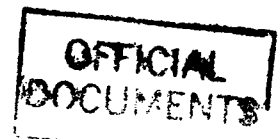


**MINISTER OF FINANCE  
AND TREASURY**



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

**SOLOMON ISLANDS GOVERNMENT**

Ref: 459/10/

Date: 26<sup>th</sup> September, 2014

Mr. Jim Kim  
President  
The World Bank  
Washington DC, 20433  
USA

Dear President Kim

**RE Letter of Development Policy**

As you are aware, Solomon Islands experienced major flooding during April 2014, imposing tragic loss of human life, extensive damage, and disruption to economic production. The total economic value of the flooding's impact is estimated at S\$787.3 million (US\$107.8 million). This is equivalent to 9.2 percent of Solomon Islands' Gross Domestic Product (GDP), which gives an indication of the scale of the flooding. The flooding severely disrupted commercial and retail activity as well as cash crop production, and led to the discontinuation of production at the Gold Ridge Mine. Growth is now forecast to be around zero percent for 2014 (from an initial forecast of 4.0 percent). Revenue is projected to decline by around SBD150 million, while government faces costs of reconstruction activities under a new reconstruction strategy of more than SBD170 million. From an initial balanced budget, Government is now forecasting a deficit of 1.6 percent of GDP for 2014.

The impacts of the flood have been far-reaching. Disruptions to local food production have introduced new inflationary pressures, which our Central Bank is monitoring closely with the possibility of further contractionary monetary policy measures. With the cessation of gold production, our foreign reserves, while still at comfortable levels, are likely to decline in future years.

The recent flooding comes in the context of longer-term challenges. The Solomon Islands economy has long been reliant on logging, which now accounts for around 16 percent of output and 15 percent of government revenues. With natural forest stocks nearing exhaustion, and the Gold Ridge Mine no longer operating, it is vital that we continue to pursue our established program of financial and economic management reforms in order to realize new sources of growth and ensure prudent macroeconomic management during this difficult time.

Mr. President, I wish to assure you that recent events have in no way distracted Government from its commitment to reform. It is clear to all that the Government's capacity to respond effectively to recent flooding was predicated on the availability of substantial fiscal and foreign exchange buffers, built up during several years of strong growth and prudent macroeconomic management. Budget support and other assistance being provided by development partners will also play an important role. We continue to work with development partners in implementing shared priority

reforms listed in the Economic and Financial Reform Program, overseen by the Core Economic Working Group (CEWG) which the World Bank is also an active member. The CEWG have a shared understanding that such reforms can contribute to our ability to both improve the living standards of Solomon Islanders and increase our resilience to any future shocks.

Our ongoing reform program for 2014 is organized under three themes: i) improved management of public expenditure and debt; ii) improved management of extractive industries; and iii) improved conditions for private sector growth.

Under 'improved management of public expenditure and debt' government has recently achieved several major reforms. A new Public Financial Management Act was passed in late 2013, overhauling the legislative framework for public financial management in Solomon Islands. In 2104, a PFM Reform Roadmap was approved, outlining a detailed and prioritized reform program for further improving PFM systems and processes, and fully implementing the provisions of the Public Financial Management Act. Consultative processes for budget formation have been improved, with provincial level consultations in 2013 being used to inform 2014 budget proposals. A mid-year budget report was prepared and published on the Ministry of Finance and Treasury's website for the first time in July 2014, significantly enhancing budget transparency.

In December 2013 the Government adopted on-lending and guarantee policies as part of the Debt Management Framework. These policies place control around the provision of on-lent loans and government guarantees to ensure that Solomon Islands' debt levels remain sustainable and affordable over the long-term. Finally, the Ministry of Education and Human Resource Development has implemented revised procedures for the approval of tertiary scholarships and the National Education Board has approved a new scholarships policy, establishing a clear and transparent policy governing the award of all government-funded scholarships. This reform will promote improved allocative efficiency in education spending while contributing to overall budget discipline.

Under 'strengthened management of extractive industries', the Multi Stakeholder Group (MSG), coordinated through the Recipient's Ministry of Finance and Treasury, has submitted Solomon Islands' first EITI Report, completing a long process towards full implementation of this international mechanism for financial transparency in the mining sector. Also under this theme, Parliament has approved legislation for a transparent and predictable mining tax regime. The introduction of this regime is necessary both to bring mining investment to Solomon Islands, but also to ensure that the benefits of this investment are widely and equitably shared.

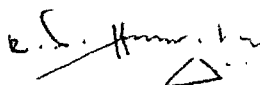
Under 'improving conditions for private sector investment', several important reforms have taken place. Government passed revised Business Names legislation in 2014. The new legislation allows sole traders, partnerships, and companies to operate a business under a registered business name. This has a range of benefits including encouraging businesses to enter the formal economy, fraud detection, protection of a business' goodwill, and tax compliance. A draft Customs and Excise Bill to update an outdated and inefficient Customs and Excise Act is now in its final version and will shortly proceed to vetting. The Solomon Islands National Infrastructure Investment Plan 2013-2023 has now been endorsed by Cabinet and launched. The Plan presents the priorities of SIG and the strategic direction for major initiatives in economic infrastructure over the next five to ten years. This is the first attempt to compile in one document the development needs for the various sub-sectors of economic infrastructure, including energy, land, sea and air transport, water and sanitation, telecommunications, and solid waste management. The Plan presents a prioritized list of infrastructure investment projects and identifies a funding strategy underpinning the priority investments. The Ministry of Development

Planning and Aid Coordination will be the agency responsible for taking the Plan forward and will oversee implementation of the plan. Finally, Parliament has approved amendments to the Land and Titles Act transferring power to allocate perpetual and fixed term estates from the Lands Commissioner to a new Lands Board. We are confident that this measure will bring important benefits in reducing transaction costs and increasing transparency of land transactions, enabling accelerated private sector development.

Government remains committed to the Core Economic Working Group process and the implementation of reforms included in the Economic and Financial Reform Program. We appreciate donor support through this process, especially in response to recent flooding.

We look forwards to working together with our development partners, including the World Bank, in recovering fully from the recent disaster and moving ahead with further growth-enhancing reforms.

Yours sincerely

A handwritten signature in black ink, appearing to read "R. S. Houenipwela", with a small triangle drawn below the end of the signature.

Hon. Rick Houenipwela  
Minister of Finance and Treasury