SOLOMON ISLANDS

Table 1	2020
Population, million	0.7
GDP, current US$ billion	1.5
GDP per capita, current US$	2317
National basic needs poverty rate (%)[a]	12.7
School enrollment, primary (% gross)[b]	112.6
Life expectancy at birth, years[a]	72.6

Source: WDI, Macro Poverty Outlook, and official data.
Notes:
(a)Solomon Islands National Statistics Office. Most recent value (2013).
(b) Most recent WDI value (2017).

A timid, but uncertain, economic rebound is expected in 2021. The economic stimulus package, infrastructure projects and strengthened external demand should contribute to economic growth. A full, post-pandemic recovery is only expected in the medium term. Several downside risks threaten the growth outlook, including reduced logging output, prolonged travel restrictions and investment delays. A strong policy response from the Government is needed to sustain livelihoods, support economic growth and maintain macroeconomic and fiscal sustainability.

Key conditions and challenges

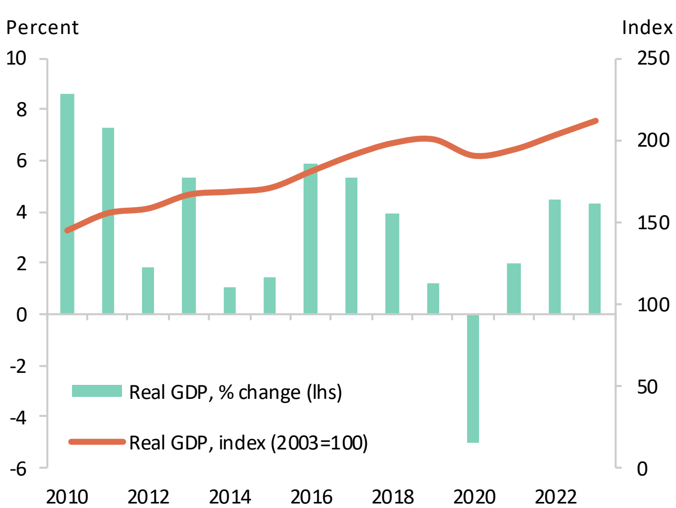
Solomon Islands is a small, remote archipelago that faces a unique set of development challenges, characterized by economic geography and state fragility. A population dispersed across a vast territory complicates access to basic public services. Relatedly, the smallness and dispersion make public service delivery and the provision of infrastructure disproportionally costly. A small domestic economy, internal division and remoteness from large export markets limit private sector development and international trade. Furthermore, natural disasters and the impacts from climate change pose a continuous threat to sustainable development. Limited state capacity and political economy dynamics tend to constrain the design and implementation of effective public policies. Finally, the country's dependence on the logging industry points to the need for economic diversification. The Solomon Islands' unique geographic and institutional features, however, limit the possibilities to diversify its economy.

The more immediate risk factors and challenges relate to COVID-19 and the need to support economic recovery. Further enhancing health sector preparedness and preventing community transmission of COVID-19 are of crucial importance. While a domestic outbreak would have substantial implications, the border restrictions in place continue to constrain economic activity and affect livelihoods. Relaxing the current prevention measures will depend on the vaccination roll-out, which generally has been slower than anticipated. Based on current projections for vaccine roll-out and the resumption of international travel, economic activity is likely to be hampered for most of 2021. Given these conditions, a concerted effort by multiple stakeholders is required to support economic recovery and poverty reduction. Effective policy measures, strong social protection programs and labor-intensive public investment projects are important components to stimulate growth. At the same time there is a need to maintain macroeconomic and fiscal sustainability, guarantee sound public financial management while taking into account the country's fragile context. A rise in export commodity prices and strong external demand from main trading partners may support the country's economic recovery.

Recent developments

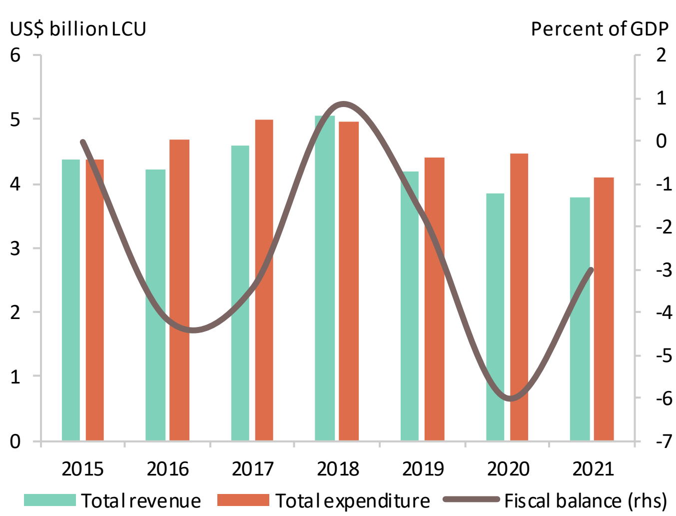
Due to the impacts of COVID-19, the economy is estimated to contract by 5 percent in 2020. Border disruptions, weak external demand and precautionary health measures led to a significant drop in primary sector production, including in fishing and logging. Furthermore, the lack of international visitor arrivals impacted the tourism sector. Visitor arrivals dropped from 8,891 in third quarter of 2019 to 96 in the third quarter of 2020.

FIGURE 1 Solomon Islands / Real GDP



Sources: World Bank staff estimates.

FIGURE 2 Solomon Islands / Fiscal indicators



Sources: World Bank staff estimates.

Large, donor-funded infrastructure projects were delayed due to travel restrictions, therefore dampening construction activity.

Leading indicators, however, suggest an economic rebound in the last quarter of 2020. The Central Bank's production index improved to 81 points in December 2020, up from 65 points in October 2020. Higher output in round logs and fishing are the main drivers of the increased economic activity. Furthermore, international prices for all export commodities trended higher in December, most notably palm oil (6 percent) and fish (5 percent), and to a lesser extent round logs (1 percent). Improved terms of trade for commodity exporters may generate positive consumption effects.

The current account deficit is expected to reach 4 percent of GDP in 2020. Declining imports – especially fuel, machineries and transport equipment – were more than offset by a fall in exports, especially in fish and minerals. The deficit on the current account is offset, however, by large foreign aid inflows. As a result, foreign reserves covered 13.3 months of imports at December 2020.

Revised fiscal estimates indicate a fiscal deficit of 6 percent of GDP in 2020, financed by budget support loans, a complete drawdown on the cash buffers and the issuance of a domestic bond. The government also built up significant domestic payment arrears – estimated 3 percent of GDP, with payments mostly due to SMEs. To provide fiscal stimulus to the economy, the Government launched an economic stimulus package (ESP) in May 2020, totaling about 2.7 percent of GDP. The roll-out of important ESP components was delayed, however, with certain recovery payments only being disbursed in the last quarter of 2020. Furthermore, at the end of 2020, the Government made public its Policy Redirection, a strategy to focus on economic recovery and to safeguard the population from the COVID-19 pandemic.

A June 2020 mobile phone survey indicates that the pandemic is taking a toll on livelihoods. Survey results showed net employment loss of between 7 and 11 percent from Jan 2020 to June 2020 which was more likely to impact women. Of those still working in June, just over half were earning the same as pre-crisis levels and one-third were working for less or not being paid at all. Also, 57 percent of respondents reduced food consumption and 27 percent had increased their household debt by delaying loan repayments or making purchases on credit. The findings thus suggest that near poor households may have been made more vulnerable to falling into poverty.

Outlook

The near-term outlook remains highly uncertain and depends on the evolution of the pandemic and policy effectiveness in supporting economic recovery. Assuming that travel restrictions begin to ease in late 2021, the economy is expected to grow this year with 2 percent. A further implementation of the economic stimulus package, the initiation of important infrastructure projects and strengthened external demand for export commodities should contribute to economic growth. Later years of the projection period may see a full post-pandemic recovery, partly driven by the economic effects of the 2023 Pacific Games. There are, however, several downside risks to the outlook. A local COVID-19 outbreak, social unrest, ineffective policy implementation, investment delays, financial sector stress, reduced logging output, prolonged travel restrictions or a severe natural disaster could all hurt economic growth.

The current account deficit is expected to remain elevated over the medium-term, as the recovery in primary exports is offset by higher imports for infrastructure projects once COVID-related restrictions are eased. The deficit will be financed through current and capital transfers, foreign direct investment and highly concessional project lending. As a result, foreign reserves are expected to cover more than 6 months of imports by 2023.

For 2021, an overall deficit of 3 percent of GDP is expected. Revenue is budgeted to remain flat. While inland revenues are projected to increase compared to 2020, customs and excise revenues are estimated to decline due to reduced log exports. Overall expenditure is expected to drop by 8.6 percent in 2021. The Solomon Islands Government is planning to contain recurrent expenditure – including a civil service hiring freeze, but increase capital spending in 2021. In the medium term, revenue is projected to recover, driven by economic growth and a series of tax reforms. To support economic recovery and finance the large infrastructure pipeline, expenditures are also expected to rise over the projection period. Therefore, it will be critical for the Solomon Islands Government to carefully manage its public finances.

TABLE 2 Solomon Islands / Macro poverty outlook indicators (annual percent change unless indicated otherwise)

	2018	2019	2020 e	2021 f	2022 f	2023 f
Real GDP growth, at constant market prices	3.9	1.2	-5.0	2.0	4.5	4.3
Inflation (Consumer Price Index end of period)	3.9	2.8	3.0	3.5	3.4	3.8
Balance of Payments						
Current account balance (% of GDP)	-3.0	-9.6	-4.0	-16.4	-13.3	-11.9
Fiscal Balance (% of GDP)	1.4	-1.2	-6.0	-3.0	-3.6	-3.7
External Debt (% of GDP)	8.2	10.0	13.5	15.5	17.6	19.9

Source: World Bank and International Monetary Fund staff estimates.
Notes: e = estimate, f = forecast.