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## INVESTMENT POLICY SHIFT OF THE SOLOMON ISLANDS NATIONAL PROVIDENT FUND BOARD, THE COUNTRY'S ONLY SUPERANNUATION SCHEME

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### ABSTRACT

*The Solomon Islands National Provident Fund (SINPF) is managed by its board of directors (BOD) and influenced by government policies. Despite vibrant growth in assets and its investment portfolios, SINPF has yet to fully realize its primary objectives to its members. Its primary objective has been to assist members still in employment with loans to acquire homes, and to provide a lump sum payment or pensions after employment. This study has investigated why the previous BODs have diverted the SINPF primary objective as social benefit to members to more economic benefits. The study has used mainly qualitative information to examine the operations of the fund and BOD over the past decades. We also interviewed current and former members and employees of the fund to get insight information of the fund. The study has found that the fund has progressively diverted its primary objectives, from direct benefit to members through personal loans and investment options to corporate-focus investment portfolios from which members can benefit, indirectly, only if the institution's main source of profit is its aggressive corporate investment policy. The study concluded that whilst the BOD is mandated to invest, on behalf of members, the funds received through members' contributions, they must not compromise the SINPF primary objective to ensure that members benefit directly from these investment initiatives. BODs are obliged to make proper and sound loan assessments when approving loans to these corporate borrowers.*

**Key words:** Investment policy, Members' contributions, Members' benefits, Superannuation.

### INTRODUCTION

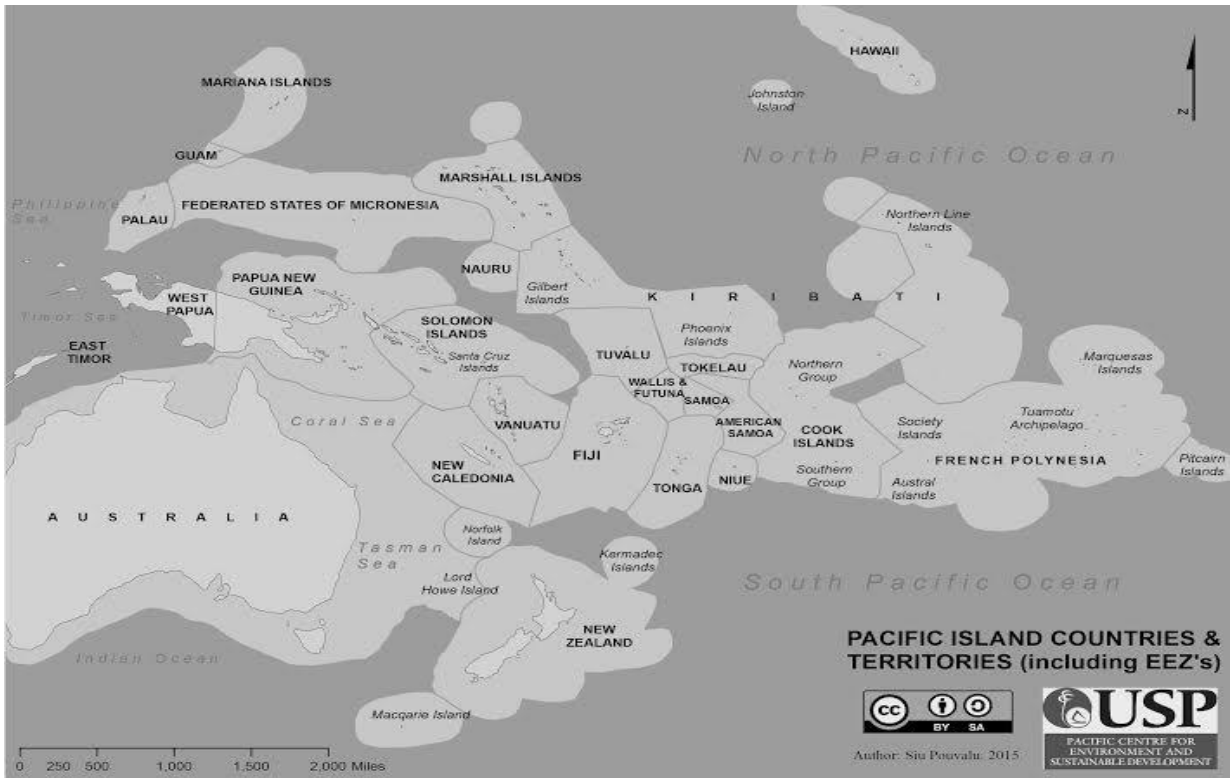
Solomon Islands is located in the Southwest Pacific about 1,900 km northeast of Australia with about 996 islands stretching a 1,450-

kilometer chain southeast from Papua New Guinea (Coleman & Kroenke, 1981). It has a population of around 537,000 inhabitants who share a total land area of approximately 27,500

km<sup>2</sup>. The majority (85 per cent) of the population lives in rural villages or communities (Gagahe, 2011) and derived their livelihoods directly from

their gardens, rivers and sea waters. In 2016 its nominal GDP was estimated by World Bank at ~USD 1.202 billion (Ozturk, et al., 2016).

Figure 1: Pacific Island countries and Territories



The country’s undeveloped mineral resources include lateritic bauxite, lead, nickel, and zinc (Asian Development Bank, 2017). Manufacturing primarily involves the processing of coconut and other vegetable oils and of cocoa on the Islands. Rural villagers also depends on handicrafts, including woodcarvings, shell inlay, mats, baskets, and shell jewelries as source of income. Some are sold in local outlets while others are

exported to overseas markets. The Solomon Islands dollar is the official currency which currently is weighted SBD\$7.60 against USD\$1(CSBSI, 2017). Tourism is still in its development stage and yet to be recognised as a major source of income (Kaczan, et al, 2008). The country’s main resources include, fish and timber, have been exploited excessively, which has resulted in their depletion. Its other export

products are derived from plantation crops: palm oil, copra and cacao (the source of cocoa). China and Australia are the major recipients (ADB, 2017). The chief imports are machinery, fuels, manufactured goods, and food, and Australia, Singapore, and China are the main suppliers. In terms of employment, only one-fifth of the country's population - an estimated 50,000 people out of a working population of 250,000 – are employed in formal economy. The other four-fifth of the population are engaged in subsistence agriculture and heavily depends on cash incomes. Further more, about 7,500 young people graduates from school to enter the workforce each year, yet only one in every six-school leaver will find paid employment (World Bank, 2016<sup>1</sup>).

## LITERATURE REVIEW

### SOLOMON ISLANDS NATIONAL PROVIDENT FUND

After its commencement in 1976, SINPF grew in membership and began to accumulate assets. Encouraged by this, the government decided to widen the Fund's membership to private sector employees as well as public servants. This implies that for all employees in the country, it is mandatory by law (SINPF Act 1976) to

contribute a fixed amount of their savings to the SINPF board for their safekeeping and administration until retirement.<sup>2</sup> Whether the employees like it or not, 5.5 per cent of their monthly or fortnightly salary or wage has to be kept by the board until the employee reaches retirement age, when the member shall be eligible to withdraw its contributions and savings from the board. The member can withdraw its contributions legally under these conditions:

- (a) the member has attained the age of fifty years; or
- (b) has died; or
- (c) is physically or mentally incapacitated from ever engaging in any further employment; or
- (d) [*is a non-citizen who*] is about to leave or has left Solomon Islands; or
- (e) has been unfairly dismissed or has been made redundant and has not, during the three (3) months period immediately preceding the date on which he applies to withdraw the amount standing to his credit in the Fund, been engaged in employment; or
- (f) has reached the age of forty (40) years and has satisfied the Board that he has retired from employment as an employee. ( Solomon Islands National Provident Fund, Cap 109).

Besides these clarifications, technically, one other ground lies where members can have access to their funds during the course of their employment. This is when members have

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<sup>1</sup> <http://www.worldbank.org/> cited 26 October, 2018

<sup>2</sup> Retirement age for public servants is 55 years.

pledged two-thirds of their contributions as collateral against borrowings they made from commercial banks. If repayments of their loans fall into arrears for more than 6 months,<sup>3</sup> the lender will lodge a claim against the borrower's SINPF two-thirds of pledged contributions. During such a situation, the lender claims the collateral (member's contributions) and pays off the member's outstanding loans plus interest with the commercial banks. Although this is a not proper way of having access to the funds, usually some members resort to this ground of withdrawal because of the difficulty in having access to these funds, loans and other investment options (their own funds) until they are qualified under any of the grounds explained above.

## FINANCIAL SYSTEM

Most Pacific Islands countries have inherited very open economies from their colonial masters (Chandra, 1995; Browne, 1989) and Solomon Islands is no exception; its open economy is an inheritance from its colonial master, Great Britain. Although the country has a thin financial system, its free market economy allows individuals or firms having the relevant skill sets with adequate resources to take advantage of opportunities to venture into and operate a whole range of business investment initiatives successfully (Lazonick, 1993). The financial

system includes four commercial banks, one central bank, one credit corporation, one superannuation fund (SINPF) and at least five insurance companies and brokers.

The country lacks a stock market although the government can still raise funds by issuing of treasury bills and bonds through the Central Bank of Solomon Islands and the SINPF through an amortization scheme. The government's current debt rate stands at 11 per cent of its GDP, which is rated as one of the strongest debt free positions within the Pacific Islands region (Debt Management Unit, 2015). The World Bank and International Monetary Fund (IMF) threshold requirement for borrowing is not more than 30 per cent of a country's GDP. After the span of years of ethnic tension in Solomon Islands, government's borrowings had reached more than 70 per cent of its GDP, one of the highest in the Pacific Islands region and in the world. During the period of financial crisis, the SINPF was also one of the main lenders to the government (Debt Management Unit, 2015).

## SOURCES OF FUNDING

The traditional sources of funds for any superannuation funds are mainly from the members' contributions (Drew & Stanford,

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<sup>3</sup> The lender could claim the customer's loan only after the loan could not be paid over 6 months.

2002). With SINPF, this sum continues to accumulate throughout the decades. This main source of funds (members' contributions) is regarded as somewhat of a liability to the board, obliging them to invest in investment projects, which must yield higher returns (Drew & Stanford, 2003). As the fund broadened its income base, it expanded to other incomes through interest earned from loans, dividends from shares and amortization schemes by government, as the SINPF board started to diversify the investment options available to them under the legislation.

### USES OF FUNDS

The board is mandated under the legislation (*Solomon Islands National Provident Fund Act*, Cap of 109) to invest the contributions of the members in a prudential manner that will benefit their shares in the fund. The original intention was that while members are still in employment the fund would have the capacity to *pool*<sup>4</sup> the members' contributions and lend out those contributions in the form of loans, to acquire personal homes (both urban and rural). In addition, members could also have access to other forms of home mortgages so that they could

benefit from them even while they are still actively employed. According to the recent financial reports, though, the fund uses the highest percentage of its funds in the form of loans to business houses (Annual Reports, 2010 and 2012).

### TRADITIONAL SERVICES PROVIDED BY THE SUPERANNUATION

To maximize the level of benefits the members would gain from their contributions, the BOD is obliged to invest and diversify the members' contributions in various investment schemes. In carrying out this function, the fund tries to transfer the level of risk across the investment options available (Thorp, 2005) a. By doing this the fund also fulfils its statutory objective to invest its members' contributions prudently and also assist members to acquire shelters and invest in micro-business activities that prepare them for their retirement lives in the rural villages in Solomon Islands. In pursuit of these objectives, the SINPF board used to provide the following services to its members: urban housing loan scheme, rural housing loan scheme, furniture housing scheme, housing refinancing loan scheme and NPF pledge scheme with the

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<sup>4</sup> That is, SINPF performs the function of an intermediary, collecting small deposits from members and lending out the contributions to the general members.

commercial banks. These investment options are seen as the traditional services provided by the fund to assist its members during its early years.

Röller and Waverman (2001) remind us that telecommunications and infrastructure development are stimulus to any economic development anywhere. In the Solomon Islands context, where government is expected to spend on such high-quality investment to boost economic growth, any effort to obtain funds for doing so looks worthwhile.

### **PROBLEM STATEMENT**

There is not much option available for working class people to invest their savings besides commercial bank to use when they retired from formal employment. The country also faces frequency of disasters from climate change induced extreme events such as sea level rise, coastal flooding, cyclone, salt water inundation and heavy rains. Thus, there need to be better management of the SINPF to ensure members benefit socially and financially at their retirement.

### **SIGNIFICANCE OF THE STUDY**

The Solomon Islands National Provident Fund (SINPF) was established by pre-independence Legislative Council legislation. The country gained independence from the Great Britain in 1978 (Steves 1996).<sup>5</sup> The late Honorable Mr. Anthony Saru introduced it as a private bill in the Legislative Council in 1970, the SINPF Act was passed in 1973 and the SINPF commenced operation three years later in 1976. The original intention with the creation of this superannuation fund was for all public servants to contribute a portion (12.5 per cent) of their wage or salary to the fund. Their contributions would accumulate, thus they could adequate savings to maintain them after many years serving as public servants (Dixon, 1993; *Solomon Islands National Provident Fund Act* Cap.109). This arrangement would relieve the government of any commitment to paying pensions to its retired public servants during their retirement years. By freeing itself from an obligation to expend its limited resources on social welfare related expenses for its retirees, the government would instead be able to allocate those funds to invest in infrastructures and schools, which could generate income and grow the economy. Thus, the study

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<sup>5</sup> The country gained independence on 7 July 1978.

ensures that it provides policy makers, board of directors and management to recommend and better strategies to ensure that members are real beneficiaries of their contributions.

## RESEARCH POSITIONS AND OBJECTIVES

The study perceives that because of the stringent measures enforced and the difficulty of the members' having access to the superannuation funds, members' SINPF contributions accumulate over the years. In pursuit of higher returns on these accumulating contributions, the recent SINPF BOD has diverted their lending policies to corporate borrowers, thus compromising the original objective of the SINPF at the time of its establishment. The main purpose of this study therefore is to ;

(i) Determine why this shift in the SINPF board investment policy over the years. After determining the shift, then study aims to identify key driving factors that influence the BOD to take such a bold stand in their decision-making to deny members from benefiting from their contributions by acquiring home loans and other household borrowings from the board (Fund).

(ii) Determine why the BOD focuses more on corporate lending as opposed to extending individual personal housing loans to members.

(iii) Recommends some strategies for ensuring the members benefit from the future investment policy of the SINPF.

## MATERIALS AND METHOD

The SINPF has three offices in the country, the main one in the capital city Honiara, and two other branches in Auki, Malaita province and Gizo in the Western province. The majority of employees in the country use the Honiara City SINPF branch services since its location is central for most of the other provincial capital centers. The study was conducted on members<sup>6</sup> from all these three branch sites, to gain a fair idea of the perceptions of members from across the country. This is asking them about the benefits that members derive from their contributions to the SINPF and how they think that SINPF has diverted its investment policy from its original objective of social security to a more corporate benefit objective.

The study was undertaken mainly from analysis of subjective information obtained from SINPF

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<sup>6</sup> SINPF Members and employees from these three provinces (Malaita, Western and Guadalcanal provinces).

members, careful review of annual reports, examination of the Solomon Islands National Provident Fund Act, Cap 109 and interviews with some current and former employees of the organization. We also conducted interviews with groups and individual members representing members of the SINPF, as well as in-depth research on the general operation and management of the organization. The research team has undertaken an appreciative enquiry with members on how they perceive the level of benefits they receive from the SINPF services. Tools the research team used to obtain information included semi-structured questionnaires, personal interviews and an intensive review of documents and annual reports.

More than 60 members completed the semi-structured questionnaires to provide the responses required for completing this manuscript. This questionnaire probed for information to capture the following areas:

(i) *The urban housing loan scheme.*<sup>7</sup> Under this section we hoped to capture the current SINPF members' thinking about the discontinuation of the urban housing loan

scheme to SINPF members. The importance of this question lies in its intention to ascertain the general members' perceptions of the current board's discontinuation of that lending policy, the lending function that specifically allowed members to obtain loans from the SINPF to acquire and own homes in the urban centres.

(ii) *The Furniture loan scheme.* The research team asked members whether the cessation of the furniture loan scheme was of any benefit and interest to members. We anticipated that members would want this scheme to continue because generally, prices of furniture in the capital or provincial headquarters are high.

(iii) *Home refinance loan scheme.* This loan scheme permitted members to refinance their home loans from any commercial banks to SINPF. The scheme is not currently operating and members who are able to obtain loans from the commercial banks have to struggle to repay their loans with the higher interest rates compared to those of SINPF. During its early years of operation SINPF also provided refinance loans, thus helping members to repay their loans at reduced interest rates. Our expectation was that members would support the re-introduction of

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<sup>7</sup> SINPF charges loan interest rates of 4 to 5 per cent while commercial bank rates are 12 to 19.5 per cent.



the home refinance scheme to enable members to refinance their loans with commercial banks.

(iv) *Rural housing scheme.* Under this rural housing scheme members were allowed to apply for loan facilities to assist them to build homes in the rural areas. Usually members pledged two-thirds of their SINPF contributions and were granted loans to build their homes in the villages. We anticipate that members would support re-introduction of this scheme as more people are returning to the villages after retirement from employment in towns.

*General perceptions about the investment shift of the SINPF.* We asked this question to gauge the level of members' satisfaction with the management and general operation of the SINPF. We anticipated receiving mixed responses from members as we suspected some would support direct and indirect benefits from the SINPF investments. According to Cooper, J. (2014) the primary objective superannuation is to benefit members after retirement.

(v) *Reason for Investment shift.* We asked this question to gauge what members perceive as some of the reasons for the shift in the SINPF investment policy. We anticipated that political influence and cronies' interests may surface as possible reasons members perceived as driving

the shift from individual to corporate objectives of investment.

At this point, we paused after obtaining the responses to the questions, to analyze and compile the results of our research, before interviewing selected former members of the board, and current and former employees to verify some of the concerns that the member respondents raised. We also reviewed reports and documents qualitatively, to compare them with results produced by our analysis of the primary data.

## **FINDINGS AND DISCUSSING**

Results of the analysis of data indicate clearly that many of the fund members are not happy with the current investment policy. This is particularly because of the general shift and diversion in SINPF board investment, away from the initial objective or strategy (of securing members' welfare and benefits) to a more neoliberal business or corporate investment orientation. Overwhelmingly 90 per cent the respondents are of the opinion that the SINPF board members over the years have diverted their

original investment policy<sup>8</sup> to a more corporate investment strategy to benefit the interests of a few members of the BOD and their associates. It is also notable that some external influence over the administration of the BOD in recent years is perceived to have influenced the shift from the original investment policy to the current one.

### **POLITICAL INFLUENCE IN APPOINTMENTS TO THE BOARD OF DIRECTORS**

Recently the government has passed the *State-Owned Enterprises Act (2007)*<sup>9</sup> which requires the appointment of the BOD to be a transparent and proper process of appointing members to the board. This process allows any interested candidate for the BOD to apply to the Chairperson and go through a stringent process in their appointment. This is seen as a positive government intervention into the governance of the state-owned superannuation fund. However, with the responsible minister still having the last say over appointment of members, some shadowy corners still remain where political elements can lurk in the recruitment of the BODs.

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<sup>8</sup> The original investment policy embodied the idea that members should benefit directly through housing loans and such like.

### **CONFLICT OF INTEREST AMONG BOARD OF DIRECTORS**

It was also evident that throughout earlier years, some elements of conflict of interest had been displayed, as evident for instance in the board's decisions during the approval process of loans and advances. We noted that some of the loans that were approved and granted to the corporate applicants were not assessed prudently. These loans should by rights have been rejected but due to political influence, they were funded without passing the assessment standards. In some instances such loans were restructured if the loan borrower could not demonstrate the capacity to repay the loans as agreed in the original loan agreement. According to Thorp, S. (2005) b this could inflate the poor management and inconsistency of making decision to serve the beneficiaries interests.

### **CRONYISM IN THE BOARD DECISION MAKING**

Solomon Islands culture has its own unique way of going about doing daily business. People have a system that is embedded in the way they do business and relate to each other. Within this "wantok system" a person does a favour to

<sup>9</sup> The SINPF is managed under the State Owned Enterprises Act 2008.

another because they come from the same tribe, area or province (Fraenkel, 2004). In the same spirit, “cronyism” in the board decision-making happens when, without any prudential consideration, loans are approved to friends or partners in a business operation. For example a seriously poor loan proposal assessment that was granted by the current BOD was the loan to improve the Tavanipupu resort. This loan has now had to be rescheduled because the borrower was not able to meet its monthly repayment commitments under the original application. The BOD has recently restructured the loan by increasing the terms to reduce the monthly repayment to cover loan interest and reduction. In some cases the lender could also appoint an administrator to manage the repayment of such poorly assessed loans.

### **CORPORATE LENDING OBJECTIVE**

Since the directors on the board have differences from the general expectations of members or other stakeholders in their lending strategy and policy, they are concerned more with creating and generating revenue to the fund than delivering their social security objective to the fund members. Creating more income for the fund has become the primary objective of the board. This has caused the SINPF to withdraw

most of its original functions since inception, so that it no longer lives up to’ their slogan “no social security without social justice”. The concerned services that are made redundant amongst their primary services include the ones that follow.

#### **(i) URBAN HOUSING LOANS**

The fund ceased its urban housing loan scheme to its members, making it difficult for them to acquire homes in urban centres, particularly Honiara. This has contributed to the limited availability of homes in the market in the capital city. During the pre-tension period, when the urban housing loan scheme was still operating, many members had managed to obtain loans from the SINPF to acquire their homes in Honiara. During the interviews, more than 80 per cent of the respondents expressed the opinion that the SINPF should re-introduce this service to enable members, especially ones who cannot afford to borrow directly from commercial banks, to acquire their own homes.

#### **(ii) REFINANCING OF HOUSING LOANS**

Most of the rural members who are unable to obtain housing loans from the SINPF have obtained their home loans from commercial

banks, which usually charge high rate to its customers. These customers (members) usually apply to SINPF to refinance their loans from these commercial banks with relatively very interest rate of 4 per cent to 5 per cent. The current interest rate for commercial and housing loans with the commercial banks ranges from 12 per cent to 19.5 per cent (ANZ, Annual report 2014). Because of the cessation of the refinancing of housing loans, members have to incur these high interest rates. The study found that more than 90 per cent of the respondents are not happy about this policy and are calling on the current BOD to consider re-opening housing loans to enable most mortgage owners with the commercial banks to transfer their loans to the SINPF board fund. Up till now, though, the SINPF continues to offer none of the services it used to provide as listed above, except the Commercial Bank NPF Pledge Loan scheme, which the Fund guarantees its members when borrowing from any of the three commercial banks.

### **(iii) FURNITURE LOANS**

More than 70 per cent of the key informants spoke of their houses being without proper furniture. This was mainly, they confirmed, because it was expensive to obtain loans from commercial banks just to acquire furniture for their own or rented homes. This could be different if the SINPF still provided furniture loans to its members.

### **SINPF OFFSHORE LOANS**

During the last BOD's term, the fund took the unprecedented step of investing SBD150M in the Singapore Stock Exchange market, an investment policy that was unpopular with members of the fund. More than 90 per cent of interviewees expressed disappointment with the last board for approving this investment. The majority of the respondents suggested that instead of investing this amount in the offshore financial sector, they should have invested in any of the commercial banks to allow members to acquire loans again at a relatively lower interest. This would generate income to contractors and allow members to have homes while the economy grows because of the productivity in the construction sector.

## **LIST OF CORPORATE COMPANIES IN WHICH SINPF HAS SHARES**

Besides extending advances or loans to various companies in the economy SINPF has gone a step further by acquiring shares in local companies. The table lists the local companies in which the SINPF has acquired shares. It is of interest to note that in more than 71 per cent (5/7) of the

## **CONCLUSION**

The recent SINPF board has shifted its investment policy strategy from that of supporting its members directly by providing services as had been mandated to a more business (Return on investment) focus. This shift of investment policy has defeated the whole purpose of the fund. While SOEs have generally gone through some process of reform that could have improved governance within the SINPF, the BOD must not be over-focused on profit that people as its original objective. It must also pay more attention to maximizing the benefits, such as homes, furniture and family businesses, the members must gain from their contributions while they are still active in their employment. Lastly, to realize the purpose of SINPF fully and ensure some tangible benefits towards improving the livelihood of its members, the BOD must redirect its current corporate investment

companies in which the SINPF has invested by share acquisition, it holds more than 65 per cent of shares. In only 29 per cent (2/7) of the companies does it hold 10 to 29 per cent of shares. This greatly increases the burden of extra responsibilities the SINPF BOD carries for the management and oversight of the companies in which they have interests.

objectives to individual (personal) investment objectives so that members are able to gain access to their funds not only when they retire but also during their active working lives when they can build and benefit from their own homes.

## **RECOMMENDATIONS**

(i) The board must not comprise the social benefit of members with the economic returns of the fund. Monetary return should only be yield when serving the social benefit of the members e.g., building homes through mortgages, starting small businesses through NPF guarantees, school fee loans to children or members (from primary to tertiary education), provision of relief funds due to climate change induced disasters etc.

(ii) To strengthen the governance by the board of directors and ensure there is loosely influence of politics on the appointments of the directors. Political influences will always result

in approval of imprudent loans. Loans must be properly assessed to avoid approval of non-viable loans.

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**Table 1. Companies in which the SINPF has acquired shares**

Companies	Percent of ownership
South Pacific Oil	95%
Providence Property Limited	90%
Sasape International Shipyard	29%
Heritage Park Hotel	10%
Home Finance Corporation	100%
Sol Tuna Limited	87%
Solomon Telekom Limited	65%