energy mix, the Recipient has submitted to Parliament the Electricity (Amendment) Bill which amends: (i) the mechanism for setting the rates and scales of electricity tariffs, and (ii) the definition of installation to allow for the inclusion of renewable energy generation equipment.	**(Indicative) Trigger #4.** 4a) To reduce electricity tariffs and diversify the energy mix, the Recipient, through its Cabinet, has submitted to Parliament the Energy Sector Bill which *inter alia* removes barriers to private sector participation in the energy sector and establishes an energy regulator. 4b) To reduce electricity tariffs and diversify the energy mix, the Recipient, through the Minister Mines, Energy and Rural Electrification has revised the 2016 Electricity Tariff Regulations.	**Results Indicator #4**: 4a) Commercial electricity tariff differential relative to structural peers in the region (Kiribati, Samoa, and Vanuatu, US$/kwh) 4b) share of renewable energy in the energy mix (excl. Tina River)	0.3 (2021) 2 percent (2023)	0.2 (2027) 5 percent (2027)
Prior Action #5. To increase access to credit, the Recipient has submitted to Parliament the Central Bank of Solomon Islands (Amendment) Bill 2023 ("CBSI Bill"), which permits the use of credit information for the purpose of improving the quality of bank credit and non-bank credits (CBSI Bill Clause 16).	**(Indicative) Trigger #5.** To increase access to credit, the Recipient, through its Cabinet, has approved an amendment to the 2016 Credit Reporting Regulations which *inter alia* implements comprehensive credit reporting.	**Results Indicator #5**: 5a) Domestic credit to private sector (as share of GDP) 5b) Loans granted to women (as a percent of total).	32.1 percent (2021-2022 average) 12 percent (2022)	35 percent (2026-2027 average) 17 percent (2027)
Prior Action #6. To promote private investment, the Recipient, through its Cabinet, has approved the Solomon Islands Investment Policy and Promotion Strategy, which sets out a framework for streamlining the process of doing business, protecting investors, simplifying investment admission and establishment, and establishing a new Investment Promotion Authority.	**(Indicative) Trigger #6.** To promote private investment, the Recipient, through its Cabinet, has submitted to Parliament an amendment to the Foreign Investment Act, which *inter alia* introduces greater transparency and predictability for investment by modernizing arbitration laws, establishing an investor grievance mechanism, and promoting regulatory independence.	**Results Indicator #6**: The number of foreign enterprises registered in Solomon Islands.	63 (2022)	75 (2027)
Pillar 3: Improving Resilience to Climate Change, Natural Disasters and Health Emergencies				

Prior Actions and Triggers		Results		
Prior Action #7. To enhance climate resilience, the Recipient, through its Cabinet, has approved the National Climate Change Policy (2023-2032) which *inter alia* sets directives to address climate change through adaptation and risk reduction measures.	**(Indicative) Trigger #7** To enhance climate resilience, the Recipient, through its Cabinet, has submitted to Parliament the Climate Change Bill which *inter alia* provides the legal mandate to the Ministry of Environment, Climate Change, Disaster Management and Meteorology to coordinate, monitor and report on progress of climate activities.	**Results Indicator #7:** Development applications screened against the climate and disaster risk ordinances developed in at least 2 local government areas.	0 percent (2023)	100 percent (2027)
Prior Action #8. To improve climate and disaster resilience of infrastructure, the Recipient, through its Cabinet, has approved for submission to Parliament: (i) the National Building Standards Bill 2023; and (ii) the National Building Code, which improve the national building standards and ensure construction methods comply with climate change and disaster resilience measures.	**(Indicative) Trigger #8**. To improve climate and disaster resilience of infrastructure, the Recipient, through the Ministry of Infrastructure Development has established an operational Building Approval Authority to assess all new public and private building applications against the new National Building Code 2023.	**Results Indicator #8:** Share of permit applications assessed for compliance with the building regulations and code (percent of total).	0 percent (2023)	100 percent (2027)
	(Indicative) Trigger #9: To improve public health emergency preparedness, the Recipient, through its Cabinet, has submitted to Parliament the Public Health Emergency Bill to inter alia (i) strengthen the governance arrangements; and (ii) improve the regulatory framework for prevention, control and response measures of public health emergencies.	**Results Indictor #9:** Number of public health emergency preparedness and response drills conducted at provincial level, incorporating gender-based violence survivors.	0 (2023)	9 (2024-2027)

RESULTS INDICATORS BY PILLAR

Baseline	Closing Period
Pillar 1: Improving Fiscal Management	
Non-logging domestic revenue (as a percent of GDP) (Text)	
Jun/2023	Jun/2027
20.4 percent (2022-2023 average)	22.4 percent (2026-2027 average)
Nickel royalty per dry tonne (in constant US$) (Text)	
Jun/2023	Jun/2027
US$1.2 (2023)	US$3 (2027)
Percentage of externally financed project proposals analyzed following PIM Appraisal Guidelines (Percentage)	
Jun/2023	Jun/2027
0	100
Pillar 2: Creating the Enabling Environment for Private Sector Development	
Commercial electricity tariff differential relative to structural peers in the region (Kiribati, Samoa, and Vanuatu, US$/KWh) (Text)	
Jun/2021	Jun/2027
0.3	0.2
Share of renewable energy in the energy mix (excl. Tina River) (Percentage)	
Jun/2023	Jun/2027
2	5
Domestic credit to private sector (as share of GDP) (Text)	
Jun/2022	Jun/2027
32.1 percent (2021-2022 average)	35 percent (2026-2027 average)
Loans granted to women (as a percent of total) (Percentage)	
Jun/2022	Jun/2027
12	17
The number of foreign enterprises registered in the Solomon Islands (Text)	
Jun/2022	Jun/2027
63	75
Pillar 3: Improving Resilience to Climate Change, Natural Disasters and Health Emergencies	
Development applications screened against the climate and disaster risk ordinances developed in at least 2 provincial government areas (Text)	
Jun/2023	Jun/2027
0 percent (2023)	100 percent (2027)

Share of permit applications assessed for compliance with the building regulations and code (percent of total) (Text)	
Jun/2023	Jun/2027
0 percent (2023)	100 percent (2027)
Number of public health emergency preparedness and response drills conducted at provincial level, incorporating gender-based violence survivors (Text)	
Jun/2023	Jun/2027
0 (2023)	9 (2024-2027)

ANNEX 2: FUND RELATIONS ANNEX

Solomon Islands—Assessment Letter for the World Bank
October 23, 2023

This note provides IMF staff's assessment of Solomon Islands' macroeconomic conditions, prospects, and policies. It is based on available information as of October 19, 2023. This assessment was requested by the World Bank for its Resilience Development Policy Operation with a Catastrophe Deferred Drawdown Option.

Recent Developments, Outlook, and Risks

1. **The economy is recovering after the recent series of global and domestic shocks, but with increases in some macroeconomic imbalances.** The recovery has been driven by infrastructure spending ahead of the Pacific Games in November 2023, although economic activity has been adversely affected by frequent power disruptions in Honiara. Real GDP is projected to grow by 2.5 percent and 2.4 percent in 2023 and 2024, respectively, while the general elections scheduled for April 2024 could temporarily stall economic activity. Inflation eased from 8.5 percent (y-o-y) at end-2022 to 3.9 percent in July 2023, but it is projected to remain above 4 percent until the end of the year on the back of increased demand from the Pacific Games. The large current account deficit of 11.3 percent of GDP is expected for 2023, albeit smaller than previously projected, reflecting lower import prices. The fiscal deficit is projected to widen to 6.3 percent of GDP in 2023, driven by significant fiscal costs of the Pacific Games and the general elections.[1]

2. **A large pipeline of infrastructure projects would support medium-term growth but is fraught with risks.** The economy is forecast to grow by around 3 percent over the medium term, supported by externally financed infrastructure projects, while the impact of declining income from logging activity will be a constraint. Both fiscal and current account deficits are expected to persist in the medium term, reflecting large spending on infrastructure, other tangible and human capital development, and declining log exports. The public debt-to-GDP ratio is projected to reach the authorities' threshold of 35 percent in 2031, driven by concessional external borrowing for infrastructure projects and increasing domestic financing.[2] Reserve coverage is expected to decline as a result, although it is forecast to remain within the adequacy range of four to seven months of imports under the baseline.

3. **Downside risks cloud the outlook.** Ongoing fiscal challenges (discussed below) could hamper the recovery, including through the accumulation of domestic arrears, and potentially increase social instability in the run-up to the general elections and rises in geopolitical tensions. High aid dependency and the shallow domestic financial market will continue to pose risks to fiscal policy implementation. The country remains vulnerable to exogenous shocks such as natural

[1] Staff's projections do not reflect prospects of a shortfall in budget financing that the government is currently facing (discussed below), owing to lack of data and high uncertainty.

[2] The latest Debt Sustainability Analysis in April 2023 indicates moderate risk of debt distress with substantial space to absorb shocks, while the country faces significant liquidity risks and rising fiscal risks including from mismanagement of infrastructure projects.

disasters amplified by climate change, volatile import and export commodity prices, and an abrupt global slowdown. On the upside, stronger-than-expected mineral exports and remittances could improve the external balance and thus shore up output.

Macroeconomic Policies

Fiscal Policy

4. **The government is currently facing a shortfall in budget financing, which is partly being covered by drawing down the government's already thin cash balance.** This is due to shortfalls in donor grants and domestic financing resulting from limited investor appetite for domestic bonds, amid rising spending pressures towards the Pacific Games. In response, the government sought budget support from additional donors, while imposing strict controls on non-Pacific Games expenditures under the amended 2023 budget. The government should tightly control expenditures related to the Pacific Games and the general elections, while carefully managing its fiscal operations in coordination with development partners, to minimize the crowding out of other essential spending and thereby the adverse impact on the ongoing recovery and social stability. The repetitive occurrence of financing shortfalls underscores the urgent need to improve budget planning and public financial management (PFM), including off-budget items.

5. **The government will face significant fiscal challenges after the Pacific Games.** Once the recovery is well established, the government should prioritize rebuilding its broad cash balance, which is being further depleted to cover part of the financing shortfall, to at least two months of total spending.[3] Prudent management of public investment projects, including maintenance, is essential to ensure that the country's large pipeline of infrastructure projects will lead to sustainable growth in line with the economy's absorptive capacity. Reforms to improve the quality and accountability of public expenditure, including through improving PFM and reviewing the Constituency Development Fund Act, need to be accelerated. The recent submission of the Value-Added Tax Bill to the Parliament is welcome, as it could mobilize significant revenues through efficiency gains, together with the tax administration modernization project.

Monetary and Exchange Rate Policies

6. **The Central Bank of Solomon Islands (CBSI) should closely monitor economic developments and be prepared to adjust its policy stance.** While it appears that inflationary pressures have eased and the recovery is ongoing, the central bank should be vigilant to risks such as a hike in global commodity prices and a possible slowdown in the economy after the Pacific Games. The CBSI's efforts to improve its capacity for economic analysis, forecasting, and monetary policy communication, with the IMF's technical assistance, serve these purposes.

7. **The CBSI's effective and independent operation needs to be underpinned by legal safeguards.** The authorities have tabled a bill to amend the CBSI Act to the Parliament, which includes a revision to allow the CBSI to buy and sell treasury bills in the primary market for "monetary policy purposes". While the CBSI emphasizes that primary purchases are intended to be

[3] It is estimated that the government's broad cash balance has been running below one month of total spending for the past few years.

used only when standard monetary policy through the banking system does not work, staff are concerned that the current bill does not adequately provide for safeguards for primary market purchases to ensure that the tool is used only in exceptional cases under clear conditions and restrictions. In addition, it is regrettable that the bill does not include an amendment to remove the voting right of the government representative on the CBSI's Board to ensure its autonomous decision making, as recommended in the IMF's safeguard assessment. On the other hand, the CBSI is in the process of adopting internationally recognized practices for internal auditing, with support from the IMF, in line with the safeguard assessment recommendation.

8. **The current exchange rate regime[4] remains appropriate, but a timely review of the currency basket is called for, given changes in trade patterns.** The current exchange rate regime has helped the authorities maintain a stable macroeconomic environment and contain imported inflation. However, Solomon Islands' external position in 2022 is assessed to be substantially weaker than the level consistent with medium-term fundamentals and desirable policies on the back of the overvalued real exchange rate. While other policies will need to adjust to restore balance, notably on the fiscal side, this assessment highlights the necessity of reviewing the currency basket to ensure that the currency composition and weights of the basket appropriately reflect the country's current trade structure. The IMF stands ready to provide necessary technical assistance for the CBSI.

Financial Sector Polices

9. **Increasing bank lending and enhancing financial integrity remains a challenge.** While the financial sector remains well capitalized and profitable, Solomon Islands continues to lag its peers both in terms of bank lending and access to financial services. Reforms to moderate credit risks for commercial banks such as reducing asymmetric information and facilitating enforcement of contracts, as well as to promote digital financial services, could spur credit growth. Strengthening credit information systems, which is included in the currently proposed amendment to the CBSI Act, would contribute to expanding access to credit. Improving legal and supervisory frameworks for AML/CFT and raising awareness of the risks are essential for ensuring integrity of Solomon Islands' financial systems.

Structural Reforms

10. **Developing new growth drivers, including by addressing governance weaknesses and corruption vulnerabilities, is an urgent priority.** Persistent low economic growth lagging behind population growth and the projected weakness of the external sector highlight the need for policy actions to enhance the competitiveness of the economy, such as in the mining, agriculture, and tourism sectors. Frequent land disputes and ineffective dispute resolution mechanisms remain long-standing obstacles to private sector development. Strengthening governance and fiscal frameworks for the mining sector including through the legislation of the Mining Act is needed to utilize the country's rich natural resources in a sustainable and inclusive manner. Progress in governance reforms and anti-corruption efforts would be further supported by strengthening the independence and capacity of anti-corruption institutions and by strengthening the Office of Auditor General

[4] The Solomon Islands dollar is pegged to an invoice-based weighted basket of currencies consisting of the US dollar, the Australian dollar, the New Zealand dollar, the Japanese yen, and the British pound.

through amending its legal framework consistent with IMF technical assistance recommendations.

IMF Relations

11. The IMF's partnership with Solomon Islands spans both surveillance and capacity building. Solomon Islands is on a standard 12-month Article IV consultation cycle. The 2023 Article IV consultation was concluded by the IMF Executive Board on April 26, 2023. Solomon Islands has received IMF technical assistance, especially through the Pacific Financial Technical Assistance Center (PFTAC), in areas such as revenue administration, debt management, central bank operation, financial supervision, AML/CFT, auditing, and statistics.

ANNEX 3: LETTER OF DEVELOPMENT POLICY

MINISTER OF FINANCE AND TREASURY

MINISTRY OF FINANCE AND TREASURY
P.O BOX 26, HONIARA
SOLOMON ISLANDS

SOLOMON ISLANDS GOVERNMENT

Ref: RF471/10/5

Date: 23rd October, 2023

Mr. Ajay Banga
President
The World Bank
Washington D.C.
20433, USA

Dear President Banga,

Letter of Development Policy

We look forward to continuing our close collaboration with the World Bank through the First Resilience Development Policy Operation with a Catastrophe Deferred Drawdown Option. The Solomon Islands Government's (SIG) program of policy initiatives presented in this letter reflects our vision to continue to build a resilient economic recovery from COVID-19, and to promote long-term sustainable development that will benefit all Solomon Islanders. This vision is set out in detail in National Development Strategy 2016-2035, and in the Democratic Coalition Government for Advancement's (DCGA) 2021 Policy Redirection. The Policy Redirection provides a roadmap to redirect scarce financial and budget resources towards the most urgent and critical pillars of the economy and set a stage for lasting recovery from the global ravages of COVID-19.

A key priority under the Policy Redirection is Tax Reform and Prudent Public Financial Management. To that end, Cabinet has submitted to Parliament the Value-added Tax (VAT) Bill. The VAT Bill is expected to increase tax compliance and reduce tax distortions to competition. To further strengthen domestic revenues, the government has targeted reforms in the mining sector to ensure that future nickel exports are priced competitively. This is a key reform, given the vast potential for future nickel developments.

To address the large investment gap faced, the government has identified the need to strengthen the Public Investment Management (PIM) system, particularly given the large externally financed public investment pipeline over coming years. As a first step, I recently approved a climate-resilient public investment framework and the establishment of a PIM Steering Committee, to promote climate-resilient public investments for sustainable growth and poverty reduction. In line with this framework, the Ministry of Finance and Treasury (MoFT) will work towards developing a PIM Policy, PIM Guidelines and Manual, and amend the 2013 Public Financial Management Act to include a PIM Chapter and provide legal backing to the policy.

To address the high cost of doing business in Solomon Islands, and promote competitiveness, a key initiative of the government has been to address the high cost of electricity. As such, the government has tabled an amendment to the Electricity Act in Parliament, which will open the market for electricity generation to independent power producers and lay the foundations for the establishment of an independent energy regulator. Critically, the revised regulations under the Act would introduce a new formula for electricity tariffs setting for both base tariffs and tariff adjustments, under the mandate of the independent energy regulator, ensuring these are free from bias, protect interests of consumers, and maximize social welfare instead of monopoly rents.

Access to financial services and credit are major challenges for both individuals and the private sector in Solomon Islands. To expand the scope of financial inclusion, the government has sought to improve the credit infrastructure and a transition to more comprehensive credit reporting, where the use of credit reporting now extends to other forms of credit besides bank-only credit. Transitioning from negative to comprehensive credit reporting will enable financial institutions to make more efficient and accurate credit decisions and expand access to credit. Over the medium-term, comprehensive credit reporting may be able to lower interest rates to borrowers with good credit histories, which could help to make credit more affordable and accessible.

The government has also taken steps to facilitate sustainable investments, both domestic and foreign. Under the program, the Cabinet has approved the Solomon Islands Investment Policy and Promotion Strategy, which seeks to boost inflows of greenfield and brownfield FDI, mergers and acquisitions, joint ventures as well as domestic investment. The policy itself outlines specific measures and priorities to improve the investment climate, generate new inward investment, better protect investors, and strengthen aftercare services; while the Promotion Strategy targets the marketing of specific industries and activities including through improvements in the regulatory environment, provides investors services to facilitate the establishment of new investment, aftercare support aimed to retain established investments and encourage reinvestment. These new streamlined investment procedures and reduced regulatory burdens will encourage local and foreign entrepreneurs to enter the market and expand their businesses.

The Solomon Islands Government remains committed to enhancing resilience against climate, disaster, and health-related shocks among the poor and vulnerable groups in the medium and long term. To this end, we have achieved two important initiatives under the proposed development policy operation.

First, the Cabinet recently approved an updated National Climate Policy 2023-2032 to strengthen the institutional framework for addressing climate change and disaster risk reduction. Specifically, the policy aims to (i) improve the enabling environment to address climate change emergencies; (ii) target adaptation actions on key vulnerabilities; and (iii) identify priority implementation arrangements for climate change actions and capacity building. As a next step, the government will seek to pass a Climate Change Bill to provide the legal mandate and clarify the roles and responsibilities of an agency to lead, implement, facilitate, and coordinate climate change activities. The Bill will also provide the basis for updating the parliament on progress on climate action, including on climate finance and its contribution to the development objectives articulated in the NDS 2016-2035.

Second, a new National Building Code (NBC) and Building Standards Bill were recently approved by the Cabinet, being the first ever overarching building legislation and enforceable Building Code for Solomon Islands. The objectives of the NBC are to (i) define minimum standards for all new buildings in Solomon Islands (unless exempt), (ii) enable the issuing of permits and to carry out building inspections, (iii) provide performance standards for wind and earthquake seismic loads; and (iv) build climate-resilient infrastructure and foster environmentally friendly construction practices, including nature-based solutions and the application of the NBC to retrofitting works. The new NBC and legislation are expected to result in improved building practices, improved safety and quality, and better resilience towards meteorological hazards.

Lastly, as a trigger for the second operation in the series, the Government is currently working on finalizing a Public Health Emergency Bill to strengthen health resilience. This need became evident during the recent COVID-19 pandemic, where the health emergency provisions under the existing National Disaster Council (NDC) Act 1989 were deemed inadequate. The new Bill addresses the shortcomings of the NDC Act.

Mr. President, the Government is firmly committed to the implementation of its medium-term reform agenda, as outlined above. Critically the financing under the program will go towards ensuring a continuity in government service delivery, while supporting our efforts towards long-term sustainable and inclusive economic growth and development. The Government and the people of Solomon Islands look forward to continuing our partnership with the World Bank in this earnest and important endeavour.

Yours Sincerely,

MINISTRY OF FINANCE AND TREASURY SOLOMON ISLANDS

Honourable Harry D Kuma, MP
Minister of Finance and Treasury

ANNEX 4: ENVIRONMENT AND POVERTY/SOCIAL ANALYSIS TABLE

Prior Actions	Significant Positive or Negative Environment Effects	Significant Poverty, Social or Distributional Effects Positive or Negative
Pillar 1: Improving Fiscal Management		
Prior Action #1. To improve revenue collection, the Recipient has submitted to Parliament the Value Added Tax (VAT) Bill, which taxes goods and services at a standard rate of 15 percent and zero-rates all exports.	No	Uncertain
Prior Action #2. To increase revenue collection in the mining sector, the Recipient, through its Minister of Mines, Energy and Rural Electrification, has made the Mine and Minerals (Nickel) (Royalty) Regulations 2023 to determine the nickel royalty based on the contained metal in the ore.	No	No
Prior Action #3. To strengthen public investment management, the Recipient, through its Ministry of Finance and Treasury, has issued a Ministerial Order which establishes a framework for managing externally financed public investments, including climate change impacts as one of the guiding principles.	Yes/Positive	No
Pillar 2: Creating the Enabling Environment for Private Sector Development		
Prior Action #4. To reduce electricity tariffs and diversify the energy mix, the Recipient has submitted to Parliament the Electricity (Amendment) Bill which amends: (i) the mechanism for setting the rates and scales of electricity tariffs, and (ii) the definition of installation to allow for the inclusion of renewable energy generation equipment.	Yes/Positive	No
Prior action #5. To increase access to credit, the Recipient has submitted to Parliament the Central Bank of Solomon Islands (Amendment) Bill 2023 ("CBSI Bill"), which permits the use of credit information for the purpose of improving the quality of bank credit and non-bank credits (CBSI Bill Clause 16).	No	Yes/Positive
Prior Action #6. To promote private investment, the Recipient, through its Cabinet, has approved the Solomon Islands Investment Policy and Promotion Strategy, which sets out a framework for streamlining the process of doing business,	No	No

protecting investors, simplifying investment admission and establishment, and establishing a new Investment Promotion Authority.		
Pillar 3: Improving Resilience to Climate Change, Natural Disasters and Health Emergencies		
Prior Action #7. To enhance climate resilience, the Recipient, through its Cabinet, has approved the National Climate Change Policy (2023-2032) which *inter alia* sets directives to address climate change through adaptation and risk reduction measures.	Yes/Positive	Yes/Positive
Prior Action #8. To improve climate and disaster resilience of infrastructure, the Recipient, through its Cabinet, has approved for submission to Parliament: (i) the National Building Standards Bill 2023; and (ii) the National Building Code, which improve the national building standards and ensure construction methods comply with climate change and disaster resilience measures.	No	Yes/Positive

ANNEX 5: PARIS ALIGNMENT ASSESSMENT

Program Development Objective(s): The proposed series of two operations supports the Solomon Islands Government in its efforts to improve fiscal management, private sector development, and climate and disaster resilience.	
Step 1: Taking into account our climate analysis (e.g., Country Climate and Development Reports or CCDRs), is the operation consistent with the country climate commitments, including for instance, the NDC, NAP, LTS, and other relevant strategies?	**Answer:** Yes. The reform program is consistent with the country's climate strategies, namely the 2021 Nationally Determined Contributions, and the National Climate Change Policy 2023 – 2027, as well as the resilient and environmentally sustainable development objectives under the NDS 2016 – 2035. On mitigation, the NDC commits to actions to increasing affordability and accessibility to electricity, developing renewable energy projects, and promoting private sector investment and participation. On adaptation, the NDC focuses on developing capacity to assess risks and vulnerabilities associated with climate variability and to improve the ability to adapt to impacts of climate change, such as through the development of National Adaptation Plan, national information system, and undertaking integrated vulnerability assessment. The proposed program directly supports the mitigation actions related to increasing affordability and accessibility to electricity, including developing renewable energy projects (PA4) and promoting private sector investment and participation (PA6). The proposed program also directly supports efforts to build climate and disaster resilience by strengthening public investment management (PA3), enhancing the framework for climate adaptation and mitigation (PA7), and improving the resilience of buildings (PA8).
Mitigation goals: assessing and reducing risks	
Pillar 1: Improving Fiscal Management	
Prior Action 1: To improve revenue collection, the Recipient has submitted to Parliament the Value Added Tax (VAT) Bill, which taxes goods and services at a standard rate of 15 percent and zero-rates all exports. **Prior Action 2**: To increase revenue collection in the mining sector, the Recipient, through its Minister of Mines, Energy and Rural Electrification, has made the Mine and Minerals (Nickel) (Royalty) Regulations 2023 to determine the nickel royalty based on the contained metal in the ore.	
Step M2.1: Is the prior action likely to cause a significant increase in GHG emissions?	**Answer**: No. **Explanation (PA1)**: The VAT Bill is expected to increase the efficiency of the tax system and contribute to increased revenue collections but would not in itself lead to a significant increase in GHG emissions. **Explanation (PA2)**: The introduction of a nickel royalty on a contained metals basis is expected to improve the fiscal regime of the mining sector, but it will not likely result in significant increase in mining activity and GHG emissions.
Step M2.2: Is the prior action likely to introduce or reinforce significant and persistent barriers to transition to the country's low-GHG emissions development pathways?	**Answer**: No.

Step M3: Is the risk of the prior action introducing or reinforcing significant and persistent barriers being reduced to low after mitigation measures have been implemented?	**Answer**: N/A
Prior Action 3: To strengthen public investment management, the Recipient, through its Ministry of Finance and Treasury, has issued a Ministerial Order which establishes a framework for managing externally financed public investments, including climate change impacts as one of the guiding principles.	
Step M2.1: Is the prior action likely to cause a significant increase in GHG emissions?	**Answer:** Yes. **Explanation**: Externally financed public investments (which comprise more than 90 percent of all public investment) supported by PA3 may be associated with an increase in GHG emissions (roads, construction etc.).
Step M2.2: Is the prior action likely to introduce or reinforce significant and persistent barriers to transition to the country's low-GHG emissions development pathways?	**Explanation:** PA3 is not likely to introduce or reinforce significant and persistent barriers to transition to the country's low-GHG emissions development pathways. First, PA3 supports the introduction of a climate-resilient framework for all externally financed public investments. Climate resilience is highlighted as a key objective in the PIM Framework, while the ensuing PIM chapter, PIM guidelines (IT3) and PIM policy will include a climate lens and sustainability considerations. Second, PA3 would not specifically favor or create more favorable conditions for fossil-fuel or carbon-intensive investments, and it is not likely to cause a significant increase in GHG emissions.
Step M3: Is the risk of the prior action introducing or reinforcing significant and persistent barriers being reduced to low after mitigation measures have been implemented?	**Answer**: N/A
Conclusion for PA 1, PA 2, and PA 3: ALIGNED with the goals of the Paris Agreement.	
Pillar 2: Creating the Enabling Environment for Private Sector Development	
Prior Action 4: To reduce electricity tariffs and diversify the energy mix, the Recipient has submitted to Parliament the Electricity (Amendment) Bill which amends: (i) the mechanism for setting the rates and scales of electricity tariffs, and (ii) the definition of installation to allow for the inclusion of renewable energy generation equipment.	
Step M2.1: Is the prior action likely to cause a significant increase in GHG emissions?	**Answer:** Yes. **Explanation**: PA4 directly supports the country's NDC goal to increase the affordability and accessibility to electricity, including through the diversification of the energy mix to increase the share of renewables. Revisions to the electricity tariff setting mechanism supported by PA4 will lead to more affordable energy prices and potentially an increase in energy use (mostly generated from diesel fuel).
Step M2.2: Is the prior action likely to introduce	Answer: No.

or reinforce significant and persistent barriers to transition to the country's low-GHG emissions development pathways?	**Explanation:** PA4 directly supports reducing reliance on imported diesel fuels and the diversification of the energy mix to increase the share of renewables. As a result, PA4 would not in itself introduce or reinforce significant and persistent barriers but rather it would support the country's transition to low-GHG emissions development pathways.
Step M3: Is the risk of the prior action introducing or reinforcing significant and persistent barriers being reduced to low after mitigation measures have been implemented?	**Answer:** N/A
Prior Action 5: To increase access to credit, the Recipient has submitted to Parliament the Central Bank of Solomon Islands (Amendment) Bill 2023 ("CBSI Bill"), which permits the use of credit information for the purpose of improving the quality of bank credit and non-bank credits (CBSI Bill Clause 16). **Prior Action 6:** To promote private investment, the Recipient, through its Cabinet, has approved the Solomon Islands Investment Policy and Promotion Strategy, which sets out a framework for streamlining the process of doing business, protecting investors, simplifying investment admission and establishment, and establishing a new Investment Promotion Authority.	
Step M2.1: Is the prior action likely to cause a significant increase in GHG emissions?	**Answer**: No. **Explanation (PA5)**: PA5 seeks to improve access to credit and will not in itself contribute to a significant increase in GHG emissions. **Explanation (PA6)**: PA6 supports the country's NDC goal to increase private sector investment and participation to implement mitigation measures. PA6 seeks to promote private investment, including by explicitly removing restrictions and opening up investments in alternative and renewable energy. While PA6, aims to improve the business environment by liberalizing agricultural and other sector-specific policies and establishing a competition policy, it does not specifically favor or create more favorable conditions for fossil-fuel or carbon-intensive investments. As a result, PA6 is not likely to cause a significant increase in GHG emissions.
Step M2.2: Is the prior action likely to introduce or reinforce significant and persistent barriers to transition to the country's low-GHG emissions development pathways?	**Answer**: No.
Step M3: Is the risk of the prior action introducing or reinforcing	**Answer**: N/A

significant and persistent barriers being reduced to low after mitigation measures have been implemented?	
Conclusion for PA 4, PA 5, and PA 6: ALIGNED with the goals of the Paris Agreement.	
Pillar 3: Improving Resilience to Climate Change, Natural Disasters and Health Emergencies	
Prior Action 7: To enhance climate resilience, the Recipient, through its Cabinet, has approved the National Climate Change Policy (2023-2032) which *inter alia* sets directives to address climate change through adaptation and risk reduction measures.	
Step M2.1: Is the prior action likely to cause a significant increase in GHG emissions?	**Answer**: No. **Explanation (PA7)**: The National Climate Change Policy directly supports climate change mitigation goals, such as the ambition to aim to achieve a 50 percent reduction in emissions by 2050 through appropriate international assistance as set out in the 2022 NDCs.
Step M2.2: Is the prior action likely to introduce or reinforce significant and persistent barriers to transition to the country's low-GHG emissions development pathways?	**Answer**: No.
Step M3: Is the risk of the prior action introducing or reinforcing significant and persistent barriers being reduced to low after mitigation measures have been implemented?	**Answer**: N/A
Prior Action 8: To improve climate and disaster resilience of infrastructure, the Recipient, through its Cabinet, has approved for submission to Parliament: (i) the National Building Standards Bill 2023; and (ii) the National Building Code, which improve the national building standards and ensure construction methods comply with climate change and disaster resilience measures.	
Step M2.1: Is the prior action likely to cause a significant increase in GHG emissions?	**Answer:** Yes. **Explanation (PA8)**: The New Building Code does not include any energy performance standards and could cause an increase in GHG emissions through buildings' carbon footprint (both embodied carbon footprint and operational carbon footprint from their energy consumption).
Step M2.2: Is the prior action likely to introduce or reinforce significant and persistent barriers to	**Answer:** Yes.

transition to the country's low-GHG emissions development pathways?	
Step M3: Is the risk of the prior action introducing or reinforcing significant and persistent barriers being reduced to low after mitigation measures have been implemented?	**Answer: Yes.** **Explanation (PA8).** The new Building Code is not expected to contribute to a significant increase in construction of new buildings (embodied carbon footprint), while the operational carbon footprint will be mitigated by measures such as PA4 and PA6 to increase the share of renewables in the energy mix. Further, the Building Code will be continuously updated to incorporate new measures. The team will continue dialogue with the government on this during the implementation of the Code.
Conclusion for PA 7 and PA 8: ALIGNED with the goals of the Paris Agreement.	
Mitigation goals: From a mitigation perspective, prior actions PA1, PA2, PA5, PA6, and PA7 are not expected to lead to a significant increase in GHG emissions nor are they expected to introduce persistent barriers to Solomon Islands' transition to low-GHG emissions development pathways. PA3, PA4 and PA8 were further assessed from a mitigation perspective to ensure that potential risks are mitigated by the country's institutional mechanisms with the conclusions that they are not expected to reinforce significant and persistent barriers to transition to the country's low-GHG emissions development pathways.	
Adaptation and resilience goals: assessing and managing the risks	
Pillar 1: Improving Fiscal Management	
Prior Action 1: To improve revenue collection, the Recipient has submitted to Parliament the Value Added Tax (VAT) Bill, which taxes goods and services at a standard rate of 15 percent and zero-rates all exports. **Prior Action 2**: To increase revenue collection in the mining sector, the Recipient, through its Minister of Mines, Energy and Rural Electrification, has made the Mine and Minerals (Nickel) (Royalty) Regulations 2023 to determine the nickel royalty based on the contained metal in the ore. **Prior Action 3:** To strengthen public investment management, the Recipient, through its Ministry of Finance and Treasury, has issued a Ministerial Order which establishes a framework for managing externally financed public investments, including climate change impacts as one of the guiding principles.	
Step A2: Are risks from climate hazards likely to have an adverse effect on the prior action's contribution to the Development Objective(s)?	**Answer**: No. **Explanation (PA1)**: Risks from climate-related natural disasters could have an adverse impact on economic activity thus on VAT revenue collection. However, PA1 seeks to increase the efficiency of the tax system and boost diversification of public revenues to also help cope with the impacts of climate risks. Access to CAT- DDO funding will further help tackle the risks. **Explanation (PA2)**: Risks from climate-related natural disasters could have an adverse impact on nickel mining activity and consequently on revenue collection from the mining sector. However, PA2 seeks to increase and boost diversification of public revenues to also help cope with the impacts of climate risks. Access to CAT- DDO funding will further help tackle the risks.

	Explanation (PA3): Risks from climate-related natural disasters could have an adverse impact on externally financed public investments supported by PA3. However, PA3 establishes a climate-resilient framework and a focus on climate resilience in the public investment management guidelines, which further combined with other policies such as PA8, the National Building Code are expected to mitigate these risks.
Step A3: Does the design of the prior action reduce the risk from climate hazards to an acceptable level, considering climate adaptation good practices applicable to the country context?	**Answer**: N/A
Conclusion for PA 1, PA 2, PA 3: ALIGNED with the goals of the Paris Agreement.	
Pillar 2: Creating the Enabling Environment for Private Sector Development	
Prior Action 4: To reduce electricity tariffs and diversify the energy mix, the Recipient has submitted to Parliament the Electricity (Amendment) Bill which amends: (i) the mechanism for setting the rates and scales of electricity tariffs, and (ii) the definition of installation to allow for the inclusion of renewable energy generation equipment. **Prior Action 5**: To increase access to credit, the Recipient has submitted to Parliament the Central Bank of Solomon Islands (Amendment) Bill 2023 ("CBSI Bill"), which permits the use of credit information for the purpose of improving the quality of bank credit and non-bank credits (CBSI Bill Clause 16). **Prior Action 6:** To promote private investment, the Recipient, through its Cabinet, has approved the Solomon Islands Investment Policy and Promotion Strategy, which sets out a framework for streamlining the process of doing business, protecting investors, simplifying investment admission and establishment, and establishing a new Investment Promotion Authority.	
Step A2: Are risks from climate hazards likely to have an adverse effect on the prior action's contribution to the Development Objective(s)?	**Answer**: No. **Explanation (PA4)**: Risks from climate hazards could impact electricity tariffs, however reforms to support the expansion of renewables in the energy mix and opening the market for generation and distribution of electricity aim to mitigate these risks. Further, reforms under PA6 to liberalize investment in alternative energy and renewables would further reduce the risks of adverse climate hazards. **Explanation (PA5)**: Risks from climate hazards, if materialized, may adversely affect private sector balance sheets and access to credit by affected households and businesses. However, risks from climate hazards will not have a material impact on the introduction of comprehensive credit reporting. This reporting would also help financial institutions make more efficient and accurate credit decision, thus, reducing risks and enhancing regulatory oversight. **Explanation (PA6)**: Risks from climate hazards can adversely affect private investment. However, PA6 seeks to promote private investment by establishing an investment Promotion Authority and enabling a more competitive investment climate that is favorable for attracting and expanding private investment. Risks from climate hazards do

	not have an adverse effect on the establishment of an investment Promotion Authority to support private sector growth.
Step A3: Does the design of the prior action reduce the risk from climate hazards to an acceptable level, considering climate adaptation good practices applicable to the country context?	**Answer**: N/A
Conclusion for PA 4, PA 5, PA 6: ALIGNED with the goals of the Paris Agreement.	
Pillar 3: Improving Resilience to Climate Change, Natural Disasters and Health Emergencies	
Prior Action 7: To enhance climate resilience, the Recipient, through its Cabinet, has approved the National Climate Change Policy (2023-2032) which *inter alia* sets directives to address climate change through adaptation and risk reduction measures. **Prior Action 8:** To improve climate and disaster resilience of infrastructure, the Recipient, through its Cabinet, has approved for submission to Parliament: (i) the National Building Standards Bill 2023; and (ii) the National Building Code, which improve the national building standards and ensure construction methods comply with climate change and disaster resilience measures.	
Step A2: Are risks from climate hazards likely to have an adverse effect on the prior action's contribution to the Development Objective(s)?	**Answer**: No. **Explanation (PA7)**: Risks from climate hazards are not likely to have an adverse effect on the approval of the National Climate Change Policy to enhance climate resilience. In addition, this prior action directly supports to strengthen the country's capacity to build climate and disaster resilience, which directly supports the NDC goal on adaptation." **Explanation (PA8)**: PA8 supports incorporating measures for disaster risks reduction and climate change adaptation. It seeks to improve resilience of all new buildings to natural hazards. The NBC applies acceptable performance standards for structural sufficiency, fire safety, health, and amenity, as well as measures for disaster risk reduction and climate change adaptation, including measures to address wind and seismic parameter resilience.
Step A3: Does the design of the prior action reduce the risk from climate hazards to an acceptable level, considering climate adaptation good practices applicable to the country context?	**Answer**: N/A
Conclusion for PA 7 and PA 8: ALIGNED with the goals of the Paris Agreement.	
Adaptation and resilience goals: Risks from climate hazards are not likely to have an adverse effect on any of the prior actions and their contribution to the Development Objective. In addition, PA3, PA7 and PA8 directly support building capacity and resilience to the impacts of climate change.	
OVERALL CONCLUSION OF PARIS ALIGNMENT ASSESSMENT: This operation is aligned with the goals of the Paris Climate Agreement as all prior actions are aligned with the mitigation and adaptation and resilience goals.	

ANNEX 6: DPO PRIOR ACTIONS AND ANALYTICAL UNDERPINNINGS

Prior Actions	Analytical Underpinnings
Pillar 1: Improving Fiscal Management	
Prior Action #1. To improve revenue collection, the Recipient has submitted to Parliament the Value Added Tax (VAT) Bill, which taxes goods and services at a standard rate of 15 percent and zero-rates all exports.	World Bank Public Expenditure Review (2022): in-depth analysis of the revenue and distributional implications of introducing VAT
Prior Action #2. To increase revenue collection in the mining sector, the Recipient, through its Minister of Mines, Energy and Rural Electrification, has made the Mine and Minerals (Nickel) (Royalty) Regulations 2023 to determine the nickel royalty based on the contained metal in the ore.	Mineral Revenue Policy Settings - IMF Technical Report (2023)
Prior Action #3. To strengthen public investment management, the Recipient, through its Ministry of Finance and Treasury, has issued a Ministerial Order which establishes a framework for managing externally financed public investments, including climate change impacts as one of the guiding principles.	World Bank Public Expenditure Review (2022): in-depth analysis of the infrastructure pipeline and PIM framework.
Pillar 2: Creating the Enabling Environment for Private Sector Development	
Prior Action #4. To reduce electricity tariffs and diversify the energy mix, the Recipient has submitted to Parliament the Electricity (Amendment) Bill which amends: (i) the mechanism for setting the rates and scales of electricity tariffs, and (ii) the definition of installation to allow for the inclusion of renewable energy generation equipment.	Castalia (2022) Solomon Islands Electricity Act Review; ABD (2023) Finding Balance: benchmarking performance and building climate resilience in Pacific State-Owned Enterprises; ADB (2020) Power Sector Assessment. Castalia (2022) recommended the establishment of an independent electricity regulator to protect interests of consumers, set electricity tariffs, issue licenses and regulate the performance of the SIEA.
Prior Action #5. To increase access to credit, the Recipient has submitted to Parliament the Central Bank of Solomon Islands (Amendment) Bill 2023 ("CBSI Bill"), which permits the use of credit information for the purpose of improving the quality of bank credit and non-bank credits (CBSI Bill Clause 16).	IFC Technical Assistance to CBSI: (i) support the introduction of revised/new legislation/regulations: local legislative review and a policy regulatory paper on the credit reporting system; (ii) support purchase of new software and IT systems; and (iii) support to design a database: analysis complete of key lenders data availability. IFC Policy Paper "Regulation of Credit Reporting in Solomon Islands" recommended that CBSI amend the existing regulations to reflect international best practices, in particular advancements under the General Principles for Credit Reporting; better regulate credit reporting and move from negative to comprehensive credit reporting;

	and support the key role and functions of CBSI as supervisor and licensor.
Prior Action #6. To promote private investment, the Recipient, through its Cabinet, has approved the Solomon Islands Investment Policy and Promotion Strategy, which sets out a framework for streamlining the process of doing business, protecting investors, simplifying investment admission and establishment, and establishing a new Investment Promotion Authority.	Adopted to closely follow G20 Investment Principles ADB Policy Paper “Continuing Reforms to Stimulate Private Sector Investment – a Private Sector Assessment for Solomon Islands” highlights the need for a cost-effective strategy to promote the country as investment destination, facilitate investment, and advocate for policy reform. World Bank to provide technical assistance for the amendment of the Foreign Investment Act.
Pillar 3: Improving Resilience to Climate Change, Natural Disasters and Health Emergencies	
Prior Action #7. To enhance climate resilience, the Recipient, through its Cabinet, has approved the National Climate Change Policy (2023-2032) which *inter alia* sets directives to address climate change through adaptation and risk reduction measures.	Climate Change Policy 2012-2017 – sets out national strategic actions for climate adaptation and mitigation and sets the national climate projections The National Disaster Management Plan of 2018- establishes disaster preparedness and response mechanisms and action plans. Solomon Islands 2023 appropriated budget policy statement- prioritizes resilience building, weatherproofing of infrastructure and appropriate a contingency fund for unforeseen events including natural disasters.
Prior Action #8. To improve climate and disaster resilience of infrastructure, the Recipient, through its Cabinet, has approved for submission to Parliament: (i) the National Building Standards Bill 2023; and (ii) the National Building Code, which improve the national building standards and ensure construction methods comply with climate change and disaster resilience measures.	National Building Code Review 2016- makes recommendation for improving building standards and practices. PRIF (2021) Regional Diagnostic Study on the Application Of Building Codes in the Pacific – Solomon Islands Case Study- recommends the use of resilient building standards Solomon Islands 2023 appropriate budget policy statement- prioritize the passage of the National Building Code Bill in 2023 calendar year.